Letter from the President

These are troubling times to be a lawyer, particularly a litigator. Public esteem for lawyers has perhaps never been lower. High profile trials only exacerbate the public perception that there is a disconnect between justice and advocacy. Whichever way one comes out on the issue of "litigation reform," we must recognize that the public widely perceives lawyers as overzealous and unethical. The enactment by Congress of the recent "securities reform" legislation, with significant bipartisan support, is merely a more specific manifestation of this phenomenon.

While much of the cynicism concerning our profession is undeniably overblown, one must concede that some of the criticism is warranted. As the economics of our profession have changed, and as the media focuses more attention on the bar, there does appear to be an increase in the number of questionable suits, all too frequently followed by overly aggressive responses.

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Drafting Settlement Agreements: Five More Pitfalls

Four years ago, in the second ABTL Report for Northern California (March ’92), I wrote about my ten favorite pitfalls in drafting settlement agreements. But time marches on, and I have discovered five more ways to snatch defeat from victory by making mistakes in the paperwork. Some come from new court decisions; others, from first-hand experience. To take yourself out of the “unwary” category, consider the following five questions:

Question No. 1: How Can The Court Retain Jurisdiction To Enforce The Settlement?

Sometimes you want the court to retain jurisdiction to supervise a settlement, particularly if it involves more than merely exchanging releases for money or there are continuing obligations or some doubt that one party will perform. But most settlements provide that the pending litigation is dismissed. So, what happens if something goes wrong after the case is already dismissed? Do you have to file a whole new action, or can you go back lickety-split to the first court to enforce?

It all depends on how you drafted the agreement. In federal court, you’ll be back to square one unless your settlement is coupled with a court order that either: (1) expressly retains jurisdiction to enforce the agreement, or (2) specifically incorporates the terms of the agreement itself. William Keeton Enterprises, Inc. v. A All American Strip-O-Rama, Inc., 96 C.D.O.S. 324 (9th Cir., Jan. 16, 1996). This case is a good example of what can go wrong. The principal issue was whether the district court had jurisdiction to enforce the parties' settlement.

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Drafting Settlement Agreements

by enjoining the defendants from using certain trade names (in the strip-tease telegram business, no less).

Unfortunately for the plaintiff, the stipulated injunction was limited to enjoining the parties from disparaging each other and did not reserve jurisdiction to enjoin the defendants from using any particular trade names, including “Strip-O-Rama.” The district court entered the injunction, but the Ninth Circuit set it aside — both because the written stipulation fell short and because the parties’ oral recitation of their agreement on the record was, in the Ninth Circuit’s words, “enigmatic.”

The bottom line is this: if you want a federal court to retain jurisdiction to enforce your settlement, you should include a provision in the agreement that makes it contingent upon a dismissal order from the court that either expressly retains jurisdiction to enforce the agreement or incorporates the terms of the settlement. See also In re Hunter, 66 F.3d 1002 (9th Cir. 1995) (bankruptcy court did not have “ancillary jurisdiction” to relieve a party from his acknowledgement of satisfaction) and Kokkonen v. Guardian Life Ins. Co., 114 S.Ct. 1673 (1994) (district court did have “inherent power” to enforce a settlement where the parties’ stipulation did not reserve the jurisdiction to do so).

One more caveat. William Keeton underscores that, if your settlement includes an injunction, your agreement (and any court order that incorporates it) must meet the requirement of FRCP Rule 65(d) that every injunction order must be specific and concise in reasonable detail the act or acts to be restrained.

**Question No. 2: How Can I Get The Mediator To Retain Jurisdiction, Post-Settlement, To Enforce The Settlement?**

A related pitfall could be a real opportunity. These days, many commercial litigation cases are resolved with a third party mediator, who becomes intimately familiar with the case, the parties, the attorneys and the negotiating history. As a result, who better to enforce the settlement or resolve disputes about its terms than the mediator? And how better to keep the parties honest than by having ready access to this mediator?

All this will be to no avail unless you include appropriate language in the settlement agreement to authorize the mediator to act as a post-settlement arbitrator. Here is an example:

Any dispute relating to or arising out of any aspect of the interpretation or performance of this Agreement shall be resolved by final and binding arbitration, in California, before [the mediator], who shall have the power to authorize such discovery, and the means to obtain it, as he or she may deem appropriate. If [the mediator] is unavailable, the arbitration shall be conducted before another [for example, JAMS arbitrator] agreed to by the parties, or if they cannot agree, before [another arbitrator selected by the mediator or if the mediator is unable to make such a selection, by an arbitrator selected by JAMS]. The cost of the arbitration shall initially be split equally, with the prevailing party, as determined by the arbitrator, then to recover its costs and attorneys’ fees incurred in the arbitration.

**Question No. 3: How Can I Minimize The Risk Of A Malicious Prosecution Case Against A Plaintiff Who Dismisses All The Defendants Pursuant To A Settlement Without A Release From One Defendant?**

Suppose that your client sues a corporation and several of its officers and directors. You negotiate a terrific settlement with the corporation and have no desire to continue the case against the individuals. But one of the individuals refuses to sign the settlement and makes vague noises about malicious prosecution. Is there anything you can do to minimize this risk?

Yes. Assuming that the defendant corporation demands a dismissal of the entire litigation as a condition of the settlement, the agreement should simply include a recital that “The release of the Released Persons, in addition to the Settling Defendants, is a necessary condition of this settlement.” This should go a long way toward avoiding, as a matter of law, a “favorable termination” that is a necessary element of a claim for malicious prosecution. See, e.g., Fuentes v. Berry, 38 Cal.App.4th 1800, 1808-11 (1995) (summary judgment denied in malicious prosecution action because, among other things, the settlement did not recite that the dismissal of all defendants was a necessary condition to the settlement). Compare Pender v. Radin, 23 Cal. App.4th 807 (1994) (summary judgment granted in malicious prosecution action because, among other things, settlement provided that all parties were to bear their own costs and fees).

**Question No. 4: How Can I Make Sure That I Have An Enforceable Settlement Agreement Before All The FORMAL Paperwork Is Completed?**

This technical point could be all-important in a very practical sense. A settlement is often negotiated in principle and is memorialized in a short document that will ultimately be replaced by a formal settlement document with all the appropriate bells and whistles. But in drafting the preliminary term sheet, you need to keep one thing in mind if you want to be able to move for summary enforcement under C.C.P. § 664.6: have the clients — not just the lawyers — sign the document. So said the California Supreme Court in Levy v. Superior Court, 10 Cal.4th 578 (1995). There, the attorneys negotiated, or thought they had negotiated, a settlement that culminated in a five-page term letter from one attorney to the other. The other attorney accepted by return fax. The first attorney’s client then balked at signing the formal agreement, and the other attorney moved for summary enforcement. Denied. Resolving a conflict among the Courts of Appeal, the California Supreme Court held that since a settlement involved a “substantial right” of the client, the word “parties” in section 664.6 should be narrowly construed to mean the litigants themselves, not
just their attorneys. *See also Johnson v. Department of Corrections*, 38 Cal.App.4th 1700 (1995), which applies the *Levy* “principals-have-to-sign” rule to oral stipulations recited into the record before the court.

Although the side that lost in *Levy* could theoretically still move to enforce the settlement through a summary judgment motion or a separate suit in equity (whatever that is), both would be cumbersome and expensive. Far better to avoid the problem through good drafting.

**Question No. 5: How Can I Use The Settlement Agreement To Help My Client With The Taxing Authorities?**

Occasionally, settlements in business litigation cases also settle personal injury claims. If so, keep in mind the general principle that section 104 of the Internal Revenue Code generally excludes from gross income the "amount of any damages received (whether by suit or agreement...) on account of personal injuries or sickness...." Section 104(a)(2) excludes from gross income damages received for nonphysical (for example, mental or emotional) as well as physical injuries. *See United States v. Burke*, 112 S.Ct. 1867, 1871 n. 6 (1992).

In determining whether a particular injury is *personal*, the tax court typically focuses upon the origin and nature of the taxpayer's litigation claim. *Threlkeld v. Commissioner*, 87 T.C. 1294 (1986). Here is where settlement agreements come in. The most common method of making allocations between personal and nonpersonal injuries under section 104 is by explicit allocation in a judgment or settlement. While the courts and the IRS are not bound by such allocations, an allocation in a written settlement is typically respected by the IRS (although allocations made only for tax purposes will not be given effect). *See K. Gideon, Lawsuits and Settlements*, Vol. A6: Forms -- Planning Aides, ¶ 2002.03 (CCH Tax Trans Lib.). The tax court has held that, "When the settlement agreement allocates clearly the settlement proceeds between tort-like personal injury damages and other damages, the allocation is generally binding for tax purposes...." *Robinson v. Commissioner*, 102 T.C. No. 7 (1994).

In sum, if an express allocation is made in a settlement agreement, it will usually be the starting point -- and often the ending point -- of the IRS' analysis. But if there is no allocation, the situation becomes much murkier: the intent of the parties must be determined "from all the facts and circumstances," including the details surrounding the underlying litigation. *Estate of Morgan v. Commissioner*, 332 F.2d 144, 150-51 (5th Cir. 1964). A well-drafted settlement with an express allocation can help avoid such an unpredictable inquiry into all the surrounding "facts and circumstances."

In closing, please mark your calendars for March 2000. By then, the *ABTL Report* will probably be available online. And I will probably have discovered at least five more pitfalls.

*Mr. Stampf is a partner in the firm of Bronson, Bronson & McKinnamon.*

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**The Manual for Complex Litigation**

"A" MID the demonstrated benefits of “fast track” direct calendaring lies at least one potential drawback – the fast track can have a tendency to limit the judicial attention directed toward complex litigation. The uniquely complex case is intruding into a daily menu of “fast food” justice and is not always easily digestible. The daily processing of the great mass of more prosaic cases, cases more easily transformed into disposition statistics, tends to divert immediate judicial attention away from the complex case. Cases settle, among them complex cases, and one of the verities of fast track judicial life is the less time expended on a case that will settle without judicial effort, the better. There is a risk to application of this maxim, however. Lack of judicial attention can permit a complex case to metastasize into a cauldron of litigation inefficiency, possibly resulting in prolonged litigation and increased expense when early judicial intervention might have efficiently structured the case for settlement (or at least for streamlined trial).

Although there is no substitute for the input of judicial time, case management techniques can mitigate the time constraints and distractions of fast track. Most of these techniques were pioneered in the direct calendar environment of Federal court, initially in antitrust cases, eventually expanding to mass torts, securities and environmental litigation, and other areas.

In 1969, the Federal Judicial Center published the *Manual for Complex Litigation*, advocating the then-novel and somewhat controversial concept of active judicial management of complex cases. By 1985, when the broadened *Manual for Complex Litigation*, Second appeared, the idea of judges participating in the management of complex cases was much more accepted. This year brings the *Manual for Complex Litigation*, Third (the "Manual") updating and refining the previous work. The Manual is available from the Government Printing Office.

The *Manual* is based upon the Federal Rules of Civil Procedure ("FRCP"), and in some instances its recommendations are not consistent with state practice. In other instances, the recommendations of the *Manual* are mandated by state practice, and no special judicial attention is required. In some respects the *Manual* is overly generic or platitudinous or describes case handling techniques that are unrealistically delicate. Nevertheless, the *Manual* is a valuable resource for complex litigation in state as well as Federal court. Cf. *Manual* at 5-6. It contains useful ideas plus citations to instructive

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The Manual for Complex Litigation

authority on techniques for effective management of a complex case notwithstanding the distractions of fast track.

This review briefly samples and summarizes the 568-page manual.

Organization

The Manual is organized into four parts. Part I, “Introduction,” sets forth the purpose and use of the Manual, and cites to other useful writings on litigation management.

Part II, “Management of Complex Litigation,” forms the heart of the Manual. It begins with “General Principles” that motivate case management and proceeds through “Pretrial Procedures,” “Trials,” “Settlement,” “Attorneys’ Fees” and “Judgments and Appeals.”

Part III (untitled), in addition to courtroom technology, deals with specialized procedures for specific categories of cases: class actions, “multiple litigation” (cases pending in different Federal courts, or in both state and Federal courts, or concurrent civil and criminal litigation), criminal cases, antitrust, mass torts (of both the single-locus mass disaster and the multiple-locus mass toxic tort or defective product variety), securities and takeover litigation, employment discrimination litigation, patent litigation, CERCLA and civil RICO actions.

Part IV (also untitled) provides checklists (for pretrial review, development of discovery plans, special appointments and referrals, etc.) plus sample case management and other orders.

What is Complex?

Early on the Manual considers “What is complex litigation?” Notwithstanding earlier (abandoned) efforts at a restrictive definition, the Manual finds some definition “important to understanding the objective of this manual,” since “there is always a risk that complexity may be introduced simply by calling litigation ‘complex.’” Hence the Manual offers a “functional definition” of complexity. Manual at 5. The Manual identifies the “defining characteristic” of complex litigation as simply the need for judicial participation with counsel in case management. Litigation involving many parties in numerous related cases or litigation involving large numbers of witnesses and documents and extensive discovery are offered as examples of “complex litigation.” On the other hand, “litigation raising difficult and novel questions of law, though challenging to the court, may require little or no management, and therefore may not be complex” as the term is used in the Manual.

The goal of case management, according to the Manual, is to bring about “a just resolution as speedily and inexpensively as possible.” Manual at 10. The practical need for judicial management to achieve a just, speedy and inexpensive resolution is thus identified as the test for complexity.

In its treatment of the “what is complex” question, the Manual is similar to the Standards of Judicial Administration Recommended by the Judicial Council (January 1, 1995) (the “Standards”). Section 19 of the Standards, entitled “Complex Litigation,” defines complex litigation in subsection (c) as “those cases that require specialized management to avoid placing unnecessary burdens on the court or the litigants. Complex litigation is not capable of precise definition but may involve, for example, multiple related cases, extensive pretrial activity, extended trial times, difficult or novel issues, and post-judgment judicial supervision, or may concern special categories such as class actions; however, no particular criterion is controlling and each situation must be examined separately.”

Early Judicial Management

The Manual proposes early collaboration of judge and counsel to develop and implement a plan for the conduct of pretrial proceedings and trial in the complex case.

“Judicial supervision is most needed and productive early in the litigation,” Manual at 11, (just when the fast track may be, unfortunately, the least likely to provide it). Cf. Standards, subsections (a), (f) and (g), “judicial management should begin early”; “time limits should be established early”; “a preliminary trial conference … should be conducted at the earliest practical date.” Once the court’s attention has been focused on the case, the Manual provides an arsenal of litigation management techniques ranging from discovery and motion scheduling and sequencing orders, early issue identification methods, development of case management programs, anticipation of compliance problems and formulation of prophylactic measures, possible appointment of special-function counsel (lead, liaison, settlement, trial), attorney compensation systems when needed, work-product and attorney client privilege protections to facilitate exchange of information, joint or parallel orders in related litigation, orders to streamline protracted trials, etc. Cf. Standards, subsections (d), (g), (h) and (i) (generally stating in cursory fashion that “methods of sound judicial management” should be used, and enumerating some categories).

Time Constraints

Citing judicial time as the scarcest resource involved in litigation, the Manual urges “...judges to use their time wisely and efficiently and to make use of all available help. Time pressures may lead some judges to think that they cannot afford to devote time to civil case management. It is true that the extra attention given by the judge to a complex case can encroach upon the time immediately available to attend to other matters. But judges have found that an investment of time in case management in the early stages of the litigation will lead to earlier dispositions, less wasteful activity, shorter trials, and, in the long run, to economies of judicial time and a lessening of judicial burdens.” Manual at 10.

Issue Identification

“The sine qua non of management of complex litigation rests on the definition of the issues in the litigation. Unless the controverted issues have been identified and

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Waiver of Damages Provisions in Construction Contracts

Many major commercial construction projects are built pursuant to a form contract drafted by the American Institute of Architects ("AIA"). Buried deep within the fine print of this contract is a provision that the owner and contractor waive all rights to sue each other for damages to the extent those damages are covered by property insurance. While this provision may not be well known to many construction litigators, it has been the subject of numerous appellate decisions, and has been used successfully by general contractors and subcontractors alike to bar multi-million dollar claims by owners and their insurers in at least 30 states, including (most recently) California.

The Waiver of Damages Provision. The AIA "Standard Form of Agreement Between Owner and Contractor" is commonly used by owners and contractors in the commercial construction context. The "General Conditions" contain two critical provisions. First, section 11.3.1 obligates the owner to purchase "all risk" property insurance to cover physical loss or damage to the construction work. Second, and most significant, section 11.3.6 provides that:

The Owner and Contractor waive all rights against (1) each other and the Subcontractors, Sub-subcontractors, agents and employees of each of the other, and (2) the Architect and separate contractors, if any, and their subcontractors, sub-subcontractors, agents and employees, for damages caused by fire or other perils to the extent covered by insurance obtained pursuant to [General Condition] Paragraph 11.3 or any other property insurance applicable to the Work....

(The numbering of these provisions has been different in prior editions of the Standard Form Agreement, though the content has generally remained the same.)

Typical Context in Which the Waiver Applies. In most construction cases, the owner sues the general contractor and its subcontractors for property damages the owner sustained due to allegedly defective work by the general contractor or its subcontractors. Sometimes the damages are covered by insurance, and the owner recovers its damages from its own property insurer. The insurer usually files a subrogation action, either in its own name or in the name of the owner, to recoup the amount paid to the owner.

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defined, the materiality of facts and the scope of discovery (and later trial) cannot be determined... Probably the most important function the judge performs in the early stages of litigation management is to press the parties toward identification, definition, and narrowing of issues." Manual at 47. Cf. Standards, subsection (h), a principal object of the preliminary conference is "to expose at an early date the essential issues in the litigation." The Manual suggests a variety of techniques to "facilitate" issue identification in the complex case: non-binding statements of counsel, periodically updated: contention interrogatories or contention-and-evidence statements; cause of action element lists; pleading refinements; early preparation of proposed findings or jury instructions; severance, bifurcation or multi-furcation; etc.

Discovery

"Discovery in complex litigation, characterized by multiple parties, difficult issues, voluminous evidence, and large numbers of witnesses, tends to proliferate and become excessively costly, time consuming, and burdensome. Early and ongoing judicial control is therefore imperative for effective management." Manual at 54.

Citing the "principle of proportionality" which dictates the legal test for discoverability in the FRCP (which is not materially different in state practice), the Manual emphasizes that even in complex litigation, the "no stone left unturned" approach is not always necessary. "Early identification and clarification of issues...is...essential to meaningful and fair discovery control." Manual at 55. Issue definition plus discovery sequencing are offered as the foundation for a cost-effective discovery plan. Cf. Standards, subsection (h). One of the principal objects of the preliminary conference is to identify the issues and "to suppress unnecessary and burdensome discovery procedures in the course of preparing for trial of those issues."

The Manual suggests techniques for tailoring a discovery plan ranging from simple scheduling orders to detailed judicial analysis and demarcation of the scope, quantity, sequencing and targeting of proposed discovery to compulsory disclosure of "core information." Techniques are proposed for expedited or streamlined resolution of discovery disputes by letter, conference call, special master, etc. Special protective or "umbrella" orders to preserve privileges or confidentiality are suggested to speed discovery production. Simplified and uniform document identification protocols, document preservation orders, the use of document depositories and computerized document imaging systems are discussed. (In Re Silicone Breast Implant Products Liability Litigation, MDL 926, for example, a CD containing 15,000 pages of documents deposited in the central document depository in Cincinnati could be purchased for $25). These proposed techniques are designed to facilitate prompt and efficient discovery while minimizing the need for "satellite litigation" regarding discovery issues.

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Waiver of Damages Provisions

Under these circumstances, does the waiver of damages provision in section 11.3.6 bar completely the owner/insurer's action, leaving the owner/insurer with no recourse whatsoever? Pursuant to numerous state and federal decisions elsewhere, and one very recent California decision, the answer most likely is "yes."

Moreover, the waiver may act as a defense where the owner's damages are covered by property insurance other than the insurance required by the contract and may also apply where the owner failed to purchase the insurance required by the contract that might have covered such damages. Further, the waiver may apply where the owner has not made any claim to its insurer or even where the insurer has rejected such a claim. Where applicable, the waiver of damages provision bars essentially all claims, including claims for strict liability, *Village of Rosemont v. Lenton Lumber Co.*, 494 N.E.2d 592, 601 (Ill. App. 1986), breach of warranty, *id.*, and negligence, *Ins. Co. of North America v. E.L. Nezolk, Inc.*, 480 So. 2d 1333, 1335 (Fla. App. 1985). The only claims not subject to the waiver are fraud claims. *See Steam Boat Development Co. v. Baugac Ind., Inc.*, 701 P.2d 127, 128 (Co. App. 1985).

Due to the broad and expanding scope that appellate courts in California and elsewhere are giving to the waiver of damages provision, counsel for general and subcontractors should consider the defense in any case where the owner's damages are or could be covered by any insurance purchased by or for the owner or by any policy that should have been purchased by the owner pursuant to the construction contract.

Lloyd's Underwriters. The first and only California appellate decision addressing the waiver of damages provision is *Lloyd's Underwriters, et al. v. Craig & Rush, Inc.*, 26 Cal. App. 4th 1194 (1994). *Lloyd's Underwriters* is especially significant because of its broad interpretation of the waiver. The owner had hired contractors to repair the roof on the owner's building. The construction contract signed by the parties contained the standard AIA provisions. Rather than purchase a separate policy, the owner relied on its existing insurance, which provided far broader coverage than required under 11.3.1. During the job, rain damaged the interior of the owner's building. The insurer paid for the damage and then brought a subrogation action against the contractors.

The Fourth District Court of Appeal affirmed summary judgment in favor of the contractors. *Id.* at 1201. The insurer had argued that the waiver provision should be narrowly construed and should not apply because the owner was only obligated under the contract to insure the contractors' work, whereas the damage for which the insurer paid was to other property of the owner's. The court rejected this narrow reading of the waiver:

The waived claims are not defined by what property is harmed (i.e., "any injury to the Work"); instead, the scope of waived claims is delimited by the source of any insurance proceeds paying for the loss.... The plain import of the emphasized language is that so long as a policy of insurance "applicable to the Work" pays for the damage, the waiver applies.

*Id.* at 1198 (emphasis in original).

Other Jurisdictions. State and federal courts elsewhere have broadly interpreted the waiver. In many decisions, as in *Lloyd's Underwriters*, the courts applied the waiver where the damages were paid out of any applicable insurance, even where the coverage was not required by the construction contract.

For example, in *State of Louisiana and Aetna Casualty & Surety Co. v. U.S.F & G. Co.*, 577 So.2d 1037 (La. App. 1991), the state's insurer — Aetna — had issued the state both a builder's risk policy (as required by the contract) and a fire insurance policy. After a fire allegedly resulting from the negligence of the general contractor damaged the project, Aetna paid the state's damages out of the fire insurance policy and brought a subrogation action against the contractor and others. The court applied the waiver and affirmed summary judgment against Aetna and the state. *Id.* at 1039. Aetna had stressed that the damages were paid under a separate fire policy and not under the builder's risk policy obtained pursuant to the AIA construction contract. The court observed, however, that "the waiver of claims in Article 11.3.6 is based upon the insurance required by 11.3.1 or any other applicable insurance..... [T]he contract does not limit coverage to one policy or the other." *Id.* at 1038-39 (emphasis in original).

In *Willis Realty v. Cimino Construction*, 623 A.2d 1287 (Me. 1993), the parties signed a contract for the construction of an addition to a building. The contractor's negligence caused the collapse of a wall on the existing building. The owner's damages were paid out of the owner's general business and property liability insurance policy. Unlike most of the other waiver cases, the property damage in *Willis Realty* was not concurrently caused by a flood, fire or other typically insured "peril." Still, the Maine Supreme Court held that the waiver provision "should be liberally construed," and barred the owner's subrogation claim. *Id.* at 1288-89 (emphasis in original).

Similarly, in *South Tippecanoe School Building Corporation v. Shambaugh & Son, Inc.*, 395 N.E.2d 320 (Ind. App. 1979), a gas explosion and fire damaged the project. The owner's builder's risk insurer paid for the loss and then brought a subrogation action against the general contractor and various subcontractors, claiming that their negligence had caused the explosion and fire.

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On CONSTRUCTION

THE American Arbitration Association (AAA) is making some significant changes to its handling of alternative dispute resolution (ADR) for construction matters. These changes are the work of the Construction Alternative Dispute Resolution Task Force, which is comprised of 55 members, including construction lawyers and representatives of various segments of the construction industry. The changes are scheduled to be adopted this spring.

The following changes are designed to speed the ADR process, give more authority to arbitrators, improve the AAA panels, and promote mediation, partnering, and the use of dispute review boards.

“Fast Track” Cases

The Task Force recommended the establishment of a “fast track” arbitration process for disputes involving less than $50,000. Significant features include:

1. Cases are to be completed promptly, with the hearing to take place within thirty days of the arbitrator’s appointment and the final award to be issued within sixty days. The time frame can be extended by agreement of the parties or by the arbitrator “in extraordinary cases when the demands of justice require it.”

2. To expedite these cases, the AAA will provide a list of arbitrators competent to handle fast track matters and available to serve on a shortened time table.

3. A mandatory preliminary hearing by telephone is to take place shortly after the appointment of an arbitrator in order to resolve procedural issues and schedule a prompt hearing.

4. Except in extraordinary circumstances, there is to be no discovery in these cases. However, parties are required to exchange copies of their exhibits at least two working days before the hearing.

5. Fast track cases generally are allotted a single hearing day, although the arbitrator may schedule an additional day for good cause. Cases involving amounts under $10,000 are to be resolved by submission of documents, unless an oral hearing is requested by one of the parties or by the arbitrator.

6. Unless the parties agree otherwise, the arbitrator is to render an award no later than seven days from the close of the hearing.

Although AAA arbitrators used to serve pro bono on the first day of arbitration, the new rules require that the arbitrator be compensated at a per case rate to be established by the AAA Regional Office. This change is intended to promote establishment of a high-quality arbitrator panel.

Regular Track Cases

These cases involve amounts in dispute ranging from $50,000 to $1 million and typically employ a single arbitrator.

1. To give the parties more input into arbitrator selection, the AAA encourages the parties to outline appropriate qualifications for arbitrators on new forms for the demand for arbitration and the answering statement.

2. Arbitrators have authority to conduct preliminary hearings as appropriate and to direct exchanges of documents and other information.

3. Under the new rules, arbitrators also have broad authority to control the proceedings, including the power to control the order of proof, bifurcate issues, exclude cumulative or irrelevant testimony or evidence, and direct the parties to focus the presentation of evidence on decisive issues with a view to expediting resolution of the dispute. Further, the arbitrator may entertain motions, including dispositive motions.

4. Arbitrators now have authority to deny requests for postponement, even those agreed to by the parties, if they are not for good cause.

5. Upon request of a party, arbitrators shall provide a written opinion. Further, arbitrators now have authority to correct technical errors in an award in order to avoid needless involvement by the court.

6. Arbitrators will be compensated from the first day of service.

Large, Complex Case

Program (LCCP)

The LCCP program was the subject of this column in the Fall 1994 issue. The LCCP rules are mandatory in cases involving claims of $1 million or more.

In addition:

1. The parties to LCCP cases are required to hold an early administrative conference with the AAA.

2. Three arbitrators, at least one of whom is to be an experienced construction lawyer, will serve on each case and will be compensated at their usual hourly rate.

3. A preliminary hearing is mandatory and may be conducted by phone.

4. LCCP arbitrators have broad authority to control discovery, including depositions.

Besides requiring payment of arbitrators for the first day of service, the Task Force made a number of additional suggestions for improving the quality of arbitrator panels. These suggestions include a requirement that an arbitrator have at least 10 years of experience, that attorney arbitrators devote at least half of their practice to construction matters, and that there be mandatory training for all new arbitrators and retraining every three years for all panelists.

Now that there are three “tracks” of cases for arbitration, lawyers may want to advise clients to use specific language in their contracts to provide, not just for the arbitration of disputes, but also for the use of the appropriate rules for disputes likely to arise. In addition, they may want to provide for mediation, partnering, or dispute review boards.

Ms. Claiborne is a partner in the firm of Bronson, Bronson & McKinnon and a member of the AAA’s Construction ADR Task Force.
Waiver of Damages Provisions

The Indiana Court of Appeal affirmed summary judgment in favor of the general contractor and subcontractors:

"The contract involved is subject but to this reasonable construction: It evinces an intent to place any risk of loss on the Work on insurance; the defendants are intended "insureds" under the builder's risk policy; and, the waiver provisions are fully applicable here."

Id. at 326.


The Waiver May Apply Even Where the Owner's Damages Are Not Covered by Insurance. Several courts have applied the waiver to bar an owner's claims even when the owner's damages were not "covered by insurance" because the owner either neglected to purchase insurance or did not purchase enough insurance to cover all its damages. For example, in Temple Eastex Inc. v. Old Orchard Creek Partners Ltd., 848 S.W.2d 724 (Tx. App. 1992), the owner and its insurer sued the general contractor, among others, to recover damages the owner sustained when a sub-subcontractor started a fire that destroyed the project. The owner had only purchased enough insurance to cover some of its damages. The Texas Court of Appeals held that, even though the owner's damages exceeded its insurance coverage, the owner still could not recover because it was obligated under the contract to acquire enough insurance to protect the full value of the work:

Old Orchard, therefore, in effect became the insurer and is liable for damages to the extent that an insurer carrier would have been liable had adequate insurance been obtained.

Id. at 731.

Similarly, in Village of Rosemont v. Lenten Lumber Company, 494 N.E.2d 592 (Ill.App. 1986), the City's insurer paid $1.5 million of $6.5 million in damages sustained when a roof collapsed. The City sued the general and various subcontractors and suppliers to recover the $5 million not covered by insurance. The Illinois Court of Appeal affirmed summary judgment in favor of the contractor, rejecting the City's contention that the waiver provision only applied to the extent of the insurance coverage.

"Id. at 600. The court held that the City's interpretation "renders the provisions illusory and could not be a rational allocation of risk to protect the party's interests, since [owner] would then totally control whether to buy insurance."


The Waiver Also Bars Subrogation Actions Brought Directly by the Insurer. If the owner's claims are barred under the waiver provision, the insurer cannot circumvent the waiver simply by suing in its own name. "Under settled principles, the insurer in its role as subrogee has no greater rights than those possessed by its insured, and its claims are subject to the same defenses." Liberty Mutual Ins. Co. v. Fales, 8 Cal. 3d 712, 717 (1973). Accordingly, the courts have uniformly held that subrogation actions brought by insurers whose insureds had waived their rights are similarly barred from pursuing a subrogation action against the contractor. See, e.g., Fire Ins. Exchange, supra, 868 P.2d at 953; Island Villa Development, supra, 334 S.E.2d at 42.

Does the Owner/Insurer Have Any Arguments to Rebut the Waiver? Owners and insurers have had some success in rebutting the waiver with one of two arguments: (1) that the waiver applies only during construction and not to claims arising after completion of construction; and (2) that the damaged property was not within the contractor's scope of work.

Many courts have stated in dicta that the waiver is intended to prevent only owner-contractor disputes "during construction":

"The cases reflect a clear intention between the parties to shift the risk of loss and any other damage during construction to an insurer in an effort to avoid disputes among the parties which might cause delays in the completion of the construction."

State of Louisiana, supra, 577 So.2d at 1039. Most of these policy pronouncements, though, came in cases where the court ultimately enforced the waiver. A few courts, however, have imposed a specific time limit on the waiver. In Automobile Insurance Company of Hartford, Connecticut v. United H.R.B. General Contractors, Inc., 876 S.W.2d 791 (Mo. App. 1994), the owner sued the contractor for damages from a fire five months after the contractor received its final payment. The Missouri Court of Appeal rejected the contractor's argument that "the waiver was intended to extend beyond the life of the contract," holding instead that the waiver terminated once the owner made its final payment to the contractor. Id. at 794; see also Fairchild v. W.O. Taylor Commercial Refrigeration & Elec. Co., 403 So.2d 1119, 1121 (Fla. App. 1981) (court refused to apply the waiver five years after completion); Blue Cross of South Western Va. v. McDevitt & Street Co., 360 S.E.2d 825, 826 (Va. Sup. Ct. 1987) (dicta that waiver would have applied up to final payment); Brodsky v. Prinum Const. Co., 354 A.2d 440, 443 (Md. App. 1976) (court enforced the waiver because there had been "no showing that the date of substantial completion had been reached...[or] that there had been an acceptance or partial acceptance").

The second line of attack with which owners and in-
Stephen Oroza

On CREDITORS’ RIGHTS

A Chapter 11 debtor-in-possession (“DIP”) acts as a trustee for its creditors and thus owes them fiduciary duties. Since few debtors regard themselves as fiduciaries of their creditors, counsel for the DIP plays a major role in insuring that the DIP actually discharges its responsibilities. Despite the practical importance of DIP’s counsel to the interests of creditors, DIP counsel often act as though they owe professional duties only to the DIP.

A significant body of authority, however, suggests that the counsel for the DIP owes duties not merely to the DIP, but to creditors of the estate. The cases in this area raise interesting and, for DIP counsel, troubling issues. Since one of the most important cases, In re Perez, 30 F.3d 1209 (9th Cir. 1994), was decided by the Ninth Circuit, California bankruptcy practitioners would do well to familiarize themselves with these issues.

In Perez, the debtor proposed a Chapter 11 plan which allowed the debtor to retain value while unsecured creditors received payment of their claims, without interest, over sixty-seven months. Confirmation of two prior plans had been denied because of their discriminatory treatment of the debtor’s principal creditor. The same creditors objected to the third plan on the ground that it did not satisfy the “cram down” provisions of Bankruptcy Code § 1129(b). These provisions require, among other things, that unsecured creditors be paid in full if the debtor is to retain anything of value under the plan. The bankruptcy court confirmed the third plan and the Bankruptcy Appellate Panel (“BAP”) affirmed. The Ninth Circuit reversed the BAP, holding that the failure of the plan to provide for the payment of interest to creditors resulted in their receipt of less than the full value of their claims.

After having decided the case, however, the Ninth Circuit went on to address the larger issues. It stated that “this case and others like it raise troubling doubts about the efficacy and fairness of our bankruptcy process.” The Court admonished counsel for the DIP that he must “keep firmly in mind that his client is the estate and not the debtor individually.” Consistent with this view, the opinion states that counsel for the DIP must resign if counsel “develops material doubts about whether a proposed course of action in fact serves the estate’s interests” and he or she is unable to dissuade the debtor from pursuing that course. “Under no circumstances, ... may the lawyer for a bankruptcy estate pursue a course of action, unless he has determined in good faith and as an exercise of his professional judgment that the course complies with the Bankruptcy Code and serves the best interests of the estate.”

A bankruptcy decision out of the Central District of California seems to go even further. In re Wild Horse, 136 B.R. 830 (C.D. Cal. 1991), holds that counsel for the DIP has an obligation, at least under some circumstances, to discover and disclose evidence of unethical conduct by the debtor. In Wild Horse, the debtor arranged for a sale of property of the estate to a business entity which was, unbeknownst to counsel for the DIP, controlled by the debtor’s principal.

The bankruptcy court severely criticized counsel for the DIP for having failed to discover the dishonest actions of her client despite the existence of “red flags” which should have alerted her to the situation. Relying in part upon Bankruptcy Rule 9011, the Court held that in preparing pleadings relating to the sale, counsel for the DIP was required to do more than accept the representations made by the client. Counsel was required independently to verify the accuracy of the material information. And, at least if the information discovered by the DIP’s attorney contradicts representations made in the pleadings, the lawyer must also report the debtor’s dishonesty to creditor representatives.

The Perez and Wild Horse decisions, and similar decisions from other jurisdictions, reach their conclusions by holding that the attorney for the DIP must represent the “estate.” The “estate,” however, is a body of assets against which numerous parties, including the debtor and various classes of creditors, assert adverse claims. If the estate is viewed as a collection of adverse interests, it is counter-intuitive to suggest that the same attorney can, much less must, represent them all.

For example, if a debtor in a single-asset real estate case proposes a plan based on aggressive assumptions about the future performance of the property, offering to pay unsecured claims with an apparently submarket rate of interest in a lump sum in five years and to leave the existing equity in place, is this plan “in the best interests of the estate” under the Ninth Circuit’s test? Where the plan aggressively (and arguably, unreasonably) shifts risk to creditors, can DIP counsel determine “in good faith and as an exercise of his professional judgment that the [plan] complies with the Bankruptcy Code and serves the best interests of the estate”? Must DIP counsel resign rather than propose the plan or must counsel make the DIP’s best case and allow the creditors to make theirs?

What if the DIP advises its attorney that it doubts that it can meet financial projections upon which the plan is based? Would counsel be able to claim that such communications were privileged or, to the contrary, would the attorney be required to tell his other client, the “estate,” the DIP’s actual views on this topic? In an adversary system, holding that DIP counsel “represents” the “estate” might be rather more glib than the courts recognize. On the other hand, as Perez demonstrates, the extreme practical significance of the DIP’s counsel as a guardian of the process makes such holdings tempting.

No matter how one ultimately analyzes these issues, after Perez, no bankruptcy practitioner, especially DIP counsel, can afford to ignore them.

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Waiver of Damages Provisions

The Manual for Complex Litigation

The special aspects of discovery of computerized data is covered, as are nonstenographic depositions, "deferred supplemental depositions," sequencing of depositions, control of abusive conduct, saving costs through a program of informal interviews, coordination with related litigation, etc. Interrogatory practice is also discussed. While the law underlying the discussion is Federal, some techniques are transferrable to state practice: development of master interrogatories, use of interrogatories from other litigation, staged or successive responses, etc.

Trial

The special trial issues more likely to arise in complex litigation form a significant portion of the Manual. The Manual discusses the need, for example, for early attention to expensive and elaborate demonstrative evidence such as computer simulations, noting "[i]t may be advisable to obtain at least a preliminary ruling or guidance concerning the admissibility of a proposed exhibit before substantial expense is incurred in its preparation (e.g., at the storyboard stage of a computer animation)." Manual at 123. The preparation of depositions for use at trial, especially videotaped depositions needing editing, is similarly discussed.

Various techniques are proposed for streamlining trial or reducing trial time. The use of test cases with a view toward possible collateral estoppel, or structuring the trial by consolidation, severance or bifurcation are treated. Various scheduling options are suggested -- the six-day week (expedites a lengthy trial), the four-and-a-half day week (one-half day for administration), the morning schedule (nine to noon, or eight to two, etc.)

To enhance jury recollection and comprehension in a lengthy or complex trial, various innovative techniques for sequencing evidence and arguments are suggested -- presenting evidence by issue category, perhaps followed by sequential verdicts; arranging closing arguments by issue; using interim opening statements or arguments; using interim jury instructions, glossaries, indexes, time lines, exhibit books and graphics.

To control costs (but also with the practical effect of expanding the court's subpoena power), the receipt of live testimony by remote video transmission is proposed (as used in In re San Juan Dupont Plaza Hotel Fire Litigation, MDL 721, and in In re Washington Public Power Supply System Litigation, MDL 551). For a sample protocol for remote video transmission testimony from the San Juan litigation, see 129 FRD at 427-30.

Other Resources

Heavily footnoted, the Manual cites to useful resources such as Judge Schwarzer's study of coordination of litigation between state and Federal courts in eleven complex cases: two groups of asbestos cases, three air crashes, two fires, two building collapses, an oil spill and an investment fraud case. William W.
A source of ongoing frustration among all segments of the patent prosecution and litigation bar and their clients is the continued uncertainty about what is a patentable invention and what is required to properly claim the invention in the biotechnology and biochemistry arenas. This uncertainty stems largely from three factors, all beyond the control of practitioners:

1. The development of the science is simply outstripping the development of the law, and will no doubt continue to do so for the foreseeable future:
2. The length of time from the original filing date of a patent application to issuance of a patent varies wildly, but can easily be eight to ten years or more;
3. The Federal Circuit, which has primary responsibility for defining what is patentable and explaining the application of its rules to new technologies, has been unwilling to start over and set clear guidelines when the accretion of statements in its opinions over the years becomes difficult to interpret.

This problem is particularly acute in biotechnology and biochemistry patents, where the science not only is rapidly changing but is often unsuited for the application of the Federal Circuit’s traditional rules governing conception and reduction to practice of an invention and whether an invention is obvious in light of prior art. The Federal Circuit has decided a string of cases over the last five years touching on the doctrines of conception, reduction to practice, and obviousness as applied to patent claims to genes, naturally occurring biological compounds, and man-made versions of such compounds. See, e.g., In re Dewel, 51 F. 3d 1552 (Fed. Cir. 1995); Burroughs-Wellcome v. Barr Laboratories, 40 F. 3d 1225 (Fed. Cir. 1994); Fiers v. Revel, 984 F. 2d 1164 (Fed. Cir. 1993); Amgen v. Chugai Pharmaceutical Co., 927 F. 2d 1200 (Fed. Cir.), cert. denied, 502 U.S. 856 (1991). Through these decisions, the Federal Circuit has created a whole new set of tests, which are often quite confusing, due to the Federal Circuit’s insistence that they are not in fact new or different.

A recent example of the Federal Circuit’s reluctance to clean up confusing precedent is In re Ochial, 71 F. 3d 1505 (Fed. Cir. 1995), decided in December of last year. Ochial was an appeal by the patent applicant from a rejection of his claims by the patent examiner and the Board of Patent Appeals and Interferences (“Board”) on obviousness grounds. Ochial’s original application (filed in 1975) claimed a process which used a new organic acid to make a new compound with antibiotic properties.

The examiner ultimately granted claims to the invention of the new acid and the new antibiotic, but denied the claims to the process. Ochial appealed this rejection, and in 1992 (seventeen years after Ochial filed his original application), the Board upheld the examiner. To grossly oversimplify the case, both the examiner and the Board found that because the process used to make the new antibiotic from the new acid was a standard one, this process was unpatentable per se.

The Federal Circuit took quite a different view of the case, holding that there could be no such thing as a per se rule governing obviousness rejections, even in a case involving the application of an admittedly standard process using a separately patented new starting material to make a separately patented new product.

Although at first glance Ochial looks like a pro-patent applicant decision, the last two pages of the decision make rather depressing reading. Both parties to the appeal argued that there was an irreconcilable conflict among the prior decisions of the Court, and urged the Court to resolve it. As the Solicitor General stated, the conflict “makes it very difficult for patent attorneys to give cogent advice to clients or for patent examiners to render consistent decisions on... patentability.” Ochial, 71 F. 3d at 1569 (emphasis added).

The Court explicitly rejected these pleas, refusing to admit that there were any conflicts or confusion in its prior decisions. Instead, the opinion suggests that the patent bar, the patent office, and the Board are simply stubbornly insisting on misinterpreting the case law for their own ends:

These disagreements...can, however, be transformed into perceived “irreconcilable conflicts” between legal rules only when, as occurred here, examiners, members of the Board, and patent lawyers purport to find competing per se rules in our precedents and argue for rejection or allowance of a particular claim accordingly.

Id. at 1572.

The Ochial opinion ends with a ringing exhortation to the PTO and the patent bar to stop clamoring for per se or brightline rules. I agree with the Federal Circuit’s rejection of a per se rule supporting obviousness rejections. But the Court’s disregard for the very real confusion in the patent bar and at the patent office is disheartening.

For practitioners who already often must wait ten or fifteen years (in Ochial’s case, almost twenty years) before finding out through a Federal Circuit decision whether an application describes a patentable invention, a few clearly stated principles would not come amiss.

Ms. Krevans is a partner in the firm of Morrison & Foerster.
Letter from the President

Whereas not too long ago (certainly in the early 70's when I started out), sanction motions were an exception employed only in the most egregious circumstances; they have, sadly, become almost commonplace.

In short, the heat generated in litigation has increased— with little impact on the merits, but significant negative consequences on our professional esteem, as well as our sense of fulfillment as lawyers. While no organization, including the ABTL, will be able to provide a cure-all, there are actions that our organization can implement.

I believe that an important step in that direction is to reinvigorate our commitment to the ABTL's "Guide to Professional Practice," which was first adopted in Northern California in the fall of 1994. In addition to promulgating certain guidelines of behavior that attempt to reconcile zealous advocacy with the elimination of needless acrimony, our Guidelines encourage the informal resolution of inter-firm disputes through the appointment of a firm contact person or ombudsman. At a recent joint meeting of the three ABTL Boards, the San Diego chapter announced that it was following our lead and adopting our guidelines. The Los Angeles chapter was encouraged to follow suit — not only by its sister chapters, but by a number of Los Angeles-based judge attendees. The point is that there will be a renewed effort, perhaps statewide, to give more meaning to our Guidelines and our informal method of dispute resolution.

On a less lofty level, we can also continue to provide a forum where practitioners and judges, plaintiffs' lawyers and defense lawyers, can meet in an informal setting to discuss and debate significant issues impacting our profession. In this vein, our two most recent programs were great successes. Judges Illston and Wilken, in our New Federal Judges Program, demonstrated the continued strength of our bench, and a program on the new securities reform legislation was, to say the least, both provocative and timely. On the horizon, we will experiment with a Peninsula-based program that will focus on the technology sector. Our Annual Seminar returns to the Four Seasons in Maui with a program entitled "Trying The Punitive Damages Case." Please reserve the dates: October 25-29, 1996.

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Five years ago, when a number of us met with representatives of the Los Angeles ABTL chapter to discuss the formation of a Northern California group, it was hard to envision that the ABTL would rapidly become the leading litigation group in all of California. With predecessor presidents in Northern California like Art Shartsis, Jerry Falk and Steve Bonse, perhaps it would have been impossible to do otherwise. It is a privilege to follow in their footsteps.

Mr. Schatz is a partner in the firm of Wilson, Sonsini, Goodrich & Rosati.

The Manual for Complex Litigation

Schwarzer, et al., Judicial Federalism in Action: Coordination of Litigation in State and Federal Courts, 78 VA. L. REV. 1689, 1700-06 (1992). Other citations are provided to most of those complex Federal cases litigated over the past 25 years that have developed or tested complex case management techniques.

In addition to numerous citations to sample orders available in the FRD or via an on-line service, the Manual provides 90 pages of forms of orders, notices, jury questionnaires, etc.

The Manual in the Fast Track

The Manual collects valuable ideas, citations and techniques that can be adapted for management of a complex case in the context of the fast track. Although complex litigation in state court is theoretically subject only to Section 19 of the Standards, the 568 pages of the Manual are a valuable supplement to the less than one page of the Standards. Nothing can substitute for ample judicial time, but proper adaptation of the techniques set forth in the Manual can help reduce any adverse impacts of the distractions and time constraints of fast track life.

The Honorable John Zebrowski is an Associate Justice of the California Court of Appeal, Second Appellate District.