WHAT I LEARNED AT THE MOVIES ABOUT LEGAL ETHICS AND PROFESSIONALISM
By Anita Modak-Truran

HOW I GOT HERE

I've been fortunate. I practice law. I make movies. I write about both. I took up my pen and started writing a film column for *The Clarion-Ledger*, a Gannett-owned newspaper, back in the late 90s, when I moved from Chicago, Illinois, to Jackson, Mississippi. (It was like a Johnny Cash song… "Yeah, I'm going to Jackson. Look out Jackson Town….") I then turned my pen to writing for *The Jackson Free Press*, an indie weekly newspaper, which provided me opportunities to write about indie films and interesting people. I threw down the pen, as well as stopped my public radio movie reviews and the television segment I had for an ABC affiliate, when I moved three years ago from Jackson to Nashville to head Butler Snow's Entertainment and Media Industry Group.

During my journey weaving law and film together in a non-linear direction with no particular destination, I lived in the state where a young lawyer in the 1980s worked 60 to 70 hours a week at a small town law practice, squeezing in time before going to the office and during courtroom recesses to work on his first novel.

John Grisham writes that he would not have written his first book if he had not been a lawyer. "I never dreamed of being a writer. I wrote only after witnessing a trial." See http://www.jgrisham.com/bio/ (last accessed January 24, 2016).

My law partners at Butler Snow have stories about the old days when Mr. Grisham would open the trunk of his car and give out copies of *A Time To Kill*. Since then, Mr. Grisham has become "the" master of the legal thriller, where his books have captured the imaginations of a global audience and movies based on his books are some of the finest in the Parthenon of all legal movies.

I handled a zoning dispute (my own) against the City of Jackson before Judge Bobby DeLaughter. Before he took the bench, Judge DeLaughter's chief claim to fame was his successful 1994 prosecution of Bryon De La Beckwith for the 1963 murder of civil rights leader Medgar Evers.

Along the way, I got to know Mississippi Supreme Court Justice James Kitchens, who was one of the court-appointed legal representatives for Mr. Beckwith. If you saw *Ghosts of Mississippi*, these names should sound familiar. *Ghosts of Mississippi*, directed by Rob Reiner and starring Alec Baldwin, Whoopi Goldberg and James Woods, was based on the true story of the final murder trial against Mr. Beckwith.

I've also met Gregory Peck, who played Atticus Finch in *To Kill a Mockingbird*, at the Cannes Film Festival. And I have countless other tales where law and film blend together. But what remains constant is that the best legally-based movies, like *To Kill A Mockingbird*, *Ghosts*

of Mississippi, *The Firm*, *The Client*, *The Pelican Brief*, *Inherit the Wind* and *My Cousin Vinny* (which is still a personal favorite), explore very real professional and ethical dilemmas faced by practicing attorneys in business and litigation. These cinematic lawyers face what we face and sometimes their choices would not be ours. Sometimes our favorite cinematic lawyers falter in walking the line between right and wrong. Sometimes our favorite cinematic lawyers inspire us to be better than we thought possible. That's the magic of movies.

Before we can talk about legal ethics and professionalism on the screen, we need to refresh our memory on fundamental concepts. And for such fundamental concepts, I look to the ABA's Model Rules of Professional Conduct ("Model Rules"). Every state has adopted these rules. See http://www.americanbar.org/groups/professional_responsibility/publications/model rules_of_professional_conduct/alpha_list_state_adopting_model_rules.html (last accessed January 24, 2016). But states have revised the rules for their own jurisdictions, and any specific inquiry of an ethical or professionalism issue requires a review of the applicable state law. For our purposes, we will be analyzing my favorite legal movies under the Model Rules.

For ease of reading, I've structured this paper as follows. First, this paper outlines the Model Rules. It sets forth the preamble and scope of the Model Rules. It then sets forth the text of some of the rules that come up in day-to-day practice. This includes rules that define the client-lawyer relationship, transactions with persons other than clients, law firms and associations and information about legal services. It does not discuss rules on public service or maintaining the integrity of the profession. Against the backdrop of the Model Rules, the paper analyzes what I've learned at the movies about legal ethics and professionalism.

A REVIEW OF THE MODEL RULES OF PROFESSIONAL CONDUCT

The Preamble

The Preamble to the Model Rules provides the starting point for understanding our ethical and professional responsibilities as lawyers. The words in the Preamble mean more to me now as a practitioner for nearly thirty years, then when I first started practice in 1987.

Ethical dilemmas do not present themselves as a neat package of true or false questions on an exam. Rather, they arise unexpectedly in the guise of ambiguity. Ultimately, when all else fails, the answer comes down to what is the right thing to do? The Preamble in the Model Rules sets out the right thing to do by reminding us what a lawyer is, how a lawyer represents clients and how a lawyer interacts with the legal system and society as a whole.

Under the Preamble, "[a] lawyer, as a member of the legal profession, is a representative of clients, an officer of the legal system and a public citizen having special responsibility for the quality of justice." Model Rules, Preamble. Under this provision, lawyers are not ordinary sellers of services. Lawyers are part of a rich and noble profession charged with doing justice. To protect the integrity of the legal system, lawyers have special responsibility for ensuring, protecting and promoting this elusive concept of justice. Lawyers

represent not only clients, but they are officers of something bigger, a legal system that replaced the battlefield for settling disputes.

Second, "[a]s a representative of clients, a lawyer performs various functions. As advisor, a lawyer provides a client with an informed understanding of the client's legal rights and obligations and explains their practical implications. As advocate, a lawyer zealously asserts the client's position under the rules of the adversary system. As negotiator, a lawyer seeks a result advantageous to the client but consistent with requirements of honest dealings with others. As an evaluator, a lawyer acts by examining a client's legal affairs and reporting about them to the client or to others." Model Rules, Preamble. This section of the Preamble identifies the four main representational functions provided by a lawyer. A lawyer serves his or her client as: (1) an advisor; (2) an advocate; (3) a negotiator; and/or (4) an evaluator. I refer to this is the quadruple threat of "AANE".

Third, "[i]n addition to these representational functions, a lawyer may serve as a third-party neutral, a nonrepresentational role helping the parties to resolve a dispute or other matter…." Model Rules, Preamble. This section of the preamble recognizes the lawyer as a mediator or arbitrator in disputes. This is a professional function separate and apart of the lawyer's representational function.

Fourth, "[I]n all professional functions a lawyer should be competent, prompt and diligent. A lawyer should maintain communication with a client concerning the representation. A lawyer should keep in confidence information relating to representation of a client except so far as disclosure is required or permitted by the Rules of Professional Conduct or other law." Model Rules, Preamble. Keeping an open line of communication with a client is pivotal to the attorney client relationship. Indeed, many disciplinary actions are initiated simply because the client was not informed of what was going on in the represented matter. The lines of confidentiality are more difficult to draw, particularly when the representation involves criminal activity, such as in legal dilemmas raised in movies like *The Firm*, where Tom Cruise learns from the FBI that his law firm represents the mob.

Fifth, "[a] lawyer's conduct should conform to the requirements of the law, both in professional service to clients and in the lawyer's business **<u>and personal affairs</u>**. A lawyer should use the law's procedures only for legitimate purposes and not to harass or intimidate others. A lawyer should demonstrate respect for the legal system and for those who serve it, including judges, other lawyers and public officials. While it is a lawyer's duty, when necessary, to challenge the rectitude of official action, it is also a lawyer's duty to uphold legal process." Model Rules, Preamble (Emphasis added). This aspirational goal is replete in gray area. So what happens when your client asks you to delay the proceedings for no specific reason other than to wear down the other side? What happens if you know objecting to an attorney's line of questioning at trial will throw them off their game? Is that legally acceptable? In *A Civil Action*, Robert Duvall's character teaches his students at Harvard Law School the concept of the objection. Does this run afoul of the Model Rules?

Sixth, "[a]s a public citizen, a lawyer should seek improvement of the law, access to the legal system, the administration of justice and the quality of service rendered by the legal profession. As a member of a learned profession, a lawyer should cultivate knowledge of the law beyond its use for clients, employ that knowledge in reform of the law and work to strengthen legal education. In addition, a lawyer should further the public's understanding of and confidence in the rule of law and the justice system because legal institutions in a constitutional democracy depend on popular participation and support to maintain their authority. A lawyer should be mindful of deficiencies in the administration of justice and of the fact that the poor, and sometimes persons who are not poor, cannot afford adequate legal assistance. **Therefore, all lawyers should devote professional time and resources and use civic influence to ensure equal access to our system of justice for all those who because of economic or social barriers cannot afford or secure adequate legal counsel**. A lawyer should aid the legal profession in pursuing these objectives and should help the bar regulate itself in the public interest." Model Rules, Preamble (Emphasis added).

Most of us believed in these principles when we applied to law school. We wanted to "improve" the legal system. Have you done that since law school? I suspect that you have because you belong to and are active in the Federation of Defense and Corporate Counsel ("FDCC"). FDCC is dedicated to the "principles of knowledge, justice and fellowship." See http://www.The federation.org/documents/75thHistoryFDCC_10-31-11.pdf (Last accessed on January 24, 2016).

Seven, "[m]any of a lawyer's professional responsibilities are prescribed in the Rules of Professional Conduct, as well as substantive and procedural law. **<u>However, a lawyer is also guided by personal conscience and the approbation of professional peers</u>**. A lawyer should strive to attain the highest level of skill, to improve the law and the legal profession and to exemplify the legal profession's ideals of public service." Model Rules, Preamble (Emphasis added).

Eight, "[a] lawyer's responsibilities as a representative of clients, an officer of the legal system and a public citizen are usually harmonious. Thus, when an opposing party is well represented, a lawyer can be a zealous advocate on behalf of a client and at the same time assume that justice is being done. So also, a lawyer can be sure that preserving client confidences ordinarily serves the public interest because people are more likely to seek legal advice, and thereby heed their legal obligations, when they know their communications will be private." Model Rules, Preamble. I love this section of the preamble, because all lawyers understand and appreciate the need for zealous advocacy and confidentiality.

Ninth, "[i]n the nature of law practice, however, conflicting responsibilities are encountered. Virtually all difficult ethical problems arise from conflict between a lawyer's responsibilities to clients, to the legal system and to the lawyer's own interest in remaining an ethical person while earning a satisfactory living. The Rules of Professional Conduct often prescribe terms for resolving such conflicts. Within the framework of these Rules, however, many difficult issues of professional discretion can arise. Such issues must be resolved through

the exercise of sensitive professional and moral judgment guided by the basic principles underlying the Rules. These principles include the lawyer's obligation zealously to protect and pursue a client's legitimate interests, within the bounds of the law, while maintaining a professional, courteous and civil attitude toward all persons involved in the legal system." Model Rules, Preamble. The drafters of the Preamble understood that there will be conflicts. It's the nature of balancing responsibility to clients, to the legal system and to earning a living as an ethical person.

Tenth, "[t]he legal profession is largely self-governing. Although other professions also have been granted powers of self-government, the legal profession is unique in this respect because of the close relationship between the profession and the processes of government and law enforcement. This connection is manifested in the fact that ultimate authority over the legal profession is vested largely in the courts." Model Rules of Professional Conduct, Preamble.

Eleventh, "[t]o the extent that lawyers meet the obligations of their professional calling, the occasion for government regulation is obviated. Self-regulation also helps maintain the legal profession's independence from government domination. An independent legal profession is an important force in preserving government under law, for abuse of legal authority is more readily challenged by a profession whose members are not dependent on government for the right to practice." Model Rules, Preamble.

Twelfth, "[t]he legal profession's relative autonomy carries with it special responsibilities of self-government. The profession has a responsibility to assure that its regulations are conceived in the public interest and not in furtherance of parochial or self-interested concerns of the bar. Every lawyer is responsible for observance of the Rules of Professional Conduct. A lawyer should also aid in securing their observance by other lawyers. Neglect of these responsibilities compromises the independence of the profession and the public interest which it serves." Model Rules, Preamble.

Lastly, "[l]awyers play a vital role in the preservation of society. The fulfillment of this role requires an understanding by lawyers of their relationship to our legal system. The Rules of Professional Conduct, when properly applied, serve to define that relationship." Model Rules, Preamble.

Scope

The Model Rules also define the scope of the rules as "rules of reason." Model Rules, Scope. "They should be interpreted with reference to the purposes of legal representation and of the law itself." *Id.* Further, the rules "presuppose a larger legal context shaping the lawyer's role. That context includes court rules and statutes relating to matters of licensure, laws defining specific obligations of lawyers and substantive and procedural law in general. The Comments are sometimes used to alert lawyers to their responsibilities under such other law." *Id.* "Compliance with the Rules, as with all law in an open society, depends primarily upon

understanding and voluntary compliance, secondarily upon reinforcement by peer and public opinion and finally, when necessary, upon enforcement through disciplinary proceedings. The Rules do not, however, exhaust the moral and ethical considerations that should inform a lawyer, for no worthwhile human activity can be completely defined by legal rules. The Rules simply provide a framework for the ethical practice of law." *Id.*

"Furthermore, for purposes of determining the lawyer's authority and responsibility, principles of substantive law external to these Rules determine whether a client-lawyer relationship exists. Most of the duties flowing from the client-lawyer relationship attach only after the client has requested the lawyer to render legal services and the lawyer has agreed to do so. **But there are some duties, such as that of confidentiality under Rule 1.6, that attach when the lawyer agrees to consider whether a client-lawyer relationship shall be established.**" Model Rules, Scope. (Emphasis added). Lastly, "[f]ailure to comply with an obligation or prohibition imposed by a Rule is a basis for invoking the disciplinary process. The Rules presuppose that disciplinary assessment of a lawyer's conduct will be made on the basis of the facts and circumstances as they existed at the time of the conduct in question and in recognition of the fact that a lawyer often has to act upon uncertain or incomplete evidence of the situation. Moreover, the Rules presuppose that whether or not discipline should be imposed for a violation, and the severity of a sanction, depend on all the circumstances, such as the willfulness and seriousness of the violation, extenuating factors and whether there have been previous violations." *Id.* Accordingly, disciplinary violations are determined on a case-by-case basis, rather than a one size fits most.

Despite what happens in practice, the Model Rules provide that "[v]iolation of a Rule should not itself give rise to a cause of action against a lawyer nor should it create any presumption in such a case that a legal duty has been breached. In addition, violation of a Rule does not necessarily warrant any other nondisciplinary remedy, such as disqualification of a lawyer in pending litigation. **The Rules are designed to provide guidance to lawyers and to provide a structure for regulating conduct through disciplinary agencies. They are not designed to be a basis for civil liability.**" Model Rules, Scope (Emphasis added).

Rules

The Model Rules are divided into eight categories. The first category is the client-lawyer relationship. The second is the lawyer's role as counselor. The third is the lawyer's role as advocate. The fourth focuses on transactions with persons other than clients. The fifth category deals with law firms and associations. The sixth sets forth guidance on public service. The seventh category focuses on information about legal services, including the hot issue of attorney advertising, solicitation of clients and communication of fields of practice and specialization. The eighth category provides guidance on maintaining the integrity of the profession.

While a working knowledge of all the rules is paramount to a successful law practice, I've outlined the rules that we will be discussing for various movies. These rules are:

CLIENT-LAWYER RELATIONSHIP

Rule 1.1 Competence

A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation.

Rule 1.2 Scope of Representation and Allocation of Authority Between Client and Lawyer

(a) Subject to paragraphs (c) and (d), a lawyer shall abide by a client's decisions concerning the objectives of representation and, as required by Rule 1.4, shall consult with the client as to the means by which they are to be pursued. A lawyer may take such action on behalf of the client as is impliedly authorized to carry out the representation. A lawyer shall abide by a client's decision whether to settle a matter. In a criminal case, the lawyer shall abide by the client's decision, after consultation with the lawyer, as to a plea to be entered, whether to waive jury trial and whether the client will testify.

(b) A lawyer's representation of a client, including representation by appointment, does not constitute an endorsement of the client's political, economic, social or moral views or activities.

(c) A lawyer may limit the scope of the representation if the limitation is reasonable under the circumstances and the client gives informed consent.

(d) A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent, but a lawyer may discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client to make a good faith effort to determine the validity, scope, meaning or application of the law.

Rule 1.3: Diligence

A lawyer shall act with reasonable diligence and promptness in representing a client.

Rule 1.4 Communications

(a) A lawyer shall:

(1) promptly inform the client of any decision or circumstance with respect to which the client's informed consent …

(2) reasonably consult with the client about the means by which the client's objectives are to be accomplished;

(3) keep the client reasonably informed about the status of the matter;

(4) promptly comply with reasonable requests for information; and

(5) consult with the client about any relevant limitation on the lawyer's conduct when the lawyer knows that the client expects assistance not permitted by the Rules of Professional Conduct or other law.

(b) A lawyer shall explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation.

Rule 1.5 Fees

(a) A lawyer shall not make an agreement for, charge, or collect an unreasonable fee or an unreasonable amount for expenses. The factors to be considered in determining the reasonableness of a fee include the following:

(1) the time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly;

(2) the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer;

(3) the fee customarily charged in the locality for similar legal services;

(4) the amount involved and the results obtained;

(5) the time limitations imposed by the client or by the circumstances;

(6) the nature and length of the professional relationship with the client;

(7) the experience, reputation, and ability of the lawyer or lawyers performing the services; and

(8) whether the fee is fixed or contingent.

(b) The scope of the representation and the basis or rate of the fee and expenses for which the client will be responsible shall be communicated to the client, preferably in writing, before or within a reasonable time after commencing the representation, except when the lawyer will charge a regularly represented client on the same basis or rate. Any changes in the basis or rate of the fee or expenses shall also be communicated to the client.

(c) A fee may be contingent on the outcome of the matter for which the service is rendered, except in a matter in which a contingent fee is prohibited by paragraph (d) or other law. A contingent fee agreement shall be in a writing signed by the client and shall state the method by which the fee is to be determined, including the percentage or percentages that shall accrue to the lawyer in the event of settlement, trial or appeal; litigation and other expenses to be deducted from the recovery; and whether such expenses are to be deducted before or after the contingent fee is calculated. The agreement must clearly notify the client of any expenses for which the client will be liable whether or not the client is the prevailing party. Upon conclusion of a contingent fee matter, the lawyer shall provide the client with a written statement stating the outcome of the matter and, if there is a recovery, showing the remittance to the client and the method of its determination.

(d) A lawyer shall not enter into an arrangement for, charge, or collect:

(1) any fee in a domestic relations matter, the payment or amount of which is contingent upon the securing of a divorce or upon the amount of alimony or support, or property settlement in lieu thereof; or

(2) a contingent fee for representing a defendant in a criminal case.

(e) A division of a fee between lawyers who are not in the same firm may be made only if:

(1) the division is in proportion to the services performed by each lawyer or each lawyer assumes joint responsibility for the representation;

(2) the client agrees to the arrangement, including the share each lawyer will receive, and the agreement is confirmed in writing; and

(3) the total fee is reasonable.

Rule 1.6 Confidentiality of Information

(a) A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation or the disclosure is permitted by paragraph (b).

(b) A lawyer may reveal information relating to the representation of a client to the extent the lawyer reasonably believes necessary:

(1) to prevent reasonably certain death or substantial bodily harm;

(2) to prevent the client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's services;

(3) to prevent, mitigate or rectify substantial injury to the financial interests or property of another that is reasonably certain to result or has resulted from the client's commission of a crime or fraud in furtherance of which the client has used the lawyer's services;

(4) to secure legal advice about the lawyer's compliance with these Rules;

(5) to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client;

(6) to comply with other law or a court order; or

(7) to detect and resolve conflicts of interest arising from the lawyer’s change of employment or from changes in the composition or

ownership of a firm, but only if the revealed information would not compromise the attorney-client privilege or otherwise prejudice the client.

(c) A lawyer shall make reasonable efforts to prevent the inadvertent or unauthorized disclosure of, or unauthorized access to, information relating to the representation of a client.

Rule 1.7 Conflict of Interest: Current Clients

(a) Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:

(1) the representation of one client will be directly adverse to another client; or

(2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.

(b) Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:

(1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;

(2) the representation is not prohibited by law;

(3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and

(4) each affected client gives informed consent, confirmed in writing.

Rule 1.8 Conflict of Interest: Current Clients: Specific Rules

(a) A lawyer shall not enter into a business transaction with a client or knowingly acquire an ownership, possessory, security or other pecuniary interest adverse to a client unless:

(1) the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing in a manner that can be reasonably understood by the client;

(2) the client is advised in writing of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent legal counsel on the transaction; and

(3) the client gives informed consent, in a writing signed by the client, to the essential terms of the transaction and the lawyer's role in the transaction, including whether the lawyer is representing the client in the transaction.

(b) A lawyer shall not use information relating to representation of a client to the disadvantage of the client unless the client gives informed consent, except as permitted or required by these Rules.

(c) A lawyer shall not solicit any substantial gift from a client, including a testamentary gift, or prepare on behalf of a client an instrument giving the lawyer or a person related to the lawyer any substantial gift unless the lawyer or other recipient of the gift is related to the client. For purposes of this paragraph, related persons include a spouse, child, grandchild, parent, grandparent or other relative or individual with whom the lawyer or the client maintains a close, familial relationship.

(d) Prior to the conclusion of representation of a client, a lawyer shall not make or negotiate an agreement giving the lawyer literary or media rights to a portrayal or account based in substantial part on information relating to the representation.

(e) A lawyer shall not provide financial assistance to a client in connection with pending or contemplated litigation, except that:

(1) a lawyer may advance court costs and expenses of litigation, the repayment of which may be contingent on the outcome of the matter; and

(2) a lawyer representing an indigent client may pay court costs and expenses of litigation on behalf of the client.

(f) A lawyer shall not accept compensation for representing a client from one other than the client unless:

(1) the client gives informed consent;

(2) there is no interference with the lawyer's independence of professional judgment or with the client-lawyer relationship; and

(3) information relating to representation of a client is protected as required by Rule 1.6.

(g) A lawyer who represents two or more clients shall not participate in making an aggregate settlement of the claims of or against the clients, or in a criminal case an aggregated agreement as to guilty or nolo contendere pleas, unless each client gives informed consent, in a writing signed by the client. The lawyer's disclosure shall include the existence and nature of all the claims or pleas involved and of the participation of each person in the settlement.

(h) A lawyer shall not:

(1) make an agreement prospectively limiting the lawyer's liability to a client for malpractice unless the client is independently represented in making the agreement; or

(2) settle a claim or potential claim for such liability with an unrepresented client or former client unless that person is advised in writing of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent legal counsel in connection therewith.

(i) A lawyer shall not acquire a proprietary interest in the cause of action or subject matter of litigation the lawyer is conducting for a client, except that the lawyer may:

(1) acquire a lien authorized by law to secure the lawyer's fee or expenses; and

(2) contract with a client for a reasonable contingent fee in a civil case.

(j) A lawyer shall not have sexual relations with a client unless a consensual sexual relationship existed between them when the client-lawyer relationship commenced.

(k) While lawyers are associated in a firm, a prohibition in the foregoing paragraphs (a) through (i) that applies to any one of them shall apply to all of them.

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Client-Lawyer Relationship Rule 1.16 Declining Or Terminating Representation

(a) Except as stated in paragraph (c), a lawyer shall not represent a client or, where representation has commenced, shall withdraw from the representation of a client if:

(1) the representation will result in violation of the rules of professional conduct or other law;

(2) the lawyer's physical or mental condition materially impairs the lawyer's ability to represent the client; or

(3) the lawyer is discharged.

(b) Except as stated in paragraph (c), a lawyer may withdraw from representing a client if:

(1) withdrawal can be accomplished without material adverse effect on the interests of the client;

(2) the client persists in a course of action involving the lawyer's services that the lawyer reasonably believes is criminal or fraudulent;

(3) the client has used the lawyer's services to perpetrate a crime or fraud;

(4) the client insists upon taking action that the lawyer considers repugnant or with which the lawyer has a fundamental disagreement;

(5) the client fails substantially to fulfill an obligation to the lawyer regarding the lawyer's services and has been given reasonable warning that the lawyer will withdraw unless the obligation is fulfilled;

(6) the representation will result in an unreasonable financial burden on the lawyer or has been rendered unreasonably difficult by the client; or

(7) other good cause for withdrawal exists.

(c) A lawyer must comply with applicable law requiring notice to or permission of a tribunal when terminating a representation. When ordered to do so by a tribunal, a lawyer shall continue representation notwithstanding good cause for terminating the representation.

(d) Upon termination of representation, a lawyer shall take steps to the extent reasonably practicable to protect a client's interests, such as giving reasonable notice to the client, allowing time for employment of other counsel, surrendering papers and property to which the client is entitled and refunding any advance payment of fee or expense that has not been earned or incurred. The lawyer may retain papers relating to the client to the extent permitted by other law.

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Rule 1.18 Duties to Prospective Client

(a) A person who consults with a lawyer about the possibility of forming a client-lawyer relationship with respect to a matter is a prospective client.

(b) Even when no client-lawyer relationship ensues, a lawyer who has learned information from a prospective client shall not use or reveal that information, except as Rule 1.9 would permit with respect to information of a former client.

(c) A lawyer subject to paragraph (b) shall not represent a client with interests materially adverse to those of a prospective client in the same or a substantially related matter if the lawyer received information from the prospective client that could be significantly harmful to that person in the matter, except as provided in paragraph (d). If a lawyer is disqualified from representation under this paragraph, no lawyer in a firm with which that lawyer is associated may knowingly undertake or continue representation in such a matter, except as provided in paragraph (d).

(d) When the lawyer has received disqualifying information as defined in paragraph (c), representation is permissible if:

(1) both the affected client and the prospective client have given informed consent, confirmed in writing, or:

(2) the lawyer who received the information took reasonable measures to avoid exposure to more disqualifying information than was reasonably necessary to determine whether to represent the prospective client; and

(i) the disqualified lawyer is timely screened from any participation in the matter and is apportioned no part of the fee therefrom; and

(ii) written notice is promptly given to the prospective client.

ADVISOR

Rule 2.1 Advisor

In representing a client, a lawyer shall exercise independent professional judgment and render candid advice. In rendering advice, a lawyer may refer not only to law but to other considerations such as moral, economic, social and political factors, that may be relevant to the client's situation.

ADVOCATE

Rule 3.1 Meritorious Claims And Contentions

A lawyer shall not bring or defend a proceeding, or assert or controvert an issue therein, unless there is a basis in law and fact for doing so that is not frivolous, which includes a good faith argument for an extension, modification or reversal of existing law. A lawyer for the defendant in a criminal proceeding, or the respondent in a proceeding that could result in incarceration, may nevertheless so defend the proceeding as to require that every element of the case be established.

Rule 3.2 Expediting Litigation

A lawyer shall make reasonable efforts to expedite litigation consistent with the interests of the client.

Rule 3.3 Candor Toward the Tribunal

(a) A lawyer shall not knowingly:

(1) make a false statement of fact or law to a tribunal or fail to correct a false statement of material fact or law previously made to the tribunal by the lawyer;

(2) fail to disclose to the tribunal legal authority in the controlling jurisdiction known to the lawyer to be directly adverse to the position of the client and not disclosed by opposing counsel; or

(3) offer evidence that the lawyer knows to be false. If a lawyer, the lawyer's client, or a witness called by the lawyer, has offered material evidence and the lawyer comes to know of its falsity, the lawyer shall take reasonable remedial measures, including, if necessary, disclosure to the tribunal. A lawyer may refuse to offer evidence, other than the testimony of a defendant in a criminal matter, that the lawyer reasonably believes is false.

(b) A lawyer who represents a client in an adjudicative proceeding and who knows that a person intends to engage, is engaging or has engaged in criminal or fraudulent conduct related to the proceeding shall take reasonable remedial measures, including, if necessary, disclosure to the tribunal.

(c) The duties stated in paragraphs (a) and (b) continue to the conclusion of the proceeding, and apply even if compliance requires disclosure of information otherwise protected by Rule 1.6.

(d) In an ex parte proceeding, a lawyer shall inform the tribunal of all material facts known to the lawyer that will enable the tribunal to make an informed decision, whether or not the facts are adverse.

Rule 3.4 Fairness to Opposing Party And Counsel

A lawyer shall not:

(a) unlawfully obstruct another party's access to evidence or unlawfully alter, destroy or conceal a document or other material having potential evidentiary value. A lawyer shall not counsel or assist another person to do any such act;

(b) falsify evidence, counsel or assist a witness to testify falsely, or offer an inducement to a witness that is prohibited by law;

(c) knowingly disobey an obligation under the rules of a tribunal except for an open refusal based on an assertion that no valid obligation exists;

(d) in pretrial procedure, make a frivolous discovery request or fail to make reasonably diligent effort to comply with a legally proper discovery request by an opposing party;

(e) in trial, allude to any matter that the lawyer does not reasonably believe is relevant or that will not be supported by admissible evidence, assert personal knowledge of facts in issue except when testifying as a witness, or state a personal opinion as to the justness of a cause, the credibility of a witness, the culpability of a civil litigant or the guilt or innocence of an accused; or

(f) request a person other than a client to refrain from voluntarily giving relevant information to another party unless:

(1) the person is a relative or an employee or other agent of a client; and

(2) the lawyer reasonably believes that the person's interests will not be adversely affected by refraining from giving such information.

Rule 3.5 Impartiality and Decorum of the Tribunal

A lawyer shall not:

(a) seek to influence a judge, juror, prospective juror or other official by means prohibited by law;

(b) communicate ex parte with such a person during the proceeding unless authorized to do so by law or court order;

(c) communicate with a juror or prospective juror after discharge of the jury if:

(1) the communication is prohibited by law or court order;

(2) the juror has made known to the lawyer a desire not to communicate; or

(3) the communication involves misrepresentation, coercion, duress or harassment; or(d) engage in conduct intended to disrupt a tribunal.

Rule 3.6 Trial Publicity

(a) A lawyer who is participating or has participated in the investigation or litigation of a matter shall not make an extrajudicial statement that the lawyer knows or reasonably should know will be disseminated by means of public communication and will have a substantial likelihood of materially prejudicing an adjudicative proceeding in the matter.

(b) Notwithstanding paragraph (a), a lawyer may state:

(1) the claim, offense or defense involved and, except when prohibited by law, the identity of the persons involved;

(2) information contained in a public record;

(3) that an investigation of a matter is in progress;

(4) the scheduling or result of any step in litigation;

(5) a request for assistance in obtaining evidence and information necessary thereto;

(6) a warning of danger concerning the behavior of a person involved, when there is reason to believe that there exists the likelihood of substantial harm to an individual or to the public interest; and

(7) in a criminal case, in addition to subparagraphs (1) through (6):

(i) the identity, residence, occupation and family status of the accused;

(ii) if the accused has not been apprehended, information necessary to aid in apprehension of that person;

(iii) the fact, time and place of arrest; and

(iv) the identity of investigating and arresting officers or agencies and the length of the investigation.

(c) Notwithstanding paragraph (a), a lawyer may make a statement that a reasonable lawyer would believe is required to protect a client from the substantial undue prejudicial effect of recent publicity not initiated by the lawyer or the lawyer's client. A statement made pursuant to this

paragraph shall be limited to such information as is necessary to mitigate the recent adverse publicity.

(d) No lawyer associated in a firm or government agency with a lawyer subject to paragraph (a) shall make a statement prohibited by paragraph (a).

TRANSACTIONS WITH PERSONS OTHER THAN CLIENTS

Rule 4.1 Truthfulness in Statements to Others

In the course of representing a client a lawyer shall not knowingly:

(a) make a false statement of material fact or law to a third person; or

(b) fail to disclose a material fact to a third person when disclosure is necessary to avoid assisting a criminal or fraudulent act by a client, unless disclosure is prohibited by Rule 1.6.

Rule 4.2 Communication With Person Represented By Counsel

In representing a client, a lawyer shall not communicate about the subject of the representation with a person the lawyer knows to be represented by another lawyer in the matter, unless the lawyer has the consent of the other lawyer or is authorized to do so by law or a court order.

Rule 4.3 Dealing with Unrepresented Person

In dealing on behalf of a client with a person who is not represented by counsel a lawyer shall not state or imply that the lawyer is disinterested. When the lawyer knows or reasonably should know that the unrepresented person misunderstands the lawyer's role in the matter, the lawyer shall make reasonable efforts to correct the misunderstanding. The lawyer shall not give legal advice to an unrepresented person, other than the advice to secure counsel, if the lawyer knows or reasonably should know that the interests of such a person are or have a reasonable possibility of being in conflict with the interests of the client.

Rule 4.4 Respect For Rights Of Third Persons

(a) In representing a client, a lawyer shall not use means that have no substantial purpose other than to embarrass, delay, or burden a third person, or use methods of obtaining evidence that violate the legal rights of such a person.

(b) A lawyer who receives a document or electronically stored information relating to the representation of the lawyer's client and knows or reasonably should know that the document or electronically stored information was inadvertently sent shall promptly notify the sender.

LAW FIRMS AND ASSOCIATIONS

Rule 5.1 Responsibilities Of Partners,Managers, And Supervisory Lawyers

(a) A partner in a law firm, and a lawyer who individually or together with other lawyers possesses comparable managerial authority in a law firm, shall make reasonable efforts to ensure that the firm has in effect measures giving reasonable assurance that all lawyers in the firm conform to the Rules of Professional Conduct.

(b) A lawyer having direct supervisory authority over another lawyer shall make reasonable efforts to ensure that the other lawyer conforms to the Rules of Professional Conduct.

(c) A lawyer shall be responsible for another lawyer's violation of the Rules of Professional Conduct if:

(1) the lawyer orders or, with knowledge of the specific conduct, ratifies the conduct involved; or

(2) the lawyer is a partner or has comparable managerial authority in the law firm in which the other lawyer practices, or has direct supervisory authority over the other lawyer, and knows of the conduct at a time when its consequences can be avoided or mitigated but fails to take reasonable remedial action.

Rule 5.2 Responsibilities of a Subordinate Lawyer

(a) A lawyer is bound by the Rules of Professional Conduct notwithstanding that the lawyer acted at the direction of another person.

(b) A subordinate lawyer does not violate the Rules of Professional Conduct if that lawyer acts in accordance with a supervisory lawyer's reasonable resolution of an arguable question of professional duty.

INFORMATION ABOUT LEGAL SERVICES

Rule 7.2 Advertising

(a) Subject to the requirements of Rules 7.1 and 7.3, a lawyer may advertise services through written, recorded or electronic communication, including public media.

(b) A lawyer shall not give anything of value to a person for recommending the lawyer's services except that a lawyer may

(1) pay the reasonable costs of advertisements or communications permitted by this Rule;

(2) pay the usual charges of a legal service plan or a not-for-profit or qualified lawyer referral service. A qualified lawyer referral service is a lawyer referral service that has been approved by an appropriate regulatory authority;

(3) pay for a law practice in accordance with Rule 1.17; and

(4) refer clients to another lawyer or a nonlawyer professional pursuant to an agreement not otherwise prohibited under these Rules that provides for the other person to refer clients or customers to the lawyer, if

(i) the reciprocal referral agreement is not exclusive, and

(ii) the client is informed of the existence and nature of the agreement.

(c) Any communication made pursuant to this rule shall include the name and office address of at least one lawyer or law firm responsible for its content.

Rule 7.3 Solicitation of Clients

(a) A lawyer shall not by in-person, live telephone or real-time electronic contact solicit professional employment when a significant motive for the lawyer's doing so is the lawyer's pecuniary gain, unless the person contacted:

(1) is a lawyer; or

(2) has a family, close personal, or prior professional relationship with the lawyer.

(b) A lawyer shall not solicit professional employment by written, recorded or electronic communication or by in-person, telephone or real-time electronic contact even when not otherwise prohibited by paragraph (a), if:

(1) the target of the solicitation has made known to the lawyer a desire not to be solicited by the lawyer; or

(2) the solicitation involves coercion, duress or harassment.

(c) Every written, recorded or electronic communication from a lawyer soliciting professional employment from anyone known to be in need of legal services in a particular matter shall include the words "Advertising Material" on the outside envelope, if any, and at the beginning and ending of any recorded or electronic communication, unless the recipient of the communication is a person specified in paragraphs (a)(1) or (a)(2).

(d) Notwithstanding the prohibitions in paragraph (a), a lawyer may participate with a prepaid or group legal service plan operated by an organization not owned or directed by the lawyer that uses in-person or telephone contact to solicit memberships or subscriptions for the plan from persons who are not known to need legal services in a particular matter covered by the plan.

Rule 7.4 Communication of Fields of Practice and Specialization

(a) A lawyer may communicate the fact that the lawyer does or does not practice in particular fields of law.

(b) A lawyer admitted to engage in patent practice before the United States Patent and Trademark Office may use the designation "Patent Attorney" or a substantially similar designation.

(c) A lawyer engaged in Admiralty practice may use the designation "Admiralty," "Proctor in Admiralty" or a substantially similar designation.

(d) A lawyer shall not state or imply that a lawyer is certified as a specialist in a particular field of law, unless:

(1) the lawyer has been certified as a specialist by an organization that has been approved by an appropriate state authority or that has been accredited by the American Bar Association; and

(2) the name of the certifying organization is clearly identified in the communication.

SO WHAT HAVE I LEARNED AT THE MOVIES ON ETHICAL AND PROFESSIONAL CONDUCT

Hollywood loves lawyers in film. In 2008, the ABA Journal published an article on the 25 greatest legal movies made. In this well written and thoughtful article, Richard Brust states: "From the incisive Henry Drummond and the droll Mr. Lincoln to the callow Danny Kaffee and the regal Atticus Finch, lawyers have provided some of Hollywood's most memorable cinematic heroes and some of its most honorable and thoughtful films." See http://www.Aba journal.com/magazine/article/the_25_greatest_legal _movies/ (last accessed January 24, 2016).

Lawyers continue to and always will make "memorable cinematic heroes" or anti-heroes in some cases. One of the finest films of 2015 was the *Bridge of Spies*. This film, directed by Steven Spielberg from a script written by Matt Charman and the Coen Brothers, tells the story of former insurance defense lawyer James B. Donovan (Tom Hanks) who is entrusted with negotiating the release of pilot shot down over the Soviet Union and the exchange of KGB spy held in U.S. custody. Mr. Donovan's work for the U.S. government may not have been legal work, but his legal skills in negotiating, strategizing and in pursuing justice for the greater good of his country make him a cinematic lawyer hero, joining the ranks of Atticus Finch in *To Kill A Mockingbird*.

To Kill A Mockingbird is about Atticus Finch, a small town lawyer in the Depression-era South. The court appoints Atticus to defend a black man against an undeserved rape charge. Most lawyers hold Atticus Finch as the ideal, because he embodies all the noble concepts of law and justice. Indeed, Atticus radiates integrity. Integrity follows Atticus like a halo in all of his course of dealings, whether it with his children whom he teaches tolerance, or to his client whom he is zealously representing in a segregated South or to the court who appointed him in an unpopular role or to the community who wants to hold a lynching of his client.

Harper Lee, who wrote the novel that was the basis of the movie, models Atticus Finch on her dad. Ms. Lee's father was an attorney and Alabama state legislator, whose 1923 defense of a black client partially inspired the novel's trial. The character of Atticus Finch parallel's Amasa Lee in many ways, including the fact that Atticus Finch is not only an attorney, but also a state legislature and a widower's single father like Ms. Lee's dad. In my opinion, Atticus Finch resonates today because it is based on how many lawyers courageously represented unpopular clients in the pursuit of justice for all.

Rob Reiner's *Ghosts of Mississippi*, which is based on a true story, focuses on the struggles of Medgar Edgar's widow (Whoopi Goldberg) and the district attorney (Alec Baldwin) to bring Bryon de la Beckwith (James Woods), a white supremacist and Klansman from Greenwood, MS, to a third trial for his 1963 slaying of Medgar Evers. The district attorney is depicted as a lawyer in pursuit of a noble cause, and there is no doubt of that.

An equally compelling part of the final Beckwith trial, which is not a plot point in the film, is that Jim Kitchens, now a Mississippi Supreme Court Justice, and Buddy Coxwell were court appointed counsel for Beckwith. Like Atticus Finch, Justice Kitchens and Mr. Coxwell zealously represented their client. In a presentation made for the Kentucky Bar Association a few months ago, Justice Kitchens wrote:

> You've stepped up to the plate and represented unpopular people yourselves. Buddy Coxwell and I aren't unique in that regard. It's what lawyers are supposed to do. All of us were taught that in law school, and I think all of us believe. Some get called upon to do it, and some don't. … **We know that if the system doesn't work for everybody, we have no right to expect it to work for anybody**.

See http://c.ymcdn.com/sites/www.kybar.org/resource/resmgr/2015_Convention/James_Kitchens.pdf (last accessed on January 24, 2016) (Emphasis added).

In P*hiladelphia*, another film based on a true story, the management at a mega-large firm fires a brilliant young lawyer named Andrew Beckett (Tom Hanks) because he has AIDS. Andrew hires a homophobic small time lawyer (Denzel Washington) as this is the only attorney in town willing to advocate for a wrongful dismissal suit. The film offers a plethora of examples of the application of the Model Rules in action, including, without limitation, communication issues before retention, how to work with a client and the allocation of authority between client and lawyer.

In contrast to the serious films we've looked at so far, let's turn to *My Cousin Vinny*, which is directed by Jonathan Lynn, a lawyer by training. In this film, two New York City "yutes" are accused of murder in rural Alabama while on their way back to college. Vinny Gambini (Joe Pesci), a cousin to one of the accused "yutes", comes to defend them. Vinny is an inexperienced, loudmouth lawyer not accustomed to Southern rules and manners, and he falters … badly!

This scene from *My Cousin Vinny* exemplifies what lawyers should NOT do. Judge Haller: "Counselor, your clients are charged with first degree murder. How do they plead?" Vinny, who is seated, "Your Honor, my clients…" Judge Haller cuts in: "Don't talk to me sitting in that chair!" Vinny: "But he [pointing to bailiff] told me to sit here." Judge Haller, "When you're addressed in this court, you'll rise. Speak to me in a clear, intelligible voice." Clearly, Vinny did not appreciate the Model Rule on decorum to the tribunal.

But the exchange gets more heated when Judge Haller sees what Vinny is wearing in his courtroom. "What are you wearing?," demands Judge Haller. "Huh?," asks VInny. "What are you wearing? Looking down at his black leather jacket, Vinny responds "Um… I'm wearing clothes… I … I don't get the question." The Judge slaps back: "When you come into my court looking like you do, you not only insult me, but you insult the integrity of this court!" Vinny responds: "I apologize, sir, but, uh... this is how I dress." Judge Haller: "Fine. I'll let you off this one time. The next time you appear in my court, you will look lawyerly. And I mean you comb your hair, and wear a suit and tie. And that suit had better be made out of some sort of... cloth. You understand me?"

In the classic legal thriller, *Anatomy of a Murder*, James Stewart plays Paul Biegel, an attorney who defends a husband who claims he suffered temporary insanity when he killed the man who raped his wife. During one of the court room scenes, Mr. Biegel accuses the district attorney of withholding evidence. Is this in line with the Model Rules? Rule 3.1 provides that a lawyer shall not "assert or controvert an issue therein, unless there is basis in law and fact for doing so that that is not frivolous." The rule recognizes that "[a] lawyer for the defendant in a criminal proceeding, or the respondent in a proceeding that could result in incarceration, may nevertheless so defend the proceeding as to require that every element of the case be established." Model Rule 3.1.

Mr. Billy Flynn in the musical version of the movie *Chicago* defends women accused of murdering their husbands. Is it appropriate for Mr. Flynn to hold press conferences before the trial? Rule 3.6 (a) provides that a lawyer participating in the investigation or litigation of a matter "shall not make an extrajudicial statement that the lawyer knows or reasonably should know will be disseminated by means of public communication and will have a substantial likelihood of materially prejudicing an adjudicative proceeding in the matter." But there is a litany of exceptions in Rule 3.6(b). Also, is it appropriate for Mr. Flynn to "razzle dazzle" the court with tricks of the trade? Rule 3.3 prohibits false statements to the court, but is the "razzle dazzle" something less than false information?. Under Rule 4.1, a lawyer shall not knowingly make a false statement of material fact or law to a third person.

An important issue for all lawyers is client confidentiality. But what happens when you learn from the federal government that your firm's only client is the mob? In *The Firm*, based on John Grisham's best seller of the same name, Mitch McDeere (Tom Cruise) accepts an exceptionally generous offer from a prestigious Firm. (Yes, it is capitalized. It's a great Firm!) But when two associates are murdered, the FBI makes a call to Mitch, wherein he learns that the Firm has one client and they don't allow associates to leave willingly. What can and can't Mitch say or do? What are Mitch's obligations as a subordinate lawyer.

Rule 5.2 provides that a lawyer is bound by the Rules of Professional Conduct **notwithstanding that the lawyer acted at the direction of another person**." Model Rule 5.2 (a) (Emphasis added). But a "subordinate lawyer does not violate the Rules of Professional Conduct if that lawyer acts in accordance with a supervisory lawyer's **reasonable resolution of an arguable question of professional duty**." *Id.* at 5.2 (b) (Emphasis added).

Should Mitch withdraw from the representation? If so, what's the best way to do so? Under Rule 1.16, Mitch can withdraw from the representation if the client persists in a course of action involving the lawyer's services that the lawyer reasonably believes is criminal or fraudulent or where the client has used the lawyer's services to perpetrate a crime or fraud. These are all difficult issues, but in this case, the penalty for withdrawing from representation is death by client. Think about that and how it should be factored into the equation.

In another Grisham book turn to movie, a young boy (Brad Renfro), who witnessed the suicide of a mafia lawyer, hires attorney Reggie Love (Susan Sarandon) to protect him when the district attorney (Tommy Lee Jones) tries to use him to take down a mob family. *The Client*, among other things, provides excellent examples of how a lawyer sets her fee, confidentiality of communication between lawyer and client, and improper communications by the district attorney to a represented party.

One of the most powerful legal films concerning the business of law is *A Civil Action*, which is based on a true story. Jan Schlictmann (John Travolta) represents the families of children who have died from the actions of two companies dumping toxic waste in the water supply. In the opening scene Jan shares his take on the personal injury legal system.

> It's like this. A dead plaintiff is rarely worth as much as a living, severely-maimed plaintiff. However, if it's a long slow agonizing death, as opposed to a quick drowning or car wreck, the value can rise considerably. A dead adult in his 20s is generally worth less than one who is middle aged. A dead woman less than a dead man. A single adult less than one who's married. Black less than white. Poor less than rich. The perfect victim is a white male professional, 40 years old, at the height of his earning power, struck down in his prime. **And the most imperfect? Well, in the calculus of personal injury law, a dead child is worth the least of all.**

(Emphasis added).

Knowing that a dead child is worth the least of all in the personal injury context does not stop Jan from zealously pursuing the case. It's never about the money, and the litigation against toxic dumping companies becomes an obsession for Jan, where the pride and hubris of the litigator overcome common sense and the rules of professional conduct.

But the other side of the "v" in this litigation exploits this to their advantage. Jerome Facher (Robert Duvall) tells his law students that "the single greatest liability a lawyer can have is pride. Pride... Pride has lost more cases than lousy evidence, idiot witnesses and a hanging judge all put together. There is absolutely no place in a courtroom for pride." Is it appropriate for Jan to reject an $8 Million settlement offer without speaking to his clients? Rule 1.4 guides lawyer client communications. What about the fact that Jan rejected this offer without consulting his law partners, who have mortgaged their homes in this quest for justice?

Movies, like *Erin Brokovich* and *Legally Blonde*, raise issues about a law firm's responsibilities regarding a non-lawyer. Under Rule 5.3, a lawyer "having direct supervisory authority over the nonlawyer shall make reasonable efforts to ensure that the person's conduct is compatible with the professional obligations of the lawyer." Model Rule 5.3. The supervising lawyer shall be responsible for conduct of such a person that would be a violation of the Rules of Professional Conduct if "the lawyer orders or, with the knowledge of the specific conduct, ratifies the conduct involved" or "the lawyer is a partner or has comparable managerial authority in the law firm in which the person is employed, or has direct supervisory authority over the person, and knows of the conduct at a time when its consequences can be avoided or mitigated but fails to take reasonable remedial action." *Id.*

And what about a law student who has pieced together the reason two U.S. Supreme Court justices have murdered? Do the rules of professional conduct apply to Darby Shaw (Julia Roberts) in *The Pelican Brief*?

Finally, films like *Inherit the Wind*, *The Verdict*, *A Few Good Men* and *Justice for All*, transcend their subject matters. They all demonstrate that zealous representation and brilliant oration lead to satisfying conclusions. But in a less direct way, they show us the nobility of justice being done.

WRAPPING UP

It's time to wrap up. It is impossible for me to discuss everything I've learned from the movies about legal ethics and professionalism. But in the end what makes all of this worth it? To paraphrase Andrew's testimony on direct examination in the final court room scene in *Philadelphia*: "every now and again, not often, but occasionally, you get to be a part of justice being done. And it really is quite a thrill when that happens." It's been a thrill.

FANTASTIC VOYAGE

The New Biotech/Human Interface and Resulting Legal Challenges

The Federation of Defense and Corporate Counsel Winter 2016 Meeting

San Diego, California February 29, 2016

Throughout the history of law and litigation, lawyers, judges and legislators have wrestled with the next new thing - novel products, unforeseen legal relationships, new diseases or new technology. Asbestos was a wonderful mineral used widely, until mesothelioma came to light. Doctors promoted cigarettes as a way to increase lung strength, until the FDA mandated warnings. Drive through food was a pure money maker, until people started spilling hot food on their laps.

Putting on our Retrospectoscopes (Patent Pending), it is now easy to see that there were potential risks with many products or procedures that, since their advent, have spawned litigation and regulatory responses.

But what is looming over the horizon. A quick look at the American Association for Justice's website reveals that plaintiff's lawyers are actively forming "working groups" to identify their next big money makers. Defense lawyers, however, are by definition reactive – they defend assaults on clients and industries. To better serve our clients, however, we need to mimic our sea faring ancestors or our earliest astronauts and venture over that horizon. We may sail off the edge of the world or rocket into a black hole, but more likely, we will discover ways to plan for what lies ahead on our clients' journeys. We should act, not just react.

The authors of the following papers have looked at what is happening today and what is coming in the future. They present predictions and solutions that we should be thinking about and more importantly talking to our clients about right now.

- Keely Dukes shares with us a fantastic voyage that has already begun by describing technology that is already in use, what is coming and some of the legal issues that have already been identified.

- Frank Deasey (with the able help of his son Michael) introduces us to "nanotechnology" and, based on the historical development of other litigation monsters, lays out the likely development of liability in this emerging field.

- Ed Ruff (with the assistance of Quinn Donnelly) focuses how the use of nanotechnology in the medical arena will impact medical liability claims in the future.

- Finally, Jeannette Dixon takes us into the world of cyber-attacks on medical technology, potential litigation related to those attacks and how regulation can be used to address those risks.

We hope that the papers spark your interest to learn more about nanotechnology and what is happening now in the tech world, but also to think about what might be over the horizon. Take this information and brainstorm what this means for your practice. Think about what legislation and regulation might be needed. Think about what your clients should be doing right now. Think about you are going to respond when the first flux-capacitor or nanobot lawsuit lands on your desk. The first left turn car case was not much different from a left turn buggy case. Will an injectable nanobot be different from an external EKG? Time will tell, but why not power up your flux-capacitor to head into the future now.

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The Fantastic Voyage from Science Fiction to Reality: The Brave New World of Modern Medical Technology

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I. Introduction

What was once the subject of science fiction is now becoming modern medical fact. The newly developed and developing medical technologies seem so "far-fetched" that they have uncanny resemblances to technologies from works of fiction written decades ago. While some of these technologies are still in the nascent stages of their development, it is clear that in this ever-changing world of medicine, what was imagined in our past is now here today. Although commonplace today, MRIs, PET scans, pacemakers, pharmacologic treatments, and organ implant surgeries were revolutionary advances in their time. Such will be the case twenty years from now when some of the medical technologies – which include nanotechnology, 24-hour non-invasive monitoring of our vital signs, the ability to read minds with computers, and others – become a part of our everyday lives.

While there are hundreds of revolutionary medical technologies in the works, here are just a few ground breaking advancements.

II. Nano-Medicine: Good Things in Small Packages

In the world of medicine, smaller is better. For this reason, nanotechnology is at the forefront of many modern diagnostic treatment and monitoring medical technologies, providing a number of diagnostic, treatment, and preventative applications.

For example, under development at Harvard's Wyss Institute, the DNA "cage" is a system that uses nanobots to deliver toxic payloads directly to cancer cells.[1] The DNA cage, as its name suggests, is made of DNA strands

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[1] Sarah Griffiths, *Nanorobots trial to begin in humans: Microscopic DNA devices could be injected into a leukemia patient in a bid to destroy abnormal cells*, Dailymail.Com, March 18, 2015, available at http://www.dailymail.co.uk/sciencetech/article-2927410/The-real-life-Matrix-MIT-researchers-reveal-interface-allow-computer-plug-brain.html.

that are formed into a box with hinges that open when exposed to specific molecules. *Id.* These "cages" are injected directly into a patient's blood stream and, as they pass through the body in the blood stream, the hinges are triggered upon contact with the cancerous cells and the "cage" releases its toxic payload in the direct vicinity of the cancerous cells." *Id.*

Due to the precision afforded by this technology, the side effects caused by current cancer treatment should be significantly reduced. *Id.* Moreover, it is anticipated that the accuracy of this delivery system will enable doctors to use toxins that are deemed too dangerous to be used in conventional cancer treatments because instead of being introduced broadly into the body, they isolate and directly destroy the cancer cells. *Id.*

This technology is a springboard to other ideas. For example, the nano-developers envision the use of the "cage" as a preventive technology, similar to flu vaccinations, where people get inoculated on a regular basis. *Id.* The developers also think this technology will eventually be used to repair previously irreparable tissues, such as the spinal cord. *Id.*

The development of nano-medicine has not stopped here; researchers have increasingly focused on "smart weapons" in battling disease and injury. Researchers have, for example, developed nanobots that were inspired by the shape of the E. coli bacteria.[2] *Id.* These devices are currently not as small as the DNA cage, but they have one significant advantage, in that they can be remotely controlled. *Id.* A magnetized flagellum, a whip like cellular organelle used by single cell organisms for movement, is attached to the body of the nanobot. *Id.* The nanobots are then injected into the targeted tissue and controlled by externally generated magnetic fields. *Id.* The hope is that one day surgeons will be able to control these devices with simple joysticks. *Id.*

These nanobots have already been tested in the sensitive environment of eyes. *Id.* After "swimming" through a gel like substance called the vitreous humor, these nanobots successfully delivered drugs directly to the retinal area of the eye. *Id.* Planned future uses for these E. coli-nanobots also include treatment of other sensitive tissues, such as the brain, small intestine, and urinary tract. *Id.*

Again, however, technology is moving rapidly not only to "smart weapon" nanotechnology, but data-gathering nanotechnology. One prime example is smart dust. This technology has been in development by the United States

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[2] Jacopo Prisco, *Will nanotechnology soon allow you to 'swallow the doctor'?*, CNN.com, January 30, 2015, available at http://www.cnn.com/2015/01/29/tech/mci-nanobots-eth/.

military since the 1990s.[3] Smart dust is a monitoring system consisting of many nanobots that are capable of measuring light, temperature, vibration, magnetism, and chemicals. *Id.* While the most recent devices are not yet microscopic because current technology requires batteries to power them, it is predicted that within this decade, "smart dust" nanobots will be developed that are one millimeter or less. *Id.* Although most of its applications are currently being developed for military purposes, some commenters forecast that medical applications for smart dust will eventually be developed.[4]

III. Jacking In: Mind-Reading Computers

The brain itself is also on the forefront of breakthrough medical technology. One of these innovations is reminiscent of a technology that played center stage in the Matrix franchise.[5] Researchers at MIT have developed extremely thin micro-fibers that are very flexible and enable computers to directly interact with the brain. *Id.* While there are conventional technologies that interact with the brain, they are limited to recording a single type of signal. *Id.* These newly developed microfibers are vastly superior because they are capable of sending messages, receiving messages, and delivering drugs to specific tissues of the brain. *Id.* In addition to monitoring brain signals, this system could deliver drugs, and at the same time, monitor the brain as it reacts to the drugs. *Id.*

These fibers start out as relatively large polymer preforms that are slowly stretched into thin fibers, less than the width of a single human hair. *Id.* The resulting fibers are flexible and can come into direct contact brain tissues without causing harm. *Id.* The fibers are also strong enough to maintain their shape and structural integrity through the stretching process. *Id.* Components that were previously measured in inches can now be made microns in size. *Id.* While this technology cannot be used to instantaneously teach a patient kung-fu or fly a helicopter, it will enable computers to interact with the brain on more sophisticated level than conventional technologies.

In a similar vein, researchers at Harvard have begun injecting flexible electronic circuits into the brains of living mice, in an effort to cross the lines

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[3] Bruno Delepierre, *Smart Dust: the Smart Equivalent of Magic Pixie Dust*, Happonomy.org, August 18, 2015, available at http://www.happonomy.org/our-world/feel-at-ease/smart-dust.

[4] *What is Smart Dust?*, WiseGeek.com, available at http://www.wisegeek.com/what-is-smart-dust.htm.

[5] *The real life Matrix: MIT researchers reveal interface that can allow a computer to plug into the brain*, TheDailyMail.com, available at http://www.dailymail.co.uk/sciencetech/article-2927410/The-real-life-Matrix-MIT-researchers-reveal-interface-allow-computer-plug-brain.html.

between electronic circuits and neuro circuits.[6] Similar to micro-polymers, these electronic circuits are preferable to conventional technologies due to their small size and flexibility. *Id.* Current technologies rely on electrical impulses sent to the brain and are large, inflexible, and require major surgeries to be implanted. *Id.* Electrical meshes, which are made from metal and plastic woven together, are one hundred thousand times more flexible than the conventional devices and can be injected with a syringe. *Id.* In the future, these devices might be able to deliver drugs in addition to sending and receiving messages. *Id.*

IV. Bond's Q Comes to Medicine: Cutting Edge Medical Apparel

The wrist watch is a conventional technology that has been around for well over a century, gaining popularity first as a ladies' fashion item and then as a practical tool for trench warfare during WWI. After teetering on the edge of obsolescence with the rise of cell phones (which effectively doubled as pocket-watches), recent developments have brought wrist watches back to the front line of preventive medical technology. The most notable example of this modern wrist watch is the Fitbit, a device that, in its simplest form, functions as an advanced, data-tracking pedometer.[7] The Fitbit uses a "3-axis accelerometer" to record the movements of the user.[8] The measurements taken by the Fitbit's accelerometer are analyzed by an algorithm that identifies motion patterns and discerns between steps and other motions. *Id.* The Fitbit takes this information and synchronizes it with the user's computer to track the user's physical activity.[9] The result is a device that turns human movements into raw data. *Id.*

But the reinvention of the wrist watch does not end there. Another new spin on wristwatches are devices that monitor the user's blood pressure. One example of this technology was developed by Hewlett-Packard and a company based out of Singapore called Healthstats.[10] Conventional blood pressure

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[6] Devin Powell, *A Flexible Circuit Has Been Injected Into Living Brains*, Smithsonian.com, June 8, 2015, available at http://www.smithsonianmag.com/science-nature/flexible-circuit-has-been-injected-living-brains-180955525/.

[7] David Sedaris, *Stepping Out: Living the Fitbit Life*, the New Yorker, June 30, 2014, available at http://www.newyorker.com/magazine/2014/06/30/stepping-out-3.

[8] Help.fitbit.com, available at https://help.fitbit.com/articles/en_US/Help_article/How-does-my-tracker-count-steps.

[9] Sedaris, *supra* note 7.

[10] Emily Singer, *A Wristwatch that Monitors Blood Pressure*, MIT Technology Review, June 30, 2013, available at http://www.technologyreview.com/news/424539/a-wristwatch-that-monitors-blood-pressure/.

measurements are typically taken by health care professionals during an appointment; however, due to the infrequency of appointments, physicians have a very limited understanding of their patient's blood pressure outside of the exam room. *Id.* A wireless monitor changes this informational dynamic by, instead, continually measuring and recording the patient's blood pressure. *Id.* These monitors detect blood pressure with sensors that measure the shape of a pressure waive as blood passes through an artery in the wrist. *Id.* The data recorded by the devices is transferred to the user's cell phone then to the cloud where it can be accessed by physicians. *Id.*

The macabre is a theme that is prevalent in many works of science fiction, and it is equally existent in the process currently being used by Google to develop a wristwatch that can detect cancer.[11] In order to ensure accuracy and realism during development, researchers at Google X laboratories in California are also growing human skin and using it as a covering for model arms, to see how light travels through human skin. *Id.* These "watches" (more accurately, monitors) are expected to detect cancer, heart attacks, and possibly other diseases. *Id.* With this monitoring technology, "patients will swallow a pill containing nano-particles" which are engineered to attach to specific "markers" associated with cancer and other diseases. *Id.* In turn, after the nano-particles attach to the diseased cells, they cause the cells to "light up" in a way that can be detected with the monitoring system. *Id.* The wristband itself is magnetic and the nano-particles are attracted to the magnet as they pass through the blood stream. *Id.*

Wearable technology, however, does not end at wrist watches. Smart tattoos, a technology which can also be used to monitor the body, have been in development for years, but current versions are difficult to power due to their size.[12] One method being evaluated that might power these smart tattoos utilizes the lactic acid contained in sweat. *Id.* Lactic acid is a byproduct of metabolic processes, but is also used by the brain as an energy source during strenuous physical activity. *Id.* The result is a smart tattoo that can generate up to 70 microwatts per cm^2 of skin. *Id.* Such a tool would allow for monitoring of vital signs, but without having to physically wear an external piece of technology. *Id.*

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[11] Lizzie Dearden, *Google is making human skin as part of research into 'wristband that can detect cancer'*, Independent, January 31, 2015, available at http://www.independent.co.uk/news/science/google-is-making-human-skin-as-part-of-research-into-wristband-that-can-detect-cancer-10015423.html.

[12] John Hewitt, *Smart tattoo generates electricity from sweat, could power future wearable computers*, ExtremeTech.com, August 15, 2014, available at http://www.extremetech.com/extreme/188088-smart-tattoo-generates-power-from-sweat.

These monitoring systems ultimately generate data which may itself be forwarded to servers for analysis either specific to the patient[13] or aggregated for general study purposes. [14] Already, the collection of health information has piqued the interest of the FTC and inspired Apple to modify developer licenses in an effort to protect user privacy. [15] These are not small questions, nor hypotheticals, given that 12% of consumers around the world are already using wearables.

V. **And This Is Just The Beginning.**

The future prospect of an artificial intelligence – such as Watson, of Jeopardy fame – making a treatment decision, rather than a human physician, is a very real prospect. [16] This, in turn, raises even more far-fetched concepts from the realm of science fiction, such as the potential for computers struggling with conflicting instructions (as with the HAL 9000 in *2001: A Space Odyssey*) and the need to proactively provide guidelines to A.I.s to protect human lives (such as with Isaac Asimov's Three Laws of Robotics).

From magical smart dust to mind reading computer interfaces, modern medical technology is changing the ways in which medicine is administered and patients are evaluated and treated. Cancer treatments are working faster and some forms of cancer, if not all forms of cancer, might someday be prevented by injectable nanobots. Computers will be able to directly communicate with the brain and monitor drugs as they are directly administered to brain tissues, all without the need of major surgery. While we may never inject microscopic submarines full of scientists into our blood stream, other forms of nanotechnology will ultimately provide the kind of medical care that only science fiction has dreamt of to this point.

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[13] Rajeev S. Kapoor, *Will Technology Replace the Physician to Diagnose and Treat Diseases?*, LinkedIn Pulse, Aug. 29, 2015, available at https://www.linkedin.com/pulse/technology-replace-physician-diagnose-treat-diseases-rajeev-s-kapoor.

[14] Jania Matthews, *Johns Hopkins Researchers to Use Apple Watch Data To Study Epilepsy*, Hub, Johns Hopkins University, Oct. 15, 2015, available at http://hub.jhu.edu/2015/10/15/apple-watch-epiwatch.

[15] Aditi Pai, *Report: FTC, Apple Discuss Apple Watch and Health Data Privacy*, MobiHealthNews, Nov. 17, 2014, available at http://mobihealthnews.com/38315/report-ftc-apple-discuss-apple-watch-and-health-data-privacy.

[16] *Artificial Intelligence and the Healthcare Sector*, Boston Commons High Tech Network, October 2015, available at http://bostoncommons.net/2015/10/artificial-intelligence-and-the-healthcare-sector/.

NANOTECHNOLOGY LITIGATION BOOM OR BUST

BY

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With special thanks to my son, Michael Ryan Deasey

I. INTRODUCTION

Nanotechnology has been broadly defined as "the understanding and control of matter at dimensions between approximately 1 and 100 nanometers (nm) where unique physical properties enable novel applications of existing materials.[1] Nanoparticles are defined as being less than 100 nanometers or 1 billionth of a meter. While there are several chemical compounds used in nanotechnology engineering, the most common compounds are silver, carbon, zinc, silver, titanium and gold. Products engineered using nanotechnology cover the spectrum of industrial, medical, and consumer products. In 2014, it was estimated that over 1400 products utilized nanotechnology engineered components. Nanotechnology is at the forefront of the medical device industry. Due to the size of engineered nanoparticles, studies have shown that these nanoparticles are more easily absorbed through skin and inhaled by humans because of their unnaturally small size, making them impervious to some of the human body's normal defense mechanisms. Many consumer products today, including food products contain nanoparticles. Within the manufacturing segment of our economy, utilization of nano-engineered particles is used commonly raising the specter of the potential for workers compensation claims. Products containing nano-engineered particles are used commonly in the United Stated which could give rise to individual or mass tort product liability litigation. The EPA predicts that by the end of 2015, consumer products with nanotechnology applications will value US $1 trillion on the world market.[2]

Environmental groups, consumer advocate groups, OSHA, the insurance industry and certain segments of the manufacturing industry have all expressed concern about the potential effects of utilizing nanotechnology engineered products. In some circles nanotechnology engineered products has been described as the next asbestos litigation. In other circles, there are predictions of uncontrollable (yet unspecified) environmental consequences from the dispersal of nanoparticles into the world's atmosphere and water supply.

Fortunately, our research has not revealed any lawsuit alleging injury caused by a product containing nanotechnology engineered particles. Thus, we are left to predict whether nanotechnology will be the next mass tort litigation (predicted to be many times larger than asbestos litigation) or simply a revolutionary breakthrough in science for the benefit and welfare for the world's inhabitants. Compounding the problem of predicting the potential for

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[1] National Nanotechnology Initiative ("NNI"), http://www.nano.gov/.

[2] Nanotechnology and Asbestos, Catherine M. Krow, 2012.

nanotechnology litigation is the dearth of scientific, reliable studies demonstrating a causal link between nanotechnology and injuries/death to humans. Several criticized studies involving mice have led to the conclusion that carbon nanotubes (which physically resemble asbestos fibers) may cause lung inflammation and granuloma development, potentially leading to mesothelioma.[3]

Further complicating the predictability of nanotechnology related litigation, is the extraordinarily different chemical, electrical, magnetic and optical qualities of nanomaterials from the same substance in larger form. For example, stable materials like aluminum can become combustible in nanoparticle form; malleable materials such as carbon can become stronger than steel; electrical insulators can become conductors; insoluble materials can become soluble; metals can change color (gold can turn red) or appear invisible.

Furthermore, nanoparticles are highly reactive because they have exceptionally high surface areas in relation to their mass, and are generally highly mobile. Nanoparticles can disburse rapidly in gasses and liquids, and may be able to pass through some membranes and even the blood-brain barrier.[4]

II. USES OF NANOPARTICLES

The use of nanoparticles increases daily. Three particular nanoparticles, carbon nanotubes (CNTs), nano sized titanium dioxide (TiO_2) and nanosilver have raised concerns regarding the potential for health risks associated with the manufacture and use of products containing these nanoparticles. CNTs nanoparticles are used in:

- Interconnective material and electrical circuits;
- Strength and performance enhancer in fabrics;
- Sports equipment and building materials;
- Biological gas and chemical sensors;
- Smart packaging to detect harmful bacteria in food; and
- Drug delivery applications.

TiO_2 nanoparticles are used in:

[3] Poland, et al, Nature Nanotechnology, "Carbon nanotubes induced into the body cavity of mice show asbestos like pathology in a pilot study, 20 May, 2008; Takagi, et al, "introduction of mesothelioma in P53 +/- mouse by intraperitoneal application of multi-wall carbon nanotubes," J. Toxicol. Sci 33:105-16, 2008.

[4] Law 360 New York, August 15, 2010.

- Paints;
- Coatings;
- Varnishes;
- Sunscreens; and
- Cosmetics.

Due to its antibacterial and antimicrobial properties, nanosilver is used in:

- Polymer coatings in bandages, medical devices, foods, storage containers, household appliances and feminine hygiene products;
- Swimming pool cleanser replacing chlorine; and
- Sheets and clothing.

III. THE POTENTIAL FOR LITIGATION

Presently, there are concerns; there is debate; there is research but there is no nanotechnology litigation. In some circles, it has been suggested that the lack of litigation is due in large measure to the fact that there are no epidemiological studies linking a disease and/or environmental problem to the use of nanotechnology engineered products. In other circles it has been suggested that the widespread use of nanotechnology in engineered products is so new that research into its potentially harmful effects on humans and the environment has not caught up with its ever expanding use. However, as we have learned from the experience of asbestos and other mass tort litigations, it is only a matter of time before a linkage is found (or perhaps created by ingenious attorneys) between nanotechnology engineered products and human disease and/or adverse environmental consequences.

If we examine the asbestos and other mass tort related litigations, we will find that the potential areas of litigation include:

- Work-related injuries (workers compensation claims);
- Individual or mass tort product liability litigation;
- Environmental impact litigation; and
- Consumer fraud litigation.

Staying with the prediction game, let us examine how and when each of these litigations could evolve:

A. WORKERS COMPENSATION CLAIMS

As with any product placed in the stream of commerce, it must be engineered and manufactured. By definition, this will involve the close interplay between nanoparticles and human beings. As discussed above, it has been shown that nanoparticles can either be inhaled or absorbed into the human body. Studies have found (although they are criticized) that certain inhaled nanoparticles can cause pleural effusion in the lungs. Another study has suggested that due to the similarity of the nanoparticle and asbestos fiber, the potential for an asbestos-like injury exists. In fact, in one of its informational fact sheets, OSHA has highlighted the potential for worker exposure to nanoparticles in a number of situations including:

- Inhaled nanoparticles may be deposited in the respiratory tract and may cause inflammation and damage to lungs, cells, and tissues. *E.g.* carbon nanotubes may be capable of causing pulmonary inflammation and fibrosis,[5]
- Titanium dioxide (TiO_2) is used in commercial applications such as paint, paper, cosmetics, and food and has been determined by NIOSH that nanoscale TiO_2 have higher mass-base potency than larger particles, and occupational exposure (by inhalation) to nanoscale TiO_2 particles should be considered a potential occupational carcinogen,[6]
- Certain nanoparticles may penetrate some membranes and may cause damage to intracellular structures and cellular functions;[7]
- Some nanomaterials may act as chemical catalysts and produce unanticipated reactions, creating a risk of explosions and fires;[8] and
- Some types of nanoparticle dust may be combustible and require less energy to ignite than larger dust particles (sugar or wood) creating the risk of explosions and fires.[9]

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[5] *See* Civ. 65 - Occupational Exposure to Nanocarbontubes and Nanofibers published by NIOSH in 2013.

[6] *See* Civ. 63- Occupational Exposure to Titanium Dioxide, published by NIOSH in April, 2011.

[7] Approaches to Safe Nanotechnology; Managing the Health and Safety Concerns Associated with Engineered Nanomaterials, published by National Institute for Safety and Health (NIOSH) in March, 2009.

[8] *See* Approaches to Safe Nanotechnology.

[9] *See* Approaches to Safe Nanotechnology; *see* OSHA Fact Worksheet titled "Working Safely with Nanomaterials".

It is clear from the foregoing that OSHA is concerned about the potential for human health risks in the utilization of nanoparticles in the manufacturing process. Unlike a typical tort action, an employee injured on the job need not show an employer's negligence to sustain a workers compensation claim. The injured worker need only show injury in the course and scope of employment coupled with an injury sustained while in the course and scope of that employment. Given OSHA's concern for detrimental health effects related to the utilization of nanoproducts in the development and manufacture of products, it is more probable than not that workers suffering diseases which cannot be linked to other exposure scenarios will be able to recover workers compensation benefits due to exposure to nanoparticles.

B. ASBESTOS AND/OR MASS TORT LITIGATION

Unlike the workers compensation venue, a plaintiff in mass tort litigation must prove liability, causation, and damages. Before the first wave of asbestos litigation, most lawyers, including litigation defense lawyers had never heard of asbestos much less pleural thickening or mesothelioma. Once it was established that exposure to asbestos was the only universally recognized cause of mesothelioma, the plaintiff's burden of proving causation was virtually eliminated. In the pleural-thickening cases, causation still remained an issue but only to the extent that the defense could establish other potential causes for pleural thickening.

Utilizing the asbestos experience as a guideline, it is a virtual certainty that if a reputable study links the exposure to nanoparticles (through ingestion, absorption, or otherwise) to a disease such as mesothelioma, pleural thickening or pleural effusion, persons exposed to nanotechnology engineered products will undoubtedly be able to sustain their burden of proof regarding causation.

Likewise, the potential exists for consumer litigation involving injury or death caused by the distribution and sale of nano-engineered products and/or products containing nanoparticles. Without a doubt, the use of such products will expand exponentially in the coming years as science (the use of nanoparticles in products) outpaces research (into potential harmful effects of nanoparticles in consumer products). Given the widespread use of nanoparticles in consumer products today, the potential for a wave of consumer litigation involving populations of claimants exponentially larger than asbestos claimants is very real.

While the plaintiffs' bar may be poised for this next wave of tort litigation, they are certainly hamstrung in proving the linkage between exposure to

nanoparticles and a particular disease mechanism. Typically, courts require such linkage in the form of epidemiological studies and expert opinion. To date, the known studies involve mice and have come under criticism. The emergence of any reliable study suggesting linkage would prove to be the catalyst for future mass tort litigation.

As with any product liability lawsuit, we foresee the potential for claims arising out of:

- Product defect (strict liability and tort);
- Negligence in the design, manufacture and sale of products;
- Failure to warn.

In those states which have adopted strict liability in tort, plaintiffs need only prove that a product containing nano-engineered components is defective and dangerous. Assuming that a reputable epidemiological study links such particles to a particular disease, the present obstacles facing plaintiffs in proving product defect in nano-engineered products will be lessened. For those states employing a negligence-based form of product liability, plaintiffs will seek to establish that the company manufacturing such products did not adequately test and/or analyze the potentially harmful effects of utilizing nano-engineered particles in its products. Finally, with respect to a failure to warn theory of liability, plaintiffs will seek to establish that the product did not adequately inform the consuming public of the potential health risks involved in utilizing a product containing nano-engineered particles.

C. CONSUMER FRAUD/CONSUMER PROTECTION LITIGATION

Unlike mass tort litigation, consumer protection claims (individual or class action) typically do not involve claims of personal injury. Rather, such claims seek economic damages in the form of a refund for the cost of the product. Since the claim is for economic damages only, such claimants do not necessarily face the burden of proving causation between the product and the injury alleged. In this scenario, the claimant can allege that had he/she known of the potential risk of using a product containing nanoparticles, he/she would not have purchased the product. Many state consumer protection statutes do not require complex proof of elements such as "actual reliance" that are required to support a claim of fraud.[10]

The potential exposure in such cases lies not with the recoverable damages, but with the potential attorneys' fees awarded in the context of class

[10] James W. Mizgera & Michael Lisak, Nanotechnology's Manufacturer's Duty to Warn and Potential Affirmative Defenses, 2011 Prod. Safety & Liab. Rep., April 11 (2011).

action litigation. Consider, for example, a consumer class action involving a popular sunscreen. The potential class could be nationwide and involve literally thousands and thousands of consumers. While the number of class members who actually receive a refund may be relatively small (in comparison to the number of consumers purchasing the sunscreen) the attorneys' fees could very likely be extraordinarily significant. When one considers the number of consumer products utilizing nanoparticles presently, coupled with the expansion of such use in additional consumer products, there will undoubtedly be an increase in the potential for additional consumer protection claims.

D. ENVIRONMENTAL IMPACT CLAIMS

Perhaps least understood of potential claims arising out of the use of nanoparticles and nanotechnology engineered products, is the potential for environmental claims. While there has been speculation in the scientific community that dispersal of nanoparticles into the water can have a detrimental effect on aquatic life, there is no definitive study which supports this notion. This is due, in part, to the fact that measuring concentrations of such nanoparticles is extremely difficult. Moreover, there has been no scientific research into how nanoparticles in the water adversely affects aquatic life. The same holds true for human beings. There have been no authoritative studies demonstrating human consumption of water containing nanoparticles can result in deleterious health effects.

Having said this, the potential for this type of litigation cannot be ignored. The inability of the nanotechnology industry to recognize the potential for adverse environmental impacts only compounds the problem. Without understanding the potential adverse environmental risks, the nanotechnology industry may find it difficult to establish protections against such risks.

IV. CONCLUSION

Predictions are just that… Predictions. If asked to handicap the potential for litigation arising out of the use of nanoparticles in the manufacturing process of nanotechnology engineered products, the odds would favor workers compensation claims as the first wave of litigation. Nanotechnology is already on OSHA's radar screen. As noted above, OSHA has already expressed its concern for adverse workplace effects on workers in the nanotechnology industry.

Without the benefit of a credible epidemiological study linking nanoparticles with a disease process, we believe the next wave of litigation favored by the plaintiff's bar will be utilization of consumer protection statutes. While such litigation would be of inconsequential benefit to the consuming

public, it would represent a tremendous windfall for attorneys instituting class actions alleging violation of consumer protection statutes. The proliferation of products containing nanotechnology engineered particles makes for a potentially nightmarish scenario for the nanotechnology industry. It is not beyond reason to suggest that within ten years the majority of the world's population will be using products containing nanotechnology engineered particles. Given the number of products involved and the population utilizing those products, how long will it take for the plaintiffs bar to recognize nanotechnology engineered products as the focal point of the next wave of consumer protection class actions? Perhaps in a nanosecond!

NANO TORTS:

The Not So Small Problems that Come with the Use of Nanotechnology in the Medical Context

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I. INTRODUCTION

One of the biggest developing areas in the medical field involves the use and application of some of the smallest medical technologies. The field of Nanotechnology encompasses science, engineering, and technology conducted at the nanoscale, or between 1 nanometer and 100 nanometers in size. The prefix "Nano" which comes from the Ancient Greek word for "dwarf" is used to describe particles that are 40,000 times smaller than the thickness of a human hair. To lend perspective, an inch is comprised of 25,400,000 nanometers, a sheet of newspaper is around 100,000 nanometers thick. [1]

In the medical field, nanotechnology provides significant opportunities to pioneer new treatments, revolutionize drug delivery methods, improve diagnostic abilities, assist with cell repair, prevent infection, and to provide new methods of therapy.[2] With the advent of these technological developments and innovative treatment methods there necessarily exists an added level of risk and uncertainty that create additional challenges from a legal perspective.

While at the early stages of development the legal issues facing the field of nanotechnology primarily involve intellectual property disputes surrounding the creation and use of the technology, as the medical applications continue to develop it is inevitable that medical malpractice actions will follow. In anticipating litigation it is critical that physicians, scientists, and attorneys are well apprised of how the current legal environment will adapt to accommodate these evolving technologies.

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[1] *What is Nanotechnology?*, Nano.gov, http://www.nano.gov/nanotech-101/what/definition (last visited Dec. 16, 2015).

[2] *Nanotechnology in Medicine – Nanomedicine*, UnderstandingNano.com, http://www.understandingnano.com/medicine.html (last visited Dec. 16, 2015).

II. Medical Malpractice and Nanotechnology

In the medical malpractice context there are three main areas that have the potential to expose physicians to liability in their use of emerging nanotechnology in their care and treatment of patients. Namely, informed consent, standard of care, and patient privacy. Medical professionals strive to provide the best and most effective care and treatment for their patients attorneys are charged with limiting the exposure of these medical professionals to liability, while supporting them in their pursuit of advances in the medical field.

A. Informed Consent

At the outset of any treatment relationship medical professionals are required to obtain the informed consent of their patients for the anticipated treatment. The requirement of informed consent is designed to further the patient's right to self-decision by providing them with all relevant medical information to empower them to make an informed decision relating to his or her medical care and treatment. [3]

Physicians are both ethically and legally required to obtain the informed consent of their patients and doing so properly helps to prevent a later claim of medical malpractice. While the requirements vary from state to state, a physician's failure to obtain the informed consent of their patient universally exposes them to liability for negligence and/or medical battery, and most certainly constitutes medical malpractice.

Generally when obtaining informed consent the physician should disclose and discuss: the diagnosis, the nature and purpose of the proposed treatment or procedure, the risks and benefits of the proposed treatment or procedure, alternative treatments available, the risks and benefits of any alternatives that exist, the risks and benefits of not receiving the contemplated treatment or procedure, any personal or economic interests that may influence the physicians' judgment, and all diagnostic tests that may rule out other possible conditions.[4]

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[3] *Opinion 8.08 Informed Consent*, American Medical Association, http://www.ama-assn.org/ama/pub/physician-resources/medical-ethics/code-medical-ethics/opinion808.page (last visited Dec. 16, 2015).

[4] *Informed Consent: What Must a Physician Disclose to a Patient*, AMA Journal of Ethics, http://journalofethics.ama-assn.org/2012/07/hlaw1-1207.html (last visited Dec. 15. 2015); *See generally Canterbury v Spence*, 464 F2d 772 (DC Cir 1972); *Gates v Jenson*, 595 P2d 919

In undertaking to obtain a patient's informed consent relating to a procedure or treatment that utilizes nanotechnology there remain many uncertainties that create a great amount of risk for both the patient and in turn the physician. While the court in *Canterbury v. Spence* noted that a physician is charged to communicate to the patient only those risks of which he is aware, it suggested that while the nondisclosure of an unknown risk may not present a problem in relation to the physicians duty to disclose, it likely will pose a problem in relation to the physician's duty to have known of the risk.[5] As a result, physicians should be cautioned to make patients aware of not only the known risks, but to stress the possibility of unknown risks due to the revolutionary nature of these emerging treatments. Some courts have even held that a physician may have a legal duty to inform the patient of that physician's experience level in a certain area of medicine.[6]

In order to avoid issues relating to the inadequacy of informed consent medical professionals who are using nanotechnology in treating their patients should be sure to obtain full written consent from each patient prior to the procedure. The consent form should clearly lay out the specific known risks and benefits as well as a clear statement indicating the possible existence of risks and benefits that are unknown at the time of the treatment. Most importantly, the physician should ensure that the patient actually understands the proposed treatment options, the risks and benefits, both known and unknown, as well as the physician's level of experience related to the specific procedure contemplated. By informing and educating the patient while obtaining consent the physician can provide quality care while avoiding potential liability. In advising clients, attorneys should strive to strike the balance between protecting their clients from the exposure to liability, while allowing them to most effectively serve their patients while advancing the field of medicine.

B. <u>Standard of Care</u>

The variety of and increasing applications of nanotechnology in the medical field is sure to create several different treatments and procedures each with their own unique standard of care. At the heart of nearly all claims sounding in medical malpractice is an alleged deviation from the standard of

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(Wash 1979); *Jandre v Physicians Insurance Co of Wisconsin*, 330 Wis 2d 50, 792 NW2d 558 (Wis Ct App 2010); *Arato v Avedon*, 5 Cal 4th 1172, 858 P2d 598 (1993).

[5] *Canterbury v Spence*, 464 F2d 772, 787 n.84 (DC Cir 1972).

[6] *Johnson v Kokemoor*, 545 NW2d 495 (Wis 1996).

care. While the specific formulation of the "standard of care" varies slightly by jurisdiction it generally encompasses that "a medical professional must possess and use the knowledge, skill, and care ordinarily used by a reasonably careful medical professional under the same or similar circumstances."[7] Generally, to prevail on a claim for medical negligence the plaintiff bears the burden of proving, by way of expert testimony, that the defendant failed to conform to the applicable standard of care.

The nascent nature of the applications of nanotechnology to the medical field makes it more difficult for the plaintiff to carry their burden. Initially, the plaintiff would be charged to elicit testimony from an expert witness defining the proper standard of care under circumstances involving the use of nanotechnology. In some jurisdictions, such as Illinois, there is a requirement that the expert who testifies regarding the practitioner's deviation (or compliance) with the standard of care must be a licensed member of the school of medicine about which he or she is providing an opinion, and likewise must be familiar with the ordinary methods, procedures, and treatment available to the practitioner.[8]

Presently, the use of nanotechnology is contemplated to span a number of areas of medicine from drug delivery, to therapy, to diagnostic techniques, but the limits of the application of these new technologies is not known. Likewise, the application is mostly theoretical. Without any basis of comparison it is difficult to impossible to identify what the applicable standard of care is in these new cases. As a result, it is likely that claims of alleged medical malpractice in this emerging area will devolve into a "battle of experts."

At the outset the pool of experts will likely include researchers like those at MIT that have developed a sensor using carbon nanotubes that when embedded into a gel and injected under the skin can be used to monitor inflammatory diseases or those at the University of Illinois who are using gelatin nanoparticles to deliver drugs to damaged brain tissue.[9] Eventually, as physicians and other medical professionals begin to use these revolutionary treatments and methods those physicians and medical professionals will fill witness chairs to serve as experts in establishing what the proper standard of care is in an action of alleged medical malpractice relating to the use of nanotechnology in a medical case.

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[7] *See* Illinois Pattern Jury Instruction 105.00.

[8] *Mozer v. Kerth*, 224 Ill.App.3d 525, 586 N.E.2d 759 (1st Dist. 1992).

[9] *Nanotechnology in Medicine – Nanomedicine*, UnderstandingNano.com, http://www.understandingnano.com/medicine.html (last visited Dec. 16, 2015).

Where the alleged injury resulted from a failure to diagnose as a result of an error of the device as opposed to the physician, the patient may be able to assert both a claim against the physician as well as a products liability action against the manufacturer of the device. In the action against the physician proper warnings and adequate informed consent will go a long way in defending the claim, but where the technology is so new it is far from certain what the result will be.

In the early cases, it is also worth noting that where the requisite informed consent is not obtained (as discussed above), testimony relating to standard of care may simply be elicited to establish that due to the inadequate consent, the physicians decision to utilize nanotechnology to address an ailment that has another more "traditional" treatment method is in and of itself a violation of the standard of care. In any event, carefully obtained consent, and the careful compliance with the proper procedures relating to the nanotech medical treatment is the surest path to avoiding liability.

C. Patient Privacy – HIPAA compliance

Patient privacy is another critical consideration in evaluating the future use and application of nanotechnology to medical treatment. While a majority of the current contemplated applications of nanotechnology in the medical field involve the manipulation of atoms and molecules to actively treat disease, prevent infection, provide therapy, and repair cells, there is the potential that in the years to come the further development of nanobots and other more sophisticated nanodevices could allow for live-action health monitoring and diagnostic abilities. Similar, wearable health and fitness tracking devices like the well-known Fitbit already exist and are in use on a larger scale, employed by people around the world to track activity, fitness, sleep patterns, heart rates, and much more.

A recent article in the *Journal of Sensor Technology*, discusses the potential for wearable sensors for remote healthcare monitoring, which would allow the use of a miniaturized physical sensors to track and report live health data to a physician.[10] Nanotechnology creates an even greater potential for not only remote monitoring, but remote treatment. The notion that a physician could both monitor and treat a patient remotely creates new opportunities for the further advancement of medicine.

While emerging technologies create great opportunities for the advancement of a medical professional's ability to monitor and treat patient

[10] Abidoye, *Using Wearable Sensors for Remote Healthcare Monitoring Systems*, Journal of Sensor Technology, Jun. 2011, http://www.scirp.org/journal/PaperInformation.aspx?PaperID=5570.

needs these opportunities carry with them risks of non-compliance with existing laws. Specifically, HIPAA, which was designed to ensure the confidentiality of all healthcare information, seems to suggest that all protected health information collected by wearable or internal devices that is transmitted to external servers or individuals must be transported and stored in compliance with HIPAA. While, technically HIPAA only applies to "covered entities" to get any meaningful use out of the information collected by wearable and internal health monitoring devices the patient would need to share that information with at the bare minimum their physician who under the act is considered a "covered entity."[11]

In order to maximize the utility of these emerging technologies, the developers of the devices, the storage and data sharing platform, the medical providers, and the patient are best suited if the entire process is HIPAA compliant. By ensuring strict compliance with HIPAA all parties avoid liability by acting to prevent the disclosure of patient data. In the event that the patient data is inadvertently disclosed liability should be assigned to the party who was in the best position to prevent that disclosure.

To further limit exposure, especially in the early stages of development of these technologies the medical care providers as well as the technology service providers could request authorizations obtaining the precautionary consent for inadvertent disclosure. While requiring authorizations for use may limit the overall field of willing users, it provides a trade-off to the clear benefits of this new technology. Ideally, both medical professionals and the technological support organizations will work to ensure HIPAA compliance at all junctures.

III. Conclusion

Improvements are generally not without cost or risk, and the same is true in this instance. The undeniable benefits that the nanotechnology and wearable and internal medical monitoring devices provide are well worth the risks faced by the medical professionals in implementing these emerging and developing technologies. With careful planning, and an understanding of both existing legal concepts and their application to these new circumstances both attorneys and medical professionals can work together to advance the field of medicine while limiting the exposure to liability. Just as the knowledge gained by physicians through the use of this new technology will help them better serve their patients; an enhanced knowledge of these new technologies will help attorneys' better serve medical professionals.

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[11] *Health Information Privacy: For Covered Entities and Business Associates*, U.S. Department of Health & Human Services, http://www.hhs.gov/ocr/privacy/hipaa/understanding/coveredentities/index.html (last visited Dec. 16, 2015).

The Cyber-Insecurity of Implantable Medical Devices and What Needs to Be Done to Protect Manufacturers, Prescribers and Patients

By

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I. Introduction

Implantable medical devices (IMDs) such as pacemakers, neuro-stimulators and drug delivery pumps have transformed healthcare by increasing the interconnectivity between medical devices and other clinical systems. IMDs save innumerable lives as they keep various illnesses controlled by providing healthcare providers immediate, real-time access to patient information which permits the remote diagnoses of disease or adjustment of prescriptions. There are approximately 300,000 IMDs implanted in patients every year[1]. To date more than 2.5 million people rely on IMDs. This reliance rate is forecast to increase by 7.7% by the end of 2015.

No longer stand-alone devices, IMDs are not afforded the protection against the cybersecurity attack that was once provided by stand-alone segregation. With increased interconnectivity between medical devices and clinical systems, the safety of IMDs are vulnerable to security breaches by hackers. The challenge to protect IMDs from hackers is exacerbated with the ever increasing usage of wireless, internet-and-network-connected devices to monitor and exchange health related information.

Research experts have discovered that wireless links used by clinicians in heart-regulating pacemakers and insulin delivering pumps to interrogate and update these devices also left these medical devices exposed to cybersecurity hackers. Advanced hacking tools and methodologies allow hackers to easily take advantage of the poor security mechanisms of IMDs permitting them to easily change the default settings or deliver remote

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[1] C. Zahn, W.B. Banine, A. Sedrakyan, and S. Claudia. Cardia device implantation in the US from 1997 through 2004; A population-based analysis. Journal of General Internal Medicine, 2007).

commands. For example, a hacker seeking to make a malicious attack against a drug delivery pump may disconnect the pumps' safeguard and turn-off the device or deliver a hazardous does of medicine to the patient. A hacker can also capture, rebroadcast the signal, and possibly shut down an implanted heart defibrillator leaving the patient in serious danger.

Recognizing that a cybersecurity breach of an IMD potentially places the patient's safety at risk, the greatest challenge for manufacturers, clinicians, hospitals and regulatory body is to find a way to respond to an every evolving cybersecurity environment while ensuring the patients safety. However, due to lack of governance of IMDs, lack of awareness of the actual security risk, and lack of preparation by organizations to deal with the risks, a coordinated proactive approach is the only way to limit the vulnerability of IMDs and ultimately protect the patient.

II. Cyber Vulnerabilities of IMDs

Although hackers have yet to exploit the cyber vulnerabilities that currently exist in IMDs, the fact remains that cyber security of these devices is often not regulated and as a result the devices remain dangerously insecure. Authentication or encryption safeguards to prevent signals from being captured is impossible due to the IMDs limited battery life.

There are three primary types of cyber-attacks that can occur against an IMD that may disrupt the functionality of the device or network connected to the device and potentially harm patients: (1) unauthorized access, (2) malware, and (3) a denial-of-service or distributed-denial-of service (DDoS) attack. Unauthorized access to an IMD occurs when a malicious actor intercepts and alters signals that are sent wirelessly to a medical device. Since IMDs use embedded computers and radios to monitor chronic disorders and treat patients, a hacker could intercept the signals and disrupt the functioning of the device. Malware is a malicious software program designed to carry out annoying or harmful actions. As manufacturers and hospitals continue to rely on off-the-shelf software, the threat of a cyber-attack to an IMD due to malware increases. A DDoS attack generally disables an IMD by continual and excessive attempts to communicate with the device, which may ultimately slow or block the devices functionality or drain the device's battery.

Cyber vulnerabilities are weaknesses that may be exploited by hackers allowing them to breach the security of an IMD’s software, operating system, its’ network connection, or the device itself. The only way to minimize the possibility of an cyber-attack against an IMD is to mitigate the risk by manufacturers, healthcare providers and governmental regulatory and legal systems sharing the responsibility for maintaining device functionality,

integrity and confidentiality of information, patient privacy, device and information availability; all which will ultimately prevent an adverse effect on patient safety.[2]

III. Governance of Cyber-attacks Against IMDs

There is currently no standard of care and very few laws that govern the role of medical device manufacturers and healthcare providers in protecting against cyber-attacks of IMDs. The three legal structures that currently govern cyber-attacks on medical devices and hospital networks are (a) statutory such as the Computer Fraud and Abuse Act, 18 U.S.C. §1030 (CFAA); (b) regulatory such as the FDA (Federal Food, Drug and Cosmetic Act (FDCA)) and HHS (Health Insurance Portability and Accountability Act (HIPAA)); and (c) common law principles.

A. Federal Statutes

The CFAA was created to deter malicious actors behind cyber-attacks through the punishment of individuals, who knowingly and intentionally conduct malicious cyber-attacks against a protected computer that recklessly cause damage, with imprisonment, fines or penalties. Under the CFAA's broad definition of the word 'computer', it can be argued that the prosecution of an individual, who knowingly and intentionally cyber-attacks an IMD that causes direct or indirect harm to a patient, would be in violation of the CFAA. The statutory language of the CFAA makes it a criminal act for a cyber-attack against a protected computer that causes $5,000 or more in damage, physically harms a patient, potentially modifies or impairs a patient diagnosis or treatment, or poses a threat to public health or safety. Recent case law supports the argument that a cyber-attack on an IMD would violate the CFAA. In *United States v. Kramer*, the Eight Circuit stated that the definition of a computer in the CFAA "is exceedingly broad…This definition captures any device that makes use of an electronic data processor."[3] Furthermore, the Seventh Circuit in *United States v. Mitra*,[4] applying the definition of a computer in the CFAA found that a cell phone was a computer. Hence, in accordance with case law established in both *Kramer* and *Mitra*, IMDs that contain either a computer chip or perform basic data processing functions should be protected under the CFAA.

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[2] US Food Drug Administration. Content of Premarket Submissions for Management for Cybersecurity in Medical Devices. US Food and Drug Administration; 2014. Available from http://www.fda.gov/downloads/medicaldevices/deviceregulationandguidance/guidancedocuments/ucm356190.pdf.

[3] *See, United States v. Kramer*, 631 F.3d 900 (8th Cir. 2011).

[4] See, *United States v. Mitra*, 405 F. 3d 492, 495 (7th Cir. 2005).

While penalties under the CFAA or other federal statutes created to address cyber-attacks against medical devices are large with prison sentencing ranging from 5 to 25 years, even large penalties may fail to deter hackers where identification of the perpetrator is very difficult. Even once identified, prosecuting a malicious actor criminally is usually impossible because the hacker can easily hide their identity, cover their tracks, or place the blame on others by spoofing the source.

B. Federal Regulation

Authorities within the healthcare industry recommend that Congress determine whether the FDA or HHS take the lead in protecting IMDs against cyber-attacks. However, as the FDA's guidance adopts the same general principles of confidentiality, integrity and availability as HIPAA, Congress may require that the FDA and HHS work together to develop a joint regulatory scheme to deal with cyber-attacks.

i. FDA

Recognizing that the vulnerability in medical devices that results in compromised device functionality, loss of data availability or integrity, or exposure of other connected devices or networks may potentially result in patient illness, injury or death, the FDA issued a non-binding draft guidance entitled *Guidance for Industry and Food and Drug Administration Staff* in June 2013 (FDA Guidance).[5] The purpose of the FDA Guidance is to provide recommendations for managing cybersecurity risks to protect the patient and the information contained, created and processed by the medical devices for manufacturers to consider and information to include in medical devices to prevent cyber breaches and mitigate the risk to patients. The FDA Guidance recommends that manufacturers establish a cybersecurity vulnerability and management approach, which utilizes cybersecurity core functions identify, protect, detect, respond and recover; as part of its software validation and risk analysis.[6] This approach should identify assets, threats and vulnerabilities; the impact of threats and vulnerabilities on device functionality and patients; the likelihood of a threat and of a vulnerability being exploited; risk levels and

[5] US Food Drug Administration. Content of Premarket Submissions for Management of Cybersecurity in Medical Devices. US Food and Drug Administration; 2014. Available from: http://www.fda.gov/downloads/medicaldevices/deviceregulationandguidance/guidancedocuments/ucm356190.pdf.

[6] 21 CFR Part 820 – Quality Systems Regulations, 21 CFR 820.30 Subpart C – Design Controls of the Quality System Regulation.

suitable mitigation strategies; and assessment of residual risk and risk assessment criteria.[7]

The main issue with the FDA Guidance is that it is not mandatory, compliance could be costly and medical device manufacturers may choose not to adopt the FDA's approach on cybersecurity. Therefore, cybersecurity of medical devices remain at an all-time low level and is virtually nonexistent in many companies despite the severity of the hacking threat.

New legal and regulatory frameworks are needed to ensure that medical device manufacturers and healthcare providers protect against cyber-attacks. There are three possible approaches that should be considered as a starting point for considering solutions to cybersecurity threats: (1) industry self-regulation; (2) equipping the FDA with expanded authority and resources to identify and address security risks before cyber-attacks occurs; or (3) the creation of a new legislative framework to address cyber-attacks.

ii. <u>HHS</u>

While industry self-regulation and FDA reform may help, until courts have the opportunity to flesh out a standard of care to incentivize medical device manufacturers and hospitals to take additional cybersecurity precautions, Congress may need to expand HIPAA. Currently HIPAA, governs the information security of hospital networks but does it not apply to cyber-attacks that do not involve patient health information. Expansion of HIPAA may incentivize medical device manufacturers and hospitals to protect against cyber-attacks through the imposition of fines on medical device manufacturers and healthcare providers if a cyber-attack on an IMD occurs This approach is believed to be in line with the Obama administration, which has focused on setting "performance objectives", rather than specifying the behavior or manner of compliance that regulated entities must adopt.[8]

HIPAA has four tiers of culpability if a patient data breach occurs. The first tier covers unknown violations that an individual would not have known through the exercise of due diligence; the second tier covers violations due to lack of reasonable care and not due to willful neglect; the third tier covers willful violations due to neglect that are discovered within a certain period of time; and the fourth tier covers violations that are due to willful neglect that

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[7] Content of Premarket Submissions for Management of Cybersecurity in Medical Devices. Guidance for Industry and Food and Drug Administration Staff. October 2, 2014.

[8] Exec. Order No. 1353, 76 Fed. Reg. 3821(Jan 21, 2011).

are not corrected in a timely manner. The damages for HIPAA violations range from $100 to $50,000 per violation with any annual maximum penalty of $1.5 million.[9]

A similar sliding scale approach could be used by Congress to incentivize medical device manufacturers and healthcare providers to adopt cybersecurity measures. This approach would force medical device manufacturers and healthcare providers to forecast future threats rather than rely on FDA or HHS standards. It will also incentivize the industry to rapidly adapt to changing threats or face liability. In the alternative, Congress could direct HHS to amend HIPAA to cover cyber-attacks and to make medical manufacturers liable. With either approach, Congress or the FDA would have to define the types of cybersecurity violations that would trigger liability and which entities would face penalties.

C. Common Law

Common law principles may impose liability on medical device manufacturers and healthcare providers that negligently fail to protect against cyber-attacks. However, similar to criminal prosecution, so long as it remains difficult to identify and prosecute the hackers responsible for cyber-attacks, common law may also be an insufficient deterrent to manufacturers to prevent cyber-attacks against IMD or medical devices connected to hospital networks. Until case law is developed it remains unclear how cyber-attacks against medical devices will play out in court. It is believed that the success of a suit filed by a patient injured by a cyber-attack against an IMD against a medical device manufacturers or hospitals for negligence will depend upon how the court treats the 'superseding cause doctrine' and on how the court views the defendant's standard of care. It is also believed that state courts will eventually develop doctrines that impose liability on medical device manufacturers and hospitals that negligently fail to take precautions against cyber-attacks.

[9] HIPAA Administration Simplification: Enforcement, 74 Fed. Reg. 56127 (Oct 30, 2009) (to be codified at 45 C.F.R. pt 160).

IV. Conclusion

Due to the fact that the current legal structure does not adequately deter malicious actors from launching cyber-attacks nor focus on the role of healthcare providers and medical device manufacturers in protecting against cyber-attacks, IMD patients remain at risk for malicious cyber-attacks. As it is only a matter of time until a malicious actor hacks an IMD or hospital network connected to a medical device and harms a patient, Congress, regulators, healthcare providers, and medical device manufacturer all owe responsibilities to patients and need to proactively address potential cyber-attacks against IMDs and medical devices connected to hospital networks.

FAST TRACK JURY TRIALS: THE JUDICIAL FAST PASS

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Fast Track Jury Trials: The Judicial Fast Pass

BRADISH J. WARING *

I. INTRODUCTION

It is the 21st century and everything is fast: fans check their cellphones for real-time scores of their favorite games, high school students read the "Spark Notes" version of assigned novels, and parents buy fast passes to avoid the lines at popular theme parks. In short, modern consumers have come to expect, and desire, speed. One area that arguably has not kept pace is the legal field. In the appropriate case, Fast Track jury trials have the potential to significantly expedite the manner in which jury trials are conducted in South Carolina.

With the rise of mandatory Alternative Dispute Resolution ("ADR") in the last couple of decades, the oft cited "burdensome and expensive" jury trial in many jurisdictions has tip-toed along the border of extinction.[1] Ironically, despite the declining percentage of cases that are actually tried to verdict, courts in many states have struggled to keep up with the increasing number of lawsuits filling up their dockets. This conundrum is particularly evident in South Carolina, where the caseload per Circuit Court Judge consistently ranks among the highest in the country. In fact, as of 2010, South Carolina had the fewest judges per population, with one judge for every 100,000 residents. The state also had more than twice the national average of filings

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* Member, Nexsen Pruet, LLC; the author would like to acknowledge the assistance of both Kara S. Grevey and Clinton T. Magill, both former summer associates at Nexsen Pruet for their kind assistance with this paper.

[1] There are many published articles about the "vanishing jury trial" and the reasons therefor. Though the topic is beyond the scope of this article, most of the scholarship on the phenomenon places at least part of the blame for fewer jury trials on the rise of ADR. For an interesting contrary viewpoint, *see*, Gene Roberts, *Whether The Vanishing (Civil) Jury Trial?* On the blog, "Gene's Desk", a*vailable at*, http://genesdesk.com/2015/03/04the-vanishing-civil-jury-trial/.

per judge, with each judge handling an estimated 5,060 filings per year. By comparison, the national average was 3.1 judges per 100,000 people and 1,780 filings per judge per year.[2]

In the larger metropolitan circuits in South Carolina, it routinely takes over two years from the time of initial case filing to receive a trial. In the face of this, active members of the South Carolina Bar came together in an attempt to propose a new form of ADR available on a statewide basis which would include the inherent integrity of a jury verdict. Was it really so far-fetched, they asked, to develop a new ADR methodology which had the potential to assist in unclogging crowded Circuit Court dockets while simultaneously providing trial lawyers an opportunity to either establish or improve their skills in the courtroom? What if litigants could replace mandatory mediations with a new process that would not only achieve the underlying benefits of arbitration; but would also provide litigants with their "day in court?" After seven years of hard work, such a process was developed, and in March 2013 the South Carolina Fast Track jury trial officially became a new tool in the alternative dispute resolution arsenal.

At its essence, the Fast Track jury trial is really just a new, albeit novel, type of ADR with a jury: "A Fast Track jury trial is a voluntary, binding jury trial, before a reduced jury panel and a mutually selected Special Hearing Officer."[3] "The mode and method of presentation of evidence can be traditional or the parties may agree on procedures to streamline the process, often in a manner similar to what is done in arbitrations."[4] Fast Track jury trials have the potential to alter the civil judicial landscape in South Carolina. The process is particularly effective for resolving certain categories of civil disputes, primarily those cases with only a few

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[2] Jean Hoefer Toal, C.J., S.C. Sup. Ct., State of Judiciary Address, (February 20, 2013), *available at,* http://www.judicial.state.sc.us/whatsnew/archivedItems.cfm?archYear=2013 .

[3] Fast Track Jury Trials Administrative Order, Appellate Case No. 2013-000389, March 7, 2013. [hereinafter Fast Track Order]; attached hereto at Appendix I.

[4] *Id.*

contested liability issues, and/or where the appropriate amount of damages or other remedy is in dispute.[5] Because of its flexible nature, the Fast Track process offers multiple advantages over other traditional ADR options.

This article explains the background and implementation of the Fast Track process in South Carolina, how the process typically works, some of its flexibilities, and the various advantages of the Fast Track jury trial.

II. BACKGROUND

In South Carolina, many attorneys nostalgically recall the old county court system which was in existence prior to the passage of the *Judicial Reform Act of 1976*.[6] These pre-ADR courts offered attorneys the option of litigating smaller civil claims in the alternate county court system rather than in the Circuit Court. The county courts were statutorily authorized to operate in a particular county with limited jurisdiction in both criminal and civil cases. For example, the county court in Charleston imposed a $12,000.00 limit on civil verdicts. This provided lawyers with the opportunity to try cases without fear of an excess verdict. County court judges were elected by the Legislature in much the same manner as Circuit Court Judges. Juries were reduced to six people; the parties were subject to the *South Carolina Rules of Evidence*; and aggrieved parties were entitled to full appellate review. Trials rarely took longer than 2-3 days. Before the rise of ADR, these courts operated as a quick and efficient alternative means of disposing of smaller contested disputes. The county courts also had the salubrious effect of providing young lawyers with the ability to gain valuable trial experience.

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[5] While personal injury cases are often well suited for the Fast Track jury trial system, breach of contract and other commercial disputes have been successfully tried to conclusion using the Fast Track option. .

[6] 1976 Act No. 690

In the late 1980's, some judges in the Charleston Division of the United States District Court began experimenting with "summary jury trials".[7] The genesis for the summary jury trial process was the then unique ADR method pioneered in 1980 by Judge Thomas Lambros, District Court Judge for the Northern District of Ohio.[8] His model consisted of an abbreviated, nonbinding alternative dispute resolution process "developed. . . as a way for litigants to obtain an indication of how a [reduced] jury would likely decide a case, providing a basis for subsequent settlement negotiations."[9] Although his model - which he termed "summary jury trials" - was initially successful,[10] its use dissipated in that federal district after Judge Lambros retired.

Back in South Carolina, following the elimination of the county courts, as noted, the Circuit Courts in South Carolina became extremely backlogged. In an attempt to alleviate the increasing length of time it took to climb the trial docket, Charleston lawyers, in the late 1990's began experimenting using the summary jury trial process in the Circuit Court.[11] The process caught on, and the results were fairly impressive. From 2010 through the end of 2012, the Charleston County Clerk of Court reported that approximately 40 percent of trials in the Circuit Court were tried to verdict in this manner.[12]

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[7] NATIONAL CLENTER FOR STATE COURTS, SHORT, SUMMARY & EXPIDITED: THE EVOLUTION OF CIVIL JURY TRIALS at 1-3 (2012), *available at* http://www.ncsc.org/SJT/ .

[8] *Id,* at 5-7.

[9] *Id,* at 5.

[10] From 1980-1984, in the Northern District of Ohio, 88 cases were selected for summary jury trial. More than half settled before the summary jury trial was held and 92% of the remaining cases settled after. *Id,* at 6.

[11] Matthew J. Story & Brittany F. Boykin, *Fast Track Jury Trials: the Abbreviation of the Traditional Jury Trial,* S.C. LAWYER MAGAZINE, July, 2013, at 38, 38.

[12] *Id,* at 38.

However, despite its relative success, some questions remained as to the ultimate utility of the summary jury trial model. Because most of the trials were non-binding,[13] an unhappy litigant could simply continue to pursue the matter in the Circuit Court. Thus, the goal of speedy resolution was thwarted and in some cases, the length of time to final verdict increased. Concomitantly, many litigants actually saw overall costs increase due to the need to try the case twice. Moreover, the nonbinding nature of the process frequently had no effect on decreasing the number of cases pending trial in the Circuit Court, something the Bench and Bar in South Carolina recognized as a growing hindrance to the effective administration of justice throughout the state.

Based in part upon the Charleston County summary jury trial experience, in 2006 the leadership of the South Carolina Bar suggested that an approach be made to South Carolina Chief Justice Jean Toal to inquire if the Supreme Court would be amenable to a Petition for the adoption of a new form of binding ADR with a jury trial component. In 2007, the Bar delivered its Petition, and in March 2013, nearly six years later, Chief Justice Toal delivered an Administrative Order authorizing the voluntary use of the Fast Track jury trial process as an alternative ADR technique throughout the state.[14]

III. THE FAST TRACK JURY TRIAL EXPLAINED

Ok, so what exactly does a Fast Track jury trial actually look like? This is a question Sam Clawson, managing member of the Clawson & Staubes LLC and a pioneer of summary jury trials in South Carolina, hears quite often. His usual reply is, "*well, what do you want it to look*

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[13] While occasionally parties would agree to make the trial binding, this was not the common practice.

[14] Fast Track Order, *supra* ("I find that a Fast Track jury trial process has been used on an *ad hoc* basis in South Carolina and has proven to be successful. Allowing implementation statewide will be beneficial to the public and aid in the efficient use of limited judicial resources.").

like?" While seemingly elusive, his response is actually an honest and accurate one. While the Rules and Procedures adopted by the South Carolina Supreme Court establish the basic framework for a standard Fast Track jury trial, the litigants are free to make modifications to the process. At a June 7, 2013 CLE on the issue, Chief Justice Toal acknowledged that the parties must first understand and accept the "binding, non-appealable nature of the [process]," but noted that "there certainly are many tweaks available."[15] Key features of the South Carolina Fast Track process are explained below as are a discussion of some of the various flexibilities available to the parties. A copy of the Administrative Order, "*Rules and Procedures for the Fast Track Jury Trial Process*", "*Consent Order: Fast Track Jury Trial and Appointment of Special Hearing Officer*", and a sample "*Opening Charge to the Jury*" in a negligence action are provided in the Appendices to this article.

A. The Basic Concept

As noted, a fast track jury trial is a voluntary, binding jury trial, before a reduced jury panel and a mutually selected Special Hearing Officer. The mode and method of presentation of evidence can be traditional or the parties may agree on procedures to streamline the process, often in a manner similar to what is done in arbitrations.[16] Fast Track jury trials are defined by their unique flexibility: the parties, by agreement, control how the case will be presented to the jury. In South Carolina, there are some mandatory features of a Fast Track jury trial, but there are also many modifications that can be made by agreement of the parties.

B. Mandatory Provisions of the Order

1. *Consent of Parties*

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[15] South Carolina Bar, *Fast Break on Fast Track Jury Trials: How It Will Work*, June 7, 2013, *available at* http://www.scbar.org/ . [hereinafter SC Bar, Fast Break on Fast Track].

[16] Fast Track Order, *supra.*

Both parties must consent to having their case tried via Fast Track. This entails entering into an agreement as to the date of the trial and the identity of the Hearing Officer. If the parties cannot reach an agreement as to the lawyer (or judge) who will preside, Fast Track cannot go forward. The parties can, however, agree to let a Circuit Court Judge decide on a Hearing Officer for the litigants. Once the parties agree, they submit the *Consent Order Granting a Fast Track Jury Trial and Appointing a Special Hearing Officer*[17] to the Chief Administrative Circuit Court judge who thereafter approves the Consent Order, which is then filed with the Clerk of Court. The agreement then becomes irrevocably binding and becomes exempt from the mandatory Court Annexed ADR Rules.

2. *No Right to Appeal and Costs*

The parties agree to waive the right to appeal the jury's determination, absent allegations of fraud. Following the jury verdict, the Clerk of Court is not required to enter judgment except upon motion to the Circuit Court and a showing that the jury's verdict has not been satisfied. Furthermore, the parties agree to waive costs and disbursements though the parties can agree to have the prevailing party pay some fees, such as the Hearing Officer's fee.

3. *Scheduling*

Fast Track trials are scheduled with the Clerk of Court in the county where the case is filed. After the parties file the Consent Order with the Clerk or Court, the case will be removed from the docket and a mutually convenient trial date will be set. Because Circuit Court proceedings have priority over Fast Track, space or staff will be allocated as may be available and suitable only after all of the needs of regularly scheduled courtroom business is met.

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[17] See, "*Consent Order: Fast Track Jury Trial and Appointment of Special Hearing Officer*", attached at Appendix III.

4. *Evidentiary Requirements*

If a party plans to offer documentary evidence at trial, they are required to serve copies of the evidence no less than 30 days before the trial, unless the parties modify that period. If a party intends to call a live expert witness, they must provide written notice to all parties and an opportunity for that expert to be deposed. Any claim for future lost earnings premised upon lost opportunity, promotion, career advancement, or similar theory shall only be proven by expert testimony or the report of any expert previously exchanged pursuant to the rules. Pretrial evidentiary issues, such as motions *in limine* and redaction of documentary evidence, will be determined in conformance with the applicable rules of evidence or the agreement of the parties at a pretrial conference held ten days prior to trial unless that period is modified by the parties in the consent order.

5. *Jury Selection*

Fast Track juries consist of a maximum of six jurors, selected from a *venire* called for a regular term of court. The Circuit Court allows each side two peremptory challenges. If the parties desire, they can agree to fewer jurors; however, Fast Track does not provide for the use of alternate jurors. Consequently, if a juror is lost during the proceedings the trial will still go forward, but with one less juror. Finally, the verdict rendered by the jury must be unanimous.

6. *Verdicts*

In the event of inconsistent verdicts, the Special Hearing Officer shall recharge the jury as appropriate and have it return to deliberation to resolve any inconsistency. Stipulations relating to high/low parameters cannot be disclosed to the jury, and if the case involves incapacitated or minor persons, the Circuit Court Judge who assigns the case to Fast Track trial

must approve any high/low parameters prior to the trial "in the same manner the Circuit Court would approve a settlement involving such persons."

7. *Special Hearing Officers*

Special Hearing Officers must be selected by the mutual consent of the parties. The Special Hearing Officer must be a member in good standing of the South Carolina Bar and must have completed the trial experiences required by the applicable *South Carolina Appellate Court Rule*.[18] The parties shall determine the compensation, if any, of the attorney appointed to serve as the Special Hearing Officer.

C. Some Flexibilities Which Fast Track Offers

1. *Evidentiary Matters*

Fast Track allows for and encourages a relaxation of the *Rules of Evidence*. In the Consent Order, the parties may agree to modify the evidentiary rules and are encouraged to stipulate to any mode and method of presentation that will expedite the process. The parties may agree to the admissibility of *ex parte* evidence including statements, video, and/or depositions. They can also agree to the admissibility of medical records and lost wage statements without the usual requirements of authentication. Finally, the parties can agree to limit the number of lay and expert witnesses. The parties are encouraged to present summaries, individual notebooks of exhibits for the jurors, and any other innovative methods of presentation. Stipulations to factual and evidentiary matters are encouraged "to the greatest extent possible." The parties are also free to deviate from the classic order of trial presentation as long as they agree and stipulate to the deviation.

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[18] Rule 403, SCACR.

2. *Verdicts*

Perhaps one of the most unique aspects of Fast Track is the encouragement of stipulations to high/low verdict parameters. A high/low stipulation in essence creates a floor and a ceiling for the litigants even where the jury verdict results in either less than the low or more that the high. Parties can also stipulate in writing that any pre-trial offer and demand remain "on the table" throughout the Fast Track jury trail. If the parties enter into such a stipulation, either side may elect to accept the last settlement proposal of the opponent at any time before the jury announces its verdict.

3. *Hearing Officers*

Another significant "tweak" that differentiates Fast Track from a regular trial is the presence of a "Special Hearing Officer," rather than a regular judge elected by the South Carolina Legislature. As noted above, the parties can agree for any lawyer to hear their case, as long as he or she is a member in good standing of the South Carolina Bar and has completed the trial experiences required by Rule 403, SCACR. However, to the extent they are available and willing; sitting Circuit Court judges are also available to preside over Fast Track trials. There is no requirement that the lawyer, retired judge, or current judge - whoever is selected - be a resident of the county in which the case will be heard. The parties also determine the compensation, if any, of the attorney appointed to serve as Special Hearing Officer. Additionally, according to Chief Justice Toal, because the solemnities of the proceedings are crucial to the success of the system and real jurors are involved, decorum is to be observed as it would be in a Circuit Court trial. In this regard, Special Hearing Officers wear robes[19], and are

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[19] See, sample "*Opening Charge to the Jury*", attached at Appendix III.

referred to as "Your Honor". While sitting, they also and have access to "back of the courthouse" chambers in the same manner as a Circuit Court Judge.[20]

D. The Advantages of Fast Track

The aim of all civil trials is to "secure the just, speedy, and inexpensive determination of every action." [21] Fast Track jury trials have the potential to make this lofty goal a reality.

1. *Advantages to Litigants*

The first and most obvious beneficiaries of Fast Track are the litigants themselves. The trials are extremely time-efficient, taking place on a mutually-set date, and usually lasting no longer than one to three days. "One of the beauties of this new program is that so many agreements can be made ahead of time," notes Paul Wickensimer, Clerk of Court for Greenville County. [22] Because the parties are able to relax evidentiary rules and authentication requirements, alter the standard order of presentation, waive any pre-or post-trial motions, and limit the number of experts and witnesses, the trial itself can be significantly streamlined, and, therefore, trial time is significantly reduced. The result is a fast and less expensive route for the parties to the litigation to receive a final determination of their dispute.

The allowance for and encouragement to set high/low parameters can also be enormously beneficial to the parties. In the average Fast Track matter, the low figure will almost always at least be enough to cover the Plaintiff's out-of-pocket litigation costs.[23] Usually however, the low figure is set at or near the defendants' evaluation of settlement value. The high figure will

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[20] SC Bar, *Fast Break on Fast Track, supra.*

[21] Rule 1, SCRCivP; Rule 1, FRCivP.

[22] SC Bar, *Fast Break on Fast Track, supra,* ("We want [the Special Hearing Officer] to look like a judge and be thought of by the jury as a judge.")

[23] *See* Steven Croley, *Summary Jury Trials in Charleston County, South Carolina,* 41 LOY. L.A.L. REV. 1585, 1612–13 (2008).

typically be the available insurance policy limit.[24] This type of agreement thus benefits both parties. The plaintiff is guaranteed not to go home empty handed, and the defendant(s) and their insurer(s) avoid any possibility of an excess verdict. In many cases, once the high/low agreement is set, the plaintiff may be able to immediately secure a check for the agreed low figure - a huge incentive for plaintiffs to agree to the proposed parameters. Additionally, the added expense of mandatory mediation is averted once the parties agree to Fast Track. Lastly, litigants get "their day in court" and have a real jury decide the contested issue(s) with finality.

2. *Advantages to Lawyers and the Courts*

The notion of the "vanishing jury trial" is not an illusion; it is a very real and current dilemma faced by courts in South Carolina and those across the country. Data on federal civil cases shows a decline in cases resolved by trial from 11.5% in 1962 to 1.8% in 2002, illustrating the historic trend away from trials.[25] There can be no doubt that there is a real concern about the lack of trial experiences available, or put differently, the lack of opportunity for lawyers to get on their feet - to get in the courtroom and present a case to a jury. Fast Track aims to get lawyers back in the courtroom. Doing so generates an opportunity for young attorneys to gain valuable trial experience and allows more practiced lawyers a chance to "dust off the cobwebs." A real benefit to practitioners in South Carolina, which utilizes a traditional "rolling docket", is the ability to have their cases set for a "date certain" and not be subject to the uncertainties of a rolling roster. Thus, attorneys gain from increased certainty in their schedules. The Fast Track system can likewise result in the maximization of judicial resources and the reduction in case

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[24] *Id,* at 1613.

[25] IAALS, A RETURN TO TRIALS: IMPLEMENTING EFFECTIVE SHORT, SUMMARY, AND EXPEDITED CIVIL ACTION PROGRAMS 1 n.1 (2012) . Furthermore, according to state court disposition data collected by NCSC from 2000 to 2009, the percentage of civil jury trials dropped from 47.5% across the period to a low 0.5% in 2009. *Id.*

backlog. Selecting Hearing Officers to preside over truncated disputes with limited issues will allow Circuit Court Judges to hear more complex, time-consuming cases.

3. *Advantages to Jurors and Witnesses*

Because Fast Track jury trials are limited to one to three days, jurors have less disruption in their lives. The anecdotal evidence is that the simplified and streamlined manner of presentation makes the process appear more professional and less antagonistic to many jurors. Likewise, because the parties are encouraged to submit most testimony by video or in written documentary fashion, fewer witness schedules are disrupted. The strain on witnesses having to leave work and wait to be called for live testimony is significantly reduced.

IV. FACING FEARS

I am apprehensive about a lawyer sitting as a "judge" on my case; these folks are not trained judges. Such apprehension is misplaced. Fast Track is really just a modified form of arbitration. If attorneys can serve impartially as arbitrators, they can certainly serve as Special Hearing Officers. In fact, in arbitration, the arbitrator(s) is asked to decide the ultimate issue(s) in the case on both liability and damages. In a Fast Track trial, the jury generally makes those decisions. Just as lawyers in a given jurisdiction know who the best mediators are, the best hearing officers will come to the fore. According to retired South Carolina Circuit Court Judge John Hamilton Smith, "The hearing officer must establish a reputation for being fair, it's just that simple. As long as the hearing officer gives the parties a fair shake, that's all good lawyers want and all good lawyers should expect." Besides, if lingering doubts exist, the parties can always select a retired or sitting Circuit Court Judge, if available.

I don't like waiving my client's rights to appeal. While it is true that parties consenting to Fast Track waive their right to appeal absent evidence of fraud, this is the same rule in most

arbitrations. The rule is a consequence of the process's greatest strength: flexibility. Because the parties pre-determine every aspect of their case - bending evidentiary rules and the like - verdicts are not appropriate for appeals. Furthermore, allowing for appeals only defeats Fast Track's purpose of providing speedy and inexpensive jury trials. Two factors may mitigate any fears relating to a waiver of appellate rights. First, the parties are entitled to make post-trial motions following the verdict, unless an agreement has been made to waive them. Thus, should grounds exist; the Special Hearing Officer can grant post trial relief. Second, the parties can agree that any pre-trial offer and/or demand remain unaltered throughout the trial. Thus, if a party thinks the trial went badly, they may elect to accept the last settlement offer or agree to the demand of their opponent(s) at any time before the verdict is announced.

OK, I'm sold on the process. Now, how do I convince my client that it is the best alternative for them, especially where my opponent is recommending it? Given the competitive nature of litigation, the common thinking is that if Fast Track is recommended by one's opponent(s) it must benefit them in some way. Nothing could be further from the truth. When it comes to saving clients' money and getting them a quick and final resolution from a jury, Fast Track is mutually beneficial. From a plaintiff attorney's perspective, one benefit of Fast Track is that it can buffer clients' unreasonable expectations. As Carl Solomon, of the Solomon Law Group in Columbia, South Carolina asserts, "You have to know your client's case and the values you are working with. Agreeing to a high/low eliminates the opportunity of a 'bell-ringer' award, but it also eliminates the chance of getting zero. Explain to your client that what matters is not what they get, but what they keep."[26] Because a Fast Track plaintiff will often to pay have much less in costs, their net award is likely to be larger.

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[26] SC Bar, *Fast Break on Fast Track, supra.*

Persuading defendants and insurers on the opposite side of the "v" also involves a discussion of money. According to Sam Clawson, "the key is money - it must make economic sense. Describe the decreased preparation costs and expert fees. In addition, the high-low option can limit their exposure on the 'high' end." According to Clawson, "You cannot always guarantee that your client will like the verdict, but they will like the Fast Track process." [27]

V. CONCLUSION

Realizing that no parent desires to stand in line at Disney World on a 95 degree day in July, the Disney marketing team got savvy and developed the "Fast Pass" program. For a small additional sum, parents and their children could gain admission to a much shorter line to the same ride with the same ups and downs. Unfortunately, for most, litigation will never be as enjoyable as an amusement park ride; however, Fast Track jury trials have the ability to afford all parties the metaphorical "fast pass" to justice.

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[27] *Id.*

APPENDIX

I. ADMINISTRATIVE ORDER; RULES AND PROCEDURES FOR FAST TRACK JURY TRIAL PROCESS

II. CONSENT ORDER: FAST TRACK JURY TRIAL AND APPOINTMENT OF SPECIAL HEARING OFFICER

III. SAMPLE OPENING CHARGE TO THE JURY IN A FAST TRACK NEGLIGENCE CASE

The Supreme Court of South Carolina

Re: Fast Track Jury Trials

Appellate Case No.: 2013-000389

ADMINISTRATIVE ORDER

Pursuant to the provisions of Article V, § 4 of the South Carolina Constitution, I find that a Fast Track jury trial process has been used on an *ad hoc* basis in South Carolina and has proven to be successful. Allowing implementation statewide will be beneficial to the public and aid in the efficient use of limited judicial resources.

I adopt the attached procedures and form for the voluntary use of the Fast Track jury trial process statewide. The Fast Track jury trial process may be implemented by the Chief Administrative Judge. This order is effective upon the date of my signature.

Jean Hoefer Toal,
Chief Justice of South Carolina

March 2013
Columbia, South Carolina

APPENDIX I

RULES AND PROCEDURES FOR THE FAST TRACK JURY TRIAL PROCESS

Nature of the Binding Fast Track Jury Trial: A Fast Track jury trial is a voluntary, binding jury trial, before a reduced jury panel and a mutually selected Special Hearing Officer. The mode and method of presentation of evidence can be traditional or the parties may agree on procedures to streamline the process, often in a manner similar to what is done in arbitrations. In the absence of agreement of counsel, adopted in the Consent Order Granting a Fast Track Jury Trial and Appointing a Special Hearing Officer, the process and rules that follow shall apply:

1. **Consent of Parties:** The parties to the Consent Order Granting a Fast Track Jury Trial and Appointing a Special Hearing Officer represent that they have the authority of their respective clients and/or insurance carriers to enter into the agreement. This agreement shall be irrevocably binding upon the parties absent fraud.

2. **Stipulation:** If the parties agree to a Fast Track jury trial, the parties shall file a Consent Order Granting a Fast Track Jury Trial and Appointing a Special Hearing Officer. Additionally, a written stipulation may be signed by the attorneys reciting any high/low parameters. The high/low parameters of a Fast Track jury trial, if any, shall not be disclosed to the jury.

3. **No Right to Appeal and Costs:** The parties further agree to waive the right to appeal from the determination of this matter, absent allegations of fraud. Written Findings of Fact and Conclusions of Law shall not be required. Following the jury verdict, the Clerk of Court shall not enter judgment except upon motion to the Circuit Court and a showing that the jury's verdict has not been satisfied. The parties agree to waive costs and disbursements.

4. **Mediation and Arbitration:** Where the parties consent to a Fast Track jury trial, the case is exempt from mandatory mediation and/or arbitration.

5. **Scheduling:** Fast Track jury trials are scheduled with the Clerk of Court in the county where the case is filed. The parties shall provide the Clerk of Court with a filed copy of the Consent Order Granting a Fast Track Jury Trial and Appointing a Special Hearing Officer. The case shall be removed from the docket and a mutually convenient trial date shall be set. Fast Track

jury trials shall not have any priority over any regularly scheduled courtroom proceeding or courtroom staff. The Clerk of Court shall allocate such space or staff as may be available and suitable only after all of the needs of regularly scheduled courtroom business are met.

6. **Pretrial Submissions:**
   a. **Documentary Evidence.** Any party intending to offer documentary evidence at trial, including, but not limited to medical bills, medical records, and lost income records, shall serve copies of such documentary evidence upon all parties not less than thirty (30) days before the scheduled trial, unless that period is modified by the order setting the case for a Fast Track jury trial.
   b. **Pretrial Conference.** No later than ten (10) days before trial, unless that period is modified by the order setting the case for a Fast Track jury trial, the Special Hearing Officer assigned to the case shall conduct a pretrial conference, at which time objections to any documentary evidence previously submitted shall be determined and witness lists shall be exchanged. If there are no objections at the time of the hearing, counsel shall so stipulate in writing. Documentary evidence that is not served at the pretrial hearing is not admissible absent the consent of all parties.

7. **Record:** A Fast Track jury trial will not be recorded by an Official Judicial Department court reporter. If either party desires to have a transcript of the proceeding, it shall be at that party's expense.

8. **Existing Offer and Demand:** The parties may stipulate in writing that the pre-trial offer and demand remain unaltered through the Fast Track jury trial. If the parties enter into this stipulation, either party may elect to accept the last settlement proposal of the opponent at any time before the verdict is announced by the jury.

9. **Jury Selection:** Fast Track juries shall consist of no more than six (6) jurors, selected from a venire called for a regular term of court. The jurors shall serve only during regular court hours during the term of court for which the Fast Track jury trial is called. The Court shall allow each side two (2) peremptory challenges. Jurors may be selected for a Fast Track jury trial only to the extent that the presiding Circuit Court Judge finds that such selection will not impede jury trials for either the Court of Common Pleas or Court of General Sessions. The Circuit Court Judge may select the jury or direct that the Special Hearing Officer select the jury.

10. **Time Limits:** The parties are encouraged to expedite the trial process by limiting the number of live witnesses. Generally, a Fast Track jury trial should not last longer than one (1) day.

11. **Rules of Evidence:** The parties may offer such evidence as is relevant and material to the dispute. The parties may, in the Consent Order Granting a Fast Track Jury Trial and Appointing a Special Hearing Officer, agree to modify the rules of evidence. The parties are encouraged to stipulate to modes and methods of presentation that will expedite the process, such as the following:
    a. The parties may agree to the admissibility of video or written depositions, affidavits, and if appropriate, ex parte depositions.
    b. The parties can agree to the admissibility, without the usual requirements of authentication and other technical requirements, of medical records, including but not limited to hospital records, ambulance records, medical records and/or reports from plaintiff's health care providers, diagnostic test results including but not limited to X-rays, MRI, CT scan, and EMT reports, or any other graphic, numerical, symbolic, or pictorial representation of medical or diagnostic procedures or tests.
    c. Past lost income may be proven by the submission of documentary evidence from the plaintiff's employer, including, but not limited to, pay stubs, tax returns, W-2 and/or 1099 forms, or lost wage statements. Any claim for future lost earnings premised upon lost opportunity, promotion, career advancement, or similar theory shall only be proven by expert testimony or the report of any expert previously exchanged pursuant to these rules.
    d. In the event a party intends to call a live expert witness, medical, or otherwise, that party shall provide written notice to all parties of such witness and provide an opportunity for the expert to be deposed.
    e. Pretrial evidentiary issues such as motions in limine and redaction of documentary evidence shall be determined in conformance with the applicable rules of evidence or the agreement of the parties by the Special Hearing Officer at the pretrial conference.
    f. The parties shall have the right to issue subpoenas to secure the attendance of witnesses or the production of documents as may be requested by any party.

12. **Case Presentation:**
    a. The Special Hearing Officer shall identify himself or herself to the Fast

Track jury as a Special Hearing Officer appointed by the court for the purpose of presiding over the Fast Track jury trial.

b. Upon agreement, counsel may present summaries, and may use photographs, diagrams, PowerPoint presentations, overhead projectors, individual notebooks of exhibits for submission to the jurors, or any other innovative method of presentation. Anything that is to be submitted to the jury as part of the presentation of the case must be exchanged ten (10) days in advance of trial, unless the parties consent. Counsel are encouraged to stipulate to factual and evidentiary matters to the greatest extent possible.

c. The parties are encouraged not to call more than three (3) witnesses for each side. On application of a party and good cause shown, the Special Hearing Officer may allow an increase in the number of witnesses. Unless otherwise stipulated, the parties shall follow a classic order of presentation.

d. The parties may agree to substitute procedures regarding the presentation of evidence upon approval of the Special Hearing Officer.

13. **Jury Verdict:** The verdict is binding, subject to any written high/low stipulation agreed upon by the parties.

14. **Post-Trial Motions:** The parties may agree to waive any motions for directed verdict, motions to set aside the verdict, motion for additur or remittitur, or any judgment rendered by said jury. If the parties so agree, the Special Hearing Officer shall not set aside any verdict or any judgment entered thereon, nor shall he or she direct that judgment be entered in favor of a party entitled to judgment as a matter of law, nor shall he or she order a new trial as to any issues where the verdict is alleged to be contrary to the weight of the evidence.

15. **Inconsistent Verdicts:** In the case of inconsistent verdicts, the Special Hearing Officer shall recharge the jury as appropriate and have it return to deliberation to resolve any inconsistency.

16. **Incapacitated Person or Minor:** In a Fast Track jury trial involving an incapacitated person or minor, the Circuit Court Judge who assigns the case to the Fast Track jury trial process must approve any high/low parameters prior to trial in the same manner the Court would approve a settlement involving such persons.

17. **Qualification of the Special Hearing Officer:** The Special Hearing Officer will be selected by the mutual consent of the parties. In all cases, the Special Hearing Officer must be a member in good standing of the South Carolina Bar and must have completed the trial experience required by Rule 403, SCACR. The parties shall determine the compensation, if any, of the attorney appointed to serve as a Special Hearing Officer. A Circuit Court Judge may also conduct a Fast Track jury trial, depending on the available resources of the Court. Nothing herein shall be construed to give a right to demand a trial by a Circuit Court Judge in a Fast Track jury trial.

18. **Mandatory Charge of the Fast Track Jurors:** The Circuit Court Judge who qualifies jurors selected for participation in a Fast Track jury trial shall charge the jurors about the nature of the Fast Track jury trial and concerning the identity and authority of the Special Hearing Officer. Fast Track jurors shall otherwise be qualified and sworn in the same manner as jurors selected for trial in the regular term of court.

FORM FOR THE FAST TRACK JURY TRIAL PROCESS

Consent Order Granting a Fast Track Jury Trial and Appointing a Special Hearing Officer

STATE OF SOUTH CAROLINA	)	IN THE COURT OF COMMON PLEAS
	)	_____JUDICIAL CIRCUIT
COUNTY OF _____	)	
	)	**CONSENT ORDER:**
_____	)	**FAST TRACK JURY TRIAL AND**
Plaintiff,	)	**APPOINTMENT OF**
vs.	)	**SPECIAL HEARING OFFICER**
	)	
_____	)	
Defendant.	)	Docket No. _____

The parties consent to the following:

1. Refer the above-captioned case to the Fast Track jury trial process.
2. Abide by the "Rules and Procedures for the Fast Track Jury Trial Process," outlined in the Chief Justice's Administrative Order, Case. No. 2013-000389 (March 7, 2013), subject to any additional written stipulations attached to this Order.
3. Select _____ to serve as the Special Hearing Officer in this Fast Track jury trial proceeding. He/She is a member in good standing of the South Carolina Bar and has completed the trial requirements of Rule 403, SCACR governing the practice of law.
4. Other:

_____

_____

_____

Attach a copy of any additional stipulations.

IT IS THEREFORE ORDERED:

1. _____ County Clerk of Court shall make available a courtroom facility and not more than ten (10) jurors from the jury venire for that week so that the parties may select a jury of six (6) to hear the above-captioned case.
2. The "Rules and Procedures for the Fast Track Jury Trial Process," outlined in the Chief Justice's Administrative Order, Case. No. 2013-000389 (March 7, 2013), shall be used at the Fast Track jury trial, subject to any additional written stipulations attached to this Order.
3. The parties are entitled to use the subpoena power authorized by the South Carolina Rules of Civil Procedure to compel attendance of witnesses, if necessary, at the Fast Track jury trial.
4. _____ is to serve as a Special Hearing Officer for the purpose of the binding Fast Track jury trial, and he/she shall have the authority to rule on all matters with regard to procedures and evidence as if he/she were sitting as a Circuit Court Judge, subject to any written stipulations attached to this Order.
5. The Special Hearing Officer does not have direct contempt power. If the Special Hearing Officer reports to the Circuit Court Chief Administrative Judge a finding of contemptuous conduct, then the parties are subject to the contempt power of a Circuit Court Judge and may have to attend a contempt hearing.

Date: _____, 20____

_____, S.C.

_____

Circuit Court Chief Administrative Judge

WE CONSENT:

_____ _____

_____ _____

_____ _____

_____ _____

SCCA 239 (06/2013)

APPENDIX II

OPENING CHARGE TO THE JURY

Good Morning Ladies and Gentlemen of the Jury. My name is _____. I will be serving as the judge during the trial of this fast track jury trial I am conducting this trial pursuant to the fast track jury trial rules set forth by the South Carolina Supreme Court.

Let me first tell you a little bit about what to expect. I am sure that each of you has seen parts of trials on television and in movies, and that may have given you some indication of the trial process, but let me give you some more concrete information about what to expect to happen in the trial of a case here in _____ County.

Once I have finished giving you this explanation of the trial process, the lawyers will make an opening statement to you. The opening statement is each lawyer's opportunity to tell what that lawyer thinks the issues are in the case and what the lawyer expects that the evidence will show about those issues.

After the opening statements, you will hear the testimony and evidence in the case. This will consist of testimony from witnesses, as well as any physical exhibits, including documents, that are introduced into evidence.

Once all of the evidence has been submitted, the attorneys will have the opportunity to make a closing statement. At that point in the trial, all of the evidence will be in, and thus the lawyers have the opportunity to tell you what they think the evidence has shown about the issues in the case. At each stage of the case, someone has to go first, and because the Plaintiff has the burden of proof, something I will explain to you further later on, the Plaintiff goes first at each stage of the case.

After the closing statements by the lawyers, I will tell you the substantive law that applies to this case, and shortly after that, you will meet as a group and discuss reaching your verdict.

At the time you were selected as jurors on this case, the judge selecting you for this jury may have used the term "fast track jury trial." You may have also noticed that there are 6 of you rather than 12 jurors. The South Carolina Judicial System has recognized that parties to civil disputes in South Carolina need to have alternative ways available to them to resolve their disputes. Some of the alternative mechanisms available to parties include processes called mediation and arbitration. The parties to this dispute have chosen the particular mechanism or manner for resolving this dispute known as a "fast track jury trial."

I cannot tell you what was in the minds of these parties and their lawyers when then they chose this particular mechanism or manner, but I can tell you that in general, fast track jury trials can be more efficient, flexible, and convenient for everyone concerned, including the jury. While there are some procedural differences between fast track jury trials and other trials, such as there being 6 jurors rather than 12, these procedural differences of course will not change the basic process or purpose of a trial. The fact that these parties have chosen a fast track jury trial as their manner or mechanism for resolving this dispute, as opposed to the other mechanisms available to them, makes this case no more important nor less important than had they chosen any other particular mechanism.

I want you to know that I personally am not an employee of the State or of _____ County. Most of the time I serve as a lawyer, just like the lawyers in this case. However, when the parties to this dispute chose to have it resolved by way of a fast track jury trial, they agreed to have me serve as the judge for this particular case, and a regular Circuit Court Judge signed an order appointing me to act in that capacity. That order gave me the authority and responsibility to act as the judge for this one case. In order to bring home to you the importance of the job that all of us have to do in this case, I am going to wear the same robe that a regular sitting circuit judge would wear, for this one particular case. [at this point put on the robe]

Under the constitution and laws of the state of South Carolina, you and I have separate and distinct duties. You alone are the sole judges of the facts of the case. The same constitution and laws that designate you as the sole finders of the facts also make me the sole judge of the law, the sole instructor of the law in this case.

I like to tell juries <u>before</u> the trial about the part of your job that is evaluating the credibility, which means believability, of the witnesses who take the stand, so that you will know to pay close attention throughout the trial. In passing upon the credibility or believability of the witnesses, you have the right to consider the interest in the outcome that a witness might have, the bias of any witness, the prejudice of any witness, and the demeanor, or manner, of any witness. You, as the judges of the facts in the case, will have to decide the force and effect and the truth of the testimony of witnesses. In making a determination about the credibility or believability of a witness, there are many factors that you may and should take into consideration, such as, as I mentioned, the demeanor or manner of the witness. You can observe whether a witness is forthright or hesitant, whether the witness' testimony was consistent, or instead contained discrepancies or

contradictions. You can consider the ability of the witness to know about the facts concerning which the witness gave testimony. Was the testimony of the witness supported and made stronger by other testimony and evidence, or was it made weaker and impeached by other testimony and evidence? Since, at the end of the trial, part of your job will be to decide how much weight to put on the different testimony of the different witnesses, please listen carefully to the testimony and be prepared, at the end of the trial, to evaluate the testimony. However, please do not start deciding the case until the very end of the case - until you have heard all of the evidence from both sides and all of the law as I give it to you. Only after you have heard all of the evidence and the law that applies to this case will you be in position to make a decision fairly about the whole case.

Although there are some different views about having jurors take notes, because I expect this case to be relatively brief, I ask that you not take notes during the case. Jurors' notes can sometimes create more problems than benefits. I am confident that the 6 of you can pay close enough attention throughout this trial that once you begin your deliberations you will be able to recall the testimony.

One particular rule that I would like for you to know about is the rule that provides for the taking of something called a deposition. A deposition is the taking of the testimony of a witness at some place and time other than during the trial itself. The rules that apply to civil cases have several situations in which depositions may properly be taken and then used during the trial. Sometimes depositions are taken and the testimony preserved by way of a word-for-word transcript of the questions and answers. Sometimes depositions are videotaped and then shown to you. In all depositions, the witness takes the same affirmation or oath that a witness takes during a trial. Thus, you should consider the testimony from any deposition just as if the witness were here testifying. You should determine the credibility or believability of the deposition testimony just like testimony given during the trial.

Please know also that there two categories of witnesses. The first category of witnesses is known as lay witnesses. Any person who is able to make observations through any of the person's five senses and then later relate or communicate about what the person observed is qualified to be a lay witness. There is a second category of witnesses, known as expert witnesses. Expert witnesses are persons who, by their training, education, or experience are allowed by the court to testify as experts in a particular field. The significance of the court finding that a witness is qualified to be an expert is that expert

witnesses are given much more latitude to give opinions. The opinions of experts, however, only constitute evidence to be considered by you, in connection with all of the other testimony and evidence in the case. You must weigh such evidence and accept or reject it in the same manner that you treat all of the other evidence in the case. In determining the weight to be given to an expert's opinion, you should consider the qualifications and credibility of the expert and the reasons given for the expert's opinion. The testimony of experts is to aid and assist you as jurors, not to dominate or control you in the decision of questions of facts. The opinions and deductions of experts do not preclude your own. You are required to decide disputed questions after comparison and consideration of all the evidence in the case.

During the testimony of expert witnesses, and in this case I anticipate that the expert testimony will come from medical experts, you will often hear the lawyers ask questions along the lines of, "Doctor, in your opinion, to a reasonable degree of medical certainty, is it your opinion that a certain event or condition most probably caused a certain result or condition?" The language of that question may come across as cumbersome and possibly even confusing. Please don't fault the lawyers. If the lawyers ask the question in that language they are trying to comply with the applicable legal standard, which is that for the expert's opinion to constitute evidence that an event caused a certain result, the expert must state that, with reasonable certainty, the result most probably was caused by the particular event. I will explain the burden of proof more fully at the end of the case, but know at this stage that ultimately a Plaintiff must prove causation to a standard of more likely than not, and that is the reason the lawyers use this somewhat cumbersome language.

Recall that I told you that the lawyers will make opening statements at the beginning of the trial, and closing statements toward the end of the trial. What they say to you does not constitute evidence. The evidence will come from the witnesses and the exhibits that are admitted into evidence. The attorneys are simply stating their viewpoints. Those viewpoints, while worthy of your consideration, are not evidence. In that regard, please know that it is proper for a lawyer to suggest to you what the lawyer thinks a fair verdict would be, but of course you are not required to follow that suggestion. You are instead required to reach your own conclusions about what the verdict should be.

During the trial, the lawyers may make objections. That is part of the lawyer's job. Should they make objections, please do not hold that against them. They are bringing a

legal matter to my attention and asking me to make a decision. Please do not give any consideration to anything the lawyers say when they make objections. If I sustain an objection, you must not speculate about what the answer might have been or about the reason for the objection.

Finally, let me tell you a little bit about what this particular case is about. This case arises from an automobile accident or collision that occurred on [DATE], at [LOCATION]. In the Complaint, the paper that the Plaintiff filed with the court to start this lawsuit, the Plaintiff stated or alleged that [_____]. In the Defendant's Answer to the Complaint, the Defendant alleged [_____].

In a case such as this, there are normally 3 issues. These are

1. Negligence,
2. Proximate Cause, and
3. Damages.

I will define those issues or terms more fully at the end of the trial. At this point, simply know that it will be the Plaintiff's burden to persuade you that more likely than not, the Defendant was negligent, and that the Defendant's negligence proximately caused the Plaintiff to suffer damages. Thus, as I said, the three issues are (1) Negligence, (2) Proximate Cause, and (3) Damages.

** OPTIONAL ADDITIONAL PARAGRAPH

Although in a case such as this, there are normally three issues, negligence, proximate cause, and damages, in this particular case, the Defendant has admitted simple negligence. The Defendant has thus admitted doing something the Defendant should not have done, or failing to do something the Defendant should have done, and thereby causing the accident or collision. However, the Defendant has not admitted the other two issues, proximate cause and damages. Thus, in this case, rather than having all 3 issues to decide, you will have only two issues to decide, proximate cause and damages. While these are two separate issues, they can be put together in the same sentence, which is that what you must decide with your verdict is whether this accident or collision <u>proximately caused</u> [PAUSE] <u>damages</u> to the Plaintiff, and if so, how much.

SMALL FIRM PRACTICE IN THE 21st CENTURY
Challenges, Advantages, Opportunities

A Collaborative Effort by and among FDCC Members presented at
FDCC Winter Meeting, San Diego, March 1, 2016

Moderator:	Christian J. Steinmetz III	Introduction, Overviews, and Ethical Issues
Panelist:	Alison R. Christian	Small Firm Technology Issues
Panelist:	Kile T. Turner	Small Firm Marketing Issues
Panelist:	David J. MacMain	Small Firm Management Issues

INTRODUCTION

It is interesting to look at the changes that have occurred in the modern law practice given the advent of new and improved technologies, the strategies employed by lawyers in marketing, and the unavoidable fact that fewer and fewer cases are being tried to juries. The exponential explosion of the number of lawyers in the wake of *L.A. Law* and other television shows of the 80s and 90s mandates that we each stay at the top of our game(s), because there are 2-3 lawyers waiting in the wings to replace us. Never has competition among us been greater. On top of keeping up with the changes in substantive law, it is vital that each of us embrace the changes and adopt the trends in the practice of law brought about by innovations in technology, marketing, and management. This must be balanced with an ever-more cloudy and muddled world of ethical considerations which sometimes accompany, but more often follow, these changes in the practice of law.

There are just over 1.3 Million licensed lawyers in the United States. Would it shock you to learn that most lawyers practice solo or in small firms of 10 lawyers or less? Probably not, because the prevalence of the number of solo practitioners will always abound in a profession known for its members' desire to control their destinies. Still, the latest statistics from the American Bar Association (ABA) demonstrate that 49% of us practice solo and 20% practice in firms of 10 or less lawyers.[1] Looking at it from another angle might bring about the proverbial *shock and awe*, because among those of us who practice in firms of any size, 89% of us practice in firms of 10 or less lawyers. This lies in comparison to on 5% in firms of 21 or more lawyers.[2] Taking a moment to step back and look around in our profession will open one's eyes and enable one to understand the role that the small firms play in our profession.

OVERVIEW OF THE IMPACT AND ROLE OF SMALL FIRMS

Small firm practitioners typically develop and implement the cutting edge strategies which

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1 ABA Lawyer Demographics Table – 2015
http://www.americanbar.org/content/dam/aba/administrative/market_research/lawyer-demographics-tables-2015.pdf

2 Id.

many within the rest of the profession later adopt and follow. As we discuss below and as we will examine during our presentation, the wonderful opportunities a practitioner enjoys within smaller firms are accompanied by challenges unique to smaller firms, challenges which require self-awareness, creativity, and a willingness to think outside of the proverbial box.

Many lawyers begin their careers with mid-size and larger firms only to leave them to form smaller "*boutique*" firms which may specialize in one or a few areas of practice. Many small firms' genesis lies within a common search for change in the method of practice among its founders. Liberation from non-billable management responsibilities, the freedom to practice in multiple practice areas, more control over one's hours and one's presence in the office are among the leading changes sought by those who leave larger firms to form small firms.

Conversely, the solo practitioners who join often seek the strength in numbers, lateral assistance, and the security of being able to practice with other specialists and like-disciplined lawyers. Sharing responsibilities for management, technology, and marketing are often significant drivers for the solo practitioner who decides to band with others.

The common theme among them all is a desire for a change from the present to a new environment in which the lawyer can practice his or her trade and service clients' needs more effectively without compromising the ultimate reward – making a living. However, the revolution does not cease once new business cards and stationery are printed – it is only beginning.

In smaller firms, the "leaner and meaner" culture leaves much less room for any vestiges of a reluctance about welcoming change, because a small firm lawyer's success (and survival) frequently depends on the ability to sculpt his or her practice to the lawyers' clients' variety of needs. It is not just enough that smaller firms' typically lower overhead results in lower hourly rates or fee structures. We have seen the resulting effect of rate-cutting wars - the quality of representation eventually suffers. Ethical corners are cut by lawyers having to take on too much work to fulfill quotas, goals, and requirements or untrained or inexperienced baby-lawyers are given too much responsibility, because only their hourly rates can accommodate the slashed fee structure.

The 21st Century client is much more aware, savvy, and attuned to needs for access, value, and successful representation. Few corporate or institutional clients are without someone within who is a veteran of over-billing or the effects of rate-cutting. The 21st Century client understands that it will have to pay for good legal representation, but it also recognizes that the traditional attorney-client relationship model has changed. Instant access (and responses) through email or texting, accountability for all billing entries, and the ability to control the litigation landscape are *de rigueur*. Certainly, the characteristics of the needs of *Coca-Cola* or

Apple will differ from Lulu & Coco's Custom Interiors, LLC, but the motifs of access, value, and success pervade both.

A small firms' flexibility to meet clients' needs is maintained through often unique and ever-revised approaches to technology, marketing, and internal management. In a smaller firm, implementing new methods, policies, and introducing new technology is much easier among 6 lawyers than among 15, 50, or 500. Levelling the playing field among 9 lawyers is a much easier task for management than to do so among 19 or 59. Finally, more and more, the specialized experience among many small "*boutique*" firms' rosters enable those firms to market themselves as business-partners and collaborators with larger firms where the client can get the best of both worlds.

Still, what may seem like a brave, new world in our profession is not without a whole host of ethical concerns which are somewhat unique to smaller firms. Questions never reached by the solo practitioner whose practice could not withstand the burden of the business and questions never considered by the larger firm practitioner whose IT department or marketing vendor address these issues are those which small firm practitioners analyze, address, and ensure continued protection of clients' interests on a daily basis.

Small Firms & Technology: A Match Made in Cyber Space

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Small firms have several distinct advantages when it comes to staying current with technology. First, it's easier to turn a small ship. There are fewer decision-makers in a small firm and if changes need to be made, they can happen relatively quickly. Second, many of the technology products charge for access on a per-user basis. At a small firm, fewer users equals lower costs. Third, technology exists to improve efficiency. Small firms already stay competitive by offering lower rates than large firms. Adding a layer of even minimally-improved efficiency through technology will result in dramatically more competitive rates. As solo practitioner and technology columnist Jeff Binnion said, "Legal technology is about finding ways to work more efficiently so you can spend more time focusing in substantive things and less time doing mundane tasks." This portion of the article will explore various ways in which small firms can provide better client service, improve their bottom-line, and free up valuable attorney time through the use of technology.

1. Adventures in the Cloud: Document Management.

Our firm maintained paper files for years. We stored electronic documents on a physical server

that lived in a mysterious, and somewhat ominous, locked room. We spent a great deal of money on off-site storage for closed files, oftentimes long after expiration of the State Bar's retention policy. The result was unnecessary overhead. There were hard costs associated with these antiquated procedures (e.g. paper, ink, staples, etc.), but there were soft costs as well. We did not make efficient use of our leased space because we storing paper files and large servers, we relied upon more support staff than a small firm should, and we could not provide our clients with the instant responses they expect from their lawyers. Our lives changed when we ditched the paper, quit the servers, and said so long to storage!

Last year, we successfully made the switch to a cloud-based document management program that allows us to store an unlimited amount of documents (from over 200 file types), share and access content remotely and securely, and collaborate both internally and externally on documents. It only cost $1,000 to make the transition and the entire office was up and running (almost seamlessly) after a few, free training sessions. Our monthly costs are also very manageable, at $20/user. The process also allowed us to determine which files we needed to maintain as open, which could be closed, and which could be ethically destroyed. So it was a win-win-win. Here are some of the features I enjoy most:

- Our entire database is searchable from any of my devices, any time. Need to find that memo on reasonable expectations and can't remember the file name? Want to show an associate a sample request for a federal fee application? Sitting at a mediation and need a copy of a specific policy? Type the search terms into Box and a list of all relevant documents is instantly generated. You can then filter the results and get exactly what you need with the speed of a Google search.

- We can collaborate intra-office on the same document and maintain all prior versions. When I am ready for my assistant to format a letter or pleading, I can tag her with a Twitter-like handle within the system and she will instantly receive notification that the document is ready to access. I even have the option of locking a document to prevent others from making changes while I am working in it.

- We can send electronic links to large document files, even to non-system users. One of the features that our clients, opposing counsel, and associates have appreciated is that we can quickly send them secure links to documents without having to send multiple emails or risk a bounce-back because the files were too big. For example, when we get a subpoena response with hundreds of pages, we can bates-label the response, upload it, and circulate a link within a matter of minutes. If you are curious about what the recipient sees, email me and I can send you a sample link.

- We can rest easy knowing our documents are as secure as possible. One of the biggest concerns that we had when moving to the cloud was maintaining our ethical obligation of confidentiality to our clients. The system uses layered encryption both in transfer and at rest. Their data centers use "biometric entry authentication, closed-circuit video monitoring, and 24/7 armed guards" and "N+1 or greater redundancy for all network components and system components."

2. Improving Cash Flow: Electronic Billing Programs.

One of the most important steps in keeping the lights on at a small firm is maintaining steady cash flow. That means getting the bills out the door on time, getting our invoices paid promptly, and tracking realization so we can make improvements. Many, if not the majority, of our clients shifted to electronic billing systems over the last several years. Our firm needed to adapt in order to meet their changing needs. In addition to our "associate lunch incentive" program (which I'm happy to talk about if you have any questions) we now rely heavily on our electronic billing software to keep the trains moving on time.

There are several practice management products on the market, but the two that our small firm considered best for our purposes after extensive vetting each offered features that are invaluable to a small firm: the ability to enter and release time online with task codes for electronic billing; maintaining our client conflict database; and creating invoices and general ledgers. They also track, however, the financial "health" of the firm.

With the LMS software we elected to use, we have 24/7 access to a Business Intelligence dashboard. I can tell how many matters we have open, how many hours a particular associate has billed each month (and can also see non-billable time they have tracked, such as marketing and pro bono hours), how much a client has paid us to date on a file, the current amount outstanding on any matter, our billing rates for that file, and how our profitability compares to the same time last year. I can also generate reports that show me each associate's realization rate, the amount of time that has been written off internally, the amount of time that has been written off by clients, and their effective hourly rate. This type of information allows our firm to make corrections on a quarterly basis, improve our efficiency for clients, and maximize profitability by year-end.

3. Save Precious Time: Document Review.

At our year-end partners' meeting we talked about how much the practice of law has changed over the course of even the last five years. We receive electronic documents in higher volume than ever before, yet there is a growing expectation we will be able to review these documents

more quickly and efficiently than ever. We need to analyze, synthesize, and organize an incredible amount of information – without the teams of litigation paralegals and young associates that are available at large firms. The other day we received a flash drive containing 7 gigabytes worth of data for expert disclosures. That was not even the parties' disclosures; it was only the experts. How does a small firm begin to process that kind of information?

The answer for us is simple: we rely heavily on electronic document review tools. We learned through trial and error that every associate has different review methods and preferences, and it is a waste of time to force them to use the same tools. We have two associates who prefer to review and physically mark-up documents on their iPads; the other two prefer to use their laptops. For our Apple Team, the product we selected allows associates to remotely access thousands of pages of paper and to mark-up the documents as though they were printed in front of them (e.g. make handwritten notes, highlights, flag pages, etc.) Our PC Team, however, prefers a different product which allows them to review and edit PDFs, create bookmarks, and cull out important pages to save as stand-alone documents. This team usually maintains a working internal memo in a Word document and can easily jump back and forth between different formats on their laptops.

Once the first-round review is complete and the important documents have been identified, we turn to other platforms for synthesizing the information and focusing the case strategy. We learned through trial and error that the some products did not work well for ground-up review but were better for organizing the case after necessary documents had been identified. Also, once we streamline the documents, we can then create "key issues", "key facts", and a cast of characters that can be color-coded, annotated, and compiled into hyper-linked summaries. This feature is very helpful in creating deposition outlines or trial witness examinations, for example. A "key facts" feature also has a field to enter important dates. These dates can then be imported to our internal platform and within seconds can create a visual chronology of the case.

4. Ace(ing) Hardware

Technology evolves daily. Hardware depreciates daily. It is seems like a lose/lose proposition. That is why many firms approach technology like some people approach cholesterol – waiting until there is a problem to make changes. Small firms cannot afford to take those kinds of risks, however. <u>They have to be proactive about planning for regular technology upgrades to avoid detrimental business interruptions</u>. The other day we upgraded one aspect of our system, and my laptop was out of commission for an hour and a half over lunch. I felt like my arms had been cut off. I cannot imagine what I would do if my laptop crashed completely!

That is why we budget for hardware replacement every 3-5 years. We made a shift over the

last few years away from desktops. Now, we lease laptops for every lawyer, our office administrator, and both paralegals for less than it cost to purchase them. We also have the option to purchase them for $1 (no, that's not a typo) at the end of the lease. That way, when the hardware becomes outdated, we can easily upgrade without being left with a bunch of equipment that has nominal street value. We also issued firm iPad Airs to all of our attorneys through a contract with our internet provider. The contract included a "cost" for leasing the devices that was offset by a credit in the same amount toward our internet. Again, this was win-win.

These mobile devices are ideal for a small firm practice. Our lawyers need the ability to work remotely, both for associate happiness purposes and as a practical reality. If we are traveling for a mediation or a deposition, we need to deliver prompt client service. With our laptops and the software described above, we are equally efficient regardless of whether we are at the office. Our people also appreciate the ability to change their scenery throughout the day. After the wave of media attention on how "sitting is the new smoking" our office made stand-up workstations available to all of our employees. Because one of our firm cultures is "Be MacGyver: Do More With Less", we also found a way to convert the $25 Ikea coffee table into a dual-level stand-up desk. Laptops and iPads worked seamlessly with these new stations and take up much less space than traditional desktops.

5. Cyber Security: What You Don't Know Can Hurt You.

No discussion of firm technology would be complete without mentioning cyber security. Even small firms cannot afford to ignore the risks posed by cyber threats. There are several free antivirus software products available (although the "free" products are geared primary for personal use). Small firms can also look into the best commercial antivirus products for 2016 (PC Mag and others) that are available for purchase. Our firm has had success with a combination of different, but affordable software products. In addition to the security features built into our Windows platform, these products create an added layer of protection that helps me sleep better at night.

These products cannot defend your firm from attacks unless you are also mounting a good offense. If your employees, like ours, are using firm-issued mobile devices or personal devices to access company information you should have several policies in place. First, I recommend a BYOD policy that sets forth parameters for who can use what technologies and where. For example, can employees connect their cell phones to the firm's wireless internet? Can employees download a firm platform app to their phone and access firm documents remotely? If so, under what circumstances? If a device goes missing, how does the firm locate and potentially disable and/or wipe that device remotely? Implementation and explanation of these policies will help protect your company. There are several outside resources available to

analyze your firm's current security health if you want to know how you rank.

The next policy that every firm needs to have is a cyber liability insurance policy. This is particularly so for small firms who do not have as many resources available to respond in the event of a security breach. These types of policies are becoming increasingly common, and some clients are actually requiring them for law firms in addition to professional liability policies. Costs for notification, forensic investigation, and fines and penalties can sky rocket quickly, even if no lawsuit is filed. In addition to the protection against third-party liability and first-party losses, such policies often provide risk management services that give firms access to IT professionals and other experts who can help implement better protocols. Our firm learned a great deal through the application process about our weaknesses and little steps we could take to enhance our security. For example, we implemented double-authentication for our devices, increased the length of our passwords, and improved our BYOD policy.

Technology is an inescapable part of the legal professional and its prevalence will only continue to increase. These tips are some of the ways that our small firm has managed to stay current and competitive without breaking the bank.

ETHICAL CONSIDERATIONS RELATED TO TECHNOLOGY MANAGEMENT IN A SMALL FIRM:

- Confidentiality: *"A lawyer shall maintain in confidence all information gained in the professional relationship with a client, including information which the client has requested to be held inviolate or the disclosure of which would be embarrassing or would likely be detrimental to the client, unless the client gives informed consent, except for disclosures that are impliedly authorized in order to carry out the representation, or are required by these Rules or other law, or by order of the Court."*[3]

- Among the paramount obligations lawyers are required to uphold every day is the confidentiality of client communications and client materials. This is not limited to merely conversations or even correspondence, but it addresses client data such as within those and within the client's documents. Accordingly, confidentiality concerns require small firms to analyze and reconcile competing factors such as:

  - *Cost-effectiveness* of storage of client data, be it on site, off site, virtual or physical. The obligation of protection does not change, but the cost, in most circumstances, is the obligation of the law firm and cannot be directly assessed

3 Rule 1.6 of the Georgia Rules on Professional Conduct (based on the ABA Model Rules adopted by Georgia on June 12, 2000 and which have been adopted in all 50 states and the District of Columbia) While these specific cites relate to the Georgia Rules, comparable and nearly identical rules are available at each State's Bar's website.

to the client. *How do we provide a cost-effective and easy-access platform so that our members and employees can fulfill this obligation?*

- The use of varying email programs among firm employees and members and the protections afforded data and communications thereby. *How do I know that this is secure and very difficult to hack or intercept?*

- Fees: *"A lawyer shall not make an agreement for, charge, or collect an unreasonable fee or an unreasonable amount for expenses. The factors to be considered in determining the reasonableness of a fee include the following:*

  - *the time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly;*
  - *the likelihood that the acceptance of the particular employment will preclude other employment by the lawyer;*
  - *the fee customarily charged in the locality for similar legal services;*
  - *the amount involved and the results obtained;*
  - *the time limitations imposed by the client or by the circumstances;*
  - *the nature and length of the professional relationship with the client;*
  - *the experience, reputation, and ability of the lawyer or lawyers performing the services; and*
  - *whether the fee is fixed or contingent.*

  - *The scope of the representation and the basis or rate of the fee and expenses for which the client will be responsible shall be communicated to the client, preferably in writing, before or within a reasonable time after commencing the representation, except when the lawyer will charge a regularly represented client on the same basis or rate. Any changes in the basis or rate of the fee or expenses shall also be communicated to the client."*[4]

- Were it only so simple and as easy as the foregoing seems to make it when it comes to the question of what constitutes upholding one's obligation to a client as to fees! While 50 years ago, it was common within our practice to work on a matter to its completion and then send the client a bill, those days have been replaced by billing platforms, TPAs, client-specific billing and expense management programs, and a need within the firm to have instant access to financial data. Questions which smaller firm practitioners must address are such as: *1. Will the totality of this* [prospective] *client's book of business*

4 Id., Rule 1.5 (a)(b)

financially justify the purchase of a particular billing platform? 2. How do I most cost-effectively analyze the cost of the value I am providing to my clients?

The simple fact remains – compliance with ethical obligations in an ever-changing technological landscape brings about a host of considerations which impact a small firm's overhead. The obligation is no different, but the impact of fulfilling such obligation presents a challenge where several factors compete within the overall analysis.

Marketing the Small Firm Advantage

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There is a prevalent idea in the legal world today that bigger is better-the bigger the firm, the better the firm. All one has to do is look at a list of "prestigious" firms to see that the more lawyers a firm has, the more likely it is to be considered "elite". Perhaps that is what is behind the current merger trend where we are seeing firms rushing to add size at an unprecedented rate. Ironically, law firm failures (Dewey & Leboeuf and Heller Erhmann are just two examples), are happening at an unprecedented rate as well. As more firms merge and become bigger, a door of opportunity is opening for a new player on the block- the small firm.

Small firms are now being called "boutique", which may better emphasize the fact that just because a firm is small, it can still provide excellent representation to its clients. In fact, in many instances, a boutique firm can offer *better* services and at a significantly lower price. Although we practice in the age of law firm mergers, now more than ever, the unique characteristics of the small firm are more in demand than ever before.

Better, faster, cheaper: those three words describe the new focus on legal spend. Not only are clients seeking (or more accurately, demanding) the best legal representation, but now the expectation is that the high quality legal representation should be provided more quickly and at a lower cost. While this may seem like a tall order if not a complete pipe dream, the reality is that better, faster, and cheaper legal representation is available—by hiring a smaller firm.

In a world where the battle worn trial lawyer with years of experience—and the battle scars to prove it—is a vanishing breed, hiring the most expensive lawyer may not get you the most *experienced* lawyer. This ironic trend in our profession may defy economic logic because usually the more rare the skill, the greater the price. However, because the value of the case is directly related to what the expected jury verdict will be — there will always be a need for experienced and skilled trial lawyers. And most of these trial lawyers can be found in smaller law firms.

One of the biggest advantages smaller firms have is that their lawyers usually have more trial experience. As jury trials become less frequent, corporate clients are going to have to look further to find lawyers to try their cases. Therefore, we can expect that the lawyers will the most trial experience will be the defense bar leaders in the future - and a majority of those lawyers will be from small firms.

One of the reasons large firms are considered "prestigious" is their strict hiring criteria and how they hire only the top students from the top law schools. Indeed, it is true that graduates from prestigious law schools are more likely to end up at larger firms—which pay larger salaries to attract and keep the "top talent." However, it is interesting to note that not a single *US News & World Report* ranked top 10 law school made the list of Top 10 Schools for Advocacy. Thus, while large firms are focused on hiring those with the best law school grades, it is not clear that they are hiring the top litigation talent. Avoiding time consuming tasks in law school such as mock trial and moot court competitions may have helped the students do better with their grades, but also made them less prepared for becoming a *real* litigator and defending their clients' interests in a *real* courtroom. As one commentator noted based on his research, "[A]*ttorney* [skills] *accrue from the development of practice skills, rather than from the more typical theoretical learning provided by most law schools…*" The author goes on to note that research "*calls into question law school grades and honors as measures of competence…*"[5]

Smaller firms frequently have business models closer to that the businesses they represent, because they take specifics steps to model their operation to that of principal or cornerstone clients. More and more, 21st Century clients tend to hire more on ability than pedigree.[6] The truth is that it is the clients that pay the law firm salaries, and there is no indication that success in law school will make one an effective and successful litigator in the courtroom.

The disconnect between the high associate billing rates and the lack of experience has been recognized by Corporate America. For example, Brian Brooks, general counsel for Fannie Mae was recently quoted as saying that the high cost of junior lawyers exemplifies the "broken" law firm profit structure.[7] The article goes on to explain that major law firms make money by leveraging lots of associate hours for each rainmaking partner. However, companies are becoming more astute in their allocation of legal spend by no longer agreeing to this practice. While the willingness to pay high rates for senior lawyers remains, the plethora of fees generated by file-churning among less experienced mid and lower level attorneys no longer

5 Lawrence Kreiger, The Geo. Wash. L. Rev. Vol. 83:554, 591; 2015.

6 Consider that when included on surveys, the Princeton law school is a perennial top 10 law school despite having closed its doors for good in 1852 after graduating a total of 11 lawyers. (Yale Daily News, March 23, 2011).

7 Martha Neil, *GC's fix for 'broken' law firm profit structure: Cut associate billing rates*; Bloomberg BNA, Aug. 11, 2015.

justifies the rates being charged at more bulky firms.

A coming trend is that more and more, one sees smaller firms receiving referrals from large firms in conflict situations or being associated by larger firms in situations where specialized or local representation is needed. The large firm does not have to worry about a competitor stealing the client, but can still be confident that the client is getting excellent representation. Because of this evolving dynamic, smaller firms tend to have a more collaborative relationship with larger firms, especially amongst firms that represent businesses and corporations. This type of relationship underscores the fact that small firms can provide top drawer services to clients in the areas where the particular firm excels.

One of the best advantages of a smaller firm is that its lawyers are not weighed down by all of the obligations necessary to run a large law office. A senior partner at a large firm may serve on various committees that decide the operation and management soaking up non-billable time that is recouped through higher rates and work by less experienced lawyers. The smaller the firm, the less likely a significant staffing hierarch needs to be established for a particular matter, and numerous partners to not have to be consulted in order to make important decisions on the case. Further, conflicts of interest are not only less likely to exist, but they can be accurately determined much more quickly as well. Large firms often employ one or more people to manage the firm's potential conflicts, which adds to the cost of overhead which is ultimately borne by the client in the form of higher fees. In fact, according to legal consulting firm Altman Weil, "*There are no economies of scale in law practice in the sense that larger firms always have higher per lawyer overhead, on average, than smaller firms.*"[8]

Finally, as discussed elsewhere in this paper, technology has done a lot to level the playing field like never before between firms of disparate size. In the past, only a big law firm could afford both the books and the extra space of an extensive library managed by a college educated librarian. With the advent of the internet, a 10 person firm has the same research capabilities as a 100 person firm. The only difference is that the billable rate of the person doing the research is much lower at the small firm.

In conclusion, small law firms have many competitive advantages over their larger counterparts. At a time where talented and experienced courtroom lawyers are at a premium, they are most likely to be found at a firm with fewer lawyers. Not only do these lawyers typically have more experience, they also work for lower rates due to lower overhead and great efficiency. Larger firms with higher hourly rates do not always correlate to superior courtroom skill. Firms of all sizes are beginning to work together to the benefit of clients. Finally,

8 Ward Bower, "*Why the Future Looks Good for Smaller Law Firms*" Altman Weil, Survey of Law Firm Economics.

technology now allows small firms to access the same information. Therefore, "better, faster, cheaper" is more readily obtainable- if you hire a small firm.

ETHICAL CONSIDERATIONS RELATIVE TO SMALL FIRM MARKETING:

- Competence: *"A lawyer shall provide competent representation to a client. Competent representation as used in this Rule means that a lawyer shall not handle a matter which the lawyer knows or should know to be beyond the lawyer's level of competence without associating another lawyer who the original lawyer reasonably believes to be competent to handle the matter in question. Competence requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation."*[9]

- Of course, the initial diamond-head ethical consideration that must touch and concern the small firm's marketing profile is "*Can this firm/lawyer handle this type or size of representation?*" Having successfully (and singularly for my clients) defended a Statewide Class-action litigation matter in a firm of 3 lawyers with no associates, the analysis of the impact of a taking on a client's book of business or even a single case (like above) must be addressed not only by the individual practitioner, but among the members of the firm as a whole. In smaller firms, firm-wide support for new endeavors, new clients, and new cases is a must so as to avoid questions as to the ability to perform not only with the requisite legal acumen, but also with the necessary resources to protect the client's interests. This is one version of knowing "*when to say when.*"

- Conflict Of Interest: General Rule: *"A lawyer shall not represent or continue to represent a client if there is a significant risk that the lawyer's own interests or the lawyer's duties to another client, a former client, or a third person will materially and adversely affect the representation of the client…"*

- Another crucial factor which must bear in the firm's marketing profile is the impact of the target representation sought by the marketing. At (almost) all costs, absent overt client consent, conflicts among representation must be avoided. These include the obvious conflict of not accepting new clients who are or are expected to be litigating or adverse to existing firm clients. However, these conflict also include the more subtle conflicts as to areas of practice among various lawyers. For example, if a small firm markets itself as the best of trial lawyers in the region and such results in one of the

9 Rule 1.1 of the Georgia Rules on Professional Conduct; (based on the ABA Model Rules adopted by Georgia on June 12, 2000 and which have been adopted in all 50 states and the District of Columbia) While these specific cites relate to the Georgia Rules, comparable and nearly identical rules are available at each State's Bar's website.

senior partners getting an opportunity to become Plaintiffs' class counsel, the question is presented as what impact will accepting this representation, regardless of whether any specific conflict exists, have on the practices of other lawyers in the firm? In a traditionally defense-oriented firm, longtime institutional clients can perceive this as a shift in firm philosophy and become less secure with their relationship with other lawyers in the firm.

Marketing takes on a variety of different profiles which vary from firm-to-firm and within the firm, lawyer-to-lawyer. Many small firms do not advertise or have firm-wide marketing platforms. Many small-firm practitioners relay on existing clients and other lawyers for referrals and to generate other business. In the advent of TV lawyers and law firm's social media marketing campaigns, small firms must take steps to remain keenly aware of changes in the landscape among legal representation so that they can make solid and unassailable decisions related to marketing themselves, be it among the general public or among other members of their professions. Ultimately, the key to avoiding ethical issues in small firm marketing is open and frequent communication among the firm's lawyers as to existing clients and prospective clients.

Small Firm Management

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Managing a small law firm has unique challenges – but also wonderful opportunities. Small firms are leaner and meaner, and often better able meet client's needs, adopt to changes and offer cost-effective legal counsel. Conversely, managing a small firm requires greater creativity, and a realistic recognition of what the small firm capabilities are – and what they are not. Staff stability, quality of life, effective use of technology and non-economic rewards are particularly important issues that small firm management must be cognizant of and able to meet. Successful small firm managers need to be able to wear multiple hats (e.g. rain-maker, practitioner, manager, and cheerleader) and be particularly smart about delegation and using other lawyer and staff talents.

Having been (1) a partner and practice group leader at a large City law firm of 175+ lawyers with 3 satellite offices for 19 years, (2) a partner and practice group leader at suburban firm of 30+ lawyers for 4 years, and (3) a founding member and managing partner of an 8 attorney firm for the past 3 years, I have seen management from various angles and perspectives. I have seen the good, the bad, and sometimes the 'ugly.' I have seen the pros and cons of each size firm; what each type of firm is well-equipped to do; and what each size firm is challenged to do. What follows is a series of bullet point issues, things to consider, and 'food for thought' from a

small firm management perspective. These are no particular order. There is no 'right' answer(s) - it is **your** firm, but it is important that you think and talk about these issues, and 're-talk' and 're-think' about them each year as things, people, perspectives and goals change.

- Partnership structure
  - Inclusive and books are open vs. closely managed and information is limited?
  - Equal equity or one-partner dominated?
  - Age of partners?
  - Is there a mentor partner(s)?
  - Young growing partner(s)?
  - Is there a need to consider succession? If so, when – 5 years, 15 years?
  - Is the firm expected/desired to grow, shrink, or stay the same size?
  - How is change in ownership interest handled?

- Management (internal) of Firm
  - Dictator? Consensus? Democracy?
  - Partners / Management must "model" desired behavior and work-ethic
  - Understanding and flexible . . . but "NO" is necessary
  - Consistent application of rules

- Management (external) of Firm
  - Common theme / message to outside world, clients and vendors
  - One voice and consistent approach
  - What do you want the firm to be "known for?"
    - One prominent lawyer(s)
    - Type of law or practice area
    - Client perception
    - Bar perception
    - Court perception

- Business model
  - What is target business(es)?
  - Do you prefer/expect the firm to be a general practice?
  - Is there a common theme to the 'type' of business you do currently?
  - Is there a desire to transition to a different or additional 'type' of business?
  - Are there clients you want to 'fire' or types of business you want to avoid?

- Rate structure?
  - Does it vary with practice area?
  - Does it vary with client?

- Does differing rate structures offer positives? Negatives?

- What is the 'firm culture?
  - Profit driven?
  - Quality of life?
  - Growing, or happy to stay the same size?

- What is the 1 year plan? 5 year plan? 10 year plan?
  - Do the members share the same vision?
  - Are the member in the same 'life/career stage'?
  - Does it vary by member?

- What is 'rewarded' through financial compensation?
  - Origination?
  - Billable Hours?
  - Track / get credit for non-billable hours ["A" (Administrative),"B" (Billing) and/or "C" (Client care or development)]?
  - Client Relationships / Contacts?
  - Management / Administration?

- What is 'target' associate? "Baby" lawyers or "Seasoned" veterans or some combination of both?
  - Baby lawyers cost less . . . need more guidance and direction . . . greater turn over . . . possible greater potential . . . work rate/life-work balance may be different due to generational issues and/or 'season of life'
  - Seasoned lawyers cost more . . . can take on greater responsibility . . . less likely to leave – but can also more likely to take business . . . motivated differently

- Staff retention – both associate and support staff
  - Loss of 1 lawyer at 8 person firm = loss of 25 lawyers at 200 person firm
  - How do you retain and keep long-term?
    - Salary?
    - Bonus?
    - "Ownership"?
    - Investment in development?
    - Quality of life?
    - Each attorney is differently motivated.

- Support staff
  - Office manager, secretary and paralegal?

- Ratio to attorneys?
- Generalists / cross-trained
- What, and how much, is delegated?
- How dependent is firm on any one or more support staff specifically?
- Which of their tasks are billable?

- What is done in-house vs. use of outside vendors
  - Accountant
  - Business advisor
  - Bookkeeper
  - IT Company
  - Website
  - Billing coordinator

- Financial Health
  - Careful screening and selection of clients
  - Retainers up-front and replenish
  - Diverse business and/or source of business
  - Monthly A/R review and calls to clients if 90+ days overdue

- How much emphasis / money spent on:
  - Associate development
  - Seminars and CLEs
  - Organizations and memberships
  - Client development and retention

- Work style and location:
  - Actual office location
  - Work at home v. expected to be in office

- 'Espirit de corps'
  - Partner meetings
    - Monthly
    - Location
  - Associate Meetings
    - Monthly/Quarterly
    - Mentoring / Lunches / Tag-alongs
  - All-Office Meetings
    - Lunches
    - "Free lunches"

- Flexibility vs. Rules
  - Family / Personal Issues
  - PTO days
  - Work at Home
- Dress Code
- "Snow" days and "holidays"
- Part-time vs. Full-Time

ETHICAL CONSIDERATIONS IN SMALL FIRM MANAGEMENT:

- As opposed to any other area addressed herein, Small Firm Management is less-regulated by Ethical concerns and canons. It is the internal working of a business, based on business-management principles towards (largely) business-oriented goals. This is not to say that Small Firm Management does not affect, create, or maintain the firm's profile to the world – it does. It *is*, however, to say that the management of a small law firm is akin to maintaining the platform on and environment in which law is practiced.

- Moreso than first meets the eye, the Small Firm Manager must be a visionary who can reasonably project the answers to such rhetorical questions or to resolve such rhetorical conflicts like:

  - We have this wonderfully lucrative business opportunity that Steinmetz has brought us, but MacMain's principal client is a competitor of Steinmetz's prospective client. *While there is no conflict in representation, how do I steer the firm through the possible minefield of potential trade secrets, proprietary information, and maintaining the requisite "walls" within the firm such that the firm and its members can fulfill its obligations without compromising clients' data or knowledge?*

  - One side: Rockne and Leahy are both 5th year lawyers, both with good client relations, good skills, and overall, the kind of lawyers that work well within the body of the firm's work and among the firm's other lawyers. They each have begun to develop their own respective books of business such that they are financial assets to the firm. If they walked, the firm would take a hit. Other side: All but one of the firm's 7 partners came from bigger firms to get out of the "firm management" environment where committees, internal boards, and the like occasioned by the number of lawyers in those firms. Turner has come right out and said that we have enough chiefs and, despite these lawyers being good, we need no more. Christian is of the belief that Rockne and Leahy each need another year or two before being offered a chance to buy into the firm.

- *Do we remain small?*
- *Will Rockne and Leahy "walk" if we do not give them a chance for admission to partnership?*
- *Will we lose Turner and/or Christian if we decide to expand?*

- Management of a small firm is in many ways much more individualized or unique than in any other environment. In larger firms, there are committees which address specific areas with the managing partner working with the chairs thereof to implement strategy and methodologies. In smaller firms, management is so much more personal between the managing member and the individual lawyers. Many lawyers, like myself, enjoy having virtually no management responsibilities due to the desire among others to handle those duties. Other small firms have weekly, or even daily meetings as a matter of course to discuss the day's business and the topics at hand. Still other small firms never need to meet on some things due to a shared philosophy, shared client concerns and expectations among all lawyers, or being composed of lawyers who each have totally different practice areas which almost never overlap. The point is that the management of a small firm is as specialized as the individual members' practice profiles dictate, and accordingly, ethical concerns are much more subtle.

- One final note on ethical considerations in small firm management is that the American Bar Association's Standing Committee on Ethics and Professional Responsibility has issued a draft proposal to amend ABA Model Rule of Professional Conduct 8.4 and Comment [3] to Rule 8.4. The proposed changes to Rule 8.4 are:

  - *It is professional misconduct for a lawyer to:*

  - *(g)* [engage in] *in conduct related to the practice of law, harass or knowingly discriminate against persons on the basis of race, sex, religion, national origin, ethnicity, disability, age, sexual orientation, gender identity, marital status or socio-economic status.*

  - *Comment:*

  - *Paragraph (g) applies to conduct related to a lawyer's practice of law, including the operation 13 and management of a law firm or law practice……..*

- The ABA will consider this change and conduct a public hearing thereon less than 4 weeks prior to the presentation of this paper at the ABA's Winter meeting in (ironically) San Diego. While this change may be considered to have been authorized by Captain

Obvious, it is nonetheless significant because it serves to expand the overt reach of ethical canons and rules to that beyond pure lawyering to law firm management. Given the impact that an individual lawyer has in a smaller firm as opposed to a larger firm, small firm managing members will now have an additional analysis through which to go when faced with employment and retention decisions.

CONCLUSION

While all recognize that all lawyers, not just small firm practitioners, deal with technological, marketing, management, and ethical issues on a regular basis as part of meeting the obligations within our profession, it is clear that the overwhelming majority of firm practitioners in the United States practice in small firms. It has been said that law follows society and technology. Accordingly, it is most often in small firms that the profession sees coming trends and the first signs of the continual reinvention of the self to remain relevant and successful from a business perspective.

This presentation looks at the practice of law in the 21st Century from the perspective of 4 small practitioners from the Northeast, Southeast, and Southwest regions of the United States. The issues each sees are identical, no matter what region the practice lies. While small firm practitioners often enjoy greater freedoms and control of their respective destinies than their larger firm counterparts, those small firm benefits are balanced by the greater "ripple effect" that an individual lawyer's decision has on the firm as a whole. The good news is that while the environments are radically different in small firms than in larger firms, trends among the practice show a trend toward collaboration and self-recognition among both camps.

One might be inclined to say that small firm lawyers might have more freedom to shoot from the hip, but with that, they are required to have better aim.

Cameras in the Examination Room? Level the Playing Field with the Use of IME and Surveillance While Keeping the Plaintiff from Turning the Tables on You

Presence of a Third Party, Attorney or Physician

Many states have a civil procedure rule that permits independent medical examinations with language almost identical to Rule 35 of the Federal Rules of Civil Procedure.

Rule 35(a) provides:

a) Order for an Examination.

> (1) In General. The court where the action is pending may order a party whose mental or physical condition--including blood group--is in controversy to submit to a physical or mental examination by a suitably licensed or certified examiner. The court has the same authority to order a party to produce for examination a person who is in its custody or under its legal control.
>
> (2) Motion and Notice; Contents of the Order. The order:
>
> (A) may be made only on motion for good cause and on notice to all parties and the person to be examined; and
>
> (B) must specify the time, place, manner, conditions, and scope of the examination, as well as the person or persons who will perform it.

The statute appears to be silent on whether a representative for the plaintiff or a third party is permitted to be present at the examination. Several states adopting the language of Rule 35(a) have held that questions concerning the presence of the representative or third party are a matter to be resolved by the trial court in exercise of its discretion. See, e.g., Hegwood v. Montana Fourth Judicial Dist. Court, 75 P.3d 308 (2003); Hayes v. Dist. Court In & For City & Cnty. of Denver, 854 P.2d 1240, 1246 (Colo. 1993).

In Hegwood, the plaintiff was injured in an automobile accident and ordered to submit to an IME. 75 P.3d 308 (2003). The plaintiff opposed the motion and sought a protective order to have (1) a court reporter and video recorder to document the entire examination and (2) plaintiff's counsel to attend the full examination. Id. at 309. Plaintiff argued that such measures were necessary since the physician who would be conducting the exam no longer practiced medicine

and, instead, conducted IMEs for insurance companies and defense counsel full time. Id. at 310. The Montana District Court denied the motion to record the examination and allow plaintiff's attorney to attend the entire examination. Id. at 310. Plaintiff subsequently filed a petition for a writ of supervisory control with the Supreme Court of Montana. Id. at 310. The Court held that it was in the sole discretion of the trial courts to determine whether a protective order should be issued permitting the plaintiff's representative to attend the IME. Id. at 311. The Court noted that merely demonstrating that an examiner performs exams for the insurance industry does not inherently establish the degree of prejudice or potential for abuse that a protective order necessitates. Id. at 312.

In some cases, such as Hegwood, the plaintiff will seek a protective order prior to the examination. However, in others the plaintiff may attempt to bring his or representative to the examination before they resort to filing a protective order with the court. If the latter situation arises, a defendant may be able to prevent the examination from occurring by having the physician object to the examination in the presence of the representative. Hayes v. Dist. Court In & For City & Cnty. of Denver is illustrative of this strategy. 854 P.2d 1240 (Colo. 1993).

In Hayes, the plaintiff was ordered to submit to an IME, but plaintiff rejected submitting to the examination on grounds that the physician was biased against plaintiffs in personal injury litigation. Plaintiff requested the trial court to enter an order requiring the examination to be conducted by another orthopedic surgeon mutually satisfactory to counsel for all parties. Id. at 1242. The trial court denied plaintiff's request and ordered the IME to proceed with the physician chosen by the defendant's counsel. Id.

Upon learning of this order, the plaintiff's counsel directed his paralegal to accompany the plaintiff to the examination and tape-record the examination. Id. Plaintiff's counsel also informed

defendant's counsel of his decision. Id. Defendant's counsel then notified the physician's office that the paralegal would be attending the examination and the physician's office manager objected, explaining that the physician did not conduct examinations under such circumstances because it hindered his ability to establish a rapport with the examinee. Id.

The trial court was notified of these difficulties and subsequently held a hearing to determine the status of a protective order that plaintiff sought in order to have the paralegal attend the examination. Id. The court found that the physician was not biased against the plaintiff or plaintiff's attorney and that he could conduct an impartial medical examination. Id. at 1243.

After the protective order was denied, plaintiff filed a motion for reconsideration claiming that the paralegal's presence was needed because his client suffered from memory loss. Id. at 1246. The Court held that questions concerning conduct of court-ordered physical examinations of personal injury plaintiffs, including the presence of third parties and tape recorders during such examinations, are to be resolved by the trial court in exercise of its discretion. Id. at 1243.

A defendant's physician similarly was able to thwart an IME from taking place in the presence of a third party in a West Virginia case. In State ex rel. Hess v. Henry, the plaintiff in a personal injury action appeared at his IME with a legal stenographer. 393 S.E.2d 666, 667 (1990). The physician objected to the stenographer and the plaintiff refused to proceed without the stenographer. Id. Unlike the cases discussed above, the defendant took additional affirmative actions to prevent the examination from occurring in the presence of a third party. The defendant filed a motion to compel discovery, which the Court granted, disallowing the stenographer's presence. Id. A second examination was scheduled, but plaintiff insisted on bringing a tape recorder to document the examination. Id. The physician again objected that this would be

intrusive and unfruitful, a neurological examination being "neither verbal nor auditory, nor otherwise capable of recordation." Id.

The defendants moved to compel discovery without the tape recorder, which motion the court granted. Id. The court refused plaintiff's request to require the defendants to disclose in advance to plaintiff or his counsel the precise types of tests the physician would conduct or the manner in which they would be conducted. Id. Plaintiff subsequently filed a writ of prohibition with the Supreme Court of Appeals. Id. at 668.

The Court granted the writ and held that the plaintiff was entitled to prior notice of the scope and manner of the examination, but also held that a third party should not be allowed to be present, nor should a tape recorder be allowed, absent a showing of good cause. Id. at 669. The Court noted that good cause should be a circumstance that implies that the truth-finding function of the examination may be threatened absent the requested presence. Id.

Defendants also can prevent a physician chosen by the plaintiff from attending the IME by attacking the credentials of the plaintiff's physician. In Astill v. Clark, the plaintiff sued defendant for personal injuries resulting from an automobile collision. 956 P.2d 1081 (Utah Ct. App. 1998). Plaintiff requested to have her chiropractor present during her IME with a neurologist and to videotape the examination. Id. at 1088. The defendant filed a motion to compel plaintiff to submit to the IME without the presence of her chiropractor and without requiring that the examination be videotaped. Id. Plaintiff claimed error in that there was no "appropriate" monitor to ensure that the IME was properly performed. Id. The Utah Court of Appeals held that it was within the trial court's discretion to require the plaintiff to be accompanied by a neurologist, rather than her chiropractor, during her IME and that because chiropractors and neurologists are trained in different fields a chiropractor is not qualified to evaluate a neurologist's performance. Id.

Recording an Independent Medical Examination

A few of the cases cited above held that the recording of an IME, like the presence of a third party at an IME, is a matter to be resolved by the trial court in exercise of its discretion. See, e.g., Hegwood v. Montana Fourth Judicial Dist. Court, 75 P.3d 308 (2003); Hayes v. Dist. Court In & For City & Cnty. of Denver, 854 P.2d 1240, 1246 (Colo. 1993). In addition, several other state courts have similarly held that the matter is to be determined by the trial court in exercising its discretion. See, e.g., Ratcliff v. Sprint Missouri, Inc., 261 S.W.3d 534 (Mo. Ct. App. 2008); Stone v. Am. Family Mut. Ins. Co., 178 Wis. 2d 589 (Ct. App. 1993)

In Ratcliff, the Missouri Court of Appeals held that the trial court acted within its discretion in not granting a protective order allowing a worker to record the independent psychological examination of him in a worker's premises liability action where Missouri's rule authorizing IME's was silent on the recording of exams. 261 S.W.3d at 534. Similarly in Stone, the Wisconsin Court of Appeals held in a case where the plaintiff requested that her IME be recorded to alleviate her anxiety, that the determination of whether an IME could be recorded should be made by the trial court on a case-by-case basis. 178 Wis. 2d at 589.

Other states require the plaintiff to demonstrate good cause warranting the recording of the IME. See, e.g., Muci v. State Farm Mut. Auto. Ins. Co., 478 Mich. 178, 193 (2007); State ex rel. Hess v. Henry, 183 W. Va. 28, 31(1990). For example, in Muci the Supreme Court of Michigan held that it was proper for the trial court to impose conditions on an IME which included videotaping where the plaintiff proffered evidence that the doctor previously engaged in inappropriate questioning. 478 Mich. At 193.

Some states similarly require the plaintiff to present special circumstances that necessitate the recording of the examination. See, e.g., Henry v. Barlow, 948 So. 2d 895 (La. App. 3 Cir. 2006); Lamendola v. Slocum, 538 N.Y.S.2d 116 (1989). In Henry, the plaintiff requested for its attorney to be present at the IME to prevent a "swearing match". Id. The Court held that the plaintiff was not permitted to have his attorney present at the examination and noted that Louisiana Code of Civil Procedure Article 1464 does not afford plaintiffs an absolute right to have their attorneys present at the examination and therefore a plaintiff must present special circumstances that warrant the presence of counsel and videotaping at his examination. Id. at 897.

The leading case in New York on the issue is Lamendola v. Slocum. 538 N.Y.S.2d 116. In Lamendola, the Third Department Appellate Division held that a plaintiff was not permitted to videotape his IME because the plaintiff failed to show that "special or unusual circumstances" existed that warranted the videotaping of the examination. Id. at 118. In an article for the New York Law Journal entitled "Law Does Not Support Videotaping IMEs", Alice Spitz noted that many New York cases have not permitted the videotaping of IMEs. She stated, "three out of the four Appellate Divisions as well as several lower courts have ruled that the videotaping of an IME was appropriately prohibited."

In addition, Spitz noted that the burden of proving special or highly unusual circumstances is extremely high and stated that the limited examples where the burden was met included where the party being examined was incompetent or comatose and "unable to review the examination with his attorney or testify at trial as to the manner in which the examination was conducted". Alice Spitz, Law Does Not Support Videotaping IMEs, NEW YORK LAW JOURNAL, Nov. 20, 2013 (Citing Mosel v. Brookhaven Mem. Hosp., 134 Misc.2d 73 (Sup. Ct. Suffolk County 1986).

Other states have explicit statutory provisions that permit the recording of IMEs. Cal. Civ. Proc. Code § 2032.510 (West). Wash. Super. Ct. Civ. R. 35. For example the California Civil Procedure Code provides that "The attorney for the examinee or for a party producing the examinee, or that attorney's representative, shall be permitted to attend and observe any physical examination conducted for discovery purposes, and to record stenographically or by audio technology any words spoken to or by the examinee during any phase of the examination.". Cal. Civ. Proc. Code § 2032.510(a) (West).

Similarly Washington's Superior Court Civil Rules provide that "Unless otherwise ordered by the court, the party being examined or that party's representative may make an audiotape recording of the examination which shall be made in an unobtrusive manner. A videotape recording of the examination may be made on agreement of the parties or by order of the court.". Wash. Super. Ct. Civ. R. 35(3).

Recently, the issue of recording an IME was front and center in New York State. In Bermejo v. New York City Health and Hospital Corporation, 2015 NY Slip Op 08374 (Nov. 18, 2015 App. Div. 2d Dept.), plaintiff was examined by Dr. Michael Katz, an orthopedist, on two occasions. Unbeknownst to the defendants, plaintiff's counsel, who was present at the second IME, secretly taped the exam.

During the trial, Dr. Katz was asked by plaintiff's counsel how long his second examination took. The doctor responded that he was "uncertain." In response to another question from counsel, he further testified that he could not recall how long the examination took and when asked, if in his experience, would it take less than fifteen minutes, he replied "quite frankly, I don't know."

At this point the trial judge intervened and told Dr. Katz that he could not accept that answer and "I will have to insist on what your custom and practice would be as to what type of, the length

of an exam of this type." Dr. Katz replied, "I think in the range of between ten and twenty minutes would be appropriate."

Plaintiff's paralegal, who was also present at the second examination (must have been a crowded room), then took the stand and testified that the exam took three minutes and that she knew it took three minutes because she "timed it" with her phone. On redirect, plaintiff's counsel then asked if she had any other information regarding how long the examination took and she stated that she did and said "you [meaning plaintiff's counsel] took a video of the examination." The judge cleared the Courtroom and then, after a lengthy argument over the course of several days, declared a mistrial.

As noted in the attached sheet concerning each state's policy with respect to IMEs, New York CPLR 3121 and case law hold that: "Decisions on requests for permission to videotape IMEs have been made on a case by case basis, and videotaping has not been allowed in the absence of special unusual circumstances".

The rationale behind these rulings contemplate that a plaintiff would normally be entitled to have his or her attorney present at an IME and therefore there would be no need to tape the exam. In attempting to justify the surreptitious taping of the IME, the plaintiff argued that he did not exchange the video because they were not going to use it on his direct case and would only use it as rebuttal evidence. Plaintiff's counsel also claimed that the recording constituted work product.

It was also noted that there was a "history" between Dr. Katz and plaintiff's counsel. In his report of the first IME, Dr. Katz noted that the plaintiff's counsel refused to allow his client to answer any questions relating to the happening of the accident, the medical treatment he received afterwards and his present complaints. Dr. Katz further noted that plaintiff's counsel "presented

quite a nasty and obstructive front towards getting the proper history…. [Plaintiff's counsel] just became nastier as questions were asked. It is highly unusual for an individual's attorney to behave as [plaintiff's counsel] did in order to mislead the examiner and try to get them to believe that these changes were acute and not chronic."

Plaintiff's attorney explained that he was further motivated to record the second IME after Dr. Katz's first IME report was issued, which contained "untrue accusations" that plaintiff's counsel had engaged in obstructive behavior.

New York State also has a discovery rule that many other State Courts employ that applies to the exchange of photographs or videotapes. CPLR 3101(a)(i) sets forth that there shall be full disclosure of all material by a party of all photographs, videotapes or audiotapes. While it was noted that this rule was enacted for the primary purpose of preventing unfair surprise in situations where a defendant uses surveillance video, the statute employs broad language, not limited to such a scenario, but instead requires disclosure of "*any* films, photographs, videotapes or audiotapes" of a party, regardless of who created the recording or for what purpose."

The Court noted that the case law contemplates that a plaintiff normally will be entitled to have his or her attorney present at an IME, but permission to employ the additional measure of videotaping the examination will be granted only where the plaintiff establishes the existence of special and unusual circumstances. The latter proposition presupposes that a request for the Court's permission to engage in videotaping will be made. What the law "does not contemplate is plaintiff's attorney taking it upon themselves to surreptitiously videotape an IME, without the knowledge of the examining physician, without notice to the defendant's counsel, without seeking permission to the Court."

The Court found against the plaintiff and sent attorneys a strong message by finding that the defendant was entitled to recover from plaintiff's counsel the costs they incurred in participating in the trial on the issue of damages, as well as the costs they incurred in making and litigating the motions at issue on these appeals and then pursuing these appeals.

What these cases show is that there is still a strong sentiment against videotaping of IMEs and that legal skullduggery will be met with intolerance and sanctions. The Appellate Judges in Bermejo were incensed that plaintiff's counsel never disclosed the existence of the videotape.

How does this play out in the future? California allows videotaping of IMEs and California, more often than not, is at the forefront of legal developments that other states eventually adopt. However, there does seem to be an innate unfairness as plaintiff's attorneys are allowed to tape IMEs while defense attorneys are prevented from gaining access to examinations of the plaintiff by plaintiff's doctors to see what truly transpires behind the curtain.

STICKS AND STONES MAY BREAK ONE'S BONES, BUT WORDS CAN RUIN A BUSINESS: PROTECTING YOUR CLIENT FROM COMMERCIAL DISPARAGEMENT

FDCC 2016 Winter Meeting
Hotel Del Coronado - San Diego, California

February 28th through March 4th, 2016

Presented to the:
Commercial Litigation Section
and
Intellectual Property Section

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Kevin C. Cain is admitted to practice in Massachusetts and Rhode Island. He AV rated by Martindale-Hubbell and a Massachusetts Super Lawyer. His practice focuses on general civil litigation, risk management, and regulatory compliance, representing public and private companies, insurers, professionals, and individuals in a variety of matters. He is a pilot with an active aviation practice, a registered patent attorney, a FINRA public arbitrator, and CIPP/US certified by IAPP.

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In the area of professional liability, he has defended law firms and individual lawyers, including significant experience defending specialized practitioners such as patent attorneys. He has also defended real estate brokers, securities brokers, registered investment advisors, insurance brokers, architects, engineers and psychologists. Additionally, he incorporates his experience as a licensed private pilot in the representation of major airlines, aircraft owners, pilots, repair facilities, fixed based operators, flight instructors, and aviation insurers. He is panel counsel to the Aircraft Owners and Pilots Association ("AOPA").

In addition to the above, Kevin has enjoyed a challenging insurance defense practice in the defense of insurers in coverage and bad faith matters and their insureds in a myriad of general liability, D&O, EPL, environmental and toxic tort cases; including extensive experience in the defense of personal injury and property damage cases. Kevin has had the pleasure of representing retailers, distributors, and product manufacturers in a number of cases alleging breach of warranty and negligent design and manufacture.

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STICKS AND STONES MAY BREAK ONE'S BONES; BUT WORDS CAN RUIN A BUSINESS: PROTECTING YOUR CLIENT FROM COMMERCIAL DISPARAGEMENT

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INTRODUCTION

Your successful corporate client calls you for advice because its biggest competitor is disparaging your client's products and services. Your enraged client wants to sue. You ask yourself "What legal and equitable remedies are available?" You may also ask yourself, "What non-legal remedies are available?" Many corporate transactional lawyers and business litigators likely will face these core questions at some point in their careers. This article is intended to help those lawyers answer such questions and counsel their clients effectively.

The first section of the article discusses the tort of commercial disparagement, including the history of the tort, how to assert a claim, and special considerations arising from internet disparagement. Some states, however, refuse to recognize that tort, and some litigators prefer the benefit of asserting alternative remedies that may be available in any given jurisdiction. Accordingly, the second section of the article provides an overview of other business disparagement-related remedies, whether assertable as additional causes of action in states that recognize the tort of commercial disparagement or assertable in states that do not recognize the tort. Indeed, injurious statements about a corporation's products or services may also constitute defamation, false advertising under the Lanham Act, statutory or common law deceptive trade practices, or tortious interference with business or economic advantage. Finally, the article concludes with information regarding the use of public relations professionals to address disparagement situations.

I. REMEDIES FOR COMMERCIAL DISPARAGEMENT

Disparagement is a subset of tort law. One is liable for disparagement when he publishes a statement that casts "doubt upon the quality of another's land, chattels or intangible things, or upon the existence or extent of his property in them." Restat. 2d of Torts, § 629. However, when a defendant engages in commercial disparagement, he has casted 'written aspersions . . . upon the quality of the plaintiff's goods," thereby preventing the plaintiff from selling them. Restat. 2d of Torts, § 626. Commercial disparagement claims, especially under federal law, typically arise when a rival merchant makes untrue and detrimental statements about a competitor's product through a comparative advertisement. (1-13 The Law of Advertising § 13.04). In this context, an advertiser has engaged in commercial disparagement when he knowingly publishes a statement that denigrates the quality of another's products, services, or business practices where such denigration is likely to cause monetary loss due to the reduction in sales. *Id.*

A. History of Commercial Disparagement

Commercial disparagement derives from the common law tort of slander of title to land, which compensates a property owner for the financial loss suffered when a defendant falsely and maliciously states that the property owner does not have the proper title to convey. *Developments in the Law--Competitive Tort*, 77 Harv. L. Rev. 893 (1964). Over time, this tort has evolved to concern many other types of disparaging remarks, including those regarding the quality of goods, services, or business practices. (1-13 The Law of Advertising § 13.04). Today, the tort

can be interchangeably described as "injurious falsehood," "trade libel," "defamation of goods," "slander of goods," "commercial disparagement," "product disparagement," or "property disparagement." *Id.* (collecting cases).

Actions for commercial disparagement are analogous to actions for defamation in the sense that both actions involve damages to reputation. *Id.* The two actions are distinct however, because defamation actions are brought to help protect the personal reputation of a plaintiff, whereas commercial disparagement suits are brought to protect the business reputation of a plaintiff. *Id.* It is in this sense that allegations of commercial disparagement are unique because they address statements only reflecting the quality of a seller's product or the character of a plaintiff's business. *Defamation of Manufacturer, Regarding Product, Other than Through Statement Charging Breach or Nonperformance of Contract*, 104 A.L.R. 5th 523, 2b.

Originally, commercial disparagement law was "exclusively a state realm area." Callmann on Unfair Comp., Tr. & Mono. § 11:1 (4th Ed.) However, in 1989, the Trademark Law Revision Act amended certain provisions of the Lanham Act (15 U.S.C. § 1125(a)) to make allegations of commercial disparagement actionable under federal law. (1-11 The Law of Advertising § 11.02). Prior to these amendments, 15 U.S.C. § 1125[2] limited false advertisement claims to instances where an individual made a claim about their own products or statements in a comparative statement. (2-31 The Law of Advertising § 31.03). Nothing in the pre-amendment act provided for relief when an individual made statements about his competitor's products or services. *Id.* However, the Trademark Law Revision Act expanded the scope of false advertising claims and made a distinct change to 15 U.S.C. § 1125(a), by adding the following language to the statute: "misrepresents the nature, characteristics, qualities, or geographic origin of his or her or another person's goods, services, or commercial activities". This additional language made commercial disparagement actionable as a false advertisement for the first time. (1-11 The Law of Advertising § 11.02); see also *Eckel Indus. v. Primary Bank*, 26 F. Supp. 2d 313, 316 (D.N.H. 1998) (explaining "that because section 43(a) applies both to false representations made by the defendant about its own goods and to false statements made by the defendant about the plaintiff's goods, the section applies to trade libel as well as unfair competition and false advertising").

B. <u>Federal Law and the Lanham Act</u>

The Lanham Act authorizes a plaintiff to bring an action for commercial disparagement[3] against a defendant when the defendant makes false and misleading statements about the plaintiff's goods. The Act provides, in pertinent part:

> (1) Any person who, on or in connection with any goods or services, or any container for goods, uses in commerce any word, term, name, symbol, or device, or any combination thereof, or any false designation of origin, false or misleading description of fact, or false or misleading representation of fact, which

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[2] The Lanham Act used to be codified at U.S.C. § 43(a) for false advertising claims.

[3] Under Lanham jurisprudence, most courts refer to the phrase "commercial disparagement" as "trade libel."

…

> (B) [I]n commercial advertising or promotion, misrepresents the nature, characteristics, qualities, or geographic origin of his or her or another person's goods, services, or commercial activities, shall be liable in a civil action by any person who believes that he or she is or is likely to be damaged by such act.

15 U.S.C. § 1125(a)(1)(B).

1. Standing Requirements

A party has standing to maintain an action for commercial disparagement or false advertising under the Lanham Act when the party pleads (1) "an injury to a commercial interest in sales or business reputation," and (2) that such injury was "proximately caused by the defendant's misrepresentations." *Lexmark Int'l, Inc. v. Static Control Components, Inc.*, 572 U.S. - - -, 134 S. Ct. 1377, 1395 (U.S. 2014).

(a) Injury to a Commercial Interest in Sales or a Business Reputation

With regards to the first requirement, the Court in *Lexmark* looked to whether the plaintiff was alleging an injury to the "zone of interest" protected by the Lanham Act. *Id.* at 1388-89. The Court found that the Act's goal was to protect persons engaged in interstate commerce against unfair competition. *Lexmark Int'l, Inc.*, 134 S. Ct. at 1389. The Court understood the concept of "unfair competition" to concern "injuries to business reputation and present sales." *Id.* at 1389-90. Accordingly, the Court explained that "to come within the zone of interests in a suit for false advertising under §1125(a), a plaintiff must allege an injury to a commercial interest in reputation or sales." *Id.* at 1390. Thus, neither a consumer nor a business who are "hoodwinked" into purchasing an inferior product from a seller have standing to bring a claim under § 1125(a)(1)(B).

Applying this principle to facts in *Lexmark*, the Court concluded that the plaintiff's alleged injuries were within the zone of interest protected by the statute because "[the plaintiff's] alleged injuries—lost sales and damage to its business reputation—are injuries to precisely the sorts of commercial interests the Act protects." *Id.* at 1393. There, the defendant, Lexmark, manufactured and sold laser printers and further sold toner cartridges for its laser printers. *Id.* at 1383. The plaintiff, Static Control, was "the market leader [in] making and selling components necessary to remanufacture Lexmark cartridges, components of which were specifically designed to mimic Lexmark's components. In turn, Static Control would sell these products to remanufacturers. *Id.* at 1384. Static Control alleged that Lexmark sent letters to most of the companies in the remanufacturing business advising that it was illegal to use Static Control's products to refurbish cartridges. *Id.* Moreover, Static Control alleged that the statements in those letters misrepresented "the nature, characteristic, and quality" of its products and injuring Static Control by (1) "diverting sales from Static Control to Lexmark," and (2) injuring Static Control's business reputation by "leading consumers and others in the trade to believe that Static Control is engaged in illegal conduct." *Id.* The Court reasoned that Static Control had standing because it was "suing not as a deceived consumer, but as a "perso[n] engaged in" 'commerce within the

control of Congress' whose position in the marketplace has been damaged by [the defendant's] false advertising." *Id.* at 1393.

(b) <u>The Alleged Injury Was Proximately Caused by the Defendant's Misrepresentations</u>

In order for a plaintiff to satisfy the proximate cause prong under § 1125(a)'s standing requirement, it "ordinarily must show economic or reputational injury flowing directly from the deception wrought by the defendant's advertising; and that that occurs when deception of consumers causes them to withhold trade from the plaintiff." *Id.* at 1391. The Court noted that the intervening step of consumer deception does not make the plaintiff's alleged commercial injuries too remote from the defendant's unlawful conduct, because in the commercial context, "all commercial injuries from false advertising are derivative of those suffered by consumers who are deceived by the advertising." *Id.* at 1390-91. In other words, in commercial disparagement cases "a plaintiff can be directly injured by a misrepresentation even where a 'third party', and not the plaintiff relied on it." *Id.* at 1391.

Applying the aforementioned principles to the facts in *Lexmark*, the Court held that Static Control's allegations satisfied the proximate cause requirement for two reasons. *Id.* at 1393. The Court characterized Lexmark's assertions that Static Control's business was "illegal" as an example of a defendant harming a plaintiff's reputation by casting aspersions on his business, thereby indicating that Static Control's injury flew directly "from the audience's belief in the disparaging statements." *Id.* Regarding this allegation, the Court noted that it was irrelevant that Static Control and Lexmark were not competitors for proximate cause purposes because the key inquiry for proximate cause is whether the plaintiff was directly harmed by the attack on its merchandise. *Id.* at 1394. The Court also found the allegation that Lexmark's false advertising proximately caused a reduction in Static Control's sales sufficient because Static Control's products could only be used for Lexmark's cartridges. *Id.* Accordingly, the Court explained, given that Static Control was the market leader in designing Lexmark products for sale to remanufacturers, it should the follow that the decrease in sales for remanufacturers would correlate directly to the decrease in sales for Static Control. *Id.*

2. <u>Elements of a Commercial Disparagement Claim</u>

In commercial disparagement actions, most jurisdictions require that a plaintiff prove[4] **each** of the following elements: (1) a false or misleading description of fact about another's product or service; (2) was made in a commercial advertisement; (3) materiality of that description or representation in that it is likely to influence the purchasing decisions of its target audience; (4) actual deception or a tendency to deceive a substantial segment of the target audience; (5) entry of the description or representation into interstate commerce; and (6) likely or actual injury to the

[4] Courts appear to be split over whether commercial disparagement claims require heightened pleading. *See, e.g., John P. Villano Inc. v. CBS, Inc.,* 176 F.R.D. 130, 131 (S.D.N.Y. 1997) ("a claim of false advertising under § 1125 . . . falls outside the ambit of Rule 9(b) and may not be the subject of any heightened pleading requirement"); but see *LT Int"l Ltd. v. Shuffle Master, Inc*., 8 F. Supp. 3d 1238, 1245 (D. Nev. 2014) (explaining that Lanham False Advertising claims must "satisfy the particularity requirement of Rule 9(b)").

plaintiff as a result of the description or representation through, for example, plaintiff's demonstrated loss of sales or good will. *See, e.g.*, *Clorox Co. v. Proctor & Gamble Commer. Co.*, 228 F.3d 24, 33 n.6 (1st Cir. 2000); *IQ Prods. Co. v. Pennzoil Prods. Co.*, 305 F.3d 368, 375 (5th Cir. 2002); *Southland Sod Farms v. Stover Seed Co.*, 108 F.3d 1134, 1139 (9th Cir. 1997).

(a) <u>False or Misleading Descriptions About Another's Product or Services</u>

Generally speaking, all jurisdictions have held that false statements constituting a Lanham Act violation fall into two categories: (1) commercial claims that are literally false as factual matter, and (2) implicitly false statements that are misleading. *See, e.g.*, *Time Warner Cable, Inc. v. DIRECTV, Inc.*, 497 F.3d 144, 153 (2d Cir. 2007).

(i) <u>Literal Falsehoods</u>

In order for a plaintiff to prevail on allegations that a claim is literally false, the message in the commercial advertisement must be unambiguous. In other words, the language in the message must be susceptible to only one interpretation. *Id.* at 158; *see, e.g.*, *Pharmacia Corp. v. GlaxoSmithKline Consumer Healthcare*, L.P., 292 F. Supp. 2d 611, 615 (D.N.J. 2003) (addressing a literal falsehood claim when the defendant, a marketer of the nicotine patch, "Nicotrol," advertised a commercial regarding its competitor's product, "Nicoderm," that depicted "a man tossing and turning in bed and said "Trying to beat cigarettes? Having trouble sleeping? You're probably using NicoDerm"). In instances where a plaintiff alleges that an advertising claim is literally false, courts focus on the substance of what is conveyed and the plaintiff must produce evidence that affirmatively shows the claim is literally false. *Time Warner Cable, Inc. v. DIRECTV, Inc.*, 497 F.3d 144, 153 (2d Cir. 2007); (1-11 The Law of Advertising § 11.02). Therefore, claims of literal falsehood are issues of fact. *Clorox Co. v. Proctor & Gamble Commer. Co.*, 228 F.3d 24, 34 (1st Cir. 2000). When a plaintiff is able to produce such evidence, courts bypass the elements of proof regarding the advertisement's deception on customers. *See, e.g.*, *Time Warner Cable, Inc. v. DIRECTV, Inc.*, 497 F.3d 144, 153 (2d Cir. 2007) (explaining, "when an advertisement is shown to be literally or facially false, consumer deception is presumed and "the court may grant relief without reference to the advertisement's [actual] impact on the buying public"). Courts may base literal falsity determinations upon either the explicit claims made by an advertisement or any claims the advertisement conveys by "necessary implication." *Clorox Co. v. Proctor & Gamble Commer. Co.*, 228 F.3d 24, 34-35 (1st Cir. 2000). If the circumstances are appropriate, courts may determine whether an advertisement is literally false "based on its own common sense and logic interpreting the message." *Doctor's Assocs. v. QIP Holder LLC*, 2010 U.S. Dist. LEXIS 14687, *43 (D. Conn. 2010). In making this determination, courts will apply the "false by necessary implication" doctrine. *See Scotts Co. v. United Indus. Corp.*, 315 F.3d 264, 274 4th Cir. 2002). Under this doctrine, "a district court evaluating whether an advertisement is literally false "must analyze the message conveyed in full context," i.e., it "must consider the advertisement in its entirety"" and determine if the audience would recognize the claim as readily as if it had been explicitly stated. *Time Warner Cable, Inc. v. DIRECTV, Inc.*, 497 F.3d 144, 158 (2d Cir. 2007). "If the words or images, considered in context, necessarily imply a false message, the advertisement is literally false and no extrinsic evidence of consumer confusion is required." *Id.*

Applying the above principles in the commercial disparagement context, the court in *Doctor's Assocs. v. QIP Holder LLC* held that a jury reasonably could conclude that a Quiznos commercial disparaging Subway sandwiches was literally false. *Doctor's Assocs.*, 2010 U.S. Dist. LEXIS 14687 at 48. There, a Quiznos commercial stated that Quiznos's prime rib sandwiches contained "two times the meat" as the Subway cheesesteak sandwich. *Id.* Quiznos argued that this statement was true because Quiznos specifications call for 5.0 ounces of meat, whereas Subway's specifications call for 2.5 ounces of meat. *Id.* at 45. The court, however, rejected this assertion because audits and surveys of Quiznos franchises revealed that 44.14% of the franchises failed to meet the requisite 5.0 ounce standard for meat, 74% of the of franchises made sandwiches containing less than 4.5 ounces of meat, and 5.86% of the franchises made sandwiches that contained less than 4.0 ounces of meat. *Id.* at 47. Accordingly, the court explained that based on such evidence, it was reasonable that the "twice the meat" language was literally false. *Id.* at 48.

Also, under the false by necessary implication doctrine, the court in *Doctor's* examined the advertisement in the full context and further concluded a jury could find the "twice the meat" language was literally false because (1) all Subway sandwiches were available with a double portion of meat, a fact Quiznos never disclosed, and (2) Quiznos had depicted a Subway cheesesteak sandwich, a sandwich long discontinued in favor of the current steak and cheese sandwich, which contains at least 2.5 ounces of meat. *Doctor's Assocs.*, 2010 U.S. Dist. LEXIS 14687 at 49. The court reasoned that such a conclusion was appropriate because the "twice the meat" message was unambiguous and sought to directly convey that a Quiznos sandwich had twice the meat as a Subway sandwich. *Id.*

(ii) <u>Implicit Falsehoods and Proving Deception</u>

Even if an advertising claim is not literally false, a plaintiff still has recourse under the Lanham Act if he or she "can show that the advertisement, while not literally false, is nevertheless likely to mislead or confuse consumers." *Time Warner Cable, Inc. v. DIRECTVInc.*, 497 F.3d 144, 153 (2d Cir. 2007). Courts have characterized misleading advertising as implied falsehoods. Implied falsehoods are statements that, "whatever its literal truth, has left an impression on the listener [or viewer] that conflicts with reality -- a claim that invites a comparison of the impression, rather than the statement, with the truth. *Id.*

To support a finding of an impliedly false message, courts rely on extrinsic evidence of consumer deception to show that the advertisement misleads the audience. *Clorox Co. v. Proctor & Gamble Commer. Co.*, 228 F.3d 24, 36 (1st Cir. 2000). In these instances, courts generally have accepted that the best evidence showing the requisite consumer deception is usually offered through a consumer survey[5] "that shows that a substantial percentage of consumers are taking away the message that the plaintiff contends the advertising is conveying." *See, e.g.,*

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[5] However, it should be noted that some courts in addition to looking at consumer surveys will also consider other forms of extrinsic evidence of deception provided they are reliable. *See Hickson Corp. v. Northern Crossarm Co.*, 357 F.3d 1256, 1261 (11th Cir. 2004) (explaining that a plaintiff attempting to establish an implied falsehood "must "present evidence of deception" in the form of consumer surveys, market research, expert testimony, or other evidence").

Johnson & Johnson Merck Consumer Pharmaceuticals Co. v. Smithkline Beecham Corp., 960 F.2d 294, 298 (2d Cir. 1992)**.**

(iii) Establishment Claims

As a general matter, allegations that advertisements are literal or implicit falsehoods fall into two different categories: non-establishment claims and establishment claims. Literal and implicit falsehoods are examples of non-establishment claims. Non-establishment claims are simply statements in commercials which do not purport to be based on test results. Non-establishment claims neither mention nor rely on tests to prove the inferiority of a competitor's product. *Castrol, Inc. v. Quaker State Corp.*, 977 F.2d 57, 62 (2d Cir. 1992). Conversely, establishment claims occur "when the challenged advertisement relies either implicitly or explicitly on scientific studies." *Johnson & Johnson Vision Care, Inc. v. Ciba Vision Corp.*, 348 F. Supp. 2d 165, 178 (S.D.N.Y. 2004). In these instances, a defendant's advertisement contends that clinical tests prove the superiority of its product over the plaintiff's product. *P&G v. Ultreo, Inc.*, 574 F. Supp. 2d 339, 345 (S.D.N.Y. 2008).

In such cases where the defendant's advertising cites consumer testing, many circuits have recognized that the plaintiff's burden of proof changes such that the plaintiff, in order to prove falsity, must either (1) prove that these tests do not establish the proposition for which they were cited, or (2) prove these tests are not sufficiently reliable to reasonably confirm the purported claim. *See, e.g.*, *Castrol, Inc. v. Quaker State Corp.*, 977 F.2d 57, 62 (2d Cir. 1992); *Castrol, Inc. v. Pennzoil Co.*, 987 F.2d 939, 952 (3d Cir. 1993); *C.B. Fleet Co. v. SmithKline Beecham Consumer Healthcare L.P.*, 131 F.3d 430, 435 (4th Cir. 1997*)*; *BASF Corp., v. Old World Trading Co.*, 41 F.3d 1081, 1090 (7th Cir. 1994); *Rhone-Poulenc Rorer Pharms. Inc. v. Marion Merrell Dow, Inc.*, 93 F.3d 511, 514-15 (8th Cir. 1996); *Southland Sod Farms v. Stover Seed Co.*, 108 F.3d 1134, 1139 (9th Cir. 1997); *Johnson & Johnson Vision Care, Inc. v. 1-800 Contacts, Inc.*, 299 F.3d 1242, 1248 (11th Cir. 2002). To meet this burden of proof, a plaintiff must either attack the validity of the defendant's tests directly or show that the defendant's tests are contradicted or unsupported by other scientific tests. *Southland Sod Farms v. Stover Seed Co.*, 108 F.3d 1134, 1139 (9th Cir. 1997); *McNeil-P.C.C., Inc. v. Bristol-Myers Squibb Co.*, 938 F.2d 1544, 1549 (2d Cir. 1991). Courts require this process because, in establishment cases, "the fact of the validation becomes an integral and critical part of the claim." *C.B. Fleet Co. v. SmithKline Beecham Consumer Healthcare, L.P.*, 131 F.3d 430, 435 (4th Cir. 1997).

Applying the above establishment claim principles in the commercial disparagement context, the court in *Star-Brite Distrib. v. Kop-Coat, Inc.* found an advertisement incorrect and misleading because the advertisement's cited test neither proved the claim it purported to substantiate nor was even reliable to reach such a conclusion. 664 F. Supp. 2d 1246, 1250 (S.D. Fla. 2009). There, the defendant's advertisement claimed that boats using its E10 based fuel would improve their performance by 138% whereas boats that used the plaintiff's E10 based fuel would only improve their performance by 4%. *Id.* The advertisement further cited the ASTM D25 test which the defendant conducted in support of its findings. *Id.* at 1249-50. The court disregarded these findings, however, because (1) the ASTM D25 test was not designed to test E10 based fuels, and (2) subsequent testing using the ASTM D25 test indicated that the plaintiff's E10 based fuel improved performance in boats by 60%. *Id.* at 1249-50; *but see Johnson & Johnson Vision Care, Inc.*, 299 F.3d at 1248-49 (11th Cir. 2002) (finding an advertisement stating that

customers preferred the defendant's contacts lens over the plaintiff's contact lens to not literally be false, despite the commercial's cited study failing to "make it clear to the consumer that the study was comparing modalities[6] . . . and not the quality of lenses with the same modality" because a survey testing for modality nevertheless still could lead to the conclusion of consumer preference).

(b) <u>Sufficiently Proving Deception</u>

In order to show the requisite consumer deception, the proffered evidence, typically in the form of a survey, must show that "a substantial percentage of consumers are taking away the message that the plaintiff contends the advertising is conveying." *Johnson & Johnson Merck Consumer Pharmaceuticals Co. v. Smithkline Beecham Corp.*, 960 F.2d 294, 298 (2d Cir. 1992). *See, e.g., Church & Dwight Co. v. S.C. Johnson & Son*, 873 F. Supp. 893, 911 (D.N.J. 1994) noting that *"courts have found survey figures to be sufficient when they revealed that 21* percent to 34 percent, "over 25 percent," and 33 percent of respondents received *a misleading* message from the ad." *Id.* (quoting 4 McCARTHY ON TRADEMARKS AND UNFAIR COMPETITION § 32:54[4], at 32-249 (3d ed. 1994)).

(i) <u>Exception to Proving Deception in Implied Falsehoods</u>

Courts have held that when there is an egregious intent by the defendant to deceive consumers, the plaintiff is no longer required to show extrinsic evidence of consumer deception. *See, e.g.*, *Johnson & Johnson v. Smithkline Beecham Corp.*, 960 F.2d 294, 298 (2d Cir. 1992) (stating, "where a plaintiff adequately demonstrates that a defendant has intentionally set out to deceive the public," and the defendant's "deliberate conduct" in this regard is of an "egregious nature," a presumption arises "that consumers are, in fact, being deceived"). This presumption of consumer deception can apply to implied falsehoods. *MMM Healthcare, Inc. v. MCS Health Mgmt. Options*, 818 F. Supp. 2d 439, 450 (D.P.R. 2011). When there are allegations that the defendant deliberately made false or misleading statements in its advertising, the key inquiry becomes whether such statements were made "with knowledge of their false or misleading nature." *Porous Media Corp. v. Pall Corp.*, 110 F.3d 1329, 1334 (8th Cir. 1997).

For example, in *PBM Prods., LLC v. Mead Johnson & Co.*, the Fourth Circuit found that a defendant's intent to deceive sufficed as evidence that the advertisement misled consumers. 639 F.3d 111, 125 (4th Cir. 2011). Making an implied falsehood claim, the plaintiff introduced into evidence the history of prior litigation with the defendant concerning other prior commercial disparagements claims. *Id.* The Fourth Circuit reasoned that such evidence was relevant because it spoke to the fact that the defendant was intent on making misleading claims about the plaintiff's product. *Id*. The Fourth Circuit further explained that intent was a reasonable inference because, "as the litigation history of the parties demonstrates, despite having twice been restrained from disseminating misleading advertising, the defendant continued to do so." *Id.* at 127. The Fourth Circuit went on to express that "a defendant's history of false advertising could, in a proper case,

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[6] In this context, modality in the consumer study referred to the "length of time wearing the lens, one day wear versus two week wear." *Johnson & Johnson Vision Care, Inc.*, 299 F.3d at 1248-49.

operate to relieve the plaintiff of presenting extrinsic evidence of consumer confusion created by an impliedly false advertisement." *Id.* at 125.

(c) Materiality

Even in cases where the plaintiff proves literal falsity, most courts[7] have held that plaintiff still must establish materiality in order to succeed on a Lanham Act claim. *See Johnson & Johnson Vision Care, Inc. v. 1-800 Contacts, Inc.*, 299 F.3d 1242, 1250 (11th Cir. 2002) (explaining "the materiality requirement is based on the premise that not all deceptions affect consumer decisions" and that even if a statement is literally false, it still may be "irrelevant to consumer decisions"). To prove that a description or representation is material, the plaintiff must show that the description or representation is likely to influence a consumer's purchasing decision. *Johnson & Johnson Vision Care, Inc.*, 299 F.3d at 1250. "A plaintiff may establish this materiality requirement by proving that the defendants misrepresented an inherent quality or characteristic of the product."[8] *Id.*

(d) Commercial Advertising or Promotion

The court in *Gordon & Breach Sci. Publishers S.A. v. Am. Inst. of Physics* promulgated the landmark four-factor test in determining whether a representation constitutes commercial advertising or promotion under the Lanham Act. That test requires that the representation must be:

> (1) commercial speech; (2) by a defendant who is in commercial competition with plaintiff; (3) for the purpose of influencing consumers to buy defendant's goods or services. While the representations need not be made in a "classic advertising campaign," but may consist instead of more informal types of "promotion," the representations (4) must be disseminated sufficiently to the relevant purchasing public to constitute "advertising" or "promotion" within that industry.

Gordon & Breach Sci. Publrs. S.A. v. Am. Inst. of Physics, 859 F. Supp. 1521, 1536 (S.D. N.Y. 1994). All circuits have adopted and cited the *Gordon & Breach* four-factor test in evaluating commercial advertising and promotion in the commercial disparagement context, except for the Second Circuit, which only adopted three elements of the four-prong test enunciated in *Gordon &*

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[7] The Fifth Circuit conflates the elements of deception and materiality and has held that in all false advertising cases, "with respect to materiality, when the statements of fact at issue are shown to be literally false, the plaintiff need not introduce evidence on the issue of the impact the statements had on consumers." *Pizza Hut, Inc. v. Papa John"s Int"l*, 227 F.3d 489, 497 (5th Cir. 2000).

[8] The Ninth Circuit and the Fifth Circuit actually look to consumer and market surveys in order to determine whether the deception is material. *See* S*outhland Sod Farms v. Stover Seed Co.*, 108 F.3d 1134, 1142 (9th Cir. 1997); *Eastman Chem. Co. v. Plastipure, Inc. & Certichem, Inc.*, 969 F. Supp. 2d 756, 762 (W.D. Tex. 2013).

Breach and declined to require that the defendant and plaintiff be competitors. *Fashion Boutique of Short Hills, Inc. v. Fendi USA, Inc.*, 314 F.3d 48, 56, 57-58 (2d Cir. 2002).

Typically, litigation regarding this element will revolve around non-television commercials. *See, e.g.,* S.*C. Johnson & Son, Inc. v. Clorox Co.*, 241 F.3d 232, 241 (2d Cir. 2001) (finding that the defendant's television commercial falsely depicting a competitor's cleaning product violated the Lanham Act, yet declining to even engage in analysis addressing whether the commercial constituted commercial advertising).

(i) <u>Commercial Speech Made by a Defendant who is in Competition with the Plaintiff</u>

Analysis regarding the "competition" element is typically concise and straightforward. *See, e.g.*, *Procter & Gamble Co. v. Haugen*, 222 F.3d 1262, 1274 (10th Cir. 2000) (finding the competition element satisfied when the defendant, a manufacturer and distributor of products for consumption, personal care, and healthcare use, disseminated a voicemail message that his competitor's products will begin to contain symbols referencing Satan); *but see Sodexho USA v. Hotel & Restaurant Emples. & Bartenders Union, Local 217*, 989 F. Supp. 169, 172 (D. Conn. 1997) (finding a union's misleading leaflets and letters to an institutional food services provider's customers not actionable under the Lanham Act because the defendant's actions were closer to that of a consumer advocate rather than a competing food service company, explaining, "the desire to exert economic pressure on a company, however, does not . . . make the defendants commercial competitors of the plaintiff [and analogizing,] [an] environmental advocate might encourage consumers to avoid Company X because it pollutes the environment, and patronize Company Y, which is known to have good environmental policies. Such an action is certainly intended to have economic impact on Company X. It does not place the environmental advocate in competition with Company X, however").

(ii) <u>Commercial Speech for the Purpose of Influencing Consumers to buy Defendant's Goods or Services</u>

Under this element, courts have considered whether the defendant's commercial speech was a part of promoting its own product. *Synygy, Inc. v. Scott-Levin, Inc.*, 51 F. Supp. 2d 570, 577 (E.D. Pa. 1999); *see, e.g., Mobius Management Sys. v. Fourth Dimension Software*, 880 F. Supp. 1005, 1008, 1020 (S.D.N.Y. 1994) (holding that the defendant's "letter on its face was made for the express purpose of influencing the purchase decision of [its competitor's prospective consumer]" when the defendant sent a letter to the consumer and not only compared its software product with the plaintiff's, but also asserted in the letter that the consumer would accrue an additional $5.6 million if the consumer chooses the plaintiff's software package over the defendant's); *but see Pitney Bowes, Inc. v. ITS Mailing Sys.*, 2010 U.S. Dist. LEXIS 24710, *2, *14 (E.D. Pa. 2010) (holding that a defendant's communications were "a far cry from communication "designed to influence customers to buy defendant's products"" when the defendant called the plaintiff's customer call center posing "as various clients of [the] Plaintiff in order to procure confidential information regarding Plaintiff's clients' accounts" because such communication was merely between the plaintiff and the defendant).

(iii) **The Representations Must be Disseminated Sufficiently to the Relevant Purchasing Public to Constitute Advertising or Promotion Within that Industry**

Courts have recognized that "in order to constitute advertising or promotion, statements must be publicly disseminated throughout the relevant industry, but need not be directed to the general public." *AMERICAN BROADCASTING CO. v. MALJACK PRODUCTIONS*, 34 F. Supp. 2d 665, 678 (N.D. Ill. 1998). Specifically, "the level of circulation required for 'public dissemination' will vary depending on the type of industry." *Id.*; *see also Porous Media Corp. v. Pall Corp.*, 173 F.3d 1109, 1121 (8th Cir. 1999) (explaining, "the required level of circulation and the relevant purchasing public will vary according to the specifics of the industry" in determining whether a "substantial segment" was reached). With respect to the dissemination requirement, the Second Circuit has noted:

> [T]he touchstone . . . is that the contested representations are part of an organized campaign to penetrate the relevant market. Proof of widespread dissemination within the relevant industry is a normal concomitant of meeting this requirement. Thus, businesses harmed by isolated disparaging statements do not have redress under the Lanham Act.

Fashion Boutique of Short Hills, Inc. v. Fendi USA, Inc., 314 F.3d 48, 57 (2d Cir. 2002).

For example, the Ninth Circuit in *Coastal Abstract Serv. v. First Am. Title Ins. Co.* held that "[w]here the potential purchasers in the market are relatively limited in number, even a single promotional presentation to an individual purchaser may be enough to trigger the protections of the [Lanham] Act." 173 F.3d 725, 735 (9th Cir. 1999). There, a mortgage corporation hired the plaintiff, an escrow agent, to assist it in a home loan refinancing project. *Id.* at 729. The plaintiff, in turn, engaged the defendant, a title insurance company, to help provide service on the project. *Id.* However, complications in the services arose prompting the defendant to solicit the project for itself and tell the mortgage company that (1) the plaintiff's "failure to disburse the loan amounts . . . created the delay in issuing the title policies," (2) the plaintiff was not "paying its bills," and (3) the plaintiff "was too small to handle the volume of business that" the mortgage corporation provided. *Id.* at 730. The Ninth Circuit explained that because the plaintiff had presented evidence showing that there "were only two or possibly three institutions involved in the kind of nationwide refinancing operation conducted by [the mortgage corporation,"] the plaintiff had met its burden of proof in establishing that "a representation to [the mortgage corporation] was a dissemination to a sufficient segment of the relevant purchasing public." *Id.* at 735; *but see Cargill Inc. v. Progressive Dairy Solutions, Inc.*, 2008 U.S. Dist. LEXIS 46972, *4, *10-11,*47-48, (E.D. Cal. 2008) (holding that a herd food manufacturer failed to establish that its competitor's disparaging statements "were disseminated sufficiently to the purchasing public" because the manufacturer operated throughout several states in the country, a relatively unlimited market with thousands of potential clients, but yet "has only provided statements made to two customers").

(e) **Entry of the Description or Representation into Interstate Commerce**

The Lanham Act provides for civil liability for any person that uses "in commerce" for any advertising that deceives or tends to deceive consumers. 15 U.S.C. § 1125(a)(1)(B); *see also Southland Sod Farms v. Stover Seed Co.*, 108 F.3d 1134, 1139 n.3 (9th Cir. 1997). To satisfy the commerce requirement, most circuits have held that only the descriptions or representations must be introduced into interstate commerce. *See Clorox Co. v. Proctor & Gamble Commer. Co.*, 228 F.3d 24, 33 n.6 (1st Cir. 2000); *PBM Prods., LLC v. Mead Johnson & Co.*, 639 F.3d 111, 120 (4th Cir. 2011); *American Council of Certified Podiatric Physicians & Surgeons v. American Bd. of Podiatric Surgery, Inc.*, 185 F.3d 606, 613 (6th Cir. 1999); *but see Arrow Rock Int'l, Inc. v. Dex Media Inc.*, 2006 U.S. Dist. LEXIS 44609, *10 (D. Idaho 2006) (holding that a complaint failed "to properly allege or plead the requisite interstate commerce requirement for a Lanham Act cause of action" when the complaint "specified" that the defendant's flyers, discouraging customers from purchasing the plaintiff's product, only "occurred within the District of Idaho").

The Eleventh Circuit takes a different approach, requiring a showing that "the misrepresented product or service affects interstate commerce." *Johnson & Johnson Vision Care, Inc. v. 1-800 Contacts, Inc.*, 299 F.3d 1242, 1247 (11th Cir. 2002). This requirement appears to focus on whether the product is in interstate commerce, rather than the advertisement itself. *See, e.g.*, *Star-Brite Distrib. v. Kop-Coat, Inc.*, 664 F. Supp. 2d 1246, 1254-1255 (S.D. Fla. 2009) (explaining "there is not [any] question that the misrepresented product or service affects interstate commerce [because] the advertised products are sold nationwide"). Since the *Lexmark* decision, it does not appear that the Eleventh Circuit has revisited the issue of whether the Act only applies to goods in interstate commerce or extends to those engaged in commercial activities in interstate commerce.

Similarly, the Third and the Fifth Circuits require that the advertised product be placed in interstate commerce to satisfy the Lanham Act's commerce requirement. *See Johnson & Johnson-Merck Consumer Pharms. Co. v. Rhone-Poulenc Rorer Pharms., Inc.*, 19 F.3d 125, 129 (3d Cir. 1994); *IQ Prods. Co. v. Pennzoil Prods. Co.*, 305 F.3d 368, 375 (5th Cir. 2002). For example, in *Highmark, Inc. v. Upmc Health Plan*, the Third Circuit held that although the defendant's advertisement was directed solely towards Pennsylvania residents, the commerce requirement nevertheless was satisfied because the defendant's advertised health plan services were available outside of Pennsylvania. 276 F.3d 160, 165-66 (3d Cir. 2001). There, the defendant, a health insurer, published a full page advertisement in the *Pittsburg Post-Gazette* comparing its insurance plans with the insurance plans that the plaintiff offered. *Id.* at 164. The ad in question allegedly contained several deceptive misstatements, including, "[a] message to the employers of Allegheny County," . . ."[i]f you were diagnosed with a serious illness tomorrow, which health plan would you rather have?" *Id.* The district court held in part that the defendant's advertisement satisfied the commerce requirement because "the Pittsburgh Post-Gazette is distributed interstate and, therefore, the Ad appeared outside Pennsylvania." *Id.* at 165. The Third Circuit affirmed the district court's holding, however, on other grounds. The court stated that the Lanham Act's commerce requirement was satisfied not because the ads themselves appeared in interstate commerce, but instead because (1) the plaintiff's health care plan "covers subscribers" dependents residing outside of Pennsylvania," (2) the plaintiff's healthcare plan "offers emergency care outside of the state and country," and (3) the subscribers of the plaintiff's healthcare plan

"have access to out-of-state hospitals such as Sloan-Kettering, the Cleveland Clinic, Massachusetts General Hospitals, and the Mayo Clinic," *Id.* at 166; *see also Daniels Sharpsmart, Inc. v. Tyco Int'l (US)*, Inc., 2006 U.S. Dist. LEXIS 100158, *17 (E.D. Tex. 2006) (finding that a container manufacturer's advertisement regarding the volume capacity of its competitor's container was actionable under the Lanham Act because the competitor's container was (1) "being sold in interstate commerce", (2) sold internationally, and (3) occupied "approximately two percent of the United States market").

(f) <u>The Likely or Actual Injury to the Plaintiff as a Result of the Description or Representation</u>

In order to satisfy the injury element, courts require that the plaintiff show that he has "been or is likely to be injured as a result of the false statement, either by direct diversion of sales from itself to defendant or by a lessening of the goodwill associated with its products." *Southland Sod Farms v. Stover Seed Co.*, 108 F.3d 1134, 1139 (9th Cir. 1997). Courts have recognized that the plaintiff's burden for this element depends on what type of relief of sought. *See Porous Media Corp. v. Pall Corp.*, 110 F.3d 1329, 1335 (8th Cir. 1997) (recognizing that "cases involving injunctive relief and those seeking monetary damages under the Lanham Act have different standards of proof"); *eMove Inc. v. SMD Software Inc.*, 2012 U.S. Dist. LEXIS 55625, *16 (D. Ariz. 2012) (explaining, "[t]he proof of injury necessary to sustain a Lanham Act claim depends on the relief sought by the plaintiff").

(i) <u>Injunctive Relief</u>

The Lanham Act provides for injunctive relief. *See* 15 U.S.C. § 1116. To obtain injunctive relief in a commercial disparagement case, courts have held that the plaintiff only needs to prove a threatened injury rather than an actual injury. *See PBM Products, LLC v. Mead Johnson & Co.*, 639 F.3d 111, 126-27 (4th Cir. 2011) (explaining a plaintiff seeking an injunction against false advertisement "need not to even point to an actual loss or diversion of sales;" instead, he just must demonstrate in some manner that provides a reasonable basis for believing that he is likely to be injured as a result of the advertising). Accordingly, the correct standard for all false advertising cases, including commercial disparagement claims, is:

> whether it is likely that [the defendant's] advertising has caused or will cause a loss of [plaintiff's] sales, not whether [the plaintiff] has come forward with specific evidence that [the defendant's] ads actually resulted in some definite loss of sales.

Johnson & Johnson v. Carter-Wallace, Inc., 631 F.2d 186, 190 (2d Cir. 1980).

(ii) <u>Presumption of Injury</u>

Courts have recognized that when a plaintiff is seeking injunctive relief in a false advertising case, there will be a presumption of injury and harm in cases where the defendant's advertisement has literally made a false comparative claim. *See, e.g.*, *Time Warner Cable, Inc. v. DIRECTV, Inc.*, 497 F.3d 144, 161-162 (2d Cir. 2007); *Osmose, Inc. v. Viance*, LLC, 612 F.3d 1298, 1320 (11th Cir. 2010). Accordingly, based on this definition of "comparative advertisement," this presumption of injury and harm would seem to apply to commercial

disparagement claims because such claims involve advertisements specifically referencing or comparing the plaintiff-competitor's product or business.

Applying the above principles, the Second Circuit in *Time Warner Cable, Inc. v. DIRECTV, Inc.*, held that the elements of causation and injury were presumed where the plaintiff demonstrated that the defendant's advertisement was literally false in referencing the plaintiff's product. 497 F.3d 144, 161-62 (2d Cir. 2007). There, the advertisement of the defendant, a satellite company, disparaged the picture quality of its competitor's product in exclaiming, "settling for cable would be illogical." *Id.* at 162. The Second Circuit granted the plaintiff's motion for preliminary injunction and explained that proof of likely injury was not necessary because, in a case where the defendant's literal false advertisement has explicitly disparaged the plaintiff's product, there were subsequently no concerns regarding speculative injuries. *Id.* The Second Circuit reasoned the plaintiff's injuries were not speculative in this case because the defendant's literal false advertisement "necessarily diminished[d] [the plaintiff's] product's value in the minds of the consumer." *Id.*; *see also Star-Brite Distrib. v. Kop-Coat, Inc.*, 664 F. Supp. 2d 1246, 1255 (S.D. Fla. 2009).

(iii) <u>Non-Presumption of Injury</u>

In cases involving a "non-presumption of injury," injunctive relief requires a showing that the defendant's representations about the plaintiff's products had a tendency to deceive consumers. *Am. Council of Certified Podiatric Physicians & Surgeons v. Am. Bd. of Podiatric Surgery, Inc.*, 185 F.3d 606, 618 (6th Cir. 1999); *see also United Indus. Corp. v. Clorox Co.*, 140 F.3d 1175, 1183 (8th Cir. 1998) (explaining, "when injunctive relief is sought under the Lanham Act, the finding of a tendency to deceive satisfies the requisite showing of irreparable harm"). For example, in *PBM Products, LLC v. Mead Johnson & Co.*, the Fourth Circuit granted the plaintiff's motion for a permanent injunction against the defendant's advertisement when the plaintiff produced evidence that the defendant's advertisement misled consumers. 639 F.3d 111, 127 (4th Cir. 2011). There, the defendant, a manufacturer of baby formula, distributed out mailers to consumers across the country, which included brochures disparaging the plaintiff's baby formula. *Id.* at 117. Those mailers, (1) stated (a) "[i]t may be tempting to try [the] less expensive [plaintiff's product], but only [the defendant's product] is clinically proven to improve brain and eye development," and (b) "All infant formulas are not the same . . . [the defendant's formula] offer expert recommended levels of DHA and ARA," (2) "displayed a checklist stating that [the defendant's baby formula] is "[p]roven to result in IQ scores similar to breastfed babies" and "[p]roven to enhance visual development," while indicating that the ["plaintiff's" formula] does not"", and (3) "provided a graphic of a duck showing a comparison of visual sharpness where one half of the graphic, captioned "with [the defendant's formula"] was clear and the other half of the graphic, captioned "without [the defendant's product," was blurry." *Id.* In response, the plaintiff conducted surveys to illustrate that the defendant's advertisement contained two implied messages: (1) "[the defendant's formula] contains two important fatty acids, DHA and ARA, and [the plaintiff's] store brand formulas do not;" and (2) "[the defendant's formula] has been clinically tested and shown to be superior to [the plaintiff's] formula with respect to brain and eye development in infants." *Id.* at 118. The Fourth Circuit afforded credibility to the plaintiff's survey and determined that such extrinsic evidence allowed the jury to reasonably conclude that the defendant's mailers deceived and discouraged consumers from even considering the plaintiff' baby formula. *Id.* at 127; *but see United Indus. Corp. v. Clorox Co.*, 140 F.3d 1175, 1183 (8th Cir.

1998) (denying the plaintiff's request for injunctive relief in an implied falsehood case where the plaintiff's view of the defendant's message and its impact was "unsupported . . . by expert testimony, surveys, or consumer reaction evidence of any kind").

(iv) Damages

The Lanham Act also provides for monetary relief. *See* 15 U.S.C. § 1117. The Second Circuit has provided the standard for the recovery of monetary damages in false advertising cases. The standard provides:

> It is well settled that in order for a Lanham Act plaintiff to receive an award of damages the plaintiff must prove either actual consumer confusion or deception resulting from the violation, *or* that *the defendant's actions were intentionally deceptive* thus giving rise to a rebuttable presumption of consumer confusion.

Merck Eprova AG v. Gnosis S.p.A., 760 F.3d 247, 256 (2d Cir. 2014).

Where the plaintiff seeks to recover monetary damages for the defendant's commercial disparagement, "the plaintiff must prove both actual damages and a causal link between defendant's violations and those damages." *Rhone-Poulenc Rorer Pharm., Inc. v. Marion Merrell Dow, Inc.*, 93 F.3d 511, 515 (8th Cir. 1996); *SMD Software, Inc. v. EMove, Inc.*, 945 F. Supp. 2d 628, 638 (E.D.N.C. 2013) (holding same). However, as 15 U.S.C. § 1117 explicitly states, monetary damages can be recovered only once a violation of 15 U.S.C. § 1125(a) has first been established. Accordingly, with respect to the injury element in false advertising cases, courts have held that proving causation and proving monetary damages are two distinct matters. *See Pharmanetics, Inc. v. Aventis Pharm., Inc.*, 182 F. App'x 267, 273 (4th Cir. 2006) (stating, "the quantum of damages, as distinguished from entitlement, must be demonstrated with specificity"); *see also Porous Media Corp. v. Pall Corp.,* 110 F.3d 1329, 1336 (8th Cir.1997) (noting that a Lanham Act plaintiff, even when presumptions of harm apply, "still b[ears] the burden of proving an evidentiary basis to justify any monetary recovery"). Therefore, even if a commercial disparagement plaintiff may not have to prove harm through, for example, consumer surveys, plaintiff nevertheless still is required to prove the harm's financial extent. *Pharmanetics, Inc.*, 182 F. App'x at 273. Simply put, a plaintiff must provide evidence that the illegal action actually caused the amount of damages the plaintiff seeks.

(v) Non-Presumption of Injury: Proving Causation for Actual Damages

Typically, a plaintiff will seek to recover actual damages incurred by the defendant's false advertisement. In these cases, the plaintiff seeks the recovery of damages it incurred in the marketplace, i.e., lost sales, lost profits, and loss of goodwill. *Balance Dynamics Corp. v. Schmitt Indus., Inc.*, 204 F.3d 683, 690 (6th Cir. 2000). In proving "actual injury," courts have held that a showing of "actual damages" is a prerequisite to recovering monetary damages. *Id.* at 691. Actual damages are demonstrated through direct evidence, such as testimony from buying members of the public, or through circumstantial evidence, such as consumer surveys or consumer reaction tests. *Sunlight Saunas, Inc. v. Sundance Sauna, Inc.*, 427 F. Supp. 2d 1032, 1060 (D. Kan. 2006).

For instance, in *Thermal Design, Inc. v. Guardian Bldg. Products, Inc.*, the court held that a plaintiff was not entitled to recover monetary damages in a literal falsehood case when it "failed to produce any evidence that it was damaged by actual consumer reliance on the misleading statements." No. 08-C-828, 2012 WL 5835797, at *1-2 (E.D. Wis. 2012). There, the plaintiff argued that because it had proven that the defendant's advertisement was literally false, it was entitled to the presumption of deception. *Id.* at 1. The court agreed with this presumption, but explained that a plaintiff seeking monetary damages "must show more than a mere presumption of actual consumer [deception] based on a finding of literal falsity." *Id.* The court reasoned that even though a plaintiff need not produce evidence of deception given the advertisement's literal falsehood, a plaintiff nevertheless must prove that it suffered injury at the hands of the defendant's advertisement, and link the actual deception with the harm its business incurred. *Id.* The court further noted that the concept regarding the causal connection between the damages and the advertisement and the concept regarding the deception are separate yet also related:

> Consumer [deception] can be used to demonstrate [the causal connection between the injury and the damages], and [the causal connection between the injury and the damages] assumes the existence of consumer [deception.] If the plaintiff offers evidence that consumers were deceived by a false representation which influenced their purchasing decisions, this would show that the plaintiff was damaged by the advertisement. But there are other ways to prove an entitlement to damages besides offering evidence of consumer [deception]. Such reliance may be shown not only by evidence of actual diversion of sales, but also by such proof of actual customer deception as surveys, or testimony of a dealer, distributor, or [a] customer on the actual deception issue [,] . . . eroding revenues, corresponding increase in competitors' revenues, and loss of sales force supports an inference that the shift in the companies' market shares was due to defendants' misconduct.

Id.

(vi) <u>Presumption of Injury</u>

Unlike with injunctive relief, literal falsity alone does not create a presumption of injury. Something more is needed to prove entitlement to monetary damages. *See, e.g., Balance Dynamics Corp. v. Schmitt Indus., Inc.*, 204 F.3d 683, 693 (6th Cir. 2000); *see also Porous Media Corp. v. Pall Corp.*, 110 F.3d 1329, 1335 (8th Cir. 1997) (explaining that in contrast to injunctive relief, courts require a heightened level of proof of injury in order to recover money damages). However, in certain circumstances, where a plaintiff has met its burden in proving **deliberate deception** in the context where **its competitor** has **mentioned the plaintiff's product** by name in an advertisement, courts have generally held that it is appropriate to utilize the **presumption of injury** regarding monetary damages. *See Merck Eprova AG v. Gnosis S.p.A.*, 760 F.3d 247, 260-61 (2d Cir. 2014); *Porous Media Corp. v. Pall Corp.*, 110 F.3d 1329, 1336-37 (8th Cir. 1997) (holding that because the defendant violated the Lanham Act in bad faith, the plaintiff was not required to provide evidence indicating actual damages in order to prove entitlement to damages); *see e.g., Southland Sod Farms v. Stover Seed Co.*, 108 F.3d 1134, 1146 (9th Cir. 1997) (explaining, "because a reasonable jury could conclude, based on the evidence submitted by Plaintiffs, that [the] Defendants' comparative advertisement claims were deliberately false within the meaning of § 43(a), Plaintiffs may be entitled to a presumption of actual consumer deception and **reliance**,

and would therefore be entitled to appropriate monetary relief unless Defendants could rebut the presumption") (emphasis added).

C. Defenses to Commercial Disparagement Claims Under Federal Law

1. Puffery

A third category of statements, aside from literal or implied falsehoods, are those categorized as puffery. *United Indus. Corp. v. Clorox Co.*, 140 F.3d 1175, 1180 (8th Cir. 1998). However, statements found to be puffery are not actionable under the Lanham Act. *Southland Sod Farms v. Stover Seed Co.*, 108 F.3d 1134, 1145 (9th Cir. 1997). Courts generally have recognized two forms of puffery: (1) a general claim of superiority that is "so vague that it can be understood as nothing more than a mere expression of opinion," and (2) an "exaggerated, blustering, and boasting statement upon which no reasonable buyer would be justified in relying." *Time Warner Cable, Inc. v. DIRECTV, Inc.*, 497 F.3d 144, 160 (2d Cir. 2007). These claims are so subjective that neither can be proven true nor false. *Id.* at 159.

Puffery is also a defense in commercial disparagement cases. *See Trade Libel: Theory and Practice Under the Common Law, the Lanham Act, and the First Amendment*, 89 Trademark Rep. 826, 856-57 (1999) (stating, "that non-factual disparaging claims are similarly immune from the new cause of action for trade libel in amended Section 43(a)"). For example, in *U.S. Healthcare, Inc. v. Blue Cross*, the defendant ran commercials featuring actors stating their preference for the defendant's health care services over the slogan, "Better than HMO. So good, it's Blue Cross and Blue Shield." 898 F.2d 914, 918 (3d Cir. 1990). There, the defendant was Blue Cross and Blue Shield, a health care insurer. HMO, the plaintiff, was a competing health insurer as well. *Id.* at 917. The Third Circuit, however, dismissed the plaintiff's commercial disparagement claim and reasoned that the defendant's advertisement was "the most innocuous kind of puffing." *Id.* at 926.

2. First Amendment Defense

The Supreme Court has made it clear that commercial speech is not afforded the same First Amendment protection as noncommercial speech. *See Dun & Bradstreet v. Greenmoss Builders*, 472 U.S. 749, 758 n.5 (U.S. 1985) (stating that "in the area of protected speech, the most prominent example of reduced protection for certain kinds of speech concerns commercial speech. Such speech, we have noted, occupies a "subordinate position in the scale of First Amendment values""). Moreover, the Court has noted that "false or misleading commercial speech should receive no protection, because commercial speech merely gives information to consumers about a producer's goods, and any false information either has no value or is harmful." *P&G v. Amway Corp.*, 242 F.3d 539, 549 (5th Cir. 2001) (referencing *Cent. Hudson Gas & Elec. Corp. v. Public Serv. Comm'n*, 447 U.S. 557, 563 (U.S. 1980) (holding "there can be no constitutional objection to the suppression of commercial messages that do not accurately inform the public about lawful activity. The government may ban forms of communication more likely to deceive the public than to inform it")).

Accordingly, applying the above principles, the legislative history, in revising the Lanham Act to make claims of commercial disparagement actionable, clearly illustrates that the

"reach of Section 43(a) specifically *extends only to false and misleading speech that is encompassed within the commercial speech doctrine* developed by the United States Supreme Court." *Gordon & Breach Sci. Publrs. S.A. v. Am. Inst. of Physics*, 859 F. Supp. 1521, 1533-34 (S.D. N.Y. 1994). In other words, while certain forms of disparagement may be protected by the First Amendment, disparaging **commercial speech** does not enjoy First Amendment protection. *See Wojnarowicz v. Am. Family Ass'n*, 745 F. Supp. 130, 142 (S.D.N.Y. 1990) (recognizing that "every instance of the Lanham Act's far-reaching application has been to practices commercial in nature, involving imitation, misrepresentation, or misappropriation in connection with the sale of goods or services by the defendant"). Accordingly, because commercial advertising under the Lanham Act does not fall under the umbrella of the First Amendment, a defendant who is liable for commercial disparagement cannot thereby invoke the First Amendment as a defense. *See Procter & Gamble Co. v. Haugen*, 222 F.3d 1262, 1276 (10th Cir. 2000).

D. Special Considerations in Internet Cases

In today's world, the internet is prime territory for commercial disparagement. This section of the article discusses special considerations occurring in internet cases.

1. Disparaging Domain Names

In *Sunlight Saunas, Inc.*, the court addressed commercial disparagement in the context of a disparaging domain name. 427 F. Supp. 2d 1032 (D. Kan. 2006). There, the plaintiff, Sunlight Saunas, Inc., and the defendant, Sundance Sauna's, Inc., were both competing manufacturers in the sauna industry. *Id.* at 1038. The plaintiff promoted its products through the website, "www.sunlightsaunas.com." *Id.* at 1039. The defendant later launched the website, "www.sunlightsaunas-exposed.com," which contained the following statements: (1) the plaintiff's saunas contain "heaters . . . made from steel rods and aluminum casing with pink paint Aluminum [that] can be incredibly toxic inside the body," (2) the plaintiff's saunas have "not been certified to the minimum standards the USA has established for safety," (3) the plaintiff lied about offering a lifetime warranty on its saunas, (4) the plaintiff's saunas are not unique because they do not even manufacture their own products, and (5) the plaintiff's saunas contain veneer roofs in contradiction of their slogan that their saunas were 100% veneer free. *Id.* at 1045-47.

A central question before the court was whether the domain name "www.sunlightsaunas-exposed.com" and the website's statements constituted commercial advertising or promotion. *Id.* at 1056. The court concluded that both satisfied the commercial advertising element, reasoning that (1) the defendant was a direct competitor of the plaintiff, (2) the defendant had no "apparent reason to disparage the plaintiff's product except to promote [its] own," and (3), the website was intended to have broad dissemination and to divert potential customers from the plaintiff. *Id.* at 1057.

Cannella v. Brennan also involved a disparaging domain name. 2014 U.S. Dist. LEXIS 107944, *1 (E.D. Pa. 2014). There, the plaintiff, First Senior Financial Group, LLC, and the defendant, Granite Financial, were competing insurance agencies. *Id.* at 1-2. Philip Cannella was an employee of the plaintiff who worked "directly with customers to provide financial information and promote[d] First Senior and its insurance products." *Id.* at 2. The defendant created the websites "www.TruthaboutCannella.com" and "www.TruthaboutCannella.net." *Id.* at

2-3. The defendant posted the following negative comments and reviews about the plaintiff's business on the website:

> (1) "They take every shortcut in financial planning they can certainly, why wouldn't they take shortcuts for cosmetic vain purposes too? Speaks to character ... or lack thereof."
>
> (2) "These are the days Cannella is most dangerous. His game is fear peddling. He motivates people to buy from him through creating and fostering fear."
>
> (3) "999am [sic] is willingly embracing a known criminal as an advertiser who continues to abuse elderly victims."
>
> (4) "I wouldn't put it past old Slippery Phil, Captain Crash Proof if he showed the agents one app and filed another to get them off of the application and so he KNOWS he doesn't to pay them."

Id. at 17. The court reasoned that these comments satisfied the interstate commerce element because the defendant posted such comments on a website, thereby making them accessible on the internet. *Id.* at 20. The court accordingly concluded that these misleading statements could have an impact on those outside the state. *Id.*

The court also found that the website's disparaging remarks constituted commercial advertising as well because (1) the "postings on the website constitute commercial speech done for the purpose of influencing consumers to buy the Defendants' goods or services," (2) the website was created to disparage the Plaintiffs and their business, (3) the "defendants' goal in posting on the website was to encourage Plaintiffs' customers and potential customers to do business with Defendants instead of the Plaintiffs," evidenced by the disparaging remarks, and (4) the fact the website was the first link to appear on a Google search for the plaintiff indicated that the website was accessible worldwide. *Id.* at 22-23.

Other cases alleging commercial disparagement by use of a domain name include *Goodman v. Doe*, 2014 U.S. Dist. LEXIS 42130, *3 (E.D.N.C. 2014) (Website "localdirtbags.com" was not commercial advertising and, therefore, not actionable as disparagement because (1) the website owner did not have an economic interest in people visiting the website and (2) the articles on the website did not propose a commercial transaction, but rather were consumer reviews); *Corizon, Inc. v. Wexford Health Sources, Inc.*, 2013 U.S. Dist. Lexis 102615 (E.D Mo. 2013) (Statements about healthcare services company on competitor's website were actionable as disparaging); and *Doctor's Assocs. V. QIP Holder LLC*, 2010 U.S. Dist. Lexis 14687 (D. Conn. 2010) (Quizno's website "meatnotmeat.com" disparaged Subway with statements like "Light Weight," "Hunger Pain Inducing," "Stale," and "Where's the meat?").

2. <u>Blogging/Posts</u>

In *NTP Marble, Inc. v. AAA Hellenic Marble, Inc.*, 2012 U.S. Dist. LEXIS 24671, *3 (E.D. Pa. 2012), the court addressed a commercial disparagement claim surrounding the posting of negative reviews. There, the plaintiff and defendant were competing corporations in the marble and granite installation business. *Id.* at 2-3. The defendant engaged in a smear campaign against

the plaintiff in which it posted numerous negative reviews about the plaintiff's business online at Citysearch, Insiderpages, Yellowbot, and Google. *Id.* at 3. These online reviews criticized the plaintiff's customer service, on-site performance, and employment practices. *Id.* at 3-4. The court held that these negative reviews coming from the defendant's IP address constituted commercial advertising, despite never even mentioning or referencing the defendant, because they (1) were commercial speech, (2) specifically warned customers about the plaintiff's service and goods, (3) were motivated by economic interests, and (4) were disseminated on the internet. *Id.* at 25-26.

Likewise in *1524948 Alberta Ltd. v. Lee*, 2011 U.S. Dist. LEXIS 77365, *1 (N.D. Ga. 2011), the court addressed a commercial disparagement claim regarding online negative reviews. There, the plaintiff operated a "penny auction website." *Id.* at 2. "Penny auctions are online auctions in which consumers must purchase bids, usually for $0.50 or $1 each." *Id.* The defendant allegedly operated a website that sold advertising space to other penny auction websites and third party affiliates. *Id.* at 3. The plaintiff alleged that the defendant, disguised as various customers, posted on its website that contained material which (1) accused the plaintiff of engaging in "bot bidding," and (2) stated the plaintiff's website consists of "THIEVES" and that the "customers never receive products even if they win an auction." *Id.* at 4-5. The court found that these online reviews were actionable in part under the Lanham Act because the plaintiff had alleged that (1) the defendant was trying to attract customers to penny auction websites in competition with the plaintiff, and (2) the defendant's website, which targeted penny auction customers, disseminated the negative reviews to anyone who accessed the website. *Id.* at 14-15.

The court in *Trekeight, LLC v. Symantec Corp.*, 2006 U.S. Dist. LEXIS 100609, *2 (S.D. Cal. 2006) also addressed a similar commercial disparagement allegation regarding internet posts. There, the plaintiff was a computer software company that offered among its products a program known as "SpywareNuker," which protected computers from spyware and adware. *Id.* at 2-3. The defendant, a software company, also offered anti-spyware products as well. *Id.* at 3. In response to a customer, the defendant posted on its website that the plaintiff's "SpywareNuker" program was adware and had potential to cause "medium damage" to a user's computer. *Id.* at 4-5.

The issue before the court was whether the defendant's internet post constituted commercial speech made for the purpose of influencing customers to purchase its products or services. *Id.* at 22. The defendant contended that its post did not constitute commercial speech because the purpose of its response was to assist consumers in managing the content of their computer's hard drive. *Id.* Because there was a question of material fact regarding the defendant's intent of the post on its website, the court accordingly denied the parties' motions for summary judgment with respect to the plaintiff's commercial disparagement claim. *Id.* at 24. The court, however, noted that the defendant's internet post caused his statements to enter into interstate commerce, thereby satisfying the interstate commerce requirement because there had been "35,859 visits to the SpywareNuker security response web page." *Id.* at 26.

Another case regarding commercial disparagement in the context of internet blogging is *Boykin Anchor Co. v. At&T Corp.*, 825 F. Supp. 2d 706 (E.D. N.C. 2011). There, the defendant, AT&T, was the leader of the telecommunications industry and used seismic anchors. *Id.* at 708. The plaintiff was a corporation that manufactured seismic anchors for the telecommunications industry. *Id.* Hilti, Inc. was the plaintiff's sole competitor for AT&T related

business regarding anchors. In response to a consumer's question as to which anchor should be used, an AT&T employee recommended in internet postings that the plaintiff's "anchors should not be used because of performance questions." *Id.* at 708-11.

The court dismissed the plaintiff's false advertising claim because the defendant's internet postings did not qualify as commercial advertising, reasoning that (1) the posts were not commercial speech because they neither proposed a commercial transaction nor were related to the economic interest of AT&T; (2) AT&T was not in competition with the plaintiff because it was merely a consumer of the plaintiff's products; and (3) there was no indication that the internet posts were designed to influence consumers to buy products or services provided by AT&T. *Id.* at 711.

eMove Inc. v. SMD Software Inc., 2012 U.S. Dist. LEXIS 55625, *37 (D. Ariz. 2012), also involved a commercial disparagement allegation regarding an internet post. There, the plaintiff, eMove, Inc., was a subsidiary of U-Haul International, Inc. The defendant, which sold the software, SiteLink Web Edition, competed with the plaintiff for business "by selling software products to the owners and managers of self-storage facilities. *Id.* at 2-3. During the midst of the competition between the parties, the defendant created the following post for an internet message board:

> In May 2008, we will release a free listing service and search engine optimization (SEO) for our Web Edition customers. We will push Web Edition customers' web sites to the top of searches using Google and other engines.
>
> Compare that to U-HAUL'S referrals. Some UHAUL dealers, but not most, claim there are referrals from other UHAUL dealers. The 2 features above are available in SiteLink out of the box. No other software offers such broad-based value, ready to use, at no more cost than one simple web site setup.
>
> Showing at or near the top of ANY search exposes owners' web sites to more clients than the narrow UHAUL system. Join UHAUL just the same, still get their referrals, but why limit exposure to **a closed network** vs. the entire web by not using SiteLink Web Edition?

Id. at 37-38 (emphasis added).

The plaintiff argued that the comments in the internet post conveyed the message that the plaintiff's product was a closed system, i.e., a website not open to internet search engines. *Id.*at 39. The court rejected the plaintiff's commercial disparagement claim because the plaintiff failed to sufficiently prove that the defendant's comments in the internet post were either literally false or misleading. *Id.* at 41. With respect to the literal falsity claim, the court first reasoned that because the final sentence in the post stated, "still gets their referrals" in reference to the plaintiff's system, nothing in the post suggested that the defendant was "asserting that eMove's affiliate sites [were] not accessible through Internet search engines." *Id.* at 40. The court further took note that it would be very "unlikely that the defendants would suggest that eMove.com itself is closed, because this assertion can be tested and proven false so easily." *Id.* Moreover, the court found that the plaintiff's implied falsehood claim was also unpersuasive because the plaintiff failed to

produce extrinsic evidence (market research or consumer surveys) of the way the statement was perceived by customers. *Id.*

3. Miscellaneous Internet Usage Regarding Commercial Disparagement

(a) Social Media and Networking

Commercial disparagement claims can also implicate social media and social networking mediums. In *AvePoint, Inc. v. Power Tools, Inc.*, 981 F. Supp. 2d 496 (W.D. Va. 2013), the plaintiff, an American corporation, was a "leading provider of infrastructure management and governance software platforms for Microsoft SharePoint products and technologies." *Id.* at 502-503. The defendant, also an American corporation, was one of the plaintiff's primary competitors. *Id.* The plaintiff alleged that the defendant engaged in a campaign of making commercially disparaging claims regarding the plaintiff's products and services via Twitter. *Id.* Specifically, the plaintiff alleged that the defendant "used Twitter to falsely brand the [plaintiff] as a Chinese company and to falsely designate China as the source and origin of [the plaintiff's] products and services." *Id.* at 520. As evidence, the plaintiff pointed to the following tweets made by the defendant:

> (1) "@Axceler #ControlPoint #MADEINTHEUSA, The #SharePoint #RedDragon is #MADEINCHINA Long live #ControlPoint !!!! #ArmyStrong #AUSA2012."
>
> (2) "No better way to end a Thursday than a HILARIOUS e-mail from the competition . . . #desperation #SinkingREDShip #MadeinCHINA #LOSING!"
>
> (3) "Ouch . . . Another #Federal Deployment Finds Out Where the Competition is Developed. #SharePoint #RedDragon."

Id.

The court found that the defendant's Twitter posts constituted commercial advertising. *Id.* at 521. The court first explained that "Twitter is a commonly-used means of advertising in the software industry, and that the messages were published and republished to hundreds of customers, potential customers, and other members of the Microsoft SharePoint community." *Id.* at 520. Second, the court noted that the defendant chose to use certain hash tags, such as "#AUSA2012, to link the messages to the United States Army Twitter community and other federal government customers of SharePoint products and/or services." *Id.* Accordingly, the court concluded that the defendant's twitter messages constituted commercial speech and were disseminated to the relevant purchasing public. *Id.*

(b) Email

Email messages also can sometimes be the basis of a commercial disparagement claim. *See ACTV, Inc. v. Walt Disney Co.*, 2002 U.S. Dist. LEXIS 8087, *1 (S.D.N.Y. 2002). There, the plaintiff, ACTV, developed a product called HyperTV, which linked Internet and television services. *Id.* Shortly after, TBS contracted for plaintiffs "to provide a HyperTV connection to TBS." *Id.* At the time, the defendant also developed a similar service called "Enhanced TV" which also linked Internet and television services. *Id.* After the defendant gave

a presentation promoting its new product, TBS sent the defendant an email (1) describing its success using the plaintiff's product, and (2) asking for a portion of the defendant's presentation. *Id.* at 2. In reply, the defendant emailed:

> Thanks for the comments and glad to hear your experiment was a success. I shared the data and survey slides with the trade at CTAM because it is important for the industry to see where and how convergence is being used and viewed by the consumer. We have spent a year developing technologies and programming concepts in this medium and we are continuing to lead the pack in this field. **As a matter of fact, ACTV completely copied our technologies and approach** and took the tools to market. Though I shared the demo and data in my presentation, all of this information is proprietary and not for distribution. Sorry I can't help you out, but maybe in your deal with ACTV, they ought to provide you with all of the data, trends, user info., etc.

Id. at 2-3 (emphasis added).

The plaintiff alleged that the defendant's statements of "ACTV completely copied our technologies and approach" constituted commercial disparagement in violation of the Lanham Act. *Id.* at 3. But the court dismissed the plaintiff's claims because the defendant's email did not constitute commercial advertising. *Id.* at 5. In particular, the court explained that it was beyond reason that a single private correspondence could qualify as advertising because if so, than any disparaging comment in the context of a commercial transaction would be actionable under the Lanham Act. *Id.*

(c) <u>Internet Links</u>

Commercial disparagement claims also can arise from internet links. *See Morningware, Inc. v. Hearthware Home Prods.*, 673 F. Supp. 2d 630 (N.D. Ill. 2009). There, the plaintiff, Morningware, and the defendant, Hearthware, were competing sellers of counter-top electric ovens. *Id.* at 632. The defendant promoted its products through its website www.mynuwaveoven.com. *Id.* Using a software program, the defendant manipulated Google so that when "an internet user enter[ed] the term "Morningware" as a search term in Google, Hearthware's advertisement link appear[ed] before a link to Morningware's website. The content of the link to Hearthware's website, www.mynuwaveoven.com, state[d], "The Real NuWave (R) Oven Pro Why Buy an Imitation? 90 Day Gty."" *Id.* at 633.

The plaintiff alleged that "the topmost placement of Hearthware's advertisement on the search results page coupled with the "Why Buy an Imitation?" statement constituted commercial disparagement because (1) it was false claim of product superiority over the plaintiff's products, and (2) it misled consumers into "believing that [the plaintiff's] products are inferior to Hearthware's because they are "Imitations," and thus fakes, of Hearthware's products, which they are not." *Id.* The court denied the defendant's motion to dismiss in part because it was plausible that the defendant's statement was made in the context of commercial advertising. *Id.* at 638-39. In particular, the court reasoned that because the defendant's advertisement only appeared after a Google search of the plaintiff's name, it was plausible to believe that the defendant's statement was intended to divert customers from the plaintiff's website to the defendant's website. *Id.* at 638-39.

(d) <u>Online Advertisement</u>

It is also quite common for commercial disparagement claims to arise regarding typical internet advertisements. For example, in *Time Warner Cable, Inc. v. DIRECTV, Inc.*, 497 F.3d 144 (2d Cir. 2007), the plaintiff and defendant were competitors in the multichannel video service industry. To promote its products, the defendant engaged in a cyberspace campaign placing banner and demonstrative advertisements on various websites. *Id.* at 150. The two internet advertisements at issue in the case were as follows:

> [The Defendant's banner ads] open by showing an image that is so highly pixelated that it is impossible to discern what is being depicted. On top of this indistinct image is superimposed the slogan, "SOURCE MATTERS." After about a second, a vertical line splits the screen into two parts, one labeled "OTHER TV" and the other "DIRECTV." On the OTHER TV side of the line, the picture is extremely pixelated and distorted, like the opening image. By contrast, the picture on the DIRECTV side is exceptionally sharp and clear. The DIRECTV screen reveals that what we have been looking at all along is an image of New York Giants quarterback Eli Manning; in another ad, it is a picture of two women snorkeling in tropical waters. The advertisements then invite browsers to **"FIND OUT WHY DIRECTV'S picture beats cable"** and to "LEARN MORE" about a special offer.
>
> The website demonstrative [ad] uses the split-screen technique to compare the picture quality of "DIRECTV" to that of "BASIC CABLE" . . . The DIRECTV side of the screen depicts, in high resolution, an image of football player Kevin Dyson making a touchdown at the Super Bowl. **The portion of the image on the BASIC CABLE side is noticeably pixelated and blurry**. This visual display is accompanied by the following text: "**If you're hooking up your high-definition TV to basic cable, you're not getting the best picture on every channel**. For unparalleled clarity, you need DIRECTV HD. You'll enjoy 100% digital picture and sound on every channel and also get the most sports in HD-including all your favorite football games in high definition with NFL SUNDAY TICKET."

Id. at 150-51 (emphasis added).

The plaintiff alleged that the defendant's internet advertisements posed a real danger to consumer reliance. *Id.* at 159. The Second Circuit, however, dismissed the plaintiff's claims because the internet advertisements were mere puffery. *Id.* at 160-61. The Second Circuit explained that the internet advertisements' depictions of cable were not just inaccurate; "they [were] not even remotely realistic." *Id.* at 161. The Second Circuit further reasoned, "it is difficult to imagine that any consumer, whatever the level of sophistication, would actually be fooled by the Internet Advertisements into thinking that cable's picture quality is so poor that the image is "nearly entirely obscured." . . . even a person not acquainted with cable would realize [the plaintiff] could not realistically supply an unwatchable blurry image and survive in the marketplace." *Id.* Accordingly, the court concluded that the comparison between the plaintiff's and defendant's picture quality was so "obviously hyperbolic that no reasonable buyer would be justified in relying on it in navigating the marketplace." *Id.*

II. ALTERNATIVE AND SUPPLEMENTAL REMEDIES TO THE TORT OF COMMERCIAL DISPARAGEMENT

A. Defamation Remedies.

Commercial disparagement often is referred to as "trade libel," "slander of goods" or "disparagement of the quality of property"; *Bose Corp. v. Consumers Union of United States, Inc.,* 466 U.S. 485, 488, 104 S.Ct. 1949, 80 L.Ed.2d 502 (1984). It is widely considered one version of the tort of tortious interference with business. Another version is defamation: the tort action for libel or slander.

Commercial disparagement protects a **property** interest and is often viewed as the business version of libel and slander. Defamation actions often are compared to disparagement, because both torts share many of the same elements and privileges. However, defamation actions protect **reputation** rather than property interests. Restatement Second of Torts § 623A Comment g (1976).

The two actions are distinct in several ways. In defamation claims, false publications generally have been presumed untruthful under the common law and intent is typically irrelevant. Slander *per se* and libel plaintiffs historically have been entitled to recover damages without proof of special harm. *Compare* Restatement Second of Torts*, id.* § 558 with *id.* §§ 629-630. By contrast, disparagement claimants historically are required to prove falsity, must show an intent to injure, and are required to prove actual damages for any recovery. *Id.* All defamation claims involve intentionally false statements made with the intent to cause harm or damage reputation. *The Tort of Disparagement and the Developing First Amendment*, 1987 Duke L.J. 727 (Sept. 1987).

Many states recognize the independent tort of commercial disparagement, including Arizona, California, Mississippi, New Jersey, New York, Nevada, Pennsylvania and Virginia. Other states, including Alabama, Georgia, Kansas and Maine, do not recognize the claim as a separate cause of action. *Astral Health & Beauty, Inc. v. Aloette of Mid-Mississippi, Inc.*, 895 F.Supp.2d 1280, 1285 (N.D. Ga. 2012). As well, some states remain unclear on the tort's availability, including: Illinois, Iowa, Kansas, Kentucky, Michigan, Tennessee and Washington.

While commercial disparagement is closely related to defamation, it is not the same tort. That distinction allows a corporate client to pursue actions for both torts in states that recognize those causes of action. Certain jurisdictions permit corporations to bring defamation actions for injury to business or financial reputation because corporations are incapable of demonstrating the natural person's typical claims for emotional injury or damage to an individual's reputation. However, corporate defamation claims can be problematic because of absolute or conditional privileges, high standards of fault and the defense of non-defamatory construction.

Injurious statements about a business organization are consistently held to defame the corporate entity, including claims that business practices are unethical or dishonest, that the business is financially unstable, insolvent or has a poor credit rating. *Brown v. Holton*, 109 Ga. 431, 34 S.E. 717 (1899) (poor credit); *Simons v. Burnham*, 102 Mich. 189, 60 N.W. 476 (1894) (heavily in debt); *Moore & Munger Co. v. Motor Trades Pub. Co.,* 170 A.D. 779, 155 N.Y.S. 929

(1st Dep't. 1915), *aff'd*, 217 N.Y. 683, 112 N.E. 1066 (1916) (bankrupt); *Witteman Bros. v. Witteman Co*., 88 Misc. 266, 151 N.Y.S.. 813 (Sup. Ct. 1914), *aff'd*, 168 A.D. 930, 152 N.Y.S. 1150 (2d Dep't. 1915) (financially irresponsible).

While defamation actions protect reputation, courts have held that statements disparaging the quality of an entity's product or service are usually not considered defamatory unless the remark charges that the entity acted dishonestly in offering the product in commerce. *Defamation or Disparagement?*, 24 Minn. L.Rev. 625, 631 (1940). Merely commenting that a small business has financial limitations does not give rise to a claim for defamation. *McLaughlin v. F. W. Woolworth Co.*, 125 Neb. 684, 251 N.W. 293 (1933) (noting in *dictum* that merely commenting about a small business's financial limits is permissible). Many of the cases addressing defamation claims in the corporate context hold that a defamatory remark made "in disparagement of a person's property, or of the quality of the articles which he manufactures or sells, and which contain no imputation upon him as an individual, or in respect to his office, profession or trade, is not actionable, unless special damages can be shown." *Hopkins Chemical Co. v. Read Drug & Chemical Co.*, 124 Md. 210, 92 Atl. 478 (1914); *Fowler v. Curtis Pub. Co.*, 182 F.2d 377 (D.C. Cir. 1950); *H*; *Cleveland Leader Printing Co. v. Nethersole*, 84 Ohio St. 118, 95 N.E. 735 (Ohio 1911).

Generally, one's client may have a viable defamation claim if it can demonstrate that the defendant made a defamatory statement of fact or concerning the client that (i) was made public; (ii) was false; and (iii) damaged the client as a result. *Cignetti v. Healy*, 89 F.Supp. 2d 106, 126 (D. Mass. 2000). Many jurisdictions also require the plaintiff to prove "fault" in defamation claims. The burden of proof in defamation claims differs depending on the status of the plaintiff. A "public figure" must prove the defendant acted with "actual malice." *Rosenblatt v. Baer*, 383 U.S. 75, 85, 86 S.Ct. 669, 15 L.Ed. 2d 597 (1966); *Gertz v. Robert Welch, Inc*., 418 U.S. 323, 345, 94 S.Ct. 2997, 41 L.Ed. 2d 789 (1974).

A statement is deemed to be published with "actual malice" if published with knowledge of its false or if the defendant acted with "reckless disregard" as to the statement's truth or falsity. *New York Times Co. v. Sullivan*, 376 U.S. 254, 267, 280, 84 S.Ct. 710, 95 A.L.R. 2d 1412 (1964); *Curtis Publ'g. Co. v. Butts*, 388 U.S. 130, 133-34 (1967) (holding that a plaintiff must prove "actual malice" to prevail in a defamation action against a public official or public figure). It is well-established that a corporation has the legal status of a "person" under the Fourteenth Amendment protections. *Santa Clara Company v. S. Pac. R.R. Co.*, 118 U.S. 394, 396, 6 S.Ct. 1132, 30 L.Ed. 118 (1886). The *New York Times* "actual malice" requirement applies to commercial disparagement and defamation claims in cases where the plaintiff is a "public figure." *Quantum Electronics Corp. v. Consumers Union of the United States*, 881 F.Supp. 753 (D.R.I. 1995); *see also*, *Bose Corp.,* 466 U.S. at 488.

While commercial disparagement actions share some of the proof elements of defamation, including fault, a commercial disparagement victim must prove special damages (pecuniary loss) whereas defamation damages to one's business reputation typically are inferred. *Flotech, Inc. v. E.I. Du Pont de Nemours Co.*, 627 F.Supp. 358, 365 (D. Mass. 1985), *aff'd*, 814 F.2d 775 (1st. Cir. 1987). A corporate defamation claim usually accompanies other tort or contract claims because those other claims often require stronger damages proof.

As a matter of public policy, courts have held that statements that might otherwise constitute commercial disparagement are protected as conditionally privileged because buyers recognize that a competitor's negative comments about another's products or services are highly biased. *Picker Int'l, Inc. v. Leavitt*, 865 F.Supp. 951, 964 (D. Mass. 1994) (quoting 3 Philip Areeda & D. Turner, Antitrust Law §738c at 281 (Little, Brown 1978); *see also*, Restatement (Second) of Torts §§ 623A, 649 (1979).

A disparaged corporate client might ask whether a court can restrain the defendant competitor's oral or written comments. Due to free speech protections, it is extremely difficult to obtain early injunctive relief to enjoin or restrain the publication of potentially defamatory statements. *New York Times Co. v. United States*, 403 U.S. 713, 714, 91 S.Ct. 2140, 29 L.Ed. 2d 822 (1971) ("Any system of prior restraints of expression comes to this Court bearing a heavy presumption against its constitutional validity.") (quoting *Bantam Books, Inc. v. Sullivan*, 372 U.S. 58, 70, 83 S.Ct. 631, 9 L.Ed. 2d 584 (1963). Prior restraint of speech is granted only in extraordinary circumstances where the publication might compromise national security or the right to a fair trial. *See, e.g.*, *Perle & Williams* on Publishing Law§ 5.13(A), at 5-65 (3d ed. 1999 & Supp. 2001). Thus, defamation remedies typically are limited to monetary damages. Given that hurdle, a false advertising claim also becomes an attractive remedy for false and derogatory remarks about a corporation's products or services.

B. <u>False Advertising Remedies under the Lanham Act</u>

As previously shown, commercial disparagement and false advertising claims are closely related. False advertising claims under the Lanham Act §43(a) can be pursued in either federal or state court. 28 U.S.C. § 1338(a).

To enjoin false advertising under the Lanham Act § 43(a), a plaintiff must demonstrate a belief that "he or she is or is likely to be damaged" by the advertising or promotion. 15 U.S.C. §1125(a)(1). Damages are recoverable when the plaintiff shows that the false advertising deceived customers, and the plaintiff suffered harm as a result thereof. Some courts presume harm in cases of false comparative advertising. *J. Thomas McCarthy, McCarthy on Trademarks and Unfair Competition* §27:30 (4th ed. 1996 & Supp. 2001).

Common defenses to false advertising include: (i) puffery (exaggeration or boast about the injured party's products upon which no reasonable consumer would rely, rather than a measurable claim of superiority); (ii) reverse puffery (exaggeration of the qualities of the products of the injured party's competitors that is so unrealistic that no reasonable consumer would take it seriously); and (iii) statements of mere opinion.

Deceptive commercial speech is outside the protection of the First Amendment; and, courts *will* enjoin certain confusing forms of deceptive commercial speech pursuant to Section 43(a) of the Lanham Act. *E&J Gallo Winery v. Gallo Cattle Co.,* 967 F.2d 1280, 1297 (9th Cir. 1992) (holding that misleading commercial speech may be restricted without violating the First Amendment) (internal citations omitted); *see also, Kelly Blue Book v. Carsmarts, Inc.,* 802 F.Supp. 278, 291-293 (C.D. Calif. 1992) ("In trademark cases, the courts are given flexibility in fashioning injunctive relief . . . ").

C. Remedies Under Unfair or Deceptive Trade Practices Statutes

Every state has enacted a statute designed to prohibit deceptive and, in some states, unfair trade practices. A majority of states has adopted some version of the Uniform Deceptive Trade Practices Act (the "Act"). The Act was enacted in 1964, amended in 1966 and then declared obsolete in 2000 by the Uniform Laws Commission. Generally, state deceptive trade practices statutes that have adopted the Act make it unlawful to engage in unfair or deceptive acts or practices in commerce or trade. The Act provides:

> *Section 2. Deceptive Trade Practices. (a) A person engages in a deceptive trade practice when, in the course of his business, vocation, or occupation, he…(8) disparages the goods, services, or business of another by false or misleading representation of fact…*
>
> *Section 3. Remedies. (a) A person likely to be damaged by a deceptive trade practice of another may be granted injunctive relief upon terms that the court considers reasonable. Proof of monetary damage, loss of profits, or intent to deceive is not required…*

Thus, a state's deceptive trade practices statute may provide an alternative remedy where it does not recognize commercial disparagement or trade libel.

Illinois state courts have held that commercial disparagement no longer is an available cause of action based upon the adoption of the Illinois Deceptive Trade Practices Act; while other cases have held that the Illinois Deceptive Trade Practices Act merely "supplemented" Illinois common law, making the commercial disparagement tort a potential cause of action. *First Health Group Corp. v. United Payors & United Providers, Inc.,* 2000 WL 5492723, *2 (N.D. Ill. 2000) (unreported decision)(noting that it is unclear whether Illinois recognizes the commercial disparagement cause of action); *Fedders Corp. v. Elite Classics,* 268 F.Supp. 2d 1051, 2014 (S.D. Ill. 2003) (federal court holding that the Illinois Deceptive Trade Practices Act "codifies the common law tort of commercial disparagement"); *see also*, *Allcare, Inc. v. Bork*, 176 Ill.App. 3d 993, 999-1000 (1st Dist. 1988) (noting the Illinois Trade Practices Act "substantially codified the common law tort of commercial disparagement, *i.e.*, disparagement of the quality of one's goods or services."). In states where the commercial disparagement tort is unclear, the best practice is to plead both common law commercial disparagement and statutory disparagement under the state's deceptive trade practices act.

The substantive provisions of these trade statutes vary among the states. For example, New York's statute proscribes deceptive practices in general terms but enumerates specific violations and also includes a catch-all provision. New York law provides that "[d]eceptive acts or practices in the conduct of any business, trade or commerce or in the furnishing of any service in this state are hereby declared unlawful" and that "[f]alse advertising in the conduct of any business, trade or commerce or in the furnishing of any service in this state is hereby declared unlawful." N.Y. Gen. Bus. Law 349(a), 350 (McKinney 1988). Other states with broadly written deceptive trade statutes include Arizona, California, Connecticut, Delaware, Kentucky, Montana, Nebraska, South Carolina, Vermont, Washington and Wisconsin. States listing specific fraudulent practices include: Alabama, Alaska, Arkansas, California, Delaware, the District of

Columbia, Georgia, Hawaii, Idaho, Illinois, Iowa, Kansas, Maine, Minnesota, Mississippi, New Hampshire, New Mexico, Ohio, Oregon, Pennsylvania, South Dakota, Pennsylvania, Tennessee, Texas, Utah, Virginia and Wyoming.

One major advantage to bringing claims under a state deceptive trade practices act is that many states specifically authorize injunctive relief. A majority of states allow consumers to recover damages. To justify injunctive relief for disparagement under the Act, the plaintiff must show irreparable injury. The definition of "consumer" varies among the states. The Texas Consumer Protection and Deceptive Trade Practices Act defines a "consumer" as "an individual, **partnership, corporation**…who seeks or acquires, by purchase or lease, any goods or services." Tex. Bus. & Com. Code Ann. §17.45(4) (emphasis added). Similarly, the North Carolina Deceptive Trade Practices Act was intended to benefit consumers; however, "its protections extend to businesses in appropriate situations." *Dalton v. Camp*, 353 N.C. 647, 656 (2001); *citing*, *Pearce v. American Defender Life Ins. Co.,* 316 N.C. 461, 469, 343 S.E.2d 174, 179 (1986); *United Labs, Inc. v. Kuykendall*, 322 N.C. 643, 665, 370 S.E.2d 375, 389 (1988). Accordingly, litigators should analyze the classes of "persons" with standing under the applicable state's Deceptive Trade Practices Act to determine whether business entities may invoke the statutory remedies.

The elements under very state's Deceptive Trade Practices Act must be scrutinized. Some states do not allow suits between competitive businesses, or limit such suits to certain circumstances. Some statutes may only protect against a limited category of remarks or remarks made only by certain business divisions. For example, the Illinois version of the Act applies to statements disparaging the quality of a business's products but does not apply to those which impute want of integrity. *Republic Tobacco, L.P. v. North Atlantic Trading Co., Inc*., 254 F.Supp. 2d. 985, 998 (N.D. Ill. 2002); *Fedders Corp. v. Elite Classics*, 268 F.Supp. 2d 1051 (S.D. Ill. 2003) (Illinois version of the Act does not provide cause of action for statement that plaintiff has infringed defendant's mark rights); *Labor Ready, Inc. v. Williams Staffing, LLC*, 149 F.Supp. 2d 398 (N.D. Ill. 2001) (Competitor's alleged false statement that the plaintiff employment agency was operating illegally and would be shut down by the city was actionable). Delaware's version of the Act does not extend to negative remarks made by one business about another when the parties are in a vertical, rather than horizontal, business relationship. *Tri-State Energy Solutions, LLP v. KVAR Energy Savings Inc.*, 884 F.Supp. 2d 168 (D. Del. 2012).

Some states that have adopted the Act provide injunctive relief, whereas others restrict recovery to monetary damages. Jurisdictions whose statutes expressly authorize punitive damages for deceptive trade practices include California, Connecticut, District of Columbia, Georgia, Idaho, Kentucky, Missouri, Oregon and Rhode Island.

Many states permit plaintiffs to recover treble damages under their deceptive trade practices statutes. Others give the court discretion in awarding such fees, while others provide automatic treble damages if the defendant acted with intent or willfulness. Jurisdictions that provide court discretion include: Alabama, Tennessee and the District of Columbia. States that provide automatic treble damages include: Delaware, New Jersey, South Carolina, Tennessee and Vermont. The North Carolina Unfair Trade Practices Act allows automatic treble damages; and the statute does **not** require proof of intentional or willful conduct. 22. N.C. Gen. Stat. § 75-16 (1977).

Another significant variation in state deceptive trade practice statutes is that some states permit only consumers to bring private claims. Some states provide for private litigant enforcement; in others, deceptive trade practices result in criminal prosecution. Some states' attorneys general may bring a lawsuit against a business enterprise for violating deceptive trade practice laws. South Dakota has not adopted the Act but grants standing to the attorney general and to "any individual" to pursue a deceptive trade practices claim. In Georgia, "[a] person engages in a deceptive trade practice when, in the course of his **business, vocation, or occupation**, he … [d]isparages the good, services, or business of another by false or misleading representation of fact…" (emphasis added); O.C.G.A. § 10-1-372(a)(8). To state a viable claim for relief, the disparaging comments must be misrepresentations of fact, not opinion. *Davita Inc. v. Nephrology Associates, P.C.*, 253 F.Supp. 2d. 1370, 1379 (S.D. Ga. 2003). Like many states, Georgia also authorizes injunctive relief to the injured business.

D. <u>Tortious Interference with Economic or Business Advantage</u>

Litigators should consider whether defamation of a corporation gives rise to a claim for tortious interference with economic advantage or business expectancy. As noted earlier, Georgia is among the states that do not recognize commercial disparagement, trade libel or injurious falsehood. The Georgia courts have held that those claims are integrated under tortious interference and defamation. *State Farm Mut. Auto. Ins. Co. v. Hernandez Auto Painting and Body Works, Inc.*, 312 Ga. App. 756, 719 S.E.2d 597, 600 (2011) (cert. denied). Other jurisdictions similarly have held that false or misleading statements in commercial speech may also give rise to claims for interference with existing or prospective business relations or economic advantage pursuant to state law. *Franklin v. Dynamic Details, Inc.*, 116 Cal.App. 4th 375, 10 Cal.Rptr.3d 429, 441 (Cal. Ct. App. 2004) ; *Dube v. Likins*, 216 Ariz. 406, 167 P.3d 93, 97-103 (Ariz. Ct. App. 2007) .

Generally, a claim for tortious interference with business relations requires a plaintiff to prove five essential elements: 1) existence of a valid business relationship; 2) the defendant's knowledge of the existence of the relationship; 3) the defendant's intentional tortious interference of the relationship; 4) the absence of justification; and 5) damages resulting from the defendant's wrongful inducement of the interference. *Flintridge Station Associates v. American Fletcher Mortgage Co., et al.,* 761 F.2d 434, 441 (7th Cir. 1985) ("[u]nder the tort of interference with a business relationship or prospective advantage in business, the same elements [as to contract interference] apply except that no contractual relationship need be shown") (citations omitted). Establishing a claim for tortious interference with prospective relations can be challenging because such claims require "that more blameworthy means be used [by the defendant] than does the tort of interference with contractual relations." *The Great Escape, Inc. v. Union City Body Co.*, 791 F.2d. 532, 542 (7th Cir. 1986).

The Restatement (Second) of Torts § 768 (1977) sets forth the elements of the "privilege of fair competition" that allows "interfering" with a business relationship:

Section 768: Competition as Proper or Improper Interference

> (1) One who intentionally causes a third person not to enter into a prospective contractual relation with another who is his competitor

> or not to continue an existing contract terminable at will does not interfere improperly with the other's relation if (a) the relation concerns a matter involved in the competition between the actor and the other and (b) the actor does not employ wrongful means and (c) his action does not create or continue an unlawful restraint of trade and (d) his purpose is at least in part to advance his interest in competing with the other. (2) The fact that one is a competitor of another for the business of a third person does not prevent his causing a breach of an existing contract with the other from being an improper interference if the contract is not terminable at will.
>
> Further:
>
> One's privilege to engage in business and to compete with others implies a privilege to induce third persons to do their business with him rather than with his competitors. In order not to hamper competition unduly, the rule stated in this Section entitles one not only to seek to divert business from his competitors generally but also from a particular competitor. And he may seek to do so directly by express inducement as well as indirectly by attractive offers of his own goods or services. The only limitations upon this are those stated in Clauses (a) to (d).

See, Great Escape at 543 (To support a claim for tortious interference with business relations under Indiana law, "[t]here must …be something "illegal" about the means employed").

To sustain a viable claim for tortious interference with prospective business relations as an alternative or supplemental remedy to commercial disparagement, the alleged interferer must have acted with improper, wrongful means and without justification. Accordingly, claims for tortious interference with prospective business relations resulting from a defendant's conduct motivated by the capitalistic spirit of competition will not prevail.

III. PUBLIC RELATIONS AS A REMEDY TO DISPARAGEMENT

In addition to the legal remedies discussed above, a company injured by disparagement may consider employing a public relations professional to assist in remedying its injuries. This section provides guidance on that path.

A. The Difference Between Public Relations and Advertising

- There's an old saying that goes: "Advertising is what you pay for, publicity is what you pray for."
- Advertising is paid airtime, or space in publications that delivers a message directly to consumers.
- Public relations provides information to the news media in the hope of gaining favorable coverage.

- Publicists work with reporters or editors to get them to write a positive story about their clients that appears in the editorial section of the magazine, newspaper, TV station or website, rather than the "paid media" section where advertising messages appear. A story has more credibility because it was independently verified by a trusted third party, rather than purchased.
- Publicists are not magicians. A story has to be newsworthy in order for the press to cover it. If reporters and editors do not think the public will be interested in your story, no connections or cajoling will convince them to run it.

B. How to Utilize Public Relations in a Disparagement Crisis

- Legal routes are just one way to combat disparagement and often courts cannot stop the publication of disparaging communications fast enough, if at all. Therefore, cases of disparagement can prompt a public relations crisis.
- A communications crisis is any situation that threatens the integrity or reputation of your company, usually brought on by adverse or negative media attention. If handled correctly the damage can be minimized.
- It is not always easy to determine the source of disparaging information (i.e. anonymous bloggers) and the legal process can be slow, time consuming, and expensive. In these cases, individuals and companies can turn to a public relations professional for crisis communications to address the adverse impact quickly and often in the forum where the communication is taking place.
- It is crucial in a crisis is tell it all, tell it fast, and tell the truth.

C. Examples of Public Relations Crises As Opposed To Disparagement

1. Spider Eggs in Bubble Yum

- Bubble Yum was the first soft bubble gum to hit the market. It was an instant success when it debuted in 1976 and sales of the candy soared. 300 million packs sold in just its first 15 months.
- An unfounded rumor that spiders' eggs had been found in Bubble Yum hit. Within 10 days, company surveys showed that over half of the children in the New York area had heard the rumor.
- Bubble Yum ran full page ads in newspapers across the country. "Somebody is telling very bad lies about a very good product," the headline proclaimed.
- The parent company spent over $100,000 battling this rumor.
- It worked. Once the rumor was debunked, sales returned to normal (which, prior to the spider egg story, were so high that production couldn't keep up with demand).

2. Accelerating Audis

- A 1986, "60 Minutes" story reported the problem of cars, specifically the Audi 5000, suddenly accelerating.
- The segment highlighted Kristi Bradosky, an Ohio woman whose son Joshua was killed when she ran him over with the family's Audi.
- Bradosky told "60 Minutes" that Audi's manufacturer, Volkswagen, was to blame for her son's death.
- The family had a $30-million lawsuit pending against Volkswagen at the time the "60 Minutes" report aired.
- A jury later determined in 1988 that the death was not due to a defect with the car, based at least in part on testimony that Bradosky admitted to police that her foot had slipped off the brake and onto the accelerator.
- The report used video to illustrate a car suddenly accelerating out of control. But it was later revealed that the car used in the demonstration was rigged with a pressurized transmission set up by one of the experts who testified for the Bradoskys in their lawsuit against Volkswagen.
- The report was devastating for Audi, which had a peak year in 1985 selling more than 74,000 cars. The manufacturer issued a recall on the model in January 1987. Fewer than 23,000 Audi 5000s were sold in 1988.
- By 1989, lawsuits against Audi sought a total of $5 billion, according to a report in the journal Media & Marketing Decisions.
- While some legal decisions found Audi liable for damages due to the design of the brake pedal, more decisions came down in Audi's favor.
- In March 1989, the National Highway Traffic Safety Administration released a report attributing the acceleration to "pedal misapplication," and found no mechanical errors in the vehicles that would have caused arbitrary movement.

3. Finger Found in Wendy's Food

- In 2005, Anna Ayala alleged she found a piece of human finger in a bowl of chili she bought at a Wendy's in California.
- The New York Times was the only major national paper to report the case in the week after the allegations surfaced. It published a short Associated Press report saying "a woman bit into part of a human finger while eating a bowl of chili at a Wendy's restaurant."
- But "Good Morning America" reported "a grisly discovery for a customer at Wendy's. A California woman found a human finger in a bowl of chili this week."
- Other media outlets began reporting on the case in detail.
- As police investigated, it became clearer that Ayala had staged the event and soon, she had dropped plans to sue Wendy's. The AP reported that Ayala had a history of suing corporations, including El Pollo Loco. She had also sued General Motors over a car accident, but the case was dismissed.
- Ayala was arrested and the case was labeled a "hoax" when she was charged with attempted larceny.

- Wendy's reported 2-to-2.5-percent losses across all of its restaurants and 20-to-50-percent drops in its San Francisco Bay Area restaurants, according to The New York Times.

4. Online Reviews

- Online reviews have a major effect on buying decisions.
- Some businesses have tried to prevent negative reviews by placing non-disparagement clauses in customer contracts. The clauses forbid customers from writing negative reviews online by pain of steep financial penalties.
- Not surprisingly, disgruntled customers dislike the clauses.
- The KlearGear case is an example of the provision. John Palmer bought his wife, Jen, Christmas gifts on KlearGear.com in 2008. The items never arrived and the PayPal transaction was automatically canceled. Jen posted a review on ripoffreport.com, saying she was unable reach anyone at KlearGear.com to resolve the case. The company emailed them three years later, saying they would be fined $3,500 if they did not remove the post within 72 hours.
- When they refused to pay, the company reported their debt to credit bureaus, and their credit rating was damaged. The couple then sued and a Utah court ordered KlearGear to pay them $306,750 in damages.
- The case caused a public relations disaster for KlearGear. Following media stories, public outcry prompted the company to protect its Twitter account and shut down its Facebook page. The incident was a case study in how not to respond to customer complaints.
- Shore Dream Vacation Rentals provided a better response. When CNN reported its contract provision that threatened fines up to $10,000 for negative reviews, the company quickly removed it. A spokeswoman told CNN the clause was intended to protect it from customers who demand compensation by threatening unreasonable negative reviews after leaving a vacation unit. The company, she added, never used the clause to fine a customer.
- Bottom Line: Non-disparagement clauses can prompt a public relations crisis. A better solution is to quickly identify complaints through social media listening and attempt to resolve issues through customer service.

D. How to Implement a Crisis Communications Plan

1. Appoint a Crisis Communication Team

- A crisis communications team should prepare and anticipate a crisis. This team will come up with a plan of action and decide who the spokesperson should be.
- When a crisis occurs, the communications team will determine the appropriate positioning or message to address the emergency.
- Things to think about: "Tell it all, tell it fast and tell the truth"
- The first and foremost goal is protecting the integrity and reputation of the Company. Never try to lie, deny or hide your involvement. If you ignore the situation it will only get worse.

- To decide on a position, it is important to step out of your role in the company and put yourself in the situation of whom ever was involved in the crisis or try to view the crisis from the eye of the public. Ignoring the situation will only make things worse.
- Keep in mind that people tend to remember what they hear first and last.

2. Prepared Statements

- If you don't communicate immediately, you lose your greatest opportunity to control events. Your first news release should include at a minimum the who, what, when and where of the situation.
- Give facts that have been gathered from reliable sources and confirmed. Don't over reach and don't speculated. If you do nothing more than show concern for the public and for your employees in your first press interaction, you are already on the right track.
- Have a prepared statement on hand that can be used to make an initial general response to the media when knowledge about the crisis first becomes known on a widespread basis or by reporters.
- It is also advisable to develop prepared statements to be made by the spokesperson at the onset of any media interview, briefing or news conference.

3. Handling Media Interviews

How to prepare for interviews

- Prepare "talking paper" on primary points you want to make.
- Anticipate questions--prepare responses.
- Practice answering questions.
- Cover controversial areas ahead of time.
- Know who will be interviewing you, if possible.
- Audiences often remember impressions, not facts.
- If you don't have the answer or can't answer, admit it and move on to another topic.
- There is no such thing as off the record.
- Don't think you have to answer every question.
- Make sure you are prepared in detail.
- Remember, the interview lasts as long as a reporter is there.

After The Interview

- You can ask to check technical points, but do not ask to see advance copy of the story.
- Never try to go over reporter's head to stop a story.
- Do not send gifts to reporters--it is considered unethical for them to accept gifts.

4. Addressing online complaints

- The faster you address a complaint, the better the chances you can convert that angry customer into a fan. Conversely, the longer a complaint sits, the more likely it will attract more complaints and turn into a crisis.
- Try to move the conversation offline to avoid a back-and-forth conversation in public. Ask them to email, call or to send a private message. This creates the appearance that you're striving to resolve the problem.
- Find out what happened to cause the complaint.
- No matter how negative the comment, thank the customer for bringing the problem to your brand's attention.
- Show respect. Keep in mind the conversation is public; so losing your temper will only damage the brand's reputation further. When social media service agents are helpful and courteous, it makes rude reviews look childish and reflects well on your brand.
- Correct misinformation. If commenters jump to the wrong conclusion about your company, correct them with the proper information and thank them for the feedback.
- And of course, provide high-quality products and superb customer service.
- Legal recourse may be considered as a last resort if the review is defamatory and dishonest. Using non-disparagement clauses to place legal restrictions on free speech simply doesn't work.

CONCLUSION

Corporate America has never been immune from competitive battles. Indeed, we all learn that competition is the lifeblood of capitalism and should drive better products, services, pricing and market share. However, when aggressive competition crosses the line and mutates into disparagement, false statements and other means of unfair play, the privilege of fair competition is undermined. Particularly, in the world of communicating through Social Media, the instant ability to sully another company's products or services requires very little effort yet results in very significant losses to the maligned business. Companies endeavoring to advance themselves through assertive, but fair, competition must be equally diligent in exercising their legal remedies when rogue competitors choose commercial disparagement, defamation, false advertising and malicious interference as their primary marketing strategies. Attorneys skilled in the remedies necessary to combat those forms of unfair business practice are valuable assets to their corporate clients. As such, the commercial disparagement area of law offers the opportunity for ongoing interaction and relationship-building among company management, in-house counsel, outside litigation counsel and public relations professionals. That formidable legal and crisis-management team can respond dynamically and aggressively to thwart and remedy the disparagement. Therefore, remember: do not let words ruin your client's business -- know how to litigate a commercial disparagement dispute.

Your Clients Don't Have to be Homer Simpson: Strategies for Avoiding Preventable Bad Faith

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INTRODUCTION

Insurers make mistakes. When insurers make mistakes, policyholders often seek to impose bad faith tort liability, whether under the common law, implied covenant of good faith and fair dealing or a state statute, on account of that mistake.

Few insurers set out to act in bad faith. Sometimes there are legitimate disagreements regarding policy interpretation. On other occasions, a series of relatively inconsequential acts or omissions flow into a claim decision unfavorable to the policyholder. This paper will focus on the last scenario – the confluence of events that later are presented by the policyholder as evidence of the insurer's bad faith.

Incompetence, inflexibility, inadvertence, paralysis, overwork, carelessness all are conditions that can contribute to a bad faith claim. They are present in just about every workplace, both inside and outside the insurance industry.

In some jurisdictions, those traits do not always matter. For example, in California, the standard for bad faith is whether the insurer's failure to provide contractual benefits was "unreasonable and without proper cause." *California Shoppers, Inc. v. Royal Globe Ins. Co.*, 175 Cal.App.3d 1, 221 Cal.Rptr. 171, 201 (1985). "Proper cause," in turn, is defined in terms that permit a mistake to trigger the necessary proper cause for an erroneous denial of policy benefits claim – in some circumstances. *Id.*

AN OUNCE OF PREVENTION IS WORTH A POUND OF CURE

Perfection may not be attainable, but in many instances, the insurer and/or its attorneys may be able to take action to reduce the incidence of claims handling errors. Taking preventive action can be a powerful tool in defeating a claim of "institutional bad faith" – where the policyholder does not blame the individual claims handler, but instead attributes the error to company management for not properly equipping, training and supervising the claims handler. Institutional bad faith claims also can involve company-wide policies and practices. Those are beyond the scope of this paper.

"Institutional bad faith" can function like the reptile theory for the policyholder bar because it allows the policyholder to argue in a way that leads jurors to conclude the same could well happen to them, if the "institutional" problem is not eliminated.

1. Situations Creating a Risk of Institutional Bad Faith

A. "Overwork"

If the bad faith claim is based upon something that was not done timely, the policyholder may argue the claims handler carried too high a claim load for the work being performed and that management should have intervened to reduce the workload to a manageable level. A failure to accomplish something is rarely due to one factor. However, contributing factors may include training, the degree of motivation of the individual employee, and other workplace disruptions.

Defense counsel needs to identify the risk early and spend sufficient time before any company depositions are taken, and identify why - in the particular case - the claims handler acted as he or she did. If counsel can identify a non-institutional and non-malicious reason for the conduct, that reason needs to be included in the defense theme of the case.

B. Ego

We've all encountered the rare claims handler who lets his or her ego interfere with proper claim handling. Whether from a desire to argue with opposing counsel and prove that counsel wrong, or simply having a closed mind, there are claims handlers who let their egos interfere with good faith claims handling. These claim handlers need to be identified early. Ideally, they should be counseled by their managers long before a bad faith claim ever surfaces. When one does, it is critical that defense counsel candidly explain the employee's issue to the client's management. It may be too late to prevent this claim, but it's not too late to redirect the employee's energy in a productive direction before the next claim.

When a claim does arise, extensive deposition preparation is necessary. Egotistical witnesses often will tell you what they believe you want to hear during preparation, only to behave harmfully while under oath. Witnesses saddled by large egos, especially those who treat opposing counsel with disdain, also have difficulty taking advice and guidance from defense counsel. Often using a trial consultant in preparation is beneficial to mitigate this effect in the client's case by inserting an objective voice into the narrative. The witness needs to understand that he or she is not required to win the case for the insurer, but simply to avoid saying things that will result in a loss.

C. Being Too Nice: No Good Deed Goes Unpunished

The claims professional who is too nice and too generous is not as rare as a Unicorn. The claims professional may create expectations for a level of performance that is above and beyond what is required by the policy and standard of care. Sometimes that results in overpayment of claims. Other times it leads to inadequate investigation and payments of amounts never due. When there is a change in instructions or personnel, the company is now faced with a policyholder whose expectations, created by company's conduct, that are not congruent with the company's obligations under the policy. Here, the best defense counsel may be able to do is to turn the good deed into an asset – evidence that the claims handler was not looking to deny payment to the policyholder.

D. Ignorance

Sometimes claim handlers are simply uninformed. The most dangerous ones are those who do not know that they are uninformed, let alone the depth of their ignorance. Training may not be as effective as desired if the information being conveyed is contrary to the beliefs and expectations of the student.

What can defense counsel do? While it may be too late to change what has happened, counsel must make a tactical decision about whether the claims handler will present better as a witness in his or her natural ignorant state, or subsequently educated.

E. HR Policies

We've probably all received discovery requests regarding the manner in which claims handling employees are compensated or evaluated. While there may be relatively few companies today where claims handler evaluations and compensation is linked to overall claims results, this is one area where company management needs to act. Claims professionals should not have an economic incentive to deny payment of monies due.

2. <u>Selected Institutional Bad Faith Cases</u>

The following list is a selection of cases involving claims of institutional bad faith. It is illustrative, rather than exhaustive.

A. White v. Continental General Ins. Co., 831 F.Supp 1545 (D. Wyo. 1993): Post-Claim Underwriting

This case involved what the policyholder bar misleadingly calls "post-claim underwriting." The insurer relied on the policy application, as it was entitled to do, and only after the loss did it investigate the truth of the responses to the policy application. In addition, underwriters were evaluated under a program in which they were required to earn "points." The points earned for uncovering facts justifying rescission of a policy were greater than those earned for more traditional underwriting activities. The District Court found on these facts that the policyholder's bad faith claim could survive a summary judgment motion.

"Post-Claim Underwriting" represents a triumph of deceptive labeling. It presumes the insurer cannot rely upon the representations made by the policyholder in an application, and having relied on those representations cannot conduct any investigation regarding them when their falsity is later revealed. In short, it gives policyholders a license to lie.

B. *Kosierowski v. Allstate Ins. Co.*, 51 F.Supp.2d 583 (E.D. Pa. 1999) and *Milhone v. Allstate Ins. Co.*, 289 F.Supp.2d 1089 (D. Ariz. 2003): Valuation Software

These are two out of a number of cases involving "Colossus" a software program used by Allstate and some other insurers to assist in valuing relatively minor bodily injury claims. In both instances, the courts found no causal connection between the use of Colossus and any harm allegedly suffered by the policyholders.

MITIGATION STRATEGIES

Don't panic. Just because your client or employer may have a problem doesn't mean liability will follow. As the two *Colossus* cases illustrate, causation matters. The damages claimed must have been caused by the allegedly wrongful conduct. If they were not, then the evidence of wrongful conduct, while embarrassing or worse and very important to the client, the conduct might not create liability.

Assuming, however, that your client, the insurer, has made a mistake, a number of alternatives are available. Not all will work in every instance. In some instances, none may work. Those alternatives include:

- A sincere apology. Especially where punitive damages are at issue, a sincere apology from the company may make a significant difference.

- Causation: No Harm = No Foul.

- Was the result correct for some other reason? Just as appellate courts affirm or reverse the outcome, if the insurer made the correct decision for the wrong reason, that is not actionable because no policy benefits were due to begin with.

- Mistakes alone may not be bad faith. If your jurisdiction has a "knowing" or lacking proper cause standard that requires the insurer or its responsible employee to know the contemplated conduct was wrong, proving that the conduct was unintentional may help.

A CANADIAN PERSPECTIVE

As a preliminary observation, litigants in Canadian common law courts face a somewhat daunting additional procedural remedy for being wrong, regardless of whether there is a finding of bad faith: the Anglo-Canadian rule on costs. While US litigants rarely face the opposing side's legal costs as a consequence of losing, in Canada the various provincial and territorial systems build in a "loser pays" rule. This can vary from jurisdiction to jurisdiction, but will usually impose a modest lower percentage of actual costs payable by the loser unless conduct suggests the court should deviate from that general rule. When conduct in the litigation itself warrants it, courts will award the highest level, known in some provinces as "solicitor-and-client" costs.

Thus, while mitigating strategies help reduce the liability in US cases, for Canadian litigants, these may also blunt the other side's argument for an increased costs award. Canadian courts also will carefully look at whether an award of bad faith punitive damages is appropriate in the face of a significant conventional damages award. This and a general reluctance to award punitive damages except in the most unusual of cases, likely explains the more modest level for punitive damages in Canadian jurisprudence.

Our highest court, citing to its own previous authority, has summarized the threshold for awarding bad faith punitive damages in one non-insurance case as follows:

> [T]his Court has stated that punitive damages should "receive the most careful consideration and the discretion to award them should be most cautiously exercised" (*Vorvis*, at pp. 1104-5). Courts should only resort to punitive damages in exceptional cases (*Whiten*, at para. 69). The independent actionable wrong

> requirement is but one of many factors that merit careful consideration by the courts in allocating punitive damages. Another important thing to be considered is that conduct meriting punitive damages awards must be "harsh, vindictive, reprehensible and malicious", as well as "extreme in its nature and such that by any reasonable standard it is deserving of full condemnation and punishment" (*Vorvis*, at p. 1108).

Honda Canada Inc. v Keays, [2008] 2 S.C.R. 362, 2008 SCC 39 at para. 68. The case involved alleged institutional bad faith in the context of a wrongful termination claim where the employer was alleged (and found by lower courts) to have implemented a discriminatory disability accommodation program. Ultimately, the Supreme Court of Canada rejected the lower court's findings on the facts. Again, as bad as they may be in a given case, the facts still must meet the legal test in the specific jurisdiction. For present purposes, the relevant Canadian standard comes from insurance-related cases.

1. <u>The Standard</u>

When determining if an insurer's conduct rises to the level of bad faith, Canadian Courts often look to the Ontario Court of Appeal's decision in *702535 Ontario Inc. v. Non-Marine Underwriters, Lloyd's of London*, [2000] O.J. No. 866 (C.A.), leave to appeal to SCC dismissed [2000] S.C.C.A. No. 258.. The panel described an insurer's duty of good faith, and the consequences of its breach, as follows:

> The relationship between an insurer and an insured is contractual in nature. The contract is one of utmost good faith. In addition to the express provisions in the policy and the statutorily mandated conditions, there is an implied obligation in every insurance contract that the insurer will deal with claims from its insured in good faith: *Whiten v. Pilot Insurance Co.* (1999), 42 O.R. (3d) 641 (Ont. C.A.). The duty of good faith requires an insurer to act both promptly and fairly when investigating, assessing and attempting to resolve claims made by its insureds.
>
> The first part of this duty speaks to the timeliness in which a claim is processed by the insurer. Although an insurer may be responsible to pay interest on a claim paid after delay, delay in payment may nevertheless

> operate to the disadvantage of an insured. The insured, having suffered a loss, will frequently be under financial pressure to settle the claim as soon as possible in order to redress the situation that underlies the claim. The duty of good faith obliges the insurer to act with reasonable promptness during each step of the claims process. Included in this duty is the obligation to pay a claim in a timely manner when there is no reasonable basis to contest coverage or to withhold payment. *Bullock v. Trafalgar Insurance Co. of Canada*, [1996] O.J. No. 2566 (Quicklaw) (Gen. Div.); *Labelle v. Guardian Insurance Co. of Can. et al*.(1989), 38 C.C.L.I. 274 (Ont. H.C.J.); *Jauvin v. L'Ami Michel Automobile Canada Ltée et al* (1986), 57 O.R. (2d) 528 (H.C.J.).

The court then proceeded to discuss the fairness element:

> The duty of good faith also requires an insurer to deal with its insured's claim fairly. The duty to act fairly applies both to the manner in which the insurer investigates and assesses the claim and to the decision whether or not to pay the claim. In making a decision whether to refuse payment of a claim from its insured, an insurer must assess the merits of the claim in a balanced and reasonable manner. It must not deny coverage or delay payment in order to take advantage of the insured's economic vulnerability or to gain bargaining leverage in negotiating a settlement. A decision by an insurer to refuse payment should be based on a reasonable interpretation of its obligations under the policy.
>
> This duty of fairness, however, does not require that an insurer necessarily be correct in making a decision to dispute its obligation to pay a claim. Mere denial of a claim that ultimately succeeds is not, in itself, an act of bad faith: *Palmer v. Royal Insurance Co. of Canada* (1995), 27 C.C.L.I. (2d) 249 (O.C.G.D.).

> What constitutes bad faith will depend on the circumstances in each case. A court considering whether the duty has been breached will look at the conduct of the insurer throughout the claims process to determine whether in light of the circumstances, as they then existed, the insurer acted fairly and promptly in responding to the claim.

Finally, the court addressed damages:

> A breach of the duty of good faith may result in an award of damages which is distinct from the proceeds payable under the policy for the insured loss and which are not restricted by the limits in the policy: See *Bullock*, supra; *Labelle*, supra.

Recently, the Saskatchewan Court of Appeal neatly summarized an insurer's duty of good faith as follows:

> I should note, as well, that there is no significant dispute in this case about the general nature of the duty of good faith owed by insurance companies to their insureds. The unequal power relationship involved in the insurance setting has led to the development of a series of obligations, implied as terms of the insurance contract, between the insurance company and the insured. Of particular relevance to this appeal are the duties of insurance companies to (a) assess claims in a balanced and fair manner, (b) advise the insured of the decision regarding the claim and of the reasons for the decision, (c) pay approved claims in a timely manner, (d) refrain from requiring an insured to sign away future rights to obtain admitted settlements, and (e) refrain from denying a claim or delaying payment in order to gain leverage or take advantage of an insured's economic vulnerability. See: *Fidler* at para. 63; *Clarfield v Crown Life Insurance Co.* (2000), 50 OR (3d) 696 (Sup Ct J) at paras 61, 62, 94, 95 and 96; *702535 Ontario Inc. v Non-Marine*

> *Underwriters, Lloyd's of London, England* (2000), 184 DLR (4th) 687 (Ont CA) [702535 Ontario Inc.].

Branco v. American Home Assurance Co., [2015] S.J. No. 286 (C.A.) at para. 97

2. Improper Investigation

Much as with the situation in the United States, an improper or biased investigation will create a problem for the insurer in Canada. For example, in both *Kogan v. Chubb Ins. Co. of Canada*, [2001] O.J. No. 1697 (S.C.J.) and *Khazzaka o/a E.S.M. Auto Body v. Commercial Union Assurance Company of Canada*, (2002), 66 O.R. No. 3110 (C.A.), the insurers accused the policyholders of committing arson. Both times, the insurers were unable to prove the policyholders committed arson. Both times, the courts found the insurers had acted in bad faith. As the court in *Kogan* explained:

> Where the insurer and/or adjuster acts unreasonably by effectively presupposing arson as the cause of the fire and taking steps to fortify this conclusion rather that objectively assessing the evidence in order to draw a reasonable conclusion therefrom, the label of bad faith will be justified and punitive damages should be awarded.

In *Khazzaka*, the appellate court was even more critical of the insurer's conduct:

> Here, the roots extend back to the early investigation, surface at trial and are supplemented by the nature of the testimony. The appellant had a duty to treat the insured fairly. It was not unfair to consult the fire department and police and refuse to accept their opinions without independent investigation. It began to be unfair conduct when the insurer persisted in denying the claim when no credible basis for alleging arson arose from that investigation. It was clearly unfair to concoct evidence of the presence of gasoline to support a defence, which may have been the jury's finding. Unfairness multiplies as all obstacles to the viability of the defence of

> arson are turned aside without concern for the insured's rights and well-being. The unfairness is further exaggerated when the defence is pursued through a trial even while the evidence of its supporters, in the trial judge's word, "crumbled" beneath them. Unfairness compounded over and over again amounts to conduct that merits the condemnation of the court when visited by an insurer that owes a duty of good faith to its insured.

CONCLUSION

Bad faith can be prevented. Bad acts and bad facts can make for bad law, but as the attorney charged with representing the client's interests, you can sometimes mitigate. This will, in jury cases, go some distance to either lessen or even prevent the perception that feeds the reptile's case. When conduct occurs that might be deemed to be bad faith, the critical question is whether it caused any harm to the policyholder. Keeping the focus on causation as the issue should be the client's goal – carrying a questionable case forward must gauge the risk of the jury losing that focus against the vindication of a zero dollar verdict.

ARBITRATING PROFESSIONAL LIABILITY & HEALTHCARE CASES: WELCOME TO THE WILD WEST

D. Jay Davis, Jr.[1]
J. Camden Hodge

Arbitration is fast becoming a preferred alternative to traditional state-court litigation, and the reasons for its allure are legion. Arbitration offers the promise of a less expensive, expedited process of dispute resolution, the proceedings are private and often cloaked with the protection of a confidentiality order, and the vast majority of arbitration awards are final and offer no or very limited rights of appeal. Because arbitrators are usually lawyers and usually have specific subject matter expertise, there exists less a belief that measured decisions will follow without the potential exposure to punitive damages and the unpredictability inherent in jury trials. Resolving a case in an arbitral forum also has the benefit of getting your client out of potentially plaintiff-friendly jurisdictions.

Despite the commonsense benefits of arbitrating your dispute, arbitration brings with it its own unique set of possible problems. For example, anecdotal evidence suggests that arbitrators do not often render a "pure" defense or plaintiff's verdict. The parties are paying arbitrators for their service, after all; accordingly, parties often worry that arbitrators will "split the baby" in issuing an award in hopes of keeping both parties relatively happy and encouraging repeat business. Further, even the pros of arbitration can cut both ways. While arbitration typically affords the parties the certainty that an award or verdict is final because of the limited appellate rights of parties to arbitration, this "benefit" can sting in the event that the arbitrator

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rules in favor of your opponent. Moreover, there always exists the possibility that your "neutral" arbitrator or panel of arbitrators has a proclivity for the not sending a plaintiff home empty-handed because they know the time and costs incurred. The fact that the rules of evidence and procedure typically are relaxed in arbitrations and that discovery often is significantly limited also can present significant problems. While limited discovery can cut litigation costs substantially, it also can make preparing for the arbitration a special challenge fraught with potential surprises.

While your client may have a burning desire to arbitrate the dispute, the decision should be carefully examined with an eye toward the likely potential of an award being rendered of some firm. Accordingly, this paper will explore a number of methods to get your case out of court and into arbitration. It also will discuss the process of navigating the arbitral proceedings, as well as the possibility of having your case adjudicated by a judge during a non-jury trial.

THE APPLICATION OF THE FEDERAL ARBITRATION ACT GENERALLY

Compelling arbitration requires an understanding of the Federal Arbitration Act ("FAA"). The text of the FAA reflects the overarching principle that arbitration agreements are a matter of contract that must be must rigorously enforced by courts according to the agreement's terms.[2] By its plain language, the FAA applies to contracts concerning maritime transactions and those "involving interstate commerce," mandating that such written arbitration agreements "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."[3] The FAA states that unless the parties have contracted to the contrary, it applies in federal or state court to any arbitration agreement regarding a transaction

[2] *Am. Exp. Co. v. Italian Colors Rest.,* 133 S. Ct. 2304 (Scalia, J) (2013); 9 U.S.C.A. § 2.
[3] 9 U.S.C. § 2 (2000). Also note that § 1 of the Act establishes that its provisions do not apply to employment contracts of "seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce."

that in fact involves interstate commerce, regardless of whether the parties contemplated an interstate transaction or not.[4] Arbitration agreements must be placed on an "equal footing" with other contracts, and courts are charged with both enforcing and protecting the "liberal federal policy favoring arbitration."[5] There is a "heavy presumption of arbitrability," requiring that when the scope of the arbitration clause is open to question, a court "***must*** decide the question in favor of arbitration."[6]

Accordingly, the FAA provides that a "party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court…for an order directing that such arbitration proceed in the manner provided for in such agreement."[7] A district court may compel arbitration if the movant demonstrates: (1) the existence of a dispute between the parties; (2) a written agreement that includes an arbitration provision which purports to cover the dispute; (3) the relationship of the transaction, which is evidenced by the agreement, to interstate or foreign commerce; and (4) the failure, neglect or refusal of the defendant to arbitrate the dispute.[8]

HOW TO COMPEL AN UNWILLING PARTY TO ARBITRATE

I. THE FEDERAL COURT APPROACH…SUE 'EM BACK

One method of enforcing an arbitration agreement is to file a separate federal action against the plaintiff in the underlying action. You will need of course a basis for Federal Jurisdiction. The process of compelling an unwilling party to arbitrate should begin as

[4] 9 U.S.C.A. § 1; *Munoz v. Green Tree Fin. Corp.*, 343 S.C. 531, 538-39, 542 S.E.2d 565, 568 (Ct. App. 2002).
[5] *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1745, 179 L. Ed. 2d 742 (2011); *Moses H. Cone Memorial Hospital v. Mercury Constr. Corp*., 460 U.S. 1, 24, 103 S.Ct. 927, 74 L.Ed.2d 765 (1983).
[6] *Levin v. Alms and Assocs.*, 634 F.3d 260, 267 (4th Cir 2011) (internal quotations omitted) (emphasis added).
[7] 9 U.S.C.A. § 9.
[8] *Am. Gen. Life & Accident Ins. Co. v. Wood*, 429 F.3d 83, 87 (4th Cir. 2005).

soon as the Plaintiff files suit in state court. In short, after the state court complaint is filed against your client, you should: (1) send the plaintiff a formal demand letter stating that all claims related to the lawsuit must be submitted to arbitration per the arbitration agreement; (2) find a jurisdictional basis to file a *federal* compliant to compel arbitration and (3) simultaneously file a motion to stay in the *state court* action.

A. *The Demand Letter*

Before a district court can compel an action to arbitration, a Plaintiff must fail, neglect, or refuse to arbitrate the dispute.[9] By sending the Plaintiff a letter or even an email demanding that the dispute be arbitrated, you are forcing Plaintiff to respond, in writing, with her position as to arbitration. If Plaintiff agrees to arbitrate, great. If she refuses, you now have written proof that Plaintiff rejected your offer to arbitrate the dispute. You also have created a justiciable controversy for the court to resolve.

B. *The Federal Complaint to Compel Arbitration and Stay State Court Proceedings*

1. Venue and Jurisdiction

The federal complaint first must establish that the district court has jurisdiction over the matter and that the venue is proper. Venue is proper in (1) the district where Plaintiff resides or (2) the district where a substantial part of the events or omissions giving rise to the claims asserted in the federal action occurred.[10]

The FAA states that the Motion to Compel Arbitration can be filed in "any United States district court which, save for such agreement, would have jurisdiction under Title 28."[11] Although the FAA is a federal act, the Supreme Court of the United States holds that the FAA

[9] *See* FN 7.
[10] *See* 28 U.S.C. § 1391(a).
[11] 9 U.S.C. § 4.

alone does not confer federal question jurisdiction.[12] Instead, there must exist some other, independent jurisdictional basis for a federal court to hear the claim.[13] Clearly, federal jurisdiction can be established by way of diversity jurisdiction under 28 U.S.C. § 1332(a) if full diversity of parties exists. In the alternative, some courts will "look through" the federal complaint and examine the underlying state court dispute already being litigating by the parties in searching for federal question jurisdiction and, occasionally, for diversity jurisdiction.[14]

2. Existence of Arbitration Agreement

Next, you must show that there is a written agreement that includes an arbitration provision which purports to cover the dispute.[15] The federal complaint should explain that the arbitration agreement was made between the Plaintiff(s) and Defendant(s). The arbitration agreement should be quoted and attached to the federal complaint, and it should clearly illustrate that the parties agreed to arbitrate. Your letter demanding arbitration and Plaintiff's subsequent refusal should be attached to the federal complaint. Plaintiff's state court complaint also should be attached and briefly described, as this proves that a genuine dispute exists between the parties. It is important not to seek any affirmative relief in state court other than to stay the action pending a federal determination of the issues, so as to avoid Plaintiff making any waiver arguments. You should also not delay your efforts to enforce the argument.

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[12] See *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp*., 460 U.S. 1, 26 n.32 (1983) ("The Arbitration Act is something of an anomaly in the field of federal-court jurisdiction. It creates a body of federal substantive law establishing and regulating the duty to honor an agreement to arbitrate, yet it does not create any independent federal-question jurisdiction under 28 U.S.C. § 1331 or otherwise. Section 4 provides for an order compelling arbitration only when the federal district court would have jurisdiction over a suit on the underlying dispute; hence, there must be diversity of citizenship or some other independent basis for federal jurisdiction before the order can issue.")

[13] *Id.*

[14] *See Vaden v. Discover Bank,* 556 U.S. 49 (2009). Most of the courts applying *Vaden* considered it limited to federal question cases, though some courts have suggested that *Vaden* could apply to diversity cases. *Garner v. BankPlus*, 484 B.R. 134, 139-40 (S.D. Miss. 2012) (collecting cases applying the "look through" approach only in federal question cases); *but see Cytec Indus., Inc. v. Powell*, 630 F. Supp. 2d 680, 686 n.2 (N.D. W. Va. 2009) (suggesting in dicta that the reasoning of *Vaden* could apply to diversity cases).

[15] *See* FN 7.

3. Relationship to Interstate or Foreign Commerce

Finally, your federal complaint must explain how the arbitration agreement relates to interstate or foreign commerce. Oftentimes, an arbitration agreement will contain such language in the body of the agreement itself. Regardless, you must be prepared to explain the relationship and offer proof at the time of filing the complaint or when the motion to compel arbitration is filed. The United States Supreme Court has interpreted the FAA's use of the phrase "involving commerce" as the functional equivalent of the term "affecting commerce" – a statutory term of art that signals the broadest possible exercise of Congress's Commerce Clause power.[16] In *Allied-Bruce*, for example, the arbitration agreement at issue was between an Alabama homeowner and the local office of a pest control company.[17] In rejecting a legal standard that looked solely to the contemplation of the parties, the Supreme Court held that the FAA's use of the words "involving commerce" encompasses more than just activities within the actual flow of interstate commerce, and should be read more broadly as any contract "affecting commerce."[18] The Court adopted a "commerce in fact" standard, meaning that a transaction that in fact involved interstate commerce was sufficient.[19] The Court found that the contract at issue satisfied that standard because of the pest control company's multi-state nature and its use of out-of-state materials.[20]

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[16] *See Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 268-69 (1995).
[17] *Id*. at 268.
[18] *Id*. at 273-74.
[19] *Id*. at 277-78.
[20] *Id*. at 282.

Eight years later, the Supreme Court reaffirmed the *Allied-Bruce* standard in summarily reversing a contrary ruling issued by a state supreme court.[21] In doing so, the Court found that a debt-restructuring agreement was a contract "evidencing a transaction involving commerce" because the debt at issue was secured by the defendant-company's assets, which included goods assembled from out-of-state parts and raw materials.[22] The Court also explained that the individual debt-restructuring transactions, taken alone, did not have to have a substantial effect on interstate commerce in order for the FAA to apply.[23] Instead, only the "general practice" needs to "bear on interstate commerce in a substantial way."[24]

Further, courts endorse the notion that arbitration agreements must be broadly interpreted, as a narrow reading of the agreements would hinder the strong federal policy encouraging arbitration.[25] Put differently, the agreement must be read in favor of the agreement's enforceability. The Fourth Circuit put it well in *American Recovery*: "we may not deny a party's request to arbitrate an issue unless it may be said with positive assurance that the arbitration clause is not susceptible of an interpretation that covers the asserted dispute."[26]

4 Equitable Estoppel / Third Party Beneficiary Arguments

In many instances, particularly in the health care industry, an arbitration agreement might be signed not by the plaintiff, but instead by her power of attorney, attorney-in-fact, next friend,

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[21] *See Citizens Bank v. Alafabco, Inc*., 539 U.S. 52 (2003) (per curiam).
[22] *Id*. at 56-57.
[23] *Id*. at 56.
[24] *Id.* at 57; *See also See, e.g., Fosler v. Midwest Care Ctr. II, Inc*., 928 N.E.2d 1, 14-15 (Ill. Ct. App. 2010) (relying on affidavit filed by nursing facility's administrator demonstrating that, among other things, the nursing facility received Medicare payments for the resident's treatment and purchased medical equipment from out-of-state vendors); *Ruszala ex rel. Mizerak v. Brookdale Living Cmtys., Inc*., 1 A.3d 806, 817 (N.J. Super. Ct. App. Div. 2010) (relying on affidavit submitted by in-house counsel for the healthcare facilities, which explained that the facilities purchased food, medicine, and medical equipment primarily from out-of-state vendors); *Bales v. Arbor Manor*, No. 4:08-CV-3072, 2008 WL 2660366, at *6 (D. Neb. July 3, 2008) (finding requisite nexus with interstate commerce); *Rainbow Health Care Ctr., Inc. v. Crutcher*, No. 07-CV-194-JHP, 2008 WL 268321, at *5 (N.D. Okla. Jan. 29, 2008) (same).
[25] *American Recovery Corp. v. Computerized Thermal Imaging, Inc.,* 96 F.3d 88 (4th Cir. 1996) (explaining that courts will read a narrow arbitration clause to be broader).
[26] *Id. (*citing *Warrior & Gulf Navigation Co*., 363 U.S. at 582-83, 80 S.Ct. at 1353)(internal citations omitted).

or other "representative." The first step is to look to the language of the arbitration agreement itself; often, it will state that the parties intend not only to bind themselves to the agreement, but also their heirs, successors, and all representatives. If you find yourself in this situation, you should assert that "[a]rbitration agreements, like other contracts, are enforceable in accordance with their terms."[27]

In addition, you also may argue that Plaintiff must arbitrate her claims because she was an intended third-party beneficiary of the Arbitration Agreement. While the language differs from state to state, a third-party beneficiary is a party that the contracting parties intended to directly benefit.[28] The "benefit" confirmed upon a third party can be the remedy of arbitration itself.[29] In the healthcare arena, the argument often can be made that the patient receives the benefit of medical care, as the patient would not have been admitted to the healthcare facility without first signing the arbitration agreement.[30]

In addition to raising the "third party beneficiary" sword, a defendant moving for arbitration in a situation where a representative of the plaintiff signed the arbitration agreement can argue that the plaintiff must arbitrate the claims pursuant to the equitable estoppel doctrine.[31] Explaining that "[w]ell-established common law principles dictate that in an appropriate case a nonsignatory can enforce, or be bound by, an arbitration provision within a contract executed by

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[27] *Munoz v. Green Tree Fin. Corp.,* 343 S.C. 531, 539, 542 S.E.2d 360, 364 (S.C. 2001) (*quoting Volt Info. Sciences, Inc. v. Bd. Of Trustees of Leland Stanford Jr. Univ.*, 489 U.S. 468, 476 (1989)).
[28] *See Helms Realty, Inc. v. Gibson-Wall Co*., 363 S.C. 334, 611 S.E.2d 485, 488 (S.C. 2005); *Edwards v. Costner*, 979 So. 2d 757 (Ala. 2007); *Cont'l Cas. Co. v. Am. Nat. Ins. Co*., 417 F.3d 727 (7th Cir. 2005); *McCutcheon v. THI of S.C. at Charleston, LLC*, No. 2:11-CV-02861, 2011 WL 6318575, at *3 (D.S.C. Dec. 15, 2011) (Norton, C.J.); *THI of S.C. at Columbia, LLC v. Wiggins*, C/A No. 3:11-888-CMC, 2011 WL 4089435, at *6 (D.S.C. Sept. 13, 2011) (Currie, J.); *see also THI of N.M. at Hobbs Center, LLC v. Patton*, Civ. No. 11-537 LH/CG, 2012 WL 112216, at *8-9 (D.N.M. Jan. 3, 2012) (following *Wiggins* and similar decisions from other jurisdictions applying analogous third-party beneficiary law).
[29] *Larsen v. First Bank*, 245 Neb. 950, 962, 515 N.W. 2d 804, 813 (Neb. 1994) (citing *Alder v. First Nat. Bank & Trust Co.*, 241 Neb. 873, 491 N.W.2d 686 (1992)); *Lauritzen v. Davis*, 214 Neb. 547, 335 N.W.2d 520 (1983); *Dworak v. Michals*, 211 Neb. 716, 320 N.W.2d 485 (1982)).
[30] *See Id.*
[31] *International Paper Co. v. Schwabedissen Maschinen & Anlagen GMBH*, 206 F.3d 411, 418 (4th Cir. 2000).

other parties," the Fourth Circuit compelled the parties to arbitration under the doctrine of equitable estoppel:

> We believe that the doctrine of equitable estoppel applies here. Equitable estoppel precludes a party from asserting rights he otherwise would have had against another when his own conduct renders assertion of those rights contrary to equity. In the arbitration context, the doctrine recognizes that a party may be estopped from asserting that the lack of his signature on a written contract precludes enforcement of the contract's arbitration clause when he has consistently maintained that other provisions of the same contract should be enforced to benefit him. To allow [a plaintiff] to claim the benefit of the contract and simultaneously avoid its burdens would both disregard equity and contravene the purposes underlying enactment of the Arbitration Act.[32]

C. *The State Court Motion to Stay*

In addition to asking the federal court to stay all state court proceedings via your federal complaint, a motion to stay the state court proceedings pending the outcome of the federal suit also should be filed in state court at the same time the federal suit is brought. This motion should explain that the defendant has filed an action in the District Court to determine the validity of an arbitration agreement entered into between the parties. Be sure to ask the state court to stay the case until the district court has made a final decision *and* the appellate process (if any) has been exhausted. Section 3 of the FAA, entitled "Stay of proceedings where issue therein referable to arbitration," states the following:

> If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

[32] *Id.* at 417-18 (internal citations and quotations omitted).

Citing this statutory provision, courts have held the "FAA clearly requires a court stay 'any suit or proceeding' pending the arbitration of 'any issue referable to arbitration under an agreement in writing for such arbitration' upon the application of one of the parties."[33] Filing this state court motion to stay is not "overkill" despite the fact that you have already asked the federal court to stay the state proceedings. By filing the state court motion, you are effectively closing another one of the plaintiff's lawyer's "doors" for making a waiver argument.

As stated ad nauseum, both federal and state policy favors the arbitration of disputes. Even when a party to the lawsuit is not a party to the arbitration agreement, it "may be advisable to stay litigation among the non-arbitrating parties pending the outcome of the arbitration."[34] Both state and federal courts also possesses inherent authority to issue a stay, and the decision to stay a case for the non-arbitrating parties is left to a court's discretion.[35]

II. THE STATE COURT APPROACH

You also have the option of attempting to enforce the arbitration agreement in state court instead of federal court. There are good reasons to consider this approach if the judge in your jurisdiction are open to arbitration. Maybe the state where you practice already has a strong history of enforcing arbitration agreements. Maybe you are uncomfortable with the idea and cost of filing a federal suit against a state court plaintiff. Maybe you simply do not want to engage in ancillary federal court litigation and bear those expenses when you already are in state court.

All are valid grounds for deciding to move to compel arbitration in state court. Instead of filing a complaint against the plaintiff, you simply would move to dismiss the plaintiff's

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[33] *Stokes v. Metro. Life Ins. Co*., 351 S.C. 606, 612, 571 S.E.2d 711, 715 (Ct. App. 2002).
[34] *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp*., 460 U.S. 1, 21, 103 S. Ct. 927, 939 (1983).
[35] *Id. See also, Landis v. N. Am. Co*., 299 U.S. 248, 254-255, 57 S. Ct. 163, 166 (1936)("[T]he power to stay proceedings is incidental to the power inherent in every court to control the disposition of the causes on its docket with economy of time and effort for itself, for counsel, and for litigants. How this can best be done calls for the exercise of judgment, which must weigh competing interests and maintain an even balance.").

complaint in state court on the basis that there is an enforceable arbitration agreement under the FAA for the same reasons cited above. After all, the FAA and its expression of the federal policy favoring arbitration are binding in state courts, too.[36] If you decide to pursue the state court approach, be sure to follow the same basic steps set forth in Section I above, including sending the Plaintiff a letter demanding arbitration. After the demand letter is rejected, simply file your Motion to Dismiss Plaintiff's Complaint, Enforce Arbitration, and Stay State Court Proceedings in state court based upon the application of the FAA described above.

III. THE NON-JURY ROUTE—APPRECIATION OPTION?

Finally, it may be a viable option to have your case heard by a judge in a non-jury trial. This route can be appealing to all parties. First, it allows the dispute to be heard by a sophisticated neutral whose credibility presumably is beyond reproach. The trial will proceed pursuant to your state's tried and true evidentiary and procedural rules, which all the parties will be familiar with and comfortable. Finally, it can be cheaper option for both parties: neither party will have to carry the costs of paying an arbitrator; instead, you only will be subject to your state's applicable court filing fees and the traditional costs of litigation. You also can avoid a long fight about the selection of an arbitrator.

This route can potentially benefit the defense in many similar ways that arbitration does. First, it affords the advantage of avoiding the "runaway jury" scenario. However, a liked judge could become a plaintiff's best friend. Next, the non-jury option may be worthy of consideration if you believe you have a strong summary judgment argument, as the judge will be familiar with or can be quickly educated by the parties as to the applicable law and more inclined to seriously consider pre-trial dispositive motions. On the other hand, a non-jury trial likely will not provide the same level of privacy that an arbitral proceeding would, and it also will also give

[36] *Zabinski v. Bright Acres Associates*, 346 S.C. 580, 590, 553 S.E.2d 110, 115 (2001).

both sides the full right of appeal not preset in arbitration. Additionally, the non-jury route may give better evidentiary protection than an arbitrator who will have to see the adverse evidence in order to exclude it.

To utilize this approach you of course must have the agreement of plaintiff's counsel. The state circuit judge then will need to order that the case be removed from the jury roster and placed on his or her non-jury roster. This is usually done by consent order. Some judges may be loath to do so, as it likely will require more "intellectual work" on their part then a standard jury trial. Accordingly, the non-jury option should be explored only when the case is particularly complex and where its legal issues conceivably may overwhelm the arbitrator.

ARBITRATION PROCEDURES BEFORE AND AT TRIAL

Now that you have successfully compelled arbitration, what procedure must you follow in actually arbitrating the case? The first step is to look to the text of the arbitration agreement. Many agreements will specify that the rules of certain arbitration programs will apply to all proceedings. For example, arbitration agreements in the healthcare arena often mandate that the American Health Lawyers Association's (AHLA) arbitration program or the American Arbitration Association (AAA), Judicial Arbitration and Mediation Service ("JAGS") or the National Arbitration Forum ("ARF") and their attendant rules and procedures will apply to the arbitration. Each will have its own unique set of rules. Read then rules. In addition to having their own set of procedural and evidentiary rules, these organizations have their own cadre of appointed neutrals, electronic filing systems, and fee schedules. You must read these rules and decide if it makes sense to use all of them. You and opposing counsel are free to make

agreements related to the use of the rules. If you do go make sure you confirm any changes in writing and serve a Consent Order from your arbitrator.

Many arbitration agreements will not mandate that a particular organization be used to arbitrate your case. Instead, many arbitration agreements will simply state that the federal rules of civil procedure or your state's respective procedural rules govern the dispute. However, and as more fully discussed below, such provisions are not always set in stone and the rules of civil procedure (especially those regarding discovery) sometimes can be "bent" to your advantage.

Also, such arbitration agreements invariably include a provision regarding the manner in which the arbitrator(s) are selected. These provisions come in various iterations. Sometimes they require that the parties must select one arbitrator by agreement and, if no agreement can be reached, that a state court judge appoint an arbitrator of its choosing. More often, the provision will ask each party to select an arbitrator. Those arbitrators in turn will in turn select a third arbitrator with that group serving as your arbitration panel.

Finally, always remember that arbitration is a matter of contract between the parties. After the arbitration agreement is enforced by the court, consider sitting down with plaintiff's counsel and explore the idea of reaching a post-arbitration agreement that is outside of the four corners of the arbitration document itself. Maybe each party wants to engage in full, traditional discovery and have a panel of arbitrators decide the case instead of the number called for by the arbitration agreement. Maybe the parties want to limit the number of witnesses to be called during the arbitral proceedings. If the parties can reach an agreement, put it in writing and have the arbitration operate under your own terms.

I. PICKING YOUR ARBITRATOR(S)

The selection of a fair arbitrator with knowledge of the subject matter of your dispute is essential to your case. This can also be a difficult and time consuming process. In the event that the arbitration agreement calls for the selection of one arbitrator per party (with those arbitrators then selecting the third), you must select a lawyer with strong, defense-oriented credentials. Plaintiff's attorney, of course, will select an equally plaintiff-oriented lawyer. Your neutral must understand the selection of the third is critical. When the two arbitrators confer to select a third member of the panel, your selection must serve as a favorable ally capable of convincing the Plaintiff's selection to agree to a truly neutral third arbitrator to round out your panel. Further, ensure that none of the arbitration panel has a potential conflict of interest. If your selection has some connection to the parties to the dispute or your clients, plaintiff's counsel likely will petition the court or the other arbitrators to have the arbitrator removed. On the flip side, if plaintiff's selection has any connection to the plaintiff's litigation – such as previously serving as co-counsel with the plaintiff's lawyer in some past matter – you always have the option of petitioning to have the arbitrator removed as well.

As noted above, arbitration agreements often call for the parties to come to an agreement as to who will serve as the *sole* arbitrator. Be realistic in your proposal of an arbitrator; your opponent almost certainly will not agree to a lawyer practicing exclusively defense work adjudicating the dispute. Remember that in the event that the parties cannot reach an agreement as to who will serve as the arbitrator, it likely will be a state judge who will appoint the arbitrator. Having a judge select the arbitrator does not guarantee that the selection will be to your liking or help advance your case. Work with opposing counsel and try to keep control of the selection process if at all possible.

I. DISCOVERY UNDER THE FAA

One of arbitration's great benefits to the client is the ability to limit discovery and the costs associated therewith. The text of the Federal Arbitration Act (again, referred to herein as the "FAA" or the "Act") reflects the overarching principle that arbitration is a matter of private contract and, consistent with that text, courts must rigorously enforce arbitration agreements according to their terms.[37] Consequently, parties may contract to provide for as expansive or limited discovery as they desire. Assuming no overreaching by a party, coercion, or duress, the courts should respect what the party's contract for in terms of discovery.[38] Indeed, the FAA does not prevent enforcement of agreements to arbitrate under different rules than those set forth in the Act itself, so long as the rules do not undermine the goals and policies of the FAA to ensure the enforceability, according to their terms, of private agreements to arbitrate.[39]

As emphasized above, parties can contract for as much or little discovery as they wish. The FAA and its limited discovery provision will apply if the parties' agreement involves commerce or if the parties have elected to use another law that is preempted by the FAA.[40] They also will apply when no other set of discovery rules are agreed upon by the parties or set by the organization that is handling the arbitration (such as the AHLA or JAMS, discussed above). Within the FAA, § 7 governs discovery and allows arbitrators to punish the failure to obey a discovery directive. In pertinent part, § 7 reads:

> The arbitrators may summon in writing any person to attend before them or any of them as a witness and in a proper case to bring with them any book, record, document, or paper which may be deemed material as evidence in the case…Said summons shall issue in the name of the arbitrator or arbitrators…and shall be

[37] *Am. Exp. Co. v. Italian Colors Rest.,* 133 S. Ct. 2304 (Scalia, J) (2013); 9 U.S.C.A. § 2
[38] *Continental Airlines, Inc. v. Mason*, 87 F.3d 1318 (9th Cir. 1996).
[39] *Osteen v. T.E. Cuttino Constr. Co.*, 315 S.C. 422, 434 S.E.2d 281 (1993).
[40] 9 U.S.C.A. § 1-14. The language "involving commerce" is to be broadly interpreted. *Allied-Bruce Terminix Co. v. Dobson*, 513 U.S. 265, 273-78 (1995).

> directed to the said person and shall be served in the same manner as subpoenas to appear and testify before the court.
>
> …
>
> If any person or persons so summoned to testify shall refuse or neglect to obey said summons, upon petition the United States district court for the district in which such arbitrators…are sitting may compel the attendance of such persons before said arbitrator...in the same manner provided by law for securing the attendance of witnesses…for neglect or refusal to attend in the courts of the United States.

No other FAA provision discusses discovery, and discovery is thus clearly limited. To be sure, parties to a private arbitration agreement pass on "certain procedural rights attendant to formal litigation in return for a more efficient and cost-effective resolution of their disputes."[41] A hallmark of arbitration is a limited discovery process.[42] Indeed, parties to a private arbitration agreement "relinquish the right to certain procedural niceties which are normally associated with a formal trial…one of these accoutrements is the right to pre-trial discovery."[43] Put differently, the "essence of arbitration is its freedom from the formality of ordinary judicial procedure."[44]

A. *Document and Deposition Discovery*

1. Discovery Regarding Non-Parties

Document and deposition discovery under § 7 is an issue that has divided the federal appellate circuits. The Fourth Circuit allows document and deposition discovery, but only in limited circumstances.[45] In *COMSAT*, the Fourth Circuit held that § 7 does not grant arbitrators the power to order pre-hearing depositions or document discovery against non-parties absent a showing of "special need or hardship" by the party seeking discovery.[46] Instead, § 7 empowers arbitrators to compel appearance and the production of documents only at the hearing itself. This

[41] *See Burton v. Bush*, 614 F.2d 389, 390-91 (4th Cir. 1980).
[42] *Id.* at 391.
[43] *Burton*, 614 F.2d at 391.
[44] *Harvey Aluminum, Inc. v. United Steelworkers of Am., AFL-CIO*, 263 F. Supp. 488, 491 (C.D. Cal. 1967) (quoting *Canuso v. City of Philadelphia*, 326 Pa. 302, 307, 192 A. 133, 136).
[45] *COMSAT Corp., v. National Science Foundation*, 190 F.3d 269, 275 (4th Cir. 1999).
[46] *Id.* at 275-78.

narrow reading was based on the Court's understanding that the FAA, by its plain language, does not authorize pre-hearing discovery against non-parties. The Court explained that this limited discovery process is fundamental to ensuring that arbitration remains an efficient alternative to courtroom litigation.

The *COMSAT* Court did not define what constitutes a "special need," opting instead to create only a floor: "at a minimum, a party must demonstrate that the information it seeks is otherwise unavailable."[47] Since *COMSAT* was decided and at the time of this writing, only one district court in the Fourth Circuit has considered § 7 and its "special need" standard. In *Gresham v. Norris*, a former employee who brought suit for alleged sexual harassment, wrongful discharge, and various other torts petitioned the district court to compel attendance of a witness at a deposition in connection with a mandatory arbitration proceeding.[48] The Respondent was not a party to the arbitration proceeding, but the Petitioner believed Respondent was a witness to conduct underlying her claim and also was a victim of sexual harassment at the hands of the same employer. Respondent was subpoenaed by Petitioner, and Respondent refused to honor the subpoena. The District Court held that the petition did "not include the requisite showing of special need or hardship."[49] Recognizing the *COMSAT* decision, the District Court wrote that the Fourth Circuit was clear in its ruling that a petitioner's "special need" must be "more than simply a general desire to conduct discovery."[50] The Petition to Compel therefore was denied, with the District Court noting that FAA still allowed the arbitrator to issue a subpoena requiring the Respondent to testify at the arbitration hearing. *Id.*

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[47] *Id.* at 276.
[48] 304 F.Supp, 2d. 795 (ED Va. 2004)
[49] *Id.* at 275.
[50] *Id.* at 276.

Our federal appellate courts are not consistent in their interpretation of the FAA's discovery provision. Unlike the Fourth Circuit, the Eighth Circuit allows document discovery from non-parties and does not have a "special need" standard.[51] In *Security Life Ins. Co.*, the Court reasoned that arbitral efficiency is furthered when the parties can review and digest documentary evidence before the arbitration hearing, though deposition discovery was not allowed. The Sixth Circuit likewise suggested that the FAA implicitly permits arbitrators to subpoena documents prior to a hearing.[52]

In contrast, the Second and Third Circuits do not allow any document discovery.[53] Both Courts explained that the language of § 7 is straightforward and clearly does not allow arbitrators to issue pre-hearing subpoenas for documents or depositions to non-parties. *Life Receivables* even went so far as to state that arbitrators cannot order third party production even when the third party is related to a party or a signatory of the arbitration agreement.

B. *Enforcing a Subpoena Issued to a Non-Party*

The next discovery oddity in arbitration proceedings regards enforcing a subpoena issued to a non-party. The FAA mandates that subpoenas be issued only by an arbitrator and can be enforced by the court in the federal district where the arbitrator sits.[54] Case rulings concerning this issue are very conflicting—particularly because the FAA does not contain a Federal Rules of Civil Procedure Rule 45 objection/protective order requirement. As such, a non-party witness

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[51] *In re Security Life Ins. Co. of America*, 228 F.3d 865, 870-71 (8th Cir 2000).
[52] *American Federation of Television and Radio Artists, AFL-CIO v. WJBK*-TV, 164 F.3d 1004, (6th Cir. 1999).
[53] *Hay Group, Inc. v. EBS Acquisition Corp*., 360 F.3d 404, 408 (3d Cir. 2004); *Life Receivables Trust v. Syndicate 102 at Lloyd's of London*, 549 F.3d 865, 870-71 (2d Cir. 2008).
[54] 9 U.S.C.A. § 7.

may choose to ignore the subpoena.[55] The FAA does permit a party to seek enforcement of a subpoena from a federal court in the district which the arbitration is pending.[56]

The issue becomes tricky when the witness, for example, is located in Pennsylvania but your arbitration proceeding is taking place in Chicago. That exact issue was considered in *Agmen, Inc. v. Kidney Center of Delaware County, Ltd.*, 1994 WL 594372 (E.D. Pa. 1994). There, Amgen was a party to an arbitration being held in Chicago, and it filed a motion to compel compliance with a subpoena issued to a non-party witness located in the Eastern District of Pennsylvania. The Pennsylvania district court held that Amgen filed its motion in the wrong district: "[s]ince the arbitrator in the underlying arbitration is sitting in Chicago, it was incumbent upon Amgen, pursuant to the plain language of Section 7 of the Federal Arbitration Act, to bring its petition to compel compliance in the United States District Court for the Northern District of Illinois."

When Amgen presented its motion to the district court in Chicago, it faced a new and different problem. The Court held that under § 7, an arbitrator sitting in Chicago had no more power to issue and enforce a subpoena issued to a person located in the Eastern District of Pennsylvania than did a district court in the Northern District of Illinois. The Court asserted that the district court in the Northern District of Illinois could issue and enforce a subpoena to a person within (a) the Northern District; (b) 100 miles of the Northern District; or (c) any place in Illinois where Illinois law permits service of subpoenas. Neither the Northern District of Illinois nor the arbitrator, however, could issue or enforce a subpoena directed to a witness located in Pennsylvania. This is quite the limitation.

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[55] *COMSAT Corp.*, 190 F.3d at 276.

[56] If any person or persons so summoned to testify shall refuse or neglect to obey said summons, upon petition the United States district court for the district in which such arbitrators…are sitting may compel the attendance of such persons before said arbitrator...in the same manner provided by law for securing the attendance of witnesses…for neglect or refusal to attend in the courts of the United States. 9 U.S.C.A. § 7.

Under Rule 45 of the Federal Rules of Civil Procedure, a party who has filed suit in in one state can serve a subpoena on a witness located in some other judicial district or state, so long as the subpoena issues from the district court in which that witness is located and any enforcement proceedings are brought in the district where the witness is located. Under § 7, however, arbitrators can issue subpoenas only from the federal district in which they are sitting, and they must bring any action to enforce their subpoena in that district. Thus, if the witness is located in a judicial district or state other than the one where the arbitrators sit, they have no power to issue or enforce a subpoena served on that witness.

Since *Agmen*, two circuit courts have considered the geographic limits on subpoenas and reached different conclusions. In *Security Life*, the Eighth Circuit ruled that the territorial limitation in Rule 45 does not apply to subpoenas for documents issued by arbitrators.[57] The Second Circuit took a wholly different approach in *Dynegy Midstream Services, LP v. Trammochem*, 451 F.3d 89, 94 (2d Cir. 2006). It asserted that § 7 specifically states that arbitrators' subpoenas are to be "served in the same manner as subpoenas to appear and testify before the court." By way of example, the Court explained that a district court in the S.D.N.Y. could not issue a subpoena to a witness in Houston, and likewise an arbitrator sitting in the S.D.N.Y. could not do so either.

Practically, most parties to arbitration will want some ability to issue subpoenas. If possible, see if the opposing party will argue to issue subpoenas under the state court action (if there was one) prior to an order compelling the case to arbitration. A consent order allowing subpoenas by consent may be an effective tool for both sides' efforts to secure third party documents.

[57] 228 F.3d at 868.

C. *Role of the Court in Arbitration Discovery*

Courts generally take a "hands-off" approach when it comes to discovery conducted in arbitration.[58] They do not appear eager to interfere with the arbitration proceeding or the role of the arbitrator in controlling discovery.[59] Occasionally, a court even will interpret a party's use of the court for discovery purposes as a waiver of the right to arbitrate the dispute.[60] Therefore, it is rare that a party to arbitration will find adequate relief from the court when it is unhappy with an arbitrators' decision regarding some aspect of discovery.

There are times, however, when a court will interfere in an arbitration's discovery dispute. The federal courts will do so only in "extraordinary circumstances," such as when the evidence likely will be lost if discovery does not occur right away. The "extraordinary circumstances" standard is difficult to meet, however, and the federal courts generally maintain their policy of not interfering with arbitration.[61]

D. *A Common Argument Against Limited Discovery*

Given the limited discovery inherent in arbitrations, a party often will squirm to find some loophole allowing for more traditional, trial-like discovery. One clever tactic is for a plaintiff to argue that either the federal or applicable state rules of civil procedure should govern the arbitration proceedings as a whole, as the rules would act as an appropriate guideline as to motions practice and the resolution of discovery disputes. Accompanying that argument likely will be standard interrogatories and requests for production

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[58] *See, e.g. Fueling Advanced Technologies v. Ford Motor Co.*, 1997 WL 733897 (N.D. Ill.) (holding that there is no basis for compelling the parties to engage in pre-arbitration discovery above and beyond what was already agreed to by the parties).
[59] *See Thompson v. Zavin*, 607 F.Supp, 780, 783 (C.D. Cal. 1984) (holding that once there is a stay of proceeding pending arbitration, the court will not interfere with arbitrators' decisions).
[60] *See* Joseph L. Forstdadt, Discovery in Arbitration, ADR & THE LAW 52 (20th ed., 2006).
[61] *See Id.*

A defense attorney seeking to limit discovery should reply that the rules of civil procedure are applicable only where the FAA is silent as to a procedural issue.[62] As stated, *supra*, the FAA contains its own discovery procedure; accordingly, a party who elects to arbitrate may not simultaneously invoke the normal discovery procedures used in courts.[63] Discussing the issue of whether oral depositions may be taken and interrogatories going to the merits of the case can be propounded in matters referable to arbitration, the federal court for the Southern District of New York ruled that:

> By voluntarily becoming a party to a contract in which arbitration was the agreed mode for settling disputes thereunder respondent chose to avail itself of procedures peculiar to the arbitral process rather than those used in judicial determinations. 'A main object of a voluntary submission to arbitration is the avoidance of formal and technical preparation of a case for the usual procedure of a judicial trial.'[64]

You should be prepared to explain that arbitration, by its very nature, does not lend itself to discovery outside the parameters set by § 7: "[t]he fundamental differences between the fact-finding process of a judicial tribunal and those of a panel of arbitrators demonstrate the need of pretrial discovery in the one <u>and its superfluity and utter incompatibility in the other</u>."[65] As Judge Learned Hand eloquently stated,

> when [parties] have adopted [arbitration], they must be content with its informalities; they may not hedge it about with those procedural limitations which it is precisely its purpose to avoid. They must content themselves with looser approximations to the enforcement of their rights than those that the law accords them, when they resort to its machinery.[66]

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[62] *Application of Deiulemar Compagnia di Navigazione S.P.A. v. M/V Allegra*, 198 F.3d 473, (4th Cir. 1999).
[63] *See* 9 U.S.C. § 7.
[64] *Penn Tanker Co. of Del. v. C. H. Z. Rolimpex, Warszawa*, 199 F. Supp. 716, 718 (S.D.N.Y. 1961) (quoting 1 Wigmore, Evidence § 4(e) (3d ed. 1940
[65] *Commercial Solvents Corp v. Louisiana Liquid Fertilizer Co*, 20 F.R.D. 359, 362 (S.D.N.Y. 1957) (emphasis added).
[66] *Am. Almond Products Co. v. Consol. Pecan Sales Co.,* 144 F.2d 448, 451 (2d Cir. 1944).

Finally, a defense attorney attempting to limit discovery should argue that arbitrators alone are afforded the power to conduct discovery by calling witnesses and subpoenaing tangible evidence and documents. 9 U.S.C. § 7. This power is not extended to the parties to the arbitration.[67] Put simply, because an arbitrator controls discovery pursuant to the strictures of § 7, Plaintiff thus has no right to serve discovery requests upon Defendants.

CONCLUSION

The use and popularity of arbitration agreements in the healthcare and professional liability settings is on the rise. These agreements are generally disliked by the plaintiff's bar, and the national media has recently investigating their effect on ordinary citizens.[68] Defense lawyers need to be able to educate their client on the pros and cons of arbitration agreements, and they must be prepared to enforce them if deemed appropriate. They can be effective tools for defense counsel, but can also be ripe with traps for the unwary. Please feel free to contact the authors with any questions, concerns, or suggestions.

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[67] *Burton*, 614 F.2d at 390-91; *CIGNA HealthCare of St. Louis, Inc. v. Kaiser*, 294 F.3d 849 (7th Cir. 2002) ("[F]or the sake of economy and in contrast to the practice in adjudication, parties to an arbitration do not conduct discovery; the arbitrators do").

[68] *See* Jessica Silver Greenberg and Robert Gebeloff, Arbitration Everywhere: Stacking the Deck of Justice, NEW YORK TIMES (October 31, 2015)
http://www.nytimes.com/2015/11/01/business/dealbook/arbitration-everywhere-stacking-the-deck-of-justice.html?_r=0
Suing a Nursing Home Could Get Easier Under Proposed Federal Rules – National Public Radio
http://www.npr.org/sections/health-shots/2015/10/19/449957318/suing-a-nursing-home-could-get-easier-under-proposed-federal-rules

HOW TO AVOID A SHIPWRECK

Trial Masters Program
FDCC Winter Meeting
San Diego, California
March, 2016

Sandra Clark, MehaffyWeber
Rob Adams, Shook Hardy & Bacon

A civil trial is well-planned from voir dire through closing argument. Prior to the trial there is usually a comprehensive discovery plan that develops the facts and legal issues that will govern the case. A good trial attorney and his team prepare and organize the case carefully so what could go wrong? What lies below the surface of the icy water that presents a possible hazard to a case? Any case can develop unique problems that must be dealt with as effectively as possible to keep from sinking the ship.

Part of this year's Trial Masters Program includes presentations from five excellent FDCC trial attorneys. These attorneys provide a variety of experience and expertise and will address how to deal with problems in trial and how to keep them from torpedoing your case. You will hear from them concerning real litigation examples. This paper deals with some hazardous "icebergs" that often arise in a civil case no matter how well prepared. This paper and the Trial Masters Program provide suggestions for dealing with those hazards. Such as, how do you handle bad facts, bad documents or bad witnesses, how important is opening statement to the overall case and how early does bad news need to be revealed? Can the use and placement of witnesses in a trial impact the outcome of the case? What can the trial attorney do to salvage a bad witness? How do you prepare a witness to be called as an adverse witness? What if the witness when called out of turn gets flustered on the stand and makes incorrect statements or simply cannot remember facts? What if the witness is not likeable or not very credible or has a "deer in the headlights" look. What if he is intimidated and shrinks into the witness chair before the very eyes of the jury?

Attorneys know that expert witnesses are crucial in most cases. There are practiced and highly compensated experts who participate in trial to help the plaintiff win. Plaintiffs put on their experts first, and if those experts do a good job in developing plaintiff's case, the jury could be convinced before you call a witness. Cross examination of experts should either discredit an expert or bolster your own witness. Cross examination of expert witnesses can be the most crucial component of a trial. Whichever side does the most effective job of cross will probably win the case.[1] There is no magic formula for cross-examination of plaintiff's primary expert? How do you discredit a major expert on cross? Conversely, can you make an opposing expert your own by supporting your theory of the case? Can you prevent having plaintiffs turn your expert into their expert?

[1] Weiner, Monique, "Thinking Outside the Science – Strategies for Cross Examining the Technical Expert," DRI Toxic Torts and Environmental Law, October 2009.

Finally, how do good trial lawyers use closing argument to end on a strong note? How does a trial attorney deal with the issue of damages, the jury charge, the weaknesses in his case? These issues are not the only ones in a trial, but if not handled skillfully, any of them could sink the ship.

I. ANCHORS AWEIGH: OPENING STATEMENT

Opening statement should be short, to the point and should be an attention getter – it is crucial for the defense of a civil case.[2] In some jurisdictions it is the first time the attorneys speak directly to the jury. (Voir Dire is widely variable – from being conducted solely by the court to being conducted individually by the attorneys.) Opening statement is the time to introduce the theme of the case, it is the time to pique the jury's interest by developing the story of the case, and it is the time to establish a chronology to set out important facts in a logical convincing way. Opening statement is not the time to waste time, it is not the time to use clichés, and it is not the time to fawn over the jury. The theme should have been established and the defense case should be about something.[3] It should not be merely reactive. Don't introduce yourself again, don't explain how opening statements work. Especially don't waste the key time in which you have the jury's complete attention.[4]

Studies have shown that the jury has made up its mind in the majority of cases by the end of opening statements. It would be a huge gamble and probable mistake for a defendant to defer its opening until its case in chief. Opening later in the case is often too little too late. By the end of opening the defense attorney should have established credibility and rapport with the jury, developed the theme of the case and established the chronology of events that set in motion a defense verdict.[5]

Q: Is opening statement the time and place to acknowledge bad facts, documents or witnesses in your case?

A. Points to consider in dealing with the bad news:

- How important are the bad details?

  If these bad facts are not critical to the case, one approach is not to mention them in the limited time of opening, and to deal with the specific facts or documents as they come up. Another approach even with a critical issue is to place it in the middle of opening with stronger points on either side so that the bad facts are not overly emphasized. Most pretrial hearings will have determined whether these

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[2] Melilli, Kenneth, "Succeeding in the Opening Statement," 29 Am. J. Trial. Advoc. 525

[3] *See* J. Ric Gass "Attacking Damages in the Catastrophic Injury Case, Part II," For the Defense, March 2003.

[4] Wilcox, Elliott "Punch Your Jurors in Mouth During Opening Statement." Wilcox publishes Trial Tips Newsletter.

[5] Melilli, *Supra*.

facts/documents will be admitted so the attorney knows that the facts/documents will be in evidence. Likely the plaintiff's counsel will mention it on opening. Again the decision is based on the analysis of how much attention do you give to a detail that may or may not be that important either to liability or damages.[6]

- Are these bad facts documents or witnesses too significant to ignore or postpone?

  If so, then you should bring them up, try your best to explain and put them into context. If you do not acknowledge an important negative issue in opening, your credibility may be shot by trying to explain later. For example, if your client breached a contract, explain that the other side breached it first. If your employee wrote a damaging memo, explain his motives for doing so. If a key witness left the accident scene, explain that he was distraught, could not render aid and was trying to find help, or was just a coward in the face of a terrible accident.

- If the bad evidence is so bad that there is nothing positive to say about it, and no way to diffuse it, you should keep it in the context of the timeline of the case, mention it and move on with more positive facts.[7]

The bad memo from a disgruntled employee may seem devastating at first, but addressing it early on and putting it in context, if possible, can minimize the damage. It then becomes a strategic question for plaintiff's attorney who may over use it. The jury may conclude that it is not a key piece of evidence and may decide that it was used primarily to prejudice your case.

In a case in which there are dramatic or even tragic photographs, it is better to address them as soon as possible to reduce the impact of the photographs as the case progresses.

B. Is opening statement the time to criticize plaintiff's case?

A general rule is not to interrupt the flow of your story and theme by attacking details of the plaintiff's case. Of course, there are exceptions and certain points may need to be addressed but likely these could be raised in your story development. To criticize plaintiff's opening could easily be a distraction and could cause confusion to the jury and may add to emphasize the plaintiff's version of the facts.[8]

Opening statement cannot be minimized. It may be the most important part of a trial. Before you give an opening statement, you should have prepared the closing argument. It should be clear from the beginning what verdict you want the jury to return.[9] So that there is no question at any part of the trial of what the result should be. It may not be a good idea to spend

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[6] *Id*
[7] *Id.*
[8] *Id.*
[9] *Id.*

much time on damages (except in a strong liability case against you) other than to establish that damages were not caused by the defendant.[10] [11]

II. HEART OF THE VOYAGE – CHOPPY WATER OF WITNESSES

A. Prepare your corporate representative and/or key fact witnesses for their role.

Because these fact witnesses will very likely be deposed prior to the trial you need to have a clear plan for what each person's role is in developing the corporate story. Try not to put too big a burden on any inexperienced witnesses. Any one of them may do a poor job on deposition or at trial so depending too much on any one of them can seriously damage your case.

How do you prepare an inexperienced corporate representative or fact witness?

- Prepare, prepare, prepare. Often a client does not like the disruption caused by the time it takes to prepare these witnesses, but this time is essential.
- Make sure the witness is familiar with all the important documents that he needs to proffer or that he may be crossed about.
- Have him review all exhibits you expect him to encounter in the case.
- If possible, choose a witness who is intelligent, credible and likeable.[12]
- Do everything possible to humanize the witness; the corporate representative or significant fact witness may be the face of the company at trial.
- Work on presentation style including verbal and non-verbal communication[13]
- Try to develop the witness' confidence; remember very few individuals enjoy the stress of being a company witness.
    - Explain the process, the logistics, practice with video.
    - Be patient.
    - Illustrate the need for proper dress, for speaking clearly.
    - Emphasize that his testimony can be used at trial so the deposition is crucial.

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[10] Morrow, James C. "Opening Statement from the Defense Perspective"
[11] *See* also Sullivan, William F. and Reich, Adam M. "Opening Statements: Tips for Effectiveness in 15 Minutes or Less."
[12] Luma, Claire "What to Do with Disaster Drivers: Rehabilitating Witness After Deposition Disaster," Trucking Law, June 2014, 8-6.
[13] *Id.*

- Make sure the witness appears comfortable. Remind him it is not the place for humor, sarcasm or anger.
- Warn the witness not to engage in small talk with plaintiff or plaintiff's counsel other than courteous remarks at breaks. We have all had witnesses who made statement during a break that he thought was "off the record."

Q: Should you ask direct questions of your witness on a discovery deposition? Most of the time, yes.

- In most cases, make a few key points on direct in the deposition. The witness may later become unavailable, and you have to use the deposition at trial. It is very difficult to designate testimony from a deposition that has no direct examination. Also, in mass tort litigation with multiple cases depositions are commonly used for some fact witnesses in various jurisdictions, and you may be limited to line/page designations at trial. It is an uncomfortable situation to have to designate cross examination questions from plaintiff's counsel or not designate anything from an important witness.

Even given all the preparation and with the witness trying to follow instructions, the deposition result may be bad. How do you deal with a bad deposition at trial?

- Live with it and do not call the "bad" witness live. If you try to explain bad prior testimony away with a weak witness on the stand, it emphasizes the bad points, makes the witness defensive and fair game for impeachment. Often a jury gets bored with deposition testimony and the bad performance in deposition does less harm than in person. Because you tried to humanize the witness and also brought out key points on a short direct, you can use excerpts from the deposition affirmatively.

- If you must call the witness live or opposing counsel subpoenas him for the trial, make sure the witness is familiar with his prior testimony. If possible put bad testimony in context. Refresh the witness' recollection and work with him on responding to impeachment from his prior testimony.

- When you know you have a bad witness either live or by deposition and there is simply no way to improve that situation, you should inoculate the jury about this witness/document from the beginning of trial.[14] Lower the jury's expectations for this witness. Try to humanize the witness and give some reason for his attitude before he testifies.[15]

[14] *Id.*
[15] *Id.*

Q: What if your important company witness is called as an adverse witness at trial?

- All witnesses within subpoena range should be prepared to be called as adverse witnesses. Prepare your witnesses (or potential witnesses) for this possibility. Do not let a witness be surprised.

- If they are not prepared, they may be intimidated, frightened and thrown completely off their planned testimony, and they may not be able to recover.

- Reassure the witness that although he will be cross examined first, to stand his ground but not argue or become defensive. Role playing can help prepare for this situation.

- An effective cross examiner will try to make an employee or corporate representative feel defensive and even ashamed for working for a "bad" company or feel responsible for the conduct or injury in question.

- Remind the witness to sit up straight and not appear to be intimidated. Body language is important in this situation, and some jurors consider themselves experts in interpreting body language even though they are likely wrong.[16]

- Assure the witness that you will develop his testimony on direct (after cross) and do so. It is preferable to put on his direct testimony immediately unless the cross was limited and did not damage the witness. If that is the case you can wait and call in your case in chief. Another reason for putting the direct on at this time is to establish and explain your theme or story during the plaintiff's case.

- The witness should listen carefully to all questions on cross, and not be bullied into agreeing with the opposing attorney if he does not agree.[17]

In a well-known Texas trial which resulted in a large verdict, an accomplished plaintiff's attorney called two of the defense medical experts as adverse witnesses. The judge allowed him to subpoena them. (They were just inside subpoena range.) These witnesses were cross-examined extensively on bias and compensation and very little if any on opinions. They were not prepared for this situation and felt that they had been ambushed. The jury completely disregarded their credentials, their expertise and their opinions. The case was virtually over after before the defense case. The defense attorney was also unprepared for this possibility and could not pick up the pieces.

B. Dealing with Plaintiff's Expert Witnesses

There are many books and major articles written on cross examination of all types of witnesses including experts.[18] This paper does not intend to re-state these excellent resources,

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[16] *Id.*

[17] Rich, Trisha, "Effectively Examining the Difficult Witness," Litigation, ABA Section Meeting, April 2014.

but it focuses on some key questions to discredit opposing experts on cross and to develop techniques for making an opposing expert your own.

Many excellent trial attorneys have developed their skills at cross examination and have synthesized the process. In an interview John Romano described what he calls the "five silver bullet questions" to use when deposing an expert.[19] The overall goal of these questions was to establish bias, limit the testimony, attack credibility of the opposing expert and strengthen credibility of your own.[20]

His five questions are:

- What do you perceive as your purpose and function in this case?

  The expert usually answers to provide a fair determination of how accident occurred. At that point, he crosses on bias.[21]

- Assume your opinion is wrong or invalid. How would you find your error?

  Often the expert uses a different analysis from the one he used in writing his report.

- What further work do you intend to do or have you been asked to do in the case?

- Do you have any criticism of any expert's methodology or techniques?

- Have you made any "credibility" judgments in this case?[22]

  To continue to show bias, it is important that the expert has made a value judgement about the plaintiff and that has influenced his opinions.[23]

The hypothetical question on cross is effective if done skillfully. Hypotheticals allow the attorney to review, repeat and reinforce in the minds of the jury favorable facts of your case.[24]

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[18] *See* Clark, Sandra F., "The Art of Cross Examination," FDCC Quarterly, Vol. 61, No. 2, Winter 2011

[19] Zevitas, Christie, Five "Silver Bullet Questions for Opposing Experts," Lawyers Weekly (an interview with John Romano, former head of Academy of Florida Trial Lawyers, the Southern Trial Lawyer Association, and author of the textbook Strategic Use of Circumstantial Evidence.

[20] *Id.*

[21] *Id.*

[22] *Id.*

See also "Five Questions to Ask Your Computer Forensics Expert," Findlaw.com, January 15, 2016.

[23] *Id.*

[24] Rubinowitz, Ben B. and Evan Forgan, "Hypothetical Questions on Cross," New York Law Journal, December 29, 2006.

Also by asking an expert to assume as true certain facts, you can box in his opinions.[25] Conversely, it may be difficult to discover all expert's opinions if he is allowed to testify responding to hypotheticals. One technique some plaintiff's experts have used effectively is to have an expert prepare a report that addresses his opinions but that states that he reserves the right to respond to hypothetical questions, and at the time of his deposition, the expert "does not know what hypothetical circumstances he may be asked about."

Every case has a theory, and the defense attorney should understand the theory of plaintiff's case. Defense counsel should cross-examine plaintiff's expert with the goals of undermining plaintiff's theory and supporting the defense theory.[26] It is crucial to have thoroughly investigated the expert, searched social medial, read all published articles and become familiar with all his opinions.[27] In addition, questions should explore the expert's relationship with the attorney, the number of cases reviewed, the amount of money paid, and the financial support for expert's research.[28] In certain types of mass tort litigation plaintiff's attorneys have provided funding for research and for publication of such research. This research supported the very opinions the expert used against the other side. Of course, this situation has occurred with defense experts as well. Investigation into the financial arrangements with experts is crucial and the attorney should assume with some experts there is one. It is devastating not to learn about research funding of plaintiff's expert and to have your own expert vulnerable on that issue.

As part of any cross of an expert, ask about assumptions.

- What assumptions did you rely on in reaching your conclusions? Identify as many assumptions as possible and show how any substantive change would result in a different conclusion.[29] If you can show that some of the assumptions are wrong, you can undermine the soundness of the expert's opinion.[30]

Of course in an important trial, it is likely that some of the bias evidence, and the expert's methodology were explored at a *Daubert* hearing. Whether or not to request a *Daubert* hearing is a strategic decision and may depend on likelihood of success, the power of any negative evidence, and the importance of the expert. Does excluding or limiting the expert result in the plaintiffs not being able to prove liability? In that case, it is well worth it.

There are two basic schools of cross-examination: destructive cross and constructive (or supportive) cross. An aggressive litigator may be tempted to try to discredit every witness, but is that a good idea? Will a jury believe that every witness is biased? Or a liar? Probably not.

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[25] *Id.*
[26] Rundell, Edward E. and Sam N. Poole, Jr., "Cross-Examination of Plaintiff's Expert: The Art of War," 48 La. J.104, August 2000.
[27] Clark, *Supra*
[28] *Id.*
[29] Rich, Trisha, "Effectively Examining the Difficult Witness," Litigation, ABA Section Meeting, April 2014.
[30] *Id.*

Destructive Cross: The goal of destructive cross is to discredit the testifying witness or another witness. This type of cross is designed to reduce the credibility of the witness or persuasive value of the opposition's evidence.[31] The use of impeachment material is a key to destructive cross, as it is the ability to attack and discredit the bases for the witnesses' statements or opinions. The questioner's goal is to establish control of the witness both in his mind and in the mind of the jury. The jury expects that and as the trial proceeds, if the attorney excels in cross, the jury will look forward to what will happen next.[32]

Supportive Cross: This type of cross examination can be used to bolster the questioner's own theory of the case and tell the defense story. It should develop favorable aspects of the case not developed on direct examination[33] or expand on these aspects. This testimony may support your witnesses or help to impeach other witnesses.

In many jurisdictions, especially in state courts, cross examination is not limited in scope to the areas covered on direct. In those jurisdictions, cross can often yield helpful testimony given by experts in other cases or from other sources. Once a witness is on the stand he is fair game. Cross examination is the defense lawyer's opportunity to tell his story and to make significant points with the jury. Jury research also shows that jurors pay closer attention to cross than any other part of a case. Effective cross could result in a defendant calling fewer witnesses. Strategically, the defense attorney may call fewer witnesses for several reasons:

- To avoid repetition of facts or details clearly brought out in the case already;
- To move the case along toward close without appearing to delay;
- To put on only key witnesses who will stand up well on cross themselves;
- To prevent giving a skilled attorney on the other side a chance to score major points himself and end on a high note during the defense case.[34]

Strategically the trial attorney needs to determine which expert might help his case.[35] Constructive cross is to get the plaintiff's expert to agree with as many opinions as you can for your expert. In this situation, you may be collegial, charming, complimentary to the expert to allow him to stop being defensive and to be agreeable. Many experts with excellent credentials will recognize the credentials of the opposing expert. It is often easier to arrive at agreement with the expert on collateral matters than on ultimate opinions, but these collateral agreements can undermine some of opposing counsel's cross examination of another expert.[36]

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[31] Fred T. Friedman, "Cross Examination Skills."
[32] Kevin Holt, "Tips for Effective Cross Examination," Litigation News, Vol. XIII, No. 4, Winter 2006.
[33] Id.
[34] Clark, *Supra*
[35] *Id.*
Danner, Douglas and Larry Varn 3 Pattern Discovery Premises Liability §21:34.
[36] *Id,* Page 1

It is better to obtain the agreements from the opposing expert before attacking him with questions regarding bias, qualifications or methodology. The opposing expert will often agree to the reputations and qualifications of your expert.[37] Effective cross examination of plaintiff's medical expert can bolster your expert's opinions. Often the plaintiff's expert will acknowledge the quality of education, credentials, professorships, awards, and publications of your expert.[38]

III. REACHING HARBOR SUCCESSFULLY – STRONG CLOSING ARGUMENT

Closing Argument is an art and can affect the outcome of the case. While many trial lawyers do not like to admit this, cases are generally not won on closing, but they might be lost. The closing, however, should help guide the jury to make the right decision. This paper narrows the discussion of closing argument to four points:

1. Tips for a Strong Closing

2. The damage dilemma – do you suggest an alternative number?

3. How do you use the Charge of the Court and verdict form in closing?

4. Should you pick up all the pieces in closing?

A. Finish strong and on high note

Closing argument is the last time to make an impression on the jury.

- Be sincere when addressing the jury just like in opening – do not spend time on clichés. The jury is most attentive the first few minutes of closing so do not waste those valuable minutes.[39]

- Closing is the opportunity to persuade the jury to do what you asked them to do in opening. Not only do you set out your case, but you should negate plaintiff's contentions. You cannot argue every point or clear up every question at the end, but that is the reason the closing arguments are developed from the beginning of trial. You should not repeat all the evidence including witness testimony – that could bore the jury and potentially irritate them by spending too much time. Highlight the important issues and evidence.[40]

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[37] *Id.* Page 2

[38] *See* Byman, Robert L, "When Your Expert Becomes Their Expert," The National Law Journal, May 2014 (For a discussion of a very tricky situation in Federal Court in which opposing expert provides helpful testimony ; How can you use this testimony)

[39] Elliott, Edgar A. "Closing Argument From the Defense Perspective," www.csattorneys.com/resources/closing-argument-from-the-defense-perspective

[40] *Id.*

- Prepare outline at the beginning of trial. You need to know where you are going and what evidence you need to get there even though you will need to revise the argument along the way.

- Practice the closing to proceed without a script. It is time to impress the jury with your knowledge of the evidence, the facts, and the law.

- Use technology – the jury will expect it. For example, show how video testimony of an adverse witness fits your theory of the case. You could play short segments of video testimony from an adverse witness that directly contradicts points in the opponent's case on liability. The jury will pay attention.

- Make sure all demonstrative evidence is easy to read, easy to hear and not tedious. Move from one to another seamlessly and make sure all technology operates properly. A jury has little patience for "amateur hour."

- Consider a visual to illustrate the timeline that was established in opening, used with witnesses. Use it again on closing.

- Be creative and be as concise as possible.[41]

- Do not ignore significant negative evidence. Do not overly emphasize the bad evidence, but provide an answer, or context for it. If the evidence has no real answer, just acknowledge it and move on.

- By closing argument, you should be able to develop the context for a negative memo prepared by a disgruntled employee and minimize the effect of the criticism.

- Leave time to deal with the Court's charge and to show the jury how to answer the verdict form in your favor.[42] Make this a visual if possible.

- If liability is contested, argue liability facts and law then damages and return to liability with a strong illustration, story or testimony/exhibit to end closing on a high note.

- Anticipate plaintiff's rebuttal and point out that you will not be able to respond.[43] Make sure you insist that plaintiff open fully in his argument so that he cannot hold

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[41] *See* Wilson, Mark B., "The Do's and Don'ts of Closing Arguments," OCTLA Gavel, Spring 2006.
[42] *Id.*
[43] *Id.*

back some real dynamite for rebuttal that you will not be able to touch. If you fail to bring this up at the charge conference, the Court may not mention it on his own.

B. Damages – Do you or don't you suggest an alternative number?

How to deal with damages on closing is a dilemma faced by nearly every defense lawyer, and it usually depends on the case. There is not one answer that fits all.[44]

In determining the damages strategy, there are several obvious questions to consider:

- How much money is plaintiff asking for? Is it relative, based on evidence?
- How serious/permanent are injuries?
- How strong is your liability case?
- How well have you set this issue up from the beginning?
- What is the basis for any alternative damage number?

The defense attorney should not shy away from damages in closing argument, but he should have set up the damages defense from the beginning of the case. The damage questions will probably have been raised in voir dire as both sides will have attempted to identify problem damages jurors.[45] Attacking high dollar jurors is critical and the trial attorney should develop questions that identify and attempt to disqualify them. Skillful plaintiff's counsel as the first speaker will have had an opportunity to identify and disqualify many, if not most of the low damages jurors.[46]

In a "no liability" case, the defense attorney should not spend as much time on damages as in a closer call on liability. Some attorneys believe that any emphasis on damages dilutes the liability case. In dealing with the dilemma of damages, the defense attorney should also consider whether suggesting $0 for damages could backfire. In a serious injury or death case, the defense attorney cannot ignore damages, but from voir dire and opening statement should establish a pledge from jurors to separate liability from damages and facts from emotion. The defense

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[44] Kogel, Josi, "Damages: The Defense Attorney's Dilemma," The Jury Expert, Vol. 22, No. 1, January 2010.

[45] McCormick, Paul D., "Countering Plaintiff's Attempts to Maximize Damages," For the Defense, September 2007.

See also Blue, Lisa A. and Robert B. Hirschorn, "Goals and Practical Tips for Voir Dire," 26 Am. J. Trial Advoc. (Fall 2002); (In a case in which the defendant admits liability obviously damages becomes the focus of the trial, but these cases are unusual and not the focus of this discussion.)

[46] Blue, Lisa "Screening Jurors in the Age of Tort Reform," 34 – APR Trial (April 1998)

attorney should acknowledge the injury and loss and show empathy for the plaintiffs, but must be sincere. Some attorneys manage this better than others.

The defense attorney should be technical and obtain concessions, if possible, from the damages experts in a personal injury case. If this expert is honest, you may be able to use his testimony to support your own damage model and avoid calling your own economist, life care plan, or vocational rehabilitation expert. Effective cross examination of the economic experts to reduce plaintiff claims for compensation is key. It is important to be patient in cross of the economic experts to chip away at his opinions and reduce various categories of damages.

The damages dilemma finally culminates in the decision of whether to suggest an alternative recovery number. In a strong liability case with large damages, most defense attorneys suggest $0 damages to avoid a suggestion of damages being considered a concession on liability.[47] In a case in which plaintiff argues for huge damages based on nothing except emotion, the defense attorney could show that a fraction of the plaintiff's damage claim would put plaintiffs in the same economic situation as before the injury. The defense attorney is taking a chance to assume the jury will discount this exaggerated number to a reasonable number.

Whatever the number you suggest, if any, it should be based on evidence (or at least common sense). If plaintiff's life care plan is exaggerated and you presented a different one, then that could support an alternative damage number. A plaintiff who argues for an excessive number based on no evidence could lose credibility and appear greedy, but leaving that outrageous number unchallenged leaves the jury with only that number offered by either side. In a recent death case, plaintiff argued for $44 million in actual damages for an elderly retired gentleman with no lost wages and little medical expense and $1 billion in punitive damages. Fortunately, there was a defense verdict on liability. After the verdict one of the jurors was asked if he had considered damages if they had found liability. He said he did not have a specific number in mind, but – "I knew plaintiff's attorney wasn't serious about that much money. He would probably have been happy with less than half of that."

In a case in which the injury and damages are mostly past and the future damages are somewhat speculative, it is probably smart to suggest alternative damage numbers. Even in a case of probable liability, it may reduce the overall damage claim by putting on a (good faith) liability defense.

C. Do you address the Court's Charge and the Verdict Form?

The allotted time for closing rushes by very quickly. If you have not planned carefully and rehearsed all parts of the closing including use of exhibits, demonstratives, testimony, you will run out of time before covering everything you though you needed/wanted to cover. No matter how prepared you are, the Court can throw you a curve. The day of closing argument, for example, the judge has a meeting to attend at lunch and reduces the time for argument from 90 minutes to 60 minutes a side. Are the Court's Charge and Jury Verdict form so important to the case that you must include them in the argument? That question should answer itself. If the jury

[47] *Id.*

does not understand the issues or know how to answer the questions, you could lose the case even if the jury wants you to win.

The jury instructions are often long, tedious or boring. You really never have enough time to cover them all, or if you do, you will lose the attention of the jury. You should highlight key instructions, key issues and key questions. A demonstrative exhibit can effectively show how to answer the questions and streamline the presentation. It is important to show how your facts fit the law, or otherwise, the jury could be confused, and not be able to figure out how to find for the defense.[48]

Incorporating the exact language that the judge will use in the final charge also adds credibility to your argument.[49] In a recent case, it was critical to show the jury that to find liability in a premises liability case, the plaintiff had to prove four elements. The defense attorney carefully pointed this out in closing. A juror after the verdict said – "we thought they proved three elements of the cause of action but not the fourth." So no liability. Matching the charge to the facts was critical. That case was a five week trial with thousands of documents, many witnesses and depositions, and it was very contentious. This jury was attentive, analytical and took its oath very seriously. It required the plaintiff to prove every element of the claim by a preponderance of the evidence. In that case, reminding the jury of the facts and the law made a difference in the outcome.

Almost every point in this paper is subject to facts of a particular case. Each may be handled differently depending on the attorney. For the Trial Masters Program we will hear from five attorneys with different styles who will address the "icebergs" under the ocean and show different approaches to safely navigate the water.

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[48] *Id.*

[49] Cleveland, William C. "Closing Arguments," Defense Counsel Journal, October 2009.

"DEFUSING THE PUNITIVE DAMAGES BOMB"

A COMPLETE GUIDE TO PROTECTING YOUR CLIENT AGAINST LARGE PUNITIVE DAMAGES AWARDS"

FEDERATION OF DEFENSE AND CORPORATE COUNSEL
2016 WINTER MEETING
CORONADO ISLAND, CALIFORNIA

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INTRODUCTION

A punitive damage claim against a corporate defendant is comparable to a ticking time-bomb, carrying potentially devastating consequences, including an uninsurable blow to the company's bottom line and irreparable damage to years of goodwill. Punitive damages have been an integral part of American jurisprudence since this country's inception, and despite the efforts of the United States Supreme Court to establish the outer constitutional limits of punitive damage awards, large corporations remain targets for juries, who are as willing as ever to send a message to the "One Percent."

Punitive damage claims impact every aspect of litigation. They allow for broad and excessive discovery, which may intrude on business-sensitive information and the valuable time of key officers and employees who become embroiled in discovery as the document demands and deposition notices pile up. They expand what may be admissible as evidence at trial. They impede and delay settlement as plaintiffs leverage unreasonable demands with the threat of punitive damages, thus escalating defense costs. In some cases, they prevent defendants from making certain admissions to keep prejudicial evidence from being introduced at trial.

Defending the corporation from a punitive damage claim requires a comprehensive and meticulous strategy that should be implemented before the responsive pleading is served. This article provides a historical overview of punitive damages, a discussion of relevant principles under federal and New York law, and a practical guide to achieving a successful outcome.

I. A BRIEF HISTORY OF PUNITIVE DAMAGES

Punitive damages date back to the world's most ancient legal systems, most notably the Code of Hammurabi in Babylonian Law, circa 1750 B.C.[1] They have been endorsed by a number of legal and religious codes throughout history, from the Old Testament of the Bible to William Blackstone's Commentaries on the Laws of England. The United States Supreme Court has traced the source of modern Anglo-American punitive damage law to 18th Century English Law, beginning with the 1763 case of *Wilkes v. Wood*, which is widely recognized as the first English case to award punitive damages. In *Wilkes*, a decision which helped mold America's Fourth Amendment search and seizure laws, punitive damages were imposed on the British Secretary of State for an unlawful search of papers compiled by Revolution supporter, John Wilkes.[2]

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[1] See, e.g., Code of Hammurabi § 8, p. 13 (R. Harper ed. 1904) ("If any one steal cattle or sheep, or an ass, or a pig or a goat, if it belong to a god or to the court, the thief shall pay thirtyfold therefor; if they belonged to a freed man of the king he shall pay tenfold; if the thief has nothing with which to pay he shall be put to death.").

[2] *Wilkes v. Wood*, 98 Eng. Rep. 489 (K.B. 1763).

The United States' first recorded punitive damage case followed in 1784. In *Genay v. Norris*, the South Carolina Supreme Court enforced vindictive damages against a physician who spiked the plaintiff's drink following a disagreement.[3] *Genay* proved to be a catalyst for punitive damages in the American Justice System. By 1874, the United States Supreme Court acknowledged punitive damages as an integral part of American jurisprudence, despite its critics.

> It is a well-established principle of the common law, that in actions of trespass and all actions on the case for torts, a jury may inflict what are called exemplary, punitive, or vindictive damages upon a defendant, having in view the enormity of his offence rather than the measure of compensation to the plaintiff. We are aware that the propriety of this doctrine has been questioned by some writers; but if repeated judicial decisions for more than a century are to be received as the best exposition of what the law is, the question will not admit of argument.[4]

Today, punitive damages remain a predominant feature of American jurisprudence and are available in all but five states. Though federal and state tort legislatures and judiciaries have sought to constrain the frequency and magnitude of punitive damages award, these claims persist in tort litigation now as much as ever, especially when large corporations are involved.

II. FEDERAL CONSTRAINTS ON PUNITIVE DAMAGES

Under the traditional common-law, the amount of the punitive award was determined by a jury and then reviewed by trial and appellate courts to ensure it was reasonable.[5] Judicial review thus acted as the primary safeguard against excessive punitive damage awards. Yet, although trial and appellate courts theoretically held the power to reduce or overturn verdicts deemed excessive, there was little guidance on the standard for review, resulting in a relaxed, plaintiff-friendly norm, requiring "only that the damages awarded be reasonably necessary to vindicate the State's legitimate interests in punishment and deterrence."[6] By the late 1980s, the frequency and magnitude of large punitive awards made clear that the law was in need of reform. As awards increased, defendants looked to the Constitution to control the mostly unregulated discretion held by juries in awarding punitive damages.

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[3] 1 S.C.L. 6 (1 Bay 1784).

[4] *Day v. Woodworth*, 54 U.S. 363, 371 (1852).

[5] *Pac. Mut. Life Ins. Co. v. Haslip*, 499 U.S. 1, 15 (1991).

[6] *BMW of N. Am. v. Gore*, 517 U.S. 559, 568 (1996).

It is now well-established that the Due Process Clause of the Fourteenth Amendment provides procedural and substantive constraints on punitive damage awards. It was a challenge based on the Excessive Fines Clause of the Eighth Amendment, however, that set in motion the Supreme Court's establishment of Constitutional limits.

A. *Browning-Ferris Indus. v. Kelco Disposal*, 492 U.S. 257 (1989)

In *Browning-Ferris Indus. v. Kelco Disposal*, the Supreme Court considered whether a punitive damages award of $6 million, compared to a compensatory award of $51,146, against a waste disposal company for tortious contractual interference and antitrust violations was an excessive fine under the Eighth Amendment.[7] After a comprehensive review of the history of the Eighth Amendment, the Court held that the Excessive Fines Clause did not apply beyond the criminal context, and therefore did not apply to punitive damages awarded in a civil case.

Despite upholding the award, the Court suggested that the Due Process Clause of the Fourteenth Amendment provided a more appropriate avenue for challenging potentially excessive punitive damages awards. Addressing an argument defense counsel raised for the first time during oral argument, the Supreme Court noted:

> There is some authority in our opinions for the view that the Due Process Clause places outer limits on the size of a civil damages award made pursuant to a statutory scheme but we have never addressed the precise question presented here: whether due process acts as a check on undue jury discretion to award punitive damages in the absence of any express statutory limit. That inquiry must await another day.[8]

B. *Pacific Mut. Life Ins. Co. v. Haslip*, 499 U.S. 42 (1991)

The day the Supreme Court alluded to in *Browning-Ferris* came two terms later. In *Pacific Mut. Life Ins. Co. v. Haslip*, the Supreme Court granted *certiorari* to Pacific Mutual Life Insurance Company ("Pacific") "to review the punitive damages procedures and award in the light of the long-enduring debate about their propriety" after the Alabama Supreme Court affirmed a $1 million verdict with an $840,000 punitive damages component for alleged fraud.[9]

Writing for the majority, Justice Blackmun acknowledged the Court's concern that "unlimited jury discretion—or unlimited judicial discretion for that

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[7] *Browning-Ferris Indus. v. Kelco Disposal*, 492 U.S. 257 (1989).

[8] *Id*. at 276-77 (internal citations removed).

[9] *Pacific Mut. Life Ins. Co. v. Haslip*, 499 U.S. 1 (1991).

matter—in the fixing of punitive damages may invite extreme results that jar one's constitutional sensibilities."[10] Despite its concern, the Court found that the centuries-old common-law method of leaving punitive damages to discretion of the jury did not violate the Due Process Clause. The Court did not end the inquiry there, however. Recognizing that it would be difficult to draw a mathematical bright-line between the constitutionally acceptable and the constitutionally unacceptable that would fit every case, the Court observed that both "general concerns of reasonableness" and the trial court's instructions to the jury on the issue of punitive damages are important pieces of the constitutional calculus.

Turning its attention to the guidance provided to the jury in the case at hand, the Court found that the trial court's instructions sufficiently "enlightened the jury as to the punitive damages' nature and purpose" and therefore "reasonably accommodated Pacific Mutual's interest in rational decisionmaking and Alabama's interest in meaningful individualized assessment of appropriate deterrence and retribution."[11]

Haslip emphasized that basic notions of due process require (1) that the appellate courts review the trial court's jury instructions to ensure they adequately apprise the jury of the purpose of punitive damages so that such damages can be fairly assessed against the defendant and (2) that the size of the punitive damages award be reviewed for its reasonableness, thus providing a genuine (although still abstract) constraint on punitive damage awards.

C. TXO Production Corp. v. Alliance Resources Corporation, 509 U.S. 443 (1993)

Even though the punitive damage award in *Haslip* was upheld, the Supreme Court made clear that due process requires appellate courts to review these awards with a higher level of scrutiny than that used in the past. The precise level of scrutiny on review was still unclear, however, and was an issue before the court two years later in *TXO Production Corp. v. Alliance Resources Corporation*.[12] There, a plurality upheld a $10 million punitive damage verdict

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[10] *Id*. at 18.

[11] Specifically, the jury was instructed to consider: (a) whether there is a reasonable relationship between the punitive damages award and the harm likely to result from the defendant's conduct as well as the harm that actually has occurred; (b) the degree of reprehensibility of the defendant's conduct, the duration of that conduct, the defendant's awareness, any concealment, and the existence and frequency of similar past conduct; (c) the profitability to the defendant of the wrongful conduct and the desirability of removing that profit and of having the defendant also sustain a loss; (d) the "financial position" of the defendant; (e) all the costs of litigation; (f) the imposition of criminal sanctions on the defendant for its conduct, these to be taken in mitigation; and (g) the existence of other civil awards against the defendant for the same conduct, these also to be taken in mitigation. *Id*.; *see also Green Oil Co. v. Hornsby*, 539 So. 2d 218, 223 (Ala. 1989).

[12] *TXO Production Corp. v. Alliance Resources Corporation*, 509 U.S. 443 (1993).

awarded by a West Virginia state jury in a slander of title action - although it was 526 times the compensatory damages award.

The court refused each party's suggestion on the standard under which the punitive damage award should be reviewed, finding that neither a rational basis standard nor heightened scrutiny were appropriate. Instead, the Court simply turned to the facts and upheld the award "in light of the amount of money potentially at stake, the bad faith of petitioner, the fact that the scheme employed in this case was part of a larger pattern of fraud, trickery and deceit, and petitioner's wealth."[13]

Ultimately, the takeaway from *TXO* was minimal, and perhaps even confusing, as the Court sidestepped the opportunity to define a clear standard for review. Instead, practitioners were left with an imprecise concept that punitive damages may not be "so grossly excessive" as to violate a defendant's due process rights. For defendants, *TXO* was seen as a small step forward, as the Court seemed to acknowledge that notwithstanding the instructions given to the jury, a punitive damages award can, in the appropriate case, violate due process based on its sheer size in light of the facts.

D. *Honda Motor Co. v. Oberg*, 512 U.S. 415 (1994)

One term later, in *Honda Motor Co. v. Oberg*, the Court found Oregon's procedure for judicial review of punitive damage awards unconstitutional. Oregon's Constitution prohibited judicial review of the amount of punitive damages awarded by a jury "unless the court can affirmatively say there is no evidence to support the verdict."[14] The Court measured Oregon's procedure against the traditional common-law procedure to evaluate whether it violated due process.

The Court found a significant difference between the scope of review of punitive damages awards in Oregon and judicial review of punitive damages awards under the common-law. Namely, while Oregon law authorized judicial review when there was some procedural error by the trial court, defendants lacked the ability to challenge a punitive damage award based purely on its amount. The Court noted that high net worth defendants are at a disproportionate risk for large punitive damage awards, and without judicial review of excessive awards, would be exposed to jury biases:

> Punitive damages pose an acute danger of arbitrary deprivation of property. Jury instructions typically leave the jury with wide discretion in choosing amounts, and the presentation of evidence of a defendant's net worth creates the potential that juries will use

[13] *Id*. at 462.

[14] *Id*. at 418.

> their verdicts to express biases against big businesses, particularly those without strong local presences. Judicial review of the amount awarded was one of the few procedural safeguards which the common law provided against that danger. [15]

Oberg established that all punitive damage awards are subject to post-verdict review to determine whether the amount comports with due process. The Supreme Court would later hold that appellate courts should apply a *de novo* standard of review when passing on district court determinations of the constitutionality of punitive damages awards. Any less demanding standard violates the Due Process Clause.[16]

E. *BMW of N. Am. v. Gore*, 517 U.S. 559 (1996)

Browning-Ferris, *Haslip*, *TXO*, and *Oberg* laid the groundwork for *BMW v. Gore*,[17] the Supreme Court's seminal case on the due process limits of punitive damages. Before *Gore*, although the Court had made strides in establishing both procedural and substantive constraints on punitive damage awards, it had not yet established a standard of review to guide appellate courts in their examination of awards. As a result, the due process limitation was still too abstract to effectively protect defendants against massive punitive awards, such as the award at issue in *Gore*, which was 500 times the compensatory award.

Gore arose out of a simple set of facts. Plaintiff, Dr. Ira Gore, Jr., purchased a brand new BMW automobile from an authorized dealer in Alabama. After the purchase, he discovered the car had been repainted. He brought suit against the American distributor of BMWs for compensatory and punitive damages, alleging, among other things, that BMW's failure to disclose the repainting constituted fraud under Alabama law.

At trial, BMW admitted that it followed a nationwide policy of concealing from its dealers—and by extension, its customers—any pre-delivery damage to new cars when the cost of repairs did not exceed three percent of the car's suggested retail price. In Dr. Gore's case, because the $601.37 cost of repainting the plaintiff's car was only about 1.5 percent of its suggested retail price, BMW did not disclose the damage or repair.

The jury found that BMW had withheld a material fact, and returned a verdict for $4,000 in compensatory damages. The jury also awarded the plaintiff $4 million in punitive damages based on a determination that BMW's nondisclosure policy constituted "gross, oppressive or malicious" fraud under Alabama law. The punitive damages award was appealed as excessive, and was

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[15] *Honda Motor Co. v. Oberg*, 512 U.S. 415, 432 (1994).

[16] *Cooper Indus. v. Leatherman Tool Group, Inc.*, 532 U.S. 424, 443 (2001).

[17] *BMW of N. Am. v. Gore*, 517 U.S. 559 (1996).

ultimately reduced to $2 million by the Alabama Supreme Court.[18] The United States Supreme Court granted *certiorari*, "to illuminate 'the character of the standard that will identify unconstitutionally excessive awards' of punitive damages."[19]

Noting that elementary notions of fairness provide that a person is given fair notice of both the conduct that will subject him to punishment *and* the severity of the penalty that will be imposed for such conduct, the Court established three guideposts for reviewing courts to use in evaluating whether a punitive damages award is excessive: (1) the degree of reprehensibility of the nondisclosure; (2) the disparity between the harm or potential harm suffered and the punitive damages award; and (3) the difference between the remedy and the civil penalties authorized or imposed in comparable cases.[20]

Based on those factors, the Court struck down the $2 million dollar punitive damage award as grossly excessive. After *Gore*, appellate courts reviewing punitive damages finally had a focused and consistent method for assessing whether the awards violated due process. Yet, despite highlighting the importance of the disparity between the actual harm suffered and the punitive damage award, the Court again declined to set a bright-line ratio between compensatory and punitive damages that may not be exceeded.

F. *State Farm Mutual Ins. Co. v. Campbell*, 538 U.S. 408 (2003).

The Supreme Court inched closer to establishing a bright-line ratio between compensatory and punitive damages seven years after *Gore*. In *State Farm Mutual Ins. Co. v. Campbell*, the Supreme Court applied the *Gore* guideposts to vacate a punitive damage award levied against State Farm Mutual Insurance Company for bad faith, fraud, and intentional infliction of emotional distress after a finding at trial that the company unreasonably decided not to settle a motor vehicle accident matter it was defending, thus exposing its insured to personal liability.[21]

Although the Court again declined to articulate a firm bright-line ratio between compensatory and punitive damages, it significantly narrowed the range of constitutional punitive damage awards by declaring that few awards exceeding a single-digit ratio between punitive and compensatory damages will satisfy due process. The Court also noted that when compensatory damages are substantial, a much lower ratio approaches the constitutional limits.

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[18] *Id*. at 567.

[19] *Id*. at 568 (*citing Oberg*, 512 U.S. at 420).

[20] *Id*. at 574-575.

[21] *State Farm Mutual Ins. Co. v. Campbell*, 538 U.S. 408 (2003).

The Court in *State Farm* was critical that the defendant had been condemned for its nationwide policies rather than for its conduct directed toward the plaintiffs. Citing to *Gore*, the Court held that the jury must be instructed that it may not use evidence of out-of-state conduct to punish a defendant for action that was lawful in the jurisdiction where it occurred. The Court further held that a defendant's dissimilar acts, independent from the acts upon which liability was premised, may not serve as the basis for punitive damages.

There were thus three important takeaways from *State Farm*. First, only in rare circumstances will a punitive damages award exceeding a 9:1 ratio to compensatory damages be deemed constitutional. Second, evidence of out-of-state conduct should not be considered by the jury when assessing punitive damages. Third, the focus of the punitive damages inquiry is the defendant's conduct directed toward the plaintiff, not toward any hypothetical plaintiff.

G. *Philip Morris v. Williams*, 549 U.S. 346 (2007)

In *Philip Morris v. Williams*, the Supreme Court reinforced the idea that the jury may assess punitive damages only for the harm done to the plaintiff, and not to other victims whose cases are not before the court. There, a widow brought an action in Oregon state court against Philip Morris, the manufacturer of Marlboro cigarettes, the brand plaintiff's decedent favored. The lawsuit alleged that the decedent was deceived into believing that Marlboro cigarettes were safe to use. The jury found Philip Morris liable for negligence and deceit and awarded the plaintiff compensatory damages in the amount of $821,000 and $79.5 million in punitive damages.[22]

The trial judge deemed the punitive damage award excessive and reduced it to $32 million. After both sides appealed, the Oregon Court of Appeals restored the $79.5 million jury award. Philip Morris appealed. The main issue on appeal to the Oregon Supreme Court concerned the trial court's jury charge. Specifically, Philip Morris sought to charge the jury with an instruction that the jury could not seek to punish the company for injury to persons not before the court. During the trial, plaintiff's counsel had made comments to the jury referencing non-parties who may have been harmed by smoking cigarettes.

The trial judge rejected the proposed instruction and instead instructed the jury that "punitive damages are awarded against a defendant to punish misconduct and to deter misconduct" and "are not intended to compensate the plaintiff or anyone else for damages caused by the defendants' conduct." Philip Morris argued that to the extent the punitive damage verdict represented punishment for harm caused to non-parties to the action, the award violated its due process right. Additionally, Philip Morris argued that the ratio of nearly 100-1 of compensatory

[22] *Philip Morris v. Williams*, 549 U.S. 346 (2007).

and punitive damages violated the Supreme Court's urging in *Gore* and *State Farm*. The Oregon Supreme Court rejected those arguments and found that the $79.5 million punitive damage award was not excessive in light of the reprehensibility of Philip Morris' conduct.

On *certiorari*, the United States Supreme Court reversed and remanded, finding that although it was permissible to consider the harm caused to non-parties to the action under the reprehensibility prong of the *Gore* analysis, a punitive damage award that punishes a defendant for injuries allegedly inflicted upon strangers to the litigation, without an opportunity to defend the charge, violated due process. Due process requires that the jury is informed that while harm to non-parties was relevant to reprehensibility, punitive damages may not be awarded to punish the manufacturer for such harm.

III. PUNITIVE DAMAGES IN NEW YORK

In contrast to compensatory damages, which are intended to remedy the concrete loss a plaintiff has suffered as a result of the defendant's wrongful conduct, punitive damages are intended to punish reprehensible conduct and deter the future occurrence of similar conduct by the defendant or others similarly situated.[23] Also called exemplary damages, punitive damages generally aim to deter "conduct that may be characterized as gross and morally reprehensible and of such wanton dishonesty as to imply a criminal indifference to civil obligations."[24]

It was not until 2013 that the New York Court of Appeals established a clear standard against which a defendant's conduct must be measured to justify the imposition of punitive damages. In *Marinaccio v. Town of Clarence*, the Court of Appeals held that punitive damages are warranted only when the alleged conduct "manifests spite or malice, or a fraudulent or evil motive on the part of the defendant, or such a conscious and deliberate disregard of the interests of others that the conduct may be called wilful or wanton." The conduct "must represent a high degree of immorality and shows such wanton dishonesty as to imply a criminal indifference to civil obligations."

Marinaccio involved an action for trespass and nuisance for the intentional diversion of storm water onto the plaintiff's property, causing significant damage to his land. The question presented was whether the evidence supported a claim for punitive damages.

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[23] *See* Restatement (Second) of Torts, Sec. 908(1) (1979) ("The purposes of awarding punitive damages, or "exemplary" damages as they are frequently called, are to punish the person doing the wrongful act and to discourage him and others from similar conduct in the future."); *Walker v. Sheldon*, 10 N.Y.2d 401, 404 (1961); *Frankson v. Brown & Williamson Tobacco Corp.*, 67 A.D.3d 213, 218-219 (2d Dept. 2009).

[24] *New York Univ. v. Cont'l Ins. Co.*, 87 N.Y.2d 308, 315 (1995)(internal citations omitted).

By way of background, the plaintiff and defendant, Kieffer Enterprises, Inc. ("KEI"), a residential real estate company, were adjoining landowners in the town of Clarence, New York ("the town"). KEI sought to develop a residential subdivision on its land and submitted a plan to the town for its approval. The town approved the plan, which required that water from the development would flow into a storm sewer and then into a ditch, creating a mitigation pond in the subdivision. Initially, the town believed the ditch was located on KEI's property, but later discovered it was actually located on the plaintiff's property, and was used without the plaintiff's permission.

The ditch was not large enough to hold all the water that was diverted from KEI's property. To address the problem, KEI installed two drainage pipes to re-route the water onto an abandoned parcel of the plaintiff's land, again without the plaintiff's permission. This resulted in over 30 acres of flooded wetland and an infestation of mosquitos and frogs (of which the plaintiff was particularly phobic).

The plaintiff commenced an action against KEI and the Town alleging, among other things, trespass and private nuisance for the flooding of his property. A jury awarded the plaintiff $250,000 in punitive damages against KEI, in addition to other compensatory damages. KEI's motion to set aside the punitive damages verdict was denied and the Appellate Division affirmed. The Court of Appeals then reversed the Appellate Division's order and vacated the punitive damages award.

The Court of Appeals rejected the plaintiff's argument that KEI willfully and wantonly caused danger to the health, safety, and welfare of the public, relying on facts showing that KEI's actions did not "imply a criminal indifference to civil obligations." Specifically, the Court set forth several acts of due diligence on KEI's part regarding the planning, making particular note that KEI "complied with all federal, state and local planning and development laws and regulations, and worked closely with the US Army Corps of Engineers, the Town Engineer and the Town Planner to secure all required permits and approvals; it hired a wetlands expert, an engineering expert, and soil expert to assist in those regards." Even though the Court found that "the injury was considerable and the tortious acts undeniably intentional," the evidence did not support a finding of punitive damages.

The *Marinaccio* standard now governs all common-law punitive damage claims in New York. While juries traditionally had relatively unbridled discretion to impose punitive damages in any amount, the *Marinaccio* Court determined, as a matter of law, that the evidence presented was insufficient to impose punitive damages in the first place. The sufficiency of evidence necessary to support a claim for punitive damages is now clearly a question to be resolved by the Court, not the jury.

IV. PUNITIVE DAMAGE DEFENSE THEMES

Based upon the New York and Federal case law, there are a number of themes defense counsel should develop in punitive damage actions: (1) the human error defense; (2) the corporate defense; (3) the regulatory defense; and (4) the due diligence defense. Of course, there may be other available defenses, depending on the facts, but any additional defenses will likely be dependent in part on the four explained below.

A. The Human Error Defense

The human error defense is most readily available where the conduct of an individual or group of individuals directly causes the harm, such as where a pilot's negligent act causes a plane crash or where an employee's carelessness, whether or not enabled by a company policy, causes an accident. The human error defense emphasizes that no one can perform his or her job perfectly, no matter how experienced he or she is. People make mistakes; no amount of training that can eliminate every error. Even the best-trained employee can take unpredictable action under particular circumstances. It is important to emphasize that despite the employee's error, all employees had the necessary training and adequate experience.

B. The Corporate Defense

The corporate defense is rooted in the complicity doctrine, and argues that the employee's actions were not endorsed, ratified, or participated in by the company. The corporate defense argues that the employee's actions were unmotivated, unintentional, and cannot alone constitute the basis for a punitive damages award. It is the corporation that is on trial—not its individual employees. A corporation has no malice independent of the malice of its officers, directors, managing agents, and employees.

C. The Regulatory Defense

The regulatory defense recognizes that the decisions and actions of most companies are dictated by laws and policies. It is therefore unjust to punish a company for following rules over which it had no control. The regulatory defense simply shows that the company followed, and hopefully exceeded, its requirements. For example, the regulatory defense in a product liability action would rely on the following:

- The authority to regulate Product X has been granted to Y Department.
- Y Department regulates Product X via the promulgation and enforcement of certain rules and regulations.

- Rigorous and strict requirements are imposed by Y Department on the quality controls for the manufacture of Product X.

- Y Department does not require manufacturers of Product X to submit periodic safety reports.

- Y Department has established, by regulations and policy, procedures for both voluntary and required Product X recalls or corrective actions to protect the public health and safety.

- Y Department does not require, by statute or regulation, that companies conduct active post-marketing vigilance, surveillance, or studies of legally marketed products of this kind.

- Y Department has established, by statute, regulation, and policy, requirements for product labeling.

Establishing the manufacturer's compliance with all policies and procedures imposed by law or required procedure renders a punitive damages award against the manufacturer fundamentally illogical. Importantly, by contrast, the violation of any safety standard does not automatically warrant punitive damages. Mere evidence of a violation of a safety regulation is insufficient to warrant the imposition of punitive damages.[25]

D. The Due Diligence Defense

The due diligence defense is an extension of the regulatory defense. The due diligence defense allows the defendant to champion everything the company did correctly, rather than defend what it did not do or what it did incorrectly. For example, in a product liability action, the due diligence defense can be established by showing:

- The product was designed, tested, marketed, and sold in compliance with the department regulations and consistent with generally accepted industry practices;

- The company conducted extensive pre-manufacture safety testing of the product prior to marketing it;

- The product labeling is appropriate and has at all times been in conformity with federal law and regulations for products of this kind;

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[25] *Heller v. Louis Provenzano, Inc.*, 303 A.D.2d 20, 26 (1st Dept. 2003) ("If the violation of a regulation does not constitute negligence per se, it surely is insufficient to sustain a claim for punitive damages, which requires a significantly higher level of culpability."); *see also Cowsert v. Macy's E., Inc.*, 74 A.D.3d 1444, 1445 (3d Dept. 2010) (denying plaintiff's motion for leave to amend the complaint to add a claim for punitive damages).

- The product is manufactured consistent with generally accepted practices in the industry;

- The company maintains a product complaint handling reporting system that complies with applicable product regulations and exceeds industry best practices;

- In response to reports of alleged product defects, the company initiated new research, consistent with generally accepted and normative industry practices;

- Implementation of labeling changes by the company represents the highest level of care in consideration of the risk of gross misuse of the product.

The due diligence defense is not limited to product liability actions. *Marinaccio*, New York's leading case on punitive damages, is an example of the due diligence defense prevailing in an action based on trespass and nuisance theories.

V. DEFENDING THE PUNITIVE DAMAGES CASE

Defense counsel should be prepared to defend a punitive damage claim even when one is absent from the pleadings, as plaintiffs may be granted leave to amend pleadings to assert punitive damage claims. To be sure, the defense of the punitive damage claim should be put in motion before answering the complaint.

A. Do Your Research

From the outset, it is important to know your jurisdiction's law on punitive damages. If your case is venued in a jurisdiction that allows liberal punitive damages awards, consider invoking appropriate choice of law rules to transfer the case to a more favorable jurisdiction.

Not all states treat punitive damages the same. New York has no statutory limit on punitive damages awards. On the other extreme, five states—Louisiana, Massachusetts, Nebraska, New Hampshire, and Washington—do not allow punitive damages at all.[26] Most states fall somewhere in the middle of those two extremes by passing specific legislation to safeguard against excessive punitive damages verdicts.

Most statutory limits on punitive damages involve a ratio to the compensatory damages awarded. Colorado, for example uses a simple 1:1 ratio; the punitive damages award may not exceed the compensatory damages award.[27]

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[26] *See* http://www.instituteforlegalreform.com/uploads/sites/1/FullHarrisSurvey.pdf

[27] Colo. Rev. Stat. § 13-21-102(1)(a).

Other states add an absolute monetary cap as an additional safeguard. For example, New Jersey limits punitive damages awards to the greater of five times the award of compensatory damages or $350,000.[28]

Some states' limits on punitive damages are even more complex. Alabama, for example, limits punitive damage awards to the greater of three times the compensatory damage award or $1.5 million in physical injury cases and the greater of three times the compensatory damage award or $500,000 in most non-physical injury cases, depending on the net worth of the business. In non-physical injury cases against businesses with a net worth of less than $2 million, punitive damage awards are limited to the greater of $50,000 or ten percent of the business's net worth up to $200,000.[29]

Limitations on punitive damages awards can also be procedural. For example, Texas requires a unanimous jury verdict to award punitive damages.[30] When comparing the punitive damage laws of multiple jurisdictions, it is important to pay particular attention to the standard required to prove punitive damages—many states require the plaintiff to establish the basis for punitive damages by clear and convincing evidence. In New York, the standard varies, depending on the Department the case is brought in. The statutory cap, if any, should be evaluated in conjunction with the standard of proof to accurately compare jurisdictions.

B. Pre-Answer Dispositive Motions

When the complaint contains a punitive damage claim, it is worth your time to evaluate whether the claim can be dismissed based on the insufficiency of the pleadings. In New York, the allegations in the Complaint must be pled with at least enough particularity to support the imposition of punitive damages. While plaintiff will be given every favorable inference, defendants have been successful in pre-answer motions to dismiss where the allegations in the pleadings do not suggest more than mere negligence.[31]

As noted above, even where punitive damages are not alleged in the complaint, defense counsel should keep in mind that the plaintiff may move for leave to amend their complaint to assert a punitive damage claim. In at least one instance in New York, a motion for leave to amend the complaint to add a punitive damage claim has even been granted after depositions were already

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[28] N.J. Stat. Ann. § 2A:15‑5.14.

[29] Ala. Code § 6-11-21.

[30] Tex. Civ. Prac. & Rem. Code §§ 41.003.

[31] *Beville v. Olean Gen. Hosp.*, 124 A.D.3d 1412, 1412 (4th Dept. 2015); *Fragrancenet.com, Inc. v. Fragrancex.com, Inc.*, 68 A.D.3d 1051, 1052 (2d Dept. 2009); *Croton Falls Fire Dist. v. Pierce Mfg. Co.*, 130 A.D.2d 456, 456 (2d Dept. 1987).

conducted.[32] In theory, this allows the plaintiff the opportunity to blindside the defense with a punitive damage claim late in the discovery period. For that reason, it is important to conduct a thorough background investigation of plaintiff's claims at the outset and note any arguably punishable conduct.

C. Preserve Constitutional Defenses

Preserve your constitutional defenses for appellate review by asserting them as affirmative defenses in the answer. Although the Due Process Clause has proved most effective in limiting punitive damage awards, affirmative defenses based upon other constitutional rights should also be raised in the pleading. Some examples of appropriate affirmative defenses in response to punitive damage claims are:

- The plaintiff's complaint fails to state a claim upon which punitive damages can be granted.

- Any award of punitive damages would be in contravention of the constitutional safeguards provided to defendants under the Constitutions of the United States and of the individual States jointly and separately.

- Any award of punitive damages would be in denial of defendant's right to equal protection of the laws as guaranteed by the Fourteenth Amendment to the United States Constitution and numerous state constitutions, as the absence of adequate and objective standards for the assessment of punitive damage fails to ensure the equality of treatment between similarly situated civil defendants and equality of treatment between criminal defendants and civil defendants.

- Any award of punitive damages based upon vague and undefined standards of liability would violate the Due Process Clause of the Fourteenth Amendment, U. S. Const. Amend. XIV, Section 1, and the Due Process Clause of the New York State Constitution, Article I, Section 6.

- Any award of punitive damages based upon any standard of proof less than "clear and convincing" evidence would violate the Due Process Clause of the Fourteenth Amendment of the United States Constitution, and the Due Process Clause of the New York State Constitution, Article I, Section 6.

- Any award of punitive damages would be in denial of the defendant's right to equal protection of the laws as guaranteed by the Fourteenth Amendment to the United States Constitution and the New York State Constitution, as the absence of adequate and objective standards for the

[32] *Blumenthal v Zacklift International, Inc.*, 2008 N.Y. Misc. LEXIS 9618, *38 (N.Y. Sup. Ct. June 4, 2008).

assessment of punitive damages fails to ensure the equality of treatment between similarly situated civil defendants and equality of treatment between criminal defendants and civil defendants.

- Any award of punitive damages would violate the defendant's Due Process Rights embraced by the Fifth and Fourteenth Amendments to the United States Constitution and the New York Constitution, as a punitive damage award would constitute a deprivation of property without due process of law.

- Any award of punitive damages would violate the Commerce Clause of Article I of the United States Constitution, constituting an undue and unreasonable burden on interstate commerce, and to the extent it punishes acts or omissions which have occurred outside of state boundaries.

- Any award of punitive damages would violate the defendant's rights under the contract clause of the United States Constitution and the New York State Constitution, as it would impair the contractual obligations of the parties to this action.

- Any award of punitive damages would contravene the constitutional prohibitions against *ex post facto* laws.

- Any award of punitive damages would violate the Double Jeopardy Clause because the defendant could be subject to multiple awards of damages for the same set of acts.

- Any award of punitive damages would violate the Eighth Amendment's guarantee that excessive fines shall not be imposed.

D. Be Focused in Discovery

As is always the case, being prepared is the key to the successful defense of a punitive damage claim. Defense counsel is entitled to know the basis for plaintiff's punitive damage claim. Craft carefully tailored interrogatories and other discovery demands to that end. Although you are likely to get vague responses to the first request, be persistent in pursuit of the precise allegations the plaintiff intends to claim against your client. Discovery motions, such as motions to compel or motions for a more definite bill of particulars, may be necessary. From a cost-effective perspective, it is always prudent to call your opponent to informally discuss the substance of the clams.

Defense counsel must do whatever it takes to remove the element of surprise at trial. That may mean deposing a few extra non-party witnesses or requesting more documents than usual. The benefit of full preparedness at trial (to the extent that "full preparedness" can actually be achieved) far outweighs the inconvenience and expense of expanded discovery.

E. Selecting the Corporate Messenger

Your client's deposition can make or break the plaintiff's punitive damages case. Failure to recognize the importance of the corporate representative's deposition is a common mistake that can have incurable consequences. Just as important as the deposition itself, though, is your identification of the appropriate corporate messenger—that is—the corporate representative who will most accurately and efficiently deliver the corporate message.

When selecting the corporate messenger, defense counsel should consider:

- Who is the "most knowledgeable" witness?
- Who is the "best" witness?
- Who is most knowledgeable about the underlying substantive issues?
- Who would be best at fielding questions?
- Who would make the best impression before a jury?

The best corporate messenger is one who has a keen understanding of the facts and issues in question in the lawsuit and is prepared to confidently deliver the corporate message. Because depositions are increasingly being recorded on video, the ideal corporate messenger is one whom a jury would respect, believe, and most of all, like.

F. Preparing the Corporate Messenger

Active tort defense litigators prepare and produce dozens of deposition witnesses each year. Although the preparation of witnesses can be mundane and monotonous, cutting corners or under-preparing your corporate messenger in a punitive damages case can spell disaster for your client. Many corporate witnesses have been through depositions before, too. It is mostly good to have an experienced witness who will not be rattled by the sights and sounds of the deposition, but it can be detrimental to have a witness that is *too* comfortable and disregards your directions. Insisting on rehashing even the simplest topics during your preparation of the witness can help convey the importance of the deposition.

By the end of your preparation, the witness should be profoundly aware of the how his or her testimony fits in with the current case and how it may be used in other cases against the defendant. Remind your witness that it is not his or her job to win the case. Testifying requires discipline, clarity, simplicity and precision that can, and should, be repeated from question to question.

The witness must be instructed to tell "the whole truth." Effective testimony sometimes requires that the witness provide additional context that has

been intentionally omitted by the questioner. It is up to the witness to fill in the context to ensure a complete and accurate answer.

For example, the questioner asks your witness this pointed question: "You threw away thousands of documents shortly after this accident occurred, didn't you?" The answer may be "yes," but that may not be the whole truth. Your witness must be prepared to answer that question with the appropriate context: "Yes. It's our regular practice to discard unnecessary paper file materials. We had no notice of this accident until many months later."

Telling the whole truth neutralizes the effect of leading questions. Of course, the most effective defense to potentially prejudicial or provocative questions is a sound routine for processing the questions. Getting the witness to listen carefully to the question, pause to ensure she understood the question, and mentally formulate a complete answer to the question before answering is easier said than done, but you must do whatever it takes to instill that habit. The witness's answering technique needs to withstand a lengthy, tiring, and potentially hostile deposition.

The witness must remain poised and courteous throughout the deposition, especially since the deposition is likely to be on video. Defense counsel can help by making sure to take breaks whenever there is a sense that the witness is becoming irritable. Your witness should never become fatigued because *you* can control it. Keep the witness fresh throughout the deposition by taking ample breaks, even if just for precautionary measure.

G. Dispositive Motions at the Close of Discovery

As noted above, as important as it was that *Marinaccio* established a concrete standard for conduct justifying punitive damages, it is just as important that it confirmed that punitive damages can be dismissed as a matter of law. Defense counsel should always move to dismiss the punitive damage claim at the close of discovery. Even if the motion is denied, you will have not only extracted the facts and theories upon which the plaintiff will rely at trial, but you will also have educated the court on the facts and standards that will apply to its review of any potential punitive damage award.

H. Bifurcation

When there is a punitive damage claim, it may be advantageous to bifurcate the trial. A bifurcated trial prevents the jury from hearing potentially prejudicial evidence, such as sensitive financial information of the corporation. A defendant's net worth is relevant to the amount of punitive damages to ensure that the award carries the proper punishment and deterrent effect and therefore may be considered by the trier of fact when assessing punitive damages.[33]

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[33] *Rupert v. Sellers*, 48 A.D.2d 265 (4th Dept. 1975)

Several states now require bifurcation when both compensatory and punitive damages are requested. In New York, bifurcation is available in the First, Third, and Fourth Departments.[34] In those jurisdictions, evidence of a defendant's financial status is not discoverable until there is some factual basis for punitive damages, that is, after the trier of fact has found the defendant liable for punitive damages.[35] This rule serves an important purpose: courts have recognized that allowing discovery of financial documents whenever punitive damages are asserted would encourage plaintiffs to assert punitive damages in every case. Instead, the plaintiff must first obtain a special verdict that she is entitled to punitive damages before she can invade the financial privacy of the defendant.[36] The Second Department has explicitly declined to endorse the majority view, but has agreed that the defendant's financial information is not relevant until a factual basis for punitive damages is established.[37]

Bifurcation also provides an ideal platform for what is described below as the "Four C's" (contrition, concession, causation, and compensation), which are highly effective as damage control techniques during trial and on summation in the event your client is found liable for punitive damages. More to the point, when a trial with a punitive damages element is not bifurcated, it is a challenge to reconcile your no-liability position with the necessary showing of contrition required to minimize the potential of punitive damages. Bifurcation allows defense counsel devote its full efforts to defeating liability first, before devoting that same effort to defeating punitive damages, if necessary.

I. Pre-trial Motions

Ensuring that the trial is bifurcated is not the end of the fight. Defense counsel should also make motions in limine to prevent prejudicial information from being asserted in both the liability and punitive damages phases of the trial. Particularly, you should move to preclude all financial information, such as net worth and financial conditions, including any references to same from the liability phase. With respect to the punitive damages phase, motions should be made to preclude the plaintiff from arguing that non-parties have also been harmed by the defendant's conduct, referencing an allegedly unlawful acts committed outside of the state's jurisdiction, and referencing other large corporations that have had large punitive damages assessed against them.

J. Jury Selection

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[34] *Suozzi v. Parente*, 161 A.D.2d 232 (1st Dept. 1990); *Dufresne v. Duemler*, 108 A.D.2d 1102 (3d Dept. 1985); *Rupert v. Sellers*, 48 A.D.2d 265 (4th Dept. 1975); *James D. Vollertsen Associates, Inc. v. John T. Nothnagle, Inc.*, 48 A.D.2d 1007 (4th Dept. 1975).

[35] *Id*.

[36] *Suozzi v. Parente*, 161 A.D.2d 232 (1st Dept. 1990).

[37] *Moran v. Int'l Playtex*, 103 A.D.2d 375, 376-377 (2d Dept. 1984)

Mock jury exercises have convincingly demonstrated that theme development is imperative to a successful defense. Themes must be carefully pieced together throughout the course of the lawsuit, not thrown together a month before the trial begins. They should also be methodically presented in a way the jury can identify with. To that end, jury composition is a priority. Careful *voir dire* questions should be crafted to ensure anyone who possesses biases is removed from the jury pool. Potential jurors could hold biased and unfavorable views of large corporations.

K. Post-Trial Motions

Should punitive damages be assessed against your client, the *Marinaccio* standard and the three guideposts articulated in *Gore* serve as the roadmap for your post-trial motion. Be sure to also challenge the verdict based on the holdings of the other Supreme Court cases above, especially with regard to the jury instructions and prejudicial statements that reference out-of-state conduct and harm to nonparties.

The Three Guideposts

a) Reprehensibility of Defendant's Misconduct

The first guidepost reflects the theory that the punishment should fit the crime. The *Gore* Court declared the reprehensibility of a defendant's misconduct to be the most important indicium of the reasonableness of a punitive damage award. In *State Farm*, the Court described the reprehensibility analysis as follows:

> We have instructed courts to determine the reprehensibility of a defendant by considering whether: the harm caused was physical as opposed to economic; the tortious conduct evinced an indifference to or a reckless disregard of the health or safety of others; the target of the conduct had financial vulnerability; the conduct involved repeated actions or was an isolated incident; and the harm was the result of intentional malice, trickery, or deceit, or mere accident. The existence of any one of these factors weighing in favor of a plaintiff may not be sufficient to sustain a punitive damages award; and the absence of all of them renders any award suspect. It should be presumed a plaintiff has been made whole for his injuries by compensatory damages, so punitive damages should only be awarded if the defendant's culpability, after having paid compensatory damages, is so reprehensible as to warrant the imposition of further sanctions to achieve punishment or deterrence.[38]

[38] *State Farm*, 538 U.S. at 419 (internal citations omitted).

b) Disparity Between the Actual or Potential Harm Suffered by the Plaintiff and the Punitive Damages Award

The second guidepost is based on the principle that the punitive damage award must bear a "reasonable relationship" to the harm actually suffered. The *State Farm* court noted that few awards exceeding a single-digit ratio between punitive and compensatory damages will satisfy due process. A greater ratio may comport with due process where a particularly egregious act results in only a small amount of economic damage. On the other hand, where the compensatory damages are substantial, a lesser ratio, perhaps equal to compensatory damages, may be required to reach the outermost limit of the due process guarantee.[39]

c) Difference Between the Punitive Damages Awarded by the Jury and the Civil Penalties Authorized or Imposed in Comparable Cases

The third guidepost allows the court to consider the maximum criminal penalty that could be imposed for comparable misconduct, based on the theory that the extent of the criminal penalty bears on how seriously a state views the misconduct. The court will "accord substantial deference" to legislative documents that address the misconduct.[40] However, courts should be careful to avoid use of the civil process to assess criminal penalties that can be imposed only after the heightened protections of a criminal trial have been observed, including, of course, its higher standards of proof. Punitive damages are not a substitute for the criminal process, and the remote possibility of a criminal sanction does not automatically sustain a punitive damages award.[41]

VI. TRIAL SUMMATIONS

A. PLAINTIFF THEMES

The plaintiff's bar has developed a number of themes that translate across most punitive damage cases. Plaintiffs fuel their punitive damage claims by capitalizing on tarnished corporate reputations and generating anger and fear toward the corporation, especially on summation. The following are common plaintiff summation themes that are effective against large corporations:

1. "The Cost of Doing Business"

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[39] *Exxon Shipping v. Baker*, 554 U.S. 471, 501 (2008).

[40] *Gore*, 517 U.S. at 583.

[41] *State Farm*, 538 U.S. at 428.

This theme evokes the "exploding gas tank case," an infamous punitive damage case whose background facts may be somewhat familiar.[42] In that case, the driver and passenger of a Pinto hatchback manufactured by Ford were badly burned when the car burst into flames after being rear ended on the freeway. The trial revealed evidence from which the jury could reasonably find that Ford's management team decided to proceed with the mass production of that model with knowledge that test results revealed significant design defects which rendered the fuel tank extremely vulnerable on rear impact at low speeds and endangered the safety and lives of the occupants. Ford was hit with a punitive damages verdict in excess of $125 million.

The award was upheld on appeal in large part because the court observed that for punitive damages to have the proper deterrent effect, they must be substantial enough that the corporation cannot treat them as a cost of doing business. The court called the threat of punitive damages "the most effective remedy for consumer protection against defectively designed mass-produced articles." Ford's conduct was found unreasonable because the design defects could have been remedied by rather inexpensive "fixes."

The "cost of doing business" theme is a dangerous one for large corporate defendants. Throughout the trial, plaintiff's counsel will have painted the picture that the corporation cut every corner it could to maximize its profits, even at the expense of consumer safety. The profits of the corporation itself and its executive officers will no doubt be well above those of the average juror, and likely the jury panel combined. In an age where corporations are increasingly viewed as bullies, the plaintiff can build a strong narrative that the corporation decided to sacrifice legal cost rather than fix its product or policy, all for the sake of maximizing its profits.

2. "Send a Message"

Plaintiff's counsel will empower the jury to make a tangible impact on society with its punitive damage verdict. After all, this is the jury's opportunity to change the world, to save a life, to leave an impact on society, to regulate the big business because no one else can reach them. It is the jury's "one shining moment." Having already compensated the plaintiff for the damages allegedly suffered at the hands of the company, the jury has the opportunity to exercise their civic duty to ensure that no one else is injured by the company's conduct again. A narrative in summation might look like this:

> There are several important things to consider in your deliberations on punitive damages. First and foremost, are you going to get their attention with the amount of the award? Is Mr. CEO going to be able to walk into upper

[42] *Grimshaw v. Ford Motor Co.*, 119 Cal. App. 3d 757 (Cal. App. 4th Dist. 1981).

> management offices get the attention of the people that need to be attendant and say we have a message and we have a serious problem that we now have to address today?

3. **"Just One Week of Sales"**

This theme was utilized to perfection in the infamous McDonald's "Hot Coffee" case.[43] The background of that case is familiar to many: in a 1994 product liability case against McDonald's, a New Mexico jury awarded $2.7 million in punitive damages to a 79-year-old woman who suffered third-degree burns when she accidentally spilled McDonald's hot coffee in her lap. Plaintiff's counsel implored the jury to consider that McDonald's made $1.35 million each day in coffee sales. The jury presumably arrived at the $2.7 million punitive damages figure by deciding to punish McDonald's for the value of two days of profits made solely from coffee sales.

Because discovery on net worth and other sensitive financial information becomes available in the punitive damage phase, plaintiff's counsel will be positioned to make a similar argument against your corporate client. Worse yet, the numbers can easily be calculated and manipulated to support a persuasive narrative for a large punitive damage verdict. For example, assume your corporate client has been found liable to the plaintiff largely due to a certain policy that it had in place for two years surrounding the subject incident. Your client now faces potential punitive damages for its alleged ratification of that policy. By manipulating the variables, the plaintiff can reasonably ask the jury to issue a punitive damage award that is the equivalent to one week of the company's profits without it seeming like an overreach:

> You have already decided that X Corporation should be punished for its retention and ratification of the policy, a policy which it knew could lead to injuries like the one plaintiff has sustained here. In asking you to issue a punitive damages award that is the equivalent of one week of X Corporation's profits, keep in mind that we are *only* asking that you punish X Corporation for less than one percent -- less than 1/100 -- of the time that dangerous policy was in effect. That's all. Less than one percent.

By strategic references to such variables as time, net worth, number of people who were complicit in the punishable conduct, etc., plaintiff's counsel can make a massive request seem rather small under the circumstances. Plaintiff's counsel can argue that such an award is small enough so as not to cause

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[43] *Liebeck v. McDonald's Rests., P.T.S., Inc.*, No. CV-93-02419, 1995 WL 360309 (N.M. Dist. Ct. Aug. 18, 1994).

significant disruption to the company, yet large enough to send a message and carry out the goals of punitive damages awards.

B. DEFENSE THEMES

Emotions tend to overwhelm reason. Particularly, anger is an emotion that builds on itself, and can spread from person to person. To succeed in a punitive damages case, plaintiff will endeavor to create and stir up anger and emotion with his themes. The corporation will be cast as a villain that chose profits over safety, putting society at large in great danger.

Defense counsel's ability to diffuse the anger is critical to the defense of a punitive damage claim. Using the "Four C's—concession, contrition, causation, and compensation—is an effective means for diffusing the anger during trial and on summation. For trial lawyers who "shoot from the hip" on summation, it should be recognized that the Four C's require a very different approach than a typical trial summation.

Defense trial counsel may deliver two closing arguments in a case involving a viable claim for punitive damages. The first closing will focus on preventing a finding that punitive damages are appropriate. The second will be an effort to limit the award in the event a pro-punitive damage verdict has been rendered.

1. Summation Themes Directed to Avoiding Imposition of Punitive Damages

a) Compliance with Industry Standards

The compliance summation theme is simply the presentation of your regulatory and due diligence defenses, which you will have established through the trial testimony of your clients and expert witnesses. For example:

> Should a company that has followed every single standard, every single regulation, should such a company be found by you folks to have acted unlawfully, maliciously? What more could they have done but follow and exceed these standards? What more could they do?
>
> If any entity is indicted for anything, the first thing you argue against them is that they didn't comply with the standard. Has there been a single witness who said that the company didn't comply with the applicable standards? Has there been anybody who said that they didn't cooperate with all the regulatory entities? Has there anybody who said that they were asked to provide

> materials to a regulatory entity and didn't provide them or provided erroneous information? Is there any such evidence in this case?

b) Good Faith Efforts

Show the jury that the company did even more than what was required of them in the name of product safety.

> You have heard no evidence that a company has to go to the cost and expense of getting a certification, of having an independent entity come in and search the womb of that company, audit them, go through their records and documents, see whether it is right or it is not right. But they get a certification anyways. They do it because it is emblematic of the credibility that this company wanted its product to have. It is symbolic of a product that works and is safe.
>
> You have rejected that. You had the right to do that, but a company that does that, I beseech you to appreciate has not acted unlawfully, has not acted with gross lack of care, has not acted maliciously, has not acted wantonly. Rather, this company has acted in the finest spirit of what it should be trying to do, notwithstanding the shortcomings that you found.

c) Humanize the Company

While the general rule on summation is that you cannot ask the jury to put themselves into a party's shoes, there is no rule against subtly asking them to put the executive officers of the company in the jury's shoes, as hard-working people, just trying to do what is right.

> Plaintiff's counsel will tell you that the way to get our attention is with money. Please appreciate that the folks at X Corporation are folks just like you. This is not a Philip Morris. This is not a huge company. These folks have tried, just like you try every single day, to do the right thing.
>
> That group of people has been profoundly affected by your verdict. They have been told by you that they haven't used enough reasonable care. They have been told that their product is defective, that it is not reasonably safe, notwithstanding the number of lives every year saved in this country by virtue of it. These are proud people.
>
> We ask you to consider the impact of just your compensatory award and what effect it is going to have on this company and

> these people. Don't indict them any further than you have by telling them that they acted unlawfully, wantonly, recklessly, that what they do everyday, year after year, evinces indifference to the well-being of their fellow man.

2. Summation Themes After a Finding in Favor of Punitive Damages - The "Four C's"

When the jury has already found your client's conduct to be unreasonable under the circumstances – whether right or wrong - the jury's verdict must be acknowledged and to a degree, accepted. It is important to practice the tone of your punitive damage summation.

a) Contrition

Insofar as the jury has determined that your client has failed in its obligations to act reasonably under the circumstances, defense counsel should deliver a sincere apology on behalf of the company for its failure to meet the jury's expectations. For instance, if the cause of action arose out of the conduct of a company employee, admit the employee's conduct was in error by the jury's view of reasonableness. That is not to say the apology should whole-heartedly endorse the jury's finding of liability. But defense counsel should be especially careful not to undermine the aptitude of the jury, who has another significant decision to make. Admit the client fell short of the jury's expectation, apologize for the harm the action or actions caused, and then move on to the other three "C's." For example:

> We regret we fell short of your mark. We regret we didn't meet your expectations, but I respectfully suggest to you that the huge compensatory award that you have already issued in this case punishes this company in many ways more than you can possibly imagine, and should be deemed by you to be fair and adequate.

b) <u>Concession</u>

Concession is much like contrition in that the errors are acknowledged, but it uses that acknowledgment to tie in an important defense theme: the human error defense. The key message is that no human, let alone a group of humans working together, as is the case in a large corporation, is perfect. While the idea of a concession on any point may be discomforting, the point is to concede only that the conduct fell short of reasonable, which builds credibility with the jury, but also allows you to draw a sharp distinction between conduct that is "negligent" and conduct that is malicious, willful, reckless, and criminally indifferent to civil obligations. For example:

> Hindsight is both a gift and a curse. It shines a spotlight on all of the things that could have been done better, but gives the company an opportunity to improve. Looking back, there are certainly things that we, as a corporation, could have done better. But the company did set proper rules and standards to keep the business running safely. There is no evidence that anyone's actions were done maliciously, willfully, or recklessly, and certainly never with the intent to cause harm.
>
> They have failed your expectations, but that doesn't mean they weren't trying very hard. That doesn't mean that they were trying to save a penny at the expense of anybody's safety. They nobly tried.

c) <u>Causation</u>

The causation theme employs the corporate defense. Where harm was caused by the conduct of an employee, defense counsel must distance the company from the individual's act. The incident should be described as a result of an isolated employee error that does not reflect the company's values or motives. The individual's lapse of judgment was the direct and sole cause of the incident, which no safety standard or regulation could have prevented. The jury should be convinced that the simplest explanation for the incident is the correct one—that the employee, acting on his own, had an unpredictable lapse of judgment, and that alone was the cause of the incident.

d) <u>Compensation</u>

The compensation theme is perhaps the most important of the Four C's. Remember that the plaintiff will look to utilize an endless number of variables in combination with your client's financial information to make a large punitive damages demand seem reasonable. Thus, the plaintiff's approach will be an exaggerated big-picture view, with reference to the *large* amount of time the conduct occurred, the *large* amount of money the corporation has made over time, the *large* impact the conduct has on the society at large, etc. Your job is to narrow the jury's reference point, focusing the jury's attention to the evidence presented at trial and the specific incident that brings the jury together. To the extent you address the big picture, focus on the utility of the company and the benefits it provides to society.

Like all of the Four C's, compensation is about diffusing anger and imploring the jury to make a fair, practical, and reasonable decision based solely on the evidence. It is important to give the jury some perspective on the goals of punitive damages and argue that those goals have already been met, even without a punitive damages award. The plaintiff has already been made whole for the harm suffered by way of the compensatory damages award. The compensatory

award was the appropriate punishment; any further damages to the plaintiff would result in an unjustified windfall to the plaintiff. Moreover, with respect to deterrence, the deterrent force includes more than just the punitive damages award; it also includes all other costs to the corporation, including legal fees and litigation costs, lost goodwill, and lost business opportunities as a result of adverse publicity.

State	Presence of representative, attorney, or other physician at IME	Permits Recording?
Alabama	Worker's Compensation Statute (b) If requested to do so by the employer, the injured employee shall submit to examination by the employer's physician at all reasonable times, but the employee shall have the right to have a physician of his or her own selection present at the examination, in which case the employee shall be liable to the physician of his or her own selection for his or her services. Ala. Code § 25-5-77	
Alaska	The Supreme Court held that a party in a civil action had the right to have his attorney present during an examination by a physician hired by his opponent Langfeldt-Haaland v. Saupe Enterprises, Inc., 768 P.2d 1144 (Alaska 1989)	YES Supreme Court aligned itself with the authorities which allow plaintiff's counsel to attend and record, as a matter of course, court-ordered medical examinations in civil cases Langfeldt-Haaland v. Saupe Enterprises, Inc., 768 P.2d 1144 (Alaska 1989).
Arizona		YES Court of Appeals held that a plaintiff who claimed that he was entitled to medical benefits for treatment of an osteoarthritic cervical condition, was entitled to use of a tape recorder during medical examination. Burton v. Indus. Comm'n of Arizona, 166 Ariz.

		238, 801 P.2d 473 (Ct. App. 1990)
Arkansas		
California	a) The attorney for the examinee or for a party producing the examinee, or that attorney's representative, shall be permitted to attend and observe any physical examination conducted for discovery purposes, and to record stenographically or by audio technology any words spoken to or by the examinee during any phase of the examination. Cal. Civ. Proc. Code § 2032.510 (West)	Yes – permits audio recording. Cal. Civ. Proc. Code § 2032.510 (West)
Colorado	Plaintiff requested for attorney's paralegal to accompany her to IME. She claimed the paralegal's presence was needed because the physician was biased against plaintiffs in personal injury actions. After her initial motion was denied, plaintiff filed a motion for reconsideration claiming that the paralegal's presence was needed because she suffered from memory loss. The Court held that questions concerning conduct of court-ordered physical examinations of personal injury plaintiffs, including presence of third parties and tape recorders during such examinations, are to be resolved by the trial court in exercise of its discretion. The Court determined that the trial court did not abuse its discretion in denying plaintiff's request because plaintiff initially only alleged that the paralegal's presence was needed to prevent the physician from acting in a biased manner and because plaintiff only claimed memory loss after her motion was denied.	In Trial Court's Discretion. Hayes v. Dist. Court In & For City & Cnty. of Denver, 854 P.2d 1240, 1246 (Colo. 1993)

	Hayes v. Dist. Court In & For City & Cnty. of Denver, 854 P.2d 1240, 1246 (Colo. 1993)	
Connecticut	At least one court has allowed a plaintiff's attorney *8-6 to be in attendance, noting that "in the context of an adversary proceeding, the plaintiffs' interest in protecting themselves from unsupervised interrogation by an agent of their opponents outweighs the defendants' interest in making the most effective use of their expert." Zabkowicz v. W. Bend Co., 585 F. Supp. 635, 636 (E.D. Wis. 1984). The majority view is to preclude a party's attorney from attending the party's examination. See Polcaro v. Daniels, No. KNL-CV-4001700-S, 2007 WL 1299159, *3 (Conn. Super. Ct. Apr. 19, 2007). Even if an examining party does not object to the attendance of counsel, a court could strictly limit the attorney's involvement to be no more than a silent observer. Polcaro v. Daniels, 2007 WL 1299159, at *7.	
Delaware	The Superior Court, held that patients' attorney could not be present at examinations, nor could attorney's office be used as location, but each patient could have her own health care practitioner present as witness and could electronically record proceedings, and maximum length was set at three hours.	YES Rochen v. Huang, 558 A.2d 1108 (Del. Super. 1988)
Florida	Prince v. Mallari, 36 So. 3d 128 (Fla. Dist. Ct. App. 5th Dist. 2010) - a plaintiff being examined in a compulsory medical examination is allowed to have his or her attorney or videographer present to guarantee, for example, that the doctor does not interrogate the plaintiff on liability questions in order to seek damaging admissions or engage in other unfair or improper conduct.	YES Prince v. Mallari, 36 So. 3d 128 (Fla. Dist. Ct. App. 5th Dist. 2010)

Georgia	Worker's Compensation: (b) The employee shall have the right to have present at such examination any duly qualified physician or surgeon provided and paid by him. No fact communicated to or otherwise learned by any physician or surgeon who may have attended or examined the employee or who may have been present at any examination shall be privileged either in hearings provided for by this chapter or in any action at law brought to recover damages against any employer who may have accepted the compensation provisions of this chapter. Ga. Code Ann. § 34-9-202 (West)	
Hawaii	Worker's Compensation: After an injury and during the period of disability, the employee, whenever ordered by the director of labor and industrial relations, shall submit to examination, at reasonable times and places, by a duly qualified physician or surgeon designated and paid by the employer. The employee shall have the right to have a physician or surgeon designated and paid by the employee present at the examination, which right, however, shall not be construed to deny to the employer's physician the right to visit the injured employee at all reasonable times and under all reasonable conditions during total disability. Haw. Rev. Stat. § 386-79 (West)	
Idaho	Upon giving of reasonable notice to the other parties, the party being examined or the person having custody or legal control of the person being examined, shall have the right to have a representative of his or her choice present. I.R.C.P. 35	

Illinois		
Indiana		Yes The Supreme Court held that both the party who is subject to court-ordered medical examination, as well as examiner, may record, by electronic means all aspects of examination. Jacob v. Chaplin, 639 N.E.2d 1010 (Ind. 1994)
Iowa	Worker's Compensation After an injury, the employee, if requested by the employer, shall submit for examination at some reasonable time and place and as often as reasonably requested, to a physician or physicians authorized to practice under the laws of this state or another state, without cost to the employee; but if the employee requests, the employee, at the employee's own cost, is entitled to have a physician or physicians of the employee's own selection present to participate in the examination. Iowa Code Ann. § 85.39 (West)	
Kansas		
Kentucky	Plaintiff brought action against MetLife, his uninsured motorist insurer for personal injuries sustained in an automobile accident caused by the alleged negligence of an uninsured motorist insurer. MetLife moved for an order requiring plaintiff to submit to a physical examination by a physician of their choice. Plaintiff alleged that the physician was biased against personal injury plaintiffs, he objected and requested that a different	In the trial court's discretion. Metro. Prop. & Cas. Ins. Co. v. Overstreet, 103 S.W.3d 31, 39 (Ky. 2003)

	doctor be appointed to conduct the examination. Alternatively, he moved for an order (1) permitting him to videotape the examination and/or permitting a physician or nurse of his choice to attend the examination, and (2) requiring the physician to provide information as to the number of CR 35.01 examinations performed by him during the past year. The lower court permitted the plaintiff to videotape the examination and ordered the physician to provide the information. MetLife appealed. The Supreme Court recognized that an examinee may be entitled to a degree of protection against a physician hired by the adversary, but stated that the recognition of this potentiality does not mean that an external presence should automatically be permitted. The Court noted that an external presence that deprives the examining party of the opportunity to level the playing field by conducting a truly objective examination would destroy the very purpose of Rule 35.01 of Kentucky's Rules of Civil Procedure, which permits independent medical examinations. Therefore the Court held that a trial court may impose an external presence at a CR 35.01 examination only upon a showing of "good cause" by the examinee.	
Louisiana	Plaintiff requested that his IME be videotaped and that his attorney be present at the examination. Plaintiff alleged mental impairment and claimed that his attorney's presence was necessary to prevent a "swearing match". The Court held that Louisiana Code of Civil Procedure Article 1464 does not afford plaintiffs an absolute right to have their attorneys present at the examination and that a plaintiff must present special circumstances that warrant the presence of counsel and videotaping at his IME. The Court did not find that plaintiff present special circumstances that warranted his attorney's	Must present special circumstances. Henry v. Barlow, 2006-283 (La. App. 3 Cir. 8/9/06), 937 So. 2d 895, 898 writ denied, 2006-2592 (La. 1/12/07), 948 So. 2d 153

	presence.	
Maine	Worker's Compensation Examination: The employee has the right to have a physician, surgeon or chiropractor of the employee's own selection present at such an examination, whose costs are paid by the employer. Me. Rev. Stat. tit. 39-A, § 207	
Maryland	The order may also make provision with respect to the right of the party being examined to have a representative present 3 Maryland Civil Procedure Forms § 49:4 (2d ed.)	
Massachusetts	Worker's Compensation: After an employee has received an injury, and from time to time thereafter during the continuance of his disability he shall, if requested by the insurer or insured, submit to an examination by a registered physician, furnished and paid for by the insurer or the insured. The employee may have a physician provided and paid for by himself present at the examination. Mass. Gen. Laws Ann. ch. 152, § 45 (West)	
Michigan	(1) If a court, board or commission, or other public body or officer orders an individual to submit to a physical examination, the order shall notify the individual that he or she has the right to have his or her attorney present at the physical examination	Trial Court will permit videotaping there is good cause. In Muci v. State Farm Mut. Auto. Ins. Co., the Supreme Court permitted that it was proper for

	Mich. Comp. Laws Ann. § 600.1445 (West)	the trial court to impose conditions on an IME which included video taping where the plaintiff proffered evidence that the doctor previously engaged in inappropriate questioning. Muci v. State Farm Mut. Auto. Ins. Co., 478 Mich. 178, 193, 732 N.W.2d 88, 96-97 (2007)
Minnesota	Worker's Compensation Examination: The employee is entitled upon request to have a personal physician present at any such examination Minn. Stat. Ann. § 176.155 (West)	
Mississippi		
Missouri	In Jensen v. Wallace, 671 S.W.2d 331 (Mo. Ct. App. 1984), the plaintiff sought to have his attorney accompany him to a physical examination by the defendant's expert. Id. at 331–32. The trial court refused the request and dismissed the plaintiff's case when the plaintiff failed to comply with its order requiring him to be examined by the doctor out of the presence of his attorney. Id. at 332. The plaintiff's principal argument on appeal was that he was constitutionally entitled to the assistance of counsel at a Rule 60.01 court-ordered medical examination. Id. The Missouri Court of Appeals found that while the court-ordered medical examination is certainly part of the discovery process, it is not a stage of the litigation that presumptively requires the presence of a party's attorney. Id. at 333.	In the trial court's discretion. In Ratcliff v. Sprint Missouri, Inc., 261 S.W.3d 534 (Mo. Ct. App. 2008) the Missouri Court of Appeals held that the trial court acted within its discretion in not granting a protective order allowing a worker to record the independent psychological examination of him by a telephone company's doctor in a worker's premises liability action arising from a worker's accident while the company was working in his building, where Missouri's rule authorizing IME's was silent on the recording of exams, the purpose of the recording, is to help with the deposition and cross-examination of the doctor, and was purely adversarial and thus inconsistent with the purpose

		of the rule, that being the elimination of uncertainty of medical aspects of the cause and the preparation of an intelligent defense.
Montana	Plaintiff requested presence of his attorney at his IME because he claimed the physician would be bias since he conducts IME's solely for the benefit of insurance companies. The Court held that these were insufficient grounds to permit the attorney to be present. The Court noted that when a party ordered to submit to a physical examination sufficiently demonstrates subjective predilections or the likelihood of prejudice, that is, the exam shifts from independent in nature to adversarial, litigants and courts should rely upon the state's rule allowing for issuance of protective orders that specifies terms and conditions of the discovery, and rule requiring court to specify time, place, manner, conditions, and scope of examination and the person or persons by whom it is to be made. Additionally the court noted that the matter of whether to impose checks and balances, such as representation or recording devices, upon the independent medical examination process is left to the discretion of the trial courts, and is to be determined based on the facts presented and authority derived from case law, discovery rule allowing for issuance of protective orders that specifies terms and conditions of the discovery, and rule requiring court to specify time, place, manner, conditions, and scope of examination and the person or persons by whom it is to be made. Rules Civ.Proc., Rules 26(c), 35(a). Hegwood v. Montana Fourth Judicial Dist. Court, 75 P.3d 308, 317 Mont. 30 (2003).	In the trial court's discretion. Hegwood v. Montana Fourth Judicial Dist. Court, 75 P.3d 308, 317 Mont. 30 (2003). Pretrial Procedure

	Pretrial Procedure	
Nebraska	Worker's Compensation Examination: The employee shall have the right to have a physician provided and paid for by himself or herself present at the examination. Neb. Rev. Stat. § 48-134	
Nevada		
New Hampshire	Worker's Compensation The employee shall have the right to have a health care provider designated and paid by himself or herself present at such examination. N.H. Rev. Stat. Ann. § 281-A:38	
New Jersey	Clients may be apprehensive about an examination to be conducted by an unfamiliar doctor. It is not uncommon for clients to want to have a familiar person present while they are examined. So too, attorneys may be apprehensive about an examination of their client to be conducted by the adversary's expert. It is not uncommon for attorneys to want to be present while their clients are being examined. Rule 4:19 (statute authorizing IME) is silent on who may be present. 42 N.J. Prac., Discovery § 5.11	

New Mexico	F. No attorney shall be present at any examination authorized under this section. N.M. Stat. Ann. § 52-1-51 (West)	
New York	A party is entitled to be examined by the defendant's chosen medical examiner in the presence of his or her attorney or other representative unless the defendant makes a positive showing of necessity for the exclusion of such an individual Jessica H. ex rel. Arp v. Spagnolo, 41 A.D.3d 1261, 839 N.Y.S.2d 638 (4th Dep't 2007); A.W. v. County of Oneida, 34 A.D.3d 1236, 827 N.Y.S.2d 790 (4th Dep't 2006); Mosca v. Explorer Charters, Ltd., 194 Misc. 2d 360, 754 N.Y.S.2d 823 (Sup 2002). The role of an attorney or representative at a party's physical examination is limited to that of observer, and no interference with or restrictions upon the physical examination are permitted. The party's attorney or representative may include a registered nurse. Absent any valid countervailing reason, the presence at the physical examination of the party's chosen representative, including a physician, should be allowed. Grange v. Sweet, 4 Misc. 3d 470, 779 N.Y.S.2d 775 (Sup 2004). 44A N.Y. Jur. 2d Disclosure § 324	There is no express statutory authority granting plaintiffs the right to videotape their IME. The leading case in NY is a third department case from 1989. Lamendola v. Slocum, 148 A.D.2d 781, 538 N.Y.S.2d 116 (1989). In Lamendola, the court held that a plaintiff was not permitted to videotape their IME absent special and unusual circumstances. Id. See also, Alice Spitz, Law Does Not Support Videotaping IMEs, NEW YORK LAW JOURNAL, Nov. 20 , 2013.
North Carolina	Worker's Compensation The injured employee has the right to have present at the independent medical examination any physician provided and paid by the employee. N.C. Gen. Stat. Ann. § 97-27 (West)	

North Dakota	Worker's Compensation - The injured employee may have a duly qualified doctor designated by that employee present at the examination or later review the written report of the doctor performing the independent medical examination, if procured and paid for by that employee. N.D. Cent. Code Ann. § 65-05-28 (West)	
Ohio	Motorist filed personal injury suit against tortfeasor, seeking recovery for injuries sustained in automobile accident. Motorist's attorney was present at IME and later testified about what happened at the IME. Court held that although plaintiff had the right to have his attorney present during the examination, the attorney did not have the right to testify as to what occurred during the IME at trial. Thomas v. Vesper, 2003-Ohio-1856, ¶ 27	
Oklahoma	D. REPRESENTATIVE MAY BE PRESENT. A representative of the person to be examined may be present at the examination. Okla. Stat. Ann. tit. 12, § 3235 (West)	Yes. The Oklahoma Supreme Court has held that the relevant provision of the IME statute allowing a representative to be present includes the right to videotape the examination. See Boswell v. Schultz, 2007 OK 94, 175 P.3d 390. In Fisch v. Stuart, 2014 OK 59, 2014 WL 2782219, the Court extended the rule to neuropsychological exams. In both instances, the trial court has the authority to enter a protective order after holding a hearing "to determine the appropriate examination safeguards necessary to provide all parties with their full statutory rights." Id. at ¶5

Oregon	Trial court granted defendant's motion to require plaintiff to be examined by independent physician in the absence of plaintiff's attorney. The Supreme Court held that whether or not counsel can insist on being present at a medical examination of his client by a physician other than the treating physician, is a matter largely within the discretion of the trial court Pemberton v. Bennett, 234 Or. 285, 287, 381 P.2d 705, 706 (1963)	
Pennsylvania	The person to be examined shall have the right to have counsel or other representative present during the examination. Pa.R.C.P. No. 4010	
Rhode Island	The employee shall have the right to have a physician provided by the employee and paid for by the employer present at the examination. R.I. Gen. Laws Ann. § 28-33-34 (West)	
South Carolina	The physician of the party to be examined may be present at the examination.	
South Dakota		
Tennessee	Worker's Compensation: (d)(1) The injured employee must submit to examination by the employer's physician at all reasonable times if requested to do so by the employer, but the employee shall have the right to have the employee's own physician present at the examination, in which case the employee shall be liable to the employee's physician for that physician's services.	

Texas		
Utah	Plaintiff sued defendant for personal injuries resulting from an automobile collision. The trial court denied plaintiff's requests to have her chiropractor present at the time of her IME with a neurologist and to videotape the IME, but allowed plaintiff to be accompanied by a neurologist of her choosing. Plaintiff claimed error in that there was no "appropriate" monitor to ensure that the IME was properly performed. The Court of Appeals held that it was within the trial court's discretion to require plaintiff to be accompanied by a neurologist, rather than her chiropractor, during her IME and that because chiropractors and neurologists are trained in different fields a chiropractor is not qualified to evaluate a neurologist's performance.	No Astill v. Clark, 956 P.2d 1081, 1088 (Utah Ct. App. 1998)
Vermont		
Virginia	Worker's Compensation -The employee shall have the right to have present at such examination any duly qualified physician or surgeon provided and paid by him. Va. Code Ann. § 65.2-607 (West)	
Washington	(2) *Representative at Examination.* The party being examined may have a representative present at the examination, who may observe but not interfere with or obstruct the examination. Wash. Super. Ct. Civ. R. 35	

West Virginia	In a personal injury action, plaintiff appeared at his IME with a legal stenographer. The physician objected to the stenographer's presence and plaintiff refused to proceed with the examination without the stenographer. Defendants filed a motion to compel discovery, which the court granted, disallowing the stenographer's presence. A second examination was scheduled, but plaintiff insisted on bringing a tape recorder along to document the examination. The physician again objected that this would be intrusive and unfruitful, a neurological examination being "neither verbal nor auditory, nor otherwise capable of recordation." The defendants moved to compel discovery without the tape recorder, which motion the court granted. The court refused, however, to require the defendants to disclose to plaintiff or his counsel in advance the precise types of tests the physician would conduct or the manner in which they would be conducted. Plaintiff subsequently a writ of prohibition with the Supreme Court of Appeals. The Court granted the writ and held that the plaintiff was entitled to prior notice of the scope and manner of the examination, but also held that a third party should not be allowed to be present, nor should a tape recorder be allowed, absent showing of good cause. The Court noted that good cause should be a circumstance that implies that truth-finding function of the examination may be threatened absent the requested presence. State ex rel. Hess v. Henry, 183 W. Va. 28, 31, 393 S.E.2d 666, 669 (1990)	Not permitted absent a showing of good cause. State ex rel. Hess v. Henry, 183 W. Va. 28, 31, 393 S.E.2d 666, 669 (1990)

Wisconsin		
Wyoming	Worker's Compensation Statute (a) In any contested proceeding, the hearing examiner may appoint a duly qualified impartial health care provider to examine the employee and give testimony. The fee for the service shall be as ordered by the hearing examiner, with mileage allowance as is allowed to other witnesses to be assessed as costs and paid as other witness fees are paid. The employer or employee may, at his own expense, also designate a qualified health care provider who may be present at the examination of the employee and give testimony at later hearings. Wyo. Stat. Ann. § 27-14-604 (West)	

LIVING IN A MATERIAL WORLD:

A 50-STATE SURVEY OF APPLICATION

MISREPRESENTATION LAWS

FDCC Winter Convention
The Hotel Del Coronado
San Diego, California
February 28 - March 4, 2016

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Living in a Material World: A 50-State Survey of Application Misrepresentation Laws

I. INTRODUCTION

This article examines the major issues that insurers face when considering whether to rescind a policy or contest the availability of coverage based upon material misrepresentations or omissions by the policyholder, and summarizes the statutory and common law frameworks that govern rescission remedies across the fifty states.

The law surrounding misrepresentations derives largely from the general law of contracts. *Couch on Insurance*, § 81:1. When entering into an insurance contract, one party possesses superior information that may affect whether another party is willing to underwrite the risk presented, or willing to assume the risk for as low a price. *Id*. The law of misrepresentation stems from the basic contractual principle that a party that has been deprived of some necessary information will not be held to the terms of the contract. *Id*.

Generally, representations are statements "offered by the insured as a basis for contracting." *Couch on Insurance*, § 81:5. Accordingly, if the insured intentionally, or in some instances negligently, offers incorrect information on an application or during negotiations for insurance, the insurer may be able to either rescind the policy prior to a loss, or assert the misrepresentation as an affirmative defense to coverage once a loss occurs.

II. ELEMENTS OF MISREPRESENTATION

A. Materiality

A threshold inquiry in almost all states is whether a misrepresented fact was material. Materiality is generally a question of fact and judged by an objective standard. There is an abundance of case law molding the boundaries of what is, and what is not, material, with each state having its own slight variation on the basic test for determining materiality. Before an insurer may avail itself of rescission to avoid liability under a policy, it must demonstrate that the incorrect fact was material. Almost all courts

require some form of material misrepresentation before they will allow an insurer to rescind the policy or deny coverage.

Courts generally find that an insured's misrepresentation or omission of fact regarding a question specifically asked on an insurance application is material. Along those same lines, insurers may face significant challenges in attempting to show materiality regarding topics not addressed on the application. *See, e.g.*, *Collins v. Pioneer Title Ins. Co.*, 629 F.2d 429 (6th Cir. 1980) (recognizing presumption that information not requested is immaterial). Insurers may face similar challenges to show materiality when the insured's circumstances change after initial policy issuance and the insured renews the policy without requiring an updated verification of information.

There are three approaches to materiality. The majority of states inquire whether a fact is regarded as material by all similar insurers. The second test, also known as the objective test, considers only what a reasonable and prudent insurer would regard as material. *See, e.g.*, American *General Life Insurance Co. v. Schoenthal Family, LLC*, 555 F.3d 1331 (11th Cir. 2009). Finally, some courts determine materiality by asking whether the particular individual insurer regarded the undisclosed facts as material to the contract.

Jurisdictions are split when determining whether the misrepresented fact must relate to the cause of the loss. The minority of courts allow coverage to be avoided only when the false representations specifically relate to the cause of loss. *See Howard v. Aid Assoc. for Lutherans*, 272 N.W.2d 910 (Minn. 1978). The majority of courts, however, determine materiality by the extent to which the misrepresentation influenced the insurer's decision to underwrite the risk, and disregards the causal connection between the false statement and loss. *Id*. Accordingly, an insurer must demonstrate, usually through the use of underwriting manuals and memoranda, and appropriate witness testimony, that it would not have issued the policy for the premium provided or assumed coverage at all had the true facts been known.

B. Reliance

Reliance generally refers to whether the insurer relied on the specific misrepresented information in issuing the insurance policy. Whereas materiality largely turns upon objective criteria, an insurer seeking to show reliance must generally satisfy a more subjective

standard. While not all jurisdictions explicitly require a showing of reliance as a separate factor from materiality, it is an implicit requirement in almost every jurisdiction that the insurer decided to underwrite the policy based upon its reliance on the misrepresentation. However, courts rarely address the issue of reliance directly.

C. Intent

The majority of jurisdictions allow rescission for misrepresentation or omission of material fact. Here, the material misrepresentation allows for coverage avoidance if the insured provides even an innocent misrepresentation or omission. As long as the misrepresentation is material to the insured's decision to issue coverage, the insured's intent in making the misrepresentation is not a required factor in the court's analysis.

However, some states provide that a misrepresentation must be made with an "actual intent to deceive" to avoid coverage. This minority approach allows for rescission of a policy for any representation, material or immaterial, that the insured knew was false and made with the intent to deceive.

III. SPECIAL CONSIDERATIONS

A. Insurer's Duty to Investigate

An insurer can generally rescind a policy if the insured concealed material facts when responding to application inquiries. *Rallod Transp. Co. v. Continental Ins. Co.*, 727 F.2d 851, 853 (9th Cir. 1984). Typically, insurers are permitted to rely on the representations made by an insured in the application process. Insurers are generally not required to investigate the truths of these representations prior to the policy's issuance. However, insureds are not obligated to volunteer information that the insurer did not request on its application or during investigations.

The duty to investigate usually arises if the insurer possesses sufficient information that puts it on notice that a possible misrepresentation occurred, and such information would lead a reasonably prudent insure to begin an inquiry into the representation. *Silver v. Colo. Cas. Ins. Co.*, 219 P.3d 324, 331 (Colo. App. 2009); *Miguel v. Metropolitan Life Ins. Co.*, 220 Fed.Appx. 961, 969, 2006 WL 2971331 (11th Cir. 2006).

If a duty to investigate is triggered, and the insurer fails to fulfill its duty, then it will be prohibited from asserting misrepresentation as a defense to coverage under the policy. Essentially, courts will bar the insurance company from rescinding a policy based upon a misrepresentation if the insurer knew of the falsity of the statement. *State Farm Mut. Auto Ins. Co. v. Price*, 396 N.E.2d 134, 136 (In. 1979). Courts also may impose a duty to investigate upon the insurer when its failure to do so would have been reckless. *Kraus v. Prudential Ins. Co. of America*, 799 F.2d 502, 505 (9th Cir. 1986).

B. Duty to Disclose

As the insured is largely in sole possession of the factual information most relevant to the risk, the majority of courts require applicants to disclose facts that are material to the hazard assumed by the insurance company. Generally, insureds are held to a standard of good faith, in that all of their answers were made in good faith and made to the best of his or her knowledge and belief. *See, e.g.*, *Dean v. Nationwide Life Ins. Co.*, 536 P.2d 1122, 1125 (Idaho 1975); *Royal Maccabees Life Ins. Co. v. Malachinski*, 161 F.Supp.2d 847 (N.D. Ill. 2001) (requiring an applicant to provide "full and complete disclosure of all relevant information" when answering the application's questions).

However, some states allow rescission for an insured's material misrepresentation regardless of whether the answers were provided in good faith. *See*, *e.g.*, *Nationwide Mut. Ins. Co. v. McBriety*, 230 A.2d 81 (Md. 1967).

C. Duty to Update

A duty is upon the insured to update an insurer with any material change between the time the application was made and the time of the policy's issuance and delivery. Courts place on the insured a continuing duty to update until the policy has issued. *Valley Farms, Ltd. v. Transcontinental Insurance Co.*, 78 P.3d 1070 (Ariz. App. 2003). It generally terminates once the application has been accepted and the policy delivered to the insured. *Gargano v. Liberty Int'l Underwriters, Inc*., 575 F. Supp. 2d 300, 308 (D. Mass. 2008) *aff'd*, 572 F.3d 45 (1st Cir. 2009).

D. Effect on Mortgagee's Right of Recovery

There is a split of authority regarding the effect of misrepresentations on mortgagees. Some states hold that the mortgagee's rights are unaffected by any act or neglect of the insured. Others, however, hold that a policy may be rescinded as it relates to both the insured and mortgagee if it is a false representation affecting a material risk.

However, some mortgage clauses provide that a mortgagee's interest is unaffected by the acts or omissions of the mortgagor. Courts find that such a clause creates a new contract between the mortgagee and insurer, thereby immunizing the mortgagee from any misrepresentations made by the mortgagor in procuring the insurance. *Meade v. North Country Co-op. Ins. Co.*, 487 N.Y.S.2d 983 (Sup. 1985).

E. Effect on Rights of Innocent Insured

Coverage for the "innocent insured" generally implicates situations wherein an insured who did not make a material misrepresentation seeks coverage under a policy despite the wrongdoing of another insured. There is a split of authority pertaining to the rights of an innocent insured. States are generally more willing to allow recovery where the innocent party is an injured third-party to the contract. However, some states allow for rescission of an innocent party's coverage based upon the misrepresentations of the other insured.

Whether a policy provides coverage for an innocent insured often depends on the language of the policy itself. For example, severability provisions may be applied to prevent rescission with regard to coverage for an innocent insured. *See, e.g.*, *In re HealthSouth Corp.*, 308 F.Supp.2d 1253 (N.D. Ala. 2004). Indeed, some policies expressly contain innocent insured provisions in the insurance contract itself. *See, e.g.*, *Bryan Bros. v. Continental Cas. Co.*, 660 F.3d 827 (4th Cir. 2011) (finding, however, that coverage was otherwise precluded by a "prior knowledge" provision). Therefore, the determination of whether an innocent insured is covered by the policy may ultimately depend on the language of the policy, notwithstanding of the split of authority among states.

F. Online Applications

Misrepresentations related to insurance applications completed online is an emerging trend that will likely present unique evidentiary issues. The threat of data loss and incorrect information entered by the

applicant, *e.g.*, "clicked the wrong box," is likely to put pressure on insurers to implement verification and data security measures. Insurer will likely need to ensure that insurance applications submitted online are maintained in their original format and accurately reflect the information actually submitted by the applicant. Insurers may also become targets of data manipulation claims. At least one insurer has faced claims it entered additional information after the applicant's submission of its application. *Nationwide Property & Cas. Ins. Co. v. Faircloth*, 2015 WL 4943962, *4 (E.D. Ark. Aug. 19, 2015).

Insurers should be prepared to offer affidavits and testimony from Information Technology ("I.T.") employees regarding how the application procedures works, how the data is stored and retrieved, and any safeguards that have been implemented to avoid incorrect or inadvertent information being supplied by the applicant.

G. Waiver or Estoppel

An insurer must be aware of actions that it takes which may lead an insured to believe that he/she does not need to disclose or comply with certain policy provisions. Where an insurer waives or accepts a misrepresentation, the effect is as though there had been no misrepresentation. A waiver is generally a final act that cannot be withdrawn.

When an insurer fails to act in good faith in addressing or acting upon a material misrepresentation, it may be estopped from asserting misrepresentation as a defense. Courts have found that insurers may waive the right to rescission for a failure to exercise due diligence in its underwriting process; for misrepresentations made on an application by the insurer's agent and without the insured's knowledge; for attempting to avoid coverage after liability arising under the policy has been incurred; or for failing to act promptly to rescind the policy after the insurer has knowledge of facts that would give it the right to rescind the policy, among other reasons. *See LeMaster v.USAA Life Ins. Co.*, 922 F.Supp 581 (M.D. Fla. 1996) (due diligence in underwriting process); *Laura Campbell Trust v. John Hancock Life Ins. Co.*, 411 F.Supp.2d 606 (D. Md. 2006) (citing *Breault v. Berkshire Life Ins. Co.*, 821 F.Supp. 410, 416 (E.D. Va. 1993) (misrepresentation by insurer's agent)); *Ramsey v. Penn Mut. Life Ins. Co.*, 787 F.3d 813 (6th Cir. 2015) (attempting to avoid policy after liability incurred); *Continental Ins. Co. v. Kingston*, 114 P.3d 1158, 1162-63 (Utah

App. 2005) (failing to act promptly to rescind or reserve right to rescind; listing cases).

H. Other Considerations

There are additional considerations related to misrepresentation and rescission of a policy which may not be addressed above or in the state-by-state discussion below. For example, some states require the application to be attached to the policy itself in order for the insurer to validly rescind an insurance policy. *See, e.g.*, MINN STAT. § 60A.08 subd. 11. In addition, an insurer's right to rescission is often dependent on language contained in the application or policy itself. While this article generally discusses the law related to misrepresentation on insurance applications and rescission due to those misrepresentations, many states have developed unique approaches to rescission under certain circumstance and independent grounds for rescission which are not addressed by this article.

IV. MISREPRESENTATION BY STATE

Alabama

Alabama primarily regulates rescission of insurance policies by statute. *See* ALA. CODE § 27-14-7. Under Alabama law, misrepresentations made by an insured on his application or during the negotiation for insurance may void the policy if those misrepresentations were (1) fraudulent, (2) material either to the acceptance of the risk or to the hazard assumed by the insurer; or (3) the insurer relied in good faith on the applicant's misrepresentations to its detriment in issuing the policy. *See* ALA. CODE § 27-14-7(a). The statute indicates that the insurer's reliance is to its detriment if "[t]he insurer in good faith would either not have issued the policy or contract, or would not have issued a policy or contract at the premium rate as applied for, or would not have issued a policy or contract in as large an amount or would not have provided coverage with respect to the hazard resulting in the loss if the true facts had been made known to the insurer as required either by the application or for the policy or contract or otherwise." ALA. CODE § 27-14-7(a)(3).

Alabama's statute does not require that an insured's misrepresentation be made with the intent to deceive; even innocent misrepresentations may be sufficient to void the policy. *See, e.g.*, *Alfa Life Ins. Corp. v. Lewis*, 910 So.2d 757 (Ala. 2005). The misrepresentation

must only be "a material contributing influence that induced the insurer to issue the policy." *Id.* at 762. While materiality of a misrepresentation is generally a jury question, some misrepresentations may be found material as a matter of law. *Id.*; *see also Clark v. Alabama Farm Bureau Mut. Cas. Ins. Co.*, 465 So.2d 1135 (Ala. App. 1984). For example, the court in *Lewis* found that a misrepresentation as to medical diagnoses, while made innocently, was material as a matter of law because the application clearly stated that eligibility for insurance was dependent on the answer to the question. *Lewis*, 910 So.2d at 762.

An insurer may waive one or more of its protections under the statute. For example, in *State Farm General Ins. Co. v. Oliver*, 658 F.Supp. 1546, (N.D. Ala. 1987), the Northern District Court of Alabama denied rescission of a policy for innocent, yet material, representations because it found that the insurer contractually excused innocent misrepresentations. The policy's terms only provided for rescission due to *intentional* concealment or misrepresentation. The insurer therefore waived its right to rescind innocent material misrepresentations as provided by statute. *See id.* at 1550; *see also In re HealthSouth Corp.*, 308 F.Supp.2d 1253 (N.D. Ala. 2004).

Alaska

Much like Alabama, insurance policies in Alaska may be rescinded where misrepresentations, omissions, concealment of facts, and incorrect statements are "(1) fraudulent; (2) material either to the acceptance of the risk, or to the hazard assumed by the insurer; or (3) the insurer in good faith would either not have issued the policy or contract, or would not have issued a policy or contract at the premium rate as applied for, or would not have issued a policy or contract in as large an amount or would not have provided coverage with respect to the hazard resulting in the loss if the true facts had been made known to the insurer as required either by the application or for the policy or contract or otherwise." *See* ALASKA STAT. § 21.42.110.

Common law interpreting Alaska's statute is sparse. However, it appears that Alaska does not require that misrepresentations be made with the intent to deceive. *See Bennett v. Hedglin*, 995 P.2d 668 (Alaska 2000). In *Bennett*, the Supreme Court of Alaska held that a rescission was proper under the statute because the misrepresentation was "material to the insurer's acceptance of the risk." *See id.* at 671.

Arizona

An insurer must prove all three elements contained in the statute in order to avoid coverage. As such, the insurer must show that the misrepresentation or omission of fact was "(1) fraudulent; (2) material either to the acceptance of the risk, or to the hazard assumed by the insurer; or (3) the insurer in good faith would either not have issued the policy or contract, or would not have issued a policy or contract at the premium rate as applied for, or would not have issued a policy or contract in as large an amount or would not have provided coverage with respect to the hazard resulting in the loss if the true facts had been made known to the insurer as required either by the application or for the policy or contract or otherwise." ARIZ. REV. STAT. § 20-1109; *see also Greves v. Ohio State Life Ins. Co.*, 821 P.2d 757, 764 (Ariz. App. 1991). Generally, "an insurer must prove that the insured committed actual or legal fraud that was material to the insurer's accepting [a] risk" in order to avoid coverage for that risk. *Valley Farms, Ltd. v. Tanscon Ins. Co.*, 78 P.3d 1070 (Ariz. App. 2003).

Actual fraud requires an intent to deceive while legal fraud does not. *Valley Farms*, 76 P.3d at 1074. Regardless of the insured's intent, "legal fraud" exists if a question asked in an insurance application "is one where the facts are presumably within the personal knowledge of the insured, and are such that the insurer would naturally have contemplated that his answers represented the actual facts" when the insured's representations actually were false. *Id.* However, if the insured's responses were to be naturally contemplated as representing opinion, actual intent to deceive is required. *Id.*

Materiality of a misrepresentation in an insurance application "exists if the facts, if truly stated, might have influenced a reasonable insurer in deciding whether to accept or reject the risk." *Medical Protective Co. v. Pang*, 606 F.Supp.2d 1049, 1058 (D. Arizona 2008) (citing *Central Nat'l Life Ins. Co. v. Peterson*, 529 P.2d 1213 (Ariz. App. 1975)).

Arkansas

Arkansas' misrepresentation statute is limited to life, accident, and health insurance policies and annuity contracts. ARK. CODE ANN. § 23-79-107. Arkansas has adopted the general statutory scheme common in many other states, which allows rescission of a policy for misrepresentations, omissions, concealment of facts, and incorrect statements that are (1) fraudulent; (2) material either to the acceptance of the risk or to the hazard assumed by the insurer; or (3) such that they would affect the insurer's good faith decisions to issue the policy, issue the policy in the amount or at the premium rates that it did, or would not have issued coverage with respect to a certain hazard if facts had been known to the insurer as required by the application for the policy or contract or otherwise. *Id.; see also Neill v. Nat'l Mut. Fire Ins. Co.*, 139 S.W.2d 484 (Ark. 2003).

The statute also provides that there is a presumption of materiality when misrepresentations are made regarding medical impairments. ARK. CODE ANN. § 23-79-107(b). A presumption of materiality also exists where there is a causal relationship between the misrepresentation and the hazard resulting in a loss under the policy or contract. *Id.* § 23-79-107(c).

As with most states, the insurer bears the burden to prove that the undisclosed facts were material to the risk assumed or that in good faith it would not have issued the policy had it known the true facts. *Burnett v. Philadelphia Life Ins. Co.*, 101 S.W.2d 843 (Ark. App. 2003). Generally, an insurance company may retroactively rescind the policy because of fraud or a material misrepresentation of the insured. *Neill v. Nat'l Mut. Fire Ins. Co.*, 139 S.W.3d 484 (Ark. 2003).

While not required in Arkansas, the insurer may rescind the policy if the misrepresentation was made with the intent to deceive the insurer. *See Mo. State Life Ins. Co. v. Witt*, 256 S.W. 46 (Ark. 1923).

California

California regulates rescission of policies for misrepresentation through a collection of statutes and common law. In California, each party to an insurance contract must communicate in good faith all facts which he believes to be material to the contract and to which the other party does not have the means to ascertain independently. CAL. INS. CODE § 332. A fact is "material" based on the "probable and reasonable influence" of that fact on a party's decision to enter into the contract or to determine the

terms upon which he or she will enter into the contract. CAL. INS. CODE § 334.

Materiality may be determined as a matter of law where no reasonable person can disagree as to its materiality. *See Fed. Ins. Co. v. Homestore, Inc.* 144 Fed. App'x. 641, 2005 WL 1926483 (9th Cir. 2005). For example, misrepresentations as to specific questions asked on an application for insurance may be sufficient to find that the misrepresentation was material as a matter of law. *Thompson v. Occidental Life Ins. Co.*, 109 Cal. Rptr. 473 (Cal. 1973); *Butcher v. Gulf Ins. Co.*, 2005 WL 1514086 (N.D. Cal. 2005). In other words, questions specifically asked by the insurer on the application represent "material" information.

The intent to deceive is not require to rescind a contract of insurance. CAL. INS. CODE §§ 330-331.

Rescission generally applies to all insureds regardless of which insured made the misrepresentation, unless the policy provides otherwise. CAL. INS. CODE § 650. In *Fed. Ins. Co. v. Homestore, Inc.*, the Ninth Circuit Court of Appeals applied California law to find that rescission was effective as to directors and officers of the insured company based on the misrepresentation of the individual who signed the application. 144 Fed. App'x 641, 2005 WL 1926483 (9th Cir. 2005); *see also TIG Ins. Co of Mich. V. Homestore, Inc.*, 2004 WL 2418318 (N.D. Cal. 2004) (finding that D&O insurer's rescission was effective as to all insureds even though misrepresentation made by CFO only).

Colorado

In Colorado, rescission generally requires an insured to make misrepresentations or omissions that are material and made knowingly. Colorado does not require an intent to deceive; however, it does require the applicant to have made the false or misleading statements knowingly. *Wade v. Olinger Life Ins. Co.*, 560 P.2d 446, 452 (Colo. 1977) (citing *Hollinger v. Mut. Benefit Life Ins. Co.*, 560 P.2d 824, 826 (Colo. 1997)). Whether the applicant's misrepresentation omission was made "knowingly" is determined by an objective standard. *Hollinger v. Mut. Benefit Life Ins. Co.*, 560 P.2d 824, 826 (Colo. 1997).

Connecticut

With some exceptions, the insurer must prove that the applicant knowingly made an untrue statement or representation that was material to the insurer's decision to insure. *See Middlesex v. Mut. Assur. Co. v. Walsh*, 590 A.2d 957 (Conn. 1996); *Pinette v. Assurance Co. of Am.*, 52 F.3d 407 (2nd Cir. 1995); *Mt. Airy Ins. Co. v. Millstein*, 928 F.Supp. 171 (D. Conn. 1996).

Intent to deceive is not required; however, if not made with the intent to deceive, the misrepresentation must be material and must be made knowingly. *Paul Revere Life Ins. Co. v. Pastena*, 725 A.2d 996 (Conn. App. 1999). That is, it must have been "known by the insured to be false when made." *Id.* Innocent misrepresentations are not adequate grounds for rescission. *Conn. Indem. Co. v. Perrotti*, 390 F.Supp.2d 158 (D. Conn. 2005).

Reliance is not required. The insurer need not prove that it relied on the misrepresentation or concealment in order to rescind the policy. *Rego v. Connecticut Ins. Placement Facility*, 219 Conn. 339 (1991).

Delaware

Delaware regulates rescission for all contracts of insurance by statute. DEL. CODE §2711. Delaware follows the general scheme applied by many states, which allows rescission for misrepresentations, omissions, concealment of facts, and incorrect statements that are "(1) fraudulent; (2) material either to the acceptance of the risk or to the hazard assumed by the insurer; or (3) such that they would affect the insurer's good faith decisions to issue the policy, issue the policy in the amount or at the premium rates that it did, or would not have issued coverage with respect to a certain hazard if facts had been known to the insurer as required by the application for the policy or contract or otherwise." *Id.*

While common law interpreting the statute is sparse, it indicates that the insurer must show that the insured knew, or should have known, that his or her response was false, misrepresented the truth, or concealed a material fact. *Grand Fraternity v. Keatley*, 27 Del. 308 (Del. 1913).

District of Columbia

Washington D.C. federal district courts allow rescission when the applicant made a statement that is (1) false and (2) is material in that it affected the insurer's risk of loss in issuing the policy. *Nat'l Union Fire Ins.*

Co. of Pittsburgh, Pa. v. Mason, Perrin & Kanovsky, 765 F.Supp. 15 (D.D.C. 1991). An insurer may also rescind the policy if the applicant made a misrepresentation with the intent to deceive. *Id.* The insurer seeking to rescind the policy must prove these elements by a "preponderance of clear and satisfactory evidence." *Id.*

Florida

Florida primarily regulates rescission by statute. FLORIDA STAT. § 627.409. The statute's text differs from most other states, but the general principles remain the same. With some exceptions, the following may prevent recovery under an insurance or annuity contract: (1) the misrepresentation, omission, concealment, or statement is fraudulent or is material to the acceptance of the risk or to the hazard assumed by the insurer; or (2) if the true facts had been known to the insurer pursuant to a policy requirement or other requirement, the insurer in good faith would not have issued the policy or contract, would not have issued it at the same premium rate, would not have issued a policy or contract in as large an amount, or would not have provided coverage with respect to the hazard resulting in the loss. *Id.*

The misrepresentation only needs to be material; intent to deceive is not required. *First Nat'l Bank Holding Co. v. Fid. And Deposit Co. of Md.*, 885 F.Supp.1533 (N.D. Fla. 1995). Therefore, even an unintentional misstatement will prevent coverage if it materially affected the risk accepted by the insurer. *Id.*

Reliance is required. The insurer must prove that the insurer relied on the misrepresentation, concealment, or omission when it entered into the insurance contract. *Griffin v. Amer. Gen. Life & Acc. Ins. Co.*, 752 So.2d 621 (Fla. App. 1999).

The fact that an insurer may investigate to verify certain answers does not defeat the insurer's right to rescind the policy. *Talley v. National Standard Life Ins. Co.*, 178 So.2d 624 (Fla. D. Ct. App. 1965) (noting that an insurer's investigation into an applicant's responses "does not absolve the applicant for insurance from a duty to speak the truth").

Georgia

Georgia's statute takes the common form adopted by many other states. O.G.C.A. § 33-24-7. That statute allows rescission of a policy for

misrepresentations, omissions, concealment of facts, or incorrect statements that are (1) fraudulent; (2) material either to the acceptance of the risk or to the hazard assumed by the insurer; or (3) such that they would affect the insurer's good faith decisions to issue the policy, issue the policy in the amount or at the premium rates that it did, or would not have issued coverage with respect to the hazard resulting in loss if facts had been known to the insurer as required by the application for the policy or contract or otherwise. *Id.*

Georgia courts have held that a material misrepresentation under the statute is "one that would influence a *prudent insurer* in determining whether or not to accept the risk, or in fixing a different amount of premium in the event of such acceptance." *American General Life Insurance Co. v. Schoenthal Family, LLC*, 555 F.3d 1331 (11th Cir. 2009) (quoting *Lively v. S. Heritage Ins. Co.*, 256 Ga.App. 195, 196, 568 S.E.2d 98, 100 (Ct.App. 2002)) (emphasis in original).

Under Georgia's statute, a false representation or misrepresentation need not be made with intent to deceive. *See Home Indem. Co. Manchester, New Hampshire v. Toombs*, 910 F.Supp. 1569 (N.D. Ga. 1995) (noting that "the subjective belief of the insured is not the issue"). A material misrepresentation will void the policy whether made in good faith or not. *Kennesaw Life & Accident Ins. Co. v. Hubbard*, 127 S.E.2d 845 (Ga. App. 1962).

Insurers may waive their right to rescind if they fail to return premiums paid by the insured. *See Weems v. American Nat. Ins. Co.*, 29 S.E.2d 500 (Ga. 1944); *Lively v. Southern Heritage Ins. Co.*, 568 S.E.2d 98 (Ga. App. 2002). In *Lively*, the court explained that multiple Georgia courts have recognized that "the failure to return premiums is a factor to be considered in determining whether an insurance company has waived the defense [of rescission] by treating the policy as an enforceable contract." *Lively*, 568 S.E.2d at 197-98.

Hawaii

Hawaii requires that the misrepresentation must either (1) materially affect the either the acceptance of the risk or the hazard assumed by the insurer or (2) be made with the intent to deceive. HAW. REV. STAT. § 431:10-209.

Materiality of a misrepresentation is generally a question of fact for the jury; however, misrepresentations on an application for insurance may become a question of law for the court to decide "[w]here the answer to such a question establishes an effective rule of law that could be applied in other cases." *See Genovia v. Jackson Nat. Life Ins. Co.*, 795 F.Supp. 1036, 1041 (D. Hawaii 1992), *overruled on other grounds* (finding that misrepresentation of smoking status is material as a matter of law on life insurance application).

An insurer does not have a duty to investigate an applicant's answer on an application for insurance, "unless the application on its face cries out for further investigation." *Gasaway v. Northwestern Mut. Life Ins. Co.*, 820 F.Supp. 1241 (D. Hawaii 1993) (explaining that the fact that the insurer had access to information contradictory to answer provided in the application did not give the insured "a license to lie").

Idaho

Idaho's statute allows rescission where misrepresentations, omissions, concealment of facts, and incorrect states are (1) fraudulent; (2) material either to the acceptance of the risk, or to the hazard assumed by the insurer; or (3) would have affected the insurer's good faith decision to issue the policy, issue the policy in the amount or with the premium rate that it did, or to provide coverage with respect to the hazard resulting in the loss. IDAHO CODE § 41-1811; *see also Wardle v. International Health & Life Ins. Co.*, 551 P.2d 623 (Idaho 1976).

In Idaho, an insured's misstatements on an application for insurance will not be sufficient grounds for rescinding a policy where the insured's answers were "made in absolute good faith and to the best of his knowledge and belief." *Dean v. Nationwide Life Ins. Co.*, 536 P.2d 1122, 1125 (Idaho 1975).

Illinois

Illinois regulates rescission by statute, which states that rescission of an insurance policy is generally appropriate when a misrepresentation or omission has been made with the "actual intent to deceive" or such that it "materially affects either the acceptance of the risk or the hazard assumed by the company." 215 ILL. COMP. STAT. ANN. 5/154. With the exception of life, accident and health, fidelity and surety, and ocean marine policies, a policy or policy renewal shall not be rescinded after the

policy has been in effect for one year or one policy terms, whichever is less. *Id.*

The statute does not render a policy void *ab initio*; rather, the statute renders the policy voidable, and the insurer can waive its right to rescind the policy. *Ill. St. Bar Ass'n Mut. Ins. Co. v. Coregis Ins. Co.*, 821 N.E.2d 706 (Ill. App. 2004).

Whether a statement is material is determined by whether a reasonably careful and intelligent person would have regarded the facts stated as substantially increasing the chances of the events insured against, so as to cause a rejection of the application or different conditions. *Ratliff v. Safeway Ins. Co.*, 628 N.E.2d 937 (Ill. App. 1993). "[A] false statement in an application for insurance is not in itself a ground for voiding the insurance policy." *Id.* (citing *Roberts v. National Liberty Group of Cos.*, 512 N.E.2d 792 (Ill. App. 1987)).

An applicant has a duty to act in good faith by making a "full and complete disclosure of all relevant information" when answering the application's questions. *Royal Maccabees Life Ins. Co. v. Malachinski*, 161 F.Supp.2d 847 (N.D. Ill. 2001). An insurer does not have a duty to investigate the accuracy of the applicant's answer to the application and is generally "entitled to rely upon the truthfulness of an applicant's answers." *Id.*

Indiana

A material misrepresentation or omission of fact in an insurance application renders the policy voidable if the misrepresentation was relied upon by the insurer in issuing the policy. *Foster v. Auto-Owners Ins. Co.*, 703 N.E.2d 657 (Ind. 1998) (citing *Colonial Penn Ins. Co. v. Guzorek*, 690 N.E.2d 664, 672 (Ind. 1997). A "material misrepresentation prevents a 'meeting of the minds' as to the risk to be insured.'" *Foster*, 703 N.E.2d at 659. A misrepresentation or omission is material if knowledge of the truth would have caused the insurer to refuse the risk or accept it at only a higher premium. *Id; see also Metro. Life Ins. Co. v. Becraft*, 12 N.E.2d 952, 954 (Ind. 1938). If the misrepresentation affects a specific risk insured, the misrepresentation may only make coverage voidable for the certain specific risk. *See Foster*, 703 N.E.2d at 659.

Intent to defraud is not required in Indiana. *See Becraft*, 12 N.E.2d at 954. Even innocent misrepresentations may make the policy voidable if

they are material. *Id.* Materiality is generally a jury question, but becomes a question of law where "there can be no reasonable difference of opinion" among reasonable men. *Id.* at 956.

Iowa

As with most other states, "fraudulent misrepresentations leading to the creation of a contract give rise to a right of rescission." *Robinson v. Perpetual Servs. Corp.*, 412 N.W.2d 562, 568 (Iowa 1987). In addition, the doctrine of equitable rescission to void a contract may be asserted when all five elements are proven: "(1) a representation, (2) falsity, (3) materiality, (4) an intent to induce the other to act or refrain from acting, and (5) justifiable reliance." *Hyler v. Garner*, 538 N.W.2d 864, 870 (Iowa 1996).

An insurer may also argue for rescission of an insurance contract as an affirmative defense to breach of contract claims. *Dishman v. American General Assurance Co.*, 193 F.Supp.2d 1119 (N.D. Iowa 2002). The insurer must prove the following six elements:

> (1) the applicant made a false representation or non-disclosure in connection with his application for insurance; (2) the representation or non-disclosure was material to the transaction, that is, the representation or non-disclosure materially affected the risk assumed by the insurer; (3) the applicant made the representation with actual knowledge of its falsity or reckless disregard of whether it was true or false or the applicant knowingly withheld material information; (4) the applicant intended to deceive the insurer; (5) the insurer relied on the applicant's representation or non-disclosure in issuing the insurance contract; and (6) the insurer would not have issued the insurance contract if it had known the true facts.

Id. at 1126.

Iowa courts have found that a misrepresentation or omission of fact is material "where a fact influences a person to enter into a transaction,

where it deceives that person or induces that person to act, or where the transaction would not have occurred without it." *Utica Mut. Ins. Co. v. Stockdale Agency*, 892 F.Supp. 1179, 1194 (N.D. Iowa 1995).

Intent to deceive is not required for rescission in Iowa. *See Rubes v. Mega Life & Health Ins. Co.*, 642 N.W.2d 263, 269 (Iowa 2002).

Kansas

In Kansas, an insurance policy may be rescinded for fraudulent misrepresentation where the applicant includes (1) an untrue statement of fact, (2) known to be untrue by the party making it, (3) made with the intent to deceive or recklessly made with disregard for the truth, (4) where another party justifiably relies on the statement and acts to his injury and detriment. *Waxse v. Reserve Life Ins. Co.*, 809 P.2d 533, 536 (Kan. 1991).

The misrepresentation also must be be material. *See American States Ins. Co. v. Ehrlich*, 701 P.2d 676 (Kan. 1985). "The test generally applied as to whether a misrepresentation is material, so as to permit an insurer to avoid its obligation under an insurance contract, is whether the knowledge of the truth would have reasonably influenced the insurer in accepting the risk or fixing the premium." *Id.* at syllabus point 2.

Fraudulent misrepresentation must be proven by clear and convincing evidence. *American Special Risk Management Corp. v. Cahow*, 2007 WL 1964952, *6 (Kan. App. 2007). The test contains both an objective and subjective part: (1) to subjectively examine the facts known to the insured when it completed the insurance application; and (2) to objectively test whether the known facts could reasonably be expected to give rise to a claim. *Id.*

Kentucky

Kentucky's misrepresentation statute takes the form commonly seen in states across the country. KY. REV. STAT. § 304.14-110. As such, rescission for misrepresentations, omissions, and incorrect statements is generally appropriate if they are (1) fraudulent; (2) material either to the acceptance of the risk, or to the hazard assumed by the insurer; or (3) would have affected the insurer's good faith decision to issues the policy, issue the policy in the amount or with the premium rate that it did, to provide coverage with respect to the hazard resulting in the loss. *Id.*

However, Kentucky expressly makes the statute inapplicable to applications for workers' compensation insurance coverage. *Id.*

If the statement is claimed to be fraudulent, the insurer must prove six elements according to the common law definition of fraud. The insurer must show by clear and convincing evidence that the applicant's statement or omissions was: (1) a material misrepresentation, (2) which was false, (3) known to be false or made recklessly, (4) made with the intent that it be acted upon, (5) acted in reliance thereon, and (6) caused injury. *Progressive Specialty Ins. Co. v. Rosing*, 891 F.Supp. 378 (W.D. Ky. 1995).

Intent to deceive is often sufficient to void a policy, but is not required. A material misrepresentation is also generally sufficient. "The rule is that a false answer is material if the insurer, acting reasonably and naturally in accordance with the usual practice of . . . insurance companies under similar circumstances, would not have accepted the application if the substantial truth had been stated therein." *Sergent v. Auto Owners Life Ins. Co.*, 2010 WL 4137448 (Ky. App. 2010) (internal citations and quotation marks omitted). If the misrepresentation is material, the applicant's intent has no consequence. *Id.*

Louisiana

Louisiana has codified its requirements to rescind due to misrepresentation. LA. REV. STAT. § 22:860. In any application for life, annuity, or health and accident insurance made in writing by the insured, a false statement that is not made with the intent to deceive will not bar the insured's right to recovery unless the statement or omission "materially affected either the acceptance of the risk or the hazard assumed by the insurer under the policy." *Id.* § 22:860B. In all other insurance policies, intent to deceive is required to defeat or void the contract of insurance. *Id.* § 22:860A.

The misrepresentation must be related to the cause of loss. Louisiana courts have explained that "[a] misrepresentation is material if the insurer would not have issued the policy had the misrepresentation not been made. If the information given by the applicant was false and the insurance company would have issued the policy anyway, the misrepresentation is not material." *Breaux v. Bene*, 664 So.2d 1377 (La. App. 1995).

In determining whether a misrepresentation or omission of fact was made with the intent to deceive, "the courts look to the surrounding circumstances indicating the insured's knowledge of the falsity of the representation made in the application and his recognition of the materiality of his misrepresentations, or to circumstances which create a reasonable assumption that the insured recognized the materiality." *Id.* at 1380.

Maine

Maine regulates misrepresentation in insurance applications by statute. ME. REV. STAT. Title 24-A, § 2411. Under the statute, misrepresentations or omissions of fact may allow rescission if they were (1) fraudulent; (2) material either to the acceptance of the risk, or to the hazard of the insurer; or (3) influenced a reasonable insurer in deciding whether to accept or reject the risk of entering into the contract, in fixing the premium rate, in fixing the amount of insurance coverage, or in providing coverage with respect to the hazard resulting in the loss. *York Mut. Ins. Co. v. Bowman*, 746 A.2d 906 (Me. 2000).

Materiality is determined by an objective standard which analyzes whether "it could reasonably be considered as affecting the insurer's decision to enter into the contract, or its evaluation of the degree or character of the risk, or its calculation of the premium to be charged." *Id.* at 909.

While a misrepresentation made with intent to deceive is generally sufficient for an insurer to rescind a policy, it is not required. *See id.* at 908 n.1 (explaining that the amendments to the statute were made to clarify that the statute should be read in the disjunctive).

Maryland

Maryland's statute is limited to applications for life or health insurance or annuities. MD CODE § 12-207. The statute allows rescission for misrepresentation or omissions of fact when they are "fraudulent or material to the acceptance of the risk or to the hazard that the insurer assumes" or if, absent the misrepresentation or omission, the insurer in good faith would not have issued the policy, issued the policy in as large an amount or at the same premium rate, or issued the policy to cover the hazard resulting in loss. *Id.*

Maryland courts have held that misrepresentations are material when they may "reasonably have affected the determination of the acceptability of the risk." *Jackson v. Hartford Life and Annuity Ins. Co.*, 201 F.Supp.2d 506, 512-13 (D. Md. 2002). The materiality of a misrepresentation is typically a question of fact for the jury, and the burden of proof lies with the party attempting to assert the defense." *Id.* at 513.

The intent to deceive is not required for rescission under Maryland law. *Nationwide Mut. Ins. Co. v. McBriety*, 230 A.2d 81 (Md. 1967) (finding that material misrepresentation is sufficient to void policy "regardless of whether the misrepresentation was made intentionally or through mistake and in good faith").

Maryland does not impose a duty on an insurance agent to investigate or verify answers to questions on insurance applications. *North American Specialty Ins. Co. v. Savage*, 977 F.Supp. 725, 730 (D. Md. 1997).

Massachusetts

In order to void a policy or deny coverage for a claim in Massachusetts based on a misrepresentation or omission of fact, "the insurer must demonstrate that the misrepresentations were made with the intent to deceive or that they increased the risk of loss to the insurer." *See Northwestern Mut. Life Ins. Co. v. Iannacchino*, 950 F.Supp. 28 (D. Mass 1997). A misrepresentation is material only if "such misrepresentation or warranty is made with actual intent to deceive" or "the matter misrepresented or made a warranty increased the risk of loss." MASS. GEN. LAWS ch. 175 § 186(a). The statute continues by specifically addressing misrepresentations regarding the physical condition or health risks to the physical condition of the insured. *Id.* § 186(b). As to the specific physical conditions of the insured, "a misrepresentation or warranty shall be deemed material if knowledge or ignorance of it would otherwise have influenced the insurer in making the contract at all, or in estimating the degree and character of the risk, or in fixing the rate of the premium. *Id.*

Massachusetts courts have explained that a fact is regarded as "material" if "the knowledge or ignorance of [it] would naturally influence the judgment of the underwriter in make the contract at all, or in estimating the degree and character of the risk, or in fixing the rate of the premium." *RLI Ins. Co. v. Santos*, 746 F.Supp.2d 255, 264 (D. Mass. 2010).

Generally, policies rescinded due to material misrepresentations are void *ab initio*. *See Northwestern Mut. Life Ins. Co. v. Iannacchino*, 950 F.Supp. 28 (D. Mass 1997).

An intent to deceive is not required for rescission, and an insurer may void the policy even if the policyholder made an innocent misrepresentation of a material fact in a policy application. *RLI Ins. Co. v. Santos*, 746 F.Supp.2d 255, 264 (D. Mass. 2010).

Michigan

In Michigan, a false statement in an insurance application that materially affects either the acceptance of the risk or the hazard assumed by the insurer voids coverage *ab initio*. *See* M.C.L. § 500.2218 (regulating disability insurance); *Housour v. Prudential Life Ins. Co. of Am.*, 136 N.W.2d 689 (Mich. App. 1965); *Lake States Ins. Co. v. Wilson*, 586 N.W.2d 113, 115 (Mich. App. 1998). The misrepresentation need not be causally linked to the specific cause of loss, "[f]or the reason that the test of materiality of misrepresentations is determined by whether or not knowledge of the true fact would, at the time the policy was issued, have increased the risk or influenced the insurer in determining whether to accept or reject the risk. *See Wickersham v. John Hancock Mut. Life Ins. Co.*, 318 N.W.2d 456 (Mich. 1982). Where the misrepresentation increases the risk assumed, no reliance need be proven. *Smith v. Globe Life*, 597 N.W.2d 28 (Mich. 1999).

The misrepresentation defense must be raised within three years of the date of the policy's issuance. M.C.L.A. § 500.3408.

Intent to deceive is not required for rescission if the insured made a misrepresentation or omission of fact that was material. *See Fakhouri v. Banner Life Ins. Co.*, 157 F.Supp.2d 751 (E.D. Mich. 2001) (finding that rescission was appropriate because insured concealed information that "materially affected the acceptance of the risk" by insurer). Materiality must be proven by clear and convincing evidence. *Zulcosky v. Farm Bureau Life Ins. Co. v. Michigan*, 1997 WL 33354561 (Mich. App. 1997) (citing *Howard v. Goden State Mut. Life Ins. Co.*, 231 N.W.2d 655 (Mich. App. 1975).

A material misrepresentation by one insured permits rescission as to all insureds. *American Guarantee & Liab. Ins. Co. v. Jacques Admiralty*

Law Firm, 121 Fed. App'x. 573, 576 (6th Cir. 2005) (applying Michigan law).

Minnesota

Pursuant to Minnesota statute, no oral or written misrepresentation in the negotiation of insurance is material, or would defeat the policy, unless (1) made with the intent to deceive or defraud, or (2) the matter misrepresented increases the risk of loss. MINN. STAT. § 60A.08 subd. 9 (expressly exempting life insurance and accident and health insurance from the statute's applicability).

Minnesota also has a statutory provision that specifically addresses D&O liability policies. MINN STAT. § 60A.08 subd. 11. D&O policy applications must be signed by a director or officer, and that director must have actual knowledge of the facts misrepresented or omitted, in order for subdivision 9 to apply. *Id.* The application also must be attached to and incorporated into the contract. *Id.*

Further, an insurer and insured are prohibited from agreeing to rescind a policy if the insurer has knowledge of any claims against the insured that would remain unsatisfied due to the financial condition of the insured. MINN STAT. § 60A.08 subd. 14.

A misrepresentation increases the risk of loss under the statute when it impairs the insurer's ability to make a reasonable decision initially to assume the risk of coverage or when there is a greater likelihood that the insurer will be liable in the future than there would have been if the facts were as the insured stated them to be. *In re Silicone Implant Ins. Coverage Lit.*, 652 N.W.2d 46, 78 (Minn. App. 2002), *aff'd in part, rev'd in part by* 667 N.W.2d 405 (Minn. 2003). Whether the misrepresentation increased the risk of loss is a question for the trier of fact unless the evidence is conclusive one way or the other. *Transam. Ins. Co. v. Austin Farm Ctr., Inc.*, 354 N.W.2d 503, 506 (Minn. App. 1984).

Intent to deceive is not required for rescission of an insurance policy in Minnesota. *See Waseca Mut. Ins. Co. v. Noska*, 331 N.W.2d 917, 924 n.1 (Minn. 1983) (noting that "[p]revious cases have established that if the material misrepresentation increases the risk of loss, the policy is avoided regardless of the intent with which it was made").

Mississippi

In Mississippi, an insurance policy may be rescinded if the insured made a misrepresentation or omission of fact which was (1) material to the risk and (2) substantially untrue. *Sanford v. Federated Guar. Ins. Co.*, 522 So.2d 214 (Miss. 1988) (noting that, on the other hand, "a representation, if substantially true and not material to the risk, will not invalidate the policy in the absence of fraud"). "The materiality of a representation is determined by the probably and reasonable effect which truthful answers would have had on the insurer." *Id.*

Notably, Mississippi courts have distinguished between an insured's "representations" and "warranties" in relation to insurance applications. *Colonial Life & Acc. Inc. Co. v. Cook*, 374 So.2d 1288, 1291 (Miss. 1979). A warranty must be "literally true" while a representation must be "substantially true" to avoid rescission. *Id.*

An insurer is not required to prove that an insured had an intent to deceive in order to void a policy. *Golden Rule Ins. Co. v. Hopkins*, 788 F.Supp. 295, 301 (S.D. Miss. 1991). This is known as the "innocent misrepresentation" standard. *Id.*

Missouri

Under Missouri law, an insurance company may avoid a policy by showing that a representation is both false and material when (1) the representation is warranted to be true, (2) the policy is conditioned upon its truth, (3) the policy provides that its falsity will avoid the policy, or (4) the application is incorporated into and attached to the policy. *See* MO. REV. STAT. §375.0021(2) (addressing cancellation of policies); *Shirkey v. Guarantee Trust Life & Ins. Co.*, 141 S.W.3d 62 (Mo. App. 2004) (citing *Cont'l Cas. Co. v. Maxwell*, 799 S.W.2d 882, 888 (Mo. App. 1990)). If the insurance company fails to show that its situation applies to at least one of the four scenarios, "then it may avoid the policy only by showing that the representation in the application was false and fraudulently made." *Shirkey*, 141 S.W.3d at 67.

Generally, a misrepresentation is material when "it is reasonably calculated to affect the action and conduct of the company in deciding whether or not to accept the risk by issuing its policy covering the risk." *Maxwell*, 799 S.W.2d at 889. Materiality is a question of fact for the jury unless "all minds would agree it is or is not material." *Id.*

Montana

In keeping with the majority of states, Montana considers statements and descriptions within an insurance policy to be representations and not warranties. MC A33-15-403(1).

Further, Montana allows an insurer three paths to rescission under a policy. Fist, an insurer must demonstrate that a misrepresentation within the application was fraudulently made. MC A33-15-403(2)(a). If, however, an insurer is unable to make such a showing of scienter, then it may void policy by showing that the false statement is material to the risk. *Id.* at (2)(b). Under this method of rescission, even innocent misrepresentations make a policy voidable. Further, whether a misrepresentation is material or not is a question of fact left for the fact finder to determine. *Schneider v. Mn. Mut. Life Ins. Co.*, 806 P.2d 1032, 1036 (MT 1991). Finally, the insurer may avoid coverage under the policy if it can in good faith establish that it would not have issued the policy for the premium rate or coverage amount provided. MC A33-15-403(2)(c).

Moreover, Section 2(c) of the statute incorporates a standard of materiality whereby the materiality of an omission or misrepresentation depends upon whether, had the truth been known, a reasonable and prudent insurer would not have issued the premium, or would have issued the policy for a higher premium. *Schneider*, 806 P.2d at 1035. This is a subjective, good faith standard. *Id*. Accordingly, materiality is determined at the time the insurer issues a policy. *Id*.

Nebraska

Nebraska's law as it relates to misrepresentation is found almost exclusively within the common law. However, the courts in Nebraska have adopted a framework for rescission due to misrepresentation that closely mirrors the requirements found in Montana. In Nebraska, an insurer seeking to raise the defense of misrepresentation within Nebraska must plead and prove three elements: 1) the misrepresentation was made knowingly and with intent to deceive; 2) the insurer relied and acted upon such statement; and 3) the insurer was deceived to its injury. *Lowry v. State Farm Mut. Auto Ins. Co.*, 421 N.W. 2d 775, 228 Neb. 171, 175 (1988). A finder of fact may, based solely upon a false statement made by the insured, conclude that the statement was made knowingly and with the intent to deceive. *Id*. at 176 (citing *White v. Medico Life Ins. Co.*, 212 Neb. 901, 327 N.W. 2d 606, 610 (1982)).

Misrepresentations, either oral or written, are not material and do not avoid the policy unless the misrepresentation deceived the company to its injury. Neb. Rev. Stat. § 44-358. However, false representations are material if an insurer would not have issued the policy if it had been aware of the facts as true. *Lowry*, 228 Neb. at 175. Thus, an insurer seeking rescission will be required to make a showing of reliance on the false representation before a court will grant rescission.

If an insurer demonstrates such reliance upon the statements made by the applicant, then it is generally not under a duty to perform its own investigation into the representations contained within the application. *Id*. at 175-176. There is, however, a limitation on this ability to rely on the insured's representations. There cannot be anything that would put the insurer on notice of the falsity of any of the answers. *Id*. at 176.

Nevada

Unless there is some evidence of waiver or circumstances that support a claim of estoppel, an insurer is not bound to the insurance contract if it was induced to enter such contract through the fraudulent misrepresentations of the insured. *Schneider v. Continental Assur. Co.*, 110 Nev. 1270, 1274, 885 P.2d 572, 574 (1994).

Nevada's misrepresentation statute follows the trend of the majority of states, in that it applies to an insured's misrepresentations, omissions, concealment of facts, and incorrect statements. The statute allows for rescission under any of the following three circumstances: 1) an intent to defraud, 2) a material misrepresentation, or 3) a misrepresentation where the insurer, in good faith, would not have issued the policy. NEV. REV. STAT. ANN. § 687B.110.

However, the courts in Nevada have clearly stated that a lack of intent to defraud does not prohibit an insurer from seeking rescission. *Siefers v. PacifiCare Life Assur. Co.,* 461 F. App'x 652, 654 (9th Cir. 2011). Consequently, innocent misrepresentations are capable of voiding a policy, if the insurer can objectively illustrate that the false statement was material or demonstrate that, under a subjective good faith standard, the insurer would not have issued the policy. Traditionally, whether a misrepresentation is material is treated as a question of fact left to the purview of the jury to determine. *Powers v. United Servs. Auto. Ass'n*, 115 Nev. 38, 979 P.2d 1286, 1289 (1999). Thus, obtaining summary judgment on the basis of materiality is highly unlikely.

New Hampshire

New Hampshire tends to follow the majority of jurisdictions. Generally, under accident or health insurance policies, a false statement in the application does not bar recovery. However, if the false statement was made with actual intent to deceive or materially affected the acceptance of the risk or assumption of the hazard by the insurer then an insurer may avail itself of the misrepresentation defense. N.H. REV. STAT. § 415:9.

Establishing that an applicant intended to deceive an insurer may prove to be a difficult standard to meet. Fortunately, New Hampshire permits rescission based upon innocent misrepresentations if the statement was material to the acceptance of risk. Materiality is determined by asking whether the statement could "reasonably be considered material in affecting the insurer's decision to enter into the contract, in estimating the degree or character of the risk, or in fixing the premium rate thereon." *Mut. Ben. Life Ins., Co. v. Gruette*, 129 N.H. 317, 320, 529 A.2d 870, 872 (1987). Further, determining materiality is a question of fact that is left in the hands of the jury, unless the record is such that the trial court must determine, as a matter of law, that the statement was material to the acceptance of the risk. *Taylor v. Metro. Life Ins. Co.*, 106 N.H. 455, 458, 214 A.2d 109, 112 (1965).

Whereas other jurisdictions impute the knowledge of soliciting agents to the insurer, New Hampshire is not chargeable with the knowledge of an agent who fraudulently wrote wrong answers on an application. *Boucouvalas v. John Hancock Mut. Life Ins. Co.*, 5 A.2d 721 (N.H. 1939).

New Jersey

Under a life insurance policy, if the insured provides a false statement in his/her application, then that statement will not bar recovery unless it materially affects the acceptance of the risk or hazard assumed by the insurer. N.J.S.A. 17B:24-3. Thus, an insurer does not need to show an actual intent to deceive by the insured. *Ledley v. William Penn Life Ins. Co.*, 138 N.J. 627, 637, 651 A.2d 92, 96 (1995). Innocent misrepresentations are sufficient capable of rescinding a policy under the theory of equitable fraud. *Id*. (citing *Metropolitan Life Ins. Co. v. Tarnowski*, 20 A.2d 421 (1941)).

However, equitable fraud is only available when the false statements materially affect the acceptance of the risk or hazard assumed. *Id*. at 97. Further, equitable fraud requires a determination of whether a question within the application is subjective or objective. Answers to subjective questions that "seek to probe the applicant's state of mind" cannot constitute equitable fraud. *Id*. at 636. As a result, an insurer cannot void the policy, if the "question is directed toward probing the knowledge of the applicant and determining the state of his mind and… the answer is a correct statement of the applicants knowledge and belief." *Id*. at 636 (citing *Ettelson v. Metropolitan Life Ins. Co.*, 164 F.2d 660, 665 (3rd Cir. 1947)).

It should be noted, however, that once two years have elapsed since the time of the policy's issuance, only fraudulent misstatements may be used to void a policy or serve as a defense. N.J.S.A. 17B:26-5.

New Mexico

New Mexico requires that false statements on the application materially affect the insurer's acceptance of the risk or the hazard assumed. N. M. S. A. 1978, § 59A-18-11.Otherwise, such statements do not bar an insured's recovery under the policy. There is a duty placed upon both the insured and insurer of fair dealing. There is no scienter requirement, nor is there a requirement that the misrepresentation be negligent. An insurer only needs to demonstrate that a misrepresentation is material. *Rael v. Am. Estate Life Ins. Co.*, 444 P.2d 290, 292 (N.M. 1968).

New Mexico courts determine materiality based upon whether the insurer would have rejected the application and risk if it had known the true facts. *John Hancock Mut. Life Ins. Co. v. Weisman,* 27 F.3d 500, 506 (10th Cir. 1994). Further, the burden of showing materiality rests upon the insurer. *Id*. (citing *Tsosie v. Found. Res. Ins. Co.*, 427 P.2d 29 (N.M. 1967)).

Moreover, an insurer seeking to void the policy bears the burden of proving that the fraudulent misrepresentations are sufficient to avoid liability. *Tsosie v. Foundation Reserve Ins. Co.*, 427 P.2d 29, 31 (N.M. 1967). An insurer can prove misrepresentation in several ways. First, a misrepresentation is "indicated when the insurer relies upon statements that were certainly known by the insured to be untrue, or when these statements "are of such a character as clearly to prove a conscious

misrepresentation." *Crow v. Capitol Bankers Life Ins. Co*., 119 N.M. 452, 459, 891 P.2d 1206, 1213 (N.M. 1995). Further, a misrepresentation is demonstrated "by the brevity of time between the applicant's representation about her health and the occurrence of the disease." *Id*. Finally, there is evidence of misrepresentation "if the insured does not disclose that she knows she suffers from a serious disease which is statistically likely to shorten her life." *Id*.

New York

The defense of misrepresentation is largely codified within New York law. New York considers a misrepresentation to be a statement of fact, either past or present, made by a prospective insured to an insurer before the entering into of an insurance contract. Only material misrepresentations can void an insurance contract or defeat recovery. Materiality requires that the insurer would have refused to enter into the contract if it had known facts were misrepresented. N.Y. INS. LAW § 3105.

Further, a misrepresentation is considered material if the insurer would not have issued the policy if it had known the facts as they actually existed. *Morales v. Castlepoint Ins. Co.*, 125 A.D.3d 947, 948 (N.Y. 2015). An insurer can satisfy this burden by producing documentation relating to its underwriting practices, including its underwriting manuals, bulletins, or rules relating to similar risks. These documents must demonstrate that the insurer would not have issued the policy had the correct facts been known and disclosed in the application.

Accordingly, the test for materiality is largely subjective, and relies greatly on the insurer's own manuals and policies. Thus, insurers in New York would be wise to clearly delineate the facts and questions contained within their applications that would be material to underwriting the proposed risk.

North Carolina

North Carolina provides for two avenues of rescission within its statutory scheme, and these avenues have been reinforced by the North Carolina courts. For an insurer to avoid coverage under the policy in North Carolina, it must show the misrepresentation is either 1) material or 2)fraudulent. N.C. GEN. STAT. § 58-3-10. Courts have ruled that the legislature in North Carolina clearly showed that it only wanted

misrepresentations that are "material to the risk" to be sufficient for policy avoidance. *Montgomery Mut. Ins. Co. v.*, 515 (N.C. 2003). Further, an insurer asserting a misrepresentation defense must show a significant relationship between the false statement and the risk being underwritten.

The courts in North Carolina have adopted the two paths to rescission codified in the Section 58-3-10. Specifically, the courts hold that before an insurer can void a policy, it must demonstrate two facts: 1) that the statement or omission in the application was untrue, and 2) that the insurer's reliance on the false statement or omission was material to the company's decision to undertake the risk. *Riddle*, 587 S.E.2d 513. Showing falsity alone is insufficient to avoid the policy coverage. *Id*.

North Carolina considers a misrepresentation as material if "the knowledge or ignorance of it would naturally influence the judgment of the insurer in making the contract, or in estimating the degree and character of the risk, or in fixing the premium." *Evanston Ins. Co. v. G&T Fabricators, Inc.*, 740 F.Supp.2d 731, 736 (N.C. 2010). A misrepresentation does not have to be intentional if it is material and false. *Id*. (citing *In re McCary*, 435 S.E.2d 359, 364 (N.C. 1993)). Thus, insures may, as with the majority of states, avail themselves of the misrepresentation defense based upon innocent misrepresentations.

Further, an insurer may rely on the statements contained within the application. An insurer is not under a duty, either legal or equitable, to question the truth of the statements contained within the application without some facts that would put it on notice that it needed to conduct an inquiry. *Id*. at 737.

North Dakota

Under the North Dakota statutory framework, insurers are able to void a policy when the insured makes a misrepresentation, oral or written, that was made with intent to deceive or increased the risk of loss. N.D.CENT. CODE § 26.1-29-25. However, the false statement must still be material before rescission will be granted.

Materiality is determined "solely by the probable and reasonable influence of the facts upon the party to whom the communication is due in forming the party's estimate of the disadvantages of the proposed contract or in making the party's inquiries." N.D.CENT. CODE § 26.1-29-17.

Ohio

Courts routinely find that nothing more completely vitiates a contract of insurance than false answers to material questions in an insurance application. An insurer can avoid coverage if an insured knowingly gives false answers to material questions on the application. Further, if the insured, upon issuance of the policy, notes false answers and conceals such falsity from the insurer, then the insurer can similarly void the policy. *Redden v. Constitutional Life Ins. Co.*, 137 S.E.2d 365 (Ohio 1961).

Under Ohio's statutory framework, a false statement in the application for sickness or accident insurance does not bar recovery unless the insurer clearly proves five elements: 1) the statement was willfully false, 3) the statement was fraudulently made, 3) that it materially affects the acceptance of the risk or the hazard assumed by the insurer, 4) that it induced the insurer to issue the policy, and 5) but for the false statement the policy would not have been issued. R.C. § 3923.14.

Oklahoma

Following the majority of jurisdictions, Oklahoma allows insurers to rescind coverage by showing a misrepresentation is fraudulent, material to the acceptance of the risk or the assumption of the hazard, or the insurer would not have issued the policy or would not have provided coverage with respect to the hazard. 36 Okl.St.Ann. § 3609. Therefore, intent to deceive is not mandatory for rescission, and innocent misrepresentations may void coverage.

Oklahoma courts define a misrepresentation as

> something which is untrue, and which the insured states with knowledge that it is untrue and with an intent to deceive, or which he states positively as true without knowing it to be true, and which has a tendency to mislead, where such fact in either case is material to the risk.

Mass. Mut. Life Ins. Co. v. Allen, 416 P.2d 935, 940 (Okla. 1965).

While intent to deceive is generally not required, if an insurer asserts that the applicant concealed some fact during the application process, then that implies some intentional withholding of facts by the

insured. *Id*. Moreover, an omission requires some intentional omission to disclose a fact or condition. Thus, courts faced with concealment or omission claims by the insurer routinely find that Section 3609 requires a finding of intent to deceive before an insurer can avoid the policy. *Hays v. Jackson Nat'l Life Ins. Co.*, 105 F.2d 583 (10th Cir. 1997).

Oregon

In Oregon, misrepresentations, omissions, or concealments will not bar recovery unless they are in a written application and that application is attached to the policy. Moreover, the insurer must show materiality and reliance on these representations, and that they are either fraudulent or material to the acceptance of the risk or the hazard assumed by the insurer. OR. REV. STAT. §742.013

For an insurer to rescind a policy, it must show by a preponderance of the evidence that it relied upon the false representations of the insured when it issued the policy. For an insurer to prove reliance, the insurer must prove three requirements: 1) reliance in fact, 2) reliance that was justified in light of the facts known to the insurer at the time, 3) the insurer's right to rely on the representations. *Id*. Factors 1 and 2 are factual, with factor 3 being a solely legal conclusion. Once an insurer establishes a prima facie case of reasonable reliance, the burden then shifts to the insured to present evidence to demonstrate that the insurer either knew or should have known that the representations were false.

Further, it must be proven that the insured either knowingly made the false representation or recklessly made such representations without knowing whether they were true or false. *Story v. Safeco Life Ins. Co.*, 40 P3d 1112, 1116 (OR. 2002).

Pennsylvania

Pennsylvania adopted a statutory provision that permits rescission for either fraud or materiality. Specifically, in a policy for health or accident insurance, a false statement in the application of a policy will not bar recovery unless the statement was made with "actual intent to deceive" or it "materially affected either the acceptance of the risk or the hazard assumed by the insurer." 40 P.S. § 757.

Under Pennsylvania law "an answer known by insured to be false when made is presumptively fraudulent." *Evans v. Penn Mut. Life Ins. Co.*,

186 A. 133 (1936). When an insurer claims fraud, it must show an actual intent to deceive. However, there are other grounds available to avoid coverage under the policy. Specifically, if the false statements materially affected the risk accepted or the hazard assumed by the insurer. *Connecticut Mut. Life Ins. Co. v. Wyman*, 718 F.2d 63 (1983).

This disjunctive provision allows an insurer to avoid coverage even if the insured did not intend to deceive, thereby allowing an insurer to rescind a policy utilizing innocent misrepresentations. The Pennsylvania courts have expressly allowed rescission under such circumstances, and held that an insurer is entitled to rescission if the "statements are false to the knowledge of the applicant but are not made with an intent to deceive[.]" *Connecticut Mut. Life Ins. Co. v. Wyman*, 718 F.2d 63, 67 (3rd Cir. 1987).

Rhode Island

Rhode Island bases its misrepresentation statute around a showing of materiality by the insurer. Thus, a false statement in an application for a policy bars recovery under the policy if the false statement materially affected either the acceptance of the risk or the hazard assumed by the insurer. R.I. Gen. Laws Ann. § 27-18.

Consequently, Rhode Island does not require intent to deceive before a policy may be avoided. Even innocent misrepresentations are sufficient for an insurer to rescind the policy and avoid coverage. *Evora v. Henry*, 559 A.2d 1038, 1040 (R.I. 1989). However, an insurer must be certain that the insured did not communicate the falsity of the statements to the insured's agent. The agent's knowledge is imputed to the insurer, and this knowledge is adequate to equitably bar the insurer from asserting the defense of misrepresentation. *Id*.

South Carolina

The majority of the law relating to misrepresentation in the insurance policy context is contained within the common law. "False representations alone will not void a policy." *Metropolitan Life Ins. Co. v. Bates*, 49 S.E.2d 201 (S.C. 1948). Accordingly, the insured's good faith in making false representations is an important consideration in determining the effect of such representations. *Id*.

Under South Carolina line, for an insurer to avoid coverage under a policy, it must show 1) that the statements were untrue, 2) that the falsity of these statements was known to the applicant, 3) that the false statements were material to the risk, and 5) that they were made with the intent to deceive and defraud the insurer. *Strickland v. Prudential Ins. Co. of America*, 292 S.E.2d 301 (S.C. 1982).

In attempting to satisfy these five elements, the insurer is charged with proving these elements under a "clear and convincing" standard of proof. *Id*. Further, the "intent to deceive" contained within the *Strickland* test presents a question for the jury, thereby making summary judgment on this issue unlikely. *Primerica Life Ins. Co. v. Ingram*, 616 S.E.2d 737, 739 (S.C.Ct.App. 2005).

Furthermore, there is generally no requirement that the loss under the policy be causally related to the material misrepresentation under a void insurance policy. *Carroll v. Jackson Nat. Life Ins. Co.*, 414 S.E.2d 777 (S.C. 1992).

South Dakota

Misrepresentations, omissions, concealment of facts, or incorrect statements do not bar recovery unless they are fraudulent or an intentional misrepresentation of a material fact, material to the acceptance of the risk or the hazard assumed, or the insurer, in good faith, would not have issued the policy in as large an amount, or would not have issued coverage for the hazard resulting in the loss. S.D. Codified Laws § 58-11-44.

A material misrepresentation, even one lacking an intent to deceive, is capable of rendering a policy as voidable. An insurer is entitled to rely on the truthfulness of the answers given in the application. *De Smet Farm Mut. Ins. Co. v. Busskohl*, 834 N.W.2d 826 (S.D. 2013). Materiality is a question of law for the court to determine. *Id*. at 834. However, the courts in South Dakota tend to utilize an objective standard when considering the materiality of a misrepresentation. South Dakota courts deem a misrepresentation material to the risk if "it is such as would reasonably influence the decision of the insurer as to whether it would accept or reject the risk." *Id*. at 834-35. Further, misrepresentations are determined by their probable and reasonable influence on the insurer. *Id*. at 835.

Tennessee

The misrepresentation statute contained with Tennessee's Code provides for rescission under fraudulent or material circumstances. This statutes provides that a misrepresentation is not material and does not defeat or void the policy unless the misrepresentation is made with "actual intent to deceive" or the "matter represented increases the risk of loss." Tenn. Code Ann. § 56-7-103.

Whether a misrepresentation is material, however, is a question of fact. *Smith v. Tennessee Farmers Life Reassurance Co.*, 210 S.W.3d 584 (TN 2006). However, the determination of whether a misrepresentation increased the risk of loss to the insurer is a question of law left to the court. *Snead v. Nationwide Prop. & Cas. Ins. Co.*, 663 F.Supp.2d 823, 826 (W.D.Tn. 2009).

Further, a misrepresentation increases the risk of loss for the insurer if it "naturally and reasonably influences the judgment of the insurer in making the contract. *Lane v. Am. Gen. Life & Accident Ins. Co.*, 252 S.W.3d 289, 295-296 (Tenn.Ct.App. 2007). In reviewing this element, the courts may use the questions found on an insurer's application to decide what conditions or situations that insurer considers pertinent to the risk of loss. *Snead*, 653 F.Supp.2d at 827.

Thus, an insurer may deny a claim under two circumstances: 1) the insured made intentional misrepresentations on the application, or 2) the misrepresentation increased the risk of loss. *Snead v. Nationwide Property & Cas. Ins. Co.*, 653 F.Supp.2d 823 (TN 2009). Under either of these factors, however, the insurer must make a threshold showing of materiality as it relates to the misrepresented statement.

Texas

Under Texas law, a material misrepresentation allows an insurer to interpose a defense in a suit based upon the policy. *Pioneer Am. Ins. Co. v. Meeker*, 300 S.W.2d 212 (Civ.App. 1957). Accordingly, Texas treats misrepresentation as an affirmative defense that must be pled and proved by the insurer.

However, the Texas statutory framework provides that policy provisions within an insurance contract that make false statements grounds for voiding the policy or make the policy voidable have no effect

and are not a defense to a suit brought under the policy. However, this provision does not apply if the matter misrepresented was material to the risk or contributed to the event under which the policy came due. Whether a misrepresentation is material or contributed is a question of fact. Tex. Ins. Code Ann. § 705.004.

A misrepresentation that is "material to the risk" is one relating to a fact that would induce the insurer to decline the insurance or charge a higher premium. *St. Paul Fire & Marine Ins. Co. v. Huff*, 172 S.W. 755 (Civ. App. 1915).

Thus, Texas courts require an insurer to plead, and prove, five elements before an insurer may avoid coverage under a policy: "1) the representation by the insured, 2) the falsity of the representation, 3) reliance thereon by the insurer, 4) the intent to deceive by the insured, and 5) the materiality of the representation." *Diggs' Estate v. Enterprise Life Ins. Co.*, 646 S.W.2d 573, 574 (Tex.Civ.App. 1982).

Utah

Utah law states that a misrepresentation does not affect the insurer's duties under the policy unless the insurer relies on it and it is either material or made with intent to deceive or the fact misrepresented contributed to the loss. Utah Code Ann. § 31A-21-105.

This provision is stated in the disjunctive, thereby allowing an insurer to void the policy if it demonstrates any one of the three. *Debridge v. Mut. Prot. Ins. Co.*, 963 P.2d 788 (UT App. 1998). Under each prong, though, there must be a threshold inquiry met that the insured made a representation. *Id*. Representations are not required to be warranted as true to be considered a misrepresentation. *ClearOne Comm. Inc. v. Nat'l Union Fire Ins. Co.*, 494 F.3d 1238, 1245 (10th Cir. 2007). The Court in *ClearOne* stated that Section 31A-21-105 makes a distinction between a falsely represented statement and a statement that violates a warranty of accuracy. *Id*. However, either a breach of warranty or misrepresentation are sufficient to rescind a policy. *Id*.

Furthermore, Utah requires that the applicant "have at least some knowledge or awareness of her misstatement…" *Id*. Thus, the statute contemplates "some level of knowledge or awareness of a misstatement" before a representation is sufficient to qualify as a misrepresentation. *Id*.

at 797. Consequently, an innocent misstatement is not considered a misrepresentation sufficient to grant an insurer rescission under the policy.

Vermont

In Vermont, a false statement on the application does not bar recovery unless the statement was made with actual intent to deceive or "unless it materially affected either the acceptance of the risk or the hazard assumed by the insurer." 8 V.SA. § 4205.

An insurer is capable of meeting this standard by "establishing that there is a causal connection between the misrepresentation and the insurer's decision to issue the policy." *RLI Ins. Co. v. Klonsky*, 771 F.Supp.2d 314, 321 (D.Vt. 2011) (citing *McAllister v. Avemco Ins. Co.,* 148 Vt. 110, 528 A.2d 758, 759 (1987)). It does not matter whether the misrepresentation was innocently made. *Id*.

Thus, the focus of a court in reviewing an insurer's request to rescind pursuant to 8 V.SA. § 4205 is on the "nexus" between the alleged false statement and the insurer's decision to issue the policy. *McAllister v. Avemco Ins. Co.*, 528 A.2d 758, 759 (Vt. 1987).

Virginia

Pursuant to Va. Code Ann. § 38.2-309, statements in an insurance policy, or made after a loss under the policy, will not bar recovery unless it is clearly proven that the answer was material to the risk when the risk was assumed and was untrue. Thus, an insurer can rescind a policy for a misrepresentation of a material fact made while applying for insurance. *Cont. Cas. Co. v. Graham & Schewe*, 339 F.Supp2d 723 (E.D.Va. 2004).

Courts generally require an insurer seeking to rescind a policy prove, by clear proof, that the statement made on the application was untrue and that the insurance company's reliance on that false statement was material to the decision to underwrite the risk. *Minn. Lawyers Mut. Ins. Co. v. Hancock*, 600 F.Supp2d 702 (Va. 2009). Thus, an insurer seeking to rescind a policy pursuant to the misrepresentation statute must make a showing that the statement was false, that is was material, and that, but for the false representation, the insurer would not have issued the policy.

Traditionally, materiality of a misrepresentation is an issue that is left to the courts to decide. *Old Republic Life Ins. Co. v. Bales*, 195 S.E.2d 854, 856 (Va. 1973). Whether or not a statement is true, and whether such a statement was knowingly made, is generally a determination reserved for the finder of fact to adjudicate. *U.S. Fidelity & Guar. Co. v. Haywood*, 177 S.E.2d 530, 532 (Va. 1970).

Usually an insurer is not required to establish that an untrue representation was willfully false or fraudulent. *Insurance Co. of N. Am. v. U.S. Gypsum Co.*, 639 F.Supp1246 (W.D.Va. 1986). If, however, the insured qualifies his or her statements by certifying that the representations within the application are "correct to the best of [its] knowledge," then the insurer is required to clearly demonstrate that the insured knowingly made false statements. *Id*. at 706 (emphasis original).

Washington

A misrepresentation is not deemed material and does not void the contract unless the misrepresentation was made "with the intent to deceive." In life or disability insurance policies, the falsity of representations do not bar recovery unless the statement was made with the actual intent to deceive or materially affected the acceptance of the risk or the hazard assumed by the insurer. Wash. Rev. Code Ann. § 48.18.090.

There are two subsections. One relates to "oral and written misrepresentation[s]… made in the negotiation of an insurance contract." *Karpenski v. Am. Gen. Life Co., LLC*, 999 F.Supp2d 1235 (W.D.Wash. 2014). The second is applicable to statements made by an insured in writing while applying for life or disability insurance. *Id*. Where this section applies, Washington law requires an insurer seeking to rescind a policy establish four elements: "1) the policyholder represented as truthful certain information during the negotiation of the insurance contract; 2) those representations were untruthful, or misrepresentations; 3) the misrepresentations were material; and 4) the misrepresentations were made with the intent to deceive." *Id*. at 1243 (citing *Cutter & Buck, Inc. v. Genesis Ins. Co.*, 306 F.Supp2d 988, 997 (W.D.Wash. 2004)).

However, where only subsection 2 is implicated, there does not necessarily need to be an actual intent to deceive. *Id*. at 1243. Rather, subsection 2 requires that a false statement "be knowingly made on the part of the insured." *Id*. (citing *Northwestern Mut.. Life Ins. Co. v. Koch*,

2009 WL 3346677 at *7). Once an insurer establishes that a false statement was knowingly made, it must then show an actual intent to deceive or that the statement materially affected either the acceptance of the risk or the hazard assumed. *Id*. at 1244.

Washington recognizes the common law doctrine of "mend the hold," which prohibits an insurer from changing the basis for its avoidance of liability after litigation has commenced. *Vision One, LLC v. Phila. Indem. Ins. Co.*, 174 Wash.2d 501, 520 (2012).

West Virginia

The common law concept of warranties, as they relate to statements by an insured in an application, is abolished in West Virginia. *Powell v. Time Ins. Co.*, 382 S.E.2d 342, 347 (W.Va. 2989). An insurer within West Virginia may rescind a policy based upon misrepresentations, omissions, concealments of facts, or incorrect statements. However, these statements do not bar recovery unless they are 1) fraudulent, 2) material to either the acceptance of the risk or assumption of the hazard, or 3) the insurer, in good faith, would not have issued the policy, or would not have issued the policy for as large an amount, or would not have provided coverage. W.Va. Code § 33-6-7. Voiding a policy due to a misrepresentation is an affirmative defense, and must be proven by a preponderance of the evidence.

In determining whether an insured's actions are fraudulent, the Court adopted its traditional rule with regard to fraud. Specifically, the Court determined that, for a misrepresentation to be fraudulent under 33-6-7(a), it must be "knowingly made with an intent to deceive the insurer and relate to material facts affecting the policy. *Powell*, 382 S.E.2d at 349. Further, the insurer cannot have any knowledge of their falsity. *Id*. at 349. Thus, for an insurer to prove an insured fraudulently misrepresented facts, the "misrepresentations, omissions, concealment of facts, and incorrect statements on an application for insurance by an insured must be knowingly made with an intent to deceive the insurer and relate to material facts affecting the policy." *Mass. Mut. Life Ins. Co. v. Thompson*, 460 S.E.2d 719, 724 (W.Va. 1995).

The West Virginia Supreme Court of Appeals defines a misrepresentation for the purposes of insurance as:

> a false representation of a material fact by one of the parties to the other, tending directly to induce such other to enter into the contract, or to do so on less favorable terms to himself, when without such representation such other party might not have entered into the contract at all, or done so on different terms.

Woody v. Continental Life Ins. Co., 141 S.E. 880 (W.Va. 1928).

Further, subsection (c) contains criteria that are based upon an objective standard of an insurer acting in "good faith." *Powell*, 382 S.E.2d at 350. This section of the provision adopts a test whereby a court asks whether a reasonably prudent insurer would consider the misrepresentations to be material to the contract. *Id*.

Wisconsin

A misrepresentation can be used as a defense only when the person making the representation knew or should have known it was false, and the insurer relies on the misrepresentation and the misrepresentation is material to the risk, or the misrepresented fact contributes to the loss. Wis. Stat. Ann. § 631.11.

To be entitled under the statute to rescind an insurance policy, the insurance company must prove:

> (1) that (a) a misrepresentation was made *and* (b) the person making it knew, or should have known, that it was false; *and* (2) either (a)(i) the insurer relied on the misrepresentation, and (ii) that misrepresentation was material, or (iii) it was made with intent to deceive; *or* (b) the misrepresented fact contributed to the loss.

Pum v. Wisconsin Physicians Serv. Ins. Corp., 727 N.W.2d 346, 351-52 (WI 2006).

Whether a statement is a representation is a question of law. Conversely, whether an insured knew a statement was false when making it is a question of fact left to the jury. *Id*.

As a threshold matter, an insurer must demonstrate that it actually relied upon the misrepresentation. *Id*. at 354. If the insurer did not rely on

the representation, then it is not material. *Id*. at 356. A material fact is "a fact that is significant or essential to the issue or matter at hand." *Id*. (citing BLACK'S LAW DICTIONARY).

Wyoming

Wyoming clearly follows the majority of jurisdictions by considering misrepresentations, omissions, concealment of facts and incorrect statements within the scope of the misrepresentation defense. Such statements do not prevent recovery unless they are fraudulent, material either to the acceptance of the risk or assumption of the hazard, or the insurer, if it had known the facts and in good faith, would not have issued the policy or contract, would not have issued it at the same premium or for as large amount, or would not have provided coverage for the hazard resulting in loss. Wyo. Stat. Ann. § 26-15-109.

Materiality is determined by "whether reasonably careful and intelligent persons would have regarded the omitted facts as substantially increasing the chances of the events insured against so as to cause a rejection of the application or different conditions, such as higher premiums. *Harper v. Fidelty & Guar. Life Ins. Co.*, 234 P.3d 1211 (Wyo. 2010). Even a good faith mistake does not excuse a material misrepresentation. *Id*. at 1217.

If an insurer can show a misrepresentation was material, then any misrepresentation, even one innocently made, will be sufficient to avoid coverage. *White v. Cont. Gen. Ins. Co.*, 831 F.Supp. 1545, 1554 (D.Wyo. 1993).

V. CONCLUSION

While each state takes its own specific approach to its rescission laws, general themes emerge. Most states read their statutes in the disjunctive and allow rescission if a misrepresentation or omission of fact is fraudulent, material, *or* affects the insurer's good faith decisions in issuing polices. Some states, like Arizona, require insurers to prove all three elements before it allows rescission. In addition, many states have addressed many of the factual scenarios that arise relating to misrepresentation, such as its effect on an innocent insured and an insurer's duty to investigate the veracity of an applicant's answers. In the end, an understanding of misrepresentation's three elements—materiality,

reliance, and intent to deceive—provides any attorney with a good start, no matter what state they find themselves in.

Teaching Moments In Leadership

By Rear Admiral Ray Smith, USN (ret)

•	Make good use of the leadership prism pointing down! Ignore at your own risk!
•	Avoid superficial measures when evaluating employees' potential.
•	Do not waste time or energy on the "mud" of life! Wash it off and move forward!
•	Maximize opportunities to work directly with your employees.
•	Learn to deal with unpredictability. It's predictable!
•	Use caution when increasing workload…slowly, at a pace which enables employees to adjust.
•	Remember, making decisions on your own produces outcomes, not necessarily solutions!
•	Find a way! There is always a way!
•	Two is one and one is none!
•	Stay situationally aware of your company's personal and business dynamics.
•	Develop a work environment where your employees continue to learn.
•	Personal recognition is vital to individual morale and effectiveness.
•	It's not the lofty sail but the unseen wind that moves the ship. You are the sail and your employees are the "unseen wind".
•	Basic leadership arithmetic! Authority + responsibility = accountability.
•	BE a personal example of what you expect from your employees.
•	"Know" your employees! They have lives outside of the work place!
•	Be aware and responsive to life crossings. You can change someone's life!
•	Create "teaching moments" within your organization. Right place, right time, right conditions!
•	Avoid empowerment! ENABLING your employees is the key to their self-esteem and productivity.
•	Learn from failure! "Sometimes the brightest light comes from a burning bridge!"
•	Do not fail at the same thing twice! "There is no wisdom gained in the second kick of a mule!"
•	Beware the Law of Unintended Consequences- i.e., great idea in concept, lousy idea in execution.
•	Do YOUR job! It is embarrassing to order an aircraft carrier anchor for your dinghy!
•	Leaders beware! Personal myths born of youth, which form the foundation of adult personalities, are almost completely devoid of facts and logic!
•	When faced with two courses of action in life, always take the one most personally uncomfortable. It will be the right one!
•	"Loyalty before all, except before honor!"
•	"Perfect knowledge" is elusive, but never emerges from one person!
•	Leaders are responsible for strategy, but they must also retain a working knowledge of the organization's tactical environment.
•	Avoid complacency, the "dark side" of success.

•	Strive for excellence! Build a team of consistent, not streak hitters!
•	Aristotle had it right! "We are what we repeatedly do!" Excellence then, is not an act but a habit!
•	Like Navy SEALs have learned, the only easy day was yesterday!
•	Manage energy- not time!