Los Angeles lawyer Diane Kimberlin explores the controversy over class actions in wage and hour disputes

Class Struggles

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Looking back at one’s past writings and thinking ahead about new ones risks embarrassment in both directions. But now that I am writing From the Chair columns for a second year, I decided to review my columns from my year as the 2001-02 chair. Last year I shared my thoughts with our readers about the defining event of September 11 and the earthquake of failures in the business world. Both events continue to affect all of us, as concerned and active citizens and as practicing lawyers.

When we hear sirens as we are driving and pull over to the side, watching the fire engines racing past, we behold American flags dancing in the air off the backs of the trucks. At those moments we recall past tragedy even as our minds conjure up thoughts of the next horrific event. We then silently ask ourselves if there is anything we can do. As I asked in October 2001, “What are our individual jobs in this new war?”

Last November I wondered, “With whom are we at war?” Now, although our country is at war, we can ask if we as individual citizens are acting as if we are truly in a state of war. My feeling is that most Americans feel more as if we are in a state of watching, worrying, and waiting for the next sickening day of tragedy.

For many of us it is difficult to see the effect of the war. Most of us have never been asked to do anything except to carry on as usual. The administration repeatedly proclaims that we are now engaged in the first war of the twenty-first century, with the implication that this new type of war against terror, terrorism, and terrorists is so different that acting vaguely vigilant, trusting in the professionals, and waiting in longer lines at airports is all that needs to be done. But credibility, trust, and support for the government will vanish quickly after the next tragic event unless the public is more invested in the prosecution of this new type of war. To borrow an old phrase from the Reagan administration, what is needed is some form of constructive engagement.

The Congress of the United States should enact a formal declaration of war. This will better prepare us all for the future inevitable strikes against our country that the government has assured us will occur. Of course enacting a declaration of war raises the “against whom” question. Answering that question will help us all understand unequivocally what we face and may help us figure out what we can do. The process would let lawyers who draft resolutions regarding the war use their skills to clarify the nature of this war for all of us. Quite carefully, we must consider if we are at war with a concept—terrorism—or with actual terrorists. Also, we must address how we can identify terrorists before they identify themselves to us through their actions. How much easier it is when another nation is the enemy. Declaring war on Iraq will be conceptually easy compared to defining our terrorist enemies in the first war of the twenty-first century.

I wrote last February about al Qaeda’s arrogance of audacity and the possibility of the United States’ arrogance of optimism. Since then, there is little obvious optimism, but a quick victory over Iraq may lead to an arrogance of achievement as the country again wins a battle.

Last April, I wrote about the Olympian corporate failures and the possibility that the legal profession would suffer collectively as attention shifted from the accountants to the lawyers involved in the scandals. The corporate executives are facing the spotlight first, and with a few tacky “perp walks” have again kept the focus off the legal profession. The most recent financial shenanigans were a bit too much for me to have imagined. Accounting profession scandals now seem lessened when contrasted with the scandals of corporate governance. Reform has arrived with a gigantic new federal law, the Sarbanes-Oxley Act of 2002, amid promises of renewed enforcement action and more eager scrutiny of the financial world by the press. As for the tarnishing of the legal profession, we will see.
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Making Preparations for Expert Witnesses

The outcome of litigation often depends on expert testimony and how it is handled

Since the introduction of the Discovery Act in 1957, an entire complex statute—namely, California Code of Civil Procedure Section 2034—has been devoted solely to expert discovery and testimony. The complexity of this statute may be appreciated by comparing it, for example, to Code of Civil Procedure Section 2025, which deals with percipient witnesses. The requirements for percipient witnesses are far less detailed than those for experts described in Section 2034(f)(2). Clearly, the importance of experts in litigation cannot be overemphasized, and the ability of counsel to understand the expert’s expected testimony is an essential part of trial preparation.

Courts have persistently stressed that litigation is not a game and that it is in the public interest that each party know as much as possible about the other’s case in order to give each a fair turn at trial and maximize the chance of settlement. Nevertheless, litigation remains adversarial, and the deposition of an opposing expert—which is usually quite expensive—is the only way for a party to know what that expert will opine at trial. As a result, it is essential for the attorney who is deposing the expert to consider several factors: the strengths and weaknesses of both sides of the case; the technical aspects of what the expert will cover; the points to cover on cross-examination at trial; the issues that the client’s expert will cover to rebut or impeach; and the proper settlement position—which may depend in great part upon the testimony of the experts for both sides.

The great influence that expert testimony can have on litigation planning, litigation itself, and settlement is implicit in Section 2034(f). The first part of this section details the need for and content of the expert witness declaration, in which the nature of the expected testimony of the expert must be described. The second part concerns the deposition of the expert, during which the expert must state all the opinions he or she is expected to give at trial. Section 2034(f)(2)(D) further specifies that the expert witness declaration include a representation that the expert will be sufficiently familiar with the pending action to submit to a meaningful oral deposition concerning the specific testimony, including any opinion and its basis that the expert is expected to give at trial.

Surprises in Court

If the expert attempts to offer a new opinion at trial, the only effective remedy for the surprised party is to ask the court to exclude those opinions that the expert did not disclose in deposition. This penalty is prescribed by the statute, and it is the only one that will accomplish justice. The party calling the expert can avoid this sanction by making sure that the expert discloses all opinions he or she may give at trial. Although an attorney typically does not like to disclose any part of the case to the other side, the courts and the legislature have made it clear that pretrial disclosure of all the opinions that the expert intends to offer is required. Failure to do so will likely jeopardize the client’s case.

With this in mind, counsel should keep certain pretrial and posttrial requirements and recommendations in mind when preparing, and preparing for, expert witnesses. First, a party’s demand for exchange of expert information must be served 10 days after the initial trial date has been set or 70 days before that trial date, whichever is closer to the trial date. Second, the parties must simultaneously serve their respective expert information 50 days before the initial trial date or 20 days after receipt of a party’s demand, whichever is later. A party may supplement its expert designation 20 days after the two sides have exchanged expert information. A party should properly prepare the expert witness declaration to include the subject areas that the expert intends to cover at trial. The declaration should be broad enough to cover all opinions that the expert may express.

Third, a party should notice the opposing expert’s deposition at least 15 days before the initial trial date. In the notice, the party should make a demand for the production of documents at the deposition. This demand should at least request the following: 1) the expert’s credentials—typically, the expert’s curriculum vitae; 2) the expert’s complete file regarding the action; 3) all documents relating to any written or oral communications between the expert and any party to the action; 4) all documents relating to the expert’s compensation regarding the action; 5) all deposition transcripts, trial transcripts, declarations, or record of testimony by the expert in any other similar matter, including but not limited to a list of the cases in which the expert testified; 6) all books, treatises, articles, essays, or other documents written by the expert regarding the subject matter of the action; and 7) all documents evidencing how much time the expert expended on the matter.

At the Deposition

At the opposing expert’s deposition, counsel should mark the expert’s curriculum vitae and witness declaration as exhibits to the expert’s deposition. Additionally, counsel should take the time to read into the record the section in the declaration regarding the subject areas of the testimony that the expert is expected to offer. This is done by carefully paraphrasing the statements in this
section. Ask the expert for his or her assignment in the matter and for all the written and oral communications regarding this assignment. Ask the expert if he or she has testified to everything regarding that subject. Also ensure that the expert will notify opposing counsel if he or she arrives at any new opinions before trial. Finally, ask the expert how much he or she has been paid and what if any future work the expert intends to perform on the matter.

The deadline for expert discovery motions is 10 days before the initial trial date. Specifically, pursuant to Section 2034(j), on objection of any party who complies with Section 2034(f), the court shall exclude from evidence the expert opinion of a witness who is offered by a party who has unreasonably failed to make the expert available for deposition. The court also has the power to impose monetary, terminating, and evidentiary sanctions against the party and the party’s counsel who has unreasonably failed to make the expert available to the opposing side for deposition.

If the expert forms any new opinions between the time of deposition and trial, counsel should immediately make the expert available for a second deposition. If an agreement with opposing counsel cannot be reached quickly, the party should seek leave to amend the expert witness declaration under Section 2034(k). If counsel wants the expert to offer an opinion at trial that the expert did not offer in deposition, counsel should make an offer of proof as to what the expert will testify to if permitted to do so. Such an offer of proof is essential to the preservation of the point on appeal.

1 Hogan & Webster, Cal. Civil Discovery §10.1, at 525 (1997).
2 See, e.g., Williams v. Volkswagen Aktiengesellschaft, 180 Cal. App. 3d 1244, 1255, 226 Cal. Rptr. 306 (1986) (stating that the Discovery Act was enacted in order to avoid turning litigation into "a game of blindman’s bluff").
3 Id.
5 Code Civ. Proc. §2034(b).
7 Code Civ. Proc. §2034(b).
10 Id.
13 Ransom v. Ransom, 215 Cal. App. 2d 258, 264, 30 Cal. Rptr. 53 (1963): The requirement of the offer of proof serves two practical purposes. First, it permits the trial court to reconsider and correct an erroneous exclusionary ruling in the light of all the facts. Second, it permits the appellate court to determine if the ruling was erroneous and, if so, whether it was sufficiently prejudicial to justify a reversal of the judgment....
On May 2, 2002, the California Supreme Court sent a shock wave through corporate boardrooms and public relations firms with its decision in Kasky v. Nike, Inc. The court ruled that Nike's public statements regarding its manufacturing processes—which were made in the wake of class action claims facing clothiers over alleged sweatshop conditions—could be regulated under California's Unfair Competition Law (UCL) and False Advertising Law. Nike had convinced the trial court, as well as the intermediate appellate court, that its public statements regarding its subcontractors located in Vietnam, China, and Indonesia were non-commercial speech and, therefore, any regulation of the statements would be subject to the highest level of scrutiny. In reversing the lower courts, the state supreme court effectively held that Nike's statements regarding its overseas labor practices were only entitled to the protection granted to advertisements. The case, which had been dismissed on demurrer, now returns to the trial court for a determination of whether Nike's public statements were false or otherwise violated California's broad UCL and False Advertising Law.

Noncommercial speech traditionally is considered political speech and is protected to the fullest extent by the U.S. and California Constitutions. Thus, content-based regulations of non-commercial speech are subject to strict scrutiny, which "requires that the regulation be narrowly tailored...to promote a compelling government interest." Content-neutral regulations of noncommercial speech, such as laws regulating the time, place, or manner of speech, are subject to intermediate scrutiny, which comprises three factors for the court to review:

1) Is the regulation of speech content-neutral?
2) Is the regulation narrowly tailored to serve a significant government interest?
3) Does the regulation leave open alternative channels of communication?

Under the U.S. and California Constitutions, commercial speech enjoys far less protection than does noncommercial speech. The U.S. Supreme Court enunciated the test for regulating commercial speech in Central Hudson Gas & Electric v. Public Service Commission:

At the outset, we must determine whether the expression is protected by the First Amendment. For commercial speech to come within that provision, it at least must concern lawful activity and not be misleading. Next, we ask whether the asserted governmental interest is substantial. If both inquiries yield positive answers, we must determine whether the regulation directly advances the governmental interest asserted, and whether it is not more extensive than necessary to serve that interest.

Thus, the First Amendment protects lawful and nonmisleading commercial speech from regulations that fail to provide a reasonable connection between the asserted governmental interest and the means used to achieve it. Although false or misleading non-commercial statements are often tolerated "to eliminate the risk of undue self-censorship and the suppression of truthful material" and thereby give freedom of expression the ‘breathing space’ it needs to survive, commercial speech does not receive this benefit because the truth of commercial speech is more easily ver-

When advising business clients, the safest option may be to suggest silence...

Jonathan A. Loeb is a partner in Alschuler Grossman Stein & Kahan LLP, where he specializes in complex commercial and intellectual property litigation. Jeffrey A. Sklar is an associate in the firm’s transactional department.
ified, and because commercial speakers are motivated by profit and thus are less susceptible to "chilling."26

Because commercial speech receives less protection than noncommercial speech, numerous laws regulating false and misleading commercial statements pass constitutional muster. Specifically at issue in Kasky were California’s UCL1 and False Advertising Law.10

**Unfair Competition and False Advertising**

The UCL defines unfair competition as “any unlawful, unfair or fraudulent business act or practice and unfair, deceptive, untrue or misleading advertising and any act prohibited by [the False Advertising Law].”71

According to the Kasky court, “The UCL’s purpose is to protect both consumers and competitors by promoting fair competition in commercial markets for goods and services.”72 In achieving this goal, the UCL casts a wide net, permitting violations of other laws to be treated as violations of the UCL (which are independently actionable).13

California’s False Advertising Law makes it unlawful for:

1. Any person, firm, corporation or association, or any employee thereof with intent directly or indirectly to dispose of real or personal property or to perform services...to induce the public to enter into any obligation relating thereto, to make or disseminate...before the public in this state,...in any newspaper or other publication...or in any other manner or means whatever...any statement, concerning that real or personal property or those services...which is untrue or misleading, and which is known, or which by the exercise of reasonable care should be known, to be untrue or misleading.14

The False Advertising Law has several elements in common with the UCL. First, both laws regulate not only false speech “but also advertising which although true, is either actually misleading or which has a capacity, likelihood or tendency to deceive or confuse the public.”15 Second, a private citizen may bring an action under the False Advertising Law on the citizen’s own behalf or on behalf of the general public.16 Finally, a violation of the False Advertising Law is treated as an independent violation of the UCL.17 A violation of the False Advertising Law is a misdemeanor punishable by up to six months in county jail, a fine of up to $2,500, or both.18 Therefore, under California law, a business that makes a true statement it reasonably should have known might be misleading to the public violates the False Advertising Law and the UCL.

In Kasky, plaintiff Marc Kasky alleged that Nike and several of its officers had committed actual fraud and deceit by making misleading and untrue statements on behalf of the company in various forms, including press releases and letters to editors of major newspapers. Kasky alleged that the defendants were liable under the UCL because their actions constituted unfair or fraudulent business practices.23 Because any person acting for the interests of the “general public” may bring an action for restitution or injunctive relief under the UCL,20 Kasky was not required to allege any injury to himself.21

The statements that Kasky referred to in his suit were ones made by Nike regarding its practices in press releases, in letters to newspapers, in a letter to university presidents and athletic directors, and in other documents distributed for public relations purposes.22 In particular, press releases responded to sweatshop allegations, addressed women’s issues, stressed the company’s code of conduct, and broadly denied exploitation of underage workers.23 In a lengthy press release, titled “Nike Production Primer,” Nike answered a series of allegations with detailed information and footnoted sources.24 Another release drew attention to a report based upon an investigation by Andrew Young, former U.S. ambassador to the United Nations, that found no evidence of illegal or unsafe working conditions at Nike factories in China, Vietnam, and Indonesia.25

The court of appeal’s opinion details how Nike was beset in 1996 and 1997 with a series of reports on working conditions in its factories that contrasted sharply with the favorable report by Young. For instance, an Australian organization published a highly critical case study on Nike’s Indonesian factories, and the Hong Kong Christian Industrial Committee released an extensive documented study of several Chinese factories, including three used by Nike, which described 11- to 12-hour workdays, compulsory overtime, violation of minimum wage laws, exposure to dangerous levels of dust and toxic fumes, and employment of workers under the age of 16.26

**Bolger and the Kasky Analysis**

The U.S. Supreme Court has held that commercial speech, at its core, is “speech proposing a commercial transaction.”27 From this premise, the Court in Bolger v. Young’s Drug Products Corporation28 identified three factors that provide “strong support” that a statement is commercial speech:

1. The speech is in advertising format.
2. The speech refers to products or services.
3. The speaker has a commercial motivation.29

At least two of these factors should be present in order to support a finding of commercial speech.30 Further, the Court has held that speech may not be immunized from being commercial speech simply because it includes political messages.31

Despite the well-settled Bolger factors, the California Supreme Court in Kasky has articulated a new and somewhat ambiguous “limited-purpose test” for deciding “whether particular speech may be subjected to laws aimed at preventing false advertising or other forms of commercial deception.”32 This test consists of three elements:

1) The speaker is someone likely to be engaged in commerce.
2) The intended audience is likely to be actual or potential buyers, customers, or persons likely to repeat the message or influence buyers or customers.
3) The content of the message is commercial in character.33

In defense of this new analytical framework, the Kasky court reasoned that the U.S. Supreme Court has never announced an “all-purpose test” to distinguish commercial and noncommercial speech.34 The court’s scrutiny of the High Court’s commercial speech decisions revealed that the precise boundaries of commercial speech are difficult to define, and bright lines are not easily drawn.35 The court also noted Justice John Paul Stevens’s admonition that efforts to describe the boundaries of commercial speech should relate to the regulatory objective of limiting commercial speech’s potential to mislead.36 In light of these acknowledged challenges and principles, the Kasky test limits itself to the question of whether particular speech is subject to regulations of deceptive commercial practices.

The Kasky court described the contours of the three prongs of its test and attempted to explain how their focus on the speaker, intended audience, and content of the message is consistent with the Bolger factors and other U.S. Supreme Court holdings.37 The commercial speaker and intended audience prongs articulated by Kasky were derived from the speaker-audience transactions considered implicit in Bolger’s focus on economically motivated speakers and advertising format.38 Further, Kasky’s departure from a strict adherence to Bolger’s advertising format requirement was justified by noting Bolger’s broad warning that each of the factors or characteristics set forth by Bolger “would [not] always be necessary to the characterization of speech as commercial.”39 Finally, commercial content was described as a “broad definition” of Bolger’s product references factor.40 This expansion of the Bolger factor was deemed necessary in order to adequately characterize the broad spectrum of statements made and topics addressed in modern image- and sales-enhancing public rela-
Certified Public Accountants

EXHIBIT 1
Lost Profits Analysis

- Expert Witnesses
- Economists
- Accountants
- Appraisers

Call: Barbara Luna, Paul White, Jack Zuckerman, Fred Warsavsky, Drew Hunt or Bill Wolf

14455 Ventura Boulevard, Suite 300, Sherman Oaks, California 91423
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tions campaigns. Yet despite the Kasky court’s efforts to reconcile its holding with Bolger, when a practitioner attempts to apply the Kasky test instead of the Bolger factors, the result is clear: With Kasky, there is a new and potentially unconstitutional test in California for commercial speech.

In Bolger, the factors determining commercial speech are fairly discrete, particularly with reference to products and services; in Kasky, the factors appear to be more inclusive. One effect of Bolger is the possibility that some corporate speech may be non-commercial. The effect of Kasky, however, appears to be that practically all corporate speech may be construed as commercial.

For example, in the case of a press release issued by a company, Bolger requires that three factors be applied to determine whether the press release is commercial speech: advertising format, product references, and commercial motivation. While most corporations admittedly act by commercial motivation, at least one of the two remaining factors should be present in order for the company’s statement to be defined as commercial speech.

The Kasky test stands in stark contrast. First, Kasky asks whether the company is likely to be engaged in commerce. The great majority of corporations are engaged in some form of commerce, so this prong is met by virtually all corporate speech. Second, Kasky asks whether the intended audience is likely to be actual or potential buyers of the company’s products or services, or “persons (such as reporters or reviewers) likely to repeat the message to or otherwise influence actual or potential buyers or customers.” Essentially all businesses will satisfy this sweeping prong by making any public statement. Indeed, in this information age, it is difficult to imagine how any company could make any public statement that would not be covered and disseminated by countless media outlets and thus reach actual or potential buyers, whether a company intends so or not.

Because the first two prongs will almost always be met, the company’s statement will be deemed commercial speech in California so long as the final prong is satisfied: whether the content of its speech is commercial. This factor is framed broadly by the Kasky court and includes not only product references as discussed in the Bolger test but also references to any business operations for the purpose of promoting sales or commercial transactions. According to the Kasky court, product references include “statements about the manner in which the products are manufactured, distributed, or sold, about repair or warranty services that the seller provides to purchasers of the product, or about the identity or qualifications of persons who manufacture, distribute, sell, service, or endorse the [products].” Similarly, references to services include statements about “the education, experience, and qualifications of the persons providing or endorsing the services.”

In response to this prong, Justice Janice Brown stated in her dissenting opinion in Kasky that “business operations, products, or services may be public issues. For example, a corporation’s business operations may be the subject of public debate in the media. These operations may even be a political issue as organizations, such as state, local or student governments, propose and pass resolutions condemning certain business practices. Under these circumstances, the corporation’s business operations undoubtedly become a matter of public concern, and speech about these operations merits the full protection of the First Amendment.”

Further, a corporation also is in the business of promoting its public image, which will likely be enhanced by public statements that it makes regardless of the issue being addressed. As a result, under the Kasky court’s broad view of commercial content, it is hard to imagine how a company could engage in meaningful public debate on any issue, whether or not the issue directly affects its business, without the company’s statement being deemed commercial.

**Advising Business Clients**

Protection of free speech under the California Constitution is at least as broad as under the U.S. Constitution. Because Kasky appears to allow less protection for commercial speech than is allowed under Bolger, the validity of Kasky is questionable. However, unless and until the U.S. Supreme Court grants certiorari to hear the Kasky case, practitioners have a burden of uncertainty to bear.

Therefore, when advising a business client on how to publicly address certain issues that the client considers noncommercial, practitioners should alert the client that the safest choice is silence. While this is the textbook example of a chilling effect, a business client runs a substantial risk in California if it makes a statement that is mistakenly false, or true but misleading.

If silence is not an option, the business client must make statements with the utmost care and diligence to verify their truth, accuracy, and completeness. In addition, thoroughly documenting the efforts taken by the client to verify the truth and veracity of a statement may go a long way toward proving that a reasonable speaker could not have known about a false or misleading representation later found in the client’s statement. Ideally, there should be no reference to the business operations, products, or services of the client in the statement.

The lesson of Kasky is that practitioners must counsel their business clients to maximize the likelihood that their public statements are characterized as noncommercial rather than commercial speech. In post-Kasky California, only the purest political speech by a business will be deemed noncommercial.
The Uniform Trade Secrets Act should not be used for anticompetitive purposes

The laudable objective of the Uniform Trade Secrets Act is to codify the common law protection of confidential business information that has competitive value. Information that is not protected or protectible by patent, copyright, or trademark may be denied to others if the broadly worded requirements of the UTSA are met. Under the UTSA, protectible information—whether it is a formula, pattern, compilation, program, device, method, technique, or process—must have some economic value from not being generally known to the public or to those to whom it would be economically useful. Additionally, the information must be the subject of reasonable efforts to maintain its secrecy. If business information meets these rather simple criteria, anyone who has possession or makes use of the information without consent may be enjoined from further use and may be liable for compensatory damages, unjust enrichment, a reasonable royalty, exemplary damages, and attorney's fees.

The UTSA is a powerful tool for businesses that seek to protect their investment in valuable competitive information. Unfortunately, it has also become a weapon used by aggressive businesses bent on stifling legitimate competition. The problem is inherent in the act's definition of a trade secret, which when taken at face value applies to practically every kind of information that a business possesses. If information that is not published in a trade publication or otherwise demonstrably known to most competitors is used in a business, the information presumably has economic value to that business. And if the business employs at least some security measures—computer password access, confidentiality agreements, or even locks on office doors—a possible trade secret is born.

The ease of stating at least a prima facie case for a trade secret and the development of sympathetic California case law has made the UTSA a route to anticompetitive conduct that would otherwise contravene California public policy. California law strongly favors vigorous competition in the marketplace—so much so that, in contrast to the laws of many states, California generally prohibits employers from enforcing covenants not to compete with employees who leave. The UTSA has in many ways undermined this procompetitive policy. An astute defense and judicial awareness of the dangers can help to ensure that the UTSA is not misused. How these dangers might arise, and some strategies for avoiding them, are important areas of concern for litigators.

Ways of Misapplication

The anticompetitive danger of the UTSA often begins with employment contracts and confidentiality agreements that have an overbroad definition of trade secrets. Employers often hope to avoid California's prohibition on covenants not to compete by defining every piece of information that an employee receives in the course of employment as a trade secret. A typical provision states: [F]inancial, personnel, sales, scientific, technical and other information regarding formulas, patterns, compilations, programs, devices, methods, techniques, operations, plans and process...[constitute] the Employer's 'trade secrets.'

When an employee quits to join or form a competing business, a foundation has been laid for the charge that the employee is using the former employer's trade secrets in the new employment. Trade secret law has been employed in many jurisdictions to enjoin former employees from working for a competitor in cases in which the "new employment...will inevitably lead [the employee] to rely on the [former employer's] trade secrets." As one commentator has observed, "[U]sing principles of commercial morality, most...courts [other than California's] have been inclined to protect trade secrets over an employee's freedom to work for a direct competitor."

In 1999, a court of appeal in California adopted this doctrine, finding that the "inevitable disclosure rule is rooted in common sense," but the California Supreme Court ordered the opinion depublished. Recently, in Schlage Lock Company v. Whyte, a California appellate court rejected the "inevitable disclosure" doctrine, finding that it is contrary to California law and policy because it creates an after-the-fact covenant not to compete, restricting employee mobility.

Strong public policy, expressed in a legislative prohibition of contracts in restraint of a trade or profession, is an important reason that the inevitable disclosure doctrine historically has not gained favor in California. The Schlage decision, however, notes that California public policy also protects trade secrets. In rejecting the inevitable disclosure doctrine, Schlage does not regard as dispositive California's public policy favoring employee mobility and instead relies on principles of contract law. Namely, Schlage holds that employees should not be held to a restrictive employment covenant imposed "after the employment contract is made and [that] therefore alters the employment relationship without the employee's consent." However, the extent to which this rationale favoring employee mobility will yield to trade secret protections incorporated into carefully drawn employment agreements remains unclear—

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By Jeffrey W. Kramer

How Misuse of the UTSA Can Be Countered
sented in this case, an employer might prevent disclosure of trade secrets through, for example, an agreed-upon and reasonable non-solicitation clause that is narrowly drafted for the purpose of protecting trade secrets.\textsuperscript{17} As a result, the UTSA may have renewed potency in California to limit competition.

Often, plaintiffs use the allegation that trade secrets have been misappropriated as a springboard to other causes of action. For example, California law defines “unfair competition” as “any unlawful, unfair or fraudulent business act or practice.”\textsuperscript{18} Plaintiffs alleging misappropriation of trade secrets invariably allege unfair competition as well, citing the misappropriation of trade secrets as the “unlawful” conduct engaged in by the defendant competitor.

Often, plaintiffs invoke the business tort of interference with prospective economic advantage, which requires pleading and proof that “the defendant not only knowingly interfered with plaintiffs’ expectancy, but engaged in conduct that was wrongful by some legal measure other than the fact of interference itself.”\textsuperscript{19} The UTSA frequently supplies this legal measure of wrongful conduct, with plaintiffs alleging that defendants used their knowledge of misappropriated trade secrets to obtain business from plaintiffs’ customers. Frequently these other causes of action cannot be pled without allegations of trade secret misappropriation.

The trade secret lawsuit can be a devastating competitive weapon, particularly against start-up or marginally financed smaller businesses. The charge is made that the departing employee or employees have taken their former employer’s trade secrets and are using them to compete in their new business. The trade secrets may be described as customer information, supplier information, manufacturing processes, financial information, or any of these in combination. If the employees have in their possession or take with them any papers or electronic information relating to their former employment, as many employees do, a preliminary injunction against the use of these materials and information derived from them is a serious risk. If a preliminary injunction—even of limited scope—issues, it places the defendant business at a serious competitive disadvantage. Even though the scope of the injunction may be relatively benign, the existence of such a court order may discourage customers, lenders, and investors from doing business with the defendant.

Crushing and intrusive discovery may be the next order of business for the aggressive trade secrets plaintiff. The discovery may be designed to learn the customers, product lines, processes, and finances of the defendant business—all of which is valuable competitive information.\textsuperscript{20} The cost of gathering and producing this information may be great, in terms of attorney’s fees, employee time, and employee morale. Key employees of the defendant business may spend their workdays preparing and sitting for depositions. The trade secret claim, regardless of its ultimate merit, can force the defendant business to yield sensitive business information to an aggressive and hated competitor and hobble the defendant business by distracting its employees and straining its financial resources.

Third-party discovery may be even more destructive. Existing and potential investors, lenders, and suppliers to the defendant business may all be targeted. The message that this discovery conveys to the investors, subtly or directly, is that they may soon be defendants. Lenders will fear that their loans may involve substantial risk. Suppliers will fear that selling to the defendant may not be worth the loss of goodwill to a larger client or the expense of becoming involved in a lawsuit.

Trade secret litigation in California poses a unique threat to investors in start-up businesses. In \textit{PMC v. Kadisha},\textsuperscript{21} the California Court of Appeal articulated a new theory of officer and director liability when a new business is the beneficiary of trade secret misappropriation or other unlawful conduct. Corporate officers or directors “may be liable for an intentional tort if: (1) the officer or director purchased or invested in the corporation the principal assets of which were the result of unlawful conduct; (2) the officer or director took control of the corporation and appointed personnel to run the corporation; and (3) the officer or director did so with knowledge or, with respect to trade secret misappropriation...had reason to know of the unlawful conduct.”\textsuperscript{22}

In \textit{PMC}, the plaintiffs—PMC and its subsidiary WFI—sued WFI’s former president and other senior managers, who left WFI to form a competing plastics manufacturing business that the plaintiffs alleged was an “exact replica of WFI.”\textsuperscript{23} The plaintiffs alleged that the defendants formed this competing business, which they also sued, by engaging in tortious conduct that included the misappropriation of trade secrets consisting of WFI’s customer lists, customer product specifications, and manufacturing specifications and processes.\textsuperscript{24} After the lawsuit was filed, defendant Neil Kadisha and others invested in the defendant start-up business; became majority shareholders, officers, and directors; appointed personnel to run the business; and effectively took control of the new corporation.\textsuperscript{25} The plaintiffs demanded that the investor defendants cause the new business to “cease and desist from the ongoing use of WFI’s confidential and proprietary information,” and then added the investor defendants to the lawsuit when they refused to comply.\textsuperscript{26}

The investor defendants moved for summary judgment on the grounds that they could not be personally liable for misappropriation of trade secrets and the other alleged wrongful conduct because they had not authorized or participated in any of the wrongful conduct, and had not done anything more than serve as directors and officers of the defendant business.\textsuperscript{27} The trial court granted the investor defendants summary judgment, but the court of appeal reversed, rejecting the investor defendants’ argument that they could not be held vicariously liable for the tortious conduct of the corporation. Noting that the “defendants purchased a corporation whose sole assets were purportedly corruptly acquired resources,” the court of appeal opined, “Liability imposed on a corporate shareholder, officer, or director who knows or has reason to know about tortious misappropriation under these circumstances and allows it to occur is not vicarious.”\textsuperscript{28}

This new business tort, born of allegations of trade secret misappropriation, poses clear risks for new business formation. Investors willing to risk a capital investment in a new business may be loathe to risk personal liability if the new business is later adjudged to have misappropriated trade secrets. Established companies, facing incipient competition from former employees, now have a powerful new strategy to stifle competition if they can make a colorable claim of misappropriation of trade secrets. By putting new investors and the officers and directors they appoint on notice of the trade secret claim, plaintiffs can make investors face a difficult choice. They can withdraw from the corporation and risk the loss of their investment or be defendants in a lawsuit, facing potential personal liability for compensatory and punitive damages. Used aggressively in this way, a claim of misappropriation of trade secrets can bring even greater pressure than before on a fragile start-up business.

**The Lessons of PMC**

\textit{PMC} demonstrates the aggressive use of the UTSA. The court of appeal reversed a summary judgment in favor of the defendant, Kadisha, who was a director of the defendant start-up business, based in part on the fact that the plaintiffs had put Kadisha on notice of their assertion that the new business was started with the plaintiffs’ trade secrets. Yet at trial the plaintiffs’ trade secret claims were defeated and adjudged by the court to have been brought in bad faith. Just as the court of
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Defendants charged with misappropriating trade secrets have a variety of tools available to minimize the damage of trade secrets claims that are marginal or made in bad faith.

An aggressive judicial response in cases in which the suppression of legitimate competition may be the intended or even unintended result of the litigation should flow from healthy judicial skepticism of trade secret allegations. The first order of business in trade secrets cases is usually the plaintiffs’ application for a temporary restraining order and preliminary injunction. Aggressive plaintiffs’ counsel typically seek a broadly worded order to prohibit a range of competitive activity that may not be tightly connected to the allegedly misappropriated trade secrets, or the trade secrets themselves may be broadly and vaguely described. There may be evidence that a defendant left the plaintiff’s employ and took hard copy or electronic information belonging to the plaintiff. If injunctive relief is to issue, it should be carefully limited to the protection of well-defined trade secrets and not used merely as a punishment against former employees for taking property belonging to their former employer. Because the issuance of injunctive relief, no matter how narrowly constrained, may have serious competitive ramifications, courts should carefully balance the equities and enjoin the use of information only when the information clearly qualifies as a trade secret.

The legislature has enacted some discovery protection in the form of Code of Civil Procedure Section 2019(d), which requires a party alleging trade secret misappropriation to “identify the trade secret with reasonable particularity” before commencing discovery relating to the trade secret. Before forcing defendants to comply with the intrusive and burdensome discovery that legitimate trade secret claims may justify, courts should require plaintiffs to state the specific information that constitutes the trade secret. Such broadly stated trade secrets as customer identities, customer purchasing requirements, the process for manufacturing certain products, or cost and profit information should not suffice. These may or may not be protectible trade secrets. Without specific information, it is impossible to tell.

All too often, employees take information belonging to their former employer with them. They may have been given the information to do their job, they may have accumulated the information themselves during their employment, or they may have taken the information when leaving. The information may be useful to the employee in taking a new position with a competitor, the information may be proprietary to the former employer in the sense that it is physical property that belongs to the former employer or was compiled by the former employer, and it may be to some extent confidential because the information or the compilation is not published or disseminated by the former employer.

But is the information a trade secret? To make this determination, courts should require objective evidence that the information has independent economic value. Although there is little case law on the meaning of this UTSA requirement, courts most frequently look to the “work effort” and cost of developing or compiling the confidential information. Courts may also look to whether the information itself is marketable or whether the information provides a competitive advantage in the industry, one example being an “innovator’s premium.”

Beyond demonstrating that time and effort were required to compile the confidential information, a party suing on a true trade secret should be able to produce evidence that the same or similar information is sold or licensed in the industry. The absence of such evidence would seem to belie an argument that the information has independent economic value. The information must also be “the subject of efforts that are reasonable under the circumstances to maintain its secrecy.” Here the required proof should demonstrate steps taken specifically to maintain the secrecy of the alleged trade secret, rather than more generalized business security measures.

The UTSA authorizes the court to award reasonable attorney’s fees to the prevailing party if “a claim of misappropriation is made in bad faith.” The legislature intended this attorney’s fees provision “as a deterrent to specious claims of misappropriation.” Recently, the California Court of Appeal has interpreted this bad faith standard to require a showing of the “objective speciousness of [the plaintiff’s] claim, as opposed to frivolousness, and its subjective bad faith in bringing or maintaining the claim.” Moreover, “[b]ad faith may be inferred where the specific shortcomings of the case are identified by opposing counsel, and the decision is made to go forward despite the inability to respond to the arguments raised.” Awarding attorney’s fees liberally when confronted with specious trade secret claims should prove to be an effective deterrent to such claims.

The final outcome of PMC demonstrates effective judicial use of the attorney’s fee provision of the UTSA. Following the entry of judgment in their favor, the defendants moved for an award of attorney’s fees under the authority of the UTSA. The court granted the defendants’ motions for attorney’s fees, finding that the plaintiffs’ trade secret claims were brought in bad faith and rejecting the plaintiffs’ argument that attorney’s fees should be strictly limited to the trade secret cause of action. Because the trade secrets claims were linked with the plaintiffs’ other claims, the court awarded the defendants most of the attorney’s fees they incurred over more than two years of intense litigation defending the trade secrets claims and the related causes of action.

The UTSA provides important protections for valuable business information but if misused has the potential for serious anticompetitive harm. Trade secret claims based on broadly defined, arguably confidential business information may be used to discourage employees from accepting employment with competing businesses; to discourage investment in start-up businesses; to support other causes of action with anticompetitive potential; and to sustain prolonged, intensive, and expensive litigation that itself may discourage or even eliminate competition. An aggressive defense of marginal trade secret claims and judicial awareness of the dangers trade secret litigation may pose are the keys to containing the dark side of the UTSA. 

1 The Uniform Trade Secrets Act, Civ. Code §§3426 et seq.
3 See Civ. Code §§3426.16(a).
4 See Civ. Code §§3426.16(b).
7 See generally B. Malseberger, COVENANTS NOT TO COMPETE: A STATE-By-STATE SURVEY (2d ed. 1996).
8 The exceptions include a person who sells the good.
will of a business or all of his or her shares in a corporation (Bus. & Prof. Code §1660) and a partner who sells his or her interest in a partnership (Bus. & Prof. Code §16602).


6 PepsiCo Inc. v. Redmond, 54 F. 3d 1262, 1269 (7th Cir. 1995).


10 Id.

11 Bus. & Prof. Code §16600.


13 Id. at 10600.

14 Bus. & Prof. Code §17200.

15 Della Penna v. Toyota Motor Sales, 11 Cal. 4th 376, 393, 45 Cal. Rptr. 2d 436, 447 (1995).

16 The defendant may seek a protective order limiting disclosure of sensitive information to the attorneys or to a limited group of the plaintiff’s representatives, but as a practical matter this order may not afford real protection.


18 Id., 78 Cal. App. 4th at 1372.

19 Id. at 1375.

20 Id. at 1374-75.

21 Id. at 1375.

22 Id. at 1374.

23 Id. at 1378-79.

24 Id. at 1389 (emphasis in original).


26 See Code Civ. Proc. §2019(d), which recognizes that the identification of such sensitive information may require protective orders, in camera hearings, sealing the records of the action, or other court orders, as authorized by the UTSA in Civ. Code §3426.6, to preserve the secrecy of the alleged trade secret.


29 See Fred Stores of Miss., Inc. v. M & H Drugs, Inc., 725 So. 2d 902, 910 (1998) (“The information on the list had independent economic value as evidenced by the fact that marketing companies are willing to pay money to obtain it.”); Hofmann-La Roche Inc. v. Yoder, 950 F. Supp. 1348, 1358 (S.D. Ohio 1997) (“[C]ourts have held, however, that the fact a party is willing to pay a large price to acquire information is evidence of the value of such information.”).


32 Civ. Code §3426.4.


34 Id., 95 Cal. App. 4th at 1262.

35 Id. at 1264.

The application of standard class action principles to claims that employers have violated California’s wage and hour laws has been the subject of much controversy and litigation in recent years and is beginning to reshape employer practices in more than one industry. Lawsuits challenging employers’ wage and hour practices on a class-wide basis have targeted a broad range of employers and industries, including fast food restaurants, chain retail stores (including those selling clothing, auto supplies, and home and decorating items, as well as drug stores and video rental stores), car rental companies, grocery stores, and insurance companies.

The lawsuits allege a variety of violations of wage and hour laws. These include requiring hourly nonexempt employees to work “off the clock,” failing to provide these employees with proper rest breaks and meal periods, and failing to accurately identify and pay for all time worked.1 Probably the most common claim brought against employers, and potentially the most costly, is the improper classification of managerial employees as exempt under the “executive” exemption or the misclassification of other employees as exempt under the “administrative” exemption.

Many employers previously unaware of the significant differences between California’s wage and hours laws and the federal Fair Labor Standards Act2 have learned at considerable cost that California’s tests for exemption from overtime pay requirements are harder to meet than those under the federal law. Multistate employers, for example, have paid huge settlements in class action litigation because their wage and hour policies had been designed to comply with the FLSA but could not pass muster under

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California law.

California wage and hour laws are more favorable to employees in other respects as well. For example, under California law, the consequences for failure to provide required rest breaks and meal periods include the equivalent of an extra hour of pay for missed breaks.2 An employer who violates any provision of the “working hours” chapter of the Labor Code3 or any provision regulating hours and days of work in any wage order issued by the Industrial Welfare Commission4 may be required to pay civil penalties. The penalty for an initial violation is $50 per affected employee per pay period. For each subsequent violation the penalty doubles to $100 per employee per pay period.5 “Waiting time penalties” of up to 30 days’ wages may be assessed against employers who fail to make timely payment of all wages (including accrued but unused vacation pay) owed to an employee who is discharged or quits.7 Prevailing plaintiffs are entitled to recover their attorney’s fees.8

Employers can face very significant liabilities when these remedies are aggregated in potential class-wide recoveries. The fact that under federal and California law individuals acting on behalf of an employer may be held personally liable for unpaid wages and penalties makes inattention to wage and hour compliance a very risky proposition.9 A claim may be maintained as a class action under California law “when the question is one of a common or general interest, of many persons, or when the parties are numerous, and it is impracticable to bring them all before the court....”10 California court’s recognize the similarities between the prerequisites for class actions under state and federal law and may look to decisions of the federal courts for guidance in determining whether a dispute should be certified for class treatment.11

Under federal law, class actions are appropriate when: “(1) the class is so numerous that joinder of all members is impracticable, (2) there are questions of law or fact common to the class, (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and (4) the representative parties will fairly and adequately protect the interests of the class.”12

Once the prerequisites are in place, federal law permits class actions if certain other conditions are present. Among these are “that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy....”13

The proponent of class certification bears the burden of proving that common ques-
tions predominate over individual ones and that the other conditions for a class action are present.14 In almost all wage and hour cases it is the plaintiffs who wish to certify the case as a class action, so they must bear this burden of proof. One of the most controversial issues facing the courts in recent years has been whether lawsuits alleging violation of wage and hour laws, especially claims that employers have misclassified workers as exempt from the requirement of overtime pay, can meet these standards and be tried as class actions.

Exempt Status

Both California and federal law provide exemptions from overtime pay requirements for executive, administrative, and professional employees. Under both California and federal law, exempt status is an affirmative defense,15 and the exemptions are to be “narrowly construed.”16 Under California law, the Industrial Welfare Commission may establish exemptions from the state’s overtime pay requirements for executive, administrative, and professional employees “provided that the employee is primarily engaged in the duties that meet the test of the exemption, customarily and regularly exercises discretion and independent judgment in performing those duties, and earns a...salary equivalent to two times the minimum wage for full-time employment.”17 The federal exemptions are authorized by the Fair Labor Standards Act and their parameters explained in regulations issued by the U.S. Department of Labor.18

The “professional” exemption is not often the subject of litigation. In the broadest terms, under federal and California law, the exemption applies to 1) employees performing work requiring advanced knowledge acquired by a prolonged course of specialized instruction, 2) employees in the artistic and the learned professions (for example, medicine, architecture, and dentistry), 3) employees who are educators, and 4) employees performing certain highly sophisticated work in computer systems analysis, programming, and software engineering.19

Under federal and California law, the executive exemption applies only to employees who regularly supervise the work of at least two full-time employees (or their equivalent in part-time employees), who are in charge of a recognized department or business division, and who have the authority to hire and fire employees or to make effective recommendations to do so.20 An administrative employee is exempt only if his or her primary duties involve the performance of “office or non-manual work directly related to management policies or general business operations of his employer or his employer’s customers.” An exempt administrative employee also regularly assists an owner, executive, or administrator; or performs technical or specialized work; or executes special assignments under only general supervision.21 All three exemptions—professional, executive, and administrative —can be lost if the employees in question spend too much time on nonexempt work, including so-called production work.22

California and federal law part company on several key points in determining the applicability of the exemptions. But the difference that lies at the heart of much recent litigation is the amount of time an executive or administrative employee may spend on nonexempt tasks and still be exempt. Under the FLSA any employee earning a salary of at least $250 per week qualifies for the so-called short test to determine exempt status under the executive or administrative exemptions.23 Because the salary required for application of the short test is minimal, the vast majority of cases determining exempt status under the FLSA use this test. It requires that the employee’s “primary duty” consist of either managerial or administrative work that “includes” the exercise of discretion and independent judgment.24 The federal law permits a finding that an employee’s primary duty consists of those tasks most important to the employer, even if they do not take up the majority of the employee’s time.25 In other words, it permits a qualitative analysis of the primary duty standard.

California law, in contrast, requires a purely quantitative analysis. An employer must show that its exempt employees spend more than 50 percent of their time engaged in exempt tasks.26 The California Supreme Court described how this analysis should be undertaken in its decision in Ramirez v. Yosemite Water Company:27

[The trial court should inquire] into the realistic requirements of the job. In so doing, the court should consider, first and foremost, how the employee actually spends his or her time. But the trial court should also consider whether the employee’s practice diverges from the employer’s realistic expectations, whether there was any concrete expression of employer displeasure over an employee’s sub-standard performance, and whether these expressions were themselves realistic given the actual overall requirements of the job.28

The Ramirez court remanded the case to the trial court with instructions to:

[1] Itemize the types of activities that it considers to be [exempt], and the approximate average times that it finds...
the employee spent on each of these activities. Because the question whether a particular activity is [exempt] is a mixed one of law and fact, this itemization will enable an appellate court to review whether the trial court’s legal classifications are correct, and whether its factual findings are supported by substantial evidence.  

Ramirez claimed that he was incorrectly classified as an exempt outside salesman. The court’s reasoning, however, applies equally to the determination of exemptions under the executive and administrative tests. The Ramirez decision was seized upon by defense counsel opposing attempts to certify claims for overtime for class treatment. Employers argued that such a fact-intensive analysis, used in the service of a test in which exempt status can turn on the proper characterization of tasks consuming only a small percentage of an employee’s time, is inherently inappropriate for application to class-wide claims.

This argument was advanced both on demurrers and in opposition to motions for class certification.  

Trial courts were not often persuaded by this argument, and a number of cases were certified for class treatment. Several employers sought review of class certification orders by writ. When the appellate courts proved unwilling to issue writs, many employers settled rather than wait for the chance of relief on appeal.

The Sav-On Analysis

Earlier this year, however, in the case of Sav-On Drug Stores, Inc. v. Superior Court, a California appellate court for the first time considered the propriety of class certification in a case challenging the exempt status of a company’s managerial employees. The court noted, “Relief by extraordinary writ is appropriate to prevent a burdensome trial in a massive class action.”

The Sav-On court reversed the trial court’s order granting certification of a class of approximately 1,400 managers employed in approximately 300 Sav-On stores. The court determined that the plaintiffs had not met their burden of proving that common issues predominated over questions that would require individualized proof at trial. Assertions in the plaintiffs’ declarations that managers’ job duties did not vary from store to store were found to be unsupported by personal knowledge. The plaintiffs also sought to persuade the court that the predominance of common questions was shown by the company’s use of uniform job descriptions and the same performance review form for all the stores, a compensation system that applied to all members of the putative class, class-wide training programs, a minimum work week of 48 hours for class members, and the classification of all managers and assistant managers as exempt. In addition, they pointed to the absence of a compliance program to train employees to differentiate between exempt and nonexempt tasks and the fact that Sav-On had not undertaken empirical studies or surveys to identify the amount of time the managers and assistant managers spent on the component tasks of their jobs.

The Sav-On court was not persuaded by these arguments. The court concluded that the plaintiffs had identified issues not likely to be in dispute at a trial on the merits. Also, they had not made an adequate showing that common issues would predominate at a trial on the central disputed issue—that is, how the putative class members spent their time. The court concluded that the “policies, practices, and procedures cited by plaintiffs do not address that issue nor show that the way the [managers and assistant managers] spend their time is so standard or uniform as to be triable on a class-wide basis.”

The Sav-On court looked to the defendant’s showing that its managers and assistant managers faced a wide variety of divergent conditions in its stores. These included the location and square footage of the stores, the number of managers, the size of the staff supervised, the mix of part-time and full-time employees, the hours the stores were open to the public, the rate of turnover among the staff, each store’s sales volume, and each manager’s style and experience. The court was convinced that these varied conditions resulted in enough of a divergence in how the company’s managers spent their workdays that individualized fact questions would need to be litigated regarding each member of the class in order to determine whether or not a particular manager spent more than half of his or her time on exempt tasks.

There is no public policy favoring class actions in the absence of a predominance of common questions, at least in part because a class action “may preclude a defendant from defending each individual claim to its fullest.” The Sav-On court rejected concerns that class members would be unlikely to seek individual redress of their claims, noting that individual awards might amount to thousands of dollars and that prevailing plaintiffs are entitled to recover their attorney’s fees. Although the Sav-On decision was a victory for employers, the court did not hold that claims regarding managerial exemptions from overtime pay can never be determined on a class-wide basis. It acknowledged that the way in which some managers spend their time might be so uniform that their exempt status could be determined on a class basis.

In Belazi v. Tandy Corporation, a trial court found such a situation shortly after the Sav-On decision was issued, in a case involving a challenge to the exempt status of managers working for Radio Shack stores. The company sought to decertify a previously certified class. The plaintiff managers successfully defended the class action status of...
their lawsuit. They argued that the company’s policies required managers to spend the majority of their time in sales activities; that the company enforced those policies by close, centralized supervision; that sales statistics showed that the managers did, in fact, spend the majority of their time selling; and that the company dictated the vast majority of managerial decisions to free its managers to focus on selling. The plaintiffs also argued that Sav-On did not require a demonstration that the duties of the managers must be identical. Instead, according to the plaintiffs, under Sav-On, the evidence must justify a reasonable inference that the duties of the managers are so uniform as to be triable on a class basis.40

In contrast, Radio Shack, founding its argument on Ramirez and Sav-On, argued that the court must look “first and foremost” to the actual work duties performed by the class members. It contended that the class certification decision was based on an unwarranted reliance on company policies, which were unknown to or not followed by a significant segment of the class and could not support a finding that common questions predominated. Radio Shack also sought to persuade the court that declarations submitted by class members and others showed wide variations in the amount of time spent by different managers on the component tasks of the job. The company argued that the evidence supported a conclusion that individualized fact inquiries were needed to determine if any given manager was exempt.41

The court, while not finding fault with the Sav-On court’s analysis, determined that the nature of the operations of the Sav-On and Radio Shack companies was sufficiently dissimilar to support a result different from that of Sav-On. Finding “a great deal of commonality” in Radio Shack’s operations, the time that managers were involved in nonmanagement duties, and the lack of discretion of the managers, the trial court denied the company’s motion to decertify the class.42

The guidance offered by Sav-On was long-awaited; it was also short-lived. On July 17, 2002, the California Supreme Court granted review of the Sav-On decision. As expected, the plaintiffs’ bar and defense counsel view this development through very different lenses.

The defense bar largely views the Sav-On decision as long-delayed recognition that efforts to apply the fact-intensive test of exempt status on a class basis will, except in the unusual case, overwhelm the employer’s ability to defend itself with any but the broadest strokes. In large part they view the granting of review as an acknowledgement by the supreme court of the need for definitive guidance on an unusually important issue and predict that the decision of the court of appeal will be affirmed.

Many in the plaintiffs’ bar see something far different. They point toward recent decisions by the supreme court establishing the right of workers to be paid for time spent “under the control” of the employer even if not actively engaged in “work.”43 They note that the supreme court recognizes that wages are a vested property right recoverable under Business and Professions Code Section 17200 and point to the court’s emphasis in Ramirez on the remedial nature of the laws regulating wages, hours, and working conditions for the protection and benefit of employees. Citing the Ramirez court’s directive on remand that the lower court should look at the average amount of time spent on the plaintiff’s various activities, plaintiffs’ counsel predict that the supreme court will endorse the use of statistics and sampling, rather than requiring exactitude, and will overrule the appellate court to permit class-based determinations of exempt status so as not to frustrate California’s public policies favoring worker protection.44

Representative Actions

The remedies of Business and Professions Code Sections 17200 et seq.—California’s Unfair Competition Law—are often pursued by employees. Indeed, plaintiffs wishing to mount a wide-scale challenge to the exempt status of a category of employees have not relied solely on attempts to certify their claims for class treatment. Many, if not most, have also asserted claims that the employer’s alleged failure to pay appropriate wages to the putative class constitute an unlawful or unfair business practice in violation of Section 17200. Section 17200 permits a “representative” plaintiff to bring an action on behalf of all “similarly situated” individuals. Employees may seek restitution of allegedly unpaid wages, and they benefit from the four-year statute of limitations under Business and Professions Code Section 17208.45

Often, these Business and Professions Code claims are overlaid with class action allegations. In its recent decision in Corbett v. Superior Court,46 the California Court of Appeal for the First Appellate District ruled, in a case of first impression, that there is no inherent incompatibility between representative actions under the unfair competition laws and class actions. A trial court may certify claims under the Unfair Competition Law for class treatment so long as the requirements of Code of Civil Procedure Section 382 are met. Plaintiffs in a “pure” representative action brought under Business and Professions Code Section 17200 may be awarded restitution, but the remedy of disgorgement of ill-gained profits into a “fluid recovery fund” is not available. The ruling in Corbett is important because it makes disgorgement into a fluid recovery fund available in an action under Section 17200, so long as plaintiffs can make the showing needed to certify a class.

Whether representative actions under Section 17200 will be subject to the same analysis used in Sav-On is a question on the horizon for practitioners. Because claims under Section 17200 are actions in equity, a defendant may persuade a court to decline to entertain an action as a representative suit if the defendant can show the potential for harm.47 In several cases the courts have determined that the need to examine individual transactions closely renders a case unsuitable for treatment as a representative action under California’s Unfair Competition Law.48

Logic suggests that the competing concerns animating the argument over the proper parameters of class litigation of exempt status and similar claims will be brought to bear on Business and Professions Code claims. Employers may argue they will be as prejudiced in their efforts to defend against a representative action under Section 17200 as they would be in a formal class action.

For example, in South Bay Chevrolet v. General Motors Acceptance Corporation,49 a car dealer challenged the methods used by the defendant to calculate interest on inventory. The court rejected the attempt to recover restitution and disgorgement on behalf of nonparty dealerships, noting that the dealerships differed in financial sophistication, intelligence, attention to detail, experience in the business, and other factors. The court determined that South Bay had failed to prove that the other businesses it sought to represent were similarly situated regarding the issues critical to determining the dispute.50

In Bronco Wine Company v. Frank A. Loglusso Farms,51 the court concluded that the defendant winery had engaged in unfair business practices in the execution of its contracts to purchase grapes from a variety of growers. The trial court ordered restitution of substantial sums to nonparty growers. However, the court of appeal determined that such a judgment might violate state and federal due process rights because a nonjoined party would be denied notice and an opportunity to be heard. The court determined that “without jurisdiction over the parties an in personam judgment is invalid,” noting that none of the nonparties in whose favor the court ordered restitution were afforded an opportunity to present their claims before the trial court through counsel of their own choice.52

26 LOS ANGELES LAWYER / NOVEMBER 2002
Likewise, the Bronco court noted that the determination of whether the business practices at issue were unfair was “a far more complex factual issue” than was presented in several other cases in which the courts were faced with purely legal questions and the amount of restitution could be determined by a simple arithmetical calculation. The Bronco court concluded, “One must question the utility of a procedure that results in a judgment that is not binding on the nonparty and has serious and fundamental due process deficiencies for parties and nonparties.”

The concerns articulated by the Bronco court have their counterparts in many of the issues under review in Sat-On. Should the Sat-On decision be affirmed and class certification become more difficult to obtain, unfair and unlawful competition claims will more likely be presented as pure representative actions. And the courts will likely see increased litigation regarding whether wage and hour claims, especially those involving fact-intensive inquiries like challenges to exempt status, can be presented on a representative basis without infringing on due process considerations.

1 California and federal law require payment for all hours persons are “suffered or permitted” by their employers to work. California law also counts time spent “under the control” of the employer as time worked. 29 U.S.C. §203(g); Morillion v. Royal Packing Co., 22 Cal. 4th 575 (2000).
3 Lab. Code §226.7.
6 Lab. Code §§58(a)(1) and (2).
7 Lab. Code §203. These penalties apply when an employer “willfully” fails to pay wages on the cessation of employment. The meaning of “willful” is under review by the California Supreme Court in Smith v. Rae Venter, 89 Cal. App. 4th 239 (2001).
9 Lab. Code: §58(a); Donovan v. Agnew, 712 F. 2d 1509, 1511 (1st Cir. 1983) (corporate officer with operational control is jointly and severally liable under the FLSA for unpaid wages); Bureerong v. Urawas, 922 F. Supp. 1450, 1467 (C.D. Cal. 1996) (“Employer includes “any person acting directly or indirectly in the interest of an employer in relation to an employee[,]” 29 U.S.C. §203(d).”) Likewise, the California labor commissioner takes the position that liability may be assessed against individuals for wages owed by a corporation under California law. See letter of June 18, 2002, from Miles Locker, Attorney for the Labor Commissioner, to Hon. John M. Watson, Judge of the Orange County Superior Court (on file with author).
10 CODE CIV. PROC. §382.
11 See, e.g., City of San Jose v. Superior Court, 12 Cal. 3d 447 (1974).
time in production work; her managerial duties were relatively more important than her cooking duties).

21 LAB. CODE §515(a); wage orders issued by the California Industrial Welfare Commission (see, e.g., Wage Order 1, 8 CAL. CODE REGS. §11010(1)(A)(1)(e), §11010(2)(K)). See also Ramirez v. Yosemite Water Co., 20 Cal. 4th 785, 797 (1999).

22 Ramirez, 20 Cal. 4th at 802.

23 Id. at n.5.


26 LAB. CODE §515(a); wage orders issued by the California Industrial Welfare Commission (see, e.g., Wage Order 1, 8 CAL. CODE REGS. §11010(1)(A)(1)(e), §11010(2)(K)). See also Ramirez v. Yosemite Water Co., 20 Cal. 4th 785, 797 (1999).

27 Ramirez, 20 Cal. 4th at 802.

28 Id. (emphasis in original).
On July 30, 2002, in response to the recent wave of corporate accounting scandals, President Bush signed into law the Sarbanes-Oxley Act. Sections 901 through 906 of Sarbanes-Oxley are collectively titled the White-Collar Criminal Penalties Enhancement Act of 2002. The WCCPEA requires CEOs and CFOs to certify the accuracy of corporate financial statements required to be filed with the SEC. The act also imposes tough criminal penalties on senior executives of companies found to have committed accounting fraud or to have failed to “fairly present” their company’s financial condition in reports filed with the SEC. It remains to be seen whether the newly required certifications represent significantly increased exposure for these senior executives, but analogous experience with longstanding certification requirements for senior executives of government contractors provides insight as to how corporate officers can best survive in a business climate now fraught with potential pitfalls.

In the mid-1980s, like today, newspaper headlines screamed allegations of fraudulent business practices. The mid-1980s uproar stemmed from charges that federal government defense contractors were intentionally including unallowable costs in proposals for government reimbursement of overhead expenses. In response, Congress passed several laws in part aimed at punishing those who attempted to defraud the federal government. One such provision is Section 911(a)(1) of the National Defense Authorization Act for Fiscal Year 1986. This section requires a senior executive of a government contractor to certify, to the best of his or her knowledge and belief, that all costs included in an indirect cost proposal were allowable under the cost principles of the Federal Acquisition Regulation and its supplements. This certificate was commonly referred to as the Weinberger Certificate.
ficate, after then-Secretary of Defense Caspar W. Weinberger, at whose insistence this requirement was first promulgated as a regulation.

Even then the idea of government contractor certification was not a novel one. The Contract Disputes Act of 1978 (CDA), which governs contract disputes with the government, has, since its enactment, provided that all claims against the government that exceed $100,000 must be accompanied by a certification that:

- The “claim is made in good faith.”
- The data supporting the claim “are accurate and complete to the best of [the] knowledge and belief” of the certifier.
- “[T]he amount requested accurately reflects the contract adjustment for which the contractor believes the government is liable.”
- “[T]he certifier is duly authorized to certify the claim on behalf of the contractor.”

The purpose of a certification requirement such as that imposed by the CDA is to trigger potential liability for a fraudulent claim. Criminal liability can ensue.

As with the new WCCPEA, the regulation implementing the Weinberger Certificate requirement mandates that the certificate be executed by a company’s senior executives, who personally face potential criminal liability if the representations contained in the certification are shown to be inaccurate. A senior executive who files a false Weinberger Certificate may face a significant monetary fine as well as five years’ imprisonment.

**Use of Certification Provisions**

Government defense contractors have been confronted with certification requirements for more than 20 years, and now the WCCPEA extends similar liability to the CEOs and CFOs of nearly all companies required to report to the SEC. Issues that have arisen in the defense contracting context provide guidance in established pursuant to this and related doctrines through factors other than proof of actual knowledge on the part of corporate officers themselves.

The responsible corporate officer doctrine grew out of the U.S. Supreme Court’s 5-4 decision in *United States v. Dotterweich*. The Court in *Dotterweich* addressed whether a corporate president could be held criminally liable for a corporation’s sale of adulterated or misbranded drugs in violation of a misdemeanor provision of the Food, Drug, and Cosmetic Act. Because the FDCA section under which the officer was prosecuted contained no express mental state requirement, the Court held that an individual acting on behalf of a company who was even “remotely entangled in the proscribed shipment” could be held strictly liable for the alleged violation.

Attorneys representing corporate officer defendants have argued—generally successfully to date—that the responsible corporate officer doctrine should apply only in cases, such as *Dotterweich*, that involve misdemeanor prosecutions under strict liability statutes like the FDCA. A few prosecutors, however, have won felony convictions of corporate managers and executives in circumstances in which the proof establishing the requirement of criminal “knowledge” was based on little more than the executive’s title alone. In prosecutions brought under federal environmental criminal laws, for example, jurors have been persuaded to infer criminal knowledge based on a corporate officer’s title
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still requires the government to prove a “responsible relationship” between a defendant’s position and the conduct alleged.

Convictions of corporate officers have also been upheld under statutes requiring a knowing violation based on the substitution of conscious avoidance of knowledge in place of actual knowledge. United States v. Hanlon involved a prosecution of a corporation’s president, COO, and attorney for, among other offenses, “knowingly” making false statements in connection with obtaining loans from a federally insured bank. The defendants conceded that a fraudulent scheme existed (undertaken by others, who fled prosecution) but asserted that their preparation of various false documents constituted unknowing participation in illegal acts. All three defendants were convicted.

On appeal, the defendants claimed that the government had presented insufficient evidence of guilty knowledge. At trial, the court had given a “conscious avoidance” instruction, also known as an ostrich or, within the Ninth Circuit, a Jewell instruction. The court instructed the jury that:

The element of knowledge of a given fact under this false statement or overvalued security charge may be satisfied by proof that a defendant acted with reckless disregard of what the truth was, unless he actually believed the contrary to be true. One may not deliberately close his eyes to what otherwise would have been obvious to him.

The Second Circuit upheld the convictions, holding that “a finding of guilty knowledge may not be avoided by a showing that the defendant closed his eyes to what was going on about him.” The appellate court stated that “see no evil is not a maxim in which the criminal defendant should take any comfort.”

The WCCPEA’s certification requirement increases the liability that CEOs and CFOs would otherwise face because, in the context of SEC reporting accuracy requirements, it reaches even beyond the knowledge instruction given in Dee. The WCCPEA’s certification provision even eliminates the need to establish knowledge by proving a “responsible relation” between a corporate officer defendant’s title and the criminal conduct alleged. Indeed, the WCCPEA instead creates 1) a responsible relation between a company’s most senior officers and the accuracy of the company’s financial statements, and 2) a duty, within the scope of this prescribed responsibility, to ensure personally that the company’s reports to the SEC “fairly present” the company’s financial condition.

As with the new WCCPEA, the Weinberger Certificate requirement enhanced the government’s ability to prove criminal knowledge on the part of a certifying corporate executive without proving actual knowledge. Through the use of certifications, the government can avoid difficulties it might otherwise face in establishing a criminal statute’s mental state requirement. By creating statutory responsibilities and duties by title alone, the certification requirement disposes of making preliminary inquiry into an officer’s duties and responsibility to infer knowledge that should accompany a title. The available avenues for establishing the requisite mens rea under the False Statements Act (FSA) illustrate the potential exposure senior executives will face under the new WCCPEA provisions.

A violation of the FSA may be established through proof that the defendant had the specific intent to make a false or fraudulent statement. Much lesser showings, however, have been held sufficient to establish that a defendant “knowingly and willfully” executed a false certification in violation of the FSA. As in Hanlon, this requirement is also satisfied by proof of a conscious purpose to avoid learning the truth, indicating a “deliberate ignorance.” Prosecutors frequently request—and, when potentially applicable, receive—a Jewell or conscious avoidance jury instruction. The purpose of such an instruction is “to prevent [the defendant] from circumventing criminal sanctions merely by deliberately closing his eyes to the obvious risk that he is engaging in unlawful conduct.” Such instructions have long been held to be acceptable in prosecutions under the FSA.

Some defendants have attempted to avert criminal liability by claiming reliance on expert advice. The so-called reliance on expert defense in FSA prosecutions, however, is held to apply only when the defendant can demonstrate that his or her accountant or attorney was presented with all relevant facts, and the defendant was “specifically advised” as to “the course of conduct taken.” The same standard can be expected to apply under the new WCCPEA.

Practical Considerations for Sarbanes-Oxley Compliance

With the history of prosecutions under the FSA and the certification requirements of the current legislation, corporate officers must undertake particularly conscientious measures to protect themselves against the possibility of criminal liability. The investigations and prosecutions of senior government contractor officials under the FSA and similar statutes provide insight into the potential criminal liability created by the new legislation’s requirement of the “fair” presentation of financial statements.
7. The certification provision of the CDA requires an authorized representative of a federal government contractor to certify that a claim against the government is:
   A. True and correct, based on the certifying officer’s information and belief.
   B. Accurate and complete.
   C. Accurate and complete to the best of the certifying representative’s knowledge and belief.

8. In the past, corporate officers often have been held criminally liable for “knowing” violations of federal criminal laws under what has become known as the responsible corporate officer doctrine.
   True.
   False.

9. The responsible corporate officer doctrine finds its roots in the U.S. Supreme Court’s decisions:
   A. Planned Parenthood of Southeastern Pennsylvania v. Casey.
   B. Friends of The Earth, Inc. v. Laidlaw Environmental Services (TOC), Inc.
   C. United States v. Dotterweich.
   D. Marbury v. Madison.

10. The broadest imposition of constructive or implied knowledge in the context of a federal criminal statute expressly requiring proof of a knowing violation may be found in:
    A. United States v. Bussey.
    B. United States v. Dee.

11. A Jewell instruction permits a finding of a knowing violation of law when the jury finds beyond a reasonable doubt that the defendant was aware of a high probability of the existence of a certain fact and deliberately avoided learning the truth.
    True.
    False.

12. The purpose of a Jewell instruction is to prevent defendants from avoiding criminal liability by deliberately closing their eyes to the obvious risk that they are engaging in unlawful conduct.
    True.
    False.

13. The purpose of certification requirements such as those imposed by the CDA, the Weinberger Certificate, and the WCCPEA is to trigger potential liability for a fraudulent claim.
    True.
    False.

14. Certification provisions such as those contained in the WCCPEA allow the government to circumvent difficulties it might otherwise face in establishing a criminal statute’s mental state requirement by creating statutory responsibilities and duties that accompany a corporate official’s title alone.
    True.
    False.

15. A violation of the federal False Statements Act (FSA) must be established through proof of a defendant’s specific intent to make a false or fraudulent statement.
    True.
    False.

16. The “reliance on expert” defense has, in the context of FSA prosecutions, been held to apply only when the defendant proves:
    A. His or her accountant or attorney was presented with all relevant facts.
    B. He or she was specifically advised as to the conduct actually undertaken.
    C. Both A and B.
    D. All of the above.

17. The WCCPEA certification requirement provides that:
    A. Certain reports filed with the SEC must be accompanied by a written statement by a reporting company’s chief executive officer and chief financial officer or equivalent.
    B. Certain reports filed with the SEC “fairly present” the reporting company’s financial condition in all material respects.
    C. Willful violations of the certification requirement are punishable by fines not to exceed $5 million or imprisonment for not more than 20 years, or both.
    D. All of the above.

18. In the context of SEC reporting requirements, accounting is somewhat subjective because different approaches are often available as appropriate accounting treatments. Therefore, statements concerning a corporation’s financial condition should plainly describe the chosen accounting methodology.
    True.
    False.

19. The SEC’s proposed rule implementing the certification requirements under the Sarbanes-Oxley Act requires the establishment and maintenance of internal controls to record, process, summarize, and report financial data.
    True.
    False.

20. Which of these corporate compliance programs will reduce the risk that accounting errors may later be characterized as corporate malfeasance?
    A. The destruction of source documents used in auditing and reporting.
    B. “See no evil” programs in which corporate officers delegate corporate auditing and reporting responsibilities to subordinates.
    C. Tiered certifications by subordinates attesting to compliance with applicable laws and regulations.
    D. All of the above.
More than one approach is often available as an appropriate accounting treatment. In very few circumstances is there simply one right answer, and choosing among available options is somewhat subjective. Therefore, the focus of the WCCPEA and the required certification should be defined in terms of adequate disclosure. Senior officials must continually keep in mind the importance of disclosure when they are seeking to minimize their exposure. Crucial to an adequate representation of financial statements is disclosure of choice of accounting methodology and the operative facts incident to that choice. This emphasis on disclosure accordingly bespeaks caution: When in doubt, a full description of the accounting decision underlying the financial statements is required. Officials should avoid being “cute” when describing the company’s financial condition.

In addition, though purchasers of securities may have differing levels of expertise in reviewing financial statements, corporate officials should consider an approach that aims for the lowest common denominator when describing their corporate finances. Senior executives can reduce the risk of being viewed as obscuring a company’s financial condition by expressing it in understandable and simple terms accompanied by disclosure of any qualification of the company’s financial statements. Courts will likely reference the average purchasing public in assigning liability for misstatements. Ambiguity and vague statements may be considered smoke screens for deceptive practices—and under the WCCPEA, where there is smoke, there is statutorily presented suspicion that a problem exists should be aggressively sought to understand and, if possible, the investigation and, if necessary, the jury.

The duty imposed by the act’s certification requirement most probably does not end once a financial statement is submitted. Upon discovery that a statement contains an error, immediate correction and disclosure of the correction will likely be required. Otherwise, silence with knowledge of an inaccuracy can be characterized as an ongoing conspiracy to mislead. Allegations of this type can entangle people who had no participation in the original omission or inaccuracy. Restated financials are certain to become the norm in the wake of the new law.

Early indication of any potential errors in financial statements must be assiduously investigated. Government contractors discovered, sometimes through painful experience, the advantages of being proactive in investigating possible accounting errors. A company’s legal position (and that of its senior officials) in any subsequent litigation is substantially enhanced significantly if the company has aggressively sought to understand and, if required, to correct financial irregularities. An early effort to investigate and correct errors also helps establish the company’s credibility with prosecutors and, if necessary, the jury.

An investigation based upon reasonable suspicion that a problem exists should be formal and thorough. Individuals not directly involved in the problem should conduct the review and, if possible, the investigation should be under the direction of the company’s counsel. A strong and competent internal audit structure within the company is useful in this activity. An early investigation fosters the required preservation of documents, an understanding of the possible problems presented, and the possibility of taking remedial action before being compelled to do so in the face of a criminal prosecution. Truly, being forewarned is to be forearmed.

The Prospect of a Government Investigation

The WCCPEA’s creation of a duty for CEOs and CFOs means that certifying senior officials will automatically be considered—and will likely be targeted—in any contemplated criminal prosecution of their company for omissions or inaccuracies in financial statements. This fact alone may substantially enhance the government’s prosecutorial enthusiasm. The inclusion of the most senior officials of a company substantially increases the publicity value of a prosecution—and the new legislation provides ready identification of “live bodies” on whom the government can focus in pursuing such a prosecution. The inclusion of senior officials also substantially enhances the ability of the government to pressure defendants to settle, particularly given the severity of the criminal sanctions that can be sought against these individuals. All these factors will promote the expenditure of resources by the government in pursuing prosecutions under the new law.

Often, initial discussions with and disclosures to federal investigators establish credibility and head off prosecutions. The government’s prosecutorial resources are limited, and prosecutors can be expected to pick the easiest targets. An early conclusion that company officials have acted reasonably will substantially dampen prosecutorial zeal. Reasonable and reasoned responses in advance of the formal initiation of criminal prosecution may go a long way toward ensuring that a company and its senior officials can avoid being caught up in a prosecution. To be prosecuted is to lose, even if the company and its officials ultimately prevail at trial. Putting together a response team when faced with the knowledge of prosecutorial interest is essential and should be done immediately.

The phenomenon of focusing on senior company officials in seeking to ensure accurate and complete financial statements is not going to go away, even as the headlines recede from the front pages of national newspapers. New cases under the FSA and the False Claims Act arising out of government contracts are still being actively pursued and prosecuted today, almost 20 years after the ini-
sial publicity that led to the enactment of those laws. The bureaucracy for prosecuting such cases is in place, and government expertise is assembled. Thus, government contractors have come to live with the fact that their senior executives face potential criminal liability for improper certifications. Their corporate peers must now follow their lead, because the Sarbanes-Oxley Act creates a new environment in which the personal criminal exposure of senior corporate executives has increased.

2 The WCCPEA certification requirements are enacted as 18 U.S.C. § 1350, “Failure of corporate officers to certify financial reports,” which provides:

(a) CERTIFICATION OF PERIODIC FINANCIALLY REPORTS.—Each periodic report containing financial statements filed by an issuer with the Securities Exchange Commission pursuant to section 15(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(a) or 78o(d)) shall be accompanied by a written statement by the chief executive officer and chief financial officer (or equivalent thereof) of the issuer.

(b) CONTENT.—The statement required under subsection (a) shall certify that the periodic report containing the financial statements fully complies with the requirements of section 15(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78o or 78o(d)) and that information contained in the periodic report fairly presents, in all material respects, the financial condition and results of operations of the issuer.

(c) CRIMINAL PENALTIES.—Whoever—

(1) certifies any statement as set forth in subsections (a) and (b) of this section knowing that the periodic report accompanying the statement does not comport with all the requirements set forth in this section shall be fined not more than $1,000,000 or imprisoned not more than 10 years, or both; or

(2) willfully certifies any statement as set forth in subsections (a) and (b) of this section knowing that the periodic report accompanying the statement does not comport with all the requirements set forth in this section shall be fined not more than $5,000,000, or imprisoned not more than 20 years, or both.

4 See 10 U.S.C. § 2324(b); 48 C.F.R. § 52.242-4.
6 41 U.S.C. § 605(c). This requirement is implemented by 48 C.F.R. § 52.233-1(d), which sets forth the language of the required certification:

I certify that the claim is made in good faith; that the supporting data are accurate and complete to the best of my knowledge and belief; that the amount requested accurately reflects the contract adjustment for which the Contractor believes the Government is liable; and that I am duly authorized to certify the claim on behalf of the Contractor.

48 C.F.R. § 52.233-1(d)(1)(i).
7 Skelly & Loy v. United States, 685 F. 2d 414, 418 n.11 (Ct. Cl. 1982); see Fischbach & Moore Int'l. Corp. v.
after the Knowledge Requirement of Section 6982(d) of RCRA.

19 Jane F. Barrett & Veronica M. Clarke, Id. at 743.


15 United States v. Dee, 912 F. 2d at 741 (4th Cir. 1990).

14 See, e.g., United States v. Johnson & Towers, Inc., 740 F. 2d 1015, 1019 (4th Cir. 1982). (stating, in a prosecution under federal environmental law, that knowledge “may be inferred by the jury as to those individuals who hold the requisite responsible positions with the corporate defendants.”)


10 United States v. Schaffer, 600 F. 2d 1120, 1122 (5th Cir. 1979) (“The requirement of an intent to deceive coupled with reckless indifference to the truth or falsity of the statement is the equivalent of knowledge.”).


7 United States v. Jewell, 532 F. 2d 697 (9th Cir. 1976).

6 In Jewell, the evidence showed that the defendant and a friend declined the offer of a stranger they met in Mexico to buy marijuana but accepted $100 from him to drive a car across the border to Los Angeles. At trial the defendant testified that he was aware that the vehicle had a secret compartment in the trunk and that he checked the glove box, under the seat, and the trunk because he thought there was probably something illegal in the car. The defendant also testified, however, that he did not investigate the secret compartment. See id. at 700.

5 Hanlon, 548 F. 2d at 1100 n.7 (emphasis added).

4 Id. at 1101.


2 It should be noted that, although the FSA requires proof that a false statement is made both “knowingly and willfully,” the new WCCPEA imposes criminal liability when a senior executive commits a “knowing” violation of the certification provision—and there are separate, heightened penalties when the violation is “willful.”

1 See United States v. Schaffer, 600 F. 2d 1120, 1122 (5th Cir. 1979) (“The requirement of an intent to deceive coupled with reckless indifference to the truth or falsity of the statement is the equivalent of knowledge.”).

9TH CIR. CRIM. JURY INSTR. §5.7 (2000 ed.).

31 United States v. Evans, 559 F.2d 244, 246 (5th Cir. 1977).

30 The Ninth Circuit today provides a model Jewell instruction: You may find that the defendant acted knowingly if you find beyond a reasonable doubt that the defendant was aware of a high probability that [e.g., drugs were in the defendant’s automobile] and deliberately avoided learning the truth.


If it were not clear before, the events of September 11, 2001, removed any doubt among the residents of the United States that terrorism inside the nation’s borders is no longer a remote possibility. The United States now accepts the fact that terrorist attacks are a constant threat. However, as illustrated by the 1993 World Trade Center and 1995 Oklahoma City bombings, terrorism is neither new to the nation nor limited to the use of hijacked airplanes. In both earlier attacks, terrorists employed seemingly innocuous chemicals, used primarily in agriculture, to produce highly explosive and dangerous weapons. In the wake of those attacks, victims sued chemical manufacturers and distributors.

On the basis of these incidents, attorneys representing entities in the chemical industry face critical questions: Given the consistent threat of terrorist attacks and the previous use of chemicals in prior attacks, what are the legal responsibilities of chemical companies to aid in the prevention of future attacks and how can these companies avoid potential liability? The answer to these questions lies in an examination of several factors:

1) A chemical company’s legal right to inquire of its customers.
2) A chemical company’s duty to inquire of its customers.
3) A chemical company’s duty to protect its site.
4) A chemical company’s duty to comply with potentially applicable federal and state statutes.
5) Legislative reaction that may impose new responsibilities and liabilities upon chemical companies.

Although a chemical company may, given the current political climate, want to inquire of its customers more thoroughly, its legal right to do so may be limited by civil rights laws. For example, Sections 1981 and 1982 of the Civil Rights Act present questions regarding the right of a vendor to inquire of its customers. Section 1981, which addresses the making and enforcement of contracts, states, “All persons within the jurisdiction of the United States shall have the same right in every State and Territory to make and enforce contracts…” Section 1982 states, “All citizens of the United States shall have the same right, in every State and Territory, as is enjoyed by white citizens thereof to inherit, purchase, lease, sell, hold, and convey real and personal property.”

When making a claim under these provisions, a plaintiff must plead three elements:

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1) the plaintiff is a member of a racial minority, 2) the defendant had an intent to discriminate on the basis of race, and 3) the discrimination concerned one or more of the activities enumerated in the statute (i.e., the making and enforcing of a contract or refusal to sell property). Furthermore, case law interpreting these two statutes has created several controlling principles:
- Both statutes extend to purely private conduct.4
- The statutes apply to national origin as well as race.5
- The statutes apply to a denial of admission to a place of business, requesting a patron to leave a place of business, or a denial of service.6
- The failure to contract or sell must pertain to a present desire or attempt to contract or sell; the statutes do not cover prospective contracting or selling.7

Because the Civil Rights laws prohibit discrimination on the basis of race or national origin, Sections 1981 and 1982 can affect how a chemical company inquires about the intent and background of potential customers. Thus, liability might arise under these statutes if a chemical company were only to inquire of customers who appear to be of Middle Eastern origin. However, the laws do not preclude a denial of service for specific, enumerated, nonracially motivated reasons. A chemical manufacturer may therefore be able to limit its liability for a civil rights claim by asking objective questions to every customer. This policy should protect the interests of the chemical company while providing a defense against a claim that its inquiries were based upon race or national origin.

**RIGHTS AND DUTIES OF CHEMICAL COMPANIES**

While a chemical company needs to be concerned about whether it may inquire of its customers, at the same time it needs to consider whether it must inquire of its customers. The answer to this question lies in the special relationship that sellers of dangerous products have with their buyers and their communities. They owe a duty to not sell their product to individuals they know or should know will use the products dangerously.8 While generally “a defendant has no duty to control the conduct of another or to warn others endangered by another’s conduct,”9 exceptions arise when a special relationship exists between the defendant and the person whose conduct needs to be controlled or between the defendant and the person injured by the third party’s conduct.9 One type of “special relationship” occurs when the supplier knows or has reason to know that the user is likely to use the product “in a manner involving unreasonable risk of physical harm to himself and others.”10

In these cases, the supplier is subject to liability for physical harm caused by the injurious use.11 Thus, a person owes a duty of care “not to provide a dangerous instrumentality to an individual whose use of the instrumentality the supplier knows or has reason to know will result in injury.”12

The Restatement (Second) of Torts provides further guidance about the liability of sellers of dangerous products when the products are used in a criminal act by third parties to injure others. Section 448 of the restatement sets forth:

The act of a third person in committing an intentional tort or crime is a superseding cause of harm to another resulting therefrom, although the actor’s negligent conduct created a situation which afforded an opportunity to the third person to commit such a tort or crime, unless the actor at the time of his negligent conduct realized or should have realized the likelihood that such a situation might be created and that a third person might avail himself of the opportunity to commit such a tort or crime.

In the Oklahoma City bombing case, the court used precisely this section to analyze the conduct of Terry Nichols. The explosive
used in the 1995 bombing was created in part from two tons of ammonium nitrate fertilizer purchased by Nichols for $457.58 from a farm supply company in central Kansas.13

The victims of the bombing brought a class action against ICI, the manufacturer of the ammonium nitrate that was allegedly used to construct the bomb.14 The plaintiffs claimed that ICI was negligent in making explosive-grade ammonium nitrate available to the perpetrators of the bombing. In analyzing causation, the court stated that causation is generally a question of fact, but that it becomes a question of law when a jury cannot reasonably find the required proximate causal nexus between defendant’s act and the plaintiff’s injuries. Under Oklahoma law, the causal nexus is broken when there is a supervening cause.15 “To be considered a supervening cause, an intervening cause must be: 1) independent of the original act; 2) adequate by itself to bring about the injury; and 3) not reasonably foreseeable.”16 As the court noted, a tortious or criminal act is more likely to be seen as a supervening cause.17

Relying upon Section 448 of the Restatement (Second) of Torts, the court determined that a third party’s criminal actions are not foreseeable simply because of the existence of a “small fringe group or the occasional irrational individual, even though it is foreseeable generally that such groups and individuals will exist.” The court also noted that the plaintiffs could point to very few occasions in which ammonium nitrate was used by terrorists due, in part, to the complexity of making the bomb and the general unavailability of many of the necessary components. The court further noted, “We simply do not believe that this is a group which rises to the level of a ‘recognizable percentage’ of the population.”18 The court therefore found that 1) it was unforeseeable that the ammonium nitrate would be used in the attack, 2) the terrorists’ actions was a superceding cause, and 3) the manufacturer was not liable for the terrorist act.

In a similar action, individuals injured in the 1993 World Trade Center bombings filed a claim against the manufacturers, distributors, and sellers of the fertilizer used in the bombing for negligently selling their products to terrorists.19 Count III of the plaintiffs’ complaint stated that the “defendants are liable because they ‘failed to provide guidelines, instructions, and/or warnings to their distributors, retailers, dealers or other suppliers to confirm that buyers in the general and unrestricted public market have legitimate and lawful purposes for use of Defendants’ products.’”20

In ruling for the defendants, the court found that “first, the defendants owed no duty to warn the middlemen; [and] second, that plaintiff is unable to allege facts showing that such a warning would have prevented the harm.”21 The court noted that the plaintiffs could not provide a single case to support its theory that defendants had a duty to warn.22 Rather, the court noted that “no cases, even under the common law, support the existence of such a duty.”23 The court also found that the plaintiffs’ “failure to warn” argument failed because the plaintiffs were unable to allege facts showing that an adequate warning would have prevented the harm.24

In addition to inquiring of their customers, chemical companies may also have a duty to protect their sites.25 When the Federal Court of Claims addressed this issue in applying the Federal Water Pollution Control Act, it failed to impose such a liability on the companies.26 However, at least one state’s supreme court, the Supreme Court of Alaska, did impose liability on the operators of an explosives storage site for failure to protect that site when thieves broke into it and caused an explosion.27

Important guidance for chemical companies came on October 22, 2001, when, in the aftermath of the events of September 11, the American Chemistry Council, the Chlorine Institute, Inc., and the Synthetic Organic
Chemical Manufacturers Association released newly formulated Site Security Guidelines for the U.S. Chemical Industry. The Executive Summary to the guidelines recognizes the historical importance of security but also noted, “During this time of crisis, every effort is being made to secure chemical manufacturing facilities and safeguard employees and communities. This attention to safety contributes to national security as many specific measures adapted to improve safety have the added benefit of enhancing plant and community security.” Similarly, the introduction to the guidelines states, “In this era of heightened concern about terrorism, sabotage, and industrial espionage, managers at chemical facilities may have even more reason to attend to the security of their companies’ people, property and information.” Counsel to chemical companies or any other site storing hazardous substances or substances that may be used as implements of terror should be acutely aware of these guidelines. (See “The Site Security Guidelines,” this page.)

In addition to general site security issues, the guidelines also address employee policies and suggest that a company establish specific hiring protocols in order to avoid hiring someone who may pose a threat. Another suggestion is to establish protocols for the firing of employees in order to avoid the risk of disgruntled employees seeking retaliation. Finally, the guidelines recognize “other areas” in need of security such as operations (processing information, design diagrams, formulations, recipes, client lists, etc.), spoken information, documents, and computer networks. Finally, the guidelines also include helpful samples of site security analysis sheets, security models, a list of other helpful resources, and a federal agencies contact list.

Civil and Criminal Liability

A chemical company could be held both civilly and criminally liable if a chemical release occurred as a result of a terrorist act on the site or was perpetrated by an individual who obtained inherently dangerous chemicals from a site in the United States. First, a company could be held liable under numerous environmental statutes that impose both civil and criminal penalties. Second, in some cases more general criminal charges have been brought against corporations and corporate officers as a result of industrial disasters. For example, if a chemical facility were the subject of an attack, prosecutors could bring...
criminal charges against the corporation and its officers for failing to have in place adequate security and safety measures.\textsuperscript{41}

In addition, various civil claims have been asserted against companies whose products were involved in terrorists attacks, including negligence, negligence per se, negligent entrustment, negligent infliction of emotional distress, intentional infliction of emotional distress, products liability, and strict liability based on an abnormally dangerous activity.\textsuperscript{34} These cases involving civil claims against manufacturers touch upon the duty and liability of manufacturers.

For example, in the Oklahoma City bombing case, Gaines-Tabb v. ICI Explosives USA, Inc., the court dismissed the plaintiffs' negligence claim, finding that Oklahoma law requires a showing that “[a]n event or injury must be that which in a natural and continuous sequence, unbroken by an independent or supervening cause, produces the event or injury and without which the event or injury would not have occurred.”\textsuperscript{35} Further, the court agreed with the defendants and found that “[t]he bombing did not occur because Nichols and McVeigh acquired AN [ammonium nitrate] fertilizer. The bombing occurred only because of the terrorists' intent to cause harm.”\textsuperscript{36} The court found that the bombing was not a foreseeable act and was, therefore, a supervening cause.

Moreover, the court found that the defendant owed no duty to the plaintiffs “to anticipate and prevent the intentional or criminal acts of a third party.”\textsuperscript{37} Although the court accepted, for purposes of appellate review, the allegation that ICI knew that ammonium nitrate was previously used by terrorists,\textsuperscript{38} the court concluded that foreseeing “the intentional or criminal acts of third parties was so slight that reasonable persons in defendant ICI's position would disregard it.”\textsuperscript{39} The court also rejected negligence per se liability, ruling that alleged regulatory violations relating to the sale of explosive material were not the proximate cause of the plaintiffs' injuries.\textsuperscript{40}

Using similar reasoning, the Third Circuit, in Port Authority of New York and New Jersey v. Arcadia Corporation, dismissed the claims of the victims of the 1993 World Trade Center bombing against the companies that manufactured the fertilizer used in the bombing.\textsuperscript{41} The plaintiffs brought claims for negligence, products liability, and failure to warn. In affirming the district court's dismissal of all the plaintiff's claims, the Third Circuit held that “the manufacturer of a raw material or component part that is not itself dangerous has no legal duty to prevent a buyer from incorporating the material or the part into another device that is or may be dangerous....[M]anufacturers have no duty to prevent a criminal misuse of their products which is entirely foreign to the purpose for which the product was intended.”\textsuperscript{42} The court noted that reasonable foreseeability “applies to those future occurrences that, in light of the general experience within the industry when the product was manufactured, objectively and reasonably could have been anticipated.”\textsuperscript{43} The court agreed with the district court's conclusion that instances over the previous 50 years in which ammonium nitrate was used to create an explosive would not have indicated that the World Trade Center bombing was more than “a remote or theoretical possibility.”\textsuperscript{44}

While ammonium nitrate is not in and of itself dangerous without additional manipulation, the Fifth Circuit, nevertheless, followed virtually the same analysis as the Gaines-Tabb and Port Authority courts when it determined that the federal government was not liable for injuries caused by an inherently dangerous explosive that was unlawfully taken by a serviceman from an Air Force base. In that case, Garza v. United States,\textsuperscript{45} the plaintiffs sued the U.S. government under the Federal Tort Claims Act for injuries sustained by their minor son that were caused by the explosive. A serviceman found an unused explosive, stole it from the base (which had no distribution, use, or return procedures for the explosives), and gave it to his civilian roommate. The Fifth Circuit agreed with the trial court that, given the high degree of care imposed by the law to those who handle explosives, the government was negligent in its care.\textsuperscript{46} The court found, however, that the plaintiffs could not show that the government was the proximate cause of their son's injuries because the serviceman's theft was an intervening cause, thus making the injuries unforeseeable to the defendant.\textsuperscript{47} According to the court, “Evidence of past thefts in that area, or in that type of military operation, or some meaningful indication of the likelihood of thefts was required before such a foreseeability finding could be made.”\textsuperscript{48}

A court could still find the manufacture, storage, or sale of a hazardous substance to be an ultrahazardous or abnormally dangerous activity and, therefore, subject to a strict liability analysis, which does not require a finding of foreseeability.\textsuperscript{49} However, most courts, in assessing civil liability when a product is used by a third party in a criminal or tortious manner, undertake a foreseeability analysis to determine liability.\textsuperscript{50} Courts seem to absolve manufacturers and distributors in the absence of evidence that the supplier knew or should have known that the third party would put others at risk.

These cases involve the conduct of a corporate defendant. However, a corporate officer could also be held individually liable under the responsible corporate officer doctrine.\textsuperscript{51} In practice, the government has tried to link the corporate officer's responsibilities to criminal conduct in such a way as to permit a jury to infer that the corporate officer knew of the violation. Indeed, in every case in which a conviction has been upheld under the responsible corporate officer doctrine, the government established that the corporate officer either had actual knowledge, or deliberately shielded himself from knowledge, of the unlawful activity of his subordinates.\textsuperscript{52}

At least one court, however, has recognized the accused executive's right to raise as an affirmative defense his or her own inability to prevent the offense: “The theory upon which responsible corporate agents are held criminally accountable for 'causing' violations of the Act permits a claim that a defendant was 'powerless' to prevent or correct the violation to 'be raised defensively at a trial on the merits.'"\textsuperscript{53} Thus, a corporate officer could arguably rebut the claim that he or she is responsible for a terrorist act by arguing that he or she was powerless to prevent the act.\textsuperscript{45}

Both the Oklahoma City bombing and the World Trade Center bombing took place in the recent past. Similar conduct by terrorists (whether native or foreign) is becoming more common and arguably more expected. Given the terrorist attacks on September 11, the standard for determining what actions an individual or entity should reasonably recognize as foreseeable will likely change substantially. While the conduct of sellers, manufacturers, and middlemen has been excused as unforeseeable in the past, the same conduct may well be considered foreseeable (or conduct that an individual or entity “should have realized” would result in injury) after the events of September 11.

**LEGISLATIVE REACTION**

The recognition that these acts are becoming frighteningly more common is evidenced by two initiatives, one on the federal level and the other on the state, to further protect the public from potential chemical attacks. In Washington, Senator Corzine introduced a bill into the Senate on October 31, 2001, titled the Chemical Security Act of 2001.\textsuperscript{54} And on February 21, 2002, Assembly member Jackson introduced into the California Assembly the California Chemical Security and Community Protection Act,\textsuperscript{55} a bill similar to the Corzine legislation. Both bills recognize the public health and safety threats associated with accidents at, terrorist and chemical attacks on, and theft of dangerous chemicals from chemical sources. Although the California legislation did not pass in this year's session and it appears unlikely that the federal bill will be
enacted this year, counsel representing chemical companies should become familiar with the proposed legislation. Although a chemical company’s right to inquire of a customer to determine if the customer has a legitimate use for its product is limited by federal civil rights laws, companies may, in fact, have a duty to make such inquiry. Likewise, companies may have a duty to take steps to protect their site from theft or attack, as indicated by the promulgation of numerous industry guidelines and pending federal and state legislation. In the past, the majority of courts have failed to impose criminal or civil liability for harm caused by the criminal acts of third parties unless that third-party act was foreseeable. However, courts must now determine whether the events of September 11, 2001, when combined with the 1995 Oklahoma City and 1993 World Trade Center bombings and the political trend to protect the public from potential chemical terrorism, have served to put all industries that deal in hazardous substances on notice to consider the foreseeability of their products being used in a terrorist attack.

If courts determine that terrorist acts involving the use of once seemingly innocuous chemicals are now foreseeable, and that all industries that deal in hazardous substances are now on notice of that foreseeability, counsel representing these companies must be aware that action that once broke the causal chain and thus severed liability may now fail to exonerate chemical manufacturers. Chemical manufacturers, however, may be able to limit their liability by objectively inquiring of all customers to prevent misuse of the product, complying with the suggestions and guidelines set forth by organized bodies representing the chemical and similar industries, and by complying with state and federal statutes and regulations.

3 Id.
7 See Morris v. Office Max, Inc., 89 F. 3d 411 (7th Cir. 1996).
9 See id. at 484.
10 Id. at 485.
11 See id.
12 Id.
Arcadia Corp., 189 F. 3d 305 (3d Cir. 1999),

See id. at 310 (quoting Plaintiff Complaint).

See id. 30

See id. 29


See id. 27

See id. 26


See id. 25

See id. 24

See id. 23

See id. 22

See id. 21

See id. 20

See id. 19

See id. 18

See id. 17

See id. 16

See id. 15

See id. 14

See id. 13

See id. 12

See id. 11

See id. 10

See id. 9

See id. 8

See id. 7

See id. 6

See id. 5

See id. 4

See id. 3

See id. 2

See id. 1

See, e.g., Emergency Planning and Community Right to Know Act (SARA Title III), 42 U.S.C. §§11001-50, 11045(b); Clean Air Act, 42 U.S.C. §§7412(a), 7413(b)-(c); Occupational Safety and Health Act (OSHA), 29 U.S.C. §§654(a)-(d), 656; Resource Conservation and Recovery Act (RCRA), 42 U.S.C. §§6922, 6923, 6924, 6928(d), & 6972; Toxic Substances Control Act (TSCA), 5 U.S.C.S. §§2604, 2605, 2606, 2615, & 2619.


See id.

See id. 41

See id. 40

See id. 39

See id. 38

See id. 37

See id. 36

See id. 35

See id. 34

See id. 33

See id. 32

See id. 31

See id. 30

See id. 29

See id. 28

See id. 27

See id. 26

See id. 25

See id. 24

See id. 23

See id. 22

See id. 21

See id. 20

See id. 19

See id. 18

See id. 17

See id. 16

See id. 15

See id. 14

See id. 13

See id. 12

See id. 11

See id. 10

See id. 9

See id. 8

See id. 7

See id. 6

See id. 5

See id. 4

See id. 3

See id. 2

See id. 1


See id. at 1312.

Id. at 1315 (quoting Supplemental Memorandum in Support of Defendants’ Motion at 8).

Id. at 1316.

See id. at 1318.

Id.

See id. at 1320.

See id. at 1323.

See Port Authority of New York and New Jersey v. Arcadia Corp., 189 F. 3d 305, 313 (3rd Cir. 1999).

See id. at 313.

See id. at 318.

See id.


See id.

See id. 41

See id. 40

See id. 39

See id. 38

See id. 37

See id. 36

See id. 35

See id. 34

See id. 33

See id. 32

See id. 31

See id. 30

See id. 29

See id. 28

See id. 27

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See id. 13

See id. 12

See id. 11

See id. 10

See id. 9

See id. 8

See id. 7

See id. 6

See id. 5

See id. 4

See id. 3

See id. 2

See id. 1


See id. at 1312.

Id. at 1315 (quoting Supplemental Memorandum in Support of Defendants’ Motion at 8).

Id. at 1316.

See id. at 1318.

Id.

See id. at 1320.

See id. at 1323.

See Port Authority of New York and New Jersey v. Arcadia Corp., 189 F. 3d 305, 313 (3rd Cir. 1999).

See id. at 313.

See id. at 318.

Id.

See id. at 1323.

See Port Authority of New York and New Jersey v. Arcadia Corp., 189 F. 3d 305, 313 (3rd Cir. 1999).

See id. at 313.

See id. at 318.

Id.

See id. at 1323.

See Port Authority of New York and New Jersey v. Arcadia Corp., 189 F. 3d 305, 313 (3rd Cir. 1999).

See id. at 313.

See id. at 318.

Id.

See id. at 1323.

See Port Authority of New York and New Jersey v. Arcadia Corp., 189 F. 3d 305, 313 (3rd Cir. 1999).

See id. at 313.

See id. at 318.

Id.

See id. at 1323.

See Port Authority of New York and New Jersey v. Arcadia Corp., 189 F. 3d 305, 313 (3rd Cir. 1999).

See id. at 313.

See id. at 318.

Id.

See id. at 1323.

See Port Authority of New York and New Jersey v. Arcadia Corp., 189 F. 3d 305, 313 (3rd Cir. 1999).

See id. at 313.

See id. at 318.

Id.

See id. at 1323.

See Port Authority of New York and New Jersey v. Arcadia Corp., 189 F. 3d 305, 313 (3rd Cir. 1999).

See id. at 313.

See id. at 318.

Id.

See id. at 1323.

See Port Authority of New York and New Jersey v. Arcadia Corp., 189 F. 3d 305, 313 (3rd Cir. 1999).

See id. at 313.

See id. at 318.

Id.

See id. at 1323.

See Port Authority of New York and New Jersey v. Arcadia Corp., 189 F. 3d 305, 313 (3rd Cir. 1999).

See id. at 313.

See id. at 318.

Id.

See id. at 1323.

See Port Authority of New York and New Jersey v. Arcadia Corp., 189 F. 3d 305, 313 (3rd Cir. 1999).

See id. at 313.

See id. at 318.

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See id. at 1323.

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See id. at 313.

See id. at 318.

Id.

See id. at 1323.

See Port Authority of New York and New Jersey v. Arcadia Corp., 189 F. 3d 305, 313 (3rd Cir. 1999).

See id. at 313.

See id. at 318.

Id.

See id. at 1323.
Avoiding Common Mistakes When Selecting an Expert Witness

The following suggestions result from my experience serving as a witness, watching hundreds of other expert witnesses, and locating witnesses when serving as a confidential consultant. They are intended to help attorneys avoid common mistakes in selecting an expert witness.

Be careful when your potential expert is too quick to agree with your position. The expert should understand the opposing party’s position and thoughtfully explain why it is incorrect. An expert who is too agreeable with your position may become too agreeable with an opponent who provides additional information. You are better off with an expert who will reach a conclusion more thoughtfully and then hold to that conclusion under pressure.

When possible, select someone who has previously been successful in witness work and is enthusiastic about doing it again. Serving as a witness is an unusual and rigorous job. Many people are not well suited to what is required. Let’s face it: The first time we do anything, we are not likely to be very good at it. We fall; we get it wrong; we may even embarrass ourselves. The same thing is true when serving as an expert witness.

Test an expert’s ability to provide short answers that are directly on point. Experts who regularly provide longer-than-necessary answers will get themselves and your case into trouble.

Select witnesses who can explain their craft to the people who will serve on your jury. Most experts primarily work with highly educated and motivated peers and students who have the basic vocabulary and education necessary to be conversant in a specialized field of study. These people are nothing like your jury. Before employing an expert, test his or her ability to explain difficult concepts quickly in simple terms.

Identify people with energy and enthusiasm. The love that experts have for their field should be contagious. Experts should be quick to offer an illustration, chart, or analogy to enliven technical explanations. Don’t presume that a candidate will become engaging and charismatic with your good coaching.

Gain a general understanding of the methodology that your proposed expert will use. Does it appeal to common sense? Inquire whether the methodology will meet the standards required of the Daubert/Kumho cases in federal court or the applicable state standard (Kelly/Frye in California).

Obtain only those experts who have the premiere credential in their field. Avoid the numerous nearly meaningless credentials that require little more than an application fee and a basic test that most people pass. Also troubling are credentials that are given based on a point system that provides credit for unrelated experience. In contrast, most noteworthy credentials require difficult tests, lengthy experience requirements, and peer evaluation.

Insist that your proposed expert and the expert’s firm perform a comprehensive conflict check. This is particularly true of the large firms that have multiple service offerings. It is costly to learn of a conflict or contrary position after you have committed yourself. A conflict could even disqualify you. I have replaced firms that have not been conscientious in this area, and I am always surprised when this basic inquiry is ignored.

Investigate the writings of the expert you are considering. In some fields, regular publications are an indication of accepted expertise. But prior publications represent a minefield of potential conflicting positions or nuances that can be exploited by your opponent. Most jurors will quickly grasp the importance of a contradictory position. But since they do not live in the academic world, they will probably not care if the expert is publishing. It is difficult to predict the twists and turns of any litigation, so the safest course is to avoid a well-published expert.

The importance of all these issues requires that you begin your search for experts early. Your litigation plan should allow sufficient time 1) to identify the right expert, 2) for the expert to perform sufficient analysis (in the role as a confidential consultant) to know whether it will be helpful to your position, and 3) for you to alter your plan based on the consultant’s preliminary conclusions.

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Protecting Your Privacy on the Internet

In order to access the Internet, every computer is assigned a unique Internet Protocol (IP) address. When accessing the Internet from home (or from a firm that does not have a network), the IP address is assigned by an Internet Service Provider (ISP), such as AOL or Earthlink. In a networked corporate setting, each computer’s IP address is assigned by the IT manager. Every request by the user’s browser to a Web site being visited leaves a record of the IP address on that site’s Web server. While IP addresses from commercial ISPs are not assigned permanently to the user (as they typically are on a corporate network) and do not show your e-mail address or your name, an ISP can match (by reviewing log-in records) a specific IP address that it assigned at a specific time to a specific user.

This lack of privacy understandably concerns many computer users. As a result, a number of services exist to cloak a user’s Internet activity. By using a service such as Anonymizer (www.anonymizer.com), users can anonymously access any Web site and leave behind the IP address of the server of the Anonymizer company rather than their own. To use Anonymizer’s free cloaking service, users type the Web address of the site they wish to visit into the address box on the Anonymizer.com home page. The only downside to this free service is enduring the advertisement for the pay version of Anonymizer displayed at the top of each site visited. A one-year subscription without the advertisement and with additional security features is available for $29.95. The Cloak (at http://www.the-cloak.com) and Go Proxy (www.goproxy.com) offer similar services to users who are concerned with their privacy.

Hidden Spyware

In 1999, the FBI loaded “key logger” software onto the computer of reputed organized crime figure Nicodemo Scarfo Jr., recording every keystroke made on his computer. This allowed the FBI to capture some of Scarfo’s passwords, which in turn allowed them to decipher information from the encryption software he was using. In that case, the judge ruled that such key logging did not constitute an illegal wiretap. (Visit http://lawlibrary.rutgers.edu/fed/html/cr00-404-1.html for more information.). Similar software, which “hides” on a hard drive once it is installed, can be purchased for $50 to $200. Originally designed to monitor the Internet activity of children and allow government and corporations to track the computer use of employees, key-logging software is increasingly being used by spouses. Computer users should know, therefore, that a parent, spouse, or employer with access to their computers (and that may include remote access) can install software that tracks and reports every key stroke. Spector Soft (one manufacturer of spy software) has placed a warning in its software’s license agreement that “requires that you inform anyone you may monitor with Spector Soft products.” Users who fear for their privacy may not conclude that this clause entirely relieves their worries, however.

Spector Soft is not the only vendor of computer spyware. Desktop Surveillance (www.datarecoverysoftware.com) and Investigator (winwhatwhere.com) also record browser activity and track every program opened, every file saved, and every keystroke (including passwords). One application, Eblaster (found at http://www.spectorsoft.com/purchase/eblaster.htm), even sends a screen shot, via e-mail, whenever the user being tracked uses the computer on which it is installed.

Electronic Footprints

Even without hidden spyware, an ordinary computer offers a wealth of data to those who know where to look. Microsoft’s Internet Explorer and Netscape’s Communicator keep a record of Web sites the user has recently visited. The History file, which is stored on the computer’s hard drive, conveniently allows users to look back at a list of recently visited sites without having to bookmark or remember a site’s Web address. The History file is not password protected; therefore, someone who leaves a computer turned on but unattended makes this information available to anyone else who accesses the computer.

The History file can also yield important forensic evidence. For example, Washington, D.C., police reviewed the History file on Chandra Levy’s computer when searching for clues that her
Web use may have inadvertently left behind. They discovered the Web request for a map to the park in which her remains were eventually found. Internet Explorer’s History can be viewed by clicking the History tab on the Navigational tool bar. Netscape Communicator’s History can be viewed by clicking on Communicator on the Menu Bar, scrolling down to Tools and then selecting History.

Many Web sites also employ cookies as a means to identify visitors. A cookie is a small piece of information that the site being visited places on the visiting user’s local hard drive. Ostensibly, cookies are intended to function as a means to expedite a user’s return visits to favorite sites or personalize the information received from a site. For example, many users are familiar with how Amazon.com uses a cookie to identify returning visitors by name and to recommend products for purchase based on their prior buying history with Amazon.

Most cookies include the address of the site that placed them on the user’s computer. These addresses, in turn, may be accessed by other Web sites to track the user’s general Web usage, identifying sites the user has visited and perhaps even the user’s passwords for those sites. Cookies can also be accessed and deciphered by someone who sits at your computer and knows where to find the cookie file. Newer versions of Communicator and Explorer can be configured to warn users before cookies are added to their computers. This gives users the option of deciding whether or not to allow cookies to be placed on their computers. Users who enable this option may be surprised how many sites employ cookies, and how some sites employ multiple cookies.

Cookies are not only placed on users’ computers by Web sites that users visit but also by third-party advertisers featured on those Web sites. One can opt out of receiving third-party cookies from two of the largest online advertising clearinghouses by visiting Network Advertising Initiative (NAI, which is found at http://networkadvertising.org/optout_nonppii.asp).

Data Collection

This summer, the largest of these advertising clearinghouses, Double Click, settled a two-year investigation with the attorneys general of 10 states regarding the way Double Click collected and used identifying information about Web users. (See the agreement at www.oag.state.ny.us/press/2002/aug/aug26a_02_attach.pdf.) As part of the settlement, Double Click promised not to combine information it gathers (from cookies generated by various ads) to create de facto master profiles for individual Web users. Double Click is also developing a means by which Web users will be able to view the information about themselves that Double Click has compiled.

The most reliable and effective way of gathering personal data, however, remains simply to ask for it. Many Web sites offer free content or prizes in return for registration. Just as the amount of information requested of a user varies from site to site, so too do the intentions of the sites gathering this information. Before entering personal information into a Web site, be sure to read the site’s privacy policy. If the site does not have a link to its privacy policy prominently displayed near a form requesting information, one should be wary of supplying any information.

There are a number of other practices you can employ to protect your privacy:

• To discover if someone has placed key-logging software on your computer, programs such as Hook Protect (visit downloads.zdnet.com/3000-2092-10025791.html), Spy Guard (www.spyguard.com), and Spy Cop (www.spycop.com) claim to be able to detect and eliminate hidden key loggers.

• Periodically, clear your history files so no one can view your surfing history.

• Use the Cookie Manager in your browser to clean out unnecessary cookies already on your computer and to warn you when cookies are being placed on your hard drive.

• Also, set the Cookie Manager to reject third-party cookies.

• Install a firewall to protect against hackers.

• Shut down your computer when you are not using it so no one can view your history or cookies.

• Install a password to open your computer, so no one will be able to access your computer after it has been shut down.

• Use the free Anonymizer. If you download the pay software, your name is registered and you may be tracked if a court order is issued.

• Before entering any sensitive data (e.g., a Social Security or credit card number) into an interactive Web form, be sure you are in a secure and trustworthy site: Check that the address begins with “https” rather than “http” and that a small locked padlock icon appears in the lower left corner of the browser’s window.

As a final precaution, computer users may simply keep in mind that computers are designed to store, copy, and share information with great speed and efficiency. These capabilities may always be exploited in ways that will dismay a particular user. Users may take significant steps to protect their privacy online, but the best advice may be: If you want to keep it a secret, don’t do it on the Web.
A Trial by Jury
Reviewed by Angela J. Davis

The police followed a standard procedure when investigating a stabbing death. They canvassed New York-area hospitals for patients admitted with cuts on their hands or arms, anticipating that the perpetrator would have at least once slipped and stabbed himself. Monte Milcray had been admitted to St. Vincent’s Hospital in the West Village around 2:00 A.M. on the same day, his right pinky almost completely severed, his clothing and personal effects covered with blood. Milcray first told investigators that he was attacked by a posse of “five white males.” His story was suspicious. Later, after investigators—unexpectedly and somewhat amazingly—succeeded in finding Milcray’s discarded clothes in a trash container, forensic analysis found the blood splatters to be a mixture of the victim’s and Milcray’s own.

When Milcray emerged from the surgery that reconnected his finger, police invited him to make a statement. Tired and in pain, Milcray at last told police the story that, with only a few variations, he would stick with through his resulting criminal prosecution. According to Milcray, he was taking a break from work when a long-haired black woman came up to him on the street, told him he was sexy, and asked if he modeled. The woman introduced herself as “Veronique” and invited Milcray to her West Village apartment around midnight when he got off work. At 11:55 that night, Milcray punched out of work and, according to his statement, made his way across town to a neighborhood that he did not know well.

Veronique, wearing a short robe, greeted him at the door. The only light in the room came from a television that she had turned to an erotic channel. Milcray reclined and undressed. Moments later, Veronique opened her robe and revealed she was a he. Milcray scrambled for his clothes, whereupon Veronique pushed him to the floor and attempted to rape him. Milcray, by this time, had managed to partially pull up his overalls. Veronique continued to bear down on him, face-to-face, repeating, “Once it gets in, it doesn’t hurt.” At this point, Milcray reached for his knife, and, he asserted, stabbed Veronique once in the chest. When she did not relent but bore down more forcefully, Milcray reached around Veronique’s back in order to “hit him a few more times,” eventually slipping out of the weakening grasp and escaping to the street, where he discovered his own injury.

After Milcray communicated his Crying Game story to detectives, they arranged for him to write it down and then arranged for an assistant DA to videotape the statement. By the end of the tape, Milcray is seen holding his bandaged right arm, asking, “What’s going to happen next?” and, “Can I go home tonight?”

A year and one-half later, a jury was impaneled to determine Milcray’s fate. Enter D. Graham Burnett—historian of science, fellow at the Center for Scholars and Writers at the New York Public Library, former lecturer at Yale and Columbia, longtime admirer of Wallace Stevens—and recent recipient of a New York jury summons. With his Ivy League credentials, legal-scholar wife who had worked for the public defender’s office, and a copy of the New York Review of Books in plain view, Burnett expected to be excused: “I promised to give any healthy prosecutor hives.” When, during voir dire, the judge informed the members of the venire that they would be expected to follow and apply the law, “whether you agree with it or not, whether you think it is a good law or a bad one,” and then inquired if any potential juror had “a problem with that,” Burnett volunteered that if he thought the defendant might face the death penalty, “I would be inclined to acquit, even if I thought him guilty.” The judge responded that the death penalty was not relevant to the case at bar and expressed no further interest in Burnett’s comment.

Despite his expectation—one that many trial lawyers might have shared—Burnett was not excused. Instead, he became the jury’s foreperson and later wrote about his experience in a New York Times Magazine article and in the memoir, A Trial by Jury.
The 11 other citizens selected along with Burnett included 2 ad-copy writers, a software developer, a vacuum cleaner repairman, an interior decorator, a self-described "independent marketing executive," a part-time security guard, an actress/bartender, 2 others of "less clear occupation," and, improbably enough, another professor of the history of science.

They acquitted. We learn this in the book's opening chapter, when Burnett describes the 12 index cards, each scrawled with the words "not guilty" that allowed Milcray to walk out the courthouse in February 2000. Burnett left the courthouse only a few minutes before Milcray. He had kept the index cards folded in the breast pocket of his blazer. And, he tells us, he was crying.

It is impossible to say, based solely upon the memoirs of one juror, whether or not the jury reached the right decision, but Burnett's own account contains many suggestions that it did not. Aside from his own weeping upon exiting the courthouse, there are the candid descriptions of how (for Burnett and his fellow jurors) sequestration bred hostility toward "the system," how the jurors openly discussed jury nullification ("we can ignore the law"), and how in the end there was a funereal shared sadness ("we had let him go").

Burnett's personal account of how he and his fellow jurors came to this point is beautifully written and frequently mesmerizing. He writes with the economy and grace of a serious admirer of poetry and brings the lapidary precision of the scientific historian to many of the more subtle evidentiary questions raised by The People v. Monte Milcray. Although A Trial by Jury is a compact 180 pages, one has the feeling that nothing has been omitted. Witnesses—including more than one drag queen who testified for the prosecution that the victim and the defendant were, contrary to the Crying Game defense, seen together previously—come to life in Burnett's filmlike retelling of their testimony. When one of them was cross-examined about the presence of whips in the victim's apartment, she (as the witness preferred to be called) replied, "Honey, we all have whips." Burnett's description of the jury's deliberations and the experience of sequestration ("the most intense sixty-six hours of my life") are likewise informed by an uncommon sensitivity and psychological insight.

And yet...for all of Burnett's talent and grace, for all of the sharpening of his critical faculties at the grindstone of academia, there is an unmistakable—and unignorable—elitism that pervades his observations. At times the snobbery is obvious and harmless, as in his descriptions of his fellow jurors. He dubs one of them—the vacuum cleaner repairman, who also "moonlights in car stereo installation" and sports a rodeo tattoo—the Faludiman after feminist author Susan Faludi's tragic tale of the white working-class male: "big chest, big gut, big debt." There are other moments when Burnett's elitism is far more alarming. Perhaps the most disturbing moments in the jury deliberations came when Burnett arrogated to himself a secret agenda to engineer a hung jury. He entrusted his frustrations to a private journal and, to his credit, reproduces a particularly unflattering passage: "There are some jurors here who are such idiots, so thoroughly oblivious to good judgment or so thick (regardless of their intentions) that it seems improper to aid them in depriving a man of his liberty."

In the end, though, Burnett retreated from his secret agenda and lost at least some of his prejudices along with it. Indeed, it is the Faludiman himself who articulated the most breathtaking epiphany in the jury room, shattering stereotypes with a "vow of faithfulness; a repudiation of sophistication that suddenly seemed overwhelmingly sage." Whether or not justice was ultimately done in The People v. Milcray, Burnett's account is powerful testimony to the ability of the jury process to strip away prejudices—even ivory tower ones—and reveal more lasting truths.
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8 CLE hours

Tax Night 2002

ON TUESDAY, NOVEMBER 12, the Taxation Section and the California Society of CPAs will present a program on current developments in taxation. This annual program will offer three breakout sessions and one general session, during which presentations will be given in the following areas: compensation and benefits, corporate tax, entertainment tax, estate and gift tax, foreign tax, pass-through entities, procedure and litigation, state and local taxation, and tax-exempt organizations.

Following a new format this year, the program will offer each person the opportunity to attend three breakout sessions and one general session. At the general session, the keynote speaker will be Gregory F. Jenner of the Treasury Department. A hosted reception will follow the program, giving participants the opportunity to network with prominent taxation attorneys and CPAs. The program will take place at the Los Angeles Marriott Hotel, 333 South Figueroa Street, Downtown. On-site registration will be available starting at 3 P.M., with the program continuing from 3:30 to 7:05 and a hosted reception from 7:05 to 8:30. The registration code number is 8061K12.

$80—CLE+PLUS members
$120—Taxation Section members
$160—LACBA members
$190—all others
$210—all at-the-door registrants
3.25 CLE hours

Persuasive Legal Writing

ON WEDNESDAY, NOVEMBER 6, the Los Angeles County Bar Association will present an event on how to attain clarity in legal writing. Presenter Daniel U. Smith will focus on past examples of great writing by Thomas Jefferson and Abraham Lincoln as well as other models of clarity in the American idiom.

This course advocates brevity, simplicity, and clarity—the opposite of what most lawyers learned in college and law school. Those who attend can also learn to structure a persuasive argument and review the key steps for effective drafting and editing. Since 1995, this seminar has been presented by the Los Angeles County Bar Association, the San Francisco Bar Association, Continuing Education of the Bar, and by law firms across California.

This event will be held at the LACBA/LEXIS Publishing Conference Center, 281 South Figueroa Street, Downtown. On-site registration and meal will begin at 5:30 P.M., with the program continuing from 6 A.M. to 9:15. The registration code number is 7094K06.

$90—CLE+PLUS members (meal included)
$100—law students (meal included)
$160—LACBA members
$195—all others
3.25 CLE hours

The Los Angeles County Bar Association is a State Bar of California MCLE approved provider. To register for the programs listed on this page, please call the Member Service Department at (213) 896-6560 or visit the Association Web site at http://forums.lacba.org/calendar.cfm. For a full listing of this month’s Association programs, please consult the November County Bar Update.
The Promise of Law Analysis Technology

Applying artificial intelligence to the practice of law will improve efficiency and accuracy

Compared to other businesses and professions, the technology of automated analysis has lagged in the legal profession. While it is true that legal professionals have embraced more routine computer functions, the legal profession has substantially underutilized the potential of computer applications to accept factual input, apply reasoning, and reach conclusions for broad areas of issues. In contrast, other professions already employ automated analysis software programs to understand business trends, manage finances, plan taxes, and diagnose medical conditions. Now, however, promising developments are on the horizon for the legal profession as well.

There are several reasons why the legal profession has lagged in this area. One is the widespread belief that the law is not a good candidate for the use of analytical computer programs because legal reasoning requires judges and jurors to employ considerable human subjectivity when making decisions. For example, fact-finders in the legal setting frequently must determine whether someone acted like a reasonably prudent person acting under similar circumstances. In contrast, so goes the argument, business, financial, and health analyses are more similar to mathematical or scientific computations.

In addition, the development of automated legal analysis has suffered from a shortage of qualified authors. Not many attorneys understand computer programming or how to communicate concepts to information technology specialists. Similarly, programmers usually lack the schooling and experience in litigation or transactional work that is needed to conceive the most optimal innovations.

Despite these obstacles—and as wildly futuristic as it may seem—computerized legal reasoning already is technologically possible and potentially of tremendous value. While no respected expert would argue that artificial intelligence is close to becoming a substitute for human reasoning, existing programming languages are capable of greatly complementing the work of law professionals. Such innovations would go well beyond producing the customary search-engine-type lists of authorities and summaries that can be generated by keyword searches or the familiar services of Westlaw or Lexis.

Instead of relying heavily upon the legal professional to discern the significance of search results, interpret meanings, and apply facts, future programs will generate custom-tailored legal analyses, in proper grammar, based upon an attorney’s input of answers to form questions. Programs will be able to predict litigation results or recommend choices among transactional or advocacy approaches by mathematically weighing the numbers and types of factors and comparing applicable cases and statutes. Moreover, when a computer finds conflicting evidence, it will be able to assume different fact patterns and predict a possible array of results.

One trend supporting this work has been the development of software-interpreting, programmer-friendly languages that make it easier to bridge the gap between professionals speaking legalese and those using technical jargon. These languages employ visually appealing interfaces that utilize code editors that interpret scripts in a manner resembling familiar English grammar, instead of requiring the writing of foreign code. This makes it easier for the programmer to modify the programming codes, a skill previously known only to a few.

Legal professionals who become adept at using these new tools will reap the benefit of substantially improved efficiency and accuracy in their legal analyses. For example, automated analysis software could remind legal researchers of a forgotten law or case or point them towards recent developments or overlooked issues. Additional efficiency would be gained by advancing the starting point for research from the cold, unapplied broad outline of law that researchers currently find when employing secondary authorities to an already partially analyzed and tailored resource.

To get the ball rolling, advocates of automated analysis software need to put their more grandiose goals—however admirable—on the back burner and pursue a more limited approach at this time. This limited agenda will include:

- The identification by legal researchers of modest goals—including beginning with simpler laws—that require limited levels of reasoning. Complexity can be added gradually as the technology develops.
- The development of custom-tailored statements generated by programs based on code embedded with the human-reasoned writings of legal professionals, as opposed to attempting to create an automated replication of the human mind.
- The development of applications by professionals who understand both legal analysis and programming.

The future is already clear: In the next 5 to 10 years attorneys will be expected to consult artificial intelligence as an integral part of their client representation. This process will become the standard of care in the profession, and those who ignore it will increase their exposure to malpractice claims.

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