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Mandatory Arbitration and Access to Justice

IN the March 1993 issue of the *ABTL Report*, Bank of America's Assistant General Counsel Arne D. Wagner defends the Bank's recent attempt to impose an alternative dispute resolution (ADR) requirement on its customers. It is reasonable to anticipate that other banks will follow suit. Wells Fargo Bank has already done so. This development bodes ill for consumers' ability to enforce their rights and safeguards under consumer protection statutes and would make equal access to justice dependent upon financial resources.

Patricia Sturdevant

Bank ADR clauses typically mandate arbitration of individual disputes and judicial references for class actions and private attorney general cases that challenge business practices and seek relief for all affected customers. Such clauses attempt to deprive bank customers of access to the courts, particularly in class actions, and insulate banks against large jury verdicts. In the words of the architect of the Bank of America's ADR plan, Winslow Christian, this change will make the Bank "less exposed to unpredictably high damage awards." The purpose of these clauses plainly is to alter the rules governing dispute resolution to favor banks.

The advantages of arbitration and reference which Mr. Wagner enumerates may provide sound reasons why parties of equal bargaining power might choose to agree to resolve their disputes in the arbitral forum. Like sex, arbitration is fine between consenting adults. Imposing arbitration and judicial reference on unwilling consumers in order to reduce bank exposure is, however, unjust. Bank ADR clauses coerce parties of unequal bargaining strength into a forum which is per-

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A New Judge Learns about Settlement Conferences

ABOUT three years ago I was appointed to the San Francisco Superior Court. During that time I have participated in over 200 settlement conferences. These are some of the things that I do to help the attorneys settle their cases.

I believe the single most important quality that a settlement judge must have is the ability to engender trust. The parties must believe that the judge will keep all confidences. They must know, without any doubt, that what is told to the judge in confidence will never be revealed to anyone. Without that trust in the judge, I believe the settlement process cannot proceed. To that end, I have developed techniques to ensure that what is told to me by the parties remains confidential. For example, I never speak numbers unless I double check with the parties and get their permission.

The Hon. William Cahill

After that, the most important attributes are patience and persistence. The judge must simply never stop trying to find solutions to the parties' concerns and problems. In a signifi-

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Settlement Conferences

cant percentage of the cases the parties start the conference with very little belief that the case will settle and, in fact, are convinced that the conference will be a waste of everyone's time. They have been given unreasonable demands or offers and see no reason to negotiate. Nevertheless, most of these cases eventually settle because neither the Court nor the parties stopped the process, no matter how long and difficult it was.

The next most important thing a judge can do is to get the clients personally involved in the settlement process as soon as possible. In fact, settlement conferences are, with few exceptions, a waste of time if the clients and decision makers are not present in the courtroom. The client is the ultimate decision maker and the court and the lawyers must keep that in mind. The client is the only party that has to live with the consequences of the decision to settle or go to trial. The lawyer has other cases in the office and the court has hundreds of cases. The client only has one case and he or she must live for years with the decisions made on the day of settlement. I believe the client must be involved in every aspect of the settlement process and therefore I personally meet with all clients and insurance representatives in every case. For many, this meeting with the judge is their only "day in court."

I also try to remember that most clients are scared or at least very anxious about being in court. Many have never been to court but they have been waiting, sometimes for years, to come to court on this one day. Even if their lawyer has prepared them well (which is often not the case), they still are in an unfamiliar place and under a lot of stress.

I try to alleviate that stress by talking with the clients as early in the process as possible and always with the attorney present. I listen to their side of the case, trying to find out why they have taken the drastic step of being in court and why they have not settled. Each client has his or her unique reason for not settling their case earlier and that reason usually relates to non-legal issues. Clients are angry at the other side (and sometimes at the system itself), and resent the fact that their case is not yet resolved. They sometimes have been hurt or humiliated by the other party. Sometimes the attorneys have not prepared the client. There are as many reasons as there are clients. In one instance a case was not settling after three conferences because a 45-year-old client did not want to disappoint her parents who had been financing the suit. The case settled after a conference call with her parents who supported the settlement and assured her that she was not "caving in." Each case has a different story, but listening to the client or insurance adjuster for as long as it takes will reveal those non-legal concerns which must be addressed before the case is ready to settle.

It is also important that the judge understand the facts of the case. Many times a case is simple and can be learned easily from reading the settlement conference statements. In more complicated cases much more needs to be done. For instance, sometimes I have the main experts present their theories to the court, the parties, and the other side's experts. I am surprised at how often the experts have not considered the other side's opinions or even heard them. An expert does not often change his or her mind publicly, but often after such a presentation the entire conference takes a new direction. The court also has an opportunity to evaluate the expert and give the parties an honest appraisal of the likely effects of the expert's testimony. Of course, this appraisal has to be well thought out and completely candid in order to have an effect.

Often in a settlement conference it becomes obvious that the parties have not communicated well during the litigation and in fact simply do not understand the other side's case. In those instances, one party's description of a case bears almost no resemblance to the other side's position, and in fact the attorneys sound like they are litigating completely different cases. When this happens, it is helpful to have the parties give each other and their clients a brief opening statement outlining why they think they will prevail. I do not permit argument between counsel but I do allow all questions to clarify the other side's case. Often the result of this exercise is that one side sees for the first time what the true issues are and how weak or strong their case actually is. Giving the parties a few days to evaluate what they have heard and resuming the conference later has helped settle several cases.

After all these preliminary discussions on the facts and the clients' reasons for pursuing litigation, we begin talking about offers and settling the case. I never ask for a party's "bottom line." If they try to tell it to me, I explain that I do not accept "bottom lines" nor do I believe them. I tell parties that I never hold parties to their "bottom line" and, if they want to move away from their figure, I expect them to do so.

I hear "bottom lines" in every conference and they rarely are the parties' final position. In fact, such a declaration often puts a party in a position of saving face, which hurts rather than helps settlement. I also believe that parties, no matter how much they try, do not truly know their final figures until they have gone through a thorough settlement process and have to decide to end negotiations or try the case.

I also insist that at no time does a party bid against itself. Often attorneys will say that the offer or demand is so outrageous that they will not counter unless the other side takes a more reasonable position. My response to that argument is that, if the other side's demand is unreasonable, make an unreasonable offer. We will always keep the parties moving toward each other and at no time will any party ever have to bid against themselves. Following this procedure more often than not results in a settlement. Less often, there is an impasse but the parties know exactly how far apart they are and they know they have tried everything to settle.

I have also learned that one of the most important roles a settlement judge has is to ensure that the attor-

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Settlement Conferences

neys "speak the same language." We all are very good at expressing ourselves clearly but we often do not listen to what is said. When there has been a misunderstanding, I immediately get the parties together so they hear each other properly. This often creates immediate problems, but avoids much bigger problems in the future. Nothing is more frustrating than putting a settlement on the record and learning that there has been a misapprehension as to its terms.

The most effective settlement conference attorneys are those who have credibility. These attorneys always have reasons for what they do. They make demands and offers that have a sound basis in reality. It is frustrating to ask why a certain figure is demanded or offered and to have an attorney respond with vague generalities. The best attorneys can tell a judge precisely how they calculated their position and freely state that there may or may not be some room for negotiation.

Aside from an unprepared, unprofessional attorney, the least effective lawyer is one who simply says "NO" and has no alternatives or reasons for his or her position. Sometimes the problem lies with the client, but most usually it is an attorney's negotiating style. Apparently these attorneys believe that frustrating the other side helps resolve a dispute. It rarely does and in fact wastes everyone's time. It also has the effect of discouraging the opposing side by making them more convinced that they will be going to trial and often terminates discussions prematurely.

Some of the more difficult cases to settle are those with multiple defendants, all of whom want the other defendants to "pay their proportionate share." These defendants make no offer unless they know all the defendants' offers. In some cases all defendants agree that plaintiff is entitled to a large amount of money, but the defendants can make no offer at all because no one can agree as to how much each will contribute. I find it most effective to have each defendant give me their individual offers confidentially and to simply offer the plaintiff a lump sum. After agreement is reached then each defendant learns how much the others have contributed. After all, each defendant has reasonably analyzed the case from its own perspective and the contribution of one is unrelated to the contribution of another. In cases where the parties insist on "paying only their share" in relation to others, I find that the cases eventually settle, but the releases are complicated, the conferences take four to five times as long, and eventually the defendants depart from their positions and make individual offers anyway.

As in all court-related matters, the best attorneys are brief and clear in their presentations. Even the most complicated case can be distilled into a short presentation. The clearer the presentation the more effective it is. After all, the attorneys are teachers, trying to explain to the judge why the case should settle at their num-

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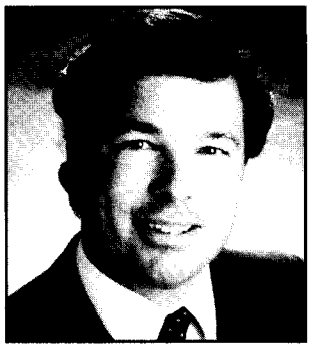
Tips For a Successful Mediation

LET'S assume that you have either heard good things about the mediation process or have even tried it once or twice. Perhaps you have a case that you believe may be ripe for a mediated resolution but you are unsure how best to get from here to there. Most of all, you do not want to spend a lot of time and effort on a structured settlement process without real confidence that it will succeed. Here are some tips:

Getting Your Client's Approval To Mediate. Usually, this step is easy. Since civil litigation can be the most inefficient, time-consuming and expensive process ever devised to resolve a monetary dispute, most clients welcome a shortcut to a fair resolution. The fact that you have suggested it also allays any client's suspicions that attorneys are inclined to stretch out litigation for their own profit, not shorten it. You can say to your client (and mean it) that you are trying to spend your client's money as if it were your own–a message that can help secure a long, ongoing relationship with any client.



Randall W. Wulff

Non-Binding Procedures

Since mediation proceedings are non-binding and confidential, if your client feels at any time that the proceedings should be terminated, you simply walk out and proceed with litigation. The substantial upside of a promptly negotiated and fair settlement often outweighs the modest downside risks, which would include: (1) the expense of the mediation should it fail (relatively minimal–perhaps a day or, at most, two); and (2) any tactical disadvantage in subsequent litigation resulting from candid disclosure to the other side of facts and legal theories before completion of discovery or trial (even this "disadvantage" is probably illusory, unless the next stop is binding arbitration without any meaningful discovery rights, in which case the risk of "showing your cards" early is one to be taken seriously).

Getting Your Opponent To Participate. Obviously, your opponent's client should benefit equally from a shortcut to a fair, negotiated settlement. Introducing the subject of mediation to your opponent, however, is a far more delicate matter. Assuming you have concluded tactically that now is the proper time to broach settlement, you still want to avoid any stigma of weakness associated with the party who makes the first overture.

First, consider an indirect approach, If, for example, the matter is pending before the American Arbitration

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Tips for a Successful Mediation

Association for arbitration, their case administrators routinely suggest mediation to all parties. A phone call to your administrator can urge that the time is right for this message from a neutral messenger.

If you decide to approach opposing counsel directly, point out to your opponent how strong and confident each of you apparently feels about your respective positions in the case; therefore, perhaps each of you could benefit from the evaluation of a neutral third party. Emphasize that mediation is not set up to prove one side wrong; rather, it assists both sides to find out that, perhaps, each is not quite as "right" as he or she thinks. Say that you are willing to run that risk if your opponent is.

The idea of mediation also sometimes springs from communications directly between the parties. As clients become increasingly sophisticated about this cost-saving tool, these conversations are becoming common.

If your opponent balks at paying a proportionate share of the mediator's hourly rate, you may consider offering to pay their share of the mediator's fees unless the mediation is successful, in which case the mediator's rate will be apportioned properly as part of the settlement. Given the extremely high success rate of mediations, this proposal is not nearly as risky as it might first sound.

Selecting The Best Mediator. Selecting an able mediator is one of the two most important factors affecting the success or failure of your mediation. Success will depend in large part upon the abilities and experience of your mediator. The instrument is only as good as the musician playing it.

Select Impartial Mediators

The mediator's impartiality must be real. Having a mediator who is also your friend can backfire and undermine the trust of the other side. While all parties should be comfortable with the mediator, close prior relationships often make the mediator's job more difficult.

There are numerous groups and organizations that offer qualified mediation services, both non-profit organizations like the American Arbitration Association, and numerous businesses that provide full-time trained mediators for profit. Even casual inquiries will open up a host of options.

Most important, do some homework on your prospective mediator. Any good mediator is more than willing to provide several references for you to contact. Call them. There is no better source of information about a mediator's skills. Mediators' styles also differ radically, and you can discern from references whether a prospective mediator's style fits your case and your client.

Have The Real Decision-Makers Present. This is the second most important (and often largely ignored) factor dictating success or failure in mediation. A mediation is akin to a chemical reaction which occurs over a matter of hours or days. People invest enough of their time and energy so that, after a while, they do not want to see it fail. It is impossible to convey accurately to someone who is not present the subtle shifts of position that occur when the facts are aired and the mediator privately puts the strengths and weaknesses of a case under a spotlight.

Insist that the entire process be observed by the individuals who can make settlement decisions. These individuals must come to the process with authority to negotiate and adequate dollars.

Ideally, each side will bring a high-level decision-maker who had no personal involvement in the events giving rise to the dispute and, therefore, no reason to be defensive. Obviously, there are some matters involving, for example, corporate entities or public agencies, where ratification of any settlement by a Board or management group will be necessary. In these instances, that organization should be expected to send the representative with enough clout in the organizational hierarchy that his or her settlement recommendation most likely will be followed.

Before the mediation starts, the lawyers should disclose who will attend and satisfy each other that an appropriate decision-maker will be attending for each side. If a problem develops, request a pre-mediation conference with the mediator to resolve this critical issue.

Set Aside Enough Time. Do not underestimate the amount of time you will need. You are much better off overestimating the length of the mediation, leaving yourself a margin of error.

Mediators Need Factual Background

While the level of fact exchange that must occur before dollars are negotiated can vary dramatically in different mediations, remember that the decision-makers and the mediator will need to hear some factual background, even if you already know the case backwards and forwards.

When blocking out dates to mediate, it is worth waiting a little longer to begin if, in trade, you get an adequate number of hours or days when all necessary parties can be present. There is real value in the momentum created by the commitment to "stay with it for as long as it takes."

Prepare. More than 90% of civil lawsuits settle. If you use a first-rate mediator to assist, settlement will occur four out of five times during a mediation. What better quality time can you spend for your client than preparing for what is likely to be the most important event of the case.

Remember, this is your opportunity to present your best case, not just to opposing counsel but also to your real adversary, the client on the other side. For once, your message will not be going through the "filters" of opposing counsel. If enough money is at stake, it can be particularly effective to have key percipient or expert witnesses attend and, without cumbersome direct or cross-examination, simply summarize the evidence they would provide in court. This procedure gives the other side an opportunity to evaluate the credibility of opposing witnesses, and it is often more credible to decision-makers than a glib attorney's presentation.

Patience. Like a mating dance, a mediation requires consenting adults on each side to succeed. Enough time has to be spent. Each side must feel that they have had a fair opportunity to present their views to the mediator as well as directly to the other side. The mediator also needs

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Tips for a Successful Mediation

enough time to reduce emotional attachments to issues, separating people from the problem. Rather than rushing to the negotiation stage of the process, trust an experienced mediator to set the pace.

Hanging On To The Settlement. If an agreement is reached in the mediation, *do not leave* until the salient terms have been written down and all parties have signed an agreement. It need not be a comprehensive final agreement; indeed, the parties should expect that the attorneys will later transform the memorandum agreement into a formal, final document. Nevertheless, the process of writing out the key terms flushes out non-monetary issues like the scope of releases, perhaps not yet even discussed but often controversial. There is no better time to resolve these other issues, while the parties are enjoying the fleeting mood of relief, forgiveness, elation and success. If you wait, these issues can come back to haunt and even scuttle what appeared to be a successful settlement. No matter what the hour, resist the temptation to eat or sleep until the job is truly done.

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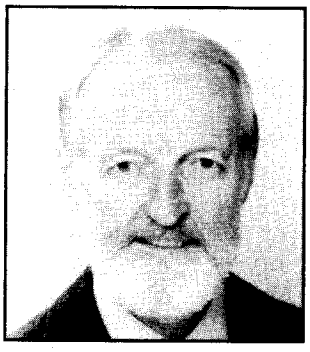
Using Trial Consultants in Business Cases

TRIAL consultants help litigators to search out bias among jurors and to speak persuasively with lay people. The systematic use of social science research methods to help lawyers win trials began less than 20 years ago. Today most business trial attorneys at least know that such services are available, but many don't know much about them. Here are some ways you can use trial consultants that taps into what is really valuable about their services.

Simulate every big trial before going to court. Trial simulations, and more informal "focus groups," are the most valuable tool that a trial consultant can offer a litigator. In a simulation, one or more groups of mock jurors hear summary versions of the arguments and evidence on both sides of a case, and then are videotaped while they deliberate to a verdict. It is simple prudence, and highly cost-effective when your client has millions at stake, to try your case out on a couple of mock juries before you take it into court.



Terry Lunsford

There is no experience quite like giving your best arguments and evidence to a group of lay people and then watching while they react–liking it, hating it, chewing it over, repeating your best points, or ignoring them and going for your opponent's arguments. Virtually every attorney who has tried this experience will say it is extremely valuable for any litigator, and it will teach you a lot about almost any case.

What you get, no matter what the trial consultant tells you, is not a prediction of the trial outcome. You do get very valuable information: How well jurors will understand your story of the case. Which issues and evidence they respond to, which ones they ignore. How they reason, in lay language, about the merits of each side's arguments. What they think of your personal style of advocacy. What analogies they use to make sense out of the case. And a lot more.

But the secret value of any simulation is the practice you get in boiling a complex case down to its essentials. When you have been preparing a complicated set of legal and factual issues for months or even years, there is great danger that you will lose the forest for the trees. Attorney after attorney has found it easy to get lost in the details and the legalities, and forget the underlying issues of the case: who did what to whom, and whether anyone was hurt by it.

When you have to summarize your case–and your

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Using Trial Consultants in Business Cases

opponents'—for a simulation, you come face-to-face again with its core elements. You become clearer about which arguments are central, which ones peripheral, which documents are "hot," which testimony will make or break your client's cause. You see where your strengths and weaknesses lie, where you have to put your precious remaining time, tying down the evidence on this point or finding a better way to explain that one. You are forcefully reminded that talking to a jury is not the same as talking to your partners and associates, or arguing to a judge. You start to see the central "jury issues" for when you take your case to trial.

Even if the case doesn't end up in trial—over 90% of business cases do not—you'll find that this process is a long leg-up in your preparation for settlement negotiations. Every settlement conference, implicitly, is an argument about what a group of lay jurors *would* decide in the case if it went to trial. A simulation, and your preparation for it, can often give you a command of that question that will impress the settlement judge and scare your opponent into being reasonable.

Using Focus Groups

Use focus groups and brief consultations on your smaller cases. You can also do research on a more modest scale if your case is a middle-sized one. Presenting the central issues and facts to two focus groups on a weekday evening will keep down your time and costs. Also, it will give you invaluable feedback from lay people comparable to your jury pool about where the hot spots in the case lie and how well you are likely to do at trial.

When your case is a small one, a consultant can still help. Most experienced trial consultants have helped out in court at many jury selections, analyzed dozens of mock trial videotapes and interviewed scores of mock or real jurors after trial. In relatively few hours, a consultant can learn your basic case facts and help you think about your case as jurors will think of it, even without doing original research. A good consultant can quickly help you isolate the "jury issues," find the central themes that will catch jurors' attention on each side of the case, draft a juror questionnaire, write specific voir dire questions, and prepare you to use voir dire. So when the case budget doesn't allow for mock jury research, use an experienced consultant as a quick substitute.

Go for more than a "juror profile." Many attorneys still think that what they want from a trial consultant is a "profile" of "the ideal juror" whom they should try to "select." That is a mistake. Of course, you can't "select" anyone for your jury; you can only *de*-select a few people by challenging them. But there is much more to voir dire than that.

Law schools don't teach very much about jury selection, but research on juries in the last two decades has produced valuable new knowledge. Most litigators are still trying to argue their case in voir dire, and judges increasingly cut off attorney questioning in response. Too many lawyers still decide which jurors to challenge on the basis of stereotypes, such as "women are good for plaintiffs, but accountants are bad." This is shooting fish in a barrel.

Instead, you need to know how to get information about jurors in voir dire, using a pretrial juror questionnaire, open-ended questions, follow-up probes, and careful analyses of panelists' answers. You need to know what kinds of juror biases are important in your particular case and which ones you most need to look out for. You need to know how to evaluate a complex web of information—about attitudes, personal experiences, personality traits, and jurors' appearance and demeanor—as well as demographic traits like gender, race, age, and occupation. A trial consultant can bring a rich practical experience and psychological knowledge to help you with this.

The Logistics of Voir Dire

You also need to know the crucial logistics of voir dire, such as getting the judge to randomly number your panel early, so you know who is coming into the box, in what sequence. Attorneys often forget that you must get time to look at questionnaires before oral questioning and time to discuss your challenges before you make them. Details like these can determine whether you win or lose a major business jury trial.

Learn to tell a story. Trial consultants can help you find the human story in your case and tell it to jurors in clear, memorable terms, starting with your opening statement and ending with oral argument. That way, the jurors can use *your* words, images, and ideas when they discuss the case in the jury room, after you and opposing counsel have stopped talking.

Research shows clearly that one of the best ways to help people take in, retain, and recall information is by putting it into a narrative form, with a chronology and human characters, motives, and sequences of actions, like the ones we use in everyday conversation. It also helps if you use short words and sentences, active verbs, rich imagery, and apt analogies, laying off the learned abstractions, legal Latin, and technical jargon. But this is hard for all of us, especially when a case is about debentures, trade secrets, or Generally Accepted Accounting Principles.

A skilled trial consultant can help you put your business case into "story" form, around a few central themes that have moral and emotional force, telling the "human" meaning of the technicalities.

Use post-trial interviews to learn what happened. Whether you try many cases or only a few, you can benefit from post-trial interviews with jurors which tell you why you won or lost and how they reached their verdict. Where a string of cases has similar legal issues and fact-questions, this is ammunition for use in the next case in the string. Even when your cases differ, you can learn a lot about your trial strategy, the strength of your evidence, what jurors didn't understand, and what each lawyer did that impressed them. Competent trial consultants are trained interviewers who know how to get jurors

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NICOLE A. DILLINGHAM

On ARBITRATION

BLIND adherence to choice of law and forum selection clauses gives rise to serious risk of procedural unfairness. First, arbitration in a distant forum may not be economically feasible for many individuals, depriving them of a meaningful right to litigate. Second, because there is generally no discovery allowed in arbitration, pre-hearing depositions cannot take place. The only option is to subpoena witnesses to appear at the hearing. But the subpoena power cannot compel a witness to travel to another state for hearing and, without depositions, the testimony simply cannot be presented. To avoid this result, it may be necessary to insist that the arbitration hearings be allowed to take place in *both* the contractually designated forum and the forum in which the witnesses are located. Third, frequently the laws of the designated forum conflict with those of the jurisdiction in which the parties operate. This is particularly true, for example, in the enforcement of non-compete provisions. Such clauses are void in California, but are permitted in other states. Similar disparities in the law are common with respect to availability of punitive damages and attorneys fees awards. If the choice of law provisions are deemed enforceable, an entity with nationwide operations may find it possible to avoid the laws of the jurisdiction in which it operates and citizens of California may be denied the protection of California law. To avoid these results, challenges to the choice of law and forum may be permissible.

Choice of Forum

The parties' designation of a choice of forum for arbitration should be disregarded where the specified locale is unreasonable or would result in substantial injustice, particularly if the provision arises out of an adhesion contract or was otherwise not fully and freely negotiated. While the American Arbitration Association clearly favors enforcement of the contractually designated forum, it will consider issues of inherent unfairness and will weigh the following factors: location of parties; location of witnesses and documents; location of site or place of materials; relative cost to the parties; place of performance of contract; laws applicable to the contract; place of previous court actions; location of most appropriate panel of arbitrators.

The recent decision in *Patterson v. ITT Consumer Financial Corp.*, 14 Cal.App. 4th 1659 (1993), is a good illustration of the kind of case where the courts declined to honor a forum selection clause. In *Patterson*, a finance company had taken defaults against numerous California residents, consumer borrowers, in arbitration proceedings held in Minnesota pursuant to a standard provision of a pre-printed loan agreement. The court of appeals held that the choice-of-forum provision for arbitration was unconscionable, outside the reasonable expectations of the borrowers, and "the likely effect of these procedures is to deny the borrower...any opportunity to a hearing, much less a hearing where the contract was signed...."

Choice of Law

Similarly, the parties' contractual choice of law to govern arbitration should not be given effect if it would violate important public policies of this state, such as protection of the right to practice a profession. *Frame v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 20 Cal. App. 3d 668 (1971). Again, this principle is in keeping with the case law declining enforcement of choice-of-law provisions in court actions. And, as with the contractual selection of a locale, the courts will consider whether the contract was entered into at arm's length and was fully negotiated, and whether the parties knew and understood the consequences of the "choice" of law. *See e.g. J. Alexander Securities, Inc. v. Mendez*, 17 Cal. App. 4th 1083 (1993) (Award of punitive damages enforced in favor of California resident although New York law, the designated choice of law, did not permit punitive damages award.) If there was no effective choice of law (for example, where an adhesion contract is to that extent unenforceable) then the choice of law must be made by determining which state has the most significant relationship to the transaction and the parties, based upon factors including: the place of negotiation of the contract, the place of performance, the location of the subject matter of the contract, and the domicile of the parties.

Nicole A. Dillingham

Either party may commence an arbitration proceeding in the desired forum, whether or not it is the contractual forum. Under the Commercial Arbitration Rules of the American Arbitration Association, Rule 11, a party has ten days to object. If an objection is filed, the petitioner can stay the arbitration and petition the court to decide the appropriate forum and applicable law. Venue for such a petition would be proper in the county where the arbitration proceeding was filed. C.C.C. § 1292.2. The petitioner may be entitled to an evidentiary hearing on whether the contract was adhesive, whether the specified locale comports with his reasonable expectations and whether it is unduly oppressive. *BOS Material Handling, Inc. v. Crown Controls Corp.*, 137 Cal. App. 3d 99, 108 (1983). In the alternative, a declaratory relief action might be filed in court to obtain a determination of these issues before arbitration. Another option is to submit these questions to the arbitration tribunal, being careful to advise the client of the considerable deference that is accorded to arbitrators' decisions once they are made.

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Mandatory Arbitration and Access to Justice

ceived to be more hospitable to the financial institution.

The notion of mandating arbitration should have no place in our justice system. Arbitration as a method of resolving disputes is a creature of contract premised on the ability of parties of equal power to choose what method of resolving disputes will best serve their mutual needs. Arbitration arose in the context of labor relations, where unions and management negotiated a way of rapidly resolving disputes before a highly skilled labor arbitrator who is trusted by both sides in order to avoid strikes and labor unrest that jeopardized the pecuniary interests of both parties and the societal interest in industrial stabilization.

Thereafter, the use of arbitration to resolve disputes expanded. It was frequently negotiated at arm's length in commercial contracts between experienced and sophisticated business entities who desired to continue their business relationships. Part of those negotiations typically included a choice of which law would govern transactions between entities in different states or countries. In this commercial context, parties should be able to freely negotiate arbitration agreements in the expectation that they will be enforced. Requiring arbitration in the bank-consumer context, however, distorts the process and raises serious issues of fairness.

The essence of arbitration is that it is consensual. The Federal Arbitration Act does not express any preference for arbitration, but simply for enforcing privately negotiated agreements to arbitrate, like any other contract, according to their terms. The consequences of arbitration are severe: even decisions that are wrong as a matter of fact or law and result in a manifest injustice cannot be overturned on appeal. *See Moncharsh v. Heily & Blase*, 3 Cal.4th 1 (1992), and Code of Civil Procedure §1280, *et seq*. The rationale for tolerating the possibility of an unfair or incorrect resolution is that parties who bargained to arbitrate should be held to it. This rationale requires a knowing consent to arbitrate. No system of resolving disputes can be considered fair if it can expose parties to manifest injustice without their knowing consent.

The Bank of America's method of communicating this change in contract terms is unlikely even to inform consumers, and does not seek (or obtain) their express consent. The Bank's notice of change of terms states:

> CHANGE OF TERMS NOTICE FOR BANKAMERICARD VISA, MASTERCARD, VISA GOLD, GOLD MASTERCARD, AND APOLLO ACCOUNTS
> Dispute Resolution – If you or we request, any controversy with us will be decided either by arbitration or reference. Controversies involving one account, or two or more accounts with at least one common owner, will be decided by arbitration under the Commercial Arbitration Rules of the American Arbitration Association. All other controversies will be decided by a reference under California Code of Civil Procedure §638 and related sections. A referee who is an active attorney or retired judge will be appointed

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Settlement Conferences

bers. A boring, drawn out presentation does not teach anything and in fact hurts a party's position. A clear, concise presentation is as effective as it is rare. Brevity is good, less is more.

Finally, the ultimate settlement technique for everyone–one that truly reveals everyone's "bottom line"–is an open trial department. Attorneys and clients walking into a courtroom filled with 50-60 potential jurors get to their actual "bottom line" quickly. Many hopeless cases settle after a trial department has been assigned. Unfortunately, by that time, money has been unnecessarily wasted. Hopefully though, the Court has given everyone an opportunity to avoid that waste by providing an opportunity for a thorough and productive settlement conference.

The Honorable William Cahill is a judge of the San Francisco Superior Court.

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Using Trial Consultants in Business Cases

talking freely and honestly about their reactions to a trial.

Keep building your knowledge of how jurors think. There are many more ways to work with a trial consultant, but the most important point is a broader one. Use these professionals to help you build your own knowledge of juries. Keep learning what the latest research is showing about how jurors reason, what biases are common in the kinds of cases you try, how you can identify biased jurors before they get on your juries, how you can present your case so the jurors will hear it and agree.

That way, you can show your business clients an advocate who knows the law and the facts but also knows about the *people* who, in a jury trial, make the final decision.

Terry Lunsford, J.D., Ph.D., is with National Jury Project/West.

COMING EVENTS

December 1, 1993	MCLE Dinner: *Electronic Data Recovery in Business Litigation* Sheraton Palace Hotel Cocktails at 6:00 p.m. Dinner at 7:00 p.m.

Call Phyllis Montoya (415) 434-1600
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CHARLES R. RICE

On SECURITIES

THE U.S. Supreme Court will consider this term whether there is an implied private right of action for "aiding and abetting" violations of section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5. *See Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, U.S. Sup. Ct. No. 92-854 (*cert. granted*, 113 S. Ct. 2927 (1993)). The time is ripe for the Court to review an area that is as fuzzy as a bear and just as dangerous for the attorneys, accountants and corporate managers who are sued for failing to detect and stop someone else's fraud.

Aiding and Abetting Liability

Although the Supreme Court has twice expressly reserved the question, *see Herman & MacLean v. Huddleston*, 459 U.S. 375, 379 n.5 (1983); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 191 n.7 (1976), every circuit that has considered this issue has found a private claim for aiding and abetting a Rule 10b-5 violation. But determining when a defendant who has not committed a primary violation may still be "secondarily" liable has not been easy. In the Ninth Circuit (and most others), a plaintiff must prove (1) an independent primary wrong; (2) actual knowledge (or, in some cases, reckless disregard) by the alleged aider and abettor of both the wrong and his or her role in furthering it; and (3) substantial assistance of the wrong. *Levine v. Diamanthuset, Inc.*, 950 F.2d 1478, 1483 (9th Cir. 1991).

Most courts use a "sliding scale" analysis that mixes the "scienter" and "substantial assistance" elements. For example, recklessness is sufficient only if the assistance is very substantial, *i.e.*, actual misrepresentations or other affirmative action. Conversely, in some circuits, mere silence (even without a duty to disclose) can be substantial assistance if there was conscious fraudulent intent. Similarly, in the Ninth Circuit, a duty to disclose may arise from "knowing assistance" of the violation. This fact-specific "sliding scale" analysis makes it very difficult for alleged aiders and abetters to win motions to dismiss or for summary judgment, so even those who would ultimately prevail on the merits must either settle or engage in protracted and expensive litigation.

Now Before The Supreme Court

The Tenth Circuit recently held that a defendant who was only reckless could be liable if it took some "affirmative action" that assisted the primary violation. *First Interstate Bank of Denver, N.A. v. Pring*, 969 F.2d 891, 902-03 (10th Cir. 1992). The Justice Department and SEC urged the Supreme Court to grant the defendant's certiorari petition in order to confirm that recklessness was sufficient in such cases. In granting the petition last June, however, the Supreme Court went beyond the issues raised by the parties and requested briefing on whether there is any implied private right of action for aiding and abetting a Rule 10b-5 violation.

If it follows recent form, the Supreme Court will try to determine Congress' original intent. Congress, however, never expressly created a private claim for even a primary violation of Rule 10b-5. Such claims are "a judicial oak which has grown from little more than a legislative acorn." *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 737 (1975). Indeed, trying to interpret Congress' original intentions regarding secondary liability when Congress didn't establish primary civil liability but remained essentially silent while the federal courts created both primary and secondary liability is an exercise that only a lawyer would attempt.

The Supreme Court has accepted judicial creation of a private claim for conduct that Congress has expressly prohibited, but it may balk at judicial creation of a private claim for less culpable conduct that Congress has not prohibited. Critics of "aiding and abetting" liability argue that (1) Congress expressly created only one form of secondary liability under the 1934 Act, *i.e.*, for defendants who "controlled" a primary violator; and (2) it expressly provided for aiding and abetting liability only in the context of certain criminal and SEC enforcement proceedings.

Charles R. Rice

In determining the appropriate statute of limitations and the availability of contribution among defendants under section 10(b), the Supreme Court has looked to the other sections of the 1934 Act that did expressly create private rights of action. Since sections 9 and 18 do not impose aiding and abetting liability, the Court may well find that Congress could not have intended aiding and abetting liability under section 10(b).

One argument in favor of aiding and abetting liability may be that requiring insured professionals to reimburse fraud victims will spread the loss and encourage professionals to police their own clients. But stigmatizing professionals as frauds and saddling them with catastrophic personal liability solely for "policy" reasons, is unfair.

The Supreme Court may opt for a more limited reform: requiring knowing or intentional conduct by the alleged aider and abetter. Secondary liability would be limited to those who consciously ally themselves with frauds, not those who are only careless watchdogs. Plaintiffs will still argue that fraudulent intent can be inferred from a defendant's reckless disregard of "red flags," but the courts should look critically at this proposed inference, especially when it requires believing that successful managers and professionals would risk their careers and net worth on a scheme to defraud.

Mr. Rice, Editor of ABTL Report Northern California, *is a partner in the firm of Shartsis, Friese & Ginsburg.*

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Mandatory Arbitration and Access to Justice

> by the court after selection by the American Arbitration Association using its procedures for selecting arbitrators. The arbitration or reference will take the place of a trial before a judge and jury. (This is a new provision for Cardmember and Apollo Account Agreements. If you continue to use your account, this new provision will apply to all past and future transactions.)

The notice was inserted as a "stuffer" in the monthly statement to credit card holders and checking account customers. It is highly questionable whether customers even read such notices, which are included with other material such as a newsletter from the Bank and solicitations to purchase luggage, insurance and other goods or services.

Moreover, the notice does not say it is a contract and does not look like the Bank's standardized cardholder agreement. It has none of the indicia of a valid and binding contract. There is no manifestation of assent by consumers to be bound to these new terms. Instead, consumers are deemed to have consented to the arbitration and reference requirements if they use their credit cards. But continuing to make charges on a credit card cannot reasonably be construed to indicate assent to arbitration or judicial reference. Nor is this purported new contract term supported by consideration. There is no benefit conferred upon the cardholder, nor any detriment suffered by the Bank. Instead, cardholders are being deprived by the Bank of substantial rights to unimpeded discovery, trial by judge or jury, and a court system funded by the taxpayers while getting nothing in return.

Finally, the terms of this new contract provision are not fully described. Nothing informs the Bank's customers that arbitration and reference will be costly or that discovery will be limited. Only those who obtain and read the rules of the American Arbitration Association will learn these important facts. Nor does the Bank explain that, as it interprets the ADR requirement, a referee's decision will automatically become the trial court's judgment. Only if the Bank's consumer customers happen to read a newspaper article that quoted Mr. Christian's press release of June 2, 1992, would they learn that the Bank construes its ADR clause to deny any judicial oversight of a referee's decision. Nor will consumers understand that case law specifies that arbitral decisions will be final and binding even if they are based on a misrepresentation of fact, apply the law incorrectly, or are unfair. Under these circumstances, no real agreement to arbitrate exists.

Even if there were a contract it would be adhesionary and unconscionable and therefore unenforceable. The ADR term is procedurally unconscionable because it is contained in a standardized form insert that is not negotiated but simply imposed by the party with greater bargaining power on a take-it-or-leave-it basis. Such a provision is not within the reasonable expectation of the consumer party. Moreover, the failure to describe many important features and consequences of arbitration and reference means that these will come as an unpleasant surprise to consumers only after a dispute has arisen. Consumers who do not know what they are losing will have no reason to consider moving their accounts to banks that do not require arbitration and reference of disputes, even if they were financially able to do so. Moreover, particularly in today's economy, not every consumer is able to pay off existing balances or obtain credit elsewhere without doing so.

The arbitration and reference provisions are also substantively unconscionable because they deprive consumers of constitutionally guaranteed rights. Article 6, §§21 and 22 of the California Constitution vest the judicial power in duly appointed or elected judges and limit the functions of commissioners and referees to "subordinate judicial duties." Consistent with this constitutional mandate, the case law uniformly holds that consent of the parties is required before cases may be decided by persons other than judges. Without such consent, as numerous cases hold, the findings of commissioners or referees are advisory only. In *In Re Edgar M.*, 14 Cal.3d 727 (1975), the Supreme Court held that the adjudication of a juvenile court matter by a referee acting without any procedures for judicial review and without the parties' consent violates the constitutional limitation of a referee to "subordinate judicial duties." *Id.* at 735.

In *In Re Horton*, 54 Cal.3d 82 (1991), the Supreme Court again confirmed that the jurisdiction of a court commissioner, or any other temporary judge, to try cases depends on the parties' stipulation. Since the judicial power of the state is vested in the courts, a judgment entered by a court commissioner without a proper stipulation would be void.

In order to meet constitutional muster, a referee's decision, in the absence of a stipulation, must be advisory only and subject to judicial review. *The People v. Perrone C.*, 26 Cal.3d 49 (1979); *In Re John H.*, 21 Cal.3d 18 (1978). Therefore, the bank's attempt to make an arbitrator's or referee's findings "the judgment of the court" without the opportunity for a rehearing by a judge is an unconstitutional delegation of the judicial power.

These constitutional requirements are also reflected in the statutory scheme governing reference. Code of Civil Procedure §638 requires a written stipulation for any reference. The case law consistently requires the written affirmation of both parties before a reference is permitted. *See e.g., In Re Hart's Estate*, 11 Cal.2d 89 (1938); *Fooshe v. Sunshine*, 96 Cal.App.2d 336 (1950).

Without consent, the reference of specific issues must be advisory only and the referee's decision becomes effective only after approval by the court. *Holt v. Kelly*, 20 Cal.3d 560 (1978). In *Bird v. Superior Court*, 112 Cal.App.3d 543 (1980), a reference exceeded statutory authority where the petitioner had not consented to reference, the issues referred were not those encompassed in Code of Civil Procedure §639, and the referee's

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MARY E. McCUTCHEON

On INSURANCE

As those of you who wrestle with insurance companies over payment of your defense fees know, Section 2860 regulates the appointment and payment of independent defense counsel (i.e., counsel selected by the insured rather than the insurer) where an insurer has agreed to defend its insured against a liability claim, but reserves its right to deny coverage pending the outcome of the case. The language of the statute is difficult to understand, and thus has been subject to misinterpretation by insurers and insureds alike. Knowing some basics about Section 2860 may help you in your struggles.

Section 2860 Does Not Abrogate 'Cumis'

Some insurer representatives claim that Section 2860 *eliminates* any duty to provide or pay for independent counsel. Section 2860 does not, however, abrogate the holding of *San Diego Navy Fed. Credit Union v. Cumis Ins. Soc., Inc.* (1984) 162 Cal.App.3d 358, 375 ("*Cumis*"). *Cumis* held that where an insurer agrees to defend its insured but reserves its rights to deny coverage for a settlement or judgment, a conflict of interest may arise which gives the insured the right to control the defense of the case, including the appointment of independent defense counsel ("*Cumis* counsel") to be selected by the insured but paid for by the insurer. Section 2860 clarifies the situations in which a conflict exists, but does not eliminate this right. See *U.S. Fidelity & Guaranty Co. v. Superior Court* (1988) 204 Cal.App.3d 1513, 1524 (enactment of Section 2860 recognizes *Cumis*'s conflict premise).

Section 2860(b) states that a conflict of interest, and thus a right to independent counsel, "does not exist as to allegations or facts in the litigation for which the insurer denies coverage...." Reading only this phrase, many insurers painstakingly draft coverage positions in which they do not expressly "reserve rights," but admit coverage for certain causes of action and deny coverage for others. They then refuse to pay for *Cumis* counsel, claiming no conflict exists. In fact, sub-section (b) continues "... however, when an insurer reserves its rights on a given issue and the outcome of that coverage issue can be controlled by counsel first retained by the insurer for the defense of the claim, a conflict of interest may exist." A complaint in which the same facts give rise to multiple causes of action, some which may be covered and some which may not be (*e.g.*, negligent or intentional conduct) is the classic example of a coverage issue whose outcome can be controlled by defense counsel. The insurer's response to the tender of defense should be analyzed carefully to ascertain whether the insurer is in effect (if not in print) reserving its rights to deny coverage based on issues which could be affected by defense counsel's litigation strategy.

Fee Limitations Limited

Section 2860(c) limits the insurer's obligation for payment of independent counsel to rates "...paid by the insurer to attorneys retained by it in the ordinary course of business...", which may be significantly less than commercial litigation rates. The statute (and, consequently, the rate limitations) does not apply, however, to all instances where an insurer is paying for counsel selected by the insured. It only applies where a policy "impose[s] a duty to defend upon an insurer." Many policies do not contain a "duty to defend," but only a duty to pay for defense costs; Section 2860 does not apply to these obligations. See *Safeway Stores, Inc. v. National Union Fire Ins. Co.* (N.D. Cal. 1993) 1993 U.S. Dist. LEXIS 2006.

In addition, the limitations of Section 2860(c) should not apply if an insurer breaches its duty to defend. In that instance, the insured may recover as damages *the fees it incurred in defending the case. Samson v. Transamerica Inc. Co.* (1981) 30 Cal.3d 220, 237. Section 2860 presupposes that a carrier has met its obligations and is defending the case; it does not purport to limit damages for breaches of policy obligations.

Mary E. McCutcheon

Furthermore, the fee limitations should not apply if the *Cumis* counsel is the only counsel defending the insured. Section 2860 assumes that two sets of counsel are defending the case – defense counsel appointed by the insurer and independent *Cumis* counsel appointed by the insured. See *e.g.*, Section 2860(f) ("both the counsel provided by the insurer and independent counsel selected by the insured...") In *National Union Fire Ins. Co. v. Hilton Hotels Corp.* (N.D.Cal. 1991) 1991 U.S. Dist. *LEXIS* 20123, Judge Patel ruled that where the insurer had chosen not to appoint panel counsel, and only one attorney (the independent attorney selected by the insured) was defending the case, the insurer was not entitled to the protection of Section 2860's fee limitations. Judge Patel reasoned that the purpose of Section 2860 is to give the insurer some monetary relief when two sets of counsel are defending the case, a protection unnecessary where the insurer pays for only one set of counsel.

Another federal court has held that the fee limitations of Section 2860(c) are not retroactive and therefore do not apply to fee agreements or insurance policies predating the effective date of the statute (January 1988). *Diamond Walnut Growers, Inc. v. American Motorists Ins. Co.* (N.D. 1991) 1991 U.S. Dist. LEXIS 7317. Thus, if an insurer agreed to pay certain rates in 1987, it cannot unilaterally lower those rates in reliance upon Section 2860(c). And in cases implicating pre-1988 policies the fee limitations of Section 2860 will not apply to the duty to defend under those older policies.

Knowing these basics may help your client to reap the benefits of Section 2860, while avoiding its limitations.

Ms. McCutcheon is a partner in the firm of Farella, Braun & Martel.

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determination was not advisory only. *Accord, International Jet Ski Boating v. Superior Court*, 232 Cal.App.3d 112 (1991). Indeed, §638 has been held to be constitutional specifically because the referee's report may be accepted or rejected by the court. *Sandoval v. Salazar*, 57 Cal.App. 756 (1922).

Finally, the constitutional guarantees of due process and equal protection contained in Article 1, §7A also require that the findings of a referee or other non-judicial officer be advisory only. *The People v. Perron C., supra. In the Matter of Gregory M.*, 68 Cal.App.3d 1085 (1977), held that due process and equal protection require a judge to review a referee's determinations. *Hebert v. Harn*, 133 Cal.App.3d 465 (1982), ruled that the statutory scheme for judicial arbitration, in order to be constitutional, required a right to *de novo* trial, by court or jury, as to law and facts. If judicial arbitration requires these constitutional safeguards, then non-judicial and non-consensual arbitration and reference must require no less.

Arbitration is particularly inadequate for resolving disputes about bank conduct because the typical arbitration clause seeks to avoid any discovery. Under California law, the right to discovery is deemed to be incorporated in agreements to arbitrate only for personal injury or wrongful death claims. In all other disputes, discovery is available only if the arbitration agreement expressly so provides. Since the typical bank ADR clause does not provide for discovery, banks would have to make available only those documents they intend to offer in support of their own claim. This would deprive consumers challenging the legality of bank charges of the evidence they need to prove their claims.

The substantive unconscionability of bank ADR clauses is exacerbated because it would greatly increase expense to consumers. Arbitration is inordinately expensive. The filing fees are $300 for a claim up to $25,000 (more than four times the $74 filing fee for Municipal Court) and $500 for a claim of $25,000 to $50,000 (almost three times the $182 fee for Superior Court). The maximum fee is $4,000 for a claim in excess of $5,000,000. If no amount can be stated, the filing fee is $1,000, subject to adjustment. If injunctive relief is sought, the fee may be any sum deemed "appropriate" by AAA. In cases involving more than two parties, an additional 10% of the administrative fee is due for each additional party. The parties must also pay fees for processing the case: $150 per party for the first 180 days and $150 per party for every 90 days thereafter that the case is pending; $100 per day for each party for hearings, for postponing hearings, and for renting hearing rooms. In addition, the parties must compensate arbitrators. Requiring these substantial fees in order to challenge bank practices is particularly egregious because cardholders, as taxpayers, have already paid for the court system to which banks would deny them access. They often cannot afford to pay a second time in order to challenge the bank's acts or practices.

Even if discovery is available in referenced disputes, it is still unconscionable to deprive consumers of access to the courts, which are established and supported by the state to afford forums for the rich and poor alike to present controversies at minimal cost to the litigants. Instead, a class of bank customers seeking to challenge unlawful conduct would be forced to bear the burden and expense of paying referees to handle law and motion issues, discovery disputes, and trial. Particularly in class actions and unlawful business practices cases, costs of reference could be many times more than litigation in court.

Bank ADR clauses would effectively insulate wrongful practices from any effective challenge. They would deprive customers of their constitutional rights without their knowledge or consent and subject them to the risk of speedy injustice. Alternative dispute resolution mechanisms can serve a useful and important purpose where the parties agree to them, but to afford both the appearance and reality of fairness and justice, they must be based on consent, not on coercion.

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