Taking Charge

John J. Collins is the Association’s 2004-05 president

PLUS

Defining Of Counsel page 15
Identity Theft Legislation page 21
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FEATURES

30 Taking an Old Route  BY MICHAEL A. GEIBELSON
The decades-old “route cases” provide a helpful rubric for analyzing contemporary trade secret litigation involving customer lists

37 Licensed to Bill  BY HOWARD B. BROWN
The courts have carved out exceptions to the rule that contractors who are not licensed at all times during a project can be denied compensation

Plus: Earn MCLE credit. MCLE Test No. 128 appears on page 41.

44 Reconstructing Justice  BY MICHAEL M. FARHANG
The coalition acted under authority of international law to restore and reform Iraq’s criminal justice system

67 Los Angeles Lawyer’s Annual Index to Articles
A complete guide to authors and articles published in Volume 26, March 2003-February 2004

DEPARTMENTS

10 President’s Page
Making law practice improvements job number one

BY JOHN J. COLLINS

14 Barristers Tips
Filing a proof of claim in bankruptcy

BY KIM TUNG

15 Practice Tips
The of counsel role and its implications for law firms

BY GREG SUESS AND RICHARDSON R. LYNN

21 Practice Tips
New California identity theft legislation

BY CHAD C. COOMBS AND KEENEN MILNER

26 Ethics Opinion No. 512
Confidentiality of fact and amount of settlement in settlement agreement

71 Computer Counselor
Free online legislative research

BY CAROLE LEVITT

76 Closing Argument
Resolving disputes with tag team mediation

BY STEVEN COHEN

74 Classifieds

75 Index to Advertisers
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Is A Malpractice Insurance Crisis Looming In Your Horizon? Are You Ready?

Over 15 carriers have withdrawn from the California market. Will your carrier be next? The changes in the marketplace are troubling. It is an unknown future. Non-renewals are commonplace. Some carriers can’t secure sufficient reinsurance to operate their professional liability programs. A major carrier was recently declared insolvent. Other carriers have been downgraded by A.M. Best. Severe underwriting restrictions are now being imposed. Rates are not certain. It’s all very unsettling.

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Welcome to the Los Angeles County Bar Association’s new year, which brings a changing of the guard for the Association’s office holders. With this new bar year comes a new look for Los Angeles Lawyer, now in its 27th year of publication. We have refreshed the style of our cover, the table of contents, and many other elements of the magazine. We hope you find the magazine visually more pleasing and easier to navigate. After all, it is our never-ending goal at the magazine to publish the articles that our readers want in a format that they like.

A welcome is also extended to R. J. Comer, who takes over for me as articles coordinator as I assume my tenure as the chair of Los Angeles Lawyer’s Editorial Board. Many thanks to Jerry Abeles, last year’s chair, for his excellent leadership of the board and the insightful words he wrote in his columns.

Becoming chair has caused me to reflect upon the years I have served as a member of the Editorial Board for the magazine. Serving as a board member has been an extremely rewarding and gratifying experience. Our monthly meetings bear a resemblance to a representative congress in which lawyers from various backgrounds and disciplines provide insight into the issues that are relevant to their constituents. Through this process, I have been exposed to a wealth of information from some of the best lawyers in Los Angeles County or anywhere, and this has contributed to my professional and personal growth. The meetings also are a constant reminder that the practice of law often must be a collaborative effort, since none of us is capable of knowing everything (although some clients expect this of us).

Through the dialogue that occurs at the magazine’s board meetings, I have gained perspective on a variety of topics, including substantive legal issues. Presumably, so have other board members. Although our method is not quite Socratic, I think that Socrates would approve of it.

As lawyers, perspective is one of the most important skills we can possess, whether our role is as an adversary, counselor, something in between, or as a business person operating the business of practicing law. Our ability to understand others—or our inability to do so—is often the difference between success and failure.

Stated altruistically, perspective helps us to provide solutions for our clients. Stated more cynically, perspective helps us strategize the chess moves necessary for our clients to gain an advantage in their transactions, litigation, or other matters. However stated or viewed, perspective is part of the reason why we are engaged by our clients.

The main purpose of this philosophical waxing is not simply to add some shine to the things we do at the magazine. Instead, I hope my words serve as a reminder of what we as lawyers need to do more often: listen and understand. There is always plenty of time to criticize and attack—two modes that we are likely to have perfected and for which we are well trained.

This is not another reminder about professionalism. It is a reminder about the process of the profession—a process that is as much about human interaction and subjective experience as it is about words, language, intellectual analysis, and objective ideas. Everyone who participates in negotiations, litigation, or other legal endeavors will bring different and subjective experiences to the process. When we understand that, and work harder to understand others, we have gained invaluable perspective, and we are better lawyers.

There is a lot of perspective to absorb in this issue of the magazine, as there will be in the months to come. As lawyers, we would not wish for anything less. Of course, Los Angeles Lawyer is only one tool available to assist lawyers. I hope that it continues to be a valuable one.

Gary S. Raskin is a principal of Garfield Tepper & Raskin, where his primary area of practice is entertainment litigation. He is the chair of the 2004-05 Los Angeles Lawyer Editorial Board.
The combined leverage, experience and resources of the Los Angeles County Bar Association and Aon are the surest way to get reasonable professional liability coverage. Many underwriters have fully or partially quit the business because of a reduction in surplus capital. Consequently, law firms face higher premiums for significantly reduced coverage...or no coverage at all, forcing them to go out of business!

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I COME TO YOU WITH DEEP ROOTS in this organization. I have been a member of the Los Angeles County Bar for approximately 42 years. My father was a member for many years before me. I have been a member of the Trial Lawyers section (now Litigation) since its formation. I have served on countless committees and chaired some. I had 3-years on the Board of Trustees in the early nineties and have now been an officer of the organization for approximately 5-years.

We are the largest local bar organization in the country aside from the ABA. We are the best bar association—voluntary or mandatory. Our Los Angeles County Bar Association and its 24,000 plus members ranks head and shoulders above any other similar group.

For the last several years my efforts have for the most part been directed toward improving the relationship between the courts and counsel. A recent survey disclosed that over 60% of our members regularly appear in a court of one type or another, i.e., civil, criminal, domestic relations/family court, probate, children’s court, landlord/tenant, etc. It has been my intent to focus on this area and as President it will continue to be my number one priority to make improvements for the practicing attorney dealing with the court system.

In the Spring of 1996 I was asked by President Laurie Zelon and president elect Shelly Sloan, to chair the Blue Ribbon Commission which was to address the delivery of services by the Los Angeles County Superior Court. A very strong committee was appointed consisting of former bar presidents, bar leaders, top trial people, judges and court administrators. A few names you might recognize—on the Bar side—Argue, Chaleff, Edmon, Feldman, Garcetti, Judge, Heinke, Ordin, Phillips, Quinn, Sloan, Schnegg, Span, Vaughn, Warren and Zelon—a remarkable group of people who have established a strong history of support for the Association. The late John Argue was able to obtain funding for the work that was to be undertaken through the generosity of the Haynes Foundation. The Executive Officer of the Court, Jack Clark, and Judges Klausner, Parkin and Chavez were important members of the group.

Over the subsequent four years focus groups were established in three court districts—Norwalk, Van Nuys and Central. The focus groups included every type and kind of stakeholder in the court system, i.e., law enforcement, local politicians, business leaders, court employees, jurors, litigants and attorneys. The Blue Ribbon Committee was assisted by two Ph.D’s from the University of Southern California School of Public Affairs/Public Administration—Dr. Robert Biller and Dr. Brian Borys.

A preliminary report was submitted in November, 1998 and a final report in June, 2000. Some of the conclusions addressed very sensitive issues concerning the manner in which the court system conducts itself and delivers justice to the stakeholders. Many recommendations were made on subjects such as judicial accountability, monitoring of users after trial by means of questionnaires, restructuring of court governance to give those in leadership positions the power to administer effectively free from the backlash from disgruntled judicial officers, elimination of local Local Rules, and, random selection replacement of Trial Judges after the exercise of C.C.P. §170.6 challenges. Many of the recommendations have been implemented, but sad to say, a good number have been ignored.

When the Blue Ribbon Commission issued its report our court system consisted of something in the area of 350 bench officers. With the advent of unification the compliment of judicial officers increased to well over 600. It is impossible today for an attorney to stay informed concerning the various Judges on the bench.

Your Association through the leadership of Executive Director Walch and Presidents Rex Heinke and Robin Meadow developed an electronic system for monitoring cases and judges. To date over 1,800 firms have signed up for the searchable register on-line service. When announced this novel program was met with a degree of judicial resistance. Some months ago a further refinement was brought on line in the “Judge Your Judge” program. This was also met with judicial criticism and we have addressed these concerns of the court leadership. We will continue these programs but with a responsible oversight group, including two judges from the Executive Committee of the Court, that will insure fairness, and when

John J. Collins, a partner with Collins, Collins, Muir & Stewart in Newport Beach, is the 2004-05 president of the Association. He can be reached via email at jcollins@ccmslaw.com.
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Please take the time to go online and give your input relative to experiences with Judges before whom you appear. We are just as anxious to applaud the efforts of those judicial officers who dispense justice in a fair and courteous manner as we are to try and modify the conduct of a troublesome few. I have had the privilege of speaking at a number of enrobing ceremonies for new Judges. I have always suggested that the golden rule of trial work be observed—“treat those attorneys and litigants coming before you as you would have wished to be treated when you were appearing in court as a practicing lawyer”. Courtesy and civility should never suffer because of the quest for good stats. Your informed, unbiased, input will be of tremendous assistance to your brother and sister lawyers and to the court leadership that has promised to work with us.

Your bar association programs enable you, the member, to have immediate electronic access to the critical information needed to conduct litigation and evaluate judicial officers. I can think of no greater service provided by the bar than these programs.

In some courts lawyers and litigants still do not receive the degree of courtesy and respect they deserve from court personnel. We have worked very hard with court leaders over the years to gain better treatment for the stakeholders that daily enter our vast array of court facilities. In the year to come I promise you that our efforts will continue in this direction. We look forward to continued, and perhaps stronger, cooperative spirit as we work with the court leadership.

We acknowledge that the Judicial Branch must be independent and it also must be adequately funded. We will continue to support the Los Angeles County Superior Court and do all we can to secure the adequate funding that is necessary for further operation of the third branch of government. Our voice will be heard.

We will not rest in our effort to ensure courtesy, respect and fair treatment to all users. Civility must be a two way street. We will oppose all efforts in the area of speedy resolution that do nothing more than deny justice to the parties. The system must not be driven by statistics.

There will be no lack of attention to the many other valuable programs we conduct. An integral part of my presidency will be the avoidance of venturing into areas of social issues which are controversial and/or divisive. The cohesiveness of the Association and staying on course with our mission is paramount to the agenda of a few.

I look forward to the coming year. Please be active and lend us your many talents.
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Filing a Proof of Claim in Bankruptcy

AN ATTORNEY WHOSE PRACTICE AREA does not include bankruptcy may nevertheless receive a call someday from a client who has a claim against a person or entity that has filed for bankruptcy. To help this client, the attorney should be familiar with the basics of filing a proof of claim, even if the attorney eventually decides to refer the matter to a practitioner who is experienced in bankruptcy matters.

The first task is to determine if the client’s claim meets the Bankruptcy Code’s definition. The term “claim” is defined in 11 USC Section 101(5). The attorney may also need to look at other sections and definitions, research case law, and consult treatises and practice guides to determine if a claim exists, and if so, whether it is secured or unsecured, and what type of secured or unsecured claim it is. The attorney should also remind the client that by filing a proof of claim, a creditor asserts the right to receive a distribution from the bankruptcy estate, but that filing a claim does not guarantee a distribution. Additionally, a proof of claim may be objected to and disallowed in whole or in part, and even if a proof of claim is valid, a creditor can expect to receive nothing if there are no assets that remain in the bankruptcy estate.

The attorney also must make sure that the deadline to file a proof of claim has not passed.

In a chapter 7 or chapter 13 case, the deadline for filing a proof of claim is called the “claims bar date” or the “bar date.” In chapter 7 or chapter 13 cases, all proofs of claims must be filed within 90 days of the initial meeting of creditors as described in 11 USC Section 341(a). This initial meeting is sometimes called the 341(a) meeting. There are, however, exceptions to this 90-day bar. In chapter 11 cases in general, the bar date for filing proofs of claim is set by the court, typically on motion by the debtor-in-possession.

If the client is already listed on the debtor’s schedules, he or she should have notice of the claims bar date, if one is set. Clients who did not receive notice, or their attorneys, can check online through the PACER system. On PACER, the bankruptcy court maintains the docket of each bankruptcy case, the dockets of adversary proceedings, and the claims register of pending bankruptcy cases. The PACER system for the central district can be accessed at www.cacb.uscourts.gov. Once the attorney has accessed the case, a click on Claims should access the claims register. The claims bar date, if any, should be at the top of that page.

Parties that fail to timely file a proof of claim may file a motion requesting the bankruptcy court to permit the claim to be filed late. The bankruptcy court may grant the motion if the failure to file the proof of claim on time was a result of excusable neglect.

Although a client may have a valid claim and be entitled to file a proof of claim, counsel should research the risks for creditors who file a proof of claim. These risks include: submitting the creditor to the jurisdiction of the bankruptcy court, giving the debtor and other creditors the right to conduct discovery regarding the creditor’s claim, and waiving the right to a jury trial. If the risks do not outweigh the potential value of the claim, the next step is to file. A proof of claim must be filed on, or substantially conform to, Official Form 10. A copy of this form may be downloaded from the bankruptcy court Web site. If a claim includes prepetition interest or other charges, such as attorney’s fees, counsel should make sure to include a detailed breakdown of these expenses as part of the claim. In addition, a summary sheet should be attached showing how the total amount was computed.

If a claim is based on a writing, a copy of the writing must be attached to the proof of claim.

The claim must be filed in accordance with Rules 3002(b) and 5005 of the Federal Rules of Bankruptcy Procedure. Pursuant to Rule 5005, a proof of claim must be filed with the clerk of the bankruptcy court in the district where the bankruptcy case is pending. Attorneys should also check the local rules of the district in which the bankruptcy case is pending. A copy of the bankruptcy court local rules may be downloaded from the bankruptcy court Web site.

Next, a copy of the filed proof of claim should be served on the debtor or debtor-in-possession and any trustee appointed in the case. After filing the proof of claim, it is advisable to check later that the bankruptcy court has the claim properly registered. To do so, it is necessary to get a copy of the claims register or access the claims register through PACER. Once the claims register is accessed, counsel should check that the claim is on the register and confirm that the details of the claim have been properly reflected.

Although a client may have a valid claim and be entitled to file a proof of claim, counsel should research the risks for creditors who file a proof of claim...If the risks do not outweigh the potential value of the claim, the next step is to file.

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1 See Timothy J. Yoo, Personal and Small Business Bankruptcy Practice in California §7.31 (2004).
2 Id. at §7.26. See also J. Scott Bovitz, et al., Colliers on Bankruptcy and Personal and Small Business Bankruptcy Practice in California (CEB, 2004).

Kim Tung practices in bankruptcy matters with Danning, Gill, Diamond & Kollitz, LLP, and is president-elect of the Barristers.
The Of Counsel Role and Its Implications for Law Firms

IF AUSTIN POWERS, THE INTERNATIONAL MAN OF MYSTERY, were somehow affiliated with an American law firm, he would certainly be of counsel to that firm. Why? Because the term “of counsel” seems to be equally shrouded in mystery, with most lawyers not entirely clear about what the term actually means. Despite this, a growing number of law firms are creating of counsel positions for lawyers—and these of counsel lawyers play a variety of differing roles depending on the firms they join. The ethical, legal, and practical issues raised by of counsel relationships are as varied (and often as ambiguous) as those roles.

Traditionally, many retired partners, in relinquishing their role in the law firm partnership, have taken the of counsel title, which gives them an office, administrative support, and the chance to ease from the scene gracefully. At a minimum, their knowledge and experience continue to be a firm resource. However, these counsel often act as if no one told them they were retired, putting in as many hours and bringing in as much business as before.

Some politicians who are turned out of office become of counsel. Typically, they become affiliated with firms in Washington, D.C., or the Washington office, perhaps opened just for them, of a home state firm. The arrangement gives them a salary with a minimum of conflicts of interest while they plot their political return or ease into the work routines of the private sector. In exchange, the firm obtains a rainmaker with political connections. One of the ultimate Washington insiders, former Senator Bob Dole, is special counsel—a variation on of counsel—in the Washington, D.C., office of Alston & Bird. Former governors and state office holders are more likely to join law firms as traditional partners in most states but may also be brought into a firm as of counsel. Former California Governor Pete Wilson, for example, is of counsel to the Los Angeles office of the 850-lawyer Bingham McCutchen firm and a principal in the Bingham Consulting Group.

The of counsel designation covers other substantial but part-time relationships, such as law professors who work on occasional cases for a firm, in-house corporate counsel, and lawyers practicing on behalf of a legal foundation. The rubric also can extend to newly hired lawyers during a trial period of association.

During the last 20 years, the of counsel position has broadened to accommodate the changing practice of law. It has been used, for example, as a substitute for a “mommy track” to partnership. Indeed, during the 1990s, the number of women holding of counsel positions tripled. Also, of counsel positions allow law firms to evaluate lateral hires before making them partners. In addition, the of counsel title has been bestowed on lawyers whose primary value to a firm is their business or technological expertise as well as on lawyers who want to combine jobs in law, business, politics, and education. The of counsel designation also allows small law firms to expand their areas of expertise and prestige by adding specialists as of counsel with the benefit of little or no increased overhead.

Many law firms are relaxing rigid definitions of lawyers’ roles by allowing greater flexibility and creativity in devising career paths. In part, these relaxed definitions result from an increasingly competitive business environment in which attracting and retaining top legal talent is difficult. Competition has been particularly fierce in the technology sector; indeed, during the boom of the late 1990s, it was not unusual for law firms to watch their clients poach the best and brightest of the firms’ lawyers. A solution devised by some firms was to allow their lawyers to become of counsel while “lending” them to client companies.

The rise in of counsel positions is also attributable to the fact that many lawyers are unsatisfied with their careers and are looking for alternatives. A lawyer’s tasks often can be tedious and monotonous. For some lawyers, an of counsel role provides them with the opportunity to try something new and different while maintaining their connection with their law firm.

In the past, a lawyer would typically work for one, or perhaps two, law firms during his or her lifetime. It is now common practice for lawyers to jump from firm to firm, from firm to client, from firm to political office, or from firm to university. The of counsel position enables law firms to smoothly move lawyers in and out of their firms while preserving and building relationships and contacts.

A survey of the 50 largest law firms in the Los Angeles County area reveals that, on average, the firms have designated about 6 percent of their lawyers as of counsel. A review of the background information of the of counsel lawyers, as provided on law firm Web sites, showed no significant correlation between the of counsel designation and character.

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characteristics such as age, years practicing law, practice area, experience, gender, education, interests, and the like.

**Defining Of Counsel**

The regulations of the American Bar Association reflect the evolution of the of counsel role. The ABA’s 1969 Model Code of Professional Responsibility required those listed on a law firm’s letterhead as of counsel to have a substantial connection with the firm, perhaps to prevent firms from “renting” the names of famous lawyers who do no real work with the firms. The Model Code was interpreted to require “a close, daily, in-house association” between the lawyer and the firm, excluding the possibility that a lawyer could be of counsel to more than one firm or a firm employee. The ABA’s view expanded so that, by 1972, the Model Code was interpreted to permit a lawyer to be of counsel to a maximum of two law firms, not just one.

In 1990, the ABA Commission on Ethics and Professional Responsibility recognized four kinds of relationships covered by the of counsel designation: 1) part-time practitioners, 2) retired partners, 3) probationary partners, and 4) permanent senior attorneys. At the same time, four other relationships were excluded from the of counsel category: 1) lawyers working together on a single case, 2) lawyers forwarding or receiving legal business, 3) lawyers and firms involved in collaborative efforts who were otherwise unrelated, and 4) outside consultants. The “daily contact” requirement was eliminated, and entire law firms were permitted to be of counsel to each other.

In California, Rule 1-400(E)(8) of the Rules of Professional Conduct states that a lawyer cannot be designated as of counsel unless the relationship between the firm and the of counsel lawyer is “close, personal, continuous, and regular.” California also excludes partners, associates, officers, and shareholders from the of counsel designation. There is no limit, however, to the number of firms to which a lawyer or another firm can be of counsel, provided that the relationship between a firm and the of counsel lawyer or firm possesses the attributes listed in Rule 1-400 (E)(8).

**Structuring the Relationship**

The of counsel relationship should be governed by a written agreement, which should specifically set forth the relationship between the firm and the of counsel lawyer, clearly state the compensation arrangements (even if it only says that there will be separate written agreements for each case on which the of counsel lawyer works), and provide the manner of terminating the relationship, among numerous other issues.

At the outset of the relationship, the firm and the of counsel lawyer should discuss (and possibly document) the expectations of the firm and the lawyer for the of counsel relationship and review their respective clients and contacts to determine if actual and possible conflicts of interest may exist. This process should be revisited periodically as the working relationship between the firm and the of counsel lawyer evolves.

Because there is, by definition, a “close, fluid, and continuing relationship between a firm and an attorney who is of counsel to that firm,” disqualification rules apply just as if the of counsel lawyer were a member of the law firm. As California Supreme Court Justice Ming Chin wrote:

For attorneys in the same firm to represent adverse parties in the same litigation is so patently improper that the rule of disqualification is a per se or “automatic” one….Conflicting representations that would disqualify all of a law firm’s attorneys are not more acceptable when an attorney of counsel to the firm creates the conflict. Clients, and the public, should expect confidentiality and loyalty from attorneys who effectively declare they practice law in a close, personal, and continuing association. These legitimate expectations would be frustrated if a firm could represent one party in litigation while an attorney of counsel to the firm represented an adversary in the same case.

Consider a scenario in which a partner in a law firm accepts a position as general counsel with a client company, and the law firm changes the partner’s status in the firm to of counsel. This arrangement maintains the strong tie between the client and the law firm, allows other lawyers in the firm access to the former partner’s knowledge, gives the former clients of the former partner the sense that the former partner is still involved in their matters, and allows the firm to continue to draw upon the former partner’s contacts. The of counsel role for the former partner preserves and strengthens the relationships among the former partner, the law firm, and the clients affected by the change in the former partner’s status at the firm.

This new relationship does, however, raise several legal and ethical issues. Suppose, for example, the of counsel lawyer reviews and

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**Checklist for Of Counsel Lawyers**

Lawyers who seek to become of counsel need to clarify their relationship with their law firms and their clients. Addressing the factors in this list will help of counsel lawyers avoid the traps that may ensnare the unwary.

- **Written Agreements.**
  - Consider whether to craft a written agreement with the partnership with which you want to be affiliated as of counsel.
  - If you or the partnership choose not to do this, examine all the reasons why.
  - If you and the partnership decide to have a written agreement delineating your relationship, address carefully what it should include. Consider whether the agreement should cover compensation, indemnification, insurance, marketing (including letterhead, business cards, Web site, firm literature, and the like), and benefits.

- **Communication.**
  - Decide who should be notified of the new of counsel relationship. This group will include clients and insurance companies, among others.

- **Conflicts of Interest.**
  - Cross-check the law firm’s clients with your clients. Set forth your affiliations, including service on boards of directors, memberships in associations, and any positions with nonprofit organizations.
  - Cross-check your contacts with the law firm’s contacts.
  - Decide if written conflict waivers should be obtained if the list of clients, affiliations, and contacts reveal any conflicts with the law firm.
  - Calendar annual, semiannual, and quarterly meetings between the firm’s ethics committee leadership or consultant and you to review your of counsel relationship. Discuss the relationship periodically between meetings.

- **Client Review.**
  - Do you have a business or financial relationship with a client in addition to your of counsel relationship with a law firm? If so, make sure you clearly communicate information about the of counsel relationship, including the conflicts it creates, to the client.
  - If a client is a publicly traded company, you should review the client’s articles, bylaws, and board charters to determine if any action is required.
  - Determine if a client has a written ethics policy. If it does, you should ensure that your of counsel relationship complies with the policy. —G.S. & R.R.L.
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approves the law firm’s bills on behalf of the company for which the lawyer is now general counsel. The lawyer’s tendency, whether consciously or subconsciously, may be to scrutinize the bill with more deference than the lawyer may have otherwise done, particularly if the lawyer is still receiving compensation from the law firm. The general counsel of counsel lawyer owes fiduciary duties to the company (as an executive officer and lawyer) and the law firm. Those interests may not always be aligned. In that event, the company should have the firm’s bills reviewed by an independent officer at the company, such as the chief financial officer, or may even hire an independent legal auditor.

Or suppose the law firm represents two clients within the same industry, and the of counsel lawyer is the general counsel to one of the two clients. Under this scenario, the of counsel lawyer may have direct access to a competitor’s confidential attorney-client information or proprietary information, which could expose the lawyer to the risk of facing allegations regarding the theft of trade secrets. California clearly treats the of counsel lawyer as a partner or associate for purposes of conflict of interest and disqualification rules.19 Therefore, the lawyer’s dual relationships to the firm as well as one of the clients must be fully disclosed to both clients. It would not be surprising if the competitor decides not to retain a client, but it may be will ing to continue being represented by the firm because of the value it places on the firm’s services and the trust it has in the of counsel lawyer. In the entertainment industry, for example, the degree of importance ascribed to relationships may explain a competitor’s lack of objection to a conflicting representation.

When structuring an of counsel relationship, careful consideration should be paid to California’s attorney-client privilege and the treatment of confidential information. Under California law, a client, whether or not a party to an action, may assert the privilege to prevent disclosure of confidential communications between the client and its lawyer. The communications protected by the privilege include information that is transmitted between a client and its lawyer during the course of their attorney-client relationship and that is not disclosed to any third persons other than anyone present during a consultation to further the interests of the client.20

If a lawyer is both a general counsel to a company and of counsel to a law firm that has been engaged by a competitor of the company, the ability of the company and its competitor to assert the attorney-client privilege may be adversely affected. Specifically, Section 962 of the California Evidence Code provides: “Where two or more clients have retained or consulted a lawyer upon a matter of common interest, none of them, nor the successor in interest of any of them, may claim a privilege under this article as to a communication made in the course of that relationship when such communication is offered in a civil proceeding between one of such clients (or his successor in interest) and another of such clients (or his successor in interest).” For the clients addressed in this statute, the attorney-client privilege may not exist in any disputes among the clients that may arise in the future in connection with the action for which the lawyer was retained.21 Thus, both the general counsel’s employer and the law firm’s other client must be advised of the potential conflict of interest and the possible loss of attorney-client confidentiality if the companies ever become adversaries in a later proceeding.

Professional Conduct

Of counsel lawyers frequently are board members and/or executive officers of public companies listed on the New York Stock Exchange, AMEX, and NASDAQ. As mandated by the Sarbanes-Oxley Act of 2002,22 the Securities and Exchange Commission has adopted rules that establish standards of professional conduct for all attorneys who handle securities law matters on behalf of public companies.23 The SEC increasingly is turning its enforcement focus to lawyers, and of counsel lawyers should take note. The attorney conduct rules establish specific guidelines that a securities lawyer must follow when representing a public company.24 Specifically, an attorney who represents a public company must comply with the SEC’s “up the ladder” reporting requirement if the attorney believes there is evidence of a material violation by the company of federal securities laws. The attorney must report the violation to the company’s chief legal officer (CLO) and possibly the chief executive officer (CEO).25 Is there a conflict of interest if the CLO or the CEO is also of counsel to the company’s law firm? Maybe. The rule requires that the reporting lawyer must be satisfied that the violation is being addressed in a competent manner. This means if the CLO or CEO has not properly handled the issue, the lawyer must report the violation first to the company’s audit committee, then to the committee of independent directors, and finally to the full board.26 The Sarbanes-Oxley regulations permit the reporting lawyer to bypass the CLO/CEO level and report the possible violation directly to the audit committee, independent directors, or the full board when reporting the violation would be futile27—as it may be when the CLO has a conflict of interest caused by his or her position as of counsel to a law firm.

Section 406 of Sarbanes-Oxley also requires public companies to disclose whether they have written ethics policies (and if they do not, why this is so).28 Of counsel lawyers who have a relationship with a public company should obtain a copy of the company’s code of ethics to determine if 1) the company is complying with the statute and 2) the of counsel relationship is in compliance with the ethics policy.

Section 301 of Sarbanes-Oxley requires that each member of the audit committee of a publicly traded company be “independent.”29 Attorneys who are of counsel to a law firm representing a company and also a member of that company’s audit committee are not independent. The new rules state that an attorney who represents a company, including of counsel attorneys, cannot longer serve on the company’s audit committee.

Of counsel lawyers who are officers, managers, directors, or interest holders of a client company should be aware that the company’s articles of incorporation or formation as well as bylaws and operating agreements may govern the relationship between the of counsel lawyer, the law firm, and the company. A company’s bylaws, for example, may specifically address issues of independence, conflicts of interest, and interested party transactions—all matters that may have an impact on the of counsel relationship. In addition, many of counsel lawyers belong to other professional associations and organizations that may regulate their professional conduct. For example, an of counsel lawyer also could be a partner in an accounting firm, requiring an examination of the rules and regulations governing accountants.

When a law firm creates an of counsel position or takes on a new client brought in by an of counsel lawyer, the firm must take into consideration the mandate of Rule 3-500 of the Rules of Professional Conduct, which states that “a member shall keep a client reasonably informed about significant developments relating to the employment or representation.” For example, a client company should be informed that a member of its board of directors is also of counsel to its law firm, and that this relationship creates a conflict of interest. The of counsel lawyer and the law firm should notify the client in writing, setting forth in sufficient detail the nature of the relationship and how it may affect the client.

Liability

A law firm may be liable for the torts committed by a lawyer who is of counsel to the firm and employed by the firm. The liability flows from the doctrine of respondent superior or because the firm negligently chose or supervised the of counsel lawyer.30 In the
case of nonemployee of counsel lawyers, the firm will be liable vicariously if it created actual authority for the of counsel lawyer or if there is apparent authority. A firm may create vicarious liability by authorizing an of counsel lawyer to perform specific tasks on the firm’s behalf, such as 1) signing checks, 2) entering into contracts, 3) negotiating and settling fees and fee disputes, 4) engaging clients, and 5) hiring and firing attorneys and staff. The firm may also be vicariously liable if the of counsel attorney performs these tasks without authority but no objection is made.

Law firms and their of counsel lawyers must address the issue of malpractice insurance. Law firm malpractice insurance policies typically treat of counsel lawyers the same as partners and associates. While the malpractice history of each lawyer in the firm (including claims filed, paid, or litigated) must be disclosed to the insurance carrier, the exposure created by of counsel lawyers is no greater than for any other lawyer. Indeed, if the of counsel status reflects a part-time role, the exposure may be even smaller.

Careful attention also must be given to letterhead designations, which can minimize common liability claims for malpractice. Listing the of counsel lawyers on law firm letterhead without designating the lawyers as of counsel or incorporating the of counsel lawyer in the law firm name creates an impression that the of counsel lawyers are partners or employees. Malpractice insurance carriers often require that a firm create letterhead that specifically designates the of counsel lawyers, and the firm should only use that letterhead in matters on which the of counsel lawyers are working. The best practice is for of counsel lawyers to use their own letterhead for all aspects of a representation that they undertake on behalf of the law firm.

Few law firms follow that practice, however, apparently because they believe that listing their of counsel lawyers on their letterhead adds prestige to their firms or serves to promote their firms. Even when a firm uses discrete sets of law firm letterhead for each of counsel, of counsel lawyers should not use the law firm letterhead for matters unrelated to the law firm because that would convey the impression to clients and others that the law firm was lending its support to the of counsel when it was not.

Suppose a law firm is being sued for malpractice and fraud, and all of the partners and of counsel lawyers have been named personally. Whether an of counsel lawyer can be held personally liable along with the partners in a malpractice and fraud action is a question of fact. Under California general partnership law, the partners of a law firm can be liable for the debts of the partnership. As one California court held, “A person dealing with a partnership usually is in no position to know of special agreements between the partners and thus cannot be charged with knowledge of such agreements absent specific notice.” In determining whether an of counsel lawyer with a firm is cloaked with the apparent authority of a partner, a court will look at several factors:
1) Does the firm have a written partnership agreement, and if so, is there a written agreement between the of counsel lawyer and the firm?
2) How is the of counsel lawyer presented to clients, the community, local bar associations, and the State Bar?
3) What do the firm’s letterhead and website state about the of counsel lawyer?
4) How is the of counsel lawyer presented on his or her business card?
5) How is the of counsel lawyer compensated—as an independent contractor who receives a 1099 or as a partner who receives a distribution of profits?
6) Does the law firm’s malpractice insurance application mention the of counsel lawyer and, if so, with what words?
7) Has the of counsel lawyer guaranteed any of the firm’s obligations (such as a lease)?

Compensation
Compensation arrangements for of counsel lawyers are as varied as the types of counsel relationships. For an of counsel lawyer engaged by a firm as a salaried consultant, there may be a range of bonus configurations, including those based on billable hours, billed and collected revenue, and percentage of contingency awards. An of counsel lawyer could receive a profit participation in the firm, which is often coupled with a straight gross revenue share of the fees paid by the of counsel lawyer’s clients. Of counsel lawyers may be hired as independent contractors. Still other of counsel lawyers are provided with office space, administrative assistance, and medical benefits.

Of counsel lawyers should be aware of Rule 2-200 of the Rules of Professional Conduct when entering into compensation arrangements with a law firm. If there is a financial arrangement between a firm and an of counsel lawyer that involves the of counsel lawyer being paid a percentage of a client’s fees paid to the firm, the rule requires a full disclosure to the client of the arrangement and the written consent of the client to its terms.

The expanding definition and use of the of counsel role allows law firms and lawyers greater flexibility in structuring their relationships. Generally, this flexibility is good for the practice of law, but it can also create problems. Careful consideration at the beginning of the of counsel relationship and per-
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Oddic reviews of the relationship can help to minimize conflicts of interest, determine liability, and assign risk, as well as create a long-lasting and profitable working alliance. Law firms and of counsel lawyers must make sure that they obtain appropriate conflict waivers, ensure confidential and privileged communications with their clients, and disclose fee-sharing arrangements when appropriate.

1 http://www.bobdole.org/current.html.
2 http://www.bingham.com/bingham/webadmin/documents/radBOF5C.pdf.
4 Round the Industry: Many Associates View Partnership Undesirable or Unattainable, 18 Legal Management No. 6 (1999).
6 The authors reviewed the lawyer rosters of the 50 largest law firms in “The 2004 List” in the Los Angeles Business Journal.
11 Id. See also Harold G. Wren & Beverly J. Glascoc, The Of Counsel Agreement 30 (2d ed. 1998).
13 Cal. Rules of Prof’l Conduct R. 1-400(E)(8).
14 Id.
16 Wren & Glascoc, supra note 11. This was written for the Senior Lawyer Division of the ABA and is the best resource for written of counsel agreements.
18 Id. at 1139-40.
19 Id.
20 Evid. Code §952.
24 See http://www.lacba.org/ShowPage.cfm?PageID=2663. This practitioner-oriented Web site contains a number of links and documents regarding Sarbanes-Oxley.
30 Wren & Glascoc, supra note 11.
32 Corp. Code §16306(a).
New California Identity Theft Legislation

**IN RECENT YEARS**, California has enacted a number of identity theft laws focusing on businesses and the need to protect consumer information at the source. Accordingly, business attorneys need to become familiar with this new legislation in order to protect their firms' client information and to guide clients through the new responsibilities that they face.

The new laws reflect that identity theft is the fastest growing crime in America. In September 2003, the Federal Trade Commission published a survey that found that in the past five years, 27 million Americans became victims of identity theft. In the 12 months preceding the survey, identity theft victims numbered 9.91 million. The same survey found that identity theft losses to businesses and financial institutions in 2002 totaled $47.6 billion. To make matters worse, the number of actual crimes may far exceed these statistics, considering that not all victims report the crimes. The two primary locations for identity theft crime are Washington, D.C., and California.

Since technology has made it easy for anyone so inclined to commit identity theft and, in many cases, get away with it, lawmakers have recognized the need to protect the private information that thieves can use to obtain credit in a person's name. This data includes social security numbers, driver's license numbers, and account numbers. In response, California lawmakers have enacted significant new legislation that obligates businesses to adequately protect confidential information, confirm the identity of the persons to whom they extend credit, and notify customers of breaches in security affecting personal information.

In California, one of the most significant recent laws is Senate Bill 1386. The bill, which became effective on July 1, 2003, requires businesses to provide prompt notice to California resident customers of any breach of security involving unencrypted personal data. The law applies to any person or business that does business in California, even if located out of state, and that owns or licenses computerized data that includes personal information. As such, the law is of very broad application. Notice is required as long as the business reasonably believes that an unauthorized person accessed personal information. Personal information consists of the individual’s first and last name (or first initial and last name) along with one of the following: 1) social security number, 2) driver’s license or California identification card number, or 3) account number or credit or debit card number if acquired in combination with any required security code that would allow access to the account. However, notice is not required if the information is encrypted.

Notice may be provided in writing or electronically. In addition, the business may be able to use a substitute form of notice if the cost of providing written or electronic notice would otherwise exceed $250,000 or involve more than 500,000 persons. Upon demonstrating that either of these conditions apply, the business may notify affected persons by e-mail, conspicuous posting of the notice on a Web site, or notifying media statewide. Businesses should first notify law enforcement agencies of the breach as notice to customers may be delayed if the agency determines that notification will negatively affect a criminal investigation.

The cost of notifying customers is a major concern to businesses and raises many questions. When does one reasonably believe security has been breached? Did the breach affect all customers or a few? Is notice required to all customers in the database if the business suspects a breach but does not know its extent? The answers to these questions may have to be determined in future court decisions.

Businesses would be ill-advised to take the new law lightly. The bill provides that an injured customer may bring a civil suit for damages and/or seek an injunction in addition to any other rights and remedies the customer may have. Although it may be difficult for an individual customer to trace an identity theft to a leak from a particular business, a business that fails to follow the law and that is exposed for not doing so could face a significant and expensive class action.

California lawmakers also have passed laws requiring businesses to verify the identity of persons seeking credit. Assembly Bill 1610, approved July 7, 2003, requires any person who uses a credit report and who determines that the consumer’s first and last name, address, or social security number on the consumer’s credit application do not match the information shown on the credit report (within a reasonable degree of certainty) to take reasonable steps to confirm that the application is not a result of identity theft. This new law also prohibits any person who uses a consumer report from extending credit (not including increases in open-ended credit plans) if the person has...
received notice that the consumer has been the victim of theft, unless the person takes reasonable steps to verify the identity of the consumer. Violation of this law is expensive: Consumers are entitled to recover actual damages, attorney’s fees, court costs, and punitive damages of up to $30,000 for each violation.

Along the same lines, Senate Bill 25, effective July 1, 2004, requires a person who uses—in connection with a loan, purchase, lease, or rental of goods—a consumer credit report that contains a security alert to take reasonable steps to verify the consumer’s identity. Like Assembly Bill 1610, Senate Bill 25 also does not apply to an increase in existing open-ended credit. The user of the report must take reasonable steps to contact the consumer by telephone if the consumer has requested telephonic verification with the security alert. Senate Bill 25 also limits use of a consumer’s social security number. Businesses will no longer be able to print or embed an individual’s social security number on a card required for access to the business’s products or services. With certain exceptions, such as applications and forms to establish, amend, or terminate an account, a consumer’s social security number may not be placed on any documents mailed unless otherwise required by law. Businesses will also be prohibited from requiring anyone to send a social security number over the Internet unless the connection is secure or the social security number is encrypted.

California has also passed legislation restricting use of a person’s driver’s license information. Effective January 1, 2004, Senate Bill 602 limits, among other things, a business’s use and retention of driver’s license or identification card information to 1) verifying age or authenticity of the card, 2) complying with any legal requirement to maintain such information, 3) transmitting the information to a check service company for approval, and 4) collecting or disclosing personal information required to report, investigate, or prevent fraud. A business may not retain such information for any other purpose, and a violation constitutes a misdemeanor punishable by imprisonment of up to one year and/or a fine of up to $10,000.

Another concern is the sharing of nonpublic information between businesses. Senate Bill 1, effective July 1, 2004, limits the ability of financial institutions to sell a consumer’s personally identifiable financial information that the financial institution obtains or is created as the result of a transaction with or services provided to the consumer. “Personally identifiable financial information” includes information that a consumer provides in connection with a credit application, account balance and payment information, and information from a consumer report. It also includes information as to a consumer’s prior business with the financial institution, information obtained in connection with collecting on or servicing a loan, and information obtained through an Internet cookie or an information collecting device on a Web server.

**SB 1 and the GLBA**

Senate Bill 1 is intended to afford greater privacy than under the federal Gramm-Leach-Bliley Act. The GLBA requires that financial institutions notify consumers of what information is protected and how the institution will protect and share the information. Under the GLBA, consumers have the right to notify financial institutions that they do not want their personal information shared with entities not affiliated with the financial institutions, although financial institutions may still share such information with its affiliates. In contrast, Senate Bill 1 requires that financial institutions must affirmatively obtain the consumer’s written consent before sharing a consumer’s nonpublic personal information with nonaffiliated third parties. In addition, Senate Bill 1 provides that a financial institution may not share information with an affiliate unless it annually provides notice of such disclosure to the consumer who does not object. A financial institution may maintain a common computer database with an affiliate and not violate this rule as long as the use of nonpublic personal information is not further disclosed except as otherwise may be permitted.

For the GLBA, “financial institutions” include firms that provide real estate settlement, tax planning, and tax return preparation services. While the GLBA does not explicitly exclude law firms, one district court recently ruled that “Congress did not intend for the GLBA’s privacy provisions to apply to attorneys who provide legal services in the fields of real estate settlement, tax-planning and tax preparation…. “ In contrast, Senate Bill 1 expressly provides an exception for professional firms. Specifically, Senate Bill 1 states that a financial institution does not include “any provider of professional services, or any wholly owned affiliate thereof, that is prohibited by rules of professional ethics and applicable law from voluntarily disclosing confidential client information without the consent of the client.” Therefore, law firms should find themselves outside the scope of Senate Bill 1.

Senate Bill 1 provides that the attorney general or the regulator with jurisdiction over the financial institution may seek penalties for violations. Financial institutions that improperly disclose or share a consumer’s personal financial information are liable for a civil penalty up to $2,500 per violation. If the unlawful disclosure involves more than one consumer but is due to negligence, the civil penalty may not exceed $500,000. However, if the disclosure results in identity theft, the penalties are doubled.

Certain provisions of Senate Bill 1, however, appear to be preempted by the federal Fair and Accurate Credit Transaction Act of 2003 (FACTA), which President George Bush signed into law on December 4, 2003. FACTA amends the Fair Credit Reporting Act and provides, among other things, that federal banking agencies must establish guidelines for financial institutions to help prevent identity theft. Specifically, the law’s purpose is “to prevent identity theft, improve resolution of consumer disputes, improve the accuracy of consumer records, make improvements in the use of, and consumer access to, credit information, and for other purposes.” FACTA limits the extent to which affiliated entities may share personal consumer information for solicitation for marketing purposes. FACTA requires that such sharing be disclosed to consumers and that consumers be given the opportunity to prohibit such sharing. FACTA does not, however, cover sharing with nonaffiliated entities.

**Additional Legislation**

The problem of identity theft in California has become so serious that Assembly Bill 1610 and Senate Bills 1 and 25 are not the only laws that have been created to address it. Other recent California legislation includes:

- Senate Bill 27, effective January 1, 2005, which requires businesses to notify customers of any disclosure of information to a third party for direct marketing purposes.
- Assembly Bill 1294, approved September 30, 2003, which prohibits debt collection once the creditor has been provided evidence that the debt is due to identity theft.
- Assembly Bill 68, effective July 1, 2004, requiring Web operators to list their privacy policy on their sites and notify users of any third parties who will receive such information.
- Assembly Bill 1772, approved July 21, 2003, and Senate Bill 684, approved September 24, 2003, which extend a person’s right to obtain information on unauthorized loan applications to other types of transactions, namely mail receiving and forwarding services and office or desk rental services.
- Senate Bill 684 also defines “application” and incorporates changes proposed by Senate Bill 602.

Not all the new laws contain specific enforcement provisions or provide a mechanism for consumers to recover damages. For example, neither Senate Bill 1 nor Assembly Bill 68 expressly provide for damages for consumers. Consumers may be able to assert
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- Barstow
- Big Bear
- Central
- Joshua Tree
- Needles
- Rancho Cucamonga
- Victorville
- San Diego Superior Court
- Central
- East County
- North County
- South County
- San Francisco Superior Court
- San Joaquin County Superior Court
- San Luis Obispo County Superior Court
- Santa Barbara County Superior Court
- Central
- Lompoc
- Santa Maria
- Santa Cruz Superior Court
- Watsonville
- Shasta County Superior Court
- Sierra County Superior Court
- Salinas Superior Court
- Sonoma Superior Court
- Stanislaus County Superior Court
- Tehama Superior Court
- Trinity County Superior Court
- Tulare County Superior Court
- Tuolumne Superior Court
- Yuba County Superior Court

**FLORIDA**
- Fifth Judicial Circuit (Ocala)
- First Judicial Circuit (Defuniak Springs, Okaloosa, Santa Rosa Beach)
- Twelfth Judicial Circuit
- Thirteenth Judicial Circuit (Tampa)
- Fifteenth Judicial Circuit (W. Palm Beach)

**GEORGIA**
- Atlanta Superior Court

**INDIANA**
- Marion County Superior Court

**LOUISIANA**
- Atlantic Superior Court

**MARYLAND**
- Second Circuit Court (Centerville)
  - Talbot County Circuit Court

**MICHIGAN**
- Fourth Judicial Dist. (Monroe)
  - Fifteenth Judicial Dist. (Massie)
- Twenty-Sixth Judicial Dist. (Benton, Minden)

**MISSISSIPPI**
- Nineteenth Judicial Circuit
- Twentieth Judicial Circuit
  - Natique (Naples)
  - Ft. Myers

**NEW JERSEY**
- Atlantic Superior Court

**NEW MEXICO**
- Dona Ana County (Las Cruces)
- First Judicial Circuit (Santa Fe)

**NEW YORK**
- New York Supreme Court
- New York City
- New York State Court
- New York County

**TEXAS**
- 22nd District Court (San Marcos)
- 33rd District Court (Burnet)
- 75th District Court (Liberty)
- 105th District Court (Corpus Christi)
- 133rd District Court (Houston)
- 219th District Court (McKinney)
- 238th District Court (Midland)
- 286th District Court (Levelland)
- 325th District Court (Ft. Worth)
- 360th District Court (Ft. Worth)
- 400th District Court
- County Courts
  - Hillsdale-#1
  - Midland
  - San Angelo
  - Tom Green

**UTAH**
- Fourth Judicial District

**WASHINGTON**
- Adams County Superior Court
- Spokane County Superior Court

**WEST VIRGINIA**
- Fourth Judicial Circuit

**UNITED STATES DISTRICT COURT**
- Eastern District of California
  - Fresno
  - Sacramento
- Northern District of California
  - Santa Clara
  - Southern District of California
  - San Diego

**UNITED STATES BANKRUPTCY COURT**
- Central District of California
  - Los Angeles
  - Riverside
- Eastern District of California
  - Fresno/Bakersfield
  - Modesto
- Sacramento
- Northern District of California
  - Oakland
  - San Francisco
  - San Jose

**HAWAII**
- Northern District of Hawaii
- Honolulu
- Maui
- Kauai
- Hawaii
- Oahu

**ILLINOIS**
- Northern District of Illinois
  - Chicago

**NEW JERSEY**
- USDC-New Jersey
- Newark

**NEW YORK**
- Southern District of New York
- District of Oregon

**OREGON**
- District of Oregon
claims for unfair business practices under California Business and Professions Code Section 17200 based on violations of the new legislation. Although this application of the law has yet to be proven, courts have broadly interpreted Section 17200 to provide individuals with causes of action for unlawful practices under civil or criminal federal and state laws. However, remedies are generally limited to restitution and injunction. Nevertheless, businesses could face expensive class action lawsuits for violating the new laws even if the new laws do not specifically provide for these actions.

Compliance

Since many of the new laws have already gone into effect, law firms and their business clients need to get systems, policies, and procedures in place quickly to protect client and customer information. Compliance with the new laws requires action in three areas: technology, policies and procedures, and training. Three lines of defense, including proactive and reactive tools, should be used to ensure comprehensive protection of information. The most effective strategy is to implement them in the following order, working from inside the company or firm toward the outside.

The first line of defense is encryption. For Senate Bill 1386, even if there is a breach, information that is encrypted is considered protected and no notice is required. As such, one means to avoid liability is to properly encrypt customer information.

All sensitive data should be encrypted, but businesses should choose encryption technology carefully. Although in theory any encryption is breakable by an intruder, the question is, how long is it going to take? If, with all the computing power on earth, it would take 200 years to decrypt the data, for all practical purposes, the encryption code is unbreakable. When implementing an encryption protocol, remember that the greater the strength of the encryption, the longer it will take to decrypt the information. For large amounts of data, the process can be extremely time-consuming and may hinder the efficient conduct of business. Therefore, managers should consider that credit cards, for example, expire in four years, so an encryption code only needs to be powerful enough to protect credit card data for four years plus one day. There is no need to do more.

Working outward from the encryption of core information, the second line of defense is an intrusion detection system, a software solution that continuously monitors the network and computers for breaches. This is a reactive, not proactive, tool that will issue an alarm when an intrusion has been detected. Unfortunately, intrusion detection systems are often not properly deployed, which results in frequent false alarms and endless adjustment, which can be extremely labor-intensive and frustrating.

The third line of defense is firewalls—hardware and software boundaries that prevent unauthorized access to files on the network. They are only effective in combination with encryption and intrusion detection systems. Technology in and of itself, however, cannot protect a business’s information from security breaches. In fact, many of the new laws involve the discreet handling of data and verification of identity. Effective protection is accomplished by a combination of technology and policies and procedures. These include technology and personnel matters, including:

- Rules that restrict access to the server and to certain categories of information to employees who require that access to conduct business.
- Policies and procedures for encrypting data; where, when, and how to save data; and when and how to purge data.
- Policies on what information may be

### Recent Anti-Identity Theft Legislation Affecting Businesses

<table>
<thead>
<tr>
<th>BILL</th>
<th>AFFECTED STATUTES</th>
<th>SUMMARY</th>
</tr>
</thead>
<tbody>
<tr>
<td>Senate Bill 1386</td>
<td>Civil Code §§1798.82, 1798.84, 1798.29</td>
<td>Requires notice to California resident customers of any security breach involving unencrypted personal data</td>
</tr>
<tr>
<td>Assembly Bill 1610</td>
<td>Civil Code §1785.20.3</td>
<td>Requires reasonable steps to verify identity of credit applicant if certain information does not reasonably match consumer credit report</td>
</tr>
<tr>
<td>Assembly Bill 1772 and Senate Bill 684</td>
<td>Penal Code §530.8</td>
<td>Extend the right of persons who discover unauthorized loan applications (or similar forms) in their names to obtain information on the unauthorized transaction</td>
</tr>
<tr>
<td>Assembly Bill 1294</td>
<td>Civil Code §1788.18</td>
<td>Prohibits debt collection once evidence of identity theft is provided</td>
</tr>
<tr>
<td>Senate Bill 602</td>
<td>Civil Code §§1785.11.1, 1785.11.2, 1799.1b, 1798.90.1 et seq., Penal Code §§530.6, 530.8 Public Utilities Code §2891</td>
<td>Limits the use and retention of driver’s license or identification card information</td>
</tr>
<tr>
<td>Senate Bill 25</td>
<td>Civil Code §§1785.11.1, 1785.11.6, 1785.15, 1786.60, 1798.85</td>
<td>Requires reasonable steps to verify a consumer’s identity if the consumer report contains a security alert and limits the use of a consumer’s social security number</td>
</tr>
<tr>
<td>Senate Bill 1</td>
<td>Financial Code §§4050 et seq.</td>
<td>Limits the ability of financial institutions to share nonpublic consumer information</td>
</tr>
<tr>
<td>Assembly Bill 68</td>
<td>Business and Professions Code §§2575 et seq.</td>
<td>Requires Web operators to list their privacy policies on their sites and notify users of any third parties who will receive personal information</td>
</tr>
<tr>
<td>Senate Bill 27</td>
<td>Civil Code §§1798.83, 1798.84</td>
<td>Requires notice to customers of any disclosure of information to a third party for direct marketing purposes</td>
</tr>
</tbody>
</table>
obtained and how it may be stored and used, such as the limits on use of social security numbers and driver’s license information that are imposed by Senate Bill 25 and Senate Bill 602.

- Policies on the maintenance and periodic changing of passwords.

- Disclosure policies for informing customers or clients how their personal information will be used, as is required by Assembly Bill 68 for Web operators and by Senate Bill 27 in the case of information provided to third parties for marketing purposes.

- Policies concerning information that leaves the business location or that is moved from one office to another on site (disks, thumb drives, laptops, and so on).

- Policies on granting access to information to third parties, including affiliates, and consideration of whether consumer approval is first required.

- Procedures for physically safeguarding access to company computers, including personal computers used by company staff. With today’s technology, a small monitoring device can be placed on a personal computer without the user’s knowledge and collect data for an extended period. These procedures may involve limiting access to the company’s workplace in general.

- Procedures for safeguarding home computers. In many firms and companies, employees take work home or use their home computers to check their company e-mail. If a firm’s attorneys work from home via a secure connection to the office, that security is useless unless home computers are also protected from third-party access. The IT departments of many firms and companies have already begun to visit employees’ homes to secure computers. In addition, if employees take laptops off site to a client’s location or a coffee shop, those laptops must be secured.

- Policies and procedures on verification of identity as required by Assembly Bill 1610 and Senate Bill 25.

- Procedures for regular or constant systems monitoring to detect breaches immediately so they can be disclosed to customers or clients.

- Human resource policies and procedures such as background checks on new hires.

- Other applicable restrictions, such as limits on debt collection activities against identity theft victims, as provided by Assembly Bill 1294.

Protection is not a matter of technology alone. The best defenses are documented and consistently enforced policies. While it is impossible to develop procedures to address the complexities of every single new law, businesses will need to proceed with caution and common sense: Keep and use only the information that is needed to conduct business, and keep it safe.

Businesses must also adequately educate personnel. Company personnel, especially those accepting or evaluating credit requests, and IT personnel and other staff collecting or handling customer information, must be educated on the new policies to prevent improper extension of credit or acquisition, use, or release of information. For example, the best intrusion detection software is useless if employees release information over the phone to someone they do not know just because the caller has identified himself or herself as “from the phone company” or “from the bank.”

Implementation of the procedures necessary to comply with the new laws obliging businesses to protect against identity theft will take teamwork. Management must focus on identity theft. Although the specific departments or individual employees of a firm or company who will be involved with identity theft compliance issues will depend on the size and organizational composition of a business, the IT department will most likely need to take a leadership role. IT professionals are in the best position and are the most skilled to monitor and enforce security. Again, policies and procedures are needed to ensure that IT personnel and other sensitive employees fully grasp the critical need to protect private information and the urgent need to notify the appropriate individuals immediately of any problems with security enforcement or breaches.

Companies with IT departments not prepared to handle the additional burdens of the new laws might decide to outsource some of the functions. It will pay off in the long run to hire IT and security experts to implement the most effective hardware and software solutions and to help develop policies and procedures that support the technology. If a breach has already occurred, computer forensics experts can often follow a trail back to the culprit.

Recently enacted legislation emphasizes the critical need to be proactive about protecting consumer information. As most businesses do not monitor new legislation to consider whether it applies to their companies, it is critical that law firms remain focused on the issue and keep clients apprised of new laws. In addition, law firms will be better able to serve their clients if they are also knowledgeable about technologies that can offer protection from identity theft. In the current climate, it is urgent that all firms and companies enhance their security, with the help of outside IT experts if necessary, and create strong policies and procedures to support the technology solutions.

2 Lawmakers have also addressed the need for privacy of personal information in other contexts, for example in the area of medical information, under the federal Health Insurance Portability and Accountability Act of 1996 (HIPAA). For more information, see Alexander S. Gareeb, Practical Implications of HIPAA, Los Angeles Lawyer, Apr. 2004, at 12.
3 Senate Bill 1386 adds Civil Code §1798.29, amends and renumbers former Civil Code §1798.82 as Civil Code §1798.84, and adds Civil Code §1798.29.
4 Civ. Code §1798.29(e).
6 Civ. Code §1798.29(g)(3).
7 Assembly Bill 1610 amends Civil Code §1785.20.3.
8 Senate Bill 25 amends Civil Code §§1785.11.1, 1785.11.2, 1785.13, 1785.15, 1786.60, and 1798.85.
9 Civil Code §1785.11.1 provides that consumers may elect to place a security alert on their credit reports by request to a consumer credit reporting agency, in writing or by telephone. The security alert notifies the user of the report that the consumer’s identity may have been subject to identity theft. Civil Code §1785.11.2 provides that a consumer may elect to place a security freeze on the consumer’s credit report by making a request in writing via certified mail. The freeze prohibits the consumer credit reporting agency from releasing the consumer’s credit report or any information from it without the consumer’s express authorization.
10 Senate Bill 602 amends Civil Code §§1785.11.1 and 1785.11.2, Penal Code §§530.6 and 530.8, and Public Utilities Code §2891. Senate Bill 602 also added Title 1.81.2 to Division 3, Part 4, of the Civil Code (beginning with §1799.80.1) and Civil Code §1799.1b. SB 602 is called the Identity Theft Prevention and Assistance Act.
11 Senate Bill 1, the California Financial Information Privacy Act, adds Division 1.2, commencing with §40350, to Title 1.81.2 of the Financial Information Privacy Act.
15 Senate Bill 27 amends Civil Code §1798.84 and repeals Civil Code §1798.83. Civil Code §1798.84 provides that any customer who is injured as a result of violation of the title is entitled to sue for damages and a civil penalty of $500 per violation or $3,000 per violation in cases in which the violation is found to be willful. The customer may also seek an injunction and reasonable attorney’s fees.
16 Assembly Bill 1294 adds Civil Code §1788.18. Civil Code §1788.30 provides that any debt collector who violates this title shall be liable to the debtor for actual damages the debtor sustains in addition to a penalty of not less than $100 and not greater than $1,000 and reasonable attorney’s fees. The debt collector is not liable if the debt collector shows that the violation is unintentional and occurred despite proper procedures in place to avoid such violation or the debt collector corrects or cures the violation as provided in the statute.
17 Assembly Bill 68, the Online Privacy Protection Act of 2003, adds ch. 22 (commencing with §22573) to div. 8 of the Business and Professions Code.
18 Assembly Bill 1772 and Senate Bill 747 amend Penal Code §530.8. In addition, §530.8(d)(2) provides that a victim may bring a civil action for damages, injunctive relief or other equitable relief, plus a penalty of $100 per day of noncompliance and reimbursements of reasonable attorney’s fees.
Formal Opinion No. 512: Confidentiality of Fact and Amount of Settlement in Settlement Agreement

SUMMARY: A settlement agreement that is otherwise agreeable to the parties may contain a confidentiality clause that prohibits a lawyer from disclosing the fact and amount of the settlement to the lawyer’s other current or future clients without violating the Rules of Professional Conduct, although the lawyer’s duties to multiple clients in the same matter may limit such a clause.


FACTS AND ISSUES PRESENTED
The parties to a lawsuit desire to settle. The defendant seeks to include in the settlement agreement a confidentiality clause that would prohibit disclosure of the fact and amount of the settlement by the plaintiff and his or her representatives, including lawyers. The plaintiff does not object to the confidentiality clause.

The inquirer seeks the committee’s opinion whether it is permissible to require, as a condition of the settlement, a confidentiality clause that would prohibit the opposing party’s lawyer from disclosing the fact and amount of the settlement to the lawyer’s other present or future clients, and whether it is permissible for the lawyer to accept such restriction, under the Rules of Professional Conduct, specifically Rule 1-500. There is no pending litigation in which this issue is being adjudicated.

DISCUSSION
The inquiry acknowledges that there is nothing improper about confidentiality provisions that are routinely bargained for in the course of settling contested actions. The inquirer does not seek to challenge the right of parties to settle their cases by entering into confidentiality provisions that would prohibit the parties and their counsel from...
disclosing settlements to the media, trade journals, or the public in general. Therefore, this inquiry does not implicate the ongoing debate over whether confidential settlements in certain kinds of cases, e.g., involving defective products, should be prohibited as a matter of public policy, a debate that would be beyond the role of this committee. Instead, the inquirer questions whether a confidentiality clause that prohibits the opposing party’s attorney from disclosing the fact and amount of the settlement to his or her other current or future clients would violate Rule 1-500.¹

Rule 1-500(A) (Agreements Restricting a Member’s Practice) states, in pertinent part:

(A) A member shall not be party to or participate in offering or making an agreement, whether in connection with the settlement of a lawsuit or otherwise, if the agreement restricts the right of a member to practice law.

The express exceptions to the rule, which include employment, shareholders’, or partnership agreements among Bar members, an agreement to pay a member upon retirement, or an agreement authorized under Business and Professions Code Sections 6092.5, subdivision (i), or 6093, are not applicable here.

The Discussion to Rule 1-500 states: Paragraph (A) makes it clear that the practice, in connection with settlement agreements, of proposing that a member refrain from representing other clients in similar litigation, is prohibited.

In California, a strong public policy favors the settlement of lawsuits, and maintaining the confidentiality of settlement terms is recognized as a valuable tool in facilitating settlements. Cho v. Superior Court, 39 Cal. App. 4th 113, 124 (1995); Philippine Export & Foreign Loan Guarantee Corporation v. Chudian, 218 Cal. App. 3d 1058, 1076-77 (1990). Thus, for example, in Chapter 3 of the Evidence Code (“Other Evidence Affected or Excluded by Extrinsic Policies”), Section 1152 provides that offers to compromise, as well as any statements or conduct made in negotiation thereof, are not admissible to prove liability. The policy is similar under federal law. See Fed. R. Evid. 408. Furthermore, Evidence Code Section 1119 provides that settlement communications during a mediation shall remain confidential, and Evidence Code Section 1123 states that a settlement agreement prepared pursuant to a mediation may be disclosed only if one of several conditions are met, including agreement by all of the parties. See generally Foxgate Homeowners’ Association, Inc. v. Bramalea California, Inc., 26 Cal. 4th 1, 14 (2001) (“confidentiality is essential to effective mediation”). Whether or not a settlement agreement contains an express confidentiality clause, the settlement of most lawsuits is a private arrangement between the parties, and the terms usually are not filed with or disclosed to the court and do not become part of the public record. The practice of permitting the parties to settle their dispute in private, and to maintain the confidentiality of the terms, also recognizes that parties may settle to avoid the uncertainty and expense of litigation, without admitting liability, and that exposure would likely deter such settlements by implying guilt.

The law draws a distinction between settlement agreements that impose confidentiality on the terms of the settlement and agreements that would directly restrict a lawyer from representing other clients in violation of Rule 1-500(A). This committee opined in Los Angeles County Bar Association Formal Opinion 468 (January 1993) that a settlement agreement in which the settling defendants’ attorneys would have agreed not to represent other nonsettling defendants against the plaintiff was barred by the rule. It made no difference that it was the plaintiff who had proposed the restriction, or that the restriction would apply to the same litigation. The opinion expressly noted, however, that it did not address the question “whether an attorney may participate in a settlement agreement containing confidentiality provisions precluding the attorney from disclosing information obtained during the settlement negotiations.” See Opinion 468 fn.1. The committee relied in part on Formal Opinion 1988-104 by the Standing Committee on Professional Responsibility and Conduct (COPRAC) construing the predecessor to Rule 1-500(A), Rule 2-109, which we found was substantially similar. In Opinion 1988-104, COPRAC opined that a settlement agreement prepared by the defendant’s attorney that would have precluded the plaintiff’s attorney from representing “any person or entity in any litigation or arbitration proceeding against [defendant] or its affiliated entities” limited the autonomy of attorneys and the ability of clients freely to choose an attorney, and therefore, restricted the right of the attorney to practice law. Both the plaintiff’s and the defendant’s attorneys were prohibited from offering or accepting such a provision as a condition of settlement. Id.

A different conclusion is reached when the settlement agreement merely restricts disclosure of the settlement terms. We are not aware of any California authority directly on point, but ABA Formal Opinion 00-417 is instructive. The ABA ethics committee was asked whether a lawyer may agree to a proposal that settlement be conditioned on his “not using any of the information learned during the current representation in any future representation against the same opposing party.” (Emphasis added.) Though the proposed settlement would be favorable to the lawyer’s client, the ABA committee noted that the lawyer’s duty to represent the interests of his client diligently and to abide by the client’s instructions conflicted with the lawyer’s duty not to agree to a limitation on his right to represent other clients. It concluded that the proposed limitation on the “use” of any information learned during the representation, while not a direct ban, would “[a]s a practical matter, . . . effectively bar the lawyer from future representation because the lawyer’s inability to use certain information may materially limit his representation of the future client and, further, may adversely affect that representation.” Id. The prohibition against using all such information was a restriction upon the lawyer’s right to practice. The present inquiry focuses on a similar perceived tension between confidentiality and the right to represent future clients.

In reaching its conclusion in Formal Opinion 00-417, however, the ABA committee drew a key distinction between a ban on using information learned during the lawsuit, and a settlement agreement that merely prohibited disclosure of the terms of the settlement. On the other hand, it is generally accepted that offering or agreeing to a bar on the lawyer’s disclosure of particular information is not a violation of the Rule 5.6(b) proscription. For example, Rule 5.6(b) does not prescribe a lawyer from agreeing not to reveal information about the facts of the particular matter or the terms of its settlement.

...A proposed settlement provision, agreed to by the client, that prohibits the lawyer from disclosing information relating to the representation is no more than what is required by the
Model Rules absent client consent, and does not necessarily limit the lawyer’s future practice in the manner accomplished by a restriction on the use of information relating to the opposing party in the matter. Thus, Rule 5.6(b) would not proscribe offering or agreeing to a nondisclosure provision. Id. (Emphasis in original.)

Therefore, the settlement agreement that is the subject of the inquiry is distinguishable from the settlement in ABA Formal Opinion 00-417 because it would prohibit the plaintiff’s lawyer from revealing the terms of the settlement but would not ban the lawyer’s use of information from the case in future representations.

In California, the client, not the lawyer, ultimately controls the terms of any settlement. People v. Davis, 48 Cal. 2d 241, 256-57 (1957), citing Anderson v. Eaton, 211 Cal. 113, 116 (1930). Thus, under Rule 3-510 of the Rules of Professional Conduct, the lawyer has a duty promptly to communicate all written settlement offers and all significant oral settlement offers to the client. The Supreme Court long ago held that authority to settle a case resides exclusively with the client. Any agreement that prohibits the client from settling the action without the lawyer’s consent is against public policy and void. Calvert v. Stoner, 33 Cal. 2d 97, 103 (1948). A confidentiality clause that merely prohibits disclosure of the fact and amount of the settlement does not constitute a restriction on the right to practice law, and therefore does not create any conflict between the lawyer’s duty to represent his or her client competently under Rule 3-110 by facilitating a favorable settlement, and his or her duty to avoid restrictions on the right to practice under Rule 1-500(A).

Although not expressly articulated, implicit in the inquiry is the notion that imposing confidentiality on the lawyer also may create a conflict of interest between the lawyer’s duty to represent his or her client competently under Rule 3-110 by facilitating a favorable settlement, and his or her duty to avoid restrictions on the right to practice under Rule 1-500(A). Information regarding the settlement arguably would be material to the latter’s claims. However, this argument misconstrues the lawyer’s obligation, and would create a conflict where none exists. If the lawyer’s obligation not to reveal the terms of the settlement were deemed to create a conflict of interest, it would not be cured by obtaining the informed written consent of both clients because the attorney would still be bound by the confidentiality clause. Furthermore, in this hypothetical example, any supposed conflict between the duties owed to different clients would arise from the confidential settlement itself, and would not depend on
whether the confidentiality clause applies to
the lawyer. In fact, it would undermine the
public policy favoring settlements if every
confidential settlement were deemed to cre-
ate a conflict of interest with a prospective
client possessing a claim against the same
opposing party.

We are aware of no reported California
cases addressing confidentiality clauses that
apply to attorneys. Moreover, the courts that
have considered the effect of confidential set-
tlements on a lawyer’s ethical duties are
divided. In Gilbert v. National Corporation
for Housing Partnerships, 71 Cal. App. 4th 1240 (1999), the court affirmed the disqual-
ification of the plaintiff’s attorney after he
sought to offer testimony by a former client
who had settled a similar case against the
same defendant. The previous settlement
agreement contained a confidentiality clause
binding on the parties, but not the lawyer, and
a penalty clause under which the plaintiff
would forfeit his settlement if the confiden-
tiality clause were breached. The court held
that the lawyer had a conflict of interest be-
because his former client risked forfeiting
her settlement if she testified in support of his
current client’s case. 

The argument that a confidentiality clause
is impermissible because it would give rise to
a conflict of interest may simply mask the
attorney’s self-interest in advertising his suc-
cess. However, the lawyer’s duty of undi-
vided loyalty obligates the lawyer not to put
his or her own personal interest in revealing
the terms of a favorable settlement above
the client’s interest in maintaining the confi-
dentiality of the settlement. This committee
opined in Formal Opinion 505 (August 2000)
that an attorney may include terms in an
engagement agreement that are intended to
induce the client not to accept a confidentiality
clause in any settlement agreement, by reduc-
ing his normal fee, but only so long as the
client retains the ability to settle the case
without the lawyer’s consent and without
the imposition of any penalty that would
constitute an unconscionable fee. We saw no
reason to question the existence of confi-
dentiality clauses in settlement agreements
then, and do not believe that it would be
unethical for an attorney to agree to the con-
fidentiality clause described in the inquiry.

CONCLUSION
A settlement agreement that prohibits a
lawyer from disclosing the fact or amount of
the settlement does not violate the Rules of
Professional Conduct, and specifically, Rule
1-500(A).

This opinion is advisory only. The com-
mittee acts on specific questions submitted ex
parte, and its opinion is based on the facts set
forth in the inquiry submitted.

1 The committee recognizes that it will not be possible
to keep the fact, and possibly the amount, of a settle-
ment confidential in every lawsuit. Settlement terms
ordinarily are not confidential when there are multiple
parties on the same side in a lawsuit, especially when
an attorney represents more than one client in the suit.
Similarly, the fact and amount of the settlement will not
be confidential when the settlement requires notice to
a class or court approval.
The “route cases” represent an effort to balance the rights of employers and former employees in trade secret lawsuits

Taking an Old Route

Employers, too, must understand what are and are not their trade secrets when training employees or pursuing litigation after they leave.

Trade secrets play an increasingly important role in determining the outcome of a variety of litigation, especially in light of the increasing attention given to California’s Unfair Competition Law and the limited enforceability of noncompetition agreements.

Often the trade secret at the center of these disputes is a former employee’s knowledge or use of a former employer’s customer list or customer information.

In determining one such recent case, the California Court of Appeal, for the first time in decades, referred to the “route cases,” a group of decisions dating from the first half of the last century that drew the boundaries for the protection of customer information learned from regular service on the routes of delivery and sales people. Today, customers’ preferences and buying habits are more likely stored electronically than on route cards in a delivery truck. But a consideration of the milkman’s, iceman’s, and laundryman’s historic efforts to maintain customer loyalty form a distinct area of common law trade secret jurisprudence and provide an excellent rubric for analyzing whether customer lists are worthy of protection as trade secrets under the Uniform Trade Secrets Act.

As one court noted, route salesmen “constitute a very small and unique group” of employees. Traditionally, they serviced a distinct group of customers using heavily annotated customer lists or customer books. As a rule, the books...contained information as to the days when the

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driver was to call, the nature and quantity of the goods usually required and other information which prepared the driver to render the particular type of service required by the many housewives who were his customers. The lists had been prepared after much inquiry and effort and they were in such form that if one driver quit his employment another could take his place and carry on effectively the business of his employment in the particular district covered by the route.  

The routes involved in these cases spanned a broad range of industries, but the common thread drawn from the cases is the extensive customer information compiled over months or years of service, accompanied by an expectation of continued business. For instance, a history of service could establish the customer’s confidence that a deliveryman would check the icebox for eggs and milk every Friday morning and that, if these staples were below what the customer liked, the supply would be replenished with the usually required amount.

Ordinarily, information acquired in the course of employment is the property of the employer. But before considering what is protected when a former employee solicits the business of a former employer’s customers, it should be recognized that an employee can advise former customers of the termination of employment and accept business from them without using the former employer’s confidential information. It is equally well settled, and often repeated, that employees cannot “be compelled to ‘wipe clean the slate of their memories.’” Nowhere is that inability to do so clearer than for sales personnel.

For instance, in Mathews Paint Company v. Seaside Paint Company, the court of appeal refused an injunction to a paint company whose former employee went to work for a competitor in a situation in which there was no allegation that the lacquer formulas of the former employer were trade secrets and in which the purchasers of lacquer in large, wholesale quantities could be readily identified from phone books. If there is nothing confidential or special about the individual customers’ requirements and if the competitors are ready and willing to fulfill those requirements, there is no use of trade secret information. As the court in Mathews Paint concluded, “A salesman necessarily becomes somewhat acquainted with the particular requirements of his customers, but the knowledge that he obtains in this manner is not in and of itself confidential information which is the property of the employer.”

In Aetna Building Maintenance Company v. West, the California Supreme Court established the test for determining what information will be protected from a former employee’s use in route cases:

To obtain relief against a former employee it must be shown:

1. The information was confidential and not readily accessible to competitors;
2. The former employee solicited the customers of his former employer with intent to injure him;
3. The former employee sought out certain preferred customers whose trade is particularly profitable and whose identities are not generally known to the trade;
4. The business is such that a customer will ordinarily patronize only one concern;
5. The established business relationship between the customer and the former employer would normally continue unless interfered with.

In Aetna, the plaintiff employer alleged that West, a former salesman and supervisor, had misappropriated trade secrets when he solicited and obtained the business of 3 of Aetna’s 200 janitorial customers. Aetna alleged that West had misappropriated customer information because he knew “the extent and type of service required by its customers, the use of certain procedures, material and equipment, the net costs of performing service for each customer and the charges made for it.” The court, however, held the route cases did not apply to the janitorial services at issue.

Prospective customers are commonly known to the trade or may easily be discovered through business directories or by observation. There is no evidence that [the former employee] sought out preferred customers. In any event, the evidence produced by Aetna is to the effect that there are no preferred customers in the trade. Accounts are sold upon the open market at flat rates without regard to either their duration or profitability. The evidence shows that the business is highly competitive and patronage depends upon efficiency of service rather than personal relationship. Contracts are of brief duration and cancellations are frequent. Under such trade conditions, equity will not enjoin the solicitation of the former employee’s customers.

The conduct of the former employee in Aetna contrasts starkly with that of former employees in Reid v. Mass Company, Inc. Reid involved the Green Book, a brochure distributed to new homeowners that listed individual vendors of home services in a particular area. The former employees knew when advertisers’ annual subscriptions to the brochure were going to expire. They then set out to create a competing Red Book with statewide customer lists and knowledge of their expiration dates in mind.

The confidential information at issue can be as minimal as the expiration dates of customers’ contracts. In the case of an advertising contract, for example, advertisers will be looking for a new contract shortly before expiration of their old one. What matters is how accessible the information is to the advertiser.
company’s competitors. In *Pasadena Ice Company v. Reeder*, the court found that customers’ “places of residence, their peculiar likes and fancies and other characteristics, a knowledge of which would greatly aid them in securing and retaining the business” constituted a trade secret.

Several cases also consider the intent and manner of the competitive behavior in deciding whether particular information is confidential. For instance, in *American Loan Corporation v. California Commercial Corporation*, the court recognized that the manner in which the defendant competed with his former employer in the purchase and sale of secured loans on real property itself demonstrated the value of the customer list. Prior to leaving the company, the employee had a secretary prepare a copy of the list, and “took a duplicate copy of the index cards with the customer’s preference indications.” The court reasoned that “if the list was easily obtainable there could have been no reason for him to be at pains to take duplicate copies of the card index or the list.”

Relationships with, as opposed to mere knowledge of, the customers can also be dispositive. In *Peerless Oakland Laundry Company v. Hickman*, the court reasoned that because the manager of a linen supply service not only came to know the likes and dislikes of his customers, but became friends with them as well, he was properly enjoined from soliciting his former employer’s customers:

> “[T]he appellant, as a part of his duties of supervising the delivery routes and receiving and adjusting complaints, had many personal contacts with customers and established friendly relations with them. It is this personal acquaintance and additional influence of the friendship developed during his employment with Peerless which makes solicitation of former customers by appellant so unfair to his former employer."

However, a former employer’s skills of salesmanship and knowledge of the markets in which the goods are sold are not protected as trade secrets if they cannot be characterized as confidential information imparted to the employee during the employment. The distinction is illustrated in *Metro Traffic Control, Inc. v. Shadow Traffic Network*, a case involving the alleged inducement of a competitor’s traffic reporters to violate noncompetition clauses. The court refused to deem the “quality, sound and personality” of the reporters a trade secret, terming them “subjective dimensions” and not part of an informational base belonging to Metro. The court concluded, “A stable of trained and talented at-will employees does not constitute an employer’s trade secret.”

Similarly, in *King v. Pacific Vitamin Corporation*, the court held that “[w]hat the employee acquires in his own right by way of experience and useful knowledge of a business may be of far greater value to him than knowledge of the identity of the employer’s customers and their business connections." Indeed, the court referred to the solicitation of a competitor’s salesmen and executives as a “universal custom.”

The *Aetna* test’s intent-to-injure element can be established by proving that the former employee intends to take business away from the former employer. An intent to divert business from one’s competitor through legitimate trade practices, even if the competitor is a former employer, does not constitute an intent to injure that would support injunctive relief. Instead, the employees must be “motivated by express malice and with the express intention of deliberately and maliciously injuring plaintiffs in their business.”

For example, an intent to injure cannot be shown by the mere employment in a field that inevitably requires a former employee to use confidential information learned in the prior employment. Under a theory of inevitable disclosure, the employer of the former employee would be entitled to an injunction without proving actual misappropriation merely if the former employee cannot perform his or her new job without inevitably using or disclosing the trade secrets of the former employer. However, in *Inn Byne v. Schlage Lock Company*, the California Court of Appeal rejected the theory of inevitable disclosure because the theory “is contrary to California law and policy because it creates an after-the-fact covenant not to compete restricting employee mobility.”

If an employer’s customer list is its primary source of business, the employer also probably needs to show that the former employees targeted certain, preferred customers. It may be enough, however, to demonstrate that certain customers were simply considered the “best business prospects.” In the language of *Reid*, it may thus be inferred that the former employees were not “merely reaping plaintiffs’ particularly profitable harvest; they were separating the wheat from the chaff as well.”

For instance, in *Klamath-Orleans Lumber, Inc. v. Miller*, employees (while still employed by the company) prepared to start up a competing industrial binder business. From memory, one of the employees jotted down the customers of the firm from across the nation. The new company then marketed only to the customers of the old company using materials that directly compared the new company’s and old company’s products. The court recognized that this “preferred” or “select” list of customers is of substantial economic value and constitutes a trade secret. In cases in which courts have considered the *Aetna* test of whether a business would ordinarily only patronize one concern suggest that a factually intensive inquiry concerning the specific company at issue may be required. Indeed, this element of the test may turn on whether only one service was actually used. Sometimes, identical products and prices are necessary for personal relationships with customers to matter. For example, in *Western Electro-Plating Company v. Henness*, the court, noting the absence of any distinction in the services provided by competitors in the chrome-plating business, found that personal and friendly contact formed the core of customer relationships. It therefore affirmed an injunction because the new business of former employees was founded upon the personal relationships created for their former employer.
If the products or services are not the same, or of the same quality, a court will likely not grant injunctive relief to prevent a former employee from selling to former customers. For instance, in *DeLuxe Box Lunch & Catering Company v. Black*, the court refused to prevent a former employee from selling box lunches at the same plant where he had sold them for his former employer. The court noted that the plant had granted permission for the defendant to sell there “on condition that the food be of a greater variety, improved quality and larger quantities than he had brought for the former employer; and also that service should be made on Saturdays, which had been discontinued by the former employer.”

In its essence, a route is premised upon an expectation that customers’ business will continue regularly and indefinitely. Like the “one concern” element, the sales records for particular customers may also be determinant of whether there is the expectation of a continued business relationship. For instance, in *Reid*, evidence that 50 to 70 percent of plaintiffs’ subscribers renew their contracts, along with deposition testimony from some of those subscribers, gave rise to the inference that the established business relationship would more often than not continue unless interfered with.

But in an industry in which personal relationships and efforts are less important than a ready supply of a variety of goods, a continued business relationship is unlikely to be found. For instance, in *King v. Pacific Vitamin Corporation*, injunctive relief was denied because of the openness of the wholesale drug market. The court rejected the plaintiff’s argument that:

> “The same friendly relationship exists between a salesman of drugs at wholesale and his customers as that which characterizes the personal relations between a route salesman and the housewives or laundrymen or dairy salesmen who are privileged to enter homes to pick up or deliver laundry, or fill the refrigerator with the usual requirements of the family.”

In *Continental Car-Na-Var Corporation v. Moseley*, one of the seminal cases determining what is permissible business practice by former employees, the court reversed the issuance of an injunction preventing a former employee involved in the manufacture and sale of floor finishing and cleaning products from doing business in the territory in which he had worked for his former employer. The former employee even sent out a letter thank-

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ing his former customers for their patronage, and assuring them of the “same conscientious treatment and attention” to their future needs. Yet, the court expressly distinguished the route cases:

In the “route” cases the services rendered or the products sold were essentially the same, and the quality of the service rendered is similar. In the case of a salesman in a commercial field, there is no assurance of an order unless he can satisfy the customer that his merchandise is better, cheaper or more salable than that of his competitor. The customer usually desires to examine, inspect and compare merchandise and prices offered to him. Each sale is a distinct transaction, not necessarily implying that another will follow.

Although the industries that gave rise to them have long since disappeared from daily life, the route cases remain useful in determining whether customers’ identities and information can be protected as a trade secret. With the principles of the route cases in mind, employers and employees should be able to aggressively, fairly, and legally compete in their respective industries, and prevent the former from taking undue advantage of trade secret law.

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1 These issues frequently arise in several contexts: 1) when assessing the validity of a noncompetition agreement under Business and Professions Code §16600, 2) in an action to enjoin someone from soliciting a former employer’s customers, and, of course, 3) in actions for damages for misappropriation of trade secrets.


3 Some customer lists are given express statutory protection under Business and Professions Code §16606 (telephone answering services) and §16607 (employment agencies).

4 See Thompson v. Impaxx, Inc., 113 Cal. App. 4th 1425, 1429-30 (2003). Because the facts of Thompson did not permit it, the court did not rely upon the route cases for its decision. But the opinion confirmed the continuing vitality of a doctrine that otherwise has gone the way of home delivery of ice, milk, and bakery goods.


8 See Empire Steam Laundry v. Lozier, 165 Cal. 95 (1913) (laundry); Santa Monica Ice etc. Co. v. Rossier, 42 Cal. App. 2d 467 (1941) (ice routes); California Intelligence Bureau v. Cunningham, 83 Cal. App. 2d 197 (1949) (subscriptions to specialized newsletters); Riess v. Sanford, 47 Cal. App. 2d 244 (1941) (cactus phonographic needles).

9 Contrast this with the case of a salesman in a commercial field, in which “there is no assurance of an order
unless he can satisfy the customer that his merchandise is better, cheaper or more salable than that of his competitor….Each sale is a distinct transaction, not necessarily implying that another will follow.” Continental Car-Na-Var Corp. v. Moseley, 24 Cal. 2d 104, 109 (1944). For example, courts have refused to apply the route cases to the real estate setting because each sale of real estate is a “distinct transaction.” Cal Francisco Inv. Corp. v. Vrionis, 14 Cal. App. 3d 318, 322-23 (1971).

“Section 2860 of the Labor Code provides that

A customer list built up by the employer over a period of years is [the employer’s] property, and its use by a former employee for his own advantage will be enjoined.” Reid v. Mass Co., Inc., 155 Cal. App. 2d 293, 303-04 (1957). Section 2860 “simply is an expression of the familiar principle that forbids an agent or trustee from using trust property or powers conferred upon him for his own benefit.” Burns v. Clark, 133 Cal. App. 3d 634, 639 (1982).

“The court concluded that the former employee could use his general knowledge of chemistry to manufacture floor wax and related commodities so long as he did not use the former employer’s “trade secrets” or secret formulas. Id. at 108, 113-14.”


16 Id. at 204-05; see also California Intelligence Bureau v. Cunningham, 83 Cal. App. 2d 197, 202 (1948) (collecting cases).

17 Id. at 205. 18 Id. (citation omitted). 19 Id. at 301-08. 20 Id. at 1522 (citing Klamath-Orleans Lumber, Inc. v. Miller, 87 Cal. App. 3d 438, 463 (1978)).

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Los Angeles Lawyer July-August 2004

36
he California Business and Professions Code requires contractors performing construction work to be licensed. While seemingly straightforward, the Contractors’ State License Law, codified at Business and Professions Code Sections 7000 et seq., contains few bright-line rules. Indeed, the answers to licensing questions are rarely simple to discern. The legislature and the courts have made many changes to the licensing law over the years, with the legislature reacting to court decisions that have been inconsistent and the courts being guided largely by desired results. An attorney addressing a licensure problem must be aware of these changes and the policies they embody. While many of the interpretive cases were decided under statutes that have been modified and amended, the decisions must still be considered to understand the current law.

Initially, counsel confronted with a licensure issue must determine whether a license is required. If the claimant is a contractor or subcontractor and does not possess a valid license, an attorney must ascertain whether the contractor may be exempt from or has substantially complied with the licensure law. If no exemption exists, counsel must assess the consequences of the contractor’s failure to have a license.

The thrust of the licensure law is the denial of any compensation to a contractor who does not possess a license at all times during the course of the construction process. In an action for the collection of compensation a plaintiff contractor must allege and prove that it was a duly licensed contractor during every stage of the performance of the work and the contract. Business and Professions Code Section 7031(b), which was added to the licensing law in 2001 by an amendment, imposes an additional mandate by requiring an unlicensed contractor to disgorge all monies received already on the project.

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Unlicensed contractors may still be entitled to compensation if they can prove substantial compliance with the licensing law.
disgorgement includes all payments made for labor, services, equipment, and materials (LSEM) paid during any portion of the project while the contractor was unlicensed.

It is a misdemeanor for any person to “engage in the business of or act in the capacity of a contractor within this state without possessing a license.”9 All contractors must include their license number on all contracts and advertising.9 Other provisions of the contractors’ licensing law impose criminal penalties upon the use or misuse of a license5 and regulate contractor advertising and participation in public bidding.6

The purpose of Section 7031 of the licensing law is succinctly set forth in a leading case, Hydrotech Systems Ltd. v. Oasis Waterpark: “to protect the public from incompetence and dishonesty in those who provide building and construction services....” The Hydrotech court further noted that:

Because of the strength and clarity of this policy, it is well settled that section 7031 applies despite injustice to the unlicensed contractor. “Section 7031 represents a legislative determination that the importance of deterring unlicensed persons from engaging in the contracting business outweighs any harshness between the parties, and that such deterrence can best be realized by denying violators the right to maintain any action for compensation in the courts of this state.”7

The absence of a license will also bar any claim by the contractor for breach of contract, including a mechanic’s lien.8 Assignees of unlicensed contractors are not entitled to enforce claims of those contractors.9 However, employees and subcontractors of unlicensed contractors may enforce their mechanic’s lien rights, as long as the subcontractors possess the required license.10

Generally, however, claims that are independent of any action to seek compensation for the LSEM furnished to a project will not be denied because of a lack of licensure. For example, an unlicensed subcontractor that was sued for furnishing defective materials to a project was not barred from maintaining an action for breach of warranty against the person providing the materials used by the subcontractor in performing its subcontract.11 Moreover, an unlicensed contractor was denied recovery of the value of the LSEM furnished by the contractor to a project but was permitted to assert a racial discrimination claim because that claim did not arise from the LSEM.12

Substantial Compliance

Section 7031 governs the rights of contractors to recover compensation for their work. The issues raised by this section are probably the most vexing of all the issues confronting contractors and their attorneys and have led to considerable litigation. The history of Section 7031 demonstrates that it is has undergone numerous legislative changes and judicial interpretations on whether an unlicensed contractor will be allowed to assert that it has substantially complied with the statute and derive compensation for its work.

The basic problem arises when an unlicensed contractor seeks compensation for work it performed. The legislature and courts have wavered between strict interpretations of the licensing law that disallow any compensation to the contractor and more liberal interpretations that permit substantial compliance with the law and thus allow compensation. Two circumstances creating the most difficulties are 1) when the contractor’s license terminates for any reason during the performance of the contract, and 2) when the contractor does not possess the required license at the time of the execution of the contract but acquires the license during the performance of the contract.

Historically, most courts have denied recovery in situations involving the expiration of a license during the course of a construction project. In Pacific Custom Pools, Inc. v. Turner Construction Company,13 the contractor was properly licensed at the commencement of the project, but its license was suspended and expired during the performance of the work, and the contractor was denied compensation. In another case, a contractor who suffered a heart attack during the course of construction and did not renew his license was denied recovery.14 In addition, a court denied recovery to a contractor who was unlicensed for five weeks during a 10-month project.15

Some courts, however, took more liberal views of the statute and permitted contractors to prevail on their claims based on substantial compliance with the licensure statutes. In Latipac Inc. v. Superior Court,16 the contractor was licensed at the time of the formation of the contract, but its license lapsed during the performance of the contract. Nevertheless, despite the lapse, the court permitted the contractor to recover on its claims. In Citizens State Bank of Long Beach v. Gentry17 and Knapp Development and Design v. Pal-Mal Properties, Ltd.,18 the courts held that unlicensed entities could receive compensation under the doctrine of substantial compliance.

In 1989, in a move to stem the apparent trend toward allowing recovery for substantial compliance, the legislature amended Section 7031 specifically to eliminate the doctrine of substantial compliance from the licensing law.19 Nevertheless, apparently recognizing that the courts should not adhere to a strict interpretation of the statute and in an effort to establish some uniformity in the law and its interpretations, the legislature amended Section 7031 in 1994 to permit limited application of the substantial compliance doctrine. The amendment, codified at Section 7031(e), allows recovery if the court determines that the contractor has substantially complied with the licensure requirements as measured by three factors: The contractor 1) had been duly licensed as a contractor prior to the performance of the work or contract, 2) acted reasonably and in good faith to maintain proper licensure, and 3) did not know or reasonably should not have known of the lack of a license. An example of a case interpreting Section 7031(e) and permitting substantial compliance is ICF Kaiser Engineers, Inc. v. Superior Court,20 in which the Contractors State Licensing Board (CSLB) notified Kaiser that its license had been suspended for its failure to comply with the requirements involving responsible managing officers and employees. The appellate court excused Kaiser from compliance with the licensure law because it was a large company and could not be expected to keep abreast of developments that resulted in its license being suspended. The court, finding that no one at Kaiser had “a clue” that Kaiser had inadvertently allowed its license to be suspended, concluded that Kaiser was not required to “know” it was not licensed and did not hold Kaiser to a standard that it “reasonably should have known.”

In another case allowing recovery, Slatkin v. White,21 the contractor’s license was suspended after the contractor had begun work on the contract. The court read the substantial compliance requirement of Section 7031(e) to permit compensation during unlicensed periods of a contract. So long as the contractor had a license when it signed the contract, did all it could do to reinstate its license, and acted reasonably and in good faith to maintain its license, the court held it could recover compensation. Slatkin may be distinguished from Turner, in which the contractor’s license also was suspended during the course of the construction. In Turner, however, the contractor had not met the second requirement of Section 7031(e) because it did not act reasonably in maintaining its license after learning of its licensure defect.

More recently, in NW Erectors, Inc. v. Niederhauser Ornamental and Metal Works Company,22 the court held that a contractor was only required to have been duly licensed prior to the performance of the “act or contract.” NW Erectors stands for the proposition that a contractor may recover for any work performed while licensed, even though the contractor was not licensed at the time of...
While the attorney general has opined that a construction manager for public projects must be licensed as a contractor or an architect or registered as an engineer, California’s licensing laws do not include construction managers as persons or entities who must be licensed.

contracting.23

When pleading substantial compliance, counsel representing unlicensed contractors should stress the elements of fairness and justice underlying their cause. It appears that the courts tend to construe the statutes according to an assessment of the respective equities of the parties.

**Determining Who Is a Contractor**

Although the license law applies to contractors, identifying who is a contractor is sometimes counterintuitive. The term “contractor” is synonymous with the term “builder” and includes persons or business entities, whether on their own or through others, that build, construct, improve, subtract, or change any building, highway, railroad, excavation, structure, development, and the like.24 A business entity qualifies as a contractor through a Responsible Managing Officer (RMO) or a Responsible Managing Employee (RME). As used in the statutes, the term “contractor” includes any subcontractor or specialty contractor. The term “contractor” is intended to be all-inclusive.

General contractors, however, are not allowed to perform only work normally performed by specialty contractors. The licensing law was amended in 1997 so that a general contractor engaged in construction work must “use...at least two unrelated building trades or crafts, or to do or superintend the whole or any part thereof.”25

General contractors may possess a Class “A” license (a general engineering contractor) or a Class “B” license (general building contractor) or both.26 A specialty license is granted to a contractor whose operations involve a specialized building trade.27 Each member of a joint venture must possess a contractor’s license. If one member of the joint venture terminates its relationship with the joint venture or its license is suspended during the joint venture operations, the joint venture will not be properly licensed.28 Partnerships may qualify through a copartner or a responsible managing employee.29

Several important cases have concluded that, under certain circumstances, developers are contractors and are required to be licensed. In a 1994 case, *Vallejo Development Company v. Beck Development Company*, the court held that an unlicensed developer was not entitled to recover the costs of the development’s infrastructure improvements. The developer was required by the city of Vallejo to install these improvements as part of the development, and the city also mandated that the developer be solely responsible for all off site and on site improvements as well as the infrastructure improvements. The developer sought to recover payment from several concerns for whom it installed some of the infrastructure improvements, arguing that it merely furnished labor and materials through licensed, third-party general contractors and was not a contractor within the meaning of Section 7026 and Section 7031 of the licensing law. In its decision, the court rejected the developer’s argument and denied compensation for the developer. The court held that the developer was acting as a contractor, stating that an entity that provides construction services and an entity that does so through others both qualify as contractors.30

On the other hand, in another case, in which a developer/general contractor was sued by a homeowner’s association for alleged defective construction, the court held that the developer, although unlicensed, could prevail on its claim for compensation. The developer was not barred and could recover against its subcontractors, whose work was responsible for the liability that was being imposed upon the developer for the alleged defective construction.31

Sureties have had problems when they undertake to complete a project for their principal that defaulted in its performance on the project. A surety that itself undertook completion of a project and was not licensed as a contractor was denied the right to recover from the owner for the LSEM furnished by the surety in completing the project.32

Many courts have demonstrated a reluctance to enforce a strict result based on a technical licensing issue. Therefore, the facts of each case must be carefully analyzed to determine if a claimant (or a respondent) has any basis to assert substantial compliance with the licensing law.

**Exemptions**

There are several exemptions to the licensure law. Persons who receive wages as their sole compensation, who do not customarily engage in an independently established business, and who do not have the right to control the manner of performance, are exempt from the provisions of the licensing law.33 Work operations that do not involve more than $500 are considered to be casual, and a contractor’s license is not required.34 An owner of property who constructs upon it a single family residential structure or no more than four such structures intended or offered for sale in a calendar year is exempt from the license law.35

A contractor’s license is required for work being performed pursuant to contracts for public works.36 However, contractors performing work on federally funded projects are exempt from the state licensing law, and a contractor’s license is not needed for California contractors who work on federal land.37 This exception does not apply, however, to California projects for public agencies that are federally funded. Under Sections 10164 and 20103.5 of the Public Contract Code, an unlicensed contractor may submit a bid to a California public entity on a project in which federal funding is involved, but it must possess a license at the time of the execution of the contract.38 However, with certain prescribed exceptions, including proj-
ects governed by Public Contract Code Sections 10164 and 20103.5, Business and Professions Code Section 7028.15 makes it a misdemeanor to engage in the business or act in the capacity of a contractor and submit a bid to a public agency without possessing a valid license.

Certain business operators are specially excluded from the definition of a contractor, such as materialmen and material suppliers that do not install or contract to install their products on a project. Equipment suppliers that also provide laborers but do not supervise the operation of the equipment are not contractors and thus are not required to be licensed.

A major issue arises when material suppliers provide workers to supervise the installation of a premanufactured product, such as cabinets. While supervisors are not required to be licensed, in many instances supervisors are permitted or instructed by the licensed contractor to manage the project in such a manner that they cannot be distinguished from the contractor itself. In these instances, the court may conclude that the supplier must be licensed as a contractor. However, in Walker v. Thornsberry, a manufacturer, not licensed as a contractor, sold a metal prefabricated restroom to a general contractor and agreed to furnish, assemble, and install the unit on a concrete foundation prepared by the general contractor. The court held that the manufacturer was not required to possess a contractor’s license.

Although what constitutes a “construction manager” is defined by statute, and many construction managers undertake general construction duties on projects, there is no requirement that they be licensed. The state attorney general has stated that a construction manager is not required to possess a contractor’s or architect’s license when acting in the capacity of an owner of a project or a project employee that receives wages as his or her sole compensation. Nevertheless, public projects are treated differently—and a construction manager for a public project must possess one of three designations. According to the attorney general, “A state or local agency may not contract with a private firm for construction project management services if all or part of such services are to be performed other than under the direction and control of a licensed architect, registered engineer, or licensed contractor.” The opinion relies upon the statutory definition of “construction project management” as “those services provided by a licensed architect, registered engineer, or licensed general contractor which meet the requirements of section 4529.5 for management and supervision of work performed on state construction projects.”

While the attorney general has opined that a construction manager for public projects must be licensed as a contractor or an architect or registered as an engineer, California’s licensing laws do not include construction managers as persons or entities who must be licensed. This apparent discrepancy in the law should be clarified by the legislature.

Responsible Managing Officers and Employees

Difficult problems in the licensure arena arise as a result of the requirement that a business entity must qualify for a contractor’s license through a Responsible Managing Officer or a Responsible Managing Employee. The qualifier must be licensed and qualified in the same license classification that is sought by the business entity. An individual may qualify for himself or herself or by an RME. A partnership may qualify by the general partner or an RME. A corporation may qualify either through an RMO or an RME. Termination of the qualifying RMO or RME by a business entity will terminate its license as a contractor. This was the problem in Kaiser.

An RME is an “individual who is a bona fide employee of the applicant and is actively engaged in the classification of work for which that responsible managing employee is the qualifying person in behalf of the applicant.” Except as provided by Section 7068.1, no person qualifying on behalf of an individual, a partnership, or a corporation may hold any other active contractor’s license.

Persons qualifying on behalf of an individual, a partnership, or a corporation are responsible for direct supervision and control of the construction operations and for full compliance with the provisions of the licensing law. Such persons may not act as the qualifier for an additional individual or firm unless: 1) “There is a common ownership of at least 20 percent of the equity of each individual or firm for which the person acts in a qualifying capacity,” or 2) the additional firm is “a subsidiary of or a joint venture with” the first firm or individual relying on the qualifier, or 3) the majority of the partners or officers are the same in both the first firm and the additional one.

By comparison, a joint venture license is issued to “any combination of individuals, corporations, partnerships, or other joint venturers, each of which holds a current active license in good standing.” This license will be suspended automatically by operation of law during any period in which any member of the joint venture does not hold a current, active license in good standing.

The RME must be a bona fide employee. The regulations define a “bona fide employee” as an employee who is permanently employed by the applicant and is actively engaged in the operation of the applicant’s contracting business for at least 32 hours or 80 percent of the total hours per week that the contracting business is in operation, whichever is less.

The requirement of direct supervision and control is important and frequently litigated. Section 823(b) of Title 16 of the California Code of Regulations defines “direct supervision and control” by RMOs and RMEs as “any one, or any combination of the following activities: (1) supervising construction, (2) managing construction activities by making technical and administrative decisions, (3) checking jobs for proper workmanship, or (4) direct supervision on construction job sites.”

During litigation, if a party’s licensure is disputed, the party must provide proof of its license by producing a verified certificate of licensure from the CSLB establishing that the party was duly licensed in the proper classification of contractors at all times during the performance of any work or contract covered by the action. Moreover, the party controverting the licensure is not required to produce a verified certificate proving its claims. When licensure or proper licensure is contested, the burden of proof to establish licensure or proper licensure is on the licensee. Indeed, a party resisting a claim is not obligated to raise the lack of license as an affirmative defense since the licensing law requires that the claimant must allege and prove that it is licensed. Still, notwithstanding statutory language, one court has held that the fact that the CSLB had issued a license was not, by itself, sufficient to prove licensure.

Two significant cases in this area provide guidance: G.E. Hetrick & Associates, Inc. v. Summit Construction and Maintenance and Buzgheia v. Lasco Sierra Grove. Hetrick involved substantial compliance with the licensing law and whether Gary Hetrick, the president of the Hetrick corporation, was the RMO of the corporation. While a certificate from the CSLB identified Gary Hetrick as such, the defendant, on a motion for summary judgment, sought to establish that Hetrick was absent from the premises during the construction. The court considered Section 7068 and Section 823(b) of Title 16 of the California Code of Regulations and decided that the plaintiff should be given the opportunity to establish that Hetrick was performing one of the four tasks required of an RMO. The importance of the case is that a certificate is not determinative without evidence demonstrating compliance with Section 823(b).

In Buzgheia, a contractor brought an
MCLE Test No. 128

The Los Angeles County Bar Association certifies that this activity has been approved for Minimum Continuing Legal Education credit by the State Bar of California in the amount of 1 hour.

1. An unlicensed contractor, although barred from enforcing a mechanic’s lien, may recover in quantum meruit against the person or entity for which the unlicensed contractor performed construction work. True. False.

2. A contractor seeking compensation for work that it performed is not required to allege that it was licensed to perform that work. The party resisting the contractor’s claim has the burden of proving the contractor was unlicensed. True. False.

3. A leading case noted that the purpose of Business and Professions Code Section 7031, which requires contractors to be licensed, is to “protect the public from incompetence and dishonesty,” and the licensing requirement should be enforced “despite injustice to the unlicensed contractor.” True. False.

4. A licensed subcontractor employed on a project by an unlicensed general contractor is nevertheless still entitled to enforce its mechanic’s lien rights. True. False.

5. A contractor is always required to possess a contractor’s license at the time of the execution of the contract. True. False.

6. An unlicensed contractor may establish substantial compliance with the licensure laws by showing that the contractor 1) had been duly licensed as a contractor prior to the performance of the work or contract, 2) acted reasonably and in good faith to maintain proper licensure, and 3) did not know or reasonably should not have known of the lack of a license. True. False.

7. A general contractor cannot possess both a Class “A” license and a Class “B” license. True. False.

8. A general contractor may engage in a construction project that involves only one building trade or craft, such as plumbing. True. False.

9. All members of a joint venture or general partnership must possess a contractor’s license. True. False.

10. Under certain circumstances, developers are contractors and must be licensed. If they are not licensed, they may be denied recovery on their claims for compensation. However, an unlicensed developer sued for defective construction may recover against third parties that caused the defects. True. False.

11. An individual performing construction work that does not involve more than $500 is not required to possess a license. True. False.

12. A property owner is not required to possess a contractor’s license if the owner is building any number of homes on the owner’s property within one calendar year. True. False.

13. A contractor need not be licensed under California law to perform work pursuant to contracts for public works, whether those public works are funded via a California public entity or by the federal government. True. False.

14. Persons furnishing equipment to a project without supervising the operation of the equipment are not required to possess a contractor’s license. True. False.

15. A material supplier that does not install its products must still possess a contractor’s license. True. False.

16. When a contractor defaults and its surety takes over to complete the project, the surety is not required to possess a contractor’s license. True. False.

17. A Responsible Managing Employee (RME) or a Responsible Managing Officer (RMO) is required to be present on the project site at least 80 percent of the total hours per week that the contracting business is in operation. True. False.

18. A contractor acting as a qualifier for a person or a company may act as the qualifier for another company if the company is a subsidiary of or a joint venture with the original person or company. True. False.

19. A certificate from the Contractors State Licensing Board stating that the contractor is licensed is sufficient to prove licensure. True. False.

20. A licensed contractor doing business under his or her own name or under a fictitious name may sell the contracting business to an unlicensed person, and the buyer may continue the business using the seller’s license. True. False.
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action against a developer for fraud. Again, the issue was whether the plaintiff contractor was properly licensed. Burghetta claimed it was licensed as a result of its employment of Charles Laird as the RME. The defendant argued that Laird did not work on the project at issue. The court stated that Burghetta had the burden of proving licensure and that the trial court wrongfully placed the burden upon the defendant to prove lack of licensure. The language in Section 7031, the court said, regarding the production of a certificate from the CSLB, only places the issue before the court or jury.

The Burghetta decision is important because, as a matter of practice, many persons and entities do not comply with Section 823(b) of Title 16 of the California Code of Regulations. It is not uncommon for major construction concerns to qualify as contractors through RMOs or RMEs who are not on the job site or do not meet any of the three alternative requirements. Nevertheless, if a defendant establishes a lack of compliance by the contractor because the RMO or RME failed to fulfill the necessary requirements, the claimant will be unable to prove it is properly licensed, and recovery for any compensation for its services will be denied.

For attorneys whose clients are defending against claims from unlicensed contractors, motions for summary judgment can be a powerful tool. In fact, many of the significant appellate decisions in this area of the law arose as a result of successful summary judgment motions.

Attorneys and contractors should be aware of the pitfalls and dangers in failing to obtain the appropriate license for their work. While some courts have excused noncompliance for reasons rooted in large measure by sympathy for one party over another, these decisions are in the minority.

Each time a court ruling strays from the doctrine of strict compliance, the legislature counteracts. On the other hand, an attorney faced with a client’s failure to comply strictly with the licensure laws should consider some of the decisions that allow for substantial compliance as well as the legislature’s more recent endorsement of the doctrine in certain specified circumstances.

The lack of consistency in the licensing decisions directly flows from the efforts of the courts to achieve results that they consider fair and equitable based on how they construe statutory language and prior case law. Unfortunately, these interpretations often stretch the language of the existing statutes and decisions beyond their intended meanings or purposes. The problems and confusion created over the years in determining the substance and reach of the licensing law are a result of vacillations by the legislature in its enactments and by the courts in interpreting legislative intent.

1 The licensing law applies to contractors and sub-contractors. The term “contractors” may be used to refer to both.
2 The existence of a license may be verified at the Web site of the Contractors State License Board (CSLB), at http://www.cslb.ca.gov, or by calling (800) 321-2752. In addition, counsel should be aware that they may obtain a status report and history of any licensee by contacting the CSLB.
3 BUS. & PROF. CODE §7028.
4 BUS. & PROF. CODE §7030.
5 LAB. CODE §1021 (misdemeanor for an unlicensed contractor to employ any worker to perform services for which a license is required); LAB. CODE §1021.5 (misdemeanor for a licensee to willingly and knowingly enter into a contract with an unlicensed independent).
6 BUS. & PROF. CODE §7027.1 (license required to advertise as a contractor); BUS. & PROF. CODE §7028.15 (license required to bid on public contracts); BUS. & PROF. CODE §7030.5 (delineating what constitutes advertising).
8 Calberton v. Cizek, 225 Cal. App. 2d 451 (1964). See also Lewis & Queen v. N. M. Ball Sons, 48 Cal. 2d 141 (1957) (holding that an unlicensed subcontractor cannot recover from the general contractor, even though the general contractor was paid for the work of the subcontractor).
16 Latipac Inc. v. Superior Court, 64 Cal. 2d 278 (1966) (strict compliance not required).
19 In further efforts to eliminate or clarify the doctrine of substantial compliance, the legislature amended Business and Professions Code §7031 in 1991, 1992, and 1993.
23 This may lead to some strange results. Consider a scenario in which a contractor is unlicensed when contracting with the owner, and the unlicensed contractor performs half the work required and is paid for that work. The unlicensed contractor then proceeds to obtain a license and complete the project. Under Business and Professions Code §7031(b), the owner
may recover from the contractor what it paid the contractor while the contractor was unlicensed, but the owner would be obligated to pay for the work performed after the contractor obtained a license. A still unanswered question is whether the respective amounts that are due for the owner and the contractor should be offset against each other.

24 Bus. & Prof. Code §7026.
26 Bus. & Prof. Code §§7056, 7057.
27 Bus. & Prof. Code §7058. For descriptions of the various types of specialty licenses, see Cal. Code Regs. tit. 16, §§832 et seq. See also NW Erectors, 115 Cal. App. 4th 512 (2004). In NW Erectors, the contractor was allowed to produce evidence that although the contract required it to perform “ornamental metal work,” for which it was not licensed, it actually was performing “structural steel work,” for which it was licensed.

29 Bus. & Prof. Code §7065. But see Cal. Code Regs. tit. 16, §865 (the death or the disassociation of a partner of a licensed partnership terminates the license).
33 Bus. & Prof. Code §7053.
34 Bus. & Prof. Code §7048.
35 Business and Professions Code §7044 merits detailed study when determining whether a particular owner is exempt from the licensure law.
37 Gartrell Constr. v. Aubry, 940 Fed. 2d 437 (9th Cir. 1991) (California enjoined from enforcing its licensing law because the state law is inapplicable to federal projects); Leslie Miller Inc. v. State of Arkansas, 352 U.S. 187 (1956).
39 Bus. & Prof. Code §§7045, 7052. See also Scientific Cages, Inc. v. Banks, 81 Cal. App. 3d 885 (1978) (materials were supplied but not installed).
43 Gov’t Code § 5425(e).
46 Gov’t Code § 5425(e).
47 The state attorney general has opined that the statute should not only apply to state construction projects but to local government projects as well, and that the omission was inadvertent by the legislature. Could the same argument for inclusion be extended to non-governmental, private projects? The broad language used in the attorney general’s opinion would seem to so indicate. 78 Ops. Cal. Atty. Gen. 48 (1995).
48 Bus. & Prof. Code §7068(b)(1).
49 Bus. & Prof. Code §7068(b)(2).
50 Bus. & Prof. Code §7068(b)(3). The CSLB does not issue licenses to LLCs.
51 Bus. & Prof. Code §7068(d).
52 Bus. & Prof. Code §7068(f).
53 Bus. & Prof. Code §7068.1.
54 Id.
55 Bus. & Prof. Code §7029.
56 Cal. Code Regs. tit. 16, §823(b). It is common practice for licensees to “loan” their license to others to use and receive a commission for the use of the license, notwithstanding that this act is a misdemeanor. Lab. Code §119. Regulations and statutes were enacted in an effort to restrict this practice, even though it still occurs fairly regularly. Moreover, it is a misdemeanor to permit another to use one’s license. Bus. & Prof. Code §§125, 7114.
57 Bus. & Prof. Code §7031(d). It is good practice, however, for counsel for a party resisting a claim to obtain a certificate from the CSLB establishing the lack or suspension of the license. Counsel should also consider subpoenaing the records of the CSLB. If the license was suspended and later reinstated, this information would appear in the board’s records and not necessarily in the certificate.
58 Precision Fabricators, Inc. v. Levant, 182 Cal. App. 2d 637 (1960). Although the court was construing an earlier version of §7031, the current version of §7031 would lead to the same result.
61 The court noted that the failure of the CSLB to take any action against Buzgheia for failure to comply with the licensure laws was not significant. Buzgheia, 60 Cal. App. 4th at 393.
WITH THE SCHEDULED JUNE 30, 2004, handover of power by the U.S.-led coalition to an Iraqi government, debate over the merits of the Iraq war and questions regarding the U.S. military’s abusive treatment of Iraqi detainees at the Abu Ghraib prison show no signs of abating. While these issues merit serious public concern, they have largely obscured a quiet but significant process of change that has taken place within the walls of Iraqi courtrooms and Iraqi criminal law books over the last year. While grappling with civil unrest, attacks by insurgents, and the ongoing reform of Iraqi governmental institutions, the coalition worked steadily to rebuild Iraq’s debilitated criminal justice system.

The April 2003 military conquest of Iraq by the coalition and the ouster of Saddam Hussein’s regime created a dangerous vacuum in law enforcement authority. Hussein’s prewar release of thousands of violent and unstable criminals from Iraqi jails, followed by the coalition’s dismantling of the Iraqi military and security apparatus, complicated postwar efforts to restore law and order. Carjacking, kidnapping, rape, and robbery became commonplace in large cities during the summer of 2003, and many Iraqi citizens feared leaving their homes. Conquering coalition forces found the Iraqi criminal justice infrastructure, especially the court system, in a state of near-total paralysis. Throughout the country, courthouses and other government buildings were looted and plundered, and law enforcement officials fled their posts fearing retaliation from an angry population or criminal gangs.

Under international law, the coalition as an occupying power had a duty to restore order in Iraq as well as a responsibility to guarantee Iraqis a functioning criminal justice system. Accordingly, coalition military and civil authorities focused over the last year on the related tasks of reconstituting the police forces and the court systems. Under Iraq’s interim constitution, signed in March 2004, legal changes made by the coalition to the Iraqi justice system remain in force. Michael M. Farhang is of counsel to Gibson, Dunn & Crutcher LLP in Los Angeles, where he practices civil and criminal litigation. He formerly served as an assistant U.S. attorney in Los Angeles. During May and June 2003, he was part of a legal team sent to Iraq by the U.S. Department of Justice to assist the Coalition Provisional Authority with reconstruction of the Iraqi judicial system.
Legal Changes

Modification of substantive and procedural criminal laws has been one of the most important means by which the CPA has undertaken reform of the Iraqi criminal justice system. Various provisions of the preexisting Iraqi penal and procedural codes were used to ensure that outcomes in criminal investigations and trials protected the Hussein regime, and the laws failed to protect rights of defendants recognized under international human rights standards. As a result, the CPA engaged in selective revision of the 1969 Iraqi Penal Code and the 1971 Law on Criminal Proceedings, removing offensive portions and inserting fundamental due process protections in accordance with international law.

The CPA can claim some justification in international law for its affirmative changes to Iraq’s legal system, which provide a hopeful contrast to the disturbing evidence of abusive practices at Abu Ghraib. The 1949 Geneva Convention Relative to the Protection of Civilian Persons in Time of War incorporates a requirement that customary due process rights be guaranteed to nonbelligerent persons by an occupying power. The convention also prohibits the use of torture. The International Covenant on Civil and Political Rights, to which the United States is a signatory, likewise prohibits the use of coercion against criminal defendants and requires that an accused not be compelled to testify against himself or confess guilt. Under the Geneva Convention, an occupying power is not obligated to leave the penal laws of an occupied territory in force if they constitute a threat to security or an obstacle to the application of the convention itself. Thus, the coalition, as an occupying power, was within its authority in revising Iraqi criminal laws where necessary to bring them into conformity with international human rights and due process standards.

Iraq’s system of criminal laws under Hussein was used to persecute political dissidents and inflict harsh punishments on those considered disloyal to the regime. Rewriting the laws from scratch, however, was not a viable option, given both the immediate need for law and order and international law requirements. The CPA chose instead to begin revising Iraq’s Penal Code on an emergency basis to conform to international human rights standards. For a number of weeks after the ouster of Hussein, the CPA failed to issue a definitive pronouncement despite the backlog of criminal detainees awaiting either prosecution or release. Ultimately, on June 10, 2003, the CPA decreed that the preexisting 1969 Iraqi Penal Code with amendments would be applied, with the temporary suspension of certain offenses relating to state security and transgressions against public officials, including insults. In addition, the CPA suspended the application of capital punishment and decreed that torture and other cruel or inhuman treatment were prohibited.

Although Iraq’s criminal laws lacked various fundamental due process protections that are considered obligatory under international law, as a structural matter Iraq’s criminal justice system was a secular one, following a French civil law model. Crimes were initially referred to an investigative magistrate empowered to gather evidence, interrogate witnesses, and ultimately refer a criminal case for trial before a trial court judge panel. One week after its order applying the Penal Code, the CPA also issued a memorandum preserving Iraq’s preexisting criminal justice system as laid out in its 1971 Law on Criminal Proceedings, with the insertion of certain procedural protections for defendants provided for under U.S. law and international human rights standards.

From a U.S. legal perspective, Iraq’s former criminal procedure code did not adequately protect a defendant’s right to silence. Although a defendant was entitled not to answer questions posed by the investigating magistrate during the investigative stage of a criminal case, the magistrate had no obligation to advise the defendant of this right. The right to remain silent was further undermined by provisions allowing the trial court to question a defendant in criminal proceedings and to consider a refusal to answer such questions as evidence of guilt.

The CPA revised the criminal procedure code to require that, at the preliminary investigative stage of a criminal case, the magistrate must administer a Miranda-type warning, reciting and further advising the accused that he or she has the right to remain silent and a right to counsel, and that no adverse inference may be drawn from the exercise of the right to silence. The CPA established a similar requirement at the arrest stage, requiring law enforcement officers to inform arrested persons of their rights to remain silent and to counsel. Finally, the CPA eliminated the provision entitling the trial court to use an accused’s silence as admissible evidence against him or her.

Iraq’s preexisting criminal procedure code also failed to establish unequivocally the right to counsel for defendants at all critical stages of felony proceedings. The CPA added provisions establishing the right to counsel for all defendants, including indigent ones, beginning at the detention stage in felony cases. The CPA added a requirement that the investigating magistrate ascertain whether an accused wishes to be represented by an attorney prior to questioning. Under the amendment, if the accused desires an attorney the magistrate or investigator cannot begin questioning until counsel is in place. Iraq’s former system of laws permitted use of confessions obtained through torture or other coercion in certain cases. Under the preexisting law, admission of a confession at trial was conditioned upon it not being the result of physical or moral coercion, threats, or promises. A chilling exception to the rule, however, allowed coerced confessions to be admitted as evidence if a court concluded that there was no “causal link” between the coercion and the confession or, alternatively, that the confession was corroborated by accompanying evidence or by further evidence acquired as a result of the confession itself. As a result, prior law effectively permitted an Iraqi court to admit evidence obtained through torture so long as the court deemed the evidence reliable. The CPA eliminated the exception to the rule banning use of coerced confessions, establishing that confessions will be admissible only if they are not the result of coercion, threats, or promises.

The widespread looting, the sabotage of public utilities and other important public installations, and an increase in violent crimes that followed the occupation led to a revision of the penalties for those crimes. The CPA increased the maximum penalties for sabotage to
to facilitating the commission of these offenses. Provisions of Iraq’s penal law allowing
shortened sentences in certain cases were suspended. Finally, in recent months, the CPA has enacted an anti-money laundering law
designed to address crimes involving illegal structuring, money laundering, and terrorist financing.
To further deter criminal activity involving natural resources (including oil and fuel products) or utility infrastructures (including power generation equipment, electrical wires and towers, water systems, and communications cabling), the CPA issued an order establishing a “confiscation hearing” process, similar in nature to a civil forfeiture proceeding, effective without the requirement of an antecedent criminal conviction. Property subject to confiscation is defined as property 1) used or intended for use in resource or infrastructure offenses, 2) acquired through or as a result of such offenses, or 3) furnished or intended to be furnished in exchange for unlawfully acquired resources or parts of utility infrastructure or to otherwise facilitate the commission of these offenses. Confiscation is authorized if the presiding magistrate determines that the property is subject to confiscation and the owner “knew or reasonably should have known” that the property was used or was intended to be used in the specified natural resources or utility infrastructure offense.

De-Baathification and Other Personnel Changes
Under the Geneva Convention, the coalition as an occupation power was authorized to remove public officials from their posts in conformity with its obligation to maintain the orderly governance of the territory and ensure its own security. Strong public sentiment among Iraqis against high-ranking members of the former regime and suspicions about the loyalties of such individuals provided the context for several CPA orders designed to restrict future government service for those closely associated with the Baath party and Hussein’s government. Under these measures, current judges or prosecutors who were former high-ranking Baath party members have been removed from their posts pursuant to investigations into their party status or corruption.
The first order issued by the CPA, on May 16, 2003, was an order to “de-Baathify” Iraq’s government institutions. The order, and its accompanying implementing memorandum, sought to eliminate the political vestiges of the Hussein government by permanently removing thousands of individuals identified as high-level Hussein holdovers from positions of governmental power. The order officially barred Baath party officials within the top four membership ranks of the party from holding government positions. In addition, the order provided that top-level ministry officials holding lower-level membership ranks and above in the Baath party would also be barred from future government service.
To establish a process for identification of affected Baath party members, the CPA initially issued decrees vesting itself with the responsibility for carrying out the vetting process for Iraqi government officials. These initial decrees provided no exceptions to the strict policy of removing those with ranking Baath party positions. In November 2003, however, the CPA officially delegated its authority to conduct de-Baathification investigations to the recently created Iraqi Governing Council. The CPA expressly recognized that “under the prior regime some Iraqis may have become affiliated with the [Baath party] for reasons not primarily related to their ideological beliefs.” In addition, the CPA granted possible exceptions for 1) government employees who received their party rank as a result of POW status during the Iran-Iraq war, 2) cases in which the CPA determined that reinstatement is in “the interests of the Iraqi people,” or 3) circumstances in which failure to reinstate would be “fundamentally unfair.” In recent months, the CPA has publicly acknowledged

Although the CPA recognized the immediacy of the near-term need to staff the criminal and civil courts with QUALIFIED AND EXPERIENCED judges during the occupation, it also established a long-term process to vet judicial officials for corruption or Baath party ties as part of its reconstruction strategy.

The CPA also made changes to the structure of the Iraqi legal system, especially the creation of new criminal courts and agencies and setting new compensation guidelines as a means to increase judicial authority and provide incentives for legal sector employment. Under the Geneva Convention, an occupying wartime power may subject the occupied territory’s population to provisions that are deemed essential to enable the occupying power to fulfill its obligations under the convention, to ensure its own security, and “to maintain the orderly government of the territory.” Under the Hague Convention, an occupying power is authorized to take all measures in its power to “restore and ensure public safety.” The CPA’s structural changes to the Iraqi justice system, especially the creation of new criminal courts, can be seen as measures aimed at accomplishing these goals.
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One of the early significant changes made by the CPA to the Iraqi legal system was the creation of a Central Criminal Court (CCC) in Baghdad. The CPA's July 2003 decision to create a national criminal court was intended to guarantee a forum in which the most serious crimes—those involving threats to public order and safety—could be tried quickly and effectively, in a forum that could also serve as a model for other Iraqi criminal courts. The CPA created a two-chambered court consisting of an investigative forum headed by an investigating magistrate and a trial forum presided over by a three-judge panel. The CPA's two-chambered court structure follows the preexisting Iraqi court structure. The CCC applies Iraq's 1969 Penal Code and its 1971 Law on Criminal Proceedings, as modified by CPA orders.

According to the CPA, the CCC represented both an effort to guarantee swift justice under the difficult circumstances of the occupation and a mechanism to address the problem of criminals undermining Iraq's reconstruction. The CPA heard cases assigned to it by the CPA administrator, who also appointed CCC judges for one-year terms following their nomination by the Judicial Review Committee. Qualifications for CCC judges include Iraqi nationality, high moral character, a background of opposition to or nonmembership in the Baath party, and a high level of “legal competence.” Judges are removable by the administrator for unethical, unlawful, or incompetent conduct. The hearings and decisions of the court are public, and the penalties applied are those specified in the existing penal law, as modified.

The CPA was authorized to refer cases to the CCC involving antigovernment activity; large-scale violence and race or ethnic-based violence; attempts to overthrow the Iraqi government or the CPA; trafficking in illegal weapons, drugs, or humans; transnational fraudulent activities; terrorism; public corruption; and other aggravated criminal conduct as delineated in CPA provisions. Defendants appearing before the CCC have a right to representation by an attorney of their choice, and indifferent defendants are entitled to experienced counsel at no cost. Defendants may appeal CCC trial court decisions to the Court of Cassation, Iraq's highest court of appeal.

Since its establishment, the CCC has adjudicated a number of publicized criminal cases, although it is unclear whether the CCC has provided Iraqis with a model forum equipped to handle the diverse needs of the Iraqi criminal justice system. One criminal case brought against three Iraqi defendants accused of smuggling 500 rocket-propelled grenades in a Red Crescent truck resulted in relatively minor sentences of one year or less. Another case involved two Ukrainians prosecuted for oil smuggling. In a third case, the CCC convicted a former governor of the Najaf area of corruption, extortion, and false imprisonment charges and sentenced him to 14 years' imprisonment. A recent case involved the convictions of three Iraqis for their attempts to utilize a roadside bomb against coalition forces.

The lack of judicial independence under the former Iraqi regime contributed greatly to popular distrust of the legal system. The CPA acted to address this concern by removing supervisory responsibilities over judicial affairs from the executive and restoring it to the judiciary. On September 13, 2003, the CPA reestablished an appointed Council of Judges, which in the past had been an administrative body charged with oversight of the judicial and prosecutorial sectors of the justice system. The CPA's order reconstituted the council as an autonomous body, albeit one with members appointed by the CPA. The CPA delegated power to the Iraqi Governing Council to establish a special tribunal for the trial of former Hussein regime members accused of genocide, crimes against humanity, war crimes, or other violations. Although the governing council had the authority to promulgate substantive and procedural legislation, it was charged with ensuring that international standards of justice apply. The CPA's order preserved the possibility of non-Iraqi nationals serving as judges of the tribunal.

Following the delegation of authority, the Iraqi Governing Council approved a law in December 2003 creating the Iraqi Special Tribunal for crimes against humanity, genocide, war crimes, and other stipulated offenses. The law defines crimes against humanity to include widespread or systematic acts of murder, enslavement, deportation, torture, rape, or persecution directed against a civilian population. The law provides for five judges to preside over each trial chamber of the tribunal. Observers have criticized the structure of the tribunal, however, charging that there is no requirement that the judges have experience working on complex criminal cases or that foreign jurists with experience in international human rights law preside. The law does, however, require the appointment of non-Iraqis to act in advisory capacities or as observers and permits the appointment of foreign judges if the governing council wishes. Human rights advocates have complained that the tribunal law does not adequately address protections for witnesses and victims, and the requirements for the burden of proof and habeas corpus have been criticized as inadequate.

In recent months, a number of Iraqi government officials working with the coalition have been assassinated, including a chief investigative judge in Mosul and another judge who was leading an investigation into local Baath party activities. Threats to Iraqi citizens (including judges) who worked with the CPA and served in the Iraqi justice system during the period of occupation necessitated the creation of special incentives for government service. The CPA mandated the standardization of civil service salaries throughout government to make government employee compensation more transparent and merit-based. In recognition of the special risks assumed by judges

Human rights advocates have complained that the tribunal law does not adequately address protections for witnesses and victims, and the requirements for the burden of proof and habeas corpus have been criticized as inadequate.
and prosecutors in the current environment, however, the CPA authorized special benefits for the families of those officials killed while on duty. The CPA's order provides for a full salary pension to the surviving families of judges or prosecutors killed while serving in office until the date that the slain officials would have reached retirement age, after which the pension reverts to the normal retirement pension amount. Families of judges or prosecutors who die in office of causes other than homicide are provided with an 80 percent salary pension until the date that the officials would have reached retirement age.

The changes to Iraq's criminal procedure code establishing a right to counsel in most criminal cases made establishment of a public defender fee system necessary as well. The CPA charged the Council of Judges with the creation of a fee schedule to govern payments to attorneys appointed to represent indigent defendants in misdemeanor and felony cases. To compensate attorneys who have been representing indigent clients since the time just prior to the war, the Council of Judges is authorized to make payments retroactive for services rendered since March 18, 2003.

Legal, personnel, and structural changes made by the CPA to Iraq's criminal justice system have strengthened its textural conformity with international law and have begun the process of ridding the system of tainted associations with the Hussein regime. Certain changes, including the creation of the CCC, the increase in penalties for certain violent crimes, and confiscation hearing procedures, demonstrate the recognized need for effective tools of law enforcement in the face of threats to stability and public order. Other changes, including the revisions to the penal and procedure codes, de-Baathification, the special tribunal on human rights crimes, the Judicial Review Committee, and the Council of Judges, can be seen as legitimizing changes designed to persuade Iraqis that their criminal justice system will be far more protective of individual rights, as well as less corruptible, in the future. Finally, changes like the creation of pensions for judges and prosecutors and a public defender fee system are properly viewed as pragmatic measures designed to create incentives for Iraqi lawyers and judges to participate in the new criminal justice system.

No doubt the handover of power to an Iraqi government will result in a revisiting of many of these measures. In the short term, however, Iraqis can claim substantial progress on the road toward a fairer, more effective system of criminal justice.

3 The United Nations Security Council called upon the United States and its coalition partners to comply with their obligations under international law, including the 1949 Geneva Convention and the 1907 Hague Regulations, in the occupation of Iraq. See United Nations Security Council Resolution No. 1483 §5 (May 22, 2003); Hague Convention Respecting the Laws and Customs of War on Land IV, Oct. 18, 1907, art. 43, 36 Stat. 2306 [hereinafter Hague Convention] (requiring an occupying power to "take all measures in [its] power to restore, and ensure, as far as possible, public order and safety, while respecting, unless absolutely prevented, the laws in force in the [occupied country]"); Geneva Convention Relative to the Protection of Civilian Persons in Time of War (IV), Aug. 12, 1949, 6 U.S.T. 3516, 3548, art. 64 [hereinafter Geneva Convention] ("[T]o the necessity for ensuring the effective administration of justice, the taking of reprisals against the [occupied country] is not to continue to function in respect of all [penal] offenses.").
4 By the Numbers, ST. PETERSBURG TIMES, Oct. 9, 2003, 2003 WL 5647786.
5 According to the Coalition Provisional Authority, its authority to issue orders and regulations emanates from U.N. Security Resolution No. 1483 and the "laws and usages of war." Coalition Provision Authority Regulation (CPA Regulation) 1 Preamble & §1 (May 16, 2003).
7 Geneva Convention, supra note 3, arts. 3(1)(a), 31-32.
8 International Covenant on Civil and Political Rights, Dec. 19, 1966, 999 U.N.T.S. 171, 176 [hereinafter ICCPR], art. 7; Paust, supra note 6, at 678 & n.9.
9 ICCPR, supra note 8, art. 14(3).
10 Geneva Convention, supra note 3, art. 54.
12 See note 4, supra.
14 Id. §3. In a subsequent order, the CPA also suspended the application of certain provisions of the Penal Code considered to be restrictive of the right to peaceful assembly. CPA Order No. 19 (July 10, 2003).
16 Coalition Provisional Authority Memorandum (CPA Memorandum) 3 Preamble & §3 (June 18, 2003).
17 Law on Criminal Proceedings, supra note 15, §126.
18 Id. §179.
19 CPA Memorandum 3 §4(c).
20 Id. §5.
21 Id. §4(g).
22 See supra note 3, arts. 3(1)(d), 64;
23 Id. §4(c)
24 Id.
26 Id.
27 CPA Memorandum 3 §4(k).
§§2-3, 5.  
30 Id. §2.  
31 CPA Order 25 §2 (Sept. 3, 2003). The order states that its procedures are in addition to other laws providing for confiscation of property after conviction.  
32 Id. §1.  
33 Id. §4.  
34 See Geneva Convention, supra note 3, arts. 54, 64; see also Hague Convention, supra note 3, art. 43.  
35 CPA Order 1 §1 (May 16, 2003).  
36 Id. §1.; CPA Memorandum 1 (June 3, 2003); CPA Order 5 (May 25, 2003) (rescinded).  
37 CPA Memorandum 7.  
38 CPA Order 15 (June 23, 2003).  
40 Geneva Convention, supra note 3, art. 64.  
41 Hague Convention, supra note 3, art. 43.  
42 Overhauling Iraq’s Courts, WALL STREET JOURNAL, June 18, 2003, 2003 WL-WSJ 3970903 (quoting Ambassador Bremer’s statement that “[the CCC] will allow us to try particularly egregious criminals quickly to show people that we are serious about creating law and order”).  
43 CPA Order 13.  
44 Id.  
45 CPA Order 3 §§8(2), 22(2).  
46 CPA Order 13 §21.  
48 CPA Order 35 (Sept. 18, 2003).  
51 CPA Order 30 (Sept. 8, 2003).  
52 CPA Order 52 §3 (Jan. 6, 2004).  
53 CPA Order 53 (Jan. 18, 2004).
Electronic discovery can offer significant advantages in a legal matter but also has the potential to add significant costs and risks if not planned and executed correctly. Whether counsel are working with in-house staff or employing an outside vendor, the process most likely to result in a successful outcome remains the same.

**Project Management.** To successfully control processes, resources, and costs it is important to have a formal project management plan in place. The plan is the road map that establishes the scope of the project, identifies the desired outcomes, and adds credibility with all parties involved. Your plan becomes the foundation that keeps your team on track, improves communication, and adds integrity to the process. Without it, you can easily get off track, miss deadlines, cause spoliation, or even inadvertently release nonresponsive or protected data.

An initial challenge facing the project manager is balancing the need to save money by doing the project in-house, with the risk that in-house resources may not have the expertise or time to successfully complete the project. Carefully evaluation of options and risk is critical at this stage.

**Strategic Discovery Planning.** Once the desired outcomes are established and constraints identified, it is time to establish the “who,” “what,” “when,” “where,” “how,” and “what if” considerations of your project. Typical questions include:

- Who will coordinate and control the project?
- What can be done in-house and what needs to be outsourced?
- When do resources need to be in place?
- What are the significant milestones in the project?
- How do we ensure the integrity of the process?
- What if the production dates slip?

While this planning process may seem time-consuming, it will save significant time, expense, and resources during the execution of the project. And more important, planning helps avoid pitfalls and issues that otherwise would have been missed.

**Data Acquisition.** One of the most often underestimated elements in the EDD process is acquisition. If not done properly the first time, you may lose the opportunity to do it again, and run the risk of endangering admissibility.

As part of the overall strategy it is important that you collect the right amount of data. If you collect too much, it significantly adds to the cost of the matter, and if you collect too little, you may miss key data that influences the outcome of the case. It is important that proper forensics images are taken and the chain of custody is maintained throughout the process.

**Data Analysis.** Once collected, you have an opportunity to further refine the data through culling out irrelevant dates, types of documents, duplicates, and near duplicates. Using the proper technology and processes, you can pare down the data set to a fraction of its original size without the loss of significant information. The latest tools and technologies are sophisticated and capable of intelligent data analysis. Consequently, a formal data analysis plan developed and executed by seasoned professional yields the best results. A word of caution—many vendors now offer their own proprietary tool for data analysis and review. Make certain the tool you use is optimal to meet your needs.

**Data Review.** Methods of data review are migrating from paper reviews to the electronic review of native files using concept analysis. The cost of review generally results in the greatest expense in the EDD process. Finding the right processes and technology can significantly impact your bottom line. (Example: The average “quality document decisions” with traditional on-screen review is 30 to 50 per hour. Using current technology, results increase to between 250 and 400 “quality document decisions” per hour.) Not only are the savings to the client significant, this also frees up resources you can use in other key areas of your litigation.

**Planning for Success.** A formal electronic discovery plan needs to be well thought out and well executed. Sounds simple—but unfortunately, in the heat of battle it is often difficult to take the time to plan and execute properly. Whether developing and executing your own EDD plan or using an outside vendor, planning early, establishing clear lines of communication, and building a credible process will increase your likelihood of success.

K. J. Kuchta is the founder and president of Forensics Consulting Solutions, a nationwide leader in electronic discovery consulting services for civil litigation and Justice Department second requests.
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<table>
<thead>
<tr>
<th>SUBJECT INDEX</th>
</tr>
</thead>
<tbody>
<tr>
<td>Civil Rights Law: “A Landmark in Diversity,” by Edwin Guthman, Mar '03:40; “The Quest to Desegregate Los Angeles Schools,” by David S. Ettinger, Mar '03:54.</td>
</tr>
</tbody>
</table>
| Judicial System: “Let’s End Un-
needed Court Appearances,” by Keith Scheuer, Closing Argument, June '03:52; “The Looming Crisis in California’s Courts,” by Robin Meadow, President’s Page, Jul/Aug '03:10.


Land Use Law: “In a Class of Their Own,” by David Pettit and Michael Schafer (MCLE Test No. 122), Jan '04:39.


Los Angeles County Bar Association: “Celebrating 125 Years of Public Service” by Miriam Krinsky, President’s Page, Mar '03:10; “Celebrating 75 Years of the Barristers” by Margaret P. Stevens, Barristers Tips, Mar '03:16; “Meeting Challenges: The Association’s History of Accomplishment,” by Patricia Phillips, Mar '03:33; “Seventy-Five Years of the Barristers,” by Margaret P. Stevens, Barristers Tips, Sept '03:12; “TAP into Trial Experience,” by Jacqueline J. Harding, Barristers Tips, Oct '03:10.


AUTHOR INDEX


Arlyn-Pessin, Bree (with David Martinez), “Undesignated Hitters” (MCLE Test No. 123), Feb '04:28.


Brown, Jeffrey N. (with Teresa A. MacDonald), “Staying Settled,” June '03:22.


Ettinger, David S., “The Quest to Desegregate Los Angeles Schools,” Mar '03:54.


Free Online Legislative Research

A lawyer who is starting research on behalf of a student who was injured in a school bus accident determines that the seat belt, and not just the impact, caused most of the student’s injuries. The attorney remembers that in the past, school buses did not have seat belts, and so becomes curious about why the bus that was involved in the accident had them. A logical first step toward an answer is a search of the California Codes for the phrase “seat belt.” Today, this search can be conducted on the Internet (and it can be conducted for any state, not just California).

In addition to state codes, many states, including California, offer varying amounts of legislative history on the Internet. California attorneys can research the California Codes or any aspect of California legislation for free at the Web page of the Office of the Legislative Counsel. This page is found at www.leginfo.ca.gov. This is the official site for all legislative materials, and it offers researchers the California law database, which is a complete (but unannotated) version of the California Codes (www.leginfo.ca.gov/calaw.html), constitution (www.leginfo.ca.gov/const.html), statutes (www.leginfo.ca.gov/statute.html), and the full text of bills going back to 1993, with their legislative history (which can be found at www.leginfo.ca.gov/bilinfo.html).

Each of these four separate databases is searchable by key word. Researchers can use Boolean connectors with multiple key words. The Boolean connectors must be in upper case (e.g., AND, OR), otherwise the search will treat the connector as a key word. To search by a phrase, enclose it with quotation marks. Wildcards can be used to extend a word by adding an asterisk to the right of the word. For example, "seat*" will find “seatbelt” or “seatbelts” (or any word beginning with the word “seat”). Searching by natural language is also an option (e.g., “Where is the law that says a school bus must install seat belts?”). Boolean searching can even be mixed into a natural language search, making it possible to define searches accurately.

At the codes search page (found at www.leginfo.ca.gov/calaw.html), the key word search “schoolbus* AND seatbelt*” (the actual search does not include the quotation marks) obtains results that include Section 27316 of the Vehicle Code. The researcher can then go to Section 27316, which states that Type 1 school buses manufactured after January 1, 2004, must have seat belts, and Type 2 buses manufactured after January 1, 2005, must have seat belts.

Once the researcher knows a specific code section, such as Section 27316 of the Vehicle Code, he or she can click on the grouping 27302-27317 and then scroll down to find Section 27316.

Intent

The unannotated code offers no indication regarding why the California Legislature mandated that new school buses must have seat belts. To search for legislative intent, the researcher must find and read the original bill and its legislative history. Knowing when the section was passed and its chapter or bill number would be useful, but the researcher soon discovers that this information is not provided in the free, unannotated code. An annotated code (print or online), however, offers this information.

A researcher can nevertheless obtain information about intent for free on the Internet with a virtual visit to the Office of the Legislative Counsel and a key word search in the bills database (www.leginfo.ca.gov/bilinfo.html). Bills can also be found by clicking the link labeled Legislation on the Web sites of the Senate (www.sen.ca.gov) or the Assembly (www.assembly.ca.gov). All three of these sites allow researchers to search by key word, bill number, or bill author. If the researcher is unsure which house proposed a certain bill, the Assembly and Senate bills can be searched together. If an attorney does know, however, which legislative body proposed the bill, it is best to limit the search to it alone. Bill information is updated after the legislature’s day has ended.

In addition, the California Law database is updated in January each year to include the statutes that become effective that year. For example, on January 1, 2004, the California Law database was updated with all statutes passed in 2003 that were scheduled to take effect in 2004. However, if a bill is to become effective during the same session in which it was passed, the California Law database is updated to reflect that instead of waiting for the next January first.

The Bills database includes:

California’s legislative Web sites...offer tools to attorneys...

monitoring bills in the current session....One allows people to e-mail a comment to the bill author....Another...allows one to receive an e-mail alert each time action is taken on a specific bill.

Carole Levitt is president of Internet For Lawyers (www.netforlawyers.com) and coauthor of The Lawyer’s Guide to Fact Finding on the Internet.
History of the Red Mass

The first recorded Red Mass, a special Mass for the Bench and Bar, was celebrated in Paris in 1249. In England, the tradition began about 1310, during the reign of Edward I. The entire Bench and Bar attended the Red Mass together at the opening of each term of Court. The priest and the judges of the High Court wore red robes, thus the Eucharistic celebration became popularly known as the Red Mass.

The tradition of the Red Mass has continued in the United States. Each year in Washington, D.C., the members of the United States Supreme Court join the President and members of Congress in the celebration of the Red Mass at the National Shrine of the Immaculate Conception. The Red Mass is also celebrated in most other state capitals and major cities throughout the United States.

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The history of each bill introduced and amended.

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Bill analyses prepared by legislative committees, explaining how a bill would change current law. Sometimes an analysis will offer background information or will identify major interest groups in support or opposition.

Any veto message concerning a bill.

Another key word search (e.g., “schoolbus* AND seatbelt*”) is a logical next step. Unfortunately, there is no cumulative search for all sessions, so one must research session by session. Searching for “schoolbus* AND seatbelt*” in the 1999-2000 session obtains a result. Assembly Bill 15 was the bill from which Section 27316 of the Vehicle Code was derived. Clicking on the first analysis unearths the following legislative intent:

“[T]his bill will help to prevent serious injuries to the over one million students in California who are transported by schoolbuses.…Similar legislation, AB 2030 (Galgagos) of last year, would have required seatbelts on schoolbuses. It died in the Senate Transportation Committee. Most of the bills introduced on this topic in the previous years were unsuccessful, but one measure AB 1974 (Molina), Chapter 329, Statutes of 1986, was enacted. This measure required the CHP to conduct a study of lap belts on schoolbuses over 10,000 pounds. CHP completed the report in December 1987, and determined that the existing research weighed against installing lap belts on schoolbuses.

The researcher has found a vein to mine.

California’s legislative Web sites also offer tools to attorneys who are monitoring bills in the current session of the legislature. One allows people to e-mail a comment to the bill author (click on Send Comment to Author located at the bottom of the screen of any displayed Assembly bill). This feature is not available for Senate bills, however. Another tool allows one to receive an e-mail alert each time action is taken on a specific bill (click on Subscribe at the bottom of the screen of any displayed bill). The Assembly site and the Legislative Counsel site offer this feature for Assembly and Senate bills.

Other Sources

Bills are not the only source of laws in California—they can also originate through ballot propositions or initiatives. The University of California Hastings College of the Law Library (http://holmes.uchastings.edu) has created two full-text searchable databases. The databases also include legal and legislative history. The propositions database includes 1) the arguments for and against each proposition, 2) the votes (and percentages), and 3) whether it passed or failed. For initiatives, one can discover whether the initiative qualified and who proposed it.

Both databases go back to 1911 and can be searched by text, number, and date. The initiatives database can also be searched by the proponent’s name or by the number assigned to the initiative. The initiatives database also has images pertinent to the initiatives, and the propositions database has digital images of entire voters’ pamphlets.

Besides California state law, California attorneys often need to search the local law of a city or county and occasionally other state and local laws. For a list of ordinances, codes, and charters promulgated by California cities and counties (with links), use the University of California at Berkeley’s IGS site (http://www.igs.berkeley.edu/library/calcodes.html). The Los Angeles City codes (Municipal Code, Charter, Administrative Code, and Planning and Zoning Code) are free on the Internet and can be searched together or separately (www.amlegal.com/los_angeles_ca). The site cautions, however, that the documents may not reflect the most current legislation and are for informational purposes only. The code and charter of Los Angeles County are found at http://municipalcodes.lexisnexis.com/codes/lacounty. Researchers can call a number provided on the site to discover if other ordinances have been adopted since the last update.

For links to the codes, regulations, bills, and constitutions of other states, see the full-text statute and legislation information at www.prairienet.org/~scruffy/f.htm. In addition, General Code’s E-Code site at www.generalcode.com/webcode2.html and the Municode.com site at www.municode.com link to municipal codes of all 50 states.

Sometimes a visit to the Web site of the state agency that regulates an area of law can provide a shortcut. For example, instead of searching the California Codes for California labor laws, a visit to the Division of Labor Standards Enforcement agency’s Web site (www.dir.ca.gov/dlse/dlse.html) can provide links to state labor laws, labor regulations, and pending labor legislation. To locate agency listings, go to the California State Portal (at www.ca.gov/state/portal/myca_homepage.jsp) and click on State Agency Index in the lower right column. Thanks to the Internet, budget-conscious legislative research has never been better.
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Noriega Clinics, p. 74
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Tel. 415-556-2000 www.ceg.uscourts.gov

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FOR ME, THE PHRASE "TAG TEAM" conjures up vivid images of a masked wrestler on the sidelines with his arms stretched far into the ring, waiting to be tagged so he could come in for the kill. I can see myself as a boy, sitting in front of a black-and-white television, my eyes glued onto a massive, muscle-bound fighting machine waiting to enter the ring to claim victory for his team.

I knew, somehow, that the wrestling matches I was watching were staged. I also knew the righteous opponents, the ones cloaked as the heroes, were more likely to win. In the end, when the final touch of hands between the two prize-winning tag team members signaled that the fight was over, I was thrilled that the good guys could display the ornate belts of champions.

Does the righteous opponent always prevail in the arena of litigation? The outcome of legal disputes is, of course, unscripted. But clearly the opponent with the best prepared team of plaintiff’s or defense counsel will produce the most compelling show. People criticize the judicial system and say it just does not work. Countless clients who prevail in litigation often find that the spoils of war have little value after computing the attorney’s fees as well as the other costs of the battle. As a result, in recent years there has been a move by clients toward alternative dispute resolution and away from litigation, with clients frequently choosing mediation.

The field of mediation comprises different styles or techniques, which are also referred to as models by those in academia. The mediation menu includes facilitative, transformative, and evaluative styles of mediation. Each of these models has the capability of bringing forth different results. Facilitative mediation helps disputing parties discuss their differences by the use of various methods of questioning. Transformative mediation allows combating opponents to mimic what might be labeled “free association” by traditional Freudians. This style of mediation has the therapeutic value of reducing disputants’ anger and hostility and thus helping to pave the road toward settlement. Evaluative mediation is the style of mediation with which most lawyers are familiar and comfortable, because it focuses on a more traditional legal analysis of how a case is progressing and what the likelihood for a potential win might be for each side.

Some mediators fare well with one model more than others, while other mediators move from technique to technique. Many mediators do not even work within the structure of the mediation models and simply follow wherever the parties seem to be leading.

Whatever approach a mediator may take in his or her analysis of the needs of the warring parties, the most familiar mediation experience is that of a single mediator leading the process. While lawyers occasionally may use two mediators working as partners directing the mediation, they may not be aware that they can use more than one mediator in a manner that I have dubbed tag team mediation. Just as in wrestling, the tag team model has awesome power.

Resolving Disputes with Tag Team Mediation

The tag team generally consists of two mediators operating sequentially. Tag team mediation focuses on the experience and skills of the first mediator for more than 80 percent of the mediation process. The first mediator uses a facilitative-transformative style of mediation. Then the second member of the tag team enters the process with a strong facilitative-evaluative style. Our firm has taken the past year to introduce this new type of dispute resolution to our clients—and work out our timing. Tag team mediation has been used to settle insurance bad faith cases, employment and discrimination matters, and real estate and construction disputes. Thus far, our use of tag team mediation has led to a staggering overall settlement rate of 97 percent.

Both members of the tag team must be seasoned mediators who are fully versed not only in the substantive law at the heart of a dispute but also in the various techniques of mediation. The first member of the tag team defuses emotions, uncovers factual differences, and lays a solid foundation that enables the parties to sufficiently move through the dispute so they will be open to and ready for the facilitative-evaluative style utilized by the second team member.

The second member of the tag team usually brings a firm, reality-based approach to the dispute. This approach involves a blend of mediation skills coupled with trial or bench experience. In our firm a retired judge is the second member of the tag team.

Some basic rules and conditions must be met to prepare the way for settlement. For example, most real estate and construction matters require the lion’s share of discovery to be completed prior to mediation. Fortunately, other matters often can be brought to an early mediation, which provides savings for clients faced with considerable discovery and other litigation costs.

High settlement rates translate into substantial time and cost savings for parties. Tag team mediation offers an amazingly effective choice for clients who want to settle their cases through mediation.

Traditional models of mediation will continue to foster settlement for many legal disputes. However, for some, tag team mediation is a style worth considering. It has achieved results that our firm has thus far been unable to duplicate with conventional alternative dispute resolution processes.

Steven Cohen is an attorney and owner of Cohen & Associates, Inc., a full-time dispute resolution practice. His major practice areas include construction defects and real property disputes and discrimination matters.

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