ASSOCIATION OF BUSINESS TRIAL LAWYERS SAN DIEGO

abtl REPORT

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To Whistleblow or Not to Whistleblow: Privileges, Ethics, and Federal Preemption

by Heather Linn Rosing, Esq., Klinedinst, Fliehman & McKillop, P.C.

A typical, everyday office water cooler conversation between attorneys: *"So, Pam, I'm a little confused about what I should do. California B & P Code section 6068(e) says that I need to maintain the secrets of my clients, even to my own peril, but I've been hearing a lot about this new Sarbanes-Oxley Act and how it could affect the attorney-client privilege. Does it require me to rat out my own client? What's up?"*

Heather Linn Rosing

Pam, of course, has been pondering this exact issue for weeks, and is glad Joe has raised it. *"Yeah, Joe, I've heard about that too. I really don't know. But I scanned a well-written, down-to-earth article in the ABTL publication this month on the subject, and thought I would read it more carefully when I had a chance. You should do the same."*

So here it is. The article you've been waiting for. Or at least that Pam and Joe have been waiting for. What is going on? What rules do you really need to know?

The starting point for any whistleblower analysis is the attorney-client privilege. So let's go there to start…

(See "Whistleblow" on page 11)

VIEW FROM THE BENCH

An Interview with Hon. Margaret McKeown of the Ninth Circuit Court of Appeals

Judge Margaret McKeown was appointed to the United States Court of Appeal for the Ninth Circuit in 1998, following a 23-year career as a litigator. Her private practice focused on intellectual property, antitrust, securities, and constitutional law. She recently relocated her chambers from Seattle to San Diego. Here, she shares with the ABTL Report her thoughts on federal appellate practice and the state of the Ninth Circuit.

Hon. Margaret McKeown

Q: Can you explain the life cycle of a Ninth Circuit appeal, from close of briefing to disposition?

(See "McKeown" on page 6)

Inside

President's Column

by Hon. J. Richard Haden

How did a judge become president of ABTL? About seven years ago, I began attending ABTL Dinner Meetings because of the outstanding programs and because I really appreciated the ABTL Ethics, Civility and Professionalism Guidelines.

Hon. J. Richard Haden

These Guidelines, available on our website or in Department 72, are designed to "eliminate unnecessary conflict and to reduce the level of contentiousness and stress in the resolution of legal disputes." Among other things, the Guidelines offer a positive approach to the discovery process. As an Independent Calendar judge, that sounded pretty good to me. Last year, ABTL recirculated the Guidelines to member firms.

I also enjoyed ABTL Reports which always contain scholarly and informative articles. Our editor John Brooks and his Editorial Board would like to hear from you if you have an article in mind.

Before long, I was invited to participate in a panel, and to join the Board, which is always an outstanding group of litigators and jurists. I have truly enjoyed the past six years as a Board member and officer. Our San Diego Chapter consistently offers the finest Dinner Meeting programs available, as well as the popular all-day seminar every other year based on the best Statewide Annual Conference materials. Our Statewide Conference is another example of ABTL's excellent legal education efforts.

This year, our Program Chair Robin Wofford has another great lineup of Dinner Meetings planned. I hope you were able to attend the panel on Sarbanes-Oxley in January and Rusty Hardin speaking on defending Arthur Andersen iin March. On May 15, Supreme Court Justice Carlos Moreno will join us. In the fall, we will present Bob Bennett, a panel of Independent Calendar judges, and "John and Abagail Adams." Each of you can help ABTL by inviting a colleague to attend one of these great programs and – better yet – encourage someone to join.

We always have about 450 members, over 50 of whom are judges, and we are always looking for more. Dana Dunwoody and his Membership Committee would appreciate your help. The best recruiting is person to person, so it is really up to our members to ensure ABTL remains strong and continues to grow.

As we complete our Tenth Year Anniversary, our Board is working hard to make this another banner year. It is a real privilege to be a part of that team. We all look forward to seeing you at the next meeting. Δ

ABTL'S ALL STAR LINEUP FOR 2003

In accordance with past tradition, ABTL has another spectacular lineup of programs for the remainder of 2003. Be sure to mark your calendar and don't miss these "must see" programs and events.

May 15, 2003
Justice Carlos Moreno
"An Insider's View of the California Supreme Court"

September 8, 2003
Bob Bennett
Renowned trial lawyer

October 17 - 19, 2003
30th Annual Seminar
"Trying the Business Punitive Damage Case"
Tamaya Resort & Spa
Santa Ana Pueblo, New Mexico

October 28, 2003:
IC Judges Panel
Hear what's happening in their courtrooms and more!

November 1, 2003
Red Bourdreau/Broderick Award Dinner
Manchester Grand Hyatt
ABTL Co-sponsor

December 8, 2003
"An Evening With John and Abigail Adams"
Certain to be a historic night. Bring the family!

An Open Letter To David E. Perrine, Former Editor of The San Diego ABTL Report, Recently Passed Away

Dear David:

David, it was a delight working with you. The Association of Business Trial Lawyers' Report is an excellent, readable and informative repository of information of interest to business litigators, thanks to you.

This letter has been written by us, two of your former co-editors, following your ABTL Report guidelines. This letter has no citations, no footnotes and minimum passive language. This letter can be read while sipping the morning coffee (or as you often put it — in one sitting on the loo).

Although we have not followed the Chicago Style Manual (as you always required) we have used your editing guidelines, The Elements of Style, by Strunk & White. We recently thumbed through the many ABTL articles dated from 1995 until 2000, when you were Chief Editor when we assisted you in the arduous, intellectually stimulating and thankless task of editing. Those articles uniformly fulfilled your primary guideline for contributors: to provide information for business litigators — not scholarly pieces, not gossip and not lugubrious congratulatory pieces about some lawyer of the year recipient. Turgid was unacceptable — simple and straightforward was required.

We well remember those long nights of editing — bloodying articles with red ink. Those editing marathons were made a little easier by Jack Daniels, but not much.

It was amazing. Remember those erstwhile writers who were affronted to their core at our temerity — "How dare you edit My Article! I am an appellate specialist — who are you!" It was amazing that some of the most heavily edited articles found their way into another San Diego County lawyers' publication — unviolated by our edits.

Being an editor is a surefire way to lose a popularity contest. Remember those articles that were beyond resuscitation and our tiptoeing around trying to avoid insulting the writer — yet subtly rejecting the articles. Amazingly, some of those articles found another publisher.

We will always remember your oft-repeated quote from John Chancellor: "It is hard to write a simple declarative sentence."

Thank you,
Karin Vogel
Charles V. Berwanger

Forum Selection and the Attorney-Work-Product Privilege

by Chris Garber, Esq., Klinedinst, Fliehman & McKillop, P.C.

Forum shopping? Can't decide between state and federal court? You've thought about the different discovery rules. You've considered the summary judgment rules. Have you thought about work product issues?

Chris Garber

In many cases, differences between federal and state work product protections won't be your first priority. But in some cases — especially cases involving sensitive pre-litigation memoranda and the like — work product protections may mean the difference between getting in or keeping out critical evidence. Federal work product protections are broader than state protections in some respects, but narrower in others.

So, it's important to know the most critical distinctions between federal and state work product protections. Here they are.

No Lay Work Product in California

The first major difference is in whose work product is protected. FRCP 26(b)(3) protects from disclosure documents and things prepared "by or for another party or by or for that other party's representative (including the other party's attorney, consultant, surety, indemnitor, insurer, or agent)…" In short, the federal attorney work product doctrine protects not only the attorney's work product, but also the client's, the client's agents, and the attorney's agents. *United States v. Chevrontexaco Corp.* (N.D. Cal. 2002) 2002 U.S. Dist. LEXIS 24971.

In contrast, California's rule applies only to an *attorney's* work product. While *pro per* litigants can claim the privilege, it does not necessarily attach to the work of the client or its agents. "Whatever the extent of the concept of an *attorney's* work product may be, it is clear that, given the broadest possible definition, it is still the attorney's work, or that of his agents or employees, that is involved, and the attorney cannot, by retroactive adoption, convert the independent work of another, already performed, into his own." *Jasper Construction, Inc. v. Foothill Junior College Dist.* (1979) 91 Cal. App. 3d 1, 16.

The difference is best illustrated by example. Consider the following internal E-mail from a corporate client's CEO to its Marketing Director:

TO: Marketing Director
FROM: CEO
SUBJECT: POSSIBLE LAWSUIT

Have you seen that our best salesman has left to work for Competitor? I believe this violates his non-compete agreement. Please investigate the situation and get back to me. I would love to sue both of those guys - especially if we can obtain an injunction just before their busy season. Let's nail them.

Messages like this are sent all the time. While this one may not be damning to the plaintiff's case, it can still hurt. Able defense counsel will argue the e-mail proves the client is a bully and the lawsuit is frivolous and harassing. Disclosure of the e-mail would distract from the central theory of the case, embarrass the client's executives, and frustrate settlement efforts while cloaking both ex-employee and Competitor in the mantle of the victim. Disclosure of the e-mail would not help the plaintiff's case. So it would obviously benefit the corporation if it could withhold the document by claiming it was protected by the work product privilege.

Now imagine the client hires your firm to file suit in California against both Competitor and the ex-employee. If the defendants' attorneys in a California state court action craft a proper discovery request that covers this document the client is

(See "Forum Selection" on page 8)

Inevitable Disclosure Doctrine Rejected in California

by Kenneth M. Fitzgerald, Esq. and Jia Yn Chen, Esq. of Latham & Watkins

After years of uncertainty and confusion, California's appellate courts have finally written the obituary for the controversial and short-lived inevitable disclosure doctrine. The Fourth District Court of Appeal definitively answered the question whether California recognizes the inevitable disclosure doctrine under trade secret law. On September 12, 2002, in *Whyte v. Schlage Lock Company*, 101 Cal. App. 4th 1443 (2002), the court explicitly rejected the inevitable disclosure doctrine as contrary to California law and public policy favoring employee mobility. According to the court, the inevitable disclosure doctrine creates an after-the-fact covenant not to compete, which is unenforceable under California law.

The doctrine of inevitable disclosure allows a trade secret owner to obtain an injunction prohibiting a former employee from working for a competitor, even though no actual or threatened misappropriation of trade secrets is shown, if the former employee's new job will "inevitably" cause the employee to rely on knowledge of the former employer's trade secrets. See *Pepsico, Inc. v. Redmond*, 54 F.3d 1262 (7th Cir. 1995). When deciding whether to issue the injunction, courts applying the doctrine of inevitable disclosure consider the degree of similarity between the employee's former and current positions, the degree of competition between the former and current employers, the current employer's efforts to safeguard its trade secrets, and the former employee's "lack of forthrightness," both in his activities before accepting his job and in his testimony.

Until the *Schlage Lock* decision, it was unclear whether California courts would adopt the doctrine. In the past, our courts have been clear that, in general, non-compete agreements are not enforceable in California. Business and Professions Code Section 16600 generally prohibits covenants not to compete and California public policy strongly favors employee mobility, although this has been conditioned on the rights of employers to protect themselves from unfair competition. See, e.g., *Metro Traffic Control, Inc. v. Shadow Traffic Network*, 22 Cal. App. 4th 853, 860-61 (1994) ("Business and Professions Code section 16600 prohibits the enforcement of *Metro's* noncompete clause except as necessary to protect trade secrets."). In 1999, the Second District Court of Appeal adopted the inevitable disclosure doctrine in California in *Electro Optical Industries, Inc. v. White*, 76 Cal. App. 4th 653 (1999). However, a year later, the California Supreme Court depublished the *Electro Optical* decision, allowing the *Schlage Lock* court to examine the issue as a matter of first impression.

Kenneth M. Fitzgerald

The *Schlage Lock* case involved two "fierce" competitors, Schlage Lock and Kwikset, who both manufactured and sold locks and related products, and competed intensely for shelf space at "big box" retailers such as The Home Depot. J. Douglas Whyte worked as Schlage's vice-president of sales and was responsible for sales to such "big box" retailers. He had signed a confidentiality agreement with Schlage, but had not signed a covenant not to compete.

Jia Yn Chen

In February 2002, Whyte, on behalf of Schlage, participated in a line review with The Home Depot. During these periodic line reviews, Home Depot reviews its supplier's product lines to determine which products it will sell and which products to remove from its shelves. As a result of this line review and Schlage's recommendations, Home Depot removed Kwikset's brand of locks and expanded Schlage's

(See "Inevitable Disclosure" on page 10)

McKeown

Continued from page 1

A: There is currently about a 7-8 month period between close of briefing and hearing in civil cases. This is an improvement from what used to be about a one year backlog. An appeal is assigned randomly to a three-judge panel. Where the judges sit in any given month is unrelated to where they keep their chambers. There are monthly sittings in Pasadena, San Francisco, and Seattle; six hearings each year in Portland; two in Hawaii; one in Alaska; and occasional special sittings in other cities.

Hearing dates are announced to the lawyers about 4-5 weeks in advance. If a party seeks a continuance due to scheduling problems, it is best to make that request immediately. If the panel has already invested time in the appeal, a continuance is less likely. Continuances are somewhat harder to obtain than in state court because the three geographically-diverse judges sit together only during the assigned week.

The panel receives the briefs and other materials about 6-8 weeks in advance of the scheduled argument date. Following Rule 34 of the Federal Rules of Appellate Procedure, oral argument may be denied if all three judges agree that the appeal is frivolous, or the dispositive issues have already been authoritatively decided, or the facts and legal arguments are adequately presented in the briefs and the record such that oral argument would not aid the decision making.

One judge of the panel will take the lead in doing the record research, and that judge will almost always get the entire record from the district court. That judge will usually be the one who writes the opinion, unless he or she dissents, although writing assignments are the prerogative of the presiding

(See "McKeown" on page 7)

Continued from page 6

judge of the panel. The judges exchange research memos in advance of oral argument. Unlike some state appellate courts, however, the judges do not prepare a draft opinion ahead of argument, nor do the panel judges conference before the hearing week. Each panel hears about 25 to 35 cases together in a hearing week. On average, it takes about 2 months from oral argument to issuance of an opinion, although many unpublished dispositions are issued within a few weeks.

Q: What are the most significant or frequent errors you see committed by non-appellate specialist litigators who handle their own appeals?

A: There are some omissions we see frequently, but I couldn't say they are restricted to non-specialists. Failure to realize the absence of appellate jurisdiction is one of these errors. The court examines threshold issues like appellate jurisdiction, standing, justiciability, mootness and ripeness at the outset of every case, even where the parties do not raise those issues. Sometimes, the appellant is attempting to appeal from something that is not a final, appealable order. Other times, this court lacks jurisdiction because the case should be in the Federal Circuit. It is important for attorneys to examine these threshold issues at the outset.

Another mistake, even where the appellate lawyer is top-notch, is the failure of the trial lawyers to properly preserve issues for appeal. We see this often with jury instructions, evidentiary objections, and motions in limine. Either there is a failure to object or the record regarding the objection is unclear. Parties often fail to get clear cut rulings on motions in limine, especially when proceedings are held in chambers off the record. It is important for attorneys to make a clear record, on the record, of all significant proceedings.

Q: Can you explain the Ninth Circuit's pro bono program?

A: About 40 percent of our case load consists of pro se appeals. Our pro se unit consults with judges where it appears that a pro se appeal raises issues that need exploration and that would benefit by professional briefing. The pro bono program has been a great success in helping both the parties and the court reach a just result.

Interested attorneys can volunteer to be part of the *pro bono* panel, and there are some nice benefits that come with that. Volunteer attorneys are guaranteed oral argument. Also, the court will pay their costs and expenses, including travel expenses to oral argument. There is no obligation on these attorneys to take any particular case. The volunteer attorneys can decline any case that is offered to them. They can also ask for cases that raise issues of particular interest to them, such as immigration cases, civil rights cases, or anything else.

Q: As an institution, does the Ninth Circuit have a character or personality that distinguishes it from other courts?

A: The nature of the cases we handle is distinctive for a number of reasons. We are bounded by two international borders and a maritime border, which gives rise to many cases raising issues of international law, immigration, and admiralty. The circuit also includes the significant technology centers in San Diego, Seattle, and the Silicon Valley, from which we get many cases raising cutting edge legal issues. Also, the vast tracts of federal lands, the many Native American tribes, and the wealth of natural resources, all give rise to cases raising issues that are less common in other circuits.

I am uniformly impressed by the care my colleagues give to cases, and by the high degree of collegiality they maintain. It is a smart, hardworking bench that takes pleasure in intellectual discourse.

Q: What do you consider to be the greatest challenges facing the Ninth Circuit presently?

A: Perhaps the biggest challenge is keeping up with the large increase in case load. When I joined the court in 1998, we received 8,000 appeals each year. The number is now 12,000. Overall, filings increased 20% last year. A large part of this increase comes from the recent increase in appeals from the Board of Immigration Appeals, such as asylum and related immigration appeals. These appeals have more that tripled in the past year, from 1,000 per year to 3,600 per year.

As appellate judges, we are writing for more than the single case in front of us. Due to the small number of cases accepted by the Supreme Court, we are the court of last resort for most litigants. Lawyers play an important role in assisting the court in reaching reasoned decisions, both by highlighting the important parts of the record, and by helping the court explore different ways of looking at and

(See "McKeown" on page 8)

McKeown

Continued from page 7

analyzing the issues.

Q: What do you consider the Ninth Circuit's greatest accomplishments of recent years?

A: Our mediation program has been a great success and has earned the compliments of many lawyers. This program has played a large role in helping us to reduce our backlog, despite the increase in the number of appeals. Another accomplishment is our improved use of technology to track related issues in different cases. That effort has helped us to put similar cases in front of the same panel, which improves the decision-making process. I also think our circuit has done a remarkable job in fostering collegiality in a very large, geographically diverse court. Δ

Forum Selection

Continued from page 4

bound to produce the above e-mail — assuming no other grounds for objections. Under California law, it falls outside the work product protection because it was drafted by neither an attorney nor an attorney's agent.

In a proceeding filed in the Southern District of California, in contrast, the federal work product rule protects the e-mail from disclosure, absent a showing by the defendants of "substantial need" for the document, and the inability to obtain the same information "without undue hardship." *Hickman v. Taylor* (1947) 329 U.S. 495, 511. This showing likely cannot be made for the e-mail, which at best relates to a tangential issue.

(See "Forum Selection" on page 9)

Continued from page 8

Federal Work Product Protection May Cover Only Documents Prepared Specifically for Litigation

A second key difference between state and federal work product protection is the treatment of attorney work performed *without* litigation in mind. California law protects any work performed by an attorney, whether litigation was contemplated or not. Without qualification, California's laws provide absolute protection for "any writing that reflects an attorney's impressions, conclusions, opinions, or legal research or theories." C.C.P. § 2018 (c).

On the other hand, the federal law protects only those documents that were "prepared in anticipation of litigation." FRCP 26(b)(3). The language is open to interpretation, however, and there is currently a split among the circuits. Some circuits interpret the rule's language broadly, protecting documents prepared "because of" litigation, even if the document was created for both business planning purposes and for reasonably anticipated litigation. The standard was most recently articulated in *U.S. v. Adlman* (2nd Cir. 1998) 134 F.3d 1194.

The second view, held by an equal number of circuits, is much more narrow. That view holds that documents are only protected if the "primary motivating purpose" behind the documents' creation was to assist in pending or anticipated litigation. *U.S. v. Davis* (5th Cir. 1981) 636 F.2d 1028, 1040. District Courts in the Ninth Circuit have traditionally followed the second view. *U.S. v. Bell* (N.D. Cal. 1994) 1994 U.S. Dist. LEXIS 17408, *74.

However, the U.S. District Court for the Northern District of California recently changed course, adopting the *Adlman* "but for" test. *United States v. Chevrontexaco Corp.* (N.D. Cal. 2002) 2002 U.S. Dist. LEXIS 24971 at *40. That court explained that *Adlman* "better serves the purposes driving the work product doctrine" and encourages parties to make "every effort to structure their deals in unobjectionable ways (to the extent possible)." *Id.*

To illustrate the federal rule, imagine the corporate client discussed above now contemplates a merger with another large corporation. Because of the size of the deal, tax consequences are a major concern. The corporate client believes it is a virtual certainty that the IRS will challenge the tax treatment of the transaction. Accordingly, it retains tax attorneys to advise on the best way to structure the deal, and how to avoid IRS objections. Using the tax attorneys' advice, the client completes the merger. But, despite the client's careful planning, the IRS challenges the tax treatment of the deal. And in the ensuing litigation, the IRS makes a discovery request for all memoranda prepared by the tax attorneys.

A court applying the *Adlman* standard would protect against disclosure documents reflecting "discussions about alternative ways to structure the transaction where those alternatives reflect thinking about the IRS' expected reaction to and treatment of the deal." *Chevrontexaco* at *46. "In contrast, documents that reflect only the logistics or mechanics of implementing business concepts" would necessarily be prepared in the "ordinary course of business," and would therefore *not* be protected. *Id.* at 47. The tax attorneys' memoranda likely fall in the former category (even if they were not communicated to the client), and would be protected from disclosure under federal law.

Under California law, the attorneys' memoranda to the client are likely subject to the absolute protections from discovery accorded by section 2018. The memoranda reflect the tax attorneys' "impressions, conclusions, opinions, and legal research or theories" and as such, "shall not be discoverable under any circumstances." Cal. Code Civ. Proc. § 2018, subd. (c).

There are many other differences between the state and federal work product doctrines. There are also further nuances to the distinctions discussed here. Litigators must keep the differences and nuances in mind. Failure to appreciate the federal law's protection of client-authored documents, or the state law's broad protection of documents not prepared "in anticipation of" litigation, may lead to a disclosure of harmful or embarrassing documents that might be avoided by a carefully selected forum. Δ

Continued from page 5

presence on its shelves. Kwikset's president was so impressed by Whyte's sales abilities, that he decided to offer him a job, asking him "what it would take to get him to leave" Schlage. Kwikset was able to provide it, because he accepted a position with Kwikset in June 2000. However, Whyte continued working for Schlage for two more weeks and did not notify Schlage of his intent to leave the company. During that two week period Whyte also continued to participate on behalf of Schlage in confidential meetings with Home Depot. When Whyte informed Schlage of his departure, the parting was not amicable. Schlage contended that Whyte disavowed a confidentiality agreement, stole trade secrets and lied about returning company information. Whyte denied these accusations and claimed that, in his exit interview, the president of Schlage vowed to destroy his career. Whyte's new position at Kwikset was substantially similar to his former position at Schlage. His duties included handling the lock products accounts for The Home Depot and other "big box" retailers.

Schlage sued Whyte in Colorado, but was denied an injunction. Whyte then filed suit in California for interference with contract and declaratory relief. Schlage filed a cross-complaint and was also granted a temporary restraining order enjoining Whyte from using or disclosing 20 categories of trade secret information and ordering him to return any such information in his possession. In response, Whyte turned over a garbage bag full of shredded documents and a zip lock bag full of destroyed computer discs. After discovery and a hearing, the Orange County Superior Court (Brenner, J.) denied Schlage's application for a preliminary injunction, finding that the information Schlage sought to protect were not trade secrets. Schlage appealed the decision.

After addressing several preliminary issues, the court turned to the question of whether inevitable disclosure is viable law in California. The court recognized that the facts in this case were "strikingly similar" to that of the leading case on the inevitable disclosure doctrine, *Pepsico, Inc. v. Redmond*, 54 Fed. 3d. 1262 (7th Cir. 1995), but that no published California decision had accepted or rejected the doctrine. Two federal district courts in California had concluded that the inevitable disclosure doctrine was not the law of California, but since these federal decisions do not establish the law of the state, nor bind its courts, the court independently considered the doctrine. The court examined decisions from other states that both accepted and rejected the inevitable disclosure doctrine. While acknowledging that the majority of jurisdictions have adopted some form of the inevitable disclosure doctrine, the court observed that "a small but growing band of cases rejects the inevitable disclosure doctrine," and found that "[t]he decisions rejecting the inevitable disclosure doctrine correctly balance competing public policies of employee mobility and protection of trade secrets." "The inevitable disclosure doctrine permits an employer to enjoin the former employee without proof of the employee's actual or threatened use of trade secrets based upon an inference (based in turn upon circumstantial evidence) that the employee inevitably will use his or her knowledge of those trade secrets in the new employment. The result is not merely an injunction against the use of trade secrets, but an injunction restricting employment."

Such an injunction restricting employment violates Business and Professions Code section 16600 which generally prohibits covenants not to compete. In addition, the doctrine "creates a de facto covenant not to compete" and "run[s] counter to the strong public policy in California favoring employee mobility." The court noted that the main problem with this covenant not to compete imposed by the inevitable disclosure doctrine is its after-the-fact nature: "The covenant is imposed after the employment contract is made and therefore alters the employment relationship without the employee's consent." The court recognized that in a situation such as with Whyte, where there was a confidentiality agreement, the inevitable disclosure doctrine would effectively convert the confidentiality agreement into a covenant not to compete. The court borrowed a statement from a federal court decision, stating, "a court should not allow a plaintiff to use inevitable disclosure as an after-the-fact noncompete agreement to enjoin an employee from working for the employer of his or her choice." The doctrine would rewrite employment agreements and these retroactive alterations would "distort the terms of the employment relationship and upset the balance

(See "Inevitable Disclosure" on page 11)

Inevitable Disclosure

Continued from page 10

which courts have attempted to achieve in constructing non-compete agreements." The result would be that the employer would obtain the benefit of a contractual provision it did not pay for, while the employee would be bound by a court imposed contract provision with no opportunity to negotiate terms or consideration.

The court's obituary for the doctrine is clear: "Lest there be any doubt about our holding, our rejection of the inevitable disclosure doctrine is complete." *Schlage Lock*, 101 Cal. App. 4th at 1463. Nevertheless, the court acknowledged the validity of carefully tailored anti-solicitation agreements with employees, which may be enforced to prevent the actual use of trade secrets such as customer lists. Thus, Business and Professions Code section 16600 "generally does not invalidate a noncompetition agreement that merely prohibits solicitation of the former employer's customers." Id. at 1462. The court further stated that an employer could "prevent disclosure of trade secrets through, for example, an agreed-upon and reasonable nonsolicitation clause that is narrowly tailored for the purpose of protecting trade secrets."

Corporate counsel would be well-advised to eschew broad non-compete agreements, and supplement non-disclosure agreements with non-solicitation agreements that specifically proscribe the solicitation of customers whose identities and purchasing preferences are truly trade secrets. Litigation counsel confronted with rogue ex-employees working for clients' competitors should abandon any hope of obtaining an injunction prohibiting the continued employment of an ex-employee by the client's competitor in the absence of evidence of actual misappropriation. Instead, effort should be focused on obtaining expedited discovery to uncover the actual misappropriation and use of trade secrets. No longer will California courts indulge the argument that an ex-employee's use of such trade secrets is inevitable, no matter how likely it would seem. Δ

Whistleblow

Continued from page 1

The Attorney-Client Privilege

The privilege varies from state to state. In California, as Joe noted, it is very strong, with few exceptions. If your client is using your services to commit a fraud, or has threatened to seriously physically harm a third party, you might be able to violate the statutory mandate for confidentiality, but that's about it.

However, in states like New Jersey, the privilege is much weaker. New Jersey says that a lawyer **must** report his client to the authorities to stop the client from "committing a criminal, illegal or fraudulent act that the lawyer reasonably believes is likely to result in death or substantial bodily harm, or substantial injury to the financial interest or property of another."

The ABA Model Rule 1.6 currently says that an attorney cannot disclose information relating to the representation of a client unless the client gives informed consent, but the attorney may reveal information to prevent reasonably certain death or substantial bodily harm. In 1997, the ABA's Ethics 2000 Commission recommended that Model Rule 1.6 be changed to allow attorneys to reveal confidences to prevent crimes and frauds of a financial nature on third parties, but the change did not pass. There has been recent discussion in ABA circles about revisiting the proposed amendments to Model Rule 1.6 and weakening the privilege in favor of protecting the public from fraudulent clients.

The Privilege and Corporations or Other Entities

The next question leading up to the ultimate answer (keep on reading!) is how the privilege applies to non-human being clients. Let's say you represent Amco, Inc. What rules govern in that situation? Can you talk to anyone employed by Amco without fear of breaching the privilege? Can you rat out an officer to the board of directors?

In California, the governing language is found in Rule of Professional Conduct 3-600. First, it says that you should make it clear in your own mind that Amco is your client, and understand that it acts "through its highest authorized officer, employee, body, or constituent overseeing the particular engagement."

(See "Whistleblow" on page 12)

Whistleblow

Continued from page 11

The rule goes on to say that if the attorney knows that the Amco corporate agent or employee is doing (or not doing) something that is "a violation of law reasonably imputable to the organization, or in a manner which is likely to result in substantial injury to the organization," the attorney **still** cannot breach the privilege and reveal the confidential information.

The attorney has the option of urging that particular lawbreaker to reconsider, and/or to report the problem to the next highest "internal authority," all the way to the highest "internal authority." But that's it. After that, if the entity refuses to rectify the situation, the attorney probably should just withdraw, the rule suggests. Of course, this is a little more difficult to do if you are in-house counsel, but the rule does apply to all attorneys across the board, without distinction as to in-house counsel and outside counsel.

The Sarbanes-Oxley Twist

There was Enron, WorldCom, Tyco, Adelphia, Xerox, Rite Aid – the list goes on. These corporate scandals and others rocked our country, and resulted in a wave of both federal and state legislation– including the Sarbanes-Oxley Act – to impose accountability on Corporate America.

The most relevant part of the Act for attorneys is Section 307. Section 307 directed the SEC to devise specifics "requiring an attorney to report evidence of a material violation of securities law or breach of fiduciary duty or similar violation by the company or any agent thereof, to the chief legal counsel or the chief executive officer of the company... and if the counsel or officer does not appropriately respond to the evidence..., requiring the attorney to report the evidence to the audit committee of the board of directors of the issuer or to another committee of the board of directors comprised solely of directors not employed directly or indirectly by the issuer, or to the board of directors."

What does this mean? No one knew exactly what to think of it back in July 2002.

But then the SEC told us. In late 2002, the SEC proposed rules requiring an outside counsel who "reasonably believes" that a material violation of securities law or breach of fiduciary duty has occurred, is occurring, or is about to occur, to report that to the chief legal officer first, and, if necessary, report the violation "up the ladder" to the audit committee. This appeared to have been contemplated by 307, and thus was something the SEC actually had the statutory authority to turn into law.

But the SEC didn't stop with the "up the ladder" reporting. They wanted the lawyer to go up and over the ladder, and basically turn the client into the SEC if the violation was not remedied. These so-called "noisy withdrawal" provisions of the SEC rules required outside counsel to withdraw from representation under certain circumstances, write the SEC a letter saying that they are withdrawing for professional considerations, and disaffirm submissions to the SEC which the attorney believes are tainted by a material violation of securities law. As an alternative, the publicly-traded company could set up a qualified legal compliance committee (QLCC), and the attorney's reporting requirements would end once the material violation was reported to the QLCC. In that case, no "noisy withdrawal" would be required.

The proposed rules were intended to apply to lawyers very broadly. The SEC stated that "the proposed rule would adopt an expansive view of who is an attorney subject to the rule, covering all attorneys who are admitted to practice law whether employed in-house by an issuer or retained to perform legal work on behalf of an issuer." It would apply not only to lawyers dealing directly with the SEC, but lawyers who advise on SEC-related subjects, lawyers who are retained to do investigations into violations of securities law, and lawyers who supervise other lawyers who fall into one of the categories. Punishment for violation of the rules could include injunctions, cease and desist orders, and civil monetary penalties.

Shockwaves hit the legal community. "But this conflicts with the ethical rules in my state!" attorneys exclaimed. Not to worry, said the SEC, for your state rules are explicitly preempted by our new federal rules, except to the extent your state rules are stronger or require even more in the way of whistleblowing.

There were "scare headlines" everywhere. Attorneys representing publicly traded companies panicked. One hundred and seventy law firms, insurers, law professors, and other interested par-

(See "Whistleblow" on page 13)

Continued from page 12

ties quickly drafted and filed comment letters with the SEC.

The SEC listened, at least a little. On January 23, 2003, the SEC extended the comment period on the "noisy withdrawal" provisions, and withdrew proposed rules making it mandatory for the attorney to document events related to the material violation. The SEC also announced that there would be an opportunity to comment on an alternative proposal.

Under the alternative to "noisy withdrawal," it is the company itself – not the attorney – that is required to report to the SEC if the company doesn't satisfy the attorney's concerns. Specifically, an issuer whose attorney has quit would be required file certain forms that have the practical effect disclosing the attorney's withdrawal and/or that fact that the attorney did not receive an appropriate response to a report of a material violation. The SEC also indicated it would solicit other alternatives from other parties. Those "in the know" believe that the SEC will ultimately end up confirming this proposed alternative.

It is still unclear, however, if the SEC's alternative proposal will impose any duty on the attorney to withdraw (even "silently") from the representation, if the company does not respond to the attorney's concerns.

Sarbanes-Oxley and Withdrawal Issues

Can an attorney really remain as counsel for a company that he knows broke or is breaking the law? Under California law (Rule 3-700), an attorney is only **required** to withdraw in very limited circumstances, including where the continued employment will cause the attorney to violate his ethical duties or the State Bar Act. This has been interpreted as meaning that the attorney must withdraw if the client is using the attorney's services in furtherance of a fraud. But what if your client is not using your services to perpetrate the fraud, but is perpetrating a fraud despite your advice to the contrary? Or what if you discover a fraudulent plan by your client that is unrelated to the scope of your representation (for example, you a labor lawyer that "stumbles across" a securities fraud scheme)? As far as 3-700 goes, the plain language of the rule says that a California attorney has no affirmative obligation to withdraw if the client is doing something illegal. Withdrawal is permissive, but not mandatory. It remains to be seen whether the SEC will create a duty of withdrawal broader than that which already exists in California.

Sarbanes-Oxley and Discretionary Whistleblowing

There is at least one area, however, where the SEC has created a direct conflict with California ethical rules. The SEC implemented part 205.3(d)(2) in the final version of the rules. 205.3(d)(2) permits – but does not require – an attorney appearing and practicing before the SEC to reveal to the SEC, without the issuer's consent, confidential information related to the representation, to the extent the attorney reasonably believes necessary: (a) to prevent the issuer from committing a material violation that is likely to cause substantial injury to the financial interest or property of the issuer or investors; (b) to prevent the issuer, in a SEC investigation or administrative proceeding, from suborning or committing perjury, or committing an act that is likely to perpetrate a fraud upon the Commission; or (c) to rectify the consequences of a material violation by the issuer that caused, or may cause, substantial injury to the financial interest or property of the issuer or investors.

This SEC rule permitting disclosure of attorney-client privileges plainly conflicts with present California law, which requires attorneys to maintain their clients' confidences at every peril to themselves.

The "Answer"

"Well, Pam, I read that superb article you mentioned, and it seems like I have more to worry about if I represent an issuer of securities. If I just represent a privately held company, all I need to worry about in California is Rule of Professional Conduct 3-600. And it looks like the SEC is going to cut those attorneys for those big public companies a break anyway. And everyone knows that mandatory withdrawal is a joke."

Pam took a sip of her coffee and replied, *"Actually, Joe, I read a bit more into the article than you. Seems like we need to expect the winds of change. California has the strongest privilege right now, but there has been a lot of discussion at the federal level*

(See "Whistleblow" on page 14)

San Diego Inn of Court College of Trial Advocacy 2003 Workshop on Evidence

The San Diego Inn of Court, a non-profit organization established in 1978 by the Honorable Louis M. Welsh and dedicated to the practical training and education of trial attorneys, provides a unique opportunity for young lawyers to practice what they learn in class at courtroom sessions presided over by distinguished judges and experienced attorneys. No other program combines outstanding lectures-demonstrations with the unique "learn by actual practice at the courthouse" approach. Enrollees will earn 10 MCLE credits for $150.00 if enrolled before May 1, 2003.

This Workshop consists of two evening lecture sessions presented by Judge Robert J. Trentacosta at Cal. Western School of Law and two evening workshop sessions at the courthouse. Enrollees conduct direct and cross-examinations, practice introducing exhibits, and learn to make appropriate objections.

Lectures May 13 & May 15
5:30 p.m.-7:30 p.m.
Workshops May 20 & May 22
5:30 p.m. - 8:30 p.m.
For more information, please call
Norma Swan @ (619) 922-7171

Whistleblow

Continued from page 13

and the ABA level about changing the standard. Can California hold out and keep 6068(e) "as is" forever? Will the public demand a change? Will we as attorneys be forced to withdraw from more engagements in the future if we learn our clients are engaged in wrongdoing, even if we don't have to rat them out? So much remains to be seen."

And Pam is correct. This is the beginning of something. How it will end up, no one knows. So know the rules as they are today, and keep an eye out for changes. Be careful if you are practicing in other jurisdictions, even on a *pro hac vice* basis, since the attorney-client privilege and accompanying whistleblower rules currently differ from state to state.

The SEC Final Rules can be viewed online at http://www.sec.gov/rules/final/33-8185.htm. Δ

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P.O. Box 16946, San Diego, CA 92176-6946

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