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Fall 2004
Vol. 9, No. 1

Message from the Incoming Chair

By Lauren J. Wachtler

What a privilege it is to assume the Chairmanship of this Section of the New York State Bar Association. At the present time, our members include 1,918 practicing attorneys and jurists from all over the state, and we are looking forward to increasing that membership above the 2,000 mark this year. My goal is to increase not only our numbers but also the diversity of our Section in gender, demographics, and years of litigation experience. We are making an effort to reach out to newer members of the Bar, who have so much to contribute to our Section.

Already this coming year, we have so many exciting projects on which the Section will be working that I have room here to highlight only a few. With the assistance of Jay Safer, I have put together a task force to investigate and report on the recent funding crisis that is threatening the federal courts in the fiscal year 2005 and beyond. Our task force is in the process of interviewing federal jurists and court administrators and expects to have a report by the end of the summer. It is our goal to present our Section's report to the House of Delegates as a voice in support of increasing funding allocations by the House and Senate subcommittees to our federal judiciary and its administrators.

On the state side, I have created a task force to address, once again, the adoption of a uniform Rules of Evidence Code for the state of New York. The task force is called the New York State Bar Association's Commercial and Federal Litigation Section Task Force on a New York Code of Evidence (NYCE) and will be chaired by Paul D. Montclare, a partner in the law firm Montclare & Wachtler. Paul's task force will be comprised of law professors, members of our Section, and state court justices throughout New York State and will examine the reasons why the prior attempts to obtain a Code of Evidence for this state have failed, and why the time is long overdue for the promulgation of a Code in New York. It is interesting to note that, when the Federal Rules of Evidence came into being in 1976, there were only four states in the country that had a state Code of Evidence. Now, New York, the leader in commercial litigation in the United States, is one of only four states that do *not* have a Code of Evidence. Our NYCE Task Force will be gathering the data for a report, which we expect to be ready by the end of the year. We welcome anyone who wishes to work on any aspect of this report and join the NYCE Task Force in this exciting and important project.

In addition to our task forces, our Section has always been at the forefront of developments in commercial litigation throughout the state, and has been recognized for the numerous reports that its various committees have drafted. Many of these incisive reports have been presented to the House of Delegates and have shaped and often changed the practice of commercial law in New York. It is my goal this year to continue to revitalize our committees and increase our recognition as leaders of the Bar. Toward this end, our committee chairs will be providing a brief description of their committees, a list of their committee members, and a photograph of themselves which will be posted on our website to encourage Section members to join a committee and work on a report or program during the course of the year. I encourage all of you to visit our website and join one of our many committees, which offer so many valuable opportunities for writing, speaking, and meeting other members of our Section with similar interests and areas of practice. Our committees are already hard at work. At the time of this writing, the Federal Procedure Committee has two reports in the works—one on the crime/fraud exception to the attorney-client privilege and another on spoliation of evidence—and the Securities Litigation and Arbitration and ADR Committees have already planned a program that will be held on October 26, entitled "Securities Arbitration 2004: A Primer for Practitioners" (*see infra*).

We have also formed a new committee, called the Electronic Discovery Committee, which will be chaired by Adam Cohen, a partner at Weil Gotshal & Manges. Adam, who was a panelist at our Spring Meeting this year, is a leader in the field of discovery and document retention issues associated with e-discovery. His treatise, "Electronic Discovery: Law and Practice," is the first comprehensive analysis of case law involving e-discovery and was cited in two of the *Zubulake* decisions relating to cost-shifting. We welcome Adam to our Executive Committee and look forward to tapping into his expertise in the coming months. Because of the extraordinary impact e-discovery has had on litigation, and the wealth of issues it has raised, this committee will certainly be busy this year. Already our Section has been asked by the Commercial Division to present a seminar for the Commercial Division justices through-

out the state to address some of the issues that they have been asked to adjudicate, and to assist them in dealing with some of the thorny issues that e-discovery continues to present. If you would like to be involved in this venture or Adam's committee, please let us know.

On another front, as many of you know from experience, although we all litigate for a living, it's not always the best way to resolve disputes for either attorneys or clients. Both federal and state courts have often recommended the use of alternative dispute resolution (ADR) as a means of resolving commercial disputes and to avoid the vagaries and vicissitudes of the courtroom. Executive Committee members Lesley Rosenthal and Ed Beane, and new Section member Ruth Raisfeld, have been working with the Honorable Kenneth Rudolph, Commercial Division, Westchester County, and Dan Weitz, ADR Coordinator for the New York State Unified Court System, on revised rules and forms to implement an active ADR program in the Westchester Commercial Division. It is our goal to coordinate this type of program in the Commercial Divisions throughout the state to assist them in operating more efficiently and effectively.

I also want to welcome to our Executive Committee several new members in addition to Adam Cohen. We are proud to announce that the Honorable Bernard Fried, who is the most recently appointed Commercial Division justice in New York County, has joined the Executive Committee. Justice Fried is a highly regarded and scholarly jurist, who has impressed the bench and bar in both the criminal and civil arenas with his preparation, his respect for attorneys, and his thoughtful decisions. We are honored to have him on our Executive Committee.

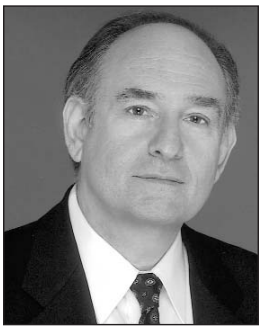
Deborah Masucci will be Co-Chairing our Arbitration and ADR Committee with Carroll Neeseman. Debbie is Director of the Dispute Resolution and Litigation Management Division of AIG, Inc., which is responsible for the strategic use of ADR in the domestic brokerage group and for increasing the alternative methods of appropriate dispute resolution used within the claims organization at AIG. Debbie, along with Carroll, provided us with an excellent program at the Spring Meeting, and Debbie will be a strong addition to the important work of this committee, which continues to press for the adoption of the Uniform Mediation Act and the Uniform Arbitration Act in this state.

We also welcome Leonard Benowich from the White Plains law firm of Roosevelt & Benowich and Gerald Hathaway of Littler Mendelson, P.C. Len practices in the areas of commercial, corporate, and real estate law, and will be joining our Evidence Committee and assisting on the New York Code of Evidence Task Force. Gerry will be chairing the Employment and Labor Relations Committee.

I am looking forward to a great year and welcome this wonderful opportunity to join with our Section members to achieve our goals.

Message from the Outgoing Chair

By Lewis M. Smoley



Given the fact that the high degree of public attention focused on litigators continues unabated, and the concomitant criticism of lawyers in general and litigators in particular continues ceaselessly, we may need to reexamine how we approach this problem. Maybe we need to go back to basics to find a way to counter such unremitting public negativity. Maybe we need to examine the fundamentals of what it means to be a professional, and what responsibilities professional status imposes on us. All too few of us take a moment to consider seriously the difference between an occupation and a profession. What does it mean to be a "professional"? Is it merely a word used to describe someone who works at a highly skilled occupation? Or are there differences between an occupation and a profession that do not necessarily relate to the knowledge and skill required of the activity?

One difference is a purely technical one, that a profession often requires issuance of a license or other formal authority from a governmental body which permits the licensee to engage in the profession. We have all gone through the rigors necessary to prepare for and take at least one bar exam as a requirement for a license to practice law. But too many of us had assumed that once that exam was passed and the license issued, our responsibilities to the profession as such had been fulfilled, and thus we had no reason to consider our professional responsibilities as ongoing. With the recent imposition of continuing legal education requirements, and the consideration of pro bono representation as an obligation for maintaining a license to practice law in this state, these erstwhile presumptions no longer hold.

But the consideration of these requirements (even if not fully implemented in certain respects) indicates much more than either a concern about the necessity of attorneys keeping abreast of developments in the law or the necessity of providing a means for representation of the indigent. Their underlying premise may well be that a professional engaged in an important service licensed by and necessary to the community has a greater duty to the community which he or she is licensed to serve. Even *Webster's Dictionary* recognizes this distinction in defining a "professional" as one who is "worthy of the high standards of a profession." I, on the other hand, suggest these standards are not limited to functional skills and expertise, but also reach beyond the conduct of the professional and the responsibilities he or she owes to the community in which he or she practices.

A true "professional" should be of service not only to the community at large through the conduct of his or her professional functions, but also to the profession itself. One reason that I believe the legal profession was so highly respected in the past (despite the occasional jibe) was the general recognition that lawyers took their responsibility to serve the community and the profession seriously. Giving of our time to community causes, representing those in need of pro bono assistance, and helping the profession both grow substantively and police itself were always factors that helped make the profession of attorney-at-law a highly respected one. But with the enormous growth of the profession, too many attorneys treat the profession as an occupation, and are satisfied to accumulate the many rewards it offers without giving anything back to the societal or the legal community in which they operate.

It would require much more space than I have available here to discuss how this unfortunate situation came about. But one way that we can help to put our profession back on track is for all of us—and I stress that unqualified universality—to give back to the profession some measure of what it has and can continue to do for us. Bar associations provide the means for accomplishing this, but joining one is not enough. Taking an active part in bar association projects with a view toward helping the profession continue to meet its responsibility to the community it serves is at least one part of the answer. The New York State Bar Association, I am proud to say, engages in an enormous number of worthy projects that necessitate active participation by litigating attorneys. Not only is the time one gives to these ventures highly rewarding on a personal level, but they fulfill at least one aspect of the responsibilities a legal professional has to his or her profession. Until we all instinctively recognize the necessity of giving some of our time (however precious) to the improvement of the profession, without the necessity of statutory or regulatory imposition of defined requirements, we need to be constantly reminded of our ongoing responsibilities as professionals to the legal profession and the community at large.

Truth or Dare: Navigating the Minefield of Voluntary Disclosures

By Thomas F. O'Neil III and Eliot J. Kirshnitz

Thomas F. O'Neil III

The most recent era of corporate scandals has only increased the expectations of federal and state prosecutors, and regulatory enforcement authorities, that corporations seeking leniency will voluntarily disclose, promptly upon discovery, any problematic conduct and will cooperate fully during any ensuing investigations.[1] Senior management and boards of directors, moreover, now routinely investigate concerns voiced by internal auditors, compliance officers, regulators and putative whistleblowers. Consequently, a corporation or a special committee of a board of directors is likely to confront the question of whether to disclose to enforcement officials the findings and conclusions generated by a highly confidential and comprehensive internal probe. That dilemma raises the critical question of whether any such revelation constitutes a waiver of evidentiary privileges that could later haunt a company in future ancillary proceedings, such as class actions, commercial litigation or parallel enforcement or debarment inquiries. Equally important is the scope of the waiver: Is it confined to the materials revealed or does it arguably extend to all related information and corporate records?

Recent case law makes clear that in deciding whether to self-police and/or self-report, companies must assume that a voluntary disclosure of factual findings and analytical work product will be deemed a waiver of one or more privileges.[2] But in an ongoing effort to reconcile incongruous policy considerations, courts have applied the doctrines of selective and partial waiver. The first "permits the client who has disclosed privileged communications to one party to continue asserting the privilege against other parties."[3] The second enables "a client who has disclosed a portion of privileged communications to continue asserting the privilege as to the remaining portions of the same communications."[4] This article delineates the parameters of the relevant privileges, traces the evolution and likely trajectory of these doctrines, and reviews the current positions of various enforcement agencies with respect to voluntary disclosures.

I. Overview

A. The Attorney-Client Privilege

Eliot J. Kirshnitz

The attorney-client privilege protects "communications between an attorney and a client, made in confidence, for the purpose of obtaining legal advice or services from the attorney."[5] Judge Cedarbaum recently enunciated the elements of the privilege:

> (1) [W]here legal advice of any kind is sought (2) from a professional legal advisor in his capacity as such, (3) the communications relating to that purpose, (4) made in confidence (5) by the client, (6) are at his instance permanently protected (7) from disclosure by himself or by the legal advisor, (8) except the protection be waived.[6]

The attorney-client privilege seeks to safeguard a client's ability to obtain informed legal advice.[7] By safeguarding communication between a client and her counsel, it encourages "full and free discussion, better enabling the client to conform h[er] conduct to the dictates of the law and to present legitimate claims and defenses if litigation ensues."[8]

B. The Work Product Doctrine

The work product doctrine generally bars a litigant from discovering material "obtained or prepared by an adversary's counsel in the course of his legal duties, provided that the work was done with an eye toward litigation."[9] In short, a party may discover:

> documents and tangible things . . . prepared in anticipation of litigation . . . by or for another party or . . . that other party's representative . . . only upon a showing that the party seeking discovery has substantial need of the materials in the preparation of the party's case and that the party is unable without undue hardship to obtain the substantial equivalent of the materials by other means.[10]

At its core, the doctrine "shelters the mental processes of the attorney, providing a privileged area within which he can analyze and prepare his client's case."[11] Thus, while factual materials falling within the scope of the doctrine may be discovered upon a showing of substantial need, an attorney's mental impressions, conclusions, opinions and legal theories, "core" or "opinion" work product, are more sacrosanct.[12] The work product doctrine promotes the adversary system by "enabling attorneys to prepare cases without fear that their work product will be used against their clients."[13]

C. The Self-Evaluative Privilege

The so-called self-evaluative privilege[14] seeks to encourage "self-improvement through uninhibited self-analysis and evaluation."[15] It is grounded in the notion that "disclosure of documents reflecting candid self-examinations will deter or suppress socially useful investigations and evaluations or compliance with the law or with professional standards."[16] Some courts have, therefore, held that materials reflecting self-appraisals and proposed remedial measures are presumptively protected from discovery.

Neither the Supreme Court nor the Second Circuit has determined whether the privilege should be recognized as a matter of federal law, and the privilege has "led a checkered existence in the federal courts."[17] Documents and information subject to this qualified privilege must

> [first], result from a critical self-analysis undertaken by the party seeking protection; second, the public must have a strong interest in preserving the free flow of the type of information sought; finally, the information must be of the type whose flow would be curtailed if discovery were allowed.[18]

Even those courts that have recognized the privilege have "limited its reach and declined to utilize it to block production of purely factual materials."[19] Hence, it applies only to the analysis and recommendations resulting from the self-evaluations and not the underlying facts discovered during the investigation.[20] In addition, it may not be asserted against the government in civil litigation[21] or in administrative[22] or grand jury proceedings.[23]

D. The Law of Waiver

Protections from disclosure "obstruct the truth-finding process," and as such have long been narrowly construed.[24] A waiver analysis depends on the nature of the privilege asserted and its fundamental purpose.[25] In short, an assertion of an evidentiary privilege or doctrine may be sustained only so long as it promotes the underlying rationale; it will be waived "when it no longer serves its useful purpose."[26] What follows is an overview of the circumstances that typically constitute a waiver of the key privileges discussed above.

1. The Attorney-Client Privilege

Because the attorney-client privilege seeks to encourage candor between clients and their counsel, it protects only those communications that are necessary to obtain informed legal advice, "which might not have been made absent the privilege."[27] Accordingly, courts generally hold that "any voluntary disclosure of such a privilege is inconsistent with the confidential relationship and thus waives the privilege."[28] As one court explained:

> If clients themselves divulge such information to third parties, chances are that they would also have divulged it to their attorneys, even without the protection of the privilege. Thus, once a client has revealed privileged information to a third party, the basic justification for the privilege no longer applies.[29]

2. The Work Product Doctrine

The work product doctrine protects the adversary system rather than preserving confidentiality and therefore, the doctrine "is not automatically waived by any disclosure to a third party."[30] Given its purpose, "only disclosing material in a way inconsistent with keeping it from an adversary waives work product protection."[31] If a party "allows an adversary to share the otherwise privileged thought processes of counsel, the need for the privilege disappears."[32]

Generally, to constitute a waiver as a matter of law, the disclosure must be "inconsistent with maintaining secrecy against opponents."[33] Thus, the doctrine is not waived where the disclosing party has a reasonable expectation that its disclosure will remain confidential vis-à-vis an adversary.[34] The courts have recognized two situations in which such a reasonable expectation of privacy exists: (1) where the disclosing party and the recipient "share a common interest in developing legal theories and analyzing information"; and (2) where the disclosing party and the recipient "have entered into an explicit agreement that the [recipient] will maintain the confidentiality of the disclosed materials."[35] Not surprisingly, then, over the past several decades, subjects and targets of criminal and regulatory enforcement investigations have entered into written joint defense agreements to bolster their assertions of the work product doctrine.[36]

3. The Self-Evaluative Privilege

While there is a dearth of case law analyzing waiver of the self-evaluative privilege, one court has observed that:

> if a party has conducted a confidential analysis of its own performance in a matter implicating a substantial public interest, with a view towards correction of errors, the disclosure of that analysis in the context of litigation may deter the party from conducting such a candid review in the future.[37]

The privilege is grounded on the policy that compelling a party to disclose the results of a confidential self-examination will chill future voluntary self-critical analysis.[38] Thus, it may be argued that the circumstances constituting waiver of the self-evaluative privilege should be analogous to those constituting waiver of the attorney-client privilege, and the few cases in the Second Circuit to touch on this issue, albeit without any analysis, appear to be in accord.[39]

II. The Selective Waiver Doctrine

While the case law concerning selective waiver undeniably is "in a state of hopeless confusion,"[40] it is helpful to review the decisions that have grappled with the concept.

A. The Seminal Eighth Circuit Ruling

In 1978, the Eighth Circuit became the first Circuit Court of Appeals to recognize the doctrine of selective waiver.[41] That case, *Diversified Industries, Inc. v. Merideth*, arose out of a proxy fight, and, among other things, alleged that Diversified had maintained a slush fund to pay bribes to obtain business.[42] The company retained outside counsel to conduct a confidential internal inquiry and the law firm produced an internal report summarizing its findings and conclusions.[43] In the meantime, the United States Securities and Exchange Commission (the "SEC" or the "Commission") initiated its own investigation of Diversified's business practices, and, in response to a Commission subpoena, Diversified voluntarily disclosed its internal report to the SEC.[44] One of the firms that allegedly was harmed thereafter brought a civil action against Diversified and sought production of the report.[45] The district court held that the document was not protected by either the attorney-client privilege or the work product doctrine, and a three-judge panel of the court of appeals affirmed that ruling.[46]

On rehearing *en banc*, the Eighth Circuit reversed, holding, first, that the report was indeed protected by the attorney-client privilege.[47] The court then turned to the question "whether Diversified waived its attorney-client privilege with respect to the privileged material by voluntarily surrendering it to the SEC pursuant to an agency subpoena."[48] The Eighth Circuit concluded that because the document was disclosed "in a separate and non-public SEC investigation," only a "selective waiver" occurred and the document was shielded from discovery by other parties.[49] As a matter of policy, the court stressed the importance of encouraging publicly traded companies to self-police their operations and business practices:

> To hold otherwise may have the effect of thwarting the developing procedure of corporations to employ independent counsel to investigate and advise them in order to protect stockholders, potential stockholders, and customers.[50]

Because the Court of Appeals determined that the report had not been prepared in anticipation of litigation, it did not adjudicate the applicability of the selective waiver doctrine to attorney work product.[51]

B. The Aftermath of *Diversified*

Three years later, the Court of Appeals for the District of Columbia Circuit expressly rejected *Diversified*, finding the selective waiver doctrine "wholly unpersuasive."[52] In *Permian Corp. v. United States*, Circuit Judge Mikva, writing for the panel, held that a company's voluntary disclosure of documents to the SEC effectively waived any protection afforded by the attorney-client privilege, rendering the materials discoverable by the U.S. Department of Energy in other administrative litigation.[53] The court squarely disagreed with the rationale enunciated in *Diversified*:

> The privilege depends on the assumption that full and frank communication will be fostered by the assurance of confidentiality. . . . The Eighth Circuit's [selective waiver] rule has little to do with this confidential link between the client and his legal advisors. Voluntary cooperation with government investigations may be a laudable activity, but it is hard to understand how such conduct improves the attorney-client relationship. If the client feels the need to keep his communications with his attorney confidential, he is free to do so under the traditional rule by consistently asserting the privilege, even when the discovery request comes from a "friendly" agency.[54]

The District of Columbia Circuit Court also perceived the selective waiver doctrine as inherently unfair, inasmuch as it would allow a party to "pick and choose among his opponents, waiving the privilege for some and resurrecting [it] to obstruct others, or to invoke [it] as to communications he has already compromised for his own benefit."[55]

Soon thereafter, the same court addressed the "harder question," whether the selective waiver doctrine shields attorney work product from discovery. The court answered that question in the negative.[56] In *In re Subpoenas Duces Tecum*, the District of Columbia Circuit held that a corporation cannot selectively assert the work product doctrine with respect to an internal investigative report produced for the SEC in connection with that agency's voluntary disclosure program.[57] The opinion rested on three factors. First, the court was convinced that the adversary system would "not be well served by allowing [parties] the advantages of selective disclosure to particular adversaries, a differential disclosure often spurred by considerations of self interest."[58] In other words, when the company decided to participate in the Commission's voluntary disclosure program, it relinquished "some of the traditional protections of the adversary system in order to avoid some of the traditional burdens that accompany adversary resolution of disputes, especially disputes with such formidable adversaries as the SEC."[59] Second, when the corporation disclosed the internal report to the Commission, it had no reasonable expectation that the agency would maintain the confidentiality of the materials.[60] Finally, the court once again rejected the Eighth Circuit's rationale in *Diversified*:

> [W]e cannot see how "the developing procedure of corporations to employ independent counsel to investigate and advise them" would be thwarted by telling a corporation that it cannot disclose the resulting reports to the SEC if it wishes to maintain their confidentiality.[61]

Significantly, the court left open the possibility that a party could "insist on a promise of confidentiality before disclosure to the SEC" as a means of protecting attorney work product from future disclosure by third parties.[62]

At least four other federal appellate courts have endorsed these rulings, declining to recognize the selective waiver doctrine with respect to both the attorney-client privilege and the work product doctrine. Moreover, the Third and the Sixth Circuits have refused to do so even where the disclosure to the government occurred pursuant to a confidentiality agreement.[63]

C. The Second Circuit

The Second Circuit is somewhat more receptive to the notion of selective waiver of evidentiary privileges but only under very specific circumstances. *In re Steinhardt Ptrs., L.P.*, addressed the question "whether disclosure of attorney work product in connection with a government investigation waives the privilege in later discovery."[64] In 1991, Steinhardt was the target of an SEC investigation concerning alleged manipulation of the market for Treasury notes.[65] In response to a request from the Enforcement Division of the Commission, Steinhardt voluntarily produced a memorandum drafted by its counsel that addressed the facts, issues, and legal theories relevant to the company's participation in the Treasury market.[66] Although the materials Steinhardt submitted were marked "FOIA Confidential Treatment Requested," the company had not, in fact, negotiated an agreement that the SEC would maintain the confidentiality of the memorandum.[67] Subsequently, when Steinhardt was named as a defendant in a consolidated securities class action, it refused to produce the work product.[68] Ruling on a motion to compel Steinhardt to produce the requested discovery, the district court held that because Steinhardt had voluntarily disclosed its work product to an adversary, it had waived the protection of the work product doctrine in the civil action.[69]

The Second Circuit agreed. Writing for the panel, District Judge Tenney, sitting by designation, explained that the work product doctrine shields a lawyer's thought processes from opposing counsel, and once a litigant allows an adversary to share them, "the need for the privilege disappears."[70] The fact that Steinhardt had cooperated with the SEC did not transform its relationship with the agency from "adversarial to friendly."[71] The court found "determinative" the fact that "Steinhardt knew that it was the subject of an SEC investigation, and that the memorandum was sought as part of this investigation."[72]

As had both the Third and the District of Columbia Circuits, the court explicitly rejected the Eighth Circuit's policy justification for selective waiver.[73] The court cautioned that the waiver doctrine "allows a party to manipulate use of the privilege through selective assertion" and that "selective assertion of privilege should not be merely another brush on an attorney's palette, utilized and manipulated to gain tactical or strategic advantage."[74] The Court of Appeals reasoned that companies have incentives to cooperate in investigations quite apart from any legal ramifications of a disclosure of their internal findings:

> Voluntary cooperation offers a corporation an opportunity to avoid extended

> formal investigation and enforcement litigation by the SEC, the possibility of leniency for prior misdeeds, and an opportunity to narrow the issues in any resulting litigation. These incentives exist regardless of whether private third party litigants have access to attorney work product disclosed to the SEC.[75]

The Second Circuit also rejected the argument that its decision would leave a corporation subject to a Hobson's choice between waiving work product protection through cooperation or incurring the wrath of enforcement authorities: "An allegation that a party facing a federal investigation and the prospect of a civil fraud suit must make difficult choices is insufficient justification for carving a substantial exception to the waiver doctrine."[76]

While it declined to apply the selective waiver doctrine on the facts presented, the court made clear that it was not adopting "a *per se* rule that all voluntary disclosures to the government waive work product protection."[77] It suggested that no waiver would occur where there existed a reasonable expectation that the disclosure would remain confidential and not fall into the hands of an adversary. More specifically, the Court of Appeals identified as viable settings for the selective waiver doctrine "situations in which the disclosing party and the government may share a common interest in developing legal theories and analyzing information," and "situations in which the SEC and the disclosing party have entered into an explicit agreement that the SEC will maintain the confidentiality of the disclosed materials."[78]

D. *Steinhardt* and Beyond

As a practical matter, the common interest exception envisioned by the Second Circuit is rarely tenable because the fact that a company voluntarily cooperates with government investigators "does not transform the relationship from adversarial to friendly."[79] Indeed, sovereign investigators have generally been found to be adversaries of the subjects and targets of their inquiries.[80]

In *Bank of America, N.A. v. Terra Nova Ins. Co.*,[81] reinsurer Terra Nova voluntarily disclosed to the New York State Insurance Department and the U.S. Attorney's Office for the Southern District of New York a report prepared by outside investigators[82] concerning the activities of one of its agents. It later asserted that in so doing, it had not waived its work product protection because the governmental authorities had not been in "an adversarial position" at the time of the disclosure.[83] Terra Nova had initiated its dialogue with the enforcement officials, and was not the subject of any probe when it produced its report.[84] The Southern District nevertheless found that the Insurance Department was "at least a potential adversary" of Terra Nova.[85] In reaching its decision, the court observed that Terra Nova's motive in contacting officials was to forestall or narrow any enforcement investigation by highlighting the exculpatory evidence it had unearthed.[86] Accordingly, the relationship between the parties was "appropriately characterized as that of potential adversaries," necessitating a finding of waiver of work product protection.[87]

The Delaware Court of Chancery likewise addressed this question, concluding that voluntary cooperation with investigators "does not transform the relationship from adversarial to friendly."[88] In essence, that court reasoned that incentives to cooperate do not render "common" or "harmonious" interests that are otherwise adverse:

> Even though they may be considered foes, a party under investigation has significant incentives to cooperate with authorities. The disclosing party often decides that the benefits of cooperation outweigh the possible damage that may be caused by the information it discloses. Such benefits often include more lenient treatment, avoidance of extensive formal investigation and enforcement litigation, and an opportunity to narrow the issues. By yielding to these formidable opponents in order to minimize future damages, a disclosing party does not make those opponents its friend. It merely concedes that it prefers not to anger such a foe.[89]

But a recent opinion from the Court of Appeals of Georgia suggests that a disclosing party might share a common interest with government investigators where inquiry focuses on rogue former officers and employees rather than on current officers and employees or the corporation itself.[90] While it is unclear whether this distinction will be endorsed by other courts, it certainly is consistent with the case law in this area.

As previously noted, while the Third and Sixth Circuits have expressly held that a confidentiality agreement does not validate an assertion of selective waiver, some district court decisions in the Second Circuit suggest otherwise. Several opinions rejecting selective waiver of work product protection expressly found relevant the absence of a written agreement of confidentiality with government investigators.[91] And recently, in *Maruzen Co., Ltd. v. HSBC USA, Inc.*, the District Court

for the Southern District of New York held that a party's voluntary disclosure of an internal investigation to the U.S Attorney's Office, the SEC, and other government authorities does not waive work product protection because of an extant confidentiality agreement.[92] There, the disclosing party convinced Judge Owen that it had an oral confidentiality agreement with government investigators based on a declaration by its attorney and a letter from the U.S. Attorney confirming that his office had agreed to treat the information as confidential.[93] Thus, the court was able to conclude that because the disclosing party had "explicit confidentiality agreements with the authorities satisfying *Steinhardt*," it had not waived its work product protection.[94]

More recently, the application of the selective waiver doctrine has been explored in some depth in three cases, from disparate jurisdictions, arising out of a high-profile corporate accounting scandal. In January 1999, McKesson HBOC, Inc. ("McKesson") was formed through the merger of McKesson Corporation and HBOC & Company.[95] Some three months later, McKesson announced the first of several downward revisions of its actual financial information for the prior several years,[96] and its board of directors authorized an audit committee and outside counsel to conduct an investigation of its accounting practices. The SEC, in turn, launched a formal investigation of the company, which also was soon defending 80 securities civil actions.[97] In May 1999, McKesson negotiated confidentiality agreements with the SEC and U.S. Attorney's Office for the Northern District of California pursuant to which the company agreed to produce its investigative report. In executing the agreement, McKesson expressly declined to waive any of its privileges.[98] Litigants subsequently demanded that McKesson produce the report and McKesson resisted, asserting various evidentiary privileges. The rulings to date make clear that the selective waiver doctrine promises to remain a strategic minefield for companies and their counsel.

In *McKesson HBOC, Inc. v. Adler*, [99] the Court of Appeals of Georgia found "some evidence" in support of McKesson's contention that it was not the adversary of the SEC, noting that the focus of the Commission's investigation was McKesson's former officers and employees, rather than current officers and employees or the company itself, and that the disclosure was made pursuant to a confidentiality agreement.[100] Indeed, the SEC went so far as to argue that it shared "certain interests" with the new managers of the corporation, who had obtained their positions largely in reaction to the allegations of wrongdoing by former officers and employees.[101] Unable to resolve what it considered material factual issues in the record, the court remanded the matter to the trial court to determine whether the fact that McKesson was not the focus of the investigation indicated that McKesson and the SEC shared a common interest.[102]

In *Saito v. McKesson HBOC, Inc.*, the Delaware Court of Chancery rejected the notion that McKesson and the SEC shared a common interest, but found that the company's voluntary disclosure to the SEC had not waived work product protection in view of the confidentiality agreement.[103] Indeed, the court explicitly adopted "a selective waiver rule for disclosures made to law enforcement pursuant to a confidentiality agreement."[104] In reaching its decision, the court carefully analyzed all facets of the relevant public policies, noting that while the subject of a government investigation has incentives to cooperate with authorities, that cooperation often requires it to divulge sensitive and incriminating information. Consequently, a company must balance whether it should "air its dirty laundry in exchange for mercy or whether to force the law enforcement agency to do its own legal work (and possibly overlook or fail to discover some of the incriminating evidence) at the cost of more stringent treatment."[105] If courts "amplify the risk of disclosure" by allowing private plaintiffs to obtain the information and materials produced to enforcement authorities, "the scales begin to tip further in favor of corporate noncompliance."[106] Moreover, by encouraging full cooperation, the doctrine enables the SEC to resolve a higher volume of investigations with greater speed and efficiency. This, in turn, enhances the protection of investors because "the integrity of the capital markets is preserved at a lower cost to society."[107] In short, the court concluded that it is "inconsistent to deny a selective waiver rule and expect continued cooperation with law enforcement agencies when a confidential disclosure is such a double-edged sword for the corporation."[108]

By contrast, in *United States v. Bergonzi*, the District Court for the Northern District of California rejected both the common interest and confidentiality agreement theories and found that McKesson had waived its work product protection by disclosing its internal report to the SEC.[109] As for the common interest exception, the court determined that McKesson and the Commission did not share a "true common goal," because the SEC could seek to impose liability on the company.[110] The court was also troubled by the fact that McKesson's confidentiality agreement was "not unconditional."[111] Because the agreement authorized the SEC, in its discretion, to disclose the materials as "required by federal law or in . . . discharge of its duties and responsibilities," the court found that McKesson could not have had a reasonable expectation of confidentiality.[112]

III. The Partial Waiver Doctrine

Another question that arises in this setting is whether disclosing a portion of a protected communication waives protection as to the remaining portions of the same communication. Generally, "[w]hen a party discloses a portion of otherwise privileged materials while withholding the rest, the privilege is waived only as to those communications actually disclosed, unless a partial waiver would be unfair to the party's adversary."[113] If a partial waiver does disadvantage an adversary—for example, by presenting a one-sided story to the court—the privilege is deemed waived as to all communications on the same subject matter.[114] Central to this analysis is the "fairness doctrine," which seeks to prevent the "prejudice to a party and distortion of the judicial process that may be caused by the privilege-holder's selective disclosure during litigation of otherwise privileged information."[115] For example, in *In re Subpoena Duces Tecum*, Judge Martin found subject matter waiver where a disclosing party attempted to use the attorney-client privilege as both "as both a sword and shield" by relying on an audit report to disclaim liability while refusing to reveal the factual basis of the report.[116] In the same vein, in *Bank of America,* Magistrate Judge Gorenstein found it "only fair" to require disclosure of the salient facts underlying the disclosure to government investigators.[117]

Courts in the Second Circuit have now made clear that a broad subject matter waiver occurs "only when confidential communications are selectively disclosed *in the course of an ongoing litigation* to gain tactical advantage."[118] While information revealed publicly loses its confidentiality, "there exists no reason in logic or equity to broaden the waiver beyond those matters actually revealed."[119] The Court of Appeals has explained that even though public disclosures may be misleading, so long as they remain "extrajudicial," "there is no *legal* prejudice that warrants broad court-imposed subject matter waiver,"[120] since even one-sided public disclosures create no risk of legal prejudice "until put at issue in . . . litigation by the privilege holder."[121] While the Southern District has suggested, in dicta, that disclosure to the SEC might qualify as "extrajudicial," and, therefore, is not susceptible to subject matter waiver,[122] other courts have observed that disclosures to government investigators are sufficiently "testimonial" to be subject to the limitations on the partial waiver doctrine.[123]

IV. Current Enforcement Oversight Policies

Against the ever-evolving case law, clients and their counsel must weigh the often inconsistent policies and practices of regulatory enforcement and legislative oversight authorities as detailed below.

A. United States Department of Justice

In January 2003, then Deputy Attorney General Larry D. Thompson within the United States Department of Justice ("DOJ") distributed a memorandum revising previously established principles governing the prosecution of corporations.[124] Among the factors a prosecutor must consider in deciding whether to charge a company is "the corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate in the investigation of its agents, including, if necessary, the waiver of corporate attorney-client and work product protection."[125] In evaluating a company's cooperation and its disclosures, prosecutors may request "a waiver of the attorney-client and work product protections, both with respect to its internal investigations and with respect to communications between specific officers, directors and employees and counsel."[126] While waiver is not an "absolute requirement," prosecutors "should consider the willingness of a corporation to waive such protection."[127] Even though the memorandum notes that waiver should normally be limited to factual investigations and contemporaneous advice of counsel, in "unusual circumstances," prosecutors may seek a waiver "with respect to communications and work product related to advice concerning the government's criminal investigation."[128]

The Antitrust Division of DOJ (the "Division") has established a voluntary disclosure program that also places a premium on corporate waivers of attorney-client and work product protections. Under that policy, a company can avoid criminal prosecution "by confessing its role in illegal activities, fully cooperating with the Division, and meeting other specified conditions."[129] The Division has adopted the very firm position that "[o]nly the first corporation to come forward with regard to a particular violation may be considered for leniency as to that violation."[130] With minor differences depending on whether a company makes its voluntary disclosures before or after the Division begins its investigation, a key condition for receiving leniency is whether the corporation "reports the wrongdoing with candor and completeness and provides full, continuing and complete cooperation" in the inquiry.[131]

To offer cooperating companies contractual protection against waiver assertions and adverse rulings, the Division's model conditional leniency letter provides that the disclosure is made in furtherance of an application for amnesty and "will not constitute a waiver of the attorney-client privilege or the work product privilege."[132] Further, as explained by Former Deputy Attorney General Gary R. Spratling, "the Division will not consider disclosures made by counsel in furtherance of the amnesty application to constitute a waiver of the

attorney-client privilege or work product privilege."[133] Similarly, the former United States Attorney for the Southern District of New York, James B. Comey, recently emphasized that DOJ does not require waiver, and does not even require cooperation.[134] Indeed, "if a corporation that chooses to cooperate can do so fully without waiving any privileges, that is fine. Waiver is not required as a measure of cooperation."[135]

If DOJ convicts a company of one or more criminal offenses, self-policing and self-reporting again become relevant. The Federal Sentencing Guidelines Manual for the Sentencing of Organizations establishes detailed rules determining the fines to impose on corporations that have been convicted of wrongdoing.[136] In a nutshell, after calculating a "base fine" amount, based on the nature and circumstances of the crime, a court must assess a set of factors to determine the company's "culpability score," which, after application to the base fine, will determine the actual range of monetary penalties that may be imposed.[137] A trial court is permitted to reduce the culpability score—and, therefore, lower the range of potential fines—if the corporation: (1) reported the violation to authorities soon after learning of it and before an "imminent threat" of disclosure; (2) fully cooperated with the government investigation; and (3) affirmatively recognized and accepted responsibility for its criminal conduct.[138]

B. The SEC

The Commission has its own leniency policy aimed at rewarding companies for their cooperation. In a 2001 Report of Investigation,[139] the SEC declined to take enforcement action against a corporation for the accounting irregularities of one of its employees, explaining its reasoning as follows:

> The company pledged and gave complete cooperation to our staff. It provided the staff with all information relevant to the underlying violations. Among other things, the company produced the details of its internal investigation, including notes and transcripts of interviews . . .; and it did not invoke the attorney-client privilege, work product protection or other privileges or protections with respect to any facts uncovered in the investigation.[140]

Then, in January 2003, the SEC withdrew a proposed rule that would have provided that disclosures made to the Commission pursuant to a confidentiality agreement, "shall not constitute a waiver of any otherwise applicable privilege or protection as to other persons."[141] Nevertheless, the SEC has remained sensitive to the privilege concerns of cooperating corporations. While recognizing that the desire for leniency may cause some companies to consider not asserting the attorney-client privilege or the work product doctrine, the SEC has acknowledged that these protections "serve important social interests" and that waiver is not "an end in itself" but only a "means (where necessary) to provide relevant and sometime critical information to the Commission staff."[142] Accordingly, the SEC follows a policy of "entering into confidentiality agreements where it determines that its receipt of information pursuant to those agreements will ultimately further the public interest, and will vigorously argue in defense of those confidentiality agreements where litigants argue that the disclosure of information pursuant to such agreements waives any privileges or protection."[143]

The Commission quite clearly honors its obligations in this regard. By way of example, in *McKesson HBOC, Inc. v. Adler*, the SEC submitted an a*micus* brief arguing that McKesson's voluntary disclosure to the Commission should not have been deemed a waiver of work product protection.[144] The SEC advised the court that it enters into confidentiality agreements with disclosing parties "only when it has reason to believe that obtaining the work product will significantly improve the quality and timeliness of its investigations."[145] It further noted that it had executed twenty such agreements between 1998 and 2001 and only when it believed that the documents sought "would enable the Commission to save substantial time and resources in conducting investigations and/or provide prompt monetary relief to investors."[146]

The Commission then explained why McKesson's work product qualified for confidential treatment. First, it allowed the SEC to complete its investigation "significantly earlier" than it otherwise would have.[147] Second, McKesson had demonstrated that it was likely to produce reliable work product because the officers who had committed the wrongdoing were no longer with the firm and the company had hired an independent law firm to determine the nature, extent, magnitude, and persons responsible for the illegality.[148] As a matter of public policy, the Commission stated that it seeks to enlist the support of the courts in upholding the provisions of its confidentiality agreements because the SEC "cannot compel parties to produce work product, and parties are much less likely to produce work product if they believe producing it to the Commission will give private litigants access to the documents."[149]

C. The United States Department of Defense

The United States Department of Defense ("DOD") also has a voluntary disclosure program that creates incentives for defense contractors "to adopt a policy of voluntarily disclosing potential civil or criminal fraud matters affecting their corporate contractual relation-

ship" with DOD.[150] It recognizes that "voluntary disclosure, coupled with full cooperation and complete access to necessary records, are strong indications of an attitude of contractor integrity even in the wake of disclosures of potential criminal liability."[151]

DOD has addressed sensitive privilege issues in its model voluntary disclosure agreement (known as the "XYZ Agreement"), in which DOD acknowledges that the disclosing entity may assert both the attorney-client privilege and the work product doctrine. While DOD reserves the right to agree or disagree with any such assertion, it agrees "not to contend that the . . . production . . . will constitute a waiver of the attorney-client and work product privileges."[152]

D. The United States Department of Health and Human Services

The Office of the Inspector General (the "OIG") of the United States Department of Health and Human Services has adopted a voluntary disclosure program to "promote a higher level of ethical and lawful conduct throughout the health care industry."[153] In establishing guidelines for conducting internal investigations and voluntary disclosures, the OIG addressed its need to verify voluntary submissions as follows:

> In the normal course of verification, the OIG will not request production of written communications subject to the attorney-client privilege. There may be documents or other materials, however, that may be covered by the work product doctrine, but which the OIG believes are critical to resolving the disclosure. The OIG is prepared to discuss with the providers' counsel ways to gain access to the underlying information without the need to waive the protections provided by an appropriately asserted claim of privilege.[154]

The OIG expects "diligent and good faith cooperation throughout the entire process," and anything falling short is "considered an aggravating factor" in assessing the appropriate resolution of the matter, which could include referral to the DOJ or other federal agencies, criminal or civil sanctions, or exclusion from participation in federal health care programs.[155]

E. The United States Environmental Protection Agency

The United States Environmental Protection Agency ("EPA") also has a long-standing voluntary disclosure program intended to encourage companies "to voluntarily discover, promptly disclose and expeditiously correct" violations of federal environmental requirements.[156] As with other agencies, EPA offers mitigation of enforcement for companies that meet specified criteria. Chief among them is the expectation that the corporation "must cooperate as required by EPA and provide the Agency with the information it needs" to determine program applicability.[157] While the program has not yet dealt with privilege waivers, it quite clearly envisions production of otherwise protected information and documents:

> In criminal cases, entities will be expected to provide, at a minimum, the following: access to all requested documents; access to all employees of the disclosing entity; assistance in investigating the violation, any noncompliance problems related to the disclosure, and any environmental consequences related to the violations; access to all information relevant to the violations disclosed, including that portion of the environmental audit report or documentation from the compliance management system that revealed the violation; and access to that individuals who conducted the audit or review.[158]

F. Congressional Investigations

While congressional committees and subcommittees have not sought to create any meaningful incentives for corporations to cooperate in their inquiries, their general refusal to recognize evidentiary privileges creates a similar risk with respect to a subsequent finding of a waiver. Often within hours of the announcement of a high-profile crisis or scandal, one or more congressional committees issue subpoenas requiring companies to produce not only commercially and legally sensitive records, but testimony at hastily convened hearings that typically precede the more comprehensive regulatory enforcement investigations as well as class actions and debarment proceedings. Under such circumstances, corporations must make a clear record that they are asserting, and not waiving, the privileges in question.

V. Conclusion

Regrettably, the current unsettled case law offers companies and their counsel little in the way of concrete protection when confronting the question of whether to make a voluntary disclosure to enforcement authorities without waiving evidentiary privileges in future proceedings. Consequently, the first step in the analysis is to review recent rulings in all potentially relevant jurisdictions. If senior management or the board of directors (or a committee thereof) concludes that the potential benefits of a disclosure outweigh the risks,

counsel should consider negotiating at the outset a written confidentiality agreement that, among other things, not only expressly provides that the company is not waiving any otherwise applicable privileges, but also requires the agency to support the corporation's position before any tribunal. However, given the uncertain state of the law, attorneys conducting internal investigations should proceed with care, under the assumption that the documents created may eventually be seen by third parties—be they sovereign entities, private litigants, or members of the public at large.

Endnotes

1. *Interview with United States Attorney James B. Comey Regarding Department of Justice's Policy on Requesting Corporations under Criminal Investigation to Waive the Attorney Client Privilege and Work Product Protection*, United States Attorneys' Bulletin (November 2003) (explaining that a corporation under investigation by the United States Department of Justice can demonstrate its good corporate citizenship by helping the government "catch the crooks").
2. *See, e.g., United States v. Mass. Inst. of Tech.,* 129 F.3d 681 (1st Cir. 1997) (finding that University forfeited attorney-client privilege and work product protection by disclosing documents to Defense Contract Audit Agency); *Westinghouse Elec. Corp. v. Philippines*, 951 F.2d 1414 (3d Cir. 1991) (finding that corporation's voluntary disclosures to the Securities and Exchange Commission and Department of Justice waived attorney-client privilege and work product protection); *In re Martin Marietta Corp.*, 856 F.2d 619 (4th Cir. 1988) (finding that employee's disclosure of otherwise privileged materials to a U.S. Attorney and the Defense Logistics Agency of the Department of Defense waived both the attorney-client privilege and non-case work product); *In re Columbia/HCA Healthcare Corp. Billing Practices Litig.*, 293 F.3d 289 (6th Cir. 2002) (finding that health care corporation waived attorney-client privilege and work product protection by disclosing documents to the Department of Justice and the Health Care Finance Administration); *In re Subpoenas Duces Tecum*, 738 F.2d 1367, 1369 (D.C. Cir. 1984) (finding that corporation's disclosure to the Securities and Exchange Commission and to a grand jury waived the attorney-client privilege and work product protection).
3. *Westinghouse Elec. Corp. v. Philippines*, 951 F.2d 1414, 1423 n.7 (3d Cir. 1991).
4. *Id.* Many courts use the less precise phrase "limited waiver" to refer to either or both doctrines, most commonly using "limited waiver" interchangeably with "selective waiver."
5. *In re Leslie Fay Cos., Inc. Sec. Litig.*, 161 F.R.D. 274, 282 (S.D.N.Y. 1995) ("*Leslie Fay II*").
6. *United States v. Stewart*, 287 F. Supp. 2d 461, 464 (S.D.N.Y. 2003) (citing *In re Grand Jury Subpoena Duces Tecum*, 731 F.2d 1032, 1036 (2d Cir. 1984)). Under Judge Wyzanski's widely cited judicial test, the privilege applies if (1) the asserted holder of the privilege is or sought to become a client; (2) the person to whom the communication was made (a) is a member of the bar of a court, or his subordinate and (b) in connection with this communication is acting as a lawyer; (3) the communication relates to a fact of which the attorney was informed (a) by his client (b) without the presence of strangers (c) for the purpose of securing primarily either (i) an opinion on law (ii) legal services or (iii) assistance in some legal proceeding, and not (d) for the purpose of committing a crime or tort; and (4) the privilege has been (a) claimed and (b) not waived by the client. *United States v. United Shoe Mach. Corp.*, 89 F. Supp. 357, 358 (D. Mass. 1950).
7. *See Upjohn Co. v. United States*, 449 U.S. 383, 389 (1981).
8. *In re Keeper of the Records*, 348 F.3d 16, 22 (1st Cir. 2003) (citing *Upjohn*, 449 U.S. at 389).
9. *In re Sealed Case*, 676 F.2d 793, 809 (D.C. Cir. 1982) (quoting *Hickman v. Taylor*, 329 U.S. 495, 511 (1947)).
10. Fed. R. Civ. P. 26(b)(3).
11. *United States v. Nobles*, 422 U.S. 225, 238 (1975).
12. *See Leslie Fay II*, 161 F.R.D. at 279; *see also* Fed. R. Civ. P. 26(b)(3) (stating that the court "shall protect against disclosure of the mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of a party concerning the litigation").
13. *Westinghouse*, 951 F.2d at 1428.
14. The privilege has also been referred to as the peer review privilege, critical self-evaluative privilege, self-critical analysis privilege, self-examination privilege, and others. *See Tharp v. Sivyer Steel Corp.*, 149 F.R.D. 177, 185 (S.D. Iowa 1993) (listing names).
15. *In re Ashanti Goldfields Sec. Litig.*, 213 F.R.D. 102, 104 (E.D.N.Y. 2003).
16. *Sheppard v. Consolidated Edison Co.*, 893 F. Supp. 6, 7 (E.D.N.Y. 1995) (quoting *Hardy v. New York News, Inc.*, 114 F.R.D. 633, 640 (S.D.N.Y. 1987).
17. *Wimer v. Sealand Serv., Inc.*, 1997 WL 375661, at *1 (S.D.N.Y. July 3, 1997) (noting that some courts have rejected the privilege outright).
18. *Sheppard*, 893 F. Supp. at 7 (quoting *Chemical Bank v. Affiliated FM Ins. Co.*, No. 87 Civ. 0150, 1994 WL 89292, at *1 (S.D.N.Y. March 16, 1994)).
19. *Robinson v. United States*, 205 F.R.D. 104, 108–109 (W.D.N.Y. 2001).
20. *See In re Crazy Eddie Sec. Litig.*, 792 F. Supp. 197, 205 (E.D.N.Y. 1992).
21. *See United States v. Dexter Corp.*, 132 F.R.D. 8, 8–10 (D. Conn. 1990).
22. *See F.T.C. v. TRW, Inc.*, 628 F.2d 207, 210–11 (D.C. Cir. 1980).
23. *See In re Grand Jury Proceedings*, 861 F. Supp. 386, 389–90 (D. Md. 1994).
24. *University of Pa. v. E.E.O.C.*, 493 U.S. 182, 189 (1990).
25. *Permian Corp. v. United States*, 665 F.2d 1214, 1219 (D.C. Cir. 1981).
26. *Saito v. McKesson HBOC, Inc.*, No. Civ.A. 18553, 2002 WL 31657622, at *3 (Del. Ch. Nov. 13, 2002).
27. *Westinghouse*, 951 F.2d at 1423–24 (quoting *Fisher v. United States*, 425 U.S. 391 (1976)); *see also In re Keeper of the Records*, 348 F.3d at 22.
28. *In re Subpoenas Duces Tecum*, 738 F.2d at 1369 (quoting *United States v. A.T.&T.*, 642 F.2d 1285, 1299 (D.C. Cir. 1980)).
29. *Westinghouse*, 951 F.2d at 1424 (citation omitted).
30. *In re Sealed Case*, 676 F.2d at 809, *see also Permian*, 665 F.2d at 1219 (quoting *A.T.&T.*, 642 F.2d at 1299) (explaining that the work product doctrine exists not to protect a confidential relationship, but "to promote the adversary system by safeguarding the fruits of an attorney's trial preparations from the discovery attempts of the opponent").
31. *Mass. Inst. of Tech.,* 129 F.3d at 687.
32. *In re Steinhardt Partners, L.P.*, 9 F.3d 230, 235 (2d Cir. 1993).
33. *Bank of Am., N.A. v. Terra Nova Ins. Co.*, 212 F.R.D. 166, 170 (S.D.N.Y. 2002) (quoting *A.T.&T.*, 642 F.2d at 1299).
34. *Saito*, 2002 WL 31657622, at *4.

35. *Steinhardt*, 9 F.3d at 236.
36. *Viacom, Inc. v. Sumitomo Corp.*, 200 F.R.D. 213, 221 n.6 (S.D.N.Y. 2001); *Lugosch v. Congel*, 219 F.R.D. 220, 241 (S.D.N.Y. 2003) (explaining that co-parties asserting the joint defense privilege are required to demonstrate that they have a shared common interest and that prior to sharing the work product amongst them, there existed an agreement to pursue a joint defense strategy).
37. *Wimer*, 1997 WL 375661, at *1.
38. *Sheppard*, 893 F. Supp. at 7.
39. *See In re Subpoena Duces Tecum*, M8-85 (JSM), 1997 U.S. Dist. LEXIS 2927, at *6 n.1 (S.D.N.Y. March 14, 1997) (declining to decide whether documents relating to an internal investigation were protected by the self-evaluative privilege because the court had already found waiver of the attorney-client privilege); *see also In re Leslie Fay Cos., Inc. Sec. Litig.*, 152 F.R.D. 42, 46 n.7 (S.D.N.Y. 1993) ("*Leslie Fay I*") (finding it "unnecessary" to address whether internal audit report was protected by either the attorney-client or self-evaluative privileges, because those privileges had been waived when the party had waived its work product protection). A waiver of work product protection will also waive the attorney-client privilege for the particular communication at issue. *See In re Sealed Case*, 676 F.2d at 812 ("An exception or waiver of the work product privilege will also serve as an exception or waiver of the attorney-client privilege, since the coverage and purposes of the attorney-client privilege are completely subsumed into the work product privilege.").
40. *Columbia/HCA Healthcare*, 293 F.3d at 294–95 (noting that "some courts have even taken internally inconsistent opinions").
41. *Diversified Industries, Inc. v. Merideth*, 572 F.2d 596 (8th Cir. 1978) (en banc).
42. *Diversified*, 572 F.2d at 607.
43. *Id.*
44. *Id.* at 611.
45. *Id.* at 600.
46. *Id.* at 602–603.
47. *Id.* at 610–11.
48. *Id.* at 611.
49. *Id.*
50. *Id.*
51. *Id.* at 611 n.4.
52. *Permian*, 665 F.2d at 1219–20.
53. *Id.* at 1220.
54. *Id.* at 1220–21.
55. *Id.* at 1221.
56. *In re Subpoenas Duces Tecum*, 738 F.2d at 1370–11.
57. *Id.* at 1371.
58. *Id.* at 1372.
59. *Id.*
60. *Id.* The opinion notes that the SEC, while the case at bar was pending in 1984, had announced its intention to propose legislation that would provide that information submitted to the Commission would be exempt from disclosure to third parties under the Freedom of Information Act ("FOIA"). The court suggests that this statement indicated the SEC's belief that, under then current law, submission of information to the Commission was not exempt from FOIA. *Id.* at 1375.
61. *Id.* at 1375.
62. *Id.*
63. *See Westinghouse*, 951 F.2d at 1427; *Columbia/HCA Healthcare*, 293 F.3d at 306–307.
64. 9 F.3d 230, 233 (2d Cir. 1993).
65. *Id.* 232.
66. *Id.*
67. *Id.*
68. *Id.*
69. *Id.* at 234.
70. *Id.* at 235.
71. *Id.* at 234.
72. *Id.*
73. The Second Circuit acknowledged that *Diversified* addressed the attorney-client privilege rather than the work product doctrine, but found that "much of the reasoning in *Diversified* has equal, if not greater, applicability in the context of the work product doctrine." *Id.* at 235.
74. *Id.*
75. *Id.* at 236 (citing *In re Subpoenas Duces Tecum*, 738 F.2d at 1369).
76. *Id.*
77. *Id.*
78. *Id.*
79. *Cooper Hosp./Univ. Med. Ctr. v. Sillivan*, 183 F.R.D. 119, 119 (D.N.J. 1998).
80. *See Saito*, 2002 WL 31657622, at *5 (collecting cases).
81. 212 F.R.D. 166 (S.D.N.Y. 2002).
82. The investigation had been performed by an outside insurance consultancy. The court acknowledged that the majority of the materials gathered by the investigation were not work product, but states, without explanation, that "some work product" had been produced in the investigation. *Id.* at 168.
83. *Id.*
84. *Id.*
85. *Id.* at 172 (quoting *Mass. Inst. of Tech.*, 129 F.3d at 686).
86. *See id.*
87. *Id.* (quotation omitted).
88. *Saito*, 2002 WL 31657622, at *5.
89. *Id.*
90. *McKesson HBOC, Inc. v. Adler*, 562 S.E.2d 809, 813 (Ga. Ct. App. 2002).
91. *See, e.g., Leslie Fay I*, 152 F.R.D. at 46.
92. No. 00 CIV. 1079(RO), 00 CIV. 1512(RO), 2002 WL 1628782, at *2 (S.D.N.Y. July 23, 2002).
93. *Id.* at *1.
94. *Id.* at *2.
95. *Saito*, 2002 WL 31657622, at *1.
96. *Id.*
97. *Adler*, 562 S.E.2d at 811, 811 n.1.
98. *United States v. Bergonzi*, 216 F.R.D. 487, 490–91 (N.D. Cal. 2003).
99. 562 S.E.2d 809, 813 (Ga. Ct. App. 2002).
100. *Id.* at 813–14.
101. *Id.* at 813; *but see Leslie Fay I*, 152 F.R.D. at 46 ("the SEC is not in a position to decide what constitutes waiver").
102. *Adler*, 562 S.E.2d at 813.
103. *Saito*, 2002 WL 31657622, at *5–*11.

104. *Id*. at *11.
105. *Id*. at *8.
106. *Id*.
107. *Id*.
108. *Id*. at *9.
109. *United States v. Bergonzi*, 216 F.R.D. 487, 495–98 (N.D. Cal. 2003).
110. *Id.* at 496.
111. *Id.* at 498.
112. *Id*. at 494, 497 n.10.
113. *Westinghouse*, 951 F.2d at 1426 n.12.
114. *Id*.
115. *von Bulow v. von Bulow*, 828 F.2d 94, 101 (2d Cir. 1987).
116. 1997 U.S. Dist. LEXIS 2927, at *10–*11.
117. *Bank of America*, 212 F.R.D. at 171.
118. *Leslie Fay II*, 161 F.R.D. at 283 n.5 (emphasis added).
119. *von Bulow*, 828 F.2d at 103.
120. *Id*.
121. *Id.*
122. *Leslie Fay II*, 161 F.R.D. at 283 n.5.
123. See, e.g., *In re Martin Marietta Corp.*, 856 F.2d at 625 (concluding that disclosure to government investigators while the government is an adversary "constitutes testimonial use").
124. "Principles of Federal Prosecution of Business Organizations," Memorandum from Deputy Attorney General Larry D. Thompson, to Heads of Department Components and U.S. Attorneys (Jan. 20, 2003).
125. *Id*.
126. *Id*.
127. *Id*.
128. *Id.*
129. U.S. Dep't of Justice Antitrust Div. Manual III-111 (3d. ed. Rev. 2002).
130. *Id*. at III-112.
131. *Id*. at III-112, III-113.
132. Model Corporate Conditional Leniency Letter, *attached to* Gary R. Spratling, Making Companies an Offer they Shouldn't Refuse, *addressed at* the District of Columbia Bar Association's 35th Annual Symposium on Associations and Antitrust (February 16, 1999).
133. Gary R. Spratling, The Corporate Leniency Policy: Answers to Recurring Questions, *addressed at* the American Bar Association Antitrust Section 1998 Spring Meeting (April 1, 1998) (transcript available at the Department of Justice website).
134. *Interview with United States Attorney James B. Comey Regarding Department of Justice's Policy on Requesting Corporations under Criminal Investigation to Waive the Attorney Client Privilege and Work Product Protection*, United States Attorneys' Bulletin (November 2003).
135. *Id.*
136. *See* Federal Sentencing Guidelines Manual, 8(c) (1998), Ch. 8, Part C.
137. *See id.* §§ 8C2.4-8C2.8.
138. *See id*. § 8C2.5(g).
139. Report of Investigation, Securities Exchange Act of 1934 § 21(a) and Comm'n Statement on the Relationship of Cooperation to Agency Enforcement Decisions Release No. 34-44969 (Oct. 23, 2001).
140. *Id.*
141. Implementation of Standards of Professional Conduct for Attorneys, 17 C.F.R. pt. 205 (proposed January 2003) (to be codified at 17 C.F.R. pt. 205.3(e)(3)).
142. Report of Investigation, Securities Exchange Act of 1934 § 21(a) and Comm'n Statement on the Relationship of Cooperation to Agency Enforcement Decisions Release No. 34-44969 (Oct. 23, 2001).
143. Implementation of Standards of Professional Conduct for Attorneys, 17 C.F.R. pt. 205 (proposed January 2003) (to be codified at 17 C.F.R. pt. 205.3(e)(3)).
144. S*ee Brief of the United States Securities and Exchange Commission, Amicus Curiae*, *McKesson HBOC, Inc. v. Adler*, 562 S.E.2d 809 (Ga. Ct. App. 2002).
145. *Id.*
146. *Id.*
147. *Id.* Other situations in which work product was deemed sufficiently beneficial included an instance in which the SEC obtained a report on which an accounting firm had spent 29,000 hours in preparation and another in which it received the results of an investigation that had cost $9 million to conduct. *See id.*
148. *Id.*
149. *Id.*
150. "Department of Defense Voluntary Disclosure Program—A Description of the Process." IGDPH 5505.50 (amended April 1990).
151. Letter from Deputy Secretary of Defense William H. Taft IV, to defense contractors (July 24, 1985).
152. "Department of Defense Voluntary Disclosure Program—A Description of the Process." IGDPH 5505.50 (amended April 1990).
153. Publication of the OIG's Provider Self-Disclosure Protocol, 62 Fed. Reg. 58399, 58399 (Oct. 30, 1998).
154. *Id.* at 58403.
155. *Id.*
156. Incentives for Self-Policing: Discovery, Disclosure, Correction and Prevention of Violations, 65 Fed. Reg. 19618, 19618 (April 11, 2000).
157. *Id*. at 19623.
158. *Id.*

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Rules, Guidelines, and Personal Preferences: Commercial Division Judges Discuss Procedural Issues in Complex Litigation

What follows is a panel discussion among ten New York State Supreme Court justices held at the Spring 2003 Meeting of the Commercial and Federal Litigation Section. The first part of the discussion focuses on the variations in the rules and their application across the Commercial Division. The second part focuses on issues common to complex litigation. The panel included ten Supreme Court justices in the Commercial Division: Hon. Leonard B. Austin, Nassau County; Hon. Louis C. Benza, Albany County; Hon. Elizabeth H. Emerson, Suffolk County; Hon. Carolyn E. Demarest, Kings County; Hon. Ira Gammerman, New York County; Hon. Richard B. Lowe III, New York County; Hon. Joseph G. Makowski, Erie County; Hon. Kenneth W. Rudolph, Westchester County; Hon. Thomas A. Stander, Monroe County; Justice Beatrice Shainswit, New York County (ret.); and Hon. Ira B. Warshawsky, Nassau County. The discussion on rules and guidelines was moderated by Robert L. Haig, a partner at Kelley, Drye & Warren LLP. The second part of the discussion focused on practices and procedures and was moderated by Mark C. Zauderer, a partner at Piper Rudnick LLP.

Part I: Rules and Guidelines

MR. HAIG: Let me start with a brief introduction to the topic of rules. You may say rules are not all that interesting and not all judges adhere to their rules on absolutely all occasions. I do think, though, that the rules in the Commercial Division probably have as much visibility outside the state of New York and maybe inside the state of New York as any other set of rules. For example, the definition of a commercial case in New York is something that has been debated literally all over the United States.

And they are also important here. They are important because there are some basic questions we hope to address today: Should the rules benefit the bar? Should they benefit the judiciary? Should they benefit the clients? How are they being applied? Are they fair? Are they efficient? Are they being used consistently? If departures are made, does the bar understand them?

I'm going to ask the judges a number of questions. I've done a little bit of due diligence and have attempted to find out about particular rules that both the bench and the bar have expressed some unhappiness about.

Let me start with a basic issue of adherence to the rules. Judge Makowski, you have got some local rules in Erie County. How rigidly do you adhere to your court rules?

JUSTICE MAKOWSKI: You know, they are there to set the table in terms of how we move cases and process cases in Erie County. I adhere to them—I won't say rigidly, but routinely. I try not to hurt lawyers through the rules. So if somebody has got a problem, then we'll sit down and talk about whether he or she wants a continuance or figure out how are we going to deal with this problem. I will adhere to them if I think a lawyer is trying to go outside the rules. Example, giving me surreply papers, which are prohibited, and trying to throw them at me at the bench on the day of oral argument, or trying to get around trial orders.

In Erie County, I consider it one big symbiotic partnership, you have your job, your opponent or opponents have their job, and I have my job. It is hard enough to get to the merits, so I try not to let the rules become an obstacle or an impediment to the process. But they are there.

Now, having said that, periodically something will happen and I'll just waive my rule. And it is my rule, so why can't I waive it? I'll just waive it, and people are always stunned. One lawyer came out and said to me: You can't do that. And I said, well, I just did; take me up.

The bottom line is that the rules are a framework on how we get cases processed in the Commercial Division. I like the lawyers to be aware of them, but they are not a club. I don't try to beat people up with them. I don't want people ignoring them or trying to take advantage, but Rule of Reason is the order of the day.

MR. HAIG: Judge Gammerman, you really don't use the Commercial Division rules in your part. And arguably, you really don't have any set rules. If that's not a fair statement, I will stand corrected.

JUSTICE GAMMERMAN: I have some rules, but they give me much more flexibility. First of all, I don't use the rules because I'm not familiar with them. My feeling is that by and large the lawyers are highly skilled, highly professional, and they really need very little guidance as to how to handle the case. When I meet the lawyers for the first time, generally either on a motion or a preliminary conference, I'll tell them how

the case is going to be handled and I expect them to follow what I tell them. And if there are problems, either we schedule a conference or I deal with it over the telephone. Sometimes the lawyers don't realize that the rules don't apply in my part, and they submit names of witnesses and they prepare trial books, which are very helpful. I would say they do it in most cases. Indeed, before the rules were ever enacted, lawyers who were skilled litigators prepared the exhibits, and worked with their adversaries to mark the exhibits.

Indeed, I don't think I like the rule about motions in limine. My own view is that in non-jury cases motions in limine are totally unnecessary. You can decide what's admissible as the trial is being conducted. And in a jury case, I like the lawyers to discuss the evidentiary issues right before the selection of the jury. I think the rules just generate paper, and I think we have far too much paper as it stands.

MR. HAIG: Let me pursue the motion in limine. There is a rule in New York County, it is Rule 29, and it says that motions in limine have to be made at least five days prior to the trial. People who are involved in the managing attorneys' offices say they have no idea whether opposing papers are permitted, whether reply papers are permitted and, if so, when those papers are to be submitted. They also complain that they don't know whether the motion in limine is supposed to go to the court office or to the individual judge, and they don't really understand how the court tracks motions in limine. Maybe I could ask the judges, when are the opposing papers due? And are reply papers permitted?

JUSTICE AUSTIN: In my part what we do is when in limine motions are made, an opposing attorney will invariably call me and say what do I do? What I'll generally do is give him or her the option. You may put in opposing papers, since it is only five days notice, or come in and argue it, and we will just take argument before the trial begins, with or without papers. The motion is calendared and we just take it at the beginning of the trial. I give the attorney the option as to whether or not to oppose it in writing.

JUSTICE LOWE: I try for the most part to handle motions in limine by way of oral argument. One side will present what they are trying to limit or what they are trying to have the court rule on, the other side will oppose it. I try to make a decision at that juncture, unless it's a complicated matter. But if that is the case that should have been done long before the five days before trial. I try to do it when we have the pretrial conference, before the trial date is set, or when the trial date is set. That is when I talk about all of the things that have to be cleaned up before we actually start the trial.

MR. HAIG: Is there a sense that it is appropriate to handle these kinds of motions differently for different judges depending on their preference, or do you have a sense that maybe this ought to be codified a little bit more, so that the bar will know how motions like this are supposed to be handled?

JUSTICE RUDOLPH: In Westchester we have a ten-day filing period, and perhaps at some point in the future I think all these rules may get some degree of similarity.

I would certainly defer to Judge Gammerman. But in my view, the reason I want the motions in limine as far in advance of the trial as practicable is because every week I either set up two non-jury trials and one jury trial or two jury trials and no non-jury trial with the hope that something is going to settle. By having the motion in limine ten days in advance of the trial, I have an opportunity to see what those issues are. I find most of them are rather complicated or complex or serious issues of evidence that must be decided, and they must be decided, in my opinion, certainly in a jury case, before the jury is selected.

If I get the motion in limine on the day the trial is scheduled, then everyone is going to be delayed, and possibly they won't even be able to select a jury if I'm in the middle of something else. I'm a one-man show in Westchester County, like a lot of the other counties that are here, and I think it is kind of important that be done.

I do see a problem starting to unfold. While motions in limine must be filed ten days before, the lawyers often make the motion returnable on the day of the trial. That has to be tightened up a little so that reply papers and so forth arrive prior to the date that people come to trial.

Where to file the papers is the only other point I want to mention. It doesn't really make much of a difference to the attorneys whether they file the motion with a court clerk or the central processing part of the court. However, as far as the judge is concerned, at least in Westchester County, if you don't file the motion with the central motion part, then the judge cannot get credit for the motion. If you file your motion in limine in Westchester County, please file it across the street so I can get credit for the work I do.

Rule 16—Pre-Trial Conferences

MR. HAIG: Let me raise another rule with you all that I've heard some unhappiness about, and that's Rule 16 of the New York County Rules having to do with conferences. There are three judges, Judge

Moscowitz, Judge Friedman and Judge Ramos, who have adopted a version of Rule 16 that flatly says no adjournments of conferences are permitted. It doesn't have any exception for good cause or anything like that. There are some members of the bar that have said that they don't like the sound of that. Other people say maybe it is not particularly realistic, and yet others say well, they do grant adjournments from time to time, and if you are going to grant adjournments, why would you have a rule that says no adjournments under any circumstances? It raises questions about inconsistency and potential unfairness. I wonder how you all feel?

JUSTICE LOWE: I think that what's behind this rule is that very often, lawyers will agree to adjourn or to delay or to go beyond the parameters of the discovery rules that have been set out. You get together for your discovery conference and you set the dates for your document discovery, for your EBTs, etcetera, and then they, the lawyers, will call each other and say well, we'll delay that. All of a sudden you'll get a stipulation sent to your chambers that we've agreed to extend the note of issue date to whatever.

JUSTICE EMERSON: We call those self-help adjournments.

JUSTICE LOWE: I think the rule is really trying to say you don't have the right to agree to violate a court-ordered requirement. You can call and say, Judge, for whatever the reasons, we would like to extend this date or extend that date or extend this conference, and then set forth your reasons. I don't think there's a judge here who would not grant the request if he or she felt that it was reasonable. But it's the self-initiated decision that we can agree to adjourn, without even notifying the court, and that may be behind that particular rule.

JUSTICE EMERSON: The other big issue I'm sure for all of us is scheduling, particularly with conferences where we're blocking out a significant part of our schedule to be able to deal with a particular matter. It becomes difficult, if not impossible, to reschedule things that you have tried to put aside enough time for so that you're efficient.

I do not think that any judge would never adjourn a conference, but when you're running a calendar, when you have trials and conferences and other matters all booked together, you need to be very cognizant that you handle everything appropriately.

JUSTICE BENZA: That's a perfect example of why you have to have commercial rules. If you take a look at the commercial rules in Albany County and the court rules of the court itself, the court rules allow for this self-help adjournment, but the commercial calendar does not.

The commercial judge is trying to get all of his or her time lined up, so that it's used beneficially. Judges have a tight schedule and when they fit something into it, they like to see that the schedule is kept. If lawyers keep playing around with it like that, you're never going to get anything done.

JUSTICE AUSTIN: One of the other things you have to remember is that looking at these conferences in a vacuum is not really an appropriate point of reference. It is a conference that's on the continuum that's leading you to trial.

I know in Nassau, at the time of the preliminary conference, we set the trial date, and those trial dates tend to be rather inviolate. If you're going to keep pushing off the conference for certification, status conferences, compliance and the like, then sooner or later we are going to get that phone call that says we need to push the trial date. And that becomes very problematic.

I've got a trial calendar that's set into December of 2004. And I'm going to then have to play with this trial because the conferences kept getting adjourned. Of course, within reason, if you need another couple of weeks or whatever, we build that into the schedule, that's not a big deal. But ultimately it comes down to the trial date. That's the problem.

JUSTICE MAKOWSKI: It comes down to the age-old problem: Who is driving this bus? Who is managing this case? Who is managing this calendar? I think my calendar is about 250 cases, give or take, and I'm sure the other judges have calendars the same size or larger. You have X hours in a day, X hours in a week and somebody has to drive the bus. So am I going to drive the bus? Am I going to let the lawyers drive the bus? Or are we going to drive the bus together? I have to manage cases. That's what they have to do. That's the way the system is set up. Under Standards and Goals, you get these nice little memos, if you don't get your decisions in a certain amount of time. This is all very real stuff. It goes to quality of life. My quality of life. And so we do take it seriously. I don't know about *no* adjournments. Maybe they are trying to set a tone. But from my perspective, I go back to that partnership concept: you've got to manage the cases. If you don't manage the cases, you don't get them disposed of.

For me it is about case management and not having a whip and a chair but using the tools that are available. Preliminary conference orders, compliance conferences, discovery conferences, as Judge Austin says, we are all here trying to move cases down the continuum.

JUSTICE EMERSON: The last thing I would say is a lot of times when we put a case on a calendar, other

than a PC or certification conference, it is because there's something we want to achieve, something has come up in motion conference, or we have looked at something and we have an issue we want to resolve, explore, and get the case ready. So there's a substantive reason you got a notice saying to appear on day X or Y for a conference.

Now can we adjust that? Absolutely, everyone has his or her individual schedule. But when we put you on the calendar, we are not only looking at where you are, but where everyone else is as well. We are trying to manage everybody appropriately.

Unifying the Rules Across the Commercial Division

MR. HAIG: Let me move onto another topic for a minute. We have got eight different counties, and the rules vary fairly substantially in some respects. Is that something that is being considered?

JUSTICE AUSTIN: My view is, and I think I share the view with many of my colleagues, that the time is coming when the Commercial Division becomes statewide, and attorneys from one county are going to be coming into another county and practicing commercial law. I believe there is a need for a common set of rules. Many of us have rules that are parallel, at least from an organizational perspective, but then each of our rules can have their own nuances attached to them. We should be trying to cut those nuances as best we can so that a commercial practitioner going into Suffolk, or Albany, or wherever is going to know the playing field. Obviously knowing whatever the local needs are or needs of that particular judge can be very advantageous, and we are going to try and change that.

JUSTICE MAKOWSKI: We have got to take a look, is this a procedural rule or is this rule having something to do with the types of cases you're going to hear? I recently broke the plane on commercial foreclosures with large complex buildings. I may be the only judge to do it. But I have a lot of distressed real estate in Buffalo, New York. The bar said we would really like somebody who is paying attention to the preservation of our assets. I think if it is procedural, you may well see this commonality. My thresholds will always be lower than Nassau County. I'm in Buffalo, New York, why wouldn't they be?

JUSTICE EMERSON: I would just add that the local issues are the ones that are probably going to be the most complex to sort through. I had the opportunity and the privilege to visit many of the working commercial divisions before we started to establish the one in Suffolk, and it allowed me to explore the differences between the divisions and to compare the ways that we handle ourselves administratively.

While at first blush you assume that both Nassau and Suffolk are similar, we have very different administrative approaches. We still work off of a TAP system, and it is a very healthy and viable TAP system near and dear to the hearts of our Bar Association. And it does create differences in the way we select, assign and handle our Commercial Division cases. I also carry a full civil calendar as well as the Commercial Division calendar. So you have to blend those things into the procedural aspects of the Commercial Division itself. I think that will be a challenge to uniform rules—respecting and working with the local needs of the different divisions.

JUSTICE DEMAREST: I would like to throw something back at the Bar Association itself. I'm the new kid around here, Kings County. We are just starting out, and we started out using other counties' rules, and then we invited the bar to come in and discuss with us how they preferred things to be done. But my question to the attorneys is whether they would rather have the judges formulate uniform rules of their own and dictate what to do, or does the bar want input?

JUSTICE SHAINSWIT: I've been sort of troubled about just that point. I don't really understand why we are ignoring the rest of the court. There are rules regarding all the judges in our court, and the lawyers grow up learning all the rules. I'm not quite convinced of the need for a separate batch of rules, especially rigid rules of the kind where you can't under any circumstances get an adjournment. I never really had rules of my own, because I thought the rules of the court were perfectly fine rules, and the lawyers would know that I would enforce them, not severely but with honor and discretion. And the more I hear about this, the more troubled I am from the viewpoint of the bar and all these new rigid rules they have to abide by.

JUSTICE BENZA: Well, I think we need the rules because lawyers have to know what cases go into the commercial part. The rules of the court don't tell you that. That's one of the reasons why the commercial part has their own rules. The courts tell you what the jurisdictional limit is, and they tell you what type of cases. I guess that from then on we, the judges, just made up some other rules hoping to make it easier to get the cases moving. Maybe we should take another look at that part. But you have to have rules. You have to know what cases go into the part, and you have to know the jurisdictional limitations.

JUSTICE STANDER: I always thought the reason for the rules was the protection of the bar. There are a lot of attorneys that come to Rochester from New York County, and they know there are Commercial Division rules. They look them up on the Internet and know

how I run my court. So they are prepared to come to Rochester, knowing that I have rules.

But the reason for the rule is that I have a calendar call, and if you don't respond to the calendar call, the case gets marked off. Everyone should know that he or she can respond electronically; they don't have to come to Rochester to respond to a calendar call. I feel better marking it off having called it, after not hearing anything in two years about a case, because I've warned all the attorneys that I have this regular calendar call that can be answered on the Internet. I think that's protection for the attorneys if they want to take the time, energy and effort to look at the rules.

The rules are there as a guideline for everybody. Yes, they may be broken in some cases, but they are also there so that we can run our court as efficiently as possible. And frankly, attorneys come in and quote rule numbers to me, and I don't know what they are. I just know how I run my court, and I'm trying to share that with you, so that you can better perform for your client in front of me.

JUSTICE MAKOWSKI: Certainly in '99 when the Commercial Division was created in Erie using the model rules, my colleague, Justice Nemoyer and myself sat down with the commercial bar, literally, to put the rules together for Erie County. And every time I'm thinking about a rule change or modification or a new rule, it is only after a dialogue with the local commercial bar, through the Bar Association, and in consultation with my administrative judge, that we make the decision to change this rule or not.

I think it is a two-way street, or it can be a two-way street if you want it to be a two-way street. I think that it is a very healthy thing, because we are here to service the commercial bar. So that is the way we have done it in Erie, and I think that's the way we'll continue to do it.

JUSTICE AUSTIN: I think there's a certain realistic approach that has to be taken. And for all of you out there, you know as well as we do that, for the most part, these are not the ten exhibits and half-a-day trial cases. These are cases that encompass exhibits that are higher than the pile of books that we got as part of the program here this weekend. The amount of paper, the amount of effort, the complexity of the issues, all mandate that judges with limited resources do the best they can to manage what is a very difficult, very complex, very heavy calendar and type of case. To do it without rules—making it something like the Wild West—is going to just confuse us, bog us down and not give us the opportunity to be able to effectively manage your case. You want us to be able to do that, and your clients certainly want us to be able to do that. So we all operate under a set of rules that enable us to accomplish that.

Motions for Discovery

MR. HAIG: Let me move onto another topic having to do with motions and pre-motion conferences and the recent decision of the Appellate Division in the First Department. Why should a lawyer making a discovery motion be required to contact the court first?

JUSTICE BENZA: Well, again, it is the congestion that exists in the calendar, and nobody needs motion practice when they don't have to make a motion. I can't remember the last discovery motion that was made. What I tell the lawyers in our conference is that if you have a discovery problem, don't make a motion, call me. I don't tell him or her you can't make the motion. I say call me before you make a motion. And I've been able to successfully stave off any discovery issues and decide right then and there. Usually the parties agree. Otherwise I'll call them in for a conference, have each lawyer argue his or her side, and decide it right then and there without the necessity of the motion.

JUSTICE AUSTIN: I think it is fair to say none of us like discovery motions. They should be unnecessary. And dealing with them informally is really the best and most efficient way to accomplish it.

JUSTICE STANDER: You have to understand, when you're talking about a discovery motion, there's usually six pages of "we need this" and seven pages of "answers," and you've got to match them all up. It is very difficult to do that on the bench. I don't have the same rule requiring a lawyer to call me. But what I do is take the application for a discovery motion, and I hold a conference, without reply papers, to see if we can resolve the issues in conference. If we can't, then I'll set it for a return date.

Sometimes there are true discovery issues that need a decision and may go up on appeal. But most of the time the lawyers get to conference and resolve their issues. So to clog up all our calendars with discovery motions and regular return dates doesn't make any sense. And it doesn't work even if it gets there, because it takes too much time on the bench to sort through what has been provided, what wasn't answered, and what's really in dispute.

JUSTICE MAKOWSKI: You can make a motion. But what I do is I immediately send it to my court attorney or to my judicial hearing officer or to my law clerk to try to resolve it. And then if they can't get it done, then I'll hear it. The point is that we try to get them resolved.

Now, a caveat on motions. Some motions are very important. I mean people start asserting the attorney/client privilege, the work product privilege, and it really matters. Then I have to pay attention, because that's going to shape that case. But do I want to sit there and say whether or not you were responsive to interrogatory 59C? No. But if it is a big important discovery motion, like whether you played straight on the expert disclosure under 3101, then I should be making that call. But the routine he or she didn't turn it over and we know she's got it? No, go away. But big discovery motions with really important technical issues do merit my time.

JUSTICE WARSHAWSKY: I think it is very clear that we don't have the time or the staff to handle what you're used to as discovery motions. We all know the CPLR controls. We know you can make your motions legally. The point is that there is not a discovery issue, I believe, that can't be decided by a conference call or by a conference. One of the problems I understand is that you write your letter and you don't get a call back from chambers in some cases. Well, there are sometimes reasons—there are always reasons, sometimes it just slips through the cracks. But for the most part in my chambers, when you get an attorney who seems to be billing on the basis of how many letters he writes or how many faxes he sends and the court is inundated by a particular attorney on a particular case, well, maybe we start ignoring that attorney's letters. It is the old boy who cries wolf situation. I have found out by speaking to my law secretary that she did that on occasion. I said we can't do that. We have a rule; we have to follow it. But that's why I think sometimes that happens. But yes, we are going to have the rule, and we are going to have a letter rule. If you request the opportunity to make the motion, then we must respond to it, or we have to change the rule.

JUSTICE AUSTIN: I think the genesis of the rule is that we want the chance to resolve the issue before formal motion practice is necessary. *Hochberg v. Davis* is very clear: We can't stop you from making the motion. We all understand that, but if you give us the chance to narrow the issues, resolve the issues, look how much we've all saved. And if we can't resolve the issues, then with our calendar issues, at least give us the chance to schedule a motion so that it is not going to be adjourned six times and clog up our calendars that way. We'll ask you how long you need to make the motion. How long do you need for your response? And we can set a return date that's convenient for your schedule and ours and be able to dispose of the motion in a much more efficient manner within the context of the scheduling that we have.

But we want and need that opportunity. Not that we are ever going to say no you can't. But at least do it within a framework that gives us the opportunity to say maybe you don't need to, or let's do it in a way that we can all work together on it.

JUSTICE DEMAREST: One of the things we can do is conference calls. My fairly limited experience at this point is to get everybody on the same call and just flesh out what the problem is. It is more efficient than all the papers and the delay. And you're reading words on a piece of paper, but you all know that you can get a lot more out of a direct conversation, even if it is on a telephone, than you can by written communications, where people sometimes obfuscate the real issues. So I think it is a lot more efficient, and it should be beneficial to you as well.

JUSTICE LOWE: Looking at the genesis of this question, the bar is primarily responsible. Rightfully so, the bar asked to have the Commercial Division created, for very valid reasons: to have complex litigation handled in one area of the courts or one court (depending on the location), so that it could speed up, streamline and unify the litigation of these kinds of cases. These rules were created in order to facilitate that objective.

I want to echo two things that were said about discovery motions. One, 90 percent of them should be resolved by the lawyers themselves. One of the most annoying things is to have lawyers come in and bicker.

The second thing is we expected and we were told, that the caliber of the bar that would be practicing before us was going to be significantly higher. And it is. But there are some practitioners who belie that perspective, and it manifests itself most often in the area of discovery. These are issues that shouldn't take our time. When they file a motion, and it goes to motion support, and from there they schedule it, and there's an answer, and it comes back to us, that's an enormous waste of time on issues that could be resolved by the attorneys themselves.

JUSTICE GAMMERMAN: There's no need for a motion, and indeed a record on discovery issues unless there is going to be an appeal. I tell the lawyers I'm going to decide it, and that if you're going to appeal it, we'll make it a record. If you're not going to appeal it, then let's move on. There are some matters that take a great deal of time. I've been fortunate enough to get the lawyers to agree to hire somebody to supervise discovery in these cases involving, let's say, a hundred thousand documents in which attorney/client privilege is claimed for 35,000. And that certainly relieves me of the responsibility of doing that. I would never do it, but somebody in the court would do it. Unless there is

going to be an appeal there is no need for discovery motions at all.

Rule 25(a)—Letter to the Court

MR. HAIG: Let me move onto another question. Judge Warshawsky, you mentioned this a minute ago, and that is the requirement—I think it is in 25(a)—which is the subject of the recent Appellate Division decision. Now, Judge Warshawsky said there are some lawyers out there who write too many letters. Clearly that's true. But how about a lawyer that's got a meritorious motion, he or she writes a letter to the court, and the court just doesn't respond to the letter. And there may be time considerations, it may be related to other things that are going on in the case. Is a requirement like that appropriate? And if so, shouldn't the judge respond to those letters within some period of time?

JUSTICE MAKOWSKI: It goes to how you respond. I don't have time to sit down and write letters. So I'll get these letters, whatever they are, and I'll schedule a conference call, and we will discuss it. But what am I going to do, sit there and answer every piece of correspondence that comes in? I have to move cases. I may say to Pam, I want these lawyers in here in the next two days. Let's get a conference call scheduled. Let's do something. Get my court attorney to do something. Being a judge, I can respond to communications any way I want. I often choose to pick up the phone and say I got your letters, let's sit down and talk about this, or do it on conference call. It is a little bit unfair to say the judge didn't respond to my letters. We generally respond. We just respond in different ways.

JUSTICE EMERSON: Bob, one thing that might be helpful is the information contained in the letter. Sometimes you get a nine-page letter that goes through all the various problems. It is very hard to sort through that and figure out what it is you're being asked to do as well as what you should be doing given your role in the case. One thing that I think would be helpful is if what you're looking for is the opportunity to either have a conference call with the judge or to have a conference with the judge, to confine your request to that. We have an issue, it is an urgent issue. In some respects I don't even think we need to know what the issue is. We would benefit from a conference. If both sides agree, I can't imagine that anyone up here wouldn't put the case down for an immediate conference. If there's a dispute, maybe you need to give a little bit of information as to the dispute and/or why it would benefit from a conference. But again, the problem is—and I can think of one case in particular, there is not a day that goes by when I don't get five or six pieces of paper from each side. And those are the cases in which you do start to say maybe I should put a no-correspondence-rule in effect for this case. A succinct request that can be easily disposed of or responded to would be helpful for us and probably helpful for the bar.

JUSTICE STANDER: And what is particularly ineffective is at the bottom of correspondence going back and forth between counsel to say "and by copy of this letter I am asking the Judge to . . ." I don't pay any attention to correspondence not written directly to me. I don't respond. I don't even set a conference. If they are writing each other, they can copy me all they want and I glance at them and put them in the file. But if you want a response from the court, direct your correspondence to the court.

JUSTICE AUSTIN: I invariably tell lawyers that I am not their pen pal. And when it just keeps escalating, what I will do is one of three things. When I get a letter seeking some relief, I will either write a note on it to tell my secretary to set a phone conference, and I usually do my phone conferences from 4:30 to 5:30 in the afternoon; I will tell her to get the parties in within two or five days; or I will pick up the phone myself, call the writer of the letter and say get your adversary on the phone in twenty minutes, and we will just deal with this. Also, if it is important enough, I'll get a court reporter in there and do it on the record, and we deal with it very, very quickly. If you're going to send a letter, we have some emergency, we need to see you right away, we need to address this, at least in your letter please include the next date you are scheduled to be before us. I just dealt with one and got them in, and the lawyer said well, I guess our conference for two days from now doesn't have to happen. I said we hustled like this to get this all together, and we were going to see you in two days anyway? That's not right. At least let us know the next time we are scheduled to see you, so we can determine whether or not we need to expedite.

JUSTICE EMERSON: I don't think people realize how many letters we get where we truly can't figure out what people want. It is not for want of verbiage. Do you want me to do something? Are you complaining about your adversary? Do you want me to know that the other side is not doing what they are supposed to be doing? You obviously know what you want, but it is not always clear to all of us.

JUSTICE MAKOWSKI: And the root cause is that a lot of these letters get written out of frustration because the other side isn't giving you the materials in discovery or didn't show up for depositions or didn't do something. So you're not playing nice, so you want us to do something about it. And we will do something about it, because we have got to manage the case. But you really have to take a step back and say is the real

problem the lawyer on the other side, or can I sit down and work it out with him or her before I go and ask the court to do something?

JUSTICE GAMMERMAN: I don't read the letters. They are read, but I don't read them. My law secretary reads the letters, and she brings to my attention every two or three days things she thinks should be brought to my attention based on what's in the letter. We have everything on the computer. The first thing she will ask me is when is this case on again, so we don't have that problem. If I see the parties are coming in to see me within a week or so, we ignore the letter completely and we will discuss it with them when they come in. If, based on what she tells me, some action has to be taken, I tell her what action has to be taken. Generally, it is a phone conference, and either she will call both sides and try to resolve the issue, or if necessary, I will call.

JUSTICE AUSTIN: That's why there's a two-page limit on those letters.

JUSTICE WARSHAWSKY: I received a letter that was bound with a plastic thing. It was twenty pages long, and this was a letter requesting the right to make a motion. I mean please, that's just not right.

MR. HAIG: What are your thoughts about the recent decision of the First Department on pre-motion conferences? I think some people have the sense that the First Department was extending the Commercial Division a very substantial amount of discretion and latitude out of appreciation for the job that the Commercial Division judges are doing in general in New York County, and out of a recognition that they are difficult cases and that they require a fairly aggressive case management approach.

JUSTICE AUSTIN: I think we need to be able to keep some control as to the flow of what comes in to be able to respond appropriately and timely. Rule 25(a), to the extent that it says you may not make a motion, is incorrect. That's clear case law. However, I don't believe that the First Department was telling us that we can't control our calendar or that we can't try to resolve matters before it gets to the motion stage. I know there are some judges who will take a motion that comes in without a pre-conference and use that as a request for a conference, and then not schedule the motion until significantly later. The effect is the same thing. We need to be able to have the opportunity to conference and resolve things before it gets to the point that we have to review the motion papers and write.

JUSTICE RUDOLPH: I think that the root of the problem here is not the decision of the First Department or permission to make a motion or reading the letters that you send. I think the problem is somewhat analogous to the discussion that's sort of developing about the uniformity of rules. There has to be some uniformity of resources. The Commercial Division, as it was created, has mushroomed and developed into a very litigious part. The average judge, at least from what I see, receives about 20 to 25 motions a week, excluding discovery motions. So we are talking about a judge and his law secretary, who are dealing with somewhere between 800 and 1,000 motions a year. While the judge's law secretary is locked in his room, the judge is in the trial part, handling the trials, jury and non-jury, motions in limine, etcetera. At times, when the judge has some spare time, he also pitches in with the law secretary to help out on drafting decisions. So the last thing a judge wants to do is (a) read a letter or (b) handle a discovery motion, which you certainly are entitled to in many, many instances, as has been pointed out today. I think that while the bar would like to see some uniformity of rules, and I can certainly appreciate that, and I think there should be, there should also be greater resources provided to the Commercial Division to support the commercial litigation that is presented to us on these many complex issues.

JUSTICE MAKOWSKI: There is an important point in the First Department's decision, and it's something, frankly, under the pressure of the moment, trial judges forget. When you write these rules, they are process rules. But you cannot affect a substantive right or right of access or cut off a party. And sometimes you really have to sit back and say what is this rule designed to do. One of my colleagues had recently written to a trial lawyer and said, disclose your witnesses. Somebody came in with a witness that wasn't on the trial list. And the judge said, well, not on the trial list, go away, he can't testify. The Fourth Department said that this is wrong, an abuse of discretion, and reversed the verdict. So the party trying to get their case in generally couldn't get the witness in, and it was outcome-determinative. It wasn't a harmless error. Because they made an offer of proof and the whole nine yards. So this is an important point here, but a subtle point. The process cannot adversely impact access to justice or the outcome. We have to be careful when we write these rules so that we are not doing that.

Dispositive Motions and the Stay of Disclosure

MR. HAIG: Let me mention two other rules. One of them is Rule 12 of the Judges Commercial Division in New York County that says that a dispositive motion will not stay disclosure unless the judge directs. And Judge Cahn has got a special version of that. I think he's the only judge that does this, which says a dispositive motion shall not stay production of documents under any circumstances. And as to other kinds of disclosure, the Judge will consider them on a case-by-case

basis. I would like to raise that to you. And then the final one is Rule 19(a), again of the Judges of the Commercial Division in New York County, which says that on a summary judgment motion you have to submit a statement of undisputed facts. I toss both of those up for any comments that you may have.

JUSTICE AUSTIN: Well, Rule 19(a) is no different from Rule 56 in the federal practice. And it gives us the opportunity to discern very quickly where the issues really are. Again, it is a management issue more than anything else. It gives us the ability to get to the heart of the issue in a much more efficient manner. If they don't want to come to us, okay. We have got plenty of business.

JUSTICE EMERSON: It is a generalization, but many times you find with these cases it is not so much the underlying facts or the result those facts dictate. People are not denying the existence of certain events. Rule 19(a) is a very efficient way of getting to the heart of the matter. And as you would in a trial, you wouldn't want to prove things that you don't need to or that aren't relevant to the issue to be decided. The same thing with a summary judgment motion. If you can't do it, obviously everyone understands. If there are truly facts in dispute, then they need to be resolved in the proper fashion. But if you don't dispute that something happened on Wednesday, those are the kind of things that you don't want us worrying about.

JUSTICE DEMAREST: It is issue-framing. It just makes sense. It saves a lot of time for us in trying to wade through people saying things in different ways and arguing points that don't have to be argued at all.

JUSTICE LOWE: With regard to the first rule, in terms of dispositive motions not staying discovery, I think most of us would agree that that's the general rule. And the reason for it is that a good 90 percent of dispositive motions do not dispose of the case. The time delay from the filing of that motion until its ultimate decision can often be extensive. Very often I will stay discovery after the oral argument, because my sense is that the motion is going to dispose of the case. Again, it is a question of: one, resources, and two, trying to make sure that that case stays on track and doesn't lose a great deal of time. Because as was mentioned before, we have the sword of Damocles over our heads, and it is Standards and Goals. Believe it or not, we have to deal with that. We get these letters from OCA, from the administrative judges, asking us to explain why these cases have not reached whatever particular stage it is supposed to be at. And we have to take time to write a letter of explanation. So the objective of these rules, as I've tried to say before, is to assist in getting these cases from point A to point Z.

JUSTICE AUSTIN: I think the discovery thing is something of a tempest in a teapot. In my part, we won't take dispositive motions until discovery is complete. Because I don't want to deal with a 3212(f) situation. How can you decide summary judgment, Judge? We still have discovery to do. In that case, if the attorney insists on making the motion, I'll take the motion and adjourn it *sine die* until discovery is complete.

Part II—Other Practices and Procedures

Introduction of the Hypothetical

MR. ZAUDERER: Let me pose this hypothetical to set up our discussion. The W.T. Smith Company is a small company that operated for some 70 years in a walk-up loft building in the west 20s in New York City. And it had a specialized product called paper folders. It is a little device that is made with some simple tools that are used to wrap wire, which in turn is sent to the cable and wire industry which completes the production of insulated electrical cable and wiring. It is a small company. It was started by W.T. Smith early in the 20th century, and had over the years reached 20 or 25 employees. Beginning in the late '40s, a young man named Baker began working for the owner and worked his way up until he eventually took over the ownership of the business when Mr. Smith retired. His wife, who had some accounting background in college, would come in from time to time and assist with the bookkeeping. The business profited modestly for many, many years into the 1990s. It had some 40 customers in the wire and cable industry, very loyal customers who bought the paper folders that were made. Unfortunately, in the latter part of the 1990s Mr. Baker became ill. He was diagnosed with cancer. And indeed, since the business certainly had been the love of his life, even in his struggling terminal illness, he managed to come in three days a week and walk up these steep stairs. Fortunately, he had the assistance of an office manager, and actually a grandson of the founder, W.T. Smith. His name was Michael Smith. Michael knew the whole business, knew the customers and certainly appeared to be of great assistance in this time of struggle for Mr. Baker. Then, unfortunately, in the late 1990s, Mr. Baker died. Mrs. Baker, not wanting this business to fall by the wayside, came in and started to look at the books. She saw that for the last year or two the business had declined some 25 or 30 percent. It was a puzzle to her. As she began to look further into this, she focused on one customer, the Acme Cable Company, whom she knew. She didn't understand it. She called up the buyer there and said, what happened to your business? The person said they had received instructions some time ago to send all payments to the Smith Company at an address in Brooklyn. She began to look further and

looked at some of the shipping records in the company, and she saw indeed there had been shipments charged to the Federal Express account of the company for shipments made from Brooklyn. Befuddled at first, she later approached Michael Smith, who had been managing things while her husband was ill, and said what's going on here? And he had not much of an answer for it. One thing led to another, and Mr. Smith quit and walked out. Now, Mrs. Baker, putting two and two together, realized she had a serious problem on her hands and believed that Mr. Smith was the cause of it. In fact, she hired a lawyer, went to court and she started a lawsuit. She accused Michael Smith of violating his duties of employment and taking customers in violation of his responsibilities, his obligations to the company. In connection with that lawsuit, which found its way to the Commercial Division, an application was made for a temporary restraining order and a preliminary injunction. In particular, the temporary restraining order application sought to stop Michael Smith from soliciting customers of the W.T. Smith Company and continuing business with any customers he may have taken in violation of his obligations of employment.

Now, Justice Rudolph, this application comes before you by the lawyer for the plaintiff, and a temporary restraining order is sought *ex parte* to that effect, and you were told this is an emergency. My company is bleeding. Will you hear that *ex parte*?

Temporary Restraining Orders

JUSTICE RUDOLPH: I would. I know my rules differ in this particular area. Many, if not most of the cases that we receive originate with an order to show cause seeking a temporary restraining order. In those types of cases I examine the papers very carefully. In this case, I'm sure Mrs. Baker would have a detailed affidavit and probably a number of exhibits which would lend credence to her action, and demonstrate that there was a serious reason and cause for issuance of a TRO. I would issue the TRO based on the fact pattern that we just heard, but I would give it a short return date, perhaps the next available motion calendar which would be every Friday. So if this was a Monday, I would make it returnable Friday and then arrange for expediting service of process. My philosophy is, if the papers warrant the issuance of TRO *ex parte* without notice to the adversary, I would issue it under the principle that I want to make sure things are held in abeyance and the issues are in place and locked. I don't want the horse to leave the barn before I close the door. I do not issue a TRO in every case I handle. I will strike the TRO if I don't think it is warranted. But if I think it is warranted, I will issue the TRO *ex parte* and I will arrange for a short return date on the motion to give the other side the opportunity to be heard.

JUSTICE BENZA: I usually call up the opposing party and say, I got an order to show cause here with a restraining order. I want you to come in and take a look at the papers or give me a submittal within four or five hours, or I'll call both of them in and hear oral arguments and then make a decision based on that.

MR. ZAUDERER: Well, Judge Benza, here we have no opposing party. We have Michael Smith and nobody else. Nobody has appeared. He's just been sued. Who do we call?

JUSTICE BENZA: I'll call the party, say you'd better get a lawyer and come on down with him.

JUSTICE STANDER: I would do pretty much what Justice Benza did. It doesn't seem there is any horse leaving the barn here in terms of a day or two. But if it is truly urgent, if, by giving notice, something is going to happen or more damage will be done, then I'll issue the TRO *ex parte*. Otherwise I try to get the parties in the next day, if not earlier to see if I can find out what the rest of the story is.

JUSTICE WARSHAWSKY: There's no way I would get on the phone or have my law secretary or secretary get on the phone and call any side. The way we work is the party who is bringing an *ex parte* application, or any application that has a TRO in it, has the responsibility of notifying the other side with 24 hours notice and saying: "I'm bringing this action tomorrow afternoon at 4:00 o'clock before Judge Warshawsky. If you want to come it is your right." That's the way we normally work it, but on very rare occasions we will do an *ex parte* TRO.

JUSTICE RUDOLPH: I think this is a typical case that really cries out for an *ex parte* TRO. And I disagree with my colleagues. Here, we have Michael Smith who has a bogus company; I think you said it was in Brooklyn, and he's working for this widow, who has his trust and confidence, and based probably on the relationship with his grandfather, he is actually receiving money from clients, and he is shipping the goods from the Bakers' company. Goods are being shipped, payments are being diverted. You have a classic case of defalcation here. If you notify Mr. Smith, he's going to clean out the bank accounts. And there are a number of things that Mr. Smith can do while I'm waiting for Mr. Smith to show up with his lawyer. And I'm not going give him that opportunity. Now, not every case is as dramatic as the case that has been presented by the moderator. I agree with that. So this happens to fall right into my lap as far as why you may consider an *ex parte* application. Most cases are not of the nature that would cry out for this emergency relief. And as I said, there has been some discussion on uniformity of rules, and I'm reconsidering my point of view. But even if I reconsider that

and do go and adopt the same view as the majority of the judges who appear in the Commercial Division, I think that cases like this should cry out for an immediate exception.

JUSTICE STANDER: My problem is when I have that conference that afternoon or the next day, the other side comes in and says well, Mr. Baker, before he died, signed a purchase agreement with me, and I have every right to do this. And this is a transition period, I have that clear right to ship and receive, and he didn't want to tell Jill because he was on his death bed. So the clear papers that appear before you in the first instance are often not quite so clear when you have that conference.

JUSTICE AUSTIN: Basically, what will happen in Nassau is you'll bring your papers in and you'll see a clerk downstairs named Wanda. You're not going to get past Wanda without having notified your adversary, normally a letter or the like, even if it is to the party. However, if you can give a good argument as to why this one shouldn't be on notice, then she'll send it up and ask what we think. In a situation like this I may well grant the TRO and make it returnable the next morning. But you have to at least make the effort to either communicate with the other side or give a reasonable explanation as to why not, either in your papers or just in a discussion so that we know that at least there's the opportunity for the other side to be heard.

JUSTICE MAKOWSKI: These are always very tough calls, because TROs *ex parte* are kind of unfair ways to start lawsuits, particularly since you're getting only one side. First question, is there counsel on the other side of this thing? And if the answer to that is no, did they just come in Friday at 2:00?

JUSTICE STANDER: 4:00.

JUSTICE WARSHAWSKY: 4:00.

JUSTICE MAKOWSKI: Why do you all time them that way? I look at the papers and immediately think irreparable injury, and clear and convincing evidence. I try to do all of these kinds of mental gymnastics on these papers, and then apply logic, reason and experience.

But what I am asking when I do all this is who am I hurting when I do this? Is there some customer that expects to get these folders on Monday, and have I've screwed that up? You've really got to think very carefully about what the temporary relief is. Are there innocent parties that I may hurt here? And then like anyone else, it is Friday, you can't get a hold of anyone else. It looks strong enough. You sign the thing, hold your breath and try to get these people in on Monday. Now, what I might do is tell my law clerk to see if he can get this party on the phone. Tell them I've just signed a temporary restraining order, and make sure they have a copy of these papers. Tell them I'm hearing it in court Monday at 2:00 o'clock. So you don't have someone coming in and saying, well, they violated your TRO, and then hit them with contempt. So you have to use a lot of common sense so you make sure the people who you are restraining know they are being restrained and they can swing back as quickly as possible.

Preliminary Injunctions and Determining the Amount of the Bond

MR. ZAUDERER: I think Justices Stander and Makowski have had an interesting premonition. Adding to the hypothetical, as we get past the TRO stage, and there is a motion for preliminary injunction, of course noticed. Now Mr. Smith appears by an attorney and puts in an interesting set of papers. The papers say essentially three things: number one, I don't know anything about Brooklyn. Number two, I have left the employment. I have no employment contract. Had no employment contract. And number three, indeed I am doing business with customers who were formerly customers of the W.T. Smith Company, but I did not solicit them while I was there. I left, I knew these people, and it is a free country. It's America. They have a right to do business with me.

And by the way, the plaintiff says in her application that the identity of the customers are trade secrets. In fact, there are no trade secrets. The customers, that is, those in the wire and cable industry, are all listed in the yellow pages. Everybody knows who they are.

And of course, there's a reply affidavit put in by the plaintiff that says with regard to the trade secret issue, well, of course, customers are in the phone book, everybody knows that. That's not the trade secret. It is who is the purchasing agent? How much do they buy? When do they want these products delivered? You can't find this in a phone book. This is truly, truly a trade secret. Now, the court has these papers, moving papers, answering papers, reply affidavit.

How do you resolve this now and what do you do?

JUSTICE LOWE: The issue of trade secrets is one of the thorny facts that come before us. And oftentimes it comes down to how you characterize it, what is it that they are seeking to protect and/or characterize as that which is not in the public domain. I would look at what efforts the plaintiff company took to protect those issues or facts that they are now claiming are within the knowledge only of the plaintiff's company. I would look toward how those customers became his customers, how they gave up 20 years of service with the

plaintiff's company. I would look to see if he's got affidavits from those companies that "we were not solicited by him." My decision on the preliminary injunction would be affected by the responses to those inquiries.

MR. ZAUDERER: Well, let me follow up with you, Judge Lowe, if I may on that. You've got the papers before you, you've got the lawyers there, the plaintiff is saying we are bleeding. The defendant is saying, I'm going to be put out of my legitimate business if this is granted. How are you going to make your inquiry? Who are you going to inquire of? Would you hold a hearing? How would you resolve that issue?

JUSTICE LOWE: Well, the application for preliminary injunction is pursued by way of a hearing. I will take testimony and evidence on the issues in order to make a determination. I'm simply not going to make a ruling without it. I would have the questions indicated earlier answered by way of either testimony or submissions, and then, after balancing the equities, and evaluating the likelihood of success on the merits and the weighing of any irreparable harm, rule on the injunction.

JUSTICE EMERSON: I may do something a little bit differently, although ultimately, we will all be doing the same thing. If a hearing is required, we will all be conducting a hearing. But the fact pattern that you've described sounds like a perfect time to not only immediately get the attorneys in but also the parties themselves, because they are the people who are in the best position to know what their immediate concerns are, the types of arrangements that they can live with, the type of—for lack of a better way to describe it—business deal that they can exist under in the interim.

So while the law, of course, requires a formal hearing and may direct us in a particular result, there are a variety of different solutions that may allow us to preserve the status quo while we prepare ourselves to resolve the ultimate legal issue, if, in fact, we even need to do so. Because what sometimes happens, as you put the business solution in place, some of the more formal issues start to resolve themselves either in their entirety or sometimes to a point where you're looking at just a narrower issue or a far more manageable focus. So again, for me to have a conversation with just the attorneys, there are going to be a lot of facts that you're not going to have at your command. It is going to be your clients who are going to say okay, well, maybe we cull out customer X, deal with it separately. We can do a lockbox for this kind of revenue, so we know you don't have a credit issue or something. There are lots of different solutions that we could never order in a formal context.

JUSTICE MAKOWSKI: Picking up on that, what you'll try to do is sift through in your mind, can I do this thing on papers or not? Do I need to decide that this is a trade secret? What I try to do, and I think everybody that does a lot of this type of work tries to do, is get the lawyers in and say, can we do a stipulated order, can we figure something out here that will create equilibrium in this case, and then we'll move forward from there. I want to determine what this TRO will look like if it is going to stay in effect. You've lost these customers; they are gone, but how do I not hurt these customers? You really have to sit there and kind of parse it out as to what has happened, what damage has been done and what are you trying to prevent in the future. Sometimes it works and sometimes it doesn't. I did one recently from the bench at oral argument. And we sat down over two and a half hours in the conference room on a Friday, and we worked out a stipulated order. That's an ideal situation. At least you're trying to get the people talking to each other. Trying to get some insight as to what this case is really about, what's important to the parties. That allows a dialogue to be created. If you can't get it done, you can't get it done. But at least you've tried. If it is controverted, and you can't make these factual decisions, clear the calendar and call your witnesses. Let's get this thing started on Thursday.

JUSTICE BENZA: What about the bond?

MR. ZAUDERER: Contrary to federal practice, in which a bond is required at both the TRO and the preliminary injunction stage, a TRO bond is not required under state law. It may be imposed by the court on the TRO, but it is mandatory on the preliminary injunction. So practitioners ask, we have a case, in which the very underpinnings are sharply disputed on the preliminary injunction motion. The court has to act quickly and make a decision on what bond must be set. The situation is further complicated by the fact that if it is ultimately determined that the preliminary injunction should not have been issued, or to put it the other way, the party was not entitled to the relief, the damages are limited to the amount of the bond. So it is a very serious matter. Justice Benza, how do you determine the amount of the bond?

JUSTICE BENZA: Well, it's not easy, but you try and figure out what they are alleging as the damages and try to reach some scope in there, and post the bond at about that amount.

MR. ZAUDERER: Well, how do you figure what that amount is, and how do you figure the damages?

JUSTICE BENZA: I use that bond a lot to get to a stipulated order.

JUSTICE EMERSON: We just had to do one, and we did it on the submission of the parties. We were looking for information that would allow us to make an informed determination as to what amount made sense in terms of the cost, the effort involved, and a clear understanding on the ultimate relief being limited by the amount of the bond. The submissions I got were that the bond should be zero and the bond should be a hundred million.

MR. ZAUDERER: Now, do you split the difference?

JUSTICE BENZA: I'll give you an exact case. We had a psychiatric nurse working for a doctor, and all of the patients wanted to go to her for treatment. The doctor took on another nurse, there was a disagreement between the nurses and the first nurse left. When she left, all of the patients went with her.

The doctor brought on a TRO to stop her from taking the patients. With health care there are some specific problems about the right of a patient. But we managed to determine the number of patients that went to the new clinic. We allowed those patients to continue there, because after all, they have the right to do that. But I had the clinic keep a special record on the amount of money that was being generated as a result of those patients. I restrained any other patient from going to that other clinic unless they reached some sort of an agreement whereby the new clinic kept a record of those patients.

JUSTICE AUSTIN: Two things. First of all, the thing that I do with regard to undertakings is I ask the attorneys what they think the appropriate amount is and invariably one of the attorneys puts a number on it. I ask the defending attorney first how much should the bond be. There are cases where I think the bond should be next to nothing, and if the defending attorney says $50,000, I'll grant it.

The second thing is that these hearings are, in effect, going to deal with the same exact issues that you have at trial. What I will generally do is say to the attorneys, "Why are we going to do it twice?" I'll give you four weeks. Do your depositions. Each of you will have two depositions to take, and at the end of the four weeks, come in, you'll have your trial on the preliminary injunction and the merits of the case as well. That has been an accepted procedure. They'll do that, and normally by the third week the case is settled.

JUSTICE RUDOLPH: I recently inherited a case that was reversed on a preliminary injunction, and therefore, we had to try the issue on damages. In this particular case that I tried there were two defendants; one was a municipality, and the other was a vendor that the municipality had engaged to build a sports and tennis complex. They were prevented from going forward with the development of that project, and there were substantial damages for both the municipality and the vendor, which was demonstrated by the evidence which included the continuation of the project after the Appellate Division made its decision. As a point of interest, since it wasn't my case from the beginning, I searched the record after the case was concluded to find out what information was presented to the original court as far as the request for appropriate bonding. In this particular case, I couldn't find anything from the defendants on that issue.

But I would say, based on my experience in this particular case, if you were representing the defendant on the issue of a preliminary injunction, it is very important in protecting your clients that you ask the court for a bond that would reasonably protect your client's interest in the event the court should issue the injunction and then ultimately you would be successful on an appeal in turning that around. I think that that's a very important matter you may want to consider. I think that that ultimate concern outweighs the negative effect of discussing the bond with the court in the first instance.

AUDIENCE MEMBER: I have a question regarding the bond. The bond, it seems to me, is kind of a strange concept in a preliminary injunction. Because plaintiff is coming in and saying it is more likely than not that I'm going to win, and I'm getting irreparably harmed. So now I have to put up money to protect the defendant. The thing to keep in mind is the bond is a policy in a civil action. The plaintiff has to deposit money with the county treasurer's office, so if they are not rich, they lose.

JUSTICE AUSTIN: Well, first of all, with regard to bonds, finding a bonding company truly is a problem. Generally, what I'll do is let the attorneys create a joint interest-bearing escrow account. And yes, the merits do come into play in terms of determining what the bond should be. However, if the judge does not grant a bond on granting a preliminary injunction, that is per se reversible. You must grant a bond. So we have to consider it. If I think the movant has an absolute slam dunk, there's no way the defendant is ultimately going to show that the injunction was improvidently granted. Then I will set a very low bond. I'll set $500, $1,000, nothing much more. However, where there is a real question and the movant has persuaded me that there should be the injunction, but one never knows in the course of litigation, then the bond will be higher.

First question is: Is there a right to the preliminary injunction? I'll only address the bond as the secondary

issue if I've determined that the answer to the first question is yes. And they are two very separate issues and analyzed from two very separate perspectives.

JUSTICE MAKOWSKI: I wouldn't want the tail to wag the dog on that, Judge. You can come in and say well, I'll put the half a million dollars bond down, and it gives you this comfort, but you might lose sight of what's the real question here. Should I be granting the injunction? While it might be a nice advocacy tool, I think it is a two-prong analysis.

Electronic Discovery

MR. ZAUDERER: Going back to the W.T. Smith case, we are past the preliminary injunction phase, and of course the plaintiff has submitted their document requests to the defendant. One of the things that's been asked for are any communications, including e-mails between Mr. Smith and the various customers that are at issuance. Documents are produced. There are e-mails, and all the e-mails and communications with the customers post-date the time when he has quit the company, and they are all very, very recent. And the plaintiff looking at this developing evidence and speaking to some customers is sure that there must be e-mails that predate, but they haven't been produced. And plaintiff raises this with the defendant, and defendant says look, we have been able to give you everything we have been able to punch out of the computer. The plaintiff says that's not sufficient. I don't know what you've deleted. The plaintiff comes in to you, Justice Emerson, and says look, based on the evidence here we would like to bring in a forensic group to take a photograph of the hard drive, and we want to look at the hard drive of Mr. Smith's computer from his house where we think this business was going on.

JUSTICE EMERSON: We are following on an earlier conversation of several weeks ago, counsel. The answer is it depends. We are going to go through the appropriate discussion of the balancing of the various elements that have been identified in the relevant task. We are going to figure out what it is you need, why you need it, what the cost is. To analyze the burden, as was just described, in a recent decision by, I guess it was, Judge Schendlin. So the answer is, it is very fact-specific, but we will treat it as a serious request and attempt to come up with an appropriate response. But without more of the facts to make that determination, I think that's as far as we can go.

MR. ZAUDERER: Has anybody come closer to making up their mind here?

JUSTICE WARSHAWSKY: Based upon the original facts that you've set forth, he's going to produce that hard drive. It is going to get cloned, going to cost from $3,000 to $5,000 to clone a hard drive. I'll use an independent forensic examiner, and that examiner will be given specific guidelines on what he is to pull out of that machine. Because, of course, we want to protect Mr. Michael Smith's confidential client list, but any e-mails that predate the date that he left that company, that exist on his hard drive will be produced.

MR. ZAUDERER: Anybody have a problem with that?

JUSTICE AUSTIN: No, I will include with that order a TRO that Mr. Smith would keep his computer intact.

JUSTICE WARSHAWSKY: And what if he says my computer had a fire? The batteries on my laptop caught fire and burned up my hard drive three days after I left the company.

JUSTICE BENZA: Well, take a look at your backup material.

JUSTICE GAMMERMAN: I've had that case. Not a fire, but one in which the expert went to the computer and not only examined the hard drive but determined that the defendant had deleted material that should not have been deleted. And a motion was made based on that activity for an interim judgment, and I struck the answer and entered a judgment against the defendant. So it seems to me that's an appropriate area of discovery, what is on the computer and what was eliminated.

JUSTICE WARSHAWSKY: Normally deletion doesn't work, so a true forensic examiner is going to find deleted, so to speak, material the way we delete material. But they can actually go in and use another program they load into the computer to really delete material from anyone's site. And that will leave traces. So you will at least be able to find that they used a program to absolutely delete and cleanse that computer.

MR. ZAUDERER: So Judge Warshawsky, may we assume, based on what we have just heard, that in commercial litigation, if we make a document request, and let us assume nothing is wrong with the request and it is relevant to the issues in the litigation, then, as a matter of course, the requesting party may ask the responding party to produce the hard drive, perhaps at its own cost; is that correct?

JUSTICE WARSHAWSKY: Yes.

MR. ZAUDERER: Anybody have a problem with that? We can all do this now in litigation, ask for the hard drive?

JUSTICE BENZA: I don't know about the cost. I don't know who is going to pay the cost.

MR. ZAUDERER: Well, who is going to pay the cost, Justice Benza?

JUSTICE BENZA: I would think maybe the plaintiff would pay for the cost because they are the one asking for reproduction of the materials not created in the ordinary course of business.

JUSTICE WARSHAWSKY: This is the ordinary course now. This has become the ordinary course of business. This is the way business is run as far as I'm concerned. I may apply or direct the plaintiffs to bear the initial cost, and if I then determine, during the course of trial, that the defendants have proceeded in their own fashion to obstruct discovery by failing to turn over what they should have turned over through normal paper requests or interrogatories or "please give me the e-mail," whatever that was, then I can switch the burden or split the burden of the costs.

JUSTICE BENZA: Well, then you give a judgment to the other side, like Judge Gammerman did?

JUSTICE WARSHAWSKY: Well, that's when we can't get it at all.

MR. ZAUDERER: Judge Benza, should Mrs. Baker, who is struggling to keep this company from sinking and barely was able to get a lawyer who would take this case on a partial contingency, have to fork up $5,000 to hire somebody to get these e-mails from Mr. Smith's hard drive?

JUSTICE BENZA: Well, yeah, if there's no extrinsic proof that shows he was hiding something, and it's only because she suspects that because of her conversations with the employees, I think she would have to pay for it. You know, that's one of the problems in this electronic discovery age. We are not talking about $500 or $1,000; we are talking about $200,000 or $300,000 or maybe a half a million dollars. And somebody is going to have to pay for it.

JUSTICE LOWE: Understand something, the original question was whether or not the plaintiff is entitled to this type of discovery. It seems to me once you make a determination that it's relevant or that there's a basis for ruling in favor of that request, then I think that the solution with regard to the cost is not very difficult.

I think it is a very reasonable approach to have the initial cost be borne by the requesting party. Then depending on the results of that, the production of that, if indeed, it does appear that there has been an intentional attempt at not providing discoverable material, then you can switch the cost, or factor that into the damages.

JUSTICE MAKOWSKI: You've got to think about the way these cases have come in and what's been requested. If you've requested all e-mails which predate termination or resignation, if you make the right request, and it is not produced and you say: we think it is there, give us an expert, we want to do a forensic test, we will sign a confidentiality agreement, we'll do all the right stuff, and then the materials *are* there, then I think you're in a different ball game. Then I think you are in a cost reversal situation, because we asked you to turn the stuff over and you didn't.

JUSTICE EMERSON: I was just going to say that's why the original answer is, it depends. You have a lot of predicate questions that need to be answered in order to get the result that was indicated.

JUSTICE BENZA: It's called equity.

JUSTICE AUSTIN: The whole question of cost is really a red herring in my opinion. There's no difference between the cost of having a forensic expert delving into a computer hard drive and having 20 associates going through a warehouse to find 300,000 documents. It is the same thing. And in fact, I dare say it is cheaper to do it with a computer than otherwise. But that's the cost of discovery; you're trying to find it. As long as it is made available and accessible, then the party that wants it, at least at first blush, pays. And then you deal with it as the matter unfolds.

JUSTICE MAKOWSKI: What if it is a mainframe? What if its got 20 million pieces of information in it? What if you've got to tie up 18 to 20 IT staff members looking for this stuff? I mean, you know, it depends—it depends how big the case is. And how big is this defendant? And are you in effect going to paralyze the ability of this defendant to do business? Are you going to tie up their IT department for four weeks, six weeks, a month? These are very real questions when you get into big electronic E-discovery cases. The judge has to be on top of his or her game.

MR. ZAUDERER: I can't resist. Judge Demarest, let's say Mr. Smith has not simply been working out of his home, but has gone to the IBM Corporation—just to pick a name. Now we know that he's been sending e-mails, has his business on the side. The plaintiff says we want all of IBM's mainframe server searched for any e-mails that were sent. Doesn't that sound like a reasonable request?

JUSTICE DEMAREST: No. Doesn't IBM have anything to say about this? You're saying they are willing to disclose everything in their existence? As I just said to Justice Emerson, the answer is settle. The point is, you've already far exceeded the value of this lawsuit by the cost of litigation. And any responsible jurist would say hey, come on, this is ridiculous because you're playing it out for an emotional value and not any real damage return here at all. So yes, that's a glib answer, but really it is true.

JUSTICE WARSHAWSKY: I don't work with mom-and-pop corporations, but when you have AT&T on one side, Sundance on another side, and a third corporation who is, let us say, the one who has to produce the material, the discovery issue comes in on a third-party motion and the third party says, wait a minute, we can produce, to you, our experts who will tell you that in order for us to do the search that you want us to do, Judge, it is going to cost us somewhere in the vicinity of $25,000 per day for approximately three months. That's when you turn to the plaintiff and say all right, counsel, now how relevant is all of this?

JUSTICE MAKOWSKI: How bad do you want this stuff?

JUSTICE BENZA: Should the fact that a party purposely makes it very difficult to retrieve information be taken into consideration when we determine who should pay?

JUSTICE GAMMERMAN: Oh, absolutely.

JUSTICE WARSHAWSKY: Certainly.

Oral Arguments

MR. ZAUDERER: On that note, let me go to my final point . . . Oral argument on motions. I think we can all agree as a matter of principle, and as advocates, we certainly feel that oral argument helps to sharpen the issues. But some practitioners have raised the concern that an enormous amount of preparation goes into the amount of oral argument, we don't know what the judge will be interested in and it is our job to be prepared. It could be days spent on oral argument. If we are fortunate, we have caught the attention of a judge on a particular issue, but we know that in many cases, given the way the court must work, the decision is written by the very, very fine law secretaries that the court is privileged to have. However, the law secretaries are not present at the oral argument, may not have heard the argument, will not have heard the argument, cannot have heard the argument. And there is a concern that perhaps whatever impression the judge had or view the judge has may not be fully communicated in the research and writing of that decision. And by the time the decision comes back to the judge for review, some of the finer and interesting points of that oral argument may have been forgotten, given the press of business. Is that a legitimate concern, Judge Lowe?

JUSTICE LOWE: I have oral argument on all of my motions, and at the end of the motions, I require the minutes to be ordered. And they are attached to the file. So that if I do it, I review the papers and I review the oral argument to find out the points that the attorneys feel are significant for me to concentrate on. If it is a case that goes to the Law Department, I attach those minutes before the case goes to the Law Department for the same reason. So oral argument is significant to me.

JUSTICE DEMAREST: The only thing I can say is whether you make your own notes, or you have a conversation with your law clerk, or you do what Judge Lowe just described, the bottom line is that the judge has to sign the ultimate decision, and in some fashion you've preserved what you found to be relevant in that oral argument. And I think you have to trust, as you do in the entire context of the judicial system, the integrity of the system and that the judge is going to be aware of the concerns and has made a decision about it.

JUSTICE MAKOWSKI: When I first became a judge in 1999 and really up through the end of last year, I thought oral argument was terrific. And then I thought it was taking too long, so I set time limits. I figured that if you go to the United States Supreme Court, they give you 30 minutes. I mean, what's the deal? And a lot of times you are developing the facts as you go along. So this year, I said no oral argument unless you ask, and here are the timelines. If I'm going to do oral argument, I have my law secretary in the courtroom for that argument. If she's not available, then I sit down, and I do a core dump with her at the end of the session, so we go through all the salient points.

At least in the Commercial Division, I really try to triage the motion. Is this one where I really need oral argument or not? Because this stuff takes forever, and you can be out there for four or five hours. And then it all kind of blends together, and you're looking at your notes. And then I'm worried about what I'm doing at 2:00 o'clock. If there is going to be oral argument, crispness is the order of the day. It really is.

JUSTICE AUSTIN: Generally, when a motion comes in, all of our motions are submitted. If we want oral argument, we'll advise counsel. And in that case, my law secretary will prepare a bench memo for me along the lines of how I think the motion should go from the papers that are submitted. If it does go that way, I'll use the bench memo as my template, and I'll decide the motion from the bench, basically dictating and adding in as is appropriate from oral argument. However, if oral argument moves me in a different way, then I'll reserve decision, get the minutes and make the decision based on that.

JUSTICE EMERSON: We don't do oral argument on our motions. Only if you really want it. But I will conference the motion, which means I've read the papers, and we have either reached the conclusion and basically are drafting it out and want to explore the conclusion before we commit it to a final order or we have some questions. If you need to make a record, i.e., conduct a formal argument on the record, we will

always afford you that opportunity. But ours is a submit calendar only.

JUSTICE GAMMERMAN: I agree. Based on the oral argument I generally know whether I'm going to decide the motion. And I decide it right then and there and dictate a decision. So there's no intermediate step between the decision and the argument. Occasionally, if there is an argument, and I haven't decided it and someone else is going to draft an opinion, that's something that is discussed before any work is done on the case.

JUSTICE STANDER: First of all, I have oral argument. But I thought the question you were going to ask was: "We put all that time into organizing our argument, then you issue your decision from the bench obviously from some prepared notes; why do I bother to come over and give oral argument?"

MR. ZAUDERER: Let me ask that question.

JUSTICE STANDER: Well, I don't know. First of all, I don't know how the other judges do it on submission only. That means you have to write on every motion. I could never get through my calendar if I had to write on every single motion. So dictating from the bench, you get the basic point, you do the order, and it is done. What I think it does is it gives you a second bite at the apple, and it gives you a chance to see if I'm on the same page as you. And I can tell you that invariably, not every term, but, at least once a month, I'll take a prepared order and slip it back in the pile, and say I'm going to write on this because I'm not real sure that I understand this issue. And I'm going to go back with my law clerk, who is sitting in the courtroom with me, and we are going to hash this out again. It gives us a second bite. It is to your advantage.

AUDIENCE MEMBER: In reviewing motion papers and having oral argument, have you ever considered writing to the litigants and saying look, I've reviewed your papers, and here is the question or here is the issue that I believe is most important? Because I know I've argued a number of cases where the very last question from the judge was a fact issue that wasn't understood or there was an issue that I had missed that the judge was interested in. Wouldn't oral argument be more meaningful if after reviewing the papers—and I know it is a burden but if you did want to have oral argument—wouldn't that be a more meaningful way for the litigants to approach oral argument?

JUSTICE WARSHAWSKY: Look, the answer is yes and yes. I have a submit calendar, unless oral argument is requested. And I don't always grant it, but when I do grant it, I've got everything in front of me. And I have frequently had my law secretary convey to the parties that the judge wants you to address the following.

A Discovery Road Map for Complex Financial Services Litigation

By Joel Finard

The successful conduct of discovery in complex financial services litigation requires the incorporation of a sophisticated understanding of the people, process, and technology employed within the industry.

The growing size, complexity and geographic span of global financial institutions has introduced into financial services litigation an unprecedented set of challenges that defy traditional litigation practices and require the development of new approaches and tools. Discovery, in particular, is complicated by the difficulty of locating and identifying the people, processes and technology within the institution that are relevant to the litigation. Furthermore, drafting requests has become an increasingly perilous exercise: financial institutions are "document factories" and have the potential to respond to over-broad requests with a document avalanche, defeating a plaintiff's efforts to find the relevant evidence and destroying the economics of litigation. Avoiding these pitfalls requires the development and integration of a discovery plan based upon a sophisticated understanding of the people, process, and technology employed within the industry.

This article outlines a Discovery Road Map (DRM), a tool facilitating the development of a discovery plan and conducting a highly focused and efficient discovery within a financial institution. Part I provides necessary background information on financial services, industry litigation and financial institutions. Part II presents a DRM for conducting discovery of a financial institution. Part III discusses the highly targeted discovery function within the DRM. Finally, Part IV offers a summary and conclusion.

Part I—Introduction

The size and complexity of financial service industry[1] litigation has grown in proportion to the number of institutions themselves. The number of cases filed and the dollar value of claims in financial services industry litigation are unprecedented. Federal securities class action litigation suits increased by 31% between 2001 and 2002, rising from 171 to 224 filings.[2] The companies sued in 2002 also lost more than $1.9 trillion in marked capitalization during the class periods, a 24% increase over the comparable figure for companies sued in 2001.[3] The previous numbers do not include the "IPO Allocation" securities class action filings.[4] In 2001, 312 cases were filed naming securities analysts and investment banks as defendants.[5] Among the largest and most complex claims facing the industry are those arising from what is now commonly referred to as "the Enron debacle"[6] and "the IPO securities litigation."[7] These cases represent claims in the billions of dollars and include as parties a virtual "Who's Who" of the largest and most complex commercial and investment banks.[8]

For anyone not an industry insider, identifying the actors and understanding the events that take place inside the banks is a formidable task. Moreover, the millions of "documents"[9] and "communications"[10] created and maintained by banks provide ample opportunity to exhaust the resources of a plaintiff unwary enough to deliver broad, "shotgun" document requests. The Discovery Road Map outlined in this article is designed to assist plaintiff attorneys in identifying and targeting the relevant actions and actors and in conducting highly focused discovery.

Financial Institutions Are "Paper Factories"

The global deregulation of financial institutions[11] has resulted in an industry dominated by large and complex entities, providing a dizzying array of financial products and services.[12] Their primary role has evolved from intermediating between lenders and borrowers to the origination, distribution and participation in both the traditional and sophisticated capital markets products and service areas.[13] The volume and complexity of transactions processed by these institutions is truly remarkable, requiring the development of highly complex and interrelated processes and procedures.[14] In addition, the oversight of such significant volume demands a sophisticated monitoring and control infrastructure. Laid over this institutional control infrastructure is a patchwork of global, national, state and other regulatory requirements designed to ensure the safety and integrity of the overall financial system.[15] Together these management and control systems generate millions and millions of electronic and paper documents and records.

The quantity of transactional volume managed by global financial institutions is extraordinary. A picture of just how large this volume is can be gleaned by examining the transactions flows of just a few key mar-

kets depicted below in Chart 1: the foreign exchange, derivatives, and U.S. public and private debt markets.

Chart 1

Foreign Exchange Volume

"On average, the equivalent of about $1.2 trillion in different currencies is traded daily in the FX market around the world."[16]

Derivatives Volume

"[In 2001], the notional amount of derivatives outstanding measured some $100 trillion—a 38% increase over the past three years. Even more remarkable than the speed of the market's growth is the change in the composition of derivatives activity, as newer products become more widely used."[17]

U.S. Public and Private Debt Outstanding

In 2001, the total amount of public and private debt in the United States, of which the financial institutions are the main underwriters as well as the primary and secondary market makers, stood at over $18.5 trillion.[18]

The figures in Chart 1 help to paint a picture of the transactional volume flowing through the industry as a whole. As would be expected, the larger institutions manage the lion's share of market volume.[19] An examination of the balance sheets of some of the largest institutions demonstrates this point.[20] In 2001, for example, the notional principal of derivatives[21] and foreign exchange outstanding at those institutions was:

JPMorgan Chase	$24 Trillion
Bank of America	$9 Trillion
Lehman Brothers	$5.4 Trillion
Merrill Lynch	$5 Trillion[22]

Financial institutions and their regulators have imposed a disciplined control infrastructure in order to manage the large volume of transactions. This is important to a litigator because each business line and each transaction has a discoverable paper trail of White Papers, New Product Approvals, Risk Reports, Operational Policy and Procedures Manuals, Status Reports, Audit Reports, Regulatory Examination Reports, Credit Reports, Customer Reports, etc. Financial institutions are indeed "Documentation Factories." This reality carries both significant positive and negative implications for the plaintiff attorney. On the positive side, it is almost certain that the institution possesses the documents needed to prove a well-founded allegation. However, the negative side is that discovering these documents can be like looking for "a needle in a haystack." Even more significant, during discovery, the defense attorney may attempt to bury the plaintiff attorney in the heaps of paper.

The successful plaintiff attorney will keep discovery highly focused and, whenever possible, will identify and request the exact documents desired.[23] This result can be achieved by using the financial institution DRM outlined in this article.

Part II—"Discovery Road Map" for Financial Institutions

Introduction

The use of the Discovery Road Map (DRM) can assist the plaintiff's attorney to identify and locate the desired documents and communication. Conceptually, the tool can be used like MapQuest, which guides the traveler to a specific level of detail.[24] The MapQuest "zoom" function allows the traveler to view the desired location from multiple levels—zooming out to see the state of the location, zooming in to identify the adjacent streets.[25]

The Discovery Road Map identifies three features of the financial institution's "landscape" to guide the litigator's discovery:

(1) People—Who were the people (department, function, title, name) involved in the actions at issue?

(2) Process—What did they do? What were their roles?

(3) Technology—Where is the information stored? In what format?

Financial institutions structure and organize themselves according to their products and services, each of which has, at its core, a transaction with a "life cycle"[26] having three phases: (1) Pre-Deal; (2) Deal; and (3) Post-Deal.[27] Each of the three transaction phases in the product life cycle will have distinct and operational characteristics: People, Processes, and Technology. Therefore, in creating a high-level DRM, the first step will be to create a matrix with the transaction life cycle on one axis and the operational characteristics (people, process, and technology) on the other axis. The matrix framework can be seen in Exhibit 1 below:

Exhibit 1

	Pre-Deal	Deal	Post Deal
People			
Process			
Technology			

The Discovery Road Map matrix shown above will need to be created for each specific product line and/or business line. It can be used at a high level in directing discovery. For example, the DRM can be used to assist the plaintiff's attorney to understand the details of a product throughout its life cycle, articulating the roles

of the people, processes and technology in supporting the specific product line. The DRM can also be used to progressively narrow down the focus of discovery through a single field in the matrix, such as the technology used to develop and present a product in the "Pre-Deal" phase. The Discovery Road Map functions both as an exhaustive checklist of all available discovery options and as a tool to support discovery focused on the particular elements of an attorney's interest.

For illustrative purposes, we will present an example of a litigation team's use of the Discovery Road Map to direct a focused discovery related to derivative transactions at a bank. This is shown in Exhibit #2 on page 39. As presented, the initial, high-level DRM presents a detailed, yet somewhat basic, understanding of derivatives transactions.[28] The next level of "magnification" will examine a specific financial institution, and will lead to an increasingly detailed and specific identification of details, down to the level required to discover the evidence necessary to build the case. While the overall structure of the DRM will remain the same, each type of transaction will require a unique DRM. An examination of equity underwriting, fixed income transactions, or syndications would each require a uniquely designed DRM to facilitate discovery. Moreover, a more detailed DRM can produce a more focused request. Some examples of this progressive movement, from the general to the specific, follow.[29]

Pre-Deal

Process

The pre-deal process includes the development of a new product or the mutation of an existing product. Included in this phase is the generation of the idea, and the shaping of it into a marketable product. This involves working with bank clients to determine their product needs and the features or constraints necessary to make a product viable.

While the creation of a new financial product goes through a series of developmental stages, all must go through a new product approval process. This is a highly structured and documented review, which includes a wide range of functions in the financial institution. The new deal process can be extremely valuable in demonstrating what an individual and, by extension, the financial institution "knew or should have known," and documenting pre-existing knowledge of a transaction.

Once a product has made it through the new product approval cycle, it must gain "Transaction Authority." Transaction Authority creates and delegates authority to execute these new deals, including any constraints such as transaction size or the type of institutions with which to trade. It is not, however, the authority to execute a specific deal.

People

There are numerous people involved in the Pre-Deal process located throughout the organization. Once an opportunity is spotted and nurtured by line management, it moves through the New Product Committee. The membership of this committee is typically comprised of senior executives from several departments (each of which can be the subject of a detailed DRM), including operations, product control, risk management, legal, compliance, audit, credit, and financial control. After submission, the proposal is reviewed and the committee members make recommendations for any modifications necessary before they grant their approval. Final approval of the product often requires review and signature by senior management.

Once approved as a new product, authority for a specific transaction is typically controlled by senior management. For example, the head of trading for the relevant trading desk will either approve or reject a new trading product such as a new Derivative, Foreign Exchange or other trading product. In addition, global risk management and compliance will typically be required to give their approval to execute a transaction of a certain size or duration (maturity), or for a given type of customer. Discovery in the Pre-Deal process establishes that certain types of deals were widely reviewed and approved, and individual transactions were authorized by department or trading desk heads.

Technology

Technology used in the Pre-deal process tends to be very flexible and includes spreadsheets or other front office[30]-designed analytics that facilitate product customization. This type of technology allows for numerous (discoverable) product iterations to meet the customer's needs. Once approved by the New Product Approval Committee, often one-off, customized technology is created to structure and price the transactions. The institution will likely wait to determine the success of product before it invests heavily in technology to make routine pricing and booking. Documentation of the New Product Approval Committee and the Transaction Authority will be available in standard databases such as e-mail and in customer information systems such as C.R.M. systems (Customer Relationship Management). These approval processes will also have digital and paper trails in the risk management system, as well as standard document repositories.

Deal

Process

The Deal process covers three important areas: (1) client management; (2) deal approval and execution; and (3) trade processing. Client management is a critical

step in the life cycle[31] of the deal. As part of client management the transaction is described, presented and ultimately sold to the client. Depending upon the size and structure of the product, this will involve a series of meetings with the client and follow-up discussions before the client is ready to execute a transaction. Next is the execution of the trade. At the point of trade execution, the client relationship manager is required to obtain authorization of the specific transaction. Transaction approval may require sign-off by senior management or may simply require the examination of credit exposure using a database to determine if an appropriate credit line exists.

Once approval is gained, the front office will execute the trade. The process of trade execution varies substantially and depends upon the type of transaction. For example, execution is simple for the purchase of currency (Foreign Exchange or FX), which is conducted over a telephone, or it can be a complicated execution involving a web of highly structured transactions. Upon execution, the trade will then be processed in the internal systems that are used to track all aspects of the deal.

People

The "Deal" stage, like the Pre-Deal stage, involves a wide variety of people from various groups within the financial institution. Client Management represents the front line, or sales, of the institution. Each product area will have a group of people who are focused on client management. The larger institutional relationships have both a sales person for each product area and a senior Relationship Manager (RM).[32] The RM is charged with understanding and managing the client's relationship throughout the institution. She maintains contact with the senior management of the customer and also facilitates transactions between the client and the institution. The RM for a given client can be an important target for discovery. She is not only a central warehouse of the institutional information, but is also likely to have attended all important internal and external client meetings, and therefore, is a valuable source of discoverable information.

Both deal approval and execution involve the participation of a broad range of individuals at the institution. When a trade is to be executed, depending upon the size and complexity of the trade, bankers from trading, credit, and risk management are involved. The trader, who plays a different role from that of the salesperson, is responsible for pricing, execution, warehousing and hedging the deal. Risk management, including the market risk and credit risk areas, as well as product control, will oversee trade execution and the management of the resulting risk from any trade.

Once the execution is complete, middle office and operations personnel will take over to process the trade. These individuals will make sure the trade is confirmed and that it is documented in the appropriate systems.

Technology

The three sub-stages in the deal process (pre-deal, deal and post-deal) require different types of technology. The systems used in the deal stage are likely to be robust and sophisticated. At this stage industrial-strength tools are required to manage the enormous volume and complexity of trades handled by the organization. In addition to the standard e-mail and recorded phone lines, which are found throughout the entire Discovery Road Map, client management will draw heavily on a Customer Relationship Management (CRM) system/database. The CRM system/database warehouses and catalogs institutional information about the customer. Depending upon the system, it will contain call reports, credit reports, and documentation of who visited the customer and when the visit occurred. This is likely to be a very important database in the discovery process. System type and functionality will vary greatly among institutions because of the high cost of integrated, institution-wide CRM systems.

As the transaction moves to the execution phase, a wide variety of systems will be used. Depending upon the product, any of several front-office trading modules may be used. In addition, several different risk systems will be used, including a credit system to make sure that the transaction is within credit limits and a risk measurement system to measure the outstanding market exposure. At the point of trade processing, the new transaction will be placed into a system that is specific to each type of transaction. In addition, other systems likely to be used include Collateral Management systems and Confirm Management systems.

Post-Deal

Process

Two areas of the Post-Deal process are potentially rich targets of discovery: risk reporting[33] and books-and-records systems.[34] Risk reporting includes the active measurement and analysis of the executed transactions. During this time the trades will be reviewed to make sure they fall into the required limits and that appropriate procedures have been followed. The last stage of the Post-Deal Process is when the transaction is entered into the books-and-records systems of the institution.

People

The Post-Deal process involves a more limited set of people than the previous two stages. In the Risk Reporting stage, Global Risk Management, Credit Risk and Product Control are involved in analyzing the risk of the transaction. In the final stage the back office and

accounting areas deal with each transaction to ensure correct processing.

Technology

Several different risk systems may be used at the Post-Deal stage, and in addition, a books-and-records system may be utilized. These systems may draw upon a centralized database for the information requirements, or the information may have to be manually reprocessed into the final set of systems. Often these systems are used for aggregation purposes and cannot handle the peculiarities of complicated transactions. Therefore, for non-traditional assets, books-and-records systems are not likely to be a valuable source for Discovery.

Part III—The Discovery Road Map "Zoom" Function—Highly Focused Discovery

While the DRM can guide the plaintiff attorney to the correct area, it is a gateway, rather than an end, for highly targeted discovery. In order to further focus discovery, the "zoom" function of the DRM, like the MapQuest zoom function, must be used. At any point along the "deal process," a substantial drill-down can and should be used to pinpoint the discovery requests.

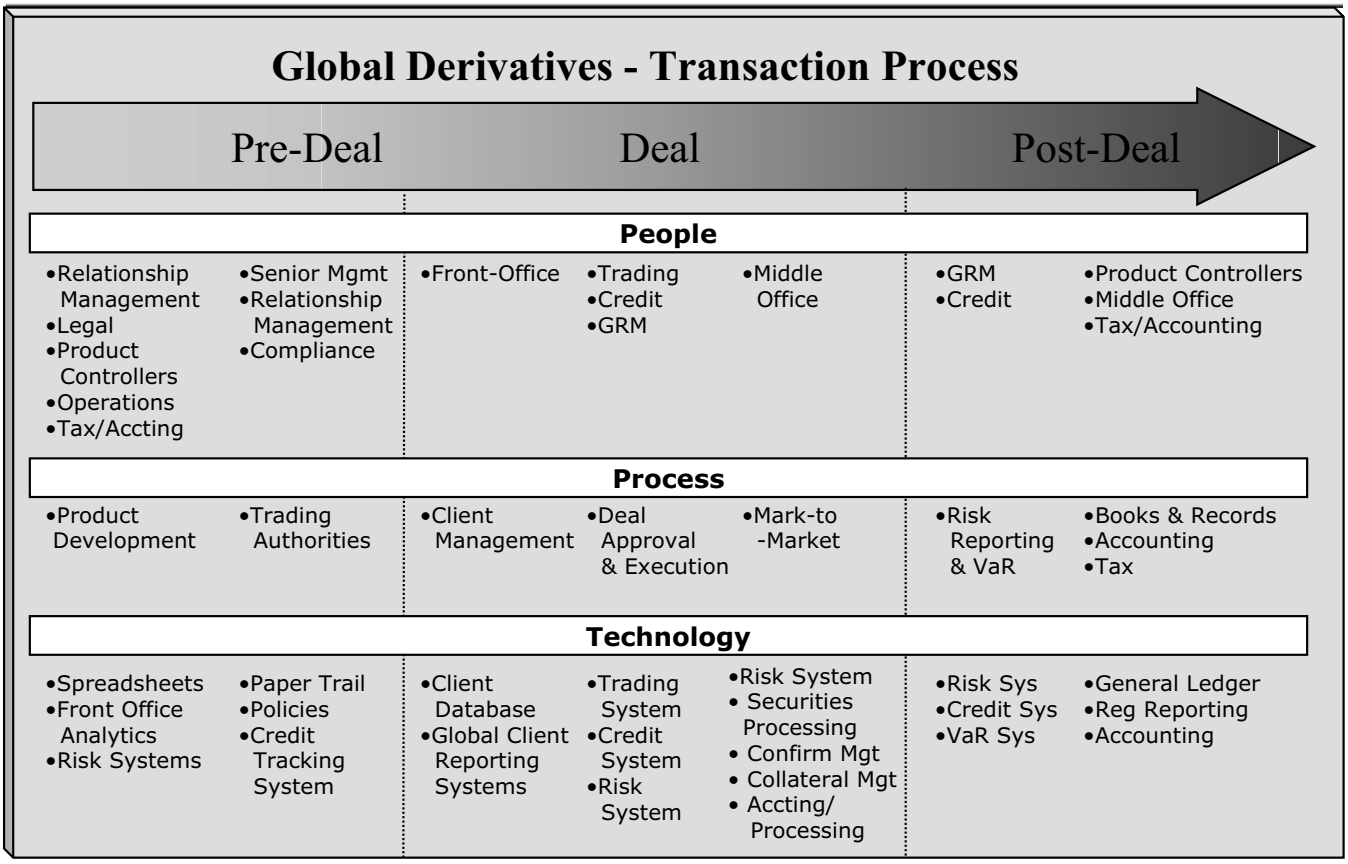
An example will help to illustrate this point. Assume the plaintiff attorney is attempting to gather evidence about highly structured derivative transactions sold by a financial institution that contributed to its client's demise. The plaintiff attorney must first understand the deal phases (pre-deal, deal, and post-deal) and the people, processes and technology that were used in these transactions for drafting Requests for Production (RFP). The attorney concludes that a key piece of evidence is necessary to demonstrate that the institution, at its most senior levels, not only understood the details of the derivative product, but also understood the implications of the derivative transaction. We apply this as an example to a hypothetical New Product Approval Process.

Example—New Product Approval Process

At this point, the attorney concludes that a drill-down of the New Product Approval Process would demonstrate knowledge of these derivative transactions and of their implications. The attorney then requests a "zoom" of the New Product Approval Process (NPAP), an example of which is shown in Exhibit #2. The zoom of the NPAP demonstrates both the people and the processes associated with creating these transactions, as

Exhibit 2

Discovery Methodology: People, Process and Technology



well as the approvals necessary to allow these types of transactions to be executed by the given institution.

The flow chart shows a typical NPAP. The idea for a new product typically starts in the front office. The next step is to draft a written description of the product/new business. This written proposal is then taken to the New Product Approval Committee. If it is determined that the idea has merit and should be taken to the formal committee, the written proposal is distributed to all its members. The Committee has a broad functional representation as shown in Exhibit #2. They then meet to discuss the proposal. During that meeting the product is reviewed and may be altered. The entire Committee, or one of its subgroups, may be required to meet again in order to address concerns which may have arisen subsequent to the aforementioned meetings. The written proposal of the product then moves into the approval stage in which all functional areas of the group will sign off on the product. Although Exhibit #2 shows a typical New Product Approval Process, each institution is likely to have specific requirements that are unique to their institution. The details of these unique requirements, as well as the names of the specific reports, should be contained in the New Product Approval Policy Manual.

Understanding the details of the NPAP would allow the plaintiff attorney to conclusively demonstrate that senior management clearly understood the implications of the derivative transaction in question. Furthermore, in the minutes and documentation of the NPAP, there will probably be detailed explanations of the product's uses and of its potential risks. The plaintiff attorney may effectively use this information to help prove the case.

Part IV—Summary and Conclusion

Modern global financial institutions have obtained a size and complexity that render traditional discovery methodologies obsolete. A litigation team can easily become lost in a wilderness of complex technologies, financial products, and business processes. The economic benefits of representing a client in a financial services litigation are easily destroyed by the costs incurred in managing the flood of documents and with identifying and organizing their relevant content. This article presents examples of how the Discovery Road Map can provide a scalable framework and a disciplined approach to the conception, formulation and conduct of discovery—from framing document requests through organizing and coding documents for proof at trial. Beginning at the highest level of organization through a "nine-box" matrix of the people, processes and technology employed at each of the three characteristic phases in the "life cycle" of each transaction, the DRM methodology facilitates a progressively deeper focus that allows the litigation team to obtain, identify and link documents to each element of each cause of action for each defendant. The resulting organization of documents can then be employed to support the proof at trial. The Discovery Road Map reduces waste by allowing discovery to be surgical in its focus, linked to specific elements of the cause of action and then coded and organized to ensure completeness and efficient presentation at trial.

Endnotes

1. "Financial service industry" in this article refers to investment banks, specifically those institutions that facilitate the transferring of funds from the ultimate lenders to the ultimate borrowers. In addition, the term includes the capital markets functions that are maintained in both large banks and investment banks such as: underwriting of bonds and securities; derivative transactions; commodity transactions (i.e., FX, oil, gas, gold, etc.), and primary and secondary market-making of the activities.
2. Cornerstone Research, 2002: A Year In Review (2003), at 4, *at* http://securities.cornerstone.com/pdfs/2002_yir.pdf.
3. *Id.* at 6.
4. *Id.* at 3, 6. "IPO Allocation" filings are lawsuits filed that relate to the number of shares in the initial public offering. In 2001 and 2002, atypical filings occurred due to the large number of investment banks and individual analysts who were named as defendants because they issued research reports and ratings that were neither objective nor accurate. Therefore, non-IPO/non-Analyst litigation is more likely an accurate measure of ongoing activity.
5. *Id.* at 3.
6. *See* Jonathan R. Macey, *Efficient Capital Markets, Corporate Disclosure, and Enron,* 89 Cornell L. Rev. 394 (2004).
7. *See In re Initial Public Offering (IPO) Securities Litigation*, 277 F. Supp. 2d 1375 (2003) (consolidation of more than 1,100 actions pending in two districts, alleging that underwriters and IPO issuers were responsible for misrepresentations in prospectuses and/or underwriter research analyst reports).
8. *Id*.
9. "Document" has a broad meaning, including items, whether in paper, database, electronic or other format(s), such as: analyses, appointment books, audit and scope plans, audit work papers, books, books of account, account statements, cables, calendars, charts, contracts, financial statements, forms, invoices, journals, ledgers, letters, lists, memoranda, minutes, notations, notes, opinions, orders, pamphlets, papers, partners', members' and employees' personnel files, partners', members' and employees' review check lists, permanent files, pictures, press releases, projections, prospectuses, publications, receipts, recordings of conferences, conversations or meetings, reports, statements, statistical records, studies, telegrams, telephone records, telex messages, transcripts, understandings, videotapes, vouchers or work papers.
10. "Communication" has a broad meaning, including any exchange of information, words, studies, or graphs by any means of transmission, sending or receipt of information of any kind by or through any means, including personal delivery, speech, writings, documents, computer electronics or electronic data, sound, radio or video signals, telecommunication, telephone, teletype, facsimile, mail, telegram, microfilm, microfiche or other media of any kind. The term "communication" also includes, without limitation, all inquiries, discussions, conversa-

tions, correspondence, negotiations, agreements, understandings, meetings, notices, requests, responses, demands, complaints or press, publicity or trade releases.

11. http://www.bloomberg.com/analysis/glossary/bfglosf.htm (defining "financial institution" as "an enterprise such as a bank whose primary business and function is to collect money from the public and invest it in financial assets such as stocks and bonds.").

12. *See* Governor Laurence H. Meyer, Remarks at the Federal Financial Institutions Examination Council, International Banking Conference, Arlington, Virginia (May 31, 2000) *at* http://www.federalreserve.gov/boarddocs/speeches/2000/20000531.htm (last updated May 31, 2000) (noting "the increasing scale, scope, span of operation, and general complexity of the largest banks operating in the United States").

13. *See* Federal Reserve Bank of N.Y., U.S. Monetary Policy and Financial Markets, at 61 (1998) *available at* http://www.ny.frb.org/education/addpub/monpol/ ("Originating, distribution, and servicing capabilities have . . . become increasingly significant elements of the banking business.").

14. *See* Steve Klinkerman, *Testing the Waters*, Banking Strategies, May/June 2001 *at* http://www.bai.org/bankingstrategies/2001-may-jun/testing_the_waters ("Financial institutions are renowned for their meticulous attention to all the details that underlie their complex operations.").

15. *See* Meyer, *supra* note 12 (discussing the challenges of supervising large, complex banking organizations).

16. Federal Reserve Bank of New York, *Fedpoint 44: U.S. Foreign Exchange Intervention*, *at* http://www.newyorkfed.org/aboutthefed/fedpoint/fed44.html (last updated Oct. 2003).

17. International Swaps and Derivatives Association, Inc., *A Retrospective of ISDA's Activities,* at 7 (2001) *available at* http://www.isda.org/whatsnew/pdf/Retrospective2001Master.pdf (last updated Apr. 12, 2002).

18. This includes: municipal, Treasury, mortgage-related, corporate, federal agencies, money market, and asset-backed debt. The Bond Market Association, *Outstanding Level of Public and Private Debt*, *at* http://www.bondmarkets.com/research/osdebt.shtml (3rd Quarter 2003).

19. International Swaps and Derivative Association, Inc., *Survey and Market Statistics, at* http://www.isda.org/statistics/recenthtml#2001end (last visited Feb. 10, 2004) (indicating the influence of large institutions on capital markets).

20. Edgar Online Access, *at* http://www.edgaronline.com/brand/eol/financial/fsFrame_vnav.asp?sym=JPM&id=0&op=balance (last visited Feb. 10, 2004) (providing JPMorgan Chase's balance sheet); *see at* http://www.edgar-online.com/brand/eol/financial/fsFrame_vnav.asp?sym=BAC&id=0&op=balance (last visited Feb. 10, 2004) (examining Bank of America's balance sheet); *see at* http://www.edgar-online.com/brand/eol/financial/fsFrame_vnav.asp?sym=LEH&id=0&op=balance (last visited Feb. 10, 2004) (listing Lehman Brothers' balance sheet); *see at* http://www.edgar-online.com/brand/eol/financial/fsFrame_vnav.asp?sym=ML&id=0&op=balance (last visited Feb. 10, 2004) (reviewing Merrill Lynch's balance sheet).

21. The term "derivative" refers to a volatile financial instrument whose value depends on or is derived from the performance of a secondary source such as an underlying bond, currency, or commodity. It is also termed derivative instrument. Derivatives transactions may be based on the value of foreign currency, U.S. Treasury bonds, stock indexes, or interest rates. The values of these underlying financial instruments are determined by market forces, such as movements in interest rates. *See* Black's Law Dictionary 712 (7th ed. 1999). *See also* http://www.bloomberg.com/analysis/glossary/bfglosd.htm (defining the term " derivative" as "a financial contract whose value is based on, or 'derived' from, a traditional security (such as a stock or bond), an asset (such as a commodity), or a market index").

22. *See supra* note 2 (indicating the notional of derivatives for 2001 year-end as well as the large institutions' balance sheets).

23. 27 Sec. Lit. Forms & Analysis § 6.19 (2003) (articulating the content of discovery documents in security litigation).

24. http://www.mapquest.com.

25. http://www.mapquest.com/about/main.adp.

26. http://www.bloomberg.com/analysis/glossary/bfglosl.htm (defining "life cycle" as "the lifetime of a product or business, from its creation to its demise or transformation").

27. *See* Linus Hakimattar, *Improving Profitability with Front-Office Systems*, National Petroleum News, March 1, 2003, at 28.

28. The DRM shown here is created from a generic bank and is not customized for the people, process and technology of a specific bank. While many of the people, process and technologies are similar across institutions, many are very different.

29. The information offered in this article about the process, people and technology involved in the Pre-Deal, Deal and Post-Deal phases of the life cycle is based upon first-hand discoveries conducted by the authors.

30. http://www.bloomberg.com/analysis/glossary/bfglosf.htm (defining the term "front office" as "refers to revenue generating sales personnel in a brokerage, insurance, or other financial services operation").

31. Although not yet commonplace, the use of virtual deal rooms can reduce the life cycle of the deal by improving channels of communication and information access, particularly with regard to highly structured long-term transactions that involve geographically dispersed parties from multiple organizations. *See* Sally R. Gonzalez, *Transaction Utopia: Virtual Deal Rooms Offer Speed, Security, and 24/7 Accessibility*, Legal Times, March 26, 2001, at 41 (discussion of the various sophistication levels of virtual deal rooms and the benefits they provide). In general, virtual deal rooms are secured Internet-accessible electronic meeting places that may provide, *inter alia*, online repositories of electronic documents, information and reference materials relevant to the transaction, electronic collaboration tools, and a logistics database including status reports, billing information, assignment and scheduling information. *Id.*

32. Manager is defined as "a person who administers or supervises the affairs of a business, office, or other organization." Black's Law Dictionary (7th ed. 2000).

33. Risk reporting in this article refers to reporting the "degree of uncertainty of return on an asset." Campbell R. Harvey, *Bloomberg Financial Glossary*, *at* http://www.bloomberg.com/analysis/glossary/bfglosr.htm (last modified Mar. 2, 2004).

34. "Books and records" in this article refers to "a book in which a detailed history of business transactions is entered" or "whatever is kept as written evidence of official doings and business transactions." Black's Law Dictionary 183 (6th ed. 1997).

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Who's in Charge? The Lead Plaintiff Provisions of the PSLRA Come of Age

By Jeffrey A. Klafter

I. Introduction

The Private Securities Litigation Reform Act (the "PSLRA") established an elaborate procedure for the appointment of the lead plaintiff(s) charged with prosecuting a class action. These provisions of the PSLRA arose from Congress' concern, expressed in the House, Senate and Conference Committee Reports on the bill, that class action securities litigation had become a "lawyer-driven" enterprise in which law firms sought to bring cases and then sought out nominally interested plaintiffs in the hope of obtaining quick settlements.[1] Congress sought to end this practice and protect investors who join class actions by increasing "the likelihood that parties with significant holdings in issuers, whose interests are more strongly aligned with the class of shareholders, will participate in the litigation and exercise control over the selection and actions of plaintiff's counsel."[2]

The statutory language, however, which was enacted in 1995 as part of the Republican Party's "Contract with America," is hardly a model of clarity. For much of the last eight years, courts have had to wrestle with its provisions with no guidance from the appellate courts. In the last two years, however, both the Third and Ninth Circuits have written extensive opinions on the subject. In addition, while there is still lower court disagreement on a number of provisions of the statute, certain of the previously unsettled areas appear to have been settled. Auctions and unwieldy groups are out and so is the appointment of "niche lead plaintiffs" to cover additional securities or offerings. The two circuit courts have also made it clear that the inquiry is a sequential one, starting with the lead plaintiff candidate with the largest financial interest, rather than a comparative one. The type of evidence necessary to rebut the presumption afforded the prospective lead plaintiff candidate with the largest financial interest has also been addressed by a number of courts. Clearly, the law is not settled on the lead plaintiff provisions, but the law has certainly matured during the last eight years and is well on its way to adulthood.

II. The Circuits Speak

After years of refusing to consider lead plaintiff issues on the grounds that such orders are not final orders,[3] both the Third and Ninth Circuits have now had occasion to write extensive opinions on the subject. While the Third Circuit decision arose from an appeal of the attorneys' fees awarded following a settlement of the action, the Ninth Circuit broke with precedent to issue a writ of mandamus vacating the district court's selection of lead plaintiff and counsel.

A. *Cendant*

In *In re Cendant Corp. Litig.*,[4] the Third Circuit Court of Appeals took the opportunity to discuss the entire statutory framework for the appointment of lead plaintiff. It clarified the approach to be utilized by district courts in determining which movant is entitled to the statutory presumption of "most adequate plaintiff" and in determining whether the presumption has been rebutted. In addition, as the lower court had utilized an *ex ante* auction procedure to establish the attorney award on appeal, the court dealt with the appropriateness of employing an auction process under the PSLRA.[5] On a related matter, the court ruled on the relevance of the fee arrangement reached between the movant and its chosen counsel and of pay-to-play allegations. Finally, the court staked out a well-reasoned standard for appointing a group as lead plaintiff.

Finding the statutory language to be far from clear, the court concluded that a district court must first determine which movant has the "largest financial interest" and then assess whether that movant "otherwise meets the requirements of Rule 23." The latter inquiry, the court found, is simply whether the movant has made a *prima facie* showing as to typicality and adequacy. Once the presumption has been afforded to the proper movant, the other movants (and not the defendant) have the opportunity to either show that the presumptively most adequate plaintiff "will not fairly or adequately protect the interests of the class" or "is subject to unique defenses that render such plaintiff incapable of adequately representing the class."[6] This inquiry, the court emphasized, is not a relative one:

> [O]nce the presumption is triggered, the question is *not* whether another movant might do a better job of protecting the interests of the class than the presumptive lead plaintiff; instead, the question is whether anyone can prove that the presumptive lead plaintiff will not do a "fair[ ] and adequate[ ]" job.[7]

The court further properly held that if the presumption has not been rebutted, the inquiry ends and the presumptive most adequate plaintiff should be appointed lead plaintiff. If, on the other hand, the presumption has been rebutted, the process must be renewed for the next movant with the largest financial interest.[8]

With regard to fee arrangements, the Third Circuit reasoned that the statutory scheme left little room for a district court to delve into the fee arrangement between the lead plaintiff and its chosen lead counsel. While the court acknowledged that the willingness and ability of the prospective lead plaintiff to select competent counsel and negotiate a reasonable retainer agreement with that counsel is relevant to the Rule 23 inquiry, it emphasized that the inquiry is a limited one:

> We stress, however, that the question at this stage is not whether the court would "approve" that movant's choice of counsel or the terms of its retainer agreement or whether another movant may have chosen better lawyers or negotiated a better fee agreement; rather, the question is whether the choices made by the movant with the largest losses are so deficient as to demonstrate that it will not fairly and adequately represent the interests of the class, thus disqualifying it from serving as lead plaintiff at all.[9]

Applying these precepts, the court held that the district court had properly rejected a challenge to the appointment of the CalPers group, consisting of the three largest public pension funds in the country, on the grounds that the challengers had negotiated a more favorable fee to the class.[10] This fact, without more, was, according to the court, insufficient to rebut the presumption. Only if the CalPers group failed to offer any objectively adequate explanation for their choice of counsel or fee agreement, however, might the presumption have been rebutted.[11] As the CalPers group clearly had an objective basis for their choice of counsel and had negotiated an extensive fee grid that was not patently unreasonable, the district court was correct in concluding that the presumption had not been rebutted on this ground.[12]

The Third Circuit also considered whether the presumption had been rebutted by allegations that plaintiffs' counsel had made campaign donations to one of the members of the CalPers group. While there was no dispute that the campaign donations had been made, there was no evidence that they played any role in the selection of counsel.[13] Where, however, such allegations could be substantiated, the Third Circuit made it clear that the presumption would be rebutted.[14]

On the subject of auctions to select counsel, the Third Circuit emphatically ruled them impermissible except in the rarest of circumstances.[15] The PSLRA, the court found, puts the choice of counsel squarely in the control of the lead plaintiff, providing that "[t]he most adequate plaintiff shall, subject to the approval of the court, select and retain counsel to represent the class."[16] The district court's role is only one of approval.[17] This conclusion, the Third Circuit found, is supported by not only the statutory language, but also the legislative history that reflects a judgment on the part of Congress that large investors are better equipped than the courts to select appropriate counsel.[18]

In reaching this conclusion, the Third Circuit expressly rejected the rationale employed by Judge Shadur in *In re Banc One Shareholders Class Actions*[19] to justify an attorney auction under the PSLRA. Judge Shadur had reasoned that the presumption would be rebutted for a prospective lead plaintiff who intended to foist a fee agreement on the class that was not as favorable as the fee agreement obtained by the court by means of a bidding process. In this circumstance, according to Judge Shadur, the presumption would be rebutted unless the prospective lead plaintiff agreed to the terms of the winning bid or to the counsel that proffered the winning bid.[20] In contrast, the Third Circuit concluded that the prospective lead plaintiff would be disqualified only if it could not offer a persuasive reason for the terms on which it retained counsel. Then, the selection process would shift to the movant with the next largest financial interest that otherwise satisfied the requirements of Rule 23.[21] A district court has no authority, the Third Circuit found, to then simply appoint the movant whose lawyer offered to work for less or condition the appointment of the presumptively most adequate plaintiff on its agreement to accept as counsel the winner of the bidding process or agree to the winning bid terms with its own counsel. This, the court found, is at odds with the PSLRA's vesting of the selection of counsel in the hands of the most adequate plaintiff, not the court.[22] Accordingly, the Third Circuit concluded, the mere fact the court can obtain better fee arrangement than counsel is not, in and of itself, sufficient to rebut the presumption.[23]

A district court's inquiry is limited, according to the Third Circuit, "to whether the lead plaintiff's selection and agreement with counsel are reasonable on their own terms."[24] To assess this, the court proffered the following non-exhaustive list of factors for the district court to consider:

> (1) the quantum of legal experience and sophistication possessed by the lead plaintiff; (2) the manner in which the lead plaintiff chose what law firms to consider; (3) the process by which the lead plaintiff selected its final choice; (4) the qualifications and experience of counsel selected by the lead plaintiff; and (5) the evidence that the retainer agreement negotiated by the lead plaintiff was (or was not) the product of serious negotiations between the lead plaintiff and the prospective lead counsel.[25]

The court went on to state that:

> We do not mean for this list to be exhaustive, or to intimate that district courts are required to give each of these factors equal weight in a particular case; at bottom, the ultimate inquiry is always whether the lead plaintiff's choices were the result of a good faith selection and negotiation process and were arrived at via meaningful arms-length bargaining. Whenever it is shown that they were not, it is the court's obligation to disapprove the lead plaintiff's choices.[26]

The only circumstance in which the Third Circuit indicated an auction could be permissible is remote at best. The court hypothesized that where a prospective lead plaintiff was repeatedly derelict in its duty to select counsel and there is an absence of any other qualified lead plaintiff, it would be appropriate for a court to become involved in the counsel selection process and, among other things, employ an auction.[27] Applying these principles, the Third Circuit reversed the lower court's decision to hold an auction, finding that there was no evidence that the CalPers group's process for selecting counsel was inadequate.[28]

B. *In re Cavanaugh*

Largely following the Third Circuit's lead, in *In re David Cavanaugh*,[29] the Ninth Circuit found numerous vices in the district court's approach to the selection of the lead plaintiff. Judge Vaughn R. Walker had appointed the lead plaintiff based on a comparison of fee agreements as well as each movant's knowledge of the case, the extent of negotiations with their chosen law firm, and their ability to monitor their chosen counsel's performance.[30] Specifically, although the so-called Cavanaugh group was presumptively the most adequate plaintiff, the district court found the presumption rebutted because a competing movant, Barton, had negotiated a better fee arrangement.[31]

The Ninth Circuit described the lead plaintiff selection process as a "simple three-step process."[32] First, notice comporting with 15 U.S.C. § 78u-4(a)(3)(A)(i) must be disseminated. Second, the presumptive lead plaintiff must be determined, and third, the other movants must have the opportunity to rebut the presumption.[33] Similar to the Third Circuit, the Ninth Circuit described step two as involving a non-adversarial *prima facie* showing and the third step as involving an adversarial process. Also, consistent with the Third Circuit, the Ninth Circuit described the appointment process to be sequential rather than comparative.[34] In contrast, the Ninth Circuit described the district court's approach as "a freewheeling comparison of the parties competing for lead plaintiff, questioning them about their business acumen, their knowledge of the lawsuit and, especially, their fee arrangements with their respective lawyers."[35] Such a "beauty contest," the Ninth Circuit declared, is not permissible under the PSLRA.[36]

The only permissible comparison is to weigh the financial losses of the competing movants. Once the movant with the largest financial interest has been determined, the focus shifts to whether that movant otherwise meets the requirements of Rule 23 and whether the presumption afforded that movant has been rebutted.[37] That is not to say that the presumptive lead plaintiff's retention of counsel is irrelevant. The Ninth Circuit stated that a district court has latitude as to what information it considers in determining whether the movant with the largest financial interest "otherwise meets the requirements of Rule 23," and may examine counsel arrangements, but only for limited purposes.[38] According to the Ninth Circuit, such purposes would include "ensuring that the plaintiff is not receiving preferential treatment through some back-door financial arrangement with counsel or proposing to employ a lawyer with a conflict of interest."[39] The focus, however, according to the Ninth Circuit, is whether the agreement "so reek[s] of self-dealing or other impropriety as to suggest that the plaintiff may have sold out the class's financial interests to the lawyer. . . ."[40] Absent such extreme circumstances, a prospective lead plaintiff has wide latitude in entering into a fee agreement with its chosen counsel.[41] Thus, how advantageous a fee arrangement the proposed lead plaintiff negotiated is not a proper inquiry and not a basis for disqualification.[42]

Such pre-appointment arrangements, the Ninth Circuit observed, are poor indicators of a movant's adequacy as they are "inherently hypothetical and contingent" and because a movant, knowing that a court will ultimately have to approve a reasonable fee, may be more concerned with retaining the best counsel than obtaining the lowest fee.[43] There is nothing inherently wrong, the Ninth Circuit reasoned, for a prospective lead plaintiff to hire a law firm best equipped to intimidate defense counsel even though they may demand a greater fee schedule.[44] In contrast, Judge Walker's approach, the Ninth Circuit noted, would put pressure on movants to retain counsel offering the lowest fees rather than counsel believed to be able to do the best job.[45]

Thus, with the Ninth Circuit's decision in *In re Cavanaugh* and the Third Circuit's decision in *Cendant*, fee arrangements with counsel, if objectively reasonable and the product of negotiation, should not provide any basis for a court to disqualify an otherwise appropriate lead plaintiff. Moreover, these Circuits have settled the question of whether an auction can be conducted in a PSLRA case and whether a court can otherwise engage in comparisons of the adequacy and typicality of the competing movants. Since these decisions and since the writing of this article, no district court has employed an auction in a PSLRA case and no court has used an arrangement with counsel to disqualify an otherwise qualified movant. Therefore, although only two Circuits have weighed in on these issues, they appear to have been settled. As discussed below, however, there remain other areas of disagreement among the courts.

III. Making Sense of the Lower Courts

A. The Certification Requirement

Section 21 (D)(a)(2)(A) of the Exchange Act, 15 U.S.C.A. § 78u-4(a)(2)(A), and section 26(a)(2)(A) of the Securities Act, 15 U.S.C.A. § 77z-1(a)(2)(A), state that "each plaintiff seeking to serve as a representative party on behalf of a class shall provide a sworn certification, which shall be personally signed by such plaintiff and filed with the complaint . . ." This seemingly straightforward provision has led to much controversy.

Shortly after the enactment of the PSLRA, in *Greebel v. FTP Software, Inc.*,[46] Chief Judge Tauro of the District of Massachusetts was called upon to decide whether, and to what extent, a defendant is entitled to challenge compliance with this requirement, and whether all contenders for lead plaintiff status are required to file a certification. Finding that the failure to file a certification with a complaint is "fatal" to the maintenance of a class action, the court reasoned that "defendants have the same interest in demanding compliance with these provisions as they have with other requirements relating to certification of a class."[47] The court further reasoned that the provision embodying the certification requirement stands in contrast to section 21(D)(a)(3)(B), which affords a right to rebut the presumption that the movant with the largest financial interest who otherwise satisfies the requirements of Rule 23, but only on the part of other members of the class.[48]

On the issue of who needs to file a certification, the court found the statutory language, which only requires a certification to be filed with a complaint, to be determinative.[49] In contrast, the court observed, a contender for lead plaintiff status is not required to file a complaint, but can seek appointment by filing a motion.[50] The court also found the issue resolved by the Senate Committee Report and the Conference Committee Report, both of which expressly state that a certification need not be filed with a motion for appointment as lead plaintiff.[51]

Two years later, departing from *Greebel* somewhat, the court in *Carson v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*[52] concluded that the failure to file a certification with a complaint was not fatal to the maintenance of a class action. Rather, the court concluded, that such failure could be cured with the filing of an amended complaint.[53] The circumstances before the court in *Carson*, however, appear to have been *sui generes.* For some reason, the class action had been initiated without any effort to comply with the requirements of the PSLRA and Carson was seeking to be replaced by new named plaintiffs who would in turn comply with the certification and other requirements.[54]

More relevant to the import of the certification requirements is *Burke v. Ruttenberg*.[55] In that case, the court rejected the plain language of the statute to hold that the certification requirement applies to all contenders for lead plaintiff, regardless of whether they filed a complaint.[56] In so doing, the court relied on the court's decision in *Chill v. Green Tree Financial Corp.*,[57] which had relied solely on the selective portions of the legislative history to bolster its conclusion. Congress, according to these courts, had expressed a desire that "basic information about the lead plaintiff should be provided at the outset of the litigation."[58] Putting aside the import of a Senate Report, that very report confirms that the certification requirement runs with the filing of a complaint.[59] These courts also found it "anomalous, if not perverse to require sworn certifications from only the plaintiffs named in a complaint, but then allow other persons to be appointed as Lead Plaintiffs. . . . "[60] These and other policy arguments advanced by these courts carry some weight but ignore the statutory language that speaks otherwise. As this area is unsettled, the safest course of action is to submit a certification regardless of whether the movant is filing a complaint.

Adding more confusion to a seemingly clear provision is the recent decision in *In re Eaton Vance Corp. Securities Litigation*.[61] There, the court held that a named plaintiff added to an amended complaint after the completion of the lead plaintiff appointment process could not serve as a class representative because he had not served a certification with the amended complaint. This decision is unprecedented and at odds with several courts, which have held that the appointment of lead plaintiffs and the certification of a class are separate and distinct inquiries.[62]

B. Determining the Largest Financial Interest

In most lead plaintiff contests, the financial interests of the prospective lead plaintiffs are neither close nor in dispute. Rather, the selection of the lead plaintiff is determined on other grounds. Certain contests, however, have required an analysis of just what the "largest financial interest" means. Chief among them is the dispute that arose between the New York City Pension Funds ("NRCPF") and New York State Common Retirement Funds ("NYSCRF") for control of the *In re McKesson HBOC, Inc. Securities Litigation.*

Each of these movants took the position before the district court that they had the largest financial interest in the relief sought. In order to permit a meaningful analysis of their contentions, the court required each of these movants to exchange trading data and file a joint submission covering the following four perspectives on losses:

(1) The number of shares purchased during the class period;

(2) The number of net shares purchased during the class period;

(3) The net funds expended during the class period; and

(4) Approximate losses from the alleged fraud.[63]

The parties had varied interpretations of each of these seemingly straightforward calculations due to the merger that occurred in the midst of the class period. As a result, HBOC shares were purchased prior to the merger, exchanged for McKesson HBOC shares in the merger, and McKesson HBOC shares were purchased following the merger. Due to these circumstances, the court found the first two factors of little help in assessing the relative financial interests of these two movants.

With regard to the third factor (net funds expended), the court found that NYSCRF had expended a net total of $15,006,015 and that NYCPF had net receipts of $681,298. Although not dispositive, the court reasoned that a net purchaser would have a greater interest in the litigation as they purchased shares during the class period and were left "holding the bag."[64] A net seller, the court observed, has arguably profited more from the fraud than it has been injured.[65] Other courts have similarly declined to resolve this issue.

Turning to the last factor (the approximate losses from the fraud), NYCPF and NYSCRF had offered differing standards for evaluating it. NYCPF urged that all economic losses be considered, while NYSCRF maintained that only damages caused by the alleged fraud should be included.[66] Finding the legislative history to be devoid of any insight on this dispute, the court noted that a dictionary definition of the phrase "financial interest" would support the latter interpretation, but found it unnecessary to resolve this issue, as it concluded that NYSCRF's economic loss and damages exceeded those of NYCPF.[67]

Other courts have similarly avoided delving deeply into this issue. For example, in *In re Critical Path Securities Litigation*,[68] the district court concluded that the analysis must focus on the "potential recovery" and that assuming the inflation were constant during the class period, the number of net shares purchased would be determinative.[69] The court went on, however, to hold that these damages must be supplemented by in-and-out damages, but offered no methodology for computing them.[70] Indeed, to afford in-and-out damages is contrary to the court's presumption that inflation was constant during the class period.[71]

As the district court noted, other courts have appointed in-and-out traders as lead plaintiffs.[72] None of these decisions, however, employed an appropriate damage analysis to determine whether the in-and-out traders had recognizable damages. Rather, their losses were simply included in determining the overall losses of the movant.

In *Royal Ahold*, the court noted two methods for ascertaining the largest financial interest, the "net/net" method and the "FIFO" method. The former, the court stated, involves consideration of, among other things: "(1) the number of shares purchased by the movant during the class period; (2) the total net funds expended by the plaintiffs during the class period; and (3) the approximate losses suffered by the plaintiffs."[73] The latter method is determined by adding "(1) shares purchased and sold during the class period; (2) shares purchased during the class period and sold during the 90-day look-back period; and (3) shares purchased during the class period and retained after the 90-day look-back period."[74] Declining to resolve which method to employ, the court stated that it would assume one of the movants had the largest financial interest and resolve the lead plaintiff issue on other grounds.[75]

The apparent unwillingness of courts to conduct anything other than a rudimentary damage analysis is, in all likelihood, a product of the complexities involved

in a full-blown damage analysis and the cause of extensive potential for disagreement. For example, two equally qualified damage experts can reach dramatically different conclusions on whether particular events during the class period either caused any inflation or reduced the inflation. There can also be disagreements on whether the proper approach to inflation should involve constant inflation throughout the class period or something else. Further, as these issues are best considered on a fully developed record, the lead plaintiff stage of the action seems to be a particularly inappropriate time to engage in such an analysis. Thus, we can expect courts to continue to make use of the four-factor test set forth above and basic damage principles in determining which movant has the largest financial interest in the relief sought. The recent wave of mutual fund cases, however, may sorely test the ability of courts to utilize the same principles. The appropriate measure of damages to investors is far from clear, and losses may be wholly unrelated to the improper trading at issue on those cases. The movants have argued that the dollar amount invested is the determinative factor. Whether the courts will embrace that standard remains to be seen.

C. The Extent to Which Groups Are Still Permissible

Following *Cendant*, which involved a group of three institutional investors, those lower courts that have had the opportunity to address the propriety of groups have appointed groups consistent with the Third Circuit's standard. Thus, in *Janovici v. O'Hanlon*,[76] the court appointed the Cedar Street Group, consisting of the Cedar Street Fund and the Cedar Street Offshore Fund—two related institutional investors, and an unrelated individual investor. Similarly, in *Royal Ahold*, the court appointed The Public Employees Retirement System of Colorado ("CoPERA") and Generic Trading of Philadelphia, LLC ("Generic").[77] In contrast, no court since *Cendant* has appointed any unwieldy group to lead a securities class action.[78]

The courts have also rejected attempts by lead-plaintiff movants to be added as a lead plaintiff to ensure that the lead plaintiffs have standing to assert all of the claims at issue in the litigation. The courts have characterized this argument as the "niche plaintiff" argument. In each decision, rather than appointing multiple lead plaintiffs comprised of competing movants, the courts have opted for the appointment of a single strong lead plaintiff with authority to add additional name plaintiffs to the action as needed to represent subclasses. In *Weinberg v. Atlas Air Worldwide Holdings, Inc.*,[79] for example, the court refused to add one of the movants as a lead plaintiff, even though the presumptive lead plaintiff lacked individual standing to assert Securities Acts claims or sue a particular defendant.[80] In addition to finding this argument to have been rejected by at least two courts within the Southern District,[81] the court reasoned that appointing multiple lead plaintiffs would "fracture the litigation" and be inconsistent with the purposes of the PSLRA.[82]

Similarly, in *Enron*, various movants sought appointment as co-lead plaintiffs to represent purchasers of preferred stock, bonds, and notes issued by Enron. Framing the issue as one of typicality, the court found that identity of claims is not required and that there is ample authority for the ability of purchasers of one security issued by a defendant to represent purchasers of other securities issued by that defendant.[83] The court further concluded that to appoint multiple lead plaintiffs to represent each purportedly disparate interest "would fracture this litigation into hundreds of classes or subclasses and obstruct any efficient and controlled progress" and that this result must give weight to the appointment of a single strong lead plaintiff.[84]

Nevertheless, recognizing that certain of the "niche plaintiff" arguments may have a place at the class certification stage, the court gave leave to raise these issues again at such time.[85] Thus, the emerging view appears to be that absent a clear conflict or jurisdictional impediment, a court is unlikely to appoint competing movants as co-lead plaintiffs.

D. Rebutting the Presumption

The PSLRA provides that the presumption in favor of the most adequate plaintiff "may be rebutted *only upon proof* by a member of the purported plaintiff class that the presumptively most adequate plaintiff . . . *will not* fairly and adequately represent the interests of the class."[86] In recent years, creativity has not been lacking in means to demonstrate the requisite proof. Extensive investigatory efforts have been devoted by competing movants in the hope of unearthing some conflict or other incapacitating fact. These efforts, however, have met with mixed results.

1. Jurisdictional Defenses

The facts of *Royal Ahold* are illustrative. Union Asset Holding AG ("Union"), a Dutch company, and the General Retirement System of Detroit ("Detroit") sought appointment as co-lead plaintiffs over the action and asserted that this group was presumptively the most adequate plaintiff. Although the Union/Detroit group arguably had greater losses, CoPERA and Generic argued that Union suffered from substantial conflicts of interest and jurisdictional defenses which rendered it atypical of the members of the class.

Specifically, CoPERA and Generic maintained that one of Union's owners, Rabobank, acted as an underwriter or co-manager for offerings of Ahold securities, rendered research reports on Ahold, acted as a member of the syndicate that provided loans to Ahold, and therefore had access to non-public information during the class period. Moreover, CoPERA and Generic contended that Union is a foreign entity that purchased foreign securities of Ahold on a foreign exchange and is therefore subject to jurisdictional defenses. On a related point, CoPERA and Generic argued that Union faced unique issues in certifying a class including similar foreign purchasers on foreign exchanges because foreign jurisdictions may not give *res judicata* effect to an opt-out notice.

The court agreed with the latter two arguments and found them sufficient to rebut the most adequate plaintiff presumption.[87] Noting that subject matter jurisdiction for claims of a foreign purchaser on a foreign exchange must rest on the "conduct" test,[88] the court observed that while a portion of the alleged fraud occurred at Royal Ahold's U.S. Foodservice subsidiary, the statements at issue were disseminated by Royal Ahold in the Netherlands. Moreover, the alleged fraud also involved Royal Ahold's foreign joint ventures and conduct at an Argentine subsidiary of the company.[89] These facts, the court found, raised a unique defense that threatened to divert a substantial amount of time and effort from the prosecution of the class's claims and that created an incentive to avoid proving purely foreign wrongdoing.[90] The court also agreed with the argument advanced by CoPERA and Generic that foreign purchasers may not be included in any certified class because foreign jurisdictions might not enforce a judgment predicated on an opt-out notice.[91]

2. Relationships Between the Lead Plaintiff or Its Owners and the Defendant

The court in *Royal Ahold* also addressed CoPERA and Generic's arguments concerning the relationship between Union and Rabobank, but held, however, that mere financial ownership, absent any direct transfer of non-public information, is not a disqualifying factor.[92]

Similarly, in *A.F.I.K. Holding SPRL v. Fass*,[93] the court held that the presumption had not been rebutted by evidence that the grandparent company of one of the proposed lead plaintiffs had loans outstanding of almost $20 million. According to the objectors to the lead plaintiff's appointment, the lead plaintiff's incentive was to recover its grandparent company's $20 million rather than its $650,000 in losses.[94] Although the court found that this relationship created a "nascent conflict," it concluded that it was akin to the type of conflict a continued holder of securities in the defendant issuer has.[95] Such a conflict, however, the court noted, has been held by the Third Circuit in *Cendant* not to raise a disabling conflict.[96] Accordingly, the court concluded, even a loan directly from the lead plaintiff to the defendant issuer in and of itself would not rebut the presumption. It would require, according to the court, not only evidence of direct contact between the prospective lead plaintiff and the defendant, but also evidence that the lead plaintiff had been privy to non-public information and traded on it.[97] This, of course, is virtually impossible to prove absent discovery, and courts will not likely permit discovery on this issue as it could substantially delay the appointment of the lead plaintiff.

3. Contributory Negligence

New Jersey's entry into the lead plaintiff arena has also spawned new case law on what type of evidence is sufficient to rebut the most adequate plaintiff presumption. In two recent cases, competing movants to New Jersey argued that New Jersey was subject to unique defenses concerning its investments in the subject securities because New Jersey officials had criticized the state's Department of Investment and blamed it for the state's losses.[98] Both decisions rejected this argument, finding that New Jersey's investments in each subject security were never publicly criticized, and that even if New Jersey was negligent, contributory negligence is not a defense to securities fraud.[99]

4. The Selection of Counsel

Both decisions also involved challenges to New Jersey's adequacy based upon its manner of selecting counsel. In *Craig*, the court noted that the Ninth Circuit and Third Circuit are in agreement that the inquiry concerning choice of counsel is a limited one, focused solely on whether the lead plaintiff's choice is so devoid of any reasonable basis. It observed, however, that district courts in Illinois and elsewhere have disagreed.[100] Concluding that it had some latitude on this issue, since the Seventh Circuit has not reached this issue, the court found it appropriate to require New Jersey to make supplemental submissions addressing the five factors that the Securities and Exchange Commission suggested should be addressed before appointing a lead plaintiff.[101]

In *Motorola*, the court addressed the same type of "pay-to-play" allegations concerning the selection of counsel that were found lacking in *Cendant*. Although the *Bergen Record* had reported that Governor McGreevey's administration considered hiring firms that made political contributions to the governor, the court found no evidence of impropriety, as the article made no mention of Motorola or the firms selected to represent New Jersey in the litigation.[102] In addition, the court noted, the chosen counsel for New Jersey had

submitted a sworn affidavit that neither the individual lawyers nor their firm had made or caused others to make political contributions to Governor McGreevey.[103] Given this uncontroverted evidence, the accusations to the contrary carried no weight.[104]

5. Investment Advisers, Day-Traders and Hedge Funds

As Congress intended, public pension funds have not been the only contenders for lead plaintiff status. Investment advisers, day-traders and hedge funds have come forward in select cases, but have been met with a plethora of challenges to their typicality.

In *Suprema Specialties*, the movant with the largest financial loss, StoneRidge Investment, was an investment adviser that had invested in Suprema itself as well as on behalf of twenty-two clients.[105] The court found several grounds for disqualifying StoneRidge as lead plaintiff. First, StoneRidge had not submitted any evidence that it had obtained permission from its clients to seek lead plaintiff status on its behalf or was attorney-in-fact for its clients.[106] Moreover, unlike other account managers who had been held to be adequate lead plaintiffs, StoneRidge did not function as a "single investor" with its clients.[107] Further, the court found that StoneRidge could not qualify as a group since no certifications had been submitted by its clients, and that even if they had, the group would be unwieldy and barred by the *Cendant* decision.[108]

Taking a different track from the district court in *Suprema Specialties*, the district court in *HPL Technologies* appointed an investment adviser whose losses dwarfed those of the other movants as lead plaintiff.[109] There, the investment adviser did not retain beneficial ownership of the shares purchased and had complete investment authority, but there was no evidence before the court that it had authority to commence suit on behalf of its clients.[110] The court, however, found the investment adviser to be the "real party in interest" as it made the actual purchases at issue and, based upon the submissions made to the court, "had complete discretion over its clients' accounts."[111] Perhaps, the court's conclusion was influenced by the fact that the investment adviser was the only institutional plaintiff seeking lead plaintiff status and its losses dwarfed those of the other movants. Judge Walker has previously expressed a preference for institutional investors.[112]

The district courts have also reached differing conclusions as to whether hedge funds and day traders can serve as lead plaintiffs. The district courts in both *In re Microstrategy Inc. Securities Litigation*[113] and *In re Bank One Shareholders Class Action*[114] declined to appoint such entities, finding their trading strategies to be atypical. The better reasoned approach is embodied by the majority of decisions which have aptly recognized that even sophisticated investors can be the victims of fraud.[115]

IV. Conclusion

While two circuit courts have provided some consistent clarity on the lead plaintiff appointment process, and the district courts have reached agreement on such issues as what types of groups may be appointed as lead plaintiffs, there remains much disagreement at the district court level on many of the issues which arise in the typical case. Thus, although the lead plaintiff provisions of the PSLRA have matured somewhat, at age eight, they clearly have more room for growth. Absent the unusual case which will present an opportunity for another circuit court to address these issues, this growth will necessarily be driven by lower court decisions which hopefully will reach some consensus on more of the relevant issues.

Endnotes

1. *Aronson v. McKesson HBOC, Inc.*, 79 F. Supp. 2d 1146, 1152 (N.D. Cal. 1999).
2. Conference Report on Securities Litigation Reform, H.R. Rep. No. 369, 104th Congress, 1st Sess. 34 (1995), reprinted in 1995 USCC&AN 679, 1995 WL 709276 at 28.
3. *See In re Bankamerica Corp. Sec. Litig.*, 263 F.3d 795 (8th Cir. 2001) (lead plaintiff order not appealable as a final order or under the collateral order doctrine); *Florida State Bd. of Admin. v. Brick*, 210 F.3d 371 (6th Cir. 2000) (determination of lead plaintiff is not an appealable final decision); *In re State of Wisconsin Inv. Bd.*, No. 00-12751-F (11th Cir., June 14, 2000) (denying petition for writ of mandamus); *Metro Services, Inc. v. Wiggins*, 158 F.3d 162, 165 (2d Cir. 1998) (determination of lead plaintiff is not an appealable final decision); *Pindus v. Flemming Companies, Inc.*, 146 F.3d 1224, 1226–27 (10th Cir. 1998) (refusing to review a lead plaintiff determination as final or pursuant to a writ of mandamus); *see also Burke v. Ruttenberg*, 317 F.3d 1261 (11th Cir. 2003) (finding SWIB had not preserved its lead plaintiff challenge for appeal).
4. 264 F.3d 201 (3d Cir. 2001), *cert. denied*, 152 L. Ed. 2d 212, 122 S. Ct. 1300 (2002).
5. In addition to the lower court decision, the Third Circuit cited the following eight PSLRA cases as employing or directing the selection of lead counsel by means of an auction process: *Raftery v. Mercury Fin. Co.*, No. 97 C 624, 1997 WL 529553 (N.D. Ill. 1997) (Lefkow, J.); *Sherleigh Assoc. LLC v. Windmere-Durable Holdings, Inc.*, 184 F.R.D. 688 (S.D. Fla. 1999) (Lenard, J.); *Wenderhold v. Cylink Corp.*, 188 F.R.D. 577 (N.D. Cal. 1999) (Walker, J.); *In re Lucent Tech., Inc. Sec. Litig.*, 194 F.R.D. 137 (D.N.J. 2000) (Lechner, J.); *In re Bank One S'holders Class Actions*, 96 F. Supp. 2d 780 (N.D. Ill. 2000) (Shadur, J.); *In re Comdisco Sec. Litig.*, 141 F. Supp. 2d 951 (N.D. Ill. 2001) (Shadur, J.); *In re Quintus Sec. Litig.*, 148 F. Supp. 2d 976 (N.D. Cal. 2001) (Walker, J.); *In re Network Assocs. Inc. Sec. Litig.*, 76 F. Supp. 2d 1017 (N.D. Cal. 1999) (Alsup, J.) (directing the lead plaintiff to undertake an auction process). 264 F.3d at 258 n.35. In addition, Judge Lechner directed the selection of counsel by means of an auction in *In re Lucent Tech., Inc., Sec. Litig.*, 221 F. Supp. 2d 472 (D.N.J. 2001) ("*Lucent II*").
6. *In re Cendant Corp. Litig.*, 264 F.3d at 263–264.
7. *Id.* at 268 (emphasis in original).

8. The Third Circuit also found the adequacy inquiry to govern the approval of groups as lead plaintiffs:

> If the court determines that the way in which a group seeking to become lead plaintiff was formed or the manner in which it is constituted would preclude it from fulfilling the tasks assigned to a lead plaintiff, the court should disqualify that movant on the grounds that it will not fairly and adequately represent the interests of the class.

264 F.3d at 266. Departing from certain other courts, the Third Circuit rejected any standard based solely on whether the members of the group had a pre-existing relationship. *Id* at 266–267. The court acknowledged, however, that the presence of such a pre-existing relationship might be relevant to the adequacy inquiry. *Id.* Employing this standard, the court approved of those decisions rejecting groups cobbled together by lawyers for the sole purpose of seeking lead plaintiff status, and groups which, due to their size, cannot be counted on to manage the litigation and their counsel. The court further was in agreement with the SEC's position that groups of more than five are generally too large to be effective lead plaintiffs.

9. *In re Cendant Corp. Litig.*, 264 F.3d at 266.
10. *Id.* at 269.
11. *Id.*
12. *Id.* at 268–269.
13. *Id.* at 269–270.
14. *Id.* Discovery, however, the court indicated, would not be available in the absence of a *prima facie* showing that the attorney selection process had been influenced by political contributions. *Id.* at 270 n.48. The court, however, confirmed the authority of a district court to require disclosure of any campaign contributions to the presumptively most adequate plaintiff by their chosen counsel, and, if there were any, "a sworn declaration describing the process by which it selected counsel and attesting to the degree to which the selection process was or was not influenced by any elected officials." *Id.* at 270 n.49.
15. *Id.* at 271–272.
16. *Id.* at 273. 15 U.S.C. § 78u-4(a)(3)(B)(v).
17. *Id.*
18. *Id.*
19. 96 F. Supp. 2d 780, 784 (N.D. Ill. 2000).
20. *Id.* at 784.
21. *In re Cendant Corp. Litig.*, 264 F.3d at 275.
22. *Id.* at 275–276.
23. *Id.* at 276.
24. *Id.*
25. *Id.*
26. *Id.*
27. *Id.* at 277.
28. *Id.* at 279–280. The lower court had invoked two principle justifications for embarking on an auction. The first was that it would simulate the market and provide a benchmark of reasonableness. The second was that it would dispel the pay-to-play issues that had arisen. 264 F.3d at 278–279. The Third Circuit found neither justification to be adequate. The first, it reasoned, would be present in any case and was unnecessary where the presumptive lead plaintiff has negotiated in good faith with its chosen counsel. The second was insufficient, as the allegations that the arrangement with counsel was tainted by campaign contributions were unsubstantiated. *Id.*
29. 306 F.3d 726 (9th Cir. 2002).
30. *Id.* at 728.
31. *Id.*
32. *Id.* at 730.
33. *Id.*
34. *Id.*
35. *Id.* at 732.
36. *Id.*
37. *Id.*
38. *Id.*
39. *Id.*
40. *Id.* at 736. Similarly, the Ninth Circuit noted that a district court would be justified in inquiring how a sole practitioner or recent law graduate proposes to prosecute the action, as such information is relevant to the adequacy of the proposed lead plaintiff. *Id* at 733.
41. *Id.* Moreover, even where the movant's choice of counsel is patently inadequate, that is not the end of consideration of the movant. Before disqualifying the movant, according to the Ninth Circuit, a district court should so advise the movant and inquire whether the movant is willing to retain alternative counsel if appointed. *Id.* at 733 n.12.
42. *Id.* at 736.
43. *Id.* at 733–34.
44. *Id.* at 735.
45. *Id.* at 734.
46. 939 F. Supp. 57 (D. Mass 1996).
47. *Id.* at 60.
48. *Id.* Based upon the same rationale, the *Greebel* court concluded that a defendant also has the right to object to the adequacy of notice.
49. *Id.*
50. *Id.* at 61.
51. *Id.* at 62; a*ccord*, *Tarica v. McDermott Int'l, Inc.*, 2000 U.S. Dist. LEXIS 5031, at *6 (E.D. La., April 13, 2000) (finding only named plaintiffs rather than all movants need comply with the certification requirement); *Aronson v. McKesson HBOC, Inc.*, 79 F. Supp. 2d 1146, 1155 (N.D. Cal. 1999) (same).
52. 1998 U.S. Dist. LEXIS 6903 (W.D. Ark. 1998).
53. *Id.* at *16–17.
54. *Id. at* * 15.
55. 102 F. Supp. 2d 1280 (N.D. Ala. 2000).
56. *Id.* at 1319–1320.
57. 181 F.R.D. 398, 410 (D. Minn. 1998).
58. *Id.* at 410 (citing Senate Report No. 104-98 at 689).
59. *Id.*
60. 102 F. Supp. 2d at 1318 (quoting *Chill*, 181 F.R.D. at 410).
61. 220 F.R.D. 162 (D. Mass 2004).
62. *See In re Cavanaugh*, 306 F. 3d at 736 ("The Reform Act did not change the standard for adequacy . . . under Rule 23."); *In re Oxford Health Plans, Inc. Sec. Litig.*, 199 F.R.D. 119, 125 (S.D.N.Y. 2001) (finding the class representative is selected not pursuant to the [Reform Act], but pursuant to Rule 23); *Greebel*, 939 F. Supp. at 60 ("[I]t seems clear that Congress recognized that these motions [for lead plaintiff and for class certification] involved distinct inquiries."). The decision has been appealed to

the First Circuit Court of Appeals pursuant to Fed. R. Civ. P. 23(f).

63. *In re McKesson HBOC, Inc. Sec. Litig*., 97 F. Supp. 2d 993, 995 (N. D. Cal. 1999). The court noted that this four-factor test had been suggested by the court in *In re Olsten Corp. Sec. Litig.*, 3 F. Supp. 2d 286, 295 (E.D.N.Y. 1998). For other courts applying it, see, e.g., *Cendant*, 264 F.3d at 262; *Schulman v. Lumenis, Ltd.*, 2003 U.S. Dist LEXIS 10348, *18 (S.D.N.Y. June 18, 2003); *Casden v. HPL Tech., Inc.*, 2003 U.S. Dist. LEXIS 19606, *12–15 (N.D. Cal., September 29, 2003) (requiring spreadsheets from which the court could conduct the four-factor test); *In re Enron Corp. Sec. Litig.*, 206 F.R.D. 427, 440 (S.D. Tex. 2002); *In re Waste Mgmt., Inc. Sec. Litig.*, 128 F. Supp. 2d 401, 409 (S.D. Tex. 2002); *In re Nice Sec. Litig.*, 188 F.R.D. 206, 217 (D.N.J. 1999).

64. *In re McKesson HBOC, Inc. Sec. Litig*., 97 F. Supp. 2d at 996–97.

65. *Id.* at 997.

66. *Id.*

67. *Id.*

68. 156 F. Supp. 2d 1102 (N.D. Cal. 2001*), relying on In re Newtork Assoc., Inc. Sec. Litig*., 76 F. Supp. 2d 1017, 1027 (N.D. Cal 1999).

69. *Id.* at 1107–1108; *see also In re Cable & Wireless PLC Sec. Litig*., 217 F.R.D. 372 (E.D. Va. 2003) (adopting the *Critical Path* court's formulation).

70. 156 F. Supp. 2d at 1107–1108.

71. *See also In re Milsetone Scientific Sec. Litig.*, 183 F.R.D. 404, 414 n.11 (D.N.J. 1998) (suggesting section 10(b) damage standards would govern lead plaintiff appointment). *Cf. In re Ribozyme Pharmaceuticals, Inc. Sec. Litig*., 192 F.R.D. 656, 659–61 (D. Colo. 2000) (rejecting use of PSLRA damage limitations in determining the largest financial interest, finding "retention losses" to be the determinative factor).

72. 156 F. Supp 2d at 1108 *(citing In re Cirrus Logic Sec*., 155 F.R.D. 654, 661–662 (N.D. Cal. 1994) (finding in/out traders can recover damages and can serve as class representatives)); *Green Tree Fin. Corp*., 181 F.R.D. at 411 (including in/out losses in "financial interest" for selection of lead plaintiff*); see also In re Royal Ahold N.V. Sec. and ERISA Litig*., 219 F.R.D. 343 (D. Md. 2003) (appointing Generic Trading as co-lead plaintiff even though it is a day-trader).

73. 219 F.R.D. at 349.

74. *Id.*

75. *Id.* at 7.

76. 2003 U.S. Dist. LEXIS 22315 (E.D. Pa., Nov. 25, 2003).

77. *See also A.F.I.K. Holding SPRL v. Fass*, 216 F.R.D. 567, 576 (D.N.J. 2003) (appointing two-member group consisting of an unrelated individual and institution); *In re Crayfish Company Sec. Litig.*, 2002 U.S. Dist. LEXIS 10134 (S.D.N.Y. 2002) (finding seven-member group not to be cumbersome and appointing as lead plaintiff); *In re Orthodontic Centers of America, Inc. Sec. Litig*., 2001 U.S. Dist. LEXIS 21816 at *13–16 (E.D. La., Dec. 19, 2001) (appointing group of four unrelated individuals and a church as co-lead plaintiff).

78. *See, e.g,. Smith v. Suprema Specialties, Inc.*, 206 F. Supp. 2d 627, 635 (D.N.J. 2002) (refusing to appoint aggregation of twenty-two unrelated plaintiffs).

79. 216 F.R.D. 248 (S.D.N.Y. 2003).

80. *Id.* at 253.

81. *In re Crayfish*, 2002 U.S. Dist. LEXIS 10134 (S.D.N.Y. 2002) and *In re Initial Public Offerings Sec. Litig.*, 214 F.R.D. 117, 122–23 (S.D.N.Y. 2002) (finding addition of class representatives to represent sub-classes to be consistent with the PSLRA).

82. *Weinberg*, 216 F.R.D. at 254.

83. 206 F.R.D. at 445–46.

84. *Id.* at 451.

85. *Id.*; *see also In re McKesson HBOC, Inc. Sec. Litig.*, 79 F. Supp. 2d 1146, 1150–151 (N.D. Cal. 1999) (finding niche plaintiffs had not met burden of showing a conflict to rebut the statutory presumption); *cf. In re Cendant Corp. Sec. Litig*., 182 F.R.D. 144 (D.N.J. 1998) (finding conflict on the part of the lead plaintiffs (stock ownership in one of the defendant underwriters) required separate representation for preferred share purchasers); *see also Cable & Wireless*, 217 F.R.D. 372 (appointing both foreign institution and domestic individual movants, concluding that foreign movant could not represent domestic purchasers and domestic movant was not an institution); *cf. Royal Ahold* (appointing domestic institution as sole lead plaintiff rather than foreign institution); *see also Laborers Local 128 Pension Fund v. Campbell Soup Co.*, 2000 U.S. Dist. LEXIS 5481 *11 (D.N.J. 2000) (appointing individual and institutional competing movants as co-lead plaintiffs to promote diversity); *In re Oxford Health Plans, Inc.*, 182 F.R.D. 42, 51 (S.D.N.Y. 1998) (same).

86. 15 U.S.C. § 78u-4(a) (3)(B)(iii)(II) (emphasis added).

87. *Royal Ahold*, 219 F.R.D. at 350–354.

88. The "conduct" test focuses on whether conduct in the United States had a role in the perpetration of a fraud on foreign investors. *Id* at 351.

89. *Id.* at 352.

90. *Id.*

91. *Id.* at 354. The court distinguished *Cable & Wireless* on the ground that in that case, the only qualified domestic purchaser was not an institution, while in *Royal Ahold*, all of the relevant movants were institutions. *Id.*

92. *Id.* at 353.

93. 216 F.R.D. 567 (D.N.J. 2003).

94. *Id.* at 574.

95. *Id.* at 575.

96. *Id.* (citing *Cendant*, 264 F.3d at 243–44).

97. 216 F.R.D. at 576.

98. *In re Motorola Sec. Litig.*, 2003 U.S. Dist LEXIS 12651 (N.D. Ill. July 23, 2003); *Craig v. Sears Roebuck & Co.*, 253 F. Supp. 2d 1046 (N.D. Ill. 2003).

99. *Motorola*, 2003 U.S. Dist LEXIS at *15–16; *Craig*, 253 F. Supp. 2d at 1048.

100. *Craig*, 253 F. Supp. 2d at 1050.

101. According to the court, these factors are :

> (1) What procedures did the plaintiff follow to identify a reasonable number of counsel with the skill and ability necessary to represent the class in the pending matter? (2) What procedures did the plaintiff follow in inviting competent counsel to compete for the right to represent the class? (3) What procedures did the plaintiff follow to negotiate a fee and expense reimbursement arrangement that promotes the best interest of the class? (4) On what basis can the plaintiff reasonably conclude that it has canvassed and actively negotiated with a sufficient number of counsel and obtained the counsel that is likely to obtain the highest net recovery to the class? (5) Did the plaintiff make inquiries into the full set of relationships between proposed lead counsel and the plaintiff and the other members of the class, and did the plaintiff reasonably conclude either that there are no such relationships or that they did not adversely affect the exercise of the plaintiff's or counsel's fiduciary obligations to the class?

253 F. Supp. 2d at 1049 (citing *Third Circuit Task Force Report on Selection of Counsel*, 74 Temple Law Review 689, 765 (2001)).

102. *Motorola*, 2003 U.S. Dist LEXIS at *18–19.

103. *Id.* at 19.

104. *See also Casden v. HPL Tech., Inc.*, 2003 U.S. Dist. LEXIS 19606, *26 (N.D. Cal., Sept. 29, 2003) (analysis of counsel did not support conclusion that "the presumptive lead plaintiff's choice of counsel was so irrational, or so tainted by self-dealing or conflict of interest, as to cast genuine and serious doubt on that plaintiff's willingness or ability to perform the functions of lead plaintiff." (quoting *In re Cavanaugh*, 306 F.3d at 732–33)).

105. 206 F. Supp. 2d at 633–34.

106. *Id.* at 634 (citing *Ezra Charitable Trust v. Rent-Way Inc.*, 136 F. Supp. 2d 435, 441 (W.D. Pa. 2001)) (asset manager should provide evidence that it "acts as attorney-in-fact for its clients and is authorized to bring suit to recover for, among other things, investment losses").

107. 206 F. Supp. 2d at 634. The court contrasted StoneRidge with the Connecticut funds under the sole control of the state Treasurer appointed in *In re Waste Mgmt., Inc.*, 128 F. Supp. 2d 401 (S.D. Tex. 2000) and the group of "affiliated pension funds or mutual funds under common management" appointed in *Sakhrani v. Brightpoint, Inc.*, 78 F. Supp. 2d 845, 846–47 (S.D. Ind. 1999).

108. *Id.* at 635.

109. 2003 U.S. Dist. LEXIS at *26–27.

110. *Id.* at *27.

111. *Id.* at *30–31.

112. *See In re Cavanaugh*, 306 F.3d at 731.

113. 110 F. Supp. 2d 427 (E.D. Va. 2000) (options trader).

114. 96 F. Supp. 2d 780 (N.D. Ill. 2000) (hedge fund).

115. *See Royal Ahold*, 219 F.R.D. at 354 ("where false information and misleading omissions pollute the market, all types of investors are injured"); *In re Oxford Health Plans, Inc. Sec. Litig.*, 199 F.R.D. 119, 123 (S.D.N.Y. 2001) ("a difference in the amount of damages, date, size, or manner of purchase will not render the claim atypical."); *Saddle Rock Partners, Ltd. v. Hiatt*, 2000 U.S. Dist. LEXIS 11931 at *10–11 (S.D.N.Y., Aug. 21, 2000) (rejecting argument that trading strategies, including being a day-trader, rendered candidate atypical); *In re CMS Energy Sec. Litig.*, 312 F. Supp. 2d (E.D. Mich. 2004) (finding length of time shares are held does not affect the typicality of the claim); *cf. Motorola*, 2003 U.S. Dist. LEXIS at *15–16 (contributory negligence not a defense to securities fraud).

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The Elusive Definition of Primary Liability Under Section 10(b) of the Securities and Exchange Act of 1934

By Anthony J. Harwood

I. Introduction: *Central Bank* Rejects Aiding and Abetting Liability

In *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*,[1] the Supreme Court eliminated aiding and abetting liability in private civil litigation under section 10(b) of the Securities and Exchange Act of 1934. In doing so, the Court adhered to its policy of strict statutory construction of the securities laws, under which it refuses to imply liabilities based on broad policy considerations which do not find expression in the language of the statute. As the Court stated:

> We reach the uncontroversial conclusion, accepted even by those courts recognizing a § 10(b) aiding and abetting cause of action, that the text of the 1934 Act does not itself reach those who aid and abet a § 10(b) violation. Unlike those courts, however, we think that conclusion resolves the case. It is inconsistent with settled methodology in § 10(b) cases to extend liability beyond the scope of conduct prohibited by the statutory text.
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> * * *
>
> As in earlier cases considering conduct prohibited by § 10(b), we again conclude that the statute prohibits only the making of a material misstatement (or omission) or the commission of a manipulative act. See *Santa Fe Industries*, 430 U.S., at 473, 97 S.Ct., at 1301 ("language of § 10(b) gives no indication that Congress meant to prohibit any conduct not involving manipulation or deception"); *Ernst & Ernst*, 425 U.S., at 214, 96 S.Ct., at 1391 ("When a statute speaks so specifically in terms of manipulation and deception . . ., we are quite unwilling to extend the scope of the statute"). The proscription does not include giving aid to a person who commits a manipulative or deceptive act. We cannot amend the statute to create liability for acts that are not themselves manipulative or deceptive within the meaning of the statute.[2]

The Court, however, warned against an expansive interpretation of its ruling, stating:

> The absence of § 10(b) aiding and abetting liability does not mean that secondary actors in the securities markets are always free from liability under the securities Acts. Any person or entity, including a lawyer, accountant, or bank, who employs a manipulative device or makes a material misstatement (or omission) on which a purchaser or seller of securities relies may be liable as a primary violator under 10b-5, assuming *all* of the requirements for primary liability under Rule 10b-5 are met.[3]

Congress limited *Central Bank* by restoring aiding and abetting liability in SEC actions only.[4] However, in private securities litigation, the days of aiding and abetting liability are over.

In applying *Central Bank's* prohibition of aiding and abetting liability, the courts have struggled in attempting to define the difference between primary liability and aiding and abetting liability. There are at present three different tests that the courts employ. These different tests are discussed below.

II. The Three Definitions of Primary Liability

A. The Substantial Participation Test

One of the first courts to address the issue of primary liability after *Central Bank* was the Ninth Circuit Court of Appeals in *In re Software Toolworks Inc.*[5] In that case plaintiff sued the issuer of a secondary offering, its accountants (Deloitte) and underwriter for violations of section 10(b). Plaintiff sought to hold Deloitte liable for misrepresentations made in two letters that the issuer filed with the SEC in response to questions that the SEC raised before the offering became effective. The first letter stated that it had been prepared after extensive "review and discussions" with Deloitte and referred the SEC to two Deloitte partners for further information. In addition, plaintiffs presented evidence that Deloitte had

played a significant role in drafting the second letter. The court held this sufficient to establish primary liability under section 10(b).[6]

As the Ninth Circuit explained in a later decision, "substantial participation or intricate involvement in the preparation of fraudulent statements is grounds for primary liability even though that participation might not lead to the actor's actual making of the statements."[7] In *In re ZZZZ Best Securities Litigation*,[8] the court found support for this result in the text of SEC Rule 10b-5, which the SEC adopted pursuant to section 10(b) of the Securities and Exchange Act.[9] Rule 10b-5 makes it illegal:

> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person in connection with the purchase or sale of any security.[10]

As explained in *In re ZZZZ Best*, Rule 10b-5(a) and (c) permit claims against a person who does not make a misrepresentation or omission under 10b-5(b), if that person engages in a scheme, device, practice or course of business in violation of 10b-5(a) or (c).[11] In *ZZZZ Best*, the court found a violation of 10b-5(a) and (c) based on the defendant accounting firm's "direct assistance" in preparing its client's public statements, even though those statements were not attributed to the accounting firm.[12]

The substantial participation test has been followed in a number of other district court decisions in the Ninth Circuit and in a few district court decisions in other circuits.[13] However, as discussed below in point B, it has been rejected in a number of other circuits, and criticized for resurrecting aiding and abetting claims in violation of *Central Bank*.[14] In addition, it has been criticized for providing inadequate guidance to participants in securities offerings because it leaves unresolved the question of how much participation is sufficiently substantial.[15]

B. The Bright Line Test

The Second Circuit, the Tenth Circuit and the Eleventh Circuit Courts of Appeals have adopted what has come to be known as the bright line test.[16] As articulated by the Second Circuit in *Shapiro v. Cantor*:

> 'a defendant must actually make a false or misleading statement in order to be held liable under Section 10(b). Anything short of such conduct is merely aiding and abetting, and no matter how substantial that aid may be, it is not enough to trigger liability under Section 10(b).'[17]

In *Shapiro*, the plaintiff alleged that the accounting firm for the issuer had "participated" in the preparation of the offering memorandum and had provided financial projections containing material misrepresentations and omissions that were attached to the offering memorandum. However, the accounting firm did not issue an opinion or certification. The court affirmed the dismissal of the complaint, holding that these allegations amounted to aiding and abetting in violation of *Central Bank*. The court stated:

> Allegations of "assisting," "participating in," "complicity in" and similar synonyms used throughout the complaint all fall within the prohibitive bar of *Central Bank*. A claim under § 10(b) must allege a defendant has made a material misstatement or omission indicating an intent to deceive or defraud in connection with the purchase or sale of a security.[18]

The court further held that to have primary liability the defendant must have or should have known that its statements would be distributed to investors.[19]

In *Wright v. Ernst & Young LLP,* the Second Circuit elaborated on the bright line rule adopted in *Shapiro*. In *Wright,* plaintiffs alleged that Ernst & Young recklessly approved the issuer's press release which misrepresented the issuer's financial condition. The press release made no mention of Ernst & Young. In affirming the district court's dismissal of the complaint the court held:

> a secondary actor cannot incur primary liability under the Act for a statement not attributed to that actor at the time of its dissemination. Such a holding would circumvent the reliance requirements of the Act, as "reliance only on representations made by others cannot itself form the basis of liability." . . . Thus, the misrepresentation must be attributed to that specific actor at the time of public dissemination, that is, in advance of the investment decision.[20]

The Tenth Circuit's *Anixter* case is an example of a statement attributable to a secondary actor giving rise

to liability under the bright line test. There, the defendant accountant had issued certifications and opinion letters. The Tenth Circuit held that the accountant had primary liability.[21]

These bright line decisions make it clear that there is no primary liability for misrepresentation or omissions unless there is a statement attributed to the defendant. But as discussed above, subdivisions (a) and (c) of Rule 10b-5 create liability for deceptive schemes and business practices that do not involve misrepresentations or omissions. In two cases, the Second Circuit has held that there is primary liability even for persons who do not make misrepresentations or omissions under subdivisions (a) and (c) of Rule 10b-5 if those persons participated in the fraud.

In *SEC v. First Jersey Securities, Inc.*,[22] the CEO of the defendant securities firm, who himself made no statements containing misrepresentations or omissions, was held primarily liable under section 10(b) because he had "'knowledge of the fraud and assisted in its perpetration.'"[23] The court further based its finding of primary liability on the CEO's role as a control person, who planned and orchestrated the fraud by directing others under his employ to make misrepresentations. The Second Circuit in *Wright* distinguished *First Jersey* on this ground, stating:

> We held Brennan [the CEO] liable for securities fraud in his capacity as a "controlling person," that is, for fraud planned and directed by upper level management. . . . Here, we confront alleged fraud by accountants—secondary actors who may no longer be held primarily liable under § 10(b) for mere knowledge and assistance in the fraud.[24]

The Second Circuit again held that there could be primary liability without a misrepresentation attributed to the defendant in *SEC v. U.S. Environmental, Inc.*[25] There, the defendant was a stock trader who, at the direction of a stock promoter, participated in a scheme to manipulate the price of a company's stock by effectuating buy and sell orders. The court held that the trader could be liable, even though he made no misrepresentations or omissions. The court distinguished *Shapiro* and *Central Bank*, stating:

> Romano [the trader], in contrast, did not simply fail to disclose information when there was no duty to do so, as in *Shapiro*, or fail to prevent another party from engaging in a fraudulent act, as in *Central Bank,* when there existed no duty to prevent such. Rather, Romano himself "commi[tted] a manipulative act," . . . by effecting the very buy and sell orders that manipulated USE's stock upward.
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> * * *
>
> Like lawyers, accountants, and banks who engage in fraudulent or deceptive practices at their clients' direction, Romano is a primary violator despite the fact that someone else directed the market manipulation scheme. The Supreme Court in *Central Bank* never intended to restrict § 10(b) liability to supervisors or directors of securities fraud schemes while excluding from liability subordinates who also violated the securities laws.[26]

As *First Jersey* and *U.S. Environmental* demonstrate, there can still be primary liability under the bright line test (at least in the Second Circuit) without a statement by the defendant containing a misrepresentation or omission, but only in limited circumstances where either: (1) the defendant directs and plans the misrepresentations of subordinates; or (2) the defendant engages in some other type of manipulative act.[27] However, as the *Wright* decision seems to indicate, there is no liability in the Second Circuit under subdivisions (a) and (c) of 10b-5 for merely helping to prepare a statement containing misrepresentations or omissions attributed to another actor.[28] This is different from the substantial participation test applied in the Ninth Circuit, under which participation in drafting statements for others that contain misrepresentations or omissions gives rise to primary liability under all three subdivisions of 10b-5.[29] Whether other exceptions to the requirement of a statement attributed to the defendant will be recognized under the bright line test remains to be seen.

The SEC has criticized this bright line test because it provides "'a safe harbor from liability for everyone except those identified with the misrepresentation by name.'"[30] The SEC's concern is that "'[c]reators of misrepresentations could escape liability as long as they concealed their identities.'"[31] Because of this concern, the SEC has proposed a third test for primary liability that was adopted in *Enron Securities Litigation* as discussed in point C below.[32]

C. The SEC's Test as Adopted in *Enron Securities Litigation*

In *In re Enron Securities Litigation.,* the District Court for the Southern District of Texas adopted a third test, which the SEC had proposed for determining primary liability. In doing so, the court took heed of criticisms of both the bright line and substantial participation tests, and gave deference to the SEC as the agency to which

Congress expressly granted rule-making authority under section 10(b). Under the SEC's test, a person who creates a statement containing a misrepresentation or omission, but does not sign the statement and is not otherwise publicly identified as the maker of the statement, can be liable as a primary violator.[33]

> 'when a person, acting alone or with others, creates a misrepresentation [on which the investor-plaintiffs relied], the person can be liable as a primary violator . . . if . . . he acts with the requisite scienter. . . . Moreover it would not be necessary for a person to be the initiator of a misrepresentation in order to be a primary violator. Provided that a plaintiff can plead and prove scienter, a person can be a primary violator if he or she writes misrepresentations for inclusion in a document to be given to investors, even if the idea for those misrepresentations came from someone else.' . . . Furthermore, 'a person who prepares a truthful and complete portion of a document would not be liable as a primary violator for misrepresentations in other portions of the document. Even assuming such a person knew of misrepresentations elsewhere in the document and thus had the requisite scienter, he or she would not have created those misrepresentations.'[34]

The court's application of this test to the law firm defendants is instructive. It held that Enron's counsel was liable as a primary violator because of its role in drafting disclosure documents and legal opinions.[35] The opinion does not make clear whether the legal opinions were distributed to investors with the law firm's knowledge. If they were, then the law firm would probably have been held liable as a primary violator even under the more restrictive bright line test. However, it appears that the disclosure documents were attributed to Enron, not the law firm, despite the law firm's role in drafting them. The court concluded that this was a basis for primary liability.[36] Under the bright line test, this would not give rise to primary liability.

The court, however, held that there was no primary liability for the law firm that represented the Special Purpose Entities ("SPEs") that participated in the allegedly manipulative transactions. Although counsel for the SPE's, like counsel for Enron, allegedly helped structure manipulative transactions and drafted documents for those transactions,[37] the court held that there was no primary liability because none of the disclosures or opinion letters that the firm drafted reached the investors or public generally, and all the allegations were conclusory and general.[38]

The *Enron* court also addressed primary liability for participating in a manipulative or deceptive contrivance, course of business or scheme to defraud under 10b-5(a) and (c).[39] The court held that there can be primary liability under subdivisions (a) and (c) in the absence of a misrepresentation provided that the plaintiff can prove:

> (1) that it was injured (2) in connection with the purchase or sale of securities (3) by relying on a market for securities (4) controlled or artificially affected by defendants' deceptive and manipulative conduct, and (5) the defendants engaged in the manipulative conduct with scienter.[40]

In holding that secondary actors can be liable for primary violations through a scheme to defraud, manipulations or deceptive business practices, the court followed and quoted from the Second Circuit's decision in *SEC v. U.S. Environmental, Inc.* Thus, while the decision in *In re Enron* clearly deviated from the Second Circuit's bright line test as it relates to misrepresentations or omissions, it applied the same standard to schemes to defraud. However, it carried the standard into new terrain, holding that Enron's counsel was liable for participating in a scheme to defraud because it structured manipulative transactions and prepared documents for manipulative transactions.[41] The Second Circuit decisions discussed above, which endorsed primary liability for participation in a scheme to defraud or other deceptive or manipulative business practices, did not impose liability based on the role of attorneys, accountants or bankers in structuring transactions. Whether the Second Circuit or any other courts would find primary liability under 10b-5(a) or (c) under circumstances similar to those before the *Enron* court is an open question.

Conclusion

The circuit courts have adopted two conflicting tests for defining primary liability after *Central Bank*, and the SEC has persuaded two district courts to adopt a third definition. This is an issue that will likely remain unresolved until there is another ruling from the Supreme Court.

Endnotes

1. 511 U.S. 164 (1994).
2. *Id.* at 177–78. Although the Court relied principally upon the language of the statute, it also found support for its holding in the legislative history, the text of other securities provisions that create express liability without providing for aiding and abet-

ting liability, policy considerations and the text of the general criminal aiding and abetting statute.

3. *Id.* at 191.
4. 15 U.S.C. 78t(e).
5. 50 F.3d 615 (9th Cir. 1994).
6. *Id.* at 628–29 & n.3.
7. *Howard v. Everex Systems, Inc*, 228 F.3d 1057 (9th Cir. 2000).
8. *See In re ZZZZ Best Sec. Lit.*, 864 F. Supp. 960 (C.D. Cal. 1994) (decided prior to *In re Software Toolworks)*.
9. Section 10(b) makes it unlawful for any person "directly or indirectly:"

> To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

15 U.S.C. § 78j(b).

10. 17 C.F.R. § 240.10b-5.
11. 864 F. Supp. at 971.
12. *Id.*
13. *See, e.g., In re Lernout & Hauspie Sec. Lit.*, 230 F. Supp. 2d 152 (D. Mass. 2002); *McNamara v. Bre-X Minerals Ltd.*, 57 F. Supp. 2d 396, 426 (E.D. Tex. 1999); *Flecker v. Hollywood Entertainment Corp*., 1997 U.S. Dist. LEXIS 5329 (D. Or. 1997); *O'Neil v. Appel*, 897 F. Supp. 995 (W.D. Mich. 1995); *Adam v. Silicon Valley Bancshares,* 884 F. Supp. 1398 (N.D. Cal. 1995); *Cashman v. Coopers & Lybrand,* 877 F. Supp. 425, 432–34 (N.D. Ill. 1995). In *Klein v. Boyd,* a panel of the Third Circuit adopted the substantial participation test, but that decision was vacated for a rehearing *en banc.* Fed. Sec. L. Rptr. (CCH) ¶ 90,136 (3d Cir. Feb. 12, 1998), *rehearing en banc granted, judgment vacated*, Fed. Sec. L. Rptr. (CCH) ¶ (3d Cir., Mar. 9, 1998). The parties subsequently settled the litigation prior to the *en banc* hearing.
14. *See, e.g., Ziemba v. Cascade Int'l, Inc.*, 256 F.3d 1194, 1205 (11th Cir. 2001); *Anixter v. Home-Stake Prod. Co.*, 77 F.3d 1215, 1226 n.10 (10th Cir. 1996); *In re MTC Elec. Tech. S'holders Lit*., 898 F. Supp. 974, 987 (E.D.N.Y. 1995).
15. *See Anixter v. Home-Stake Prod. Co.*, 77 F.3d 1215, 1226–27 (10th Cir. 1996).
16. *Ziemba v. Cascade Int'l, Inc*., 256 F.3d 1194 (11th Cir. 2001); *Wright v. Ernst & Young LLP,* 152 F.3d 169 (2d Cir. 1998); *Shapiro v. Cantor,* 123 F.3d 717 (2d Cir. 1997); *Anixter v. Home Stake Prod. Co.*, 77 F.3d 1215 (10th Cir. 1996). District courts in other circuits have also adopted the bright line test. *In re Kendall Square Research Corp. Sec. Lit.*, 868 F. Supp. 26, 28 (D. Mass. 1994); *Vosgerichian v. Commodore Intern.*, 862 F. Supp. 1371, 1378 (E.D. Pa. 1994).
17. 123 F.3d at 720 (quoting *In re MTC Elect. Tech. S'holders Litig.*, 898 F. Supp at 987).
18. *Id.* at 720–21.
19. *Id. a*t 720.
20. 152 F.3d at 175 (quoting *Anixter,* 77 F.3d at 1225) (citation omitted).
21. 77 F.3d at 1226–27.
22. 101 F.3d 1450 (2d Cir. 1996).
23. 101 F.3d at 1472 (quoting *Azrielli v. Cohen Law Offices*, 21 F.3d 512, 517 (2d Cir. 1994)).
24. *Wright*, 152 F.3d at 176 (citation omitted).
25. 155 F.3d 107 (2d Cir. 1998).
26. 155 F.3d at 112.
27. S*ee also Rich v. Maidstone Fin., Inc.*, 2002 WL 31867724 at *7–9 & n.6 (S.D.N.Y., Dec. 20, 2002). Although both *First Jersey* and *U.S. Environmental* were actions that the SEC brought, the alleged violations occurred before Congress had reinstituted aiding and abetting liability in SEC proceedings. Therefore, in both decisions, the court assumed without deciding that the SEC had to prove primary liability.
28. *See Wright*, 152 F.3d at 176.
29. *See supra* notes 8–12 and accompanying text.
30. *In re Enron Corp. Sec. Lit.*, 235 F. Supp. 2d 549, 586–87 (S.D. Tex. 2002) (quoting the SEC's *amicus curiae* brief).
31. *Id.*
32. *Id.* at 588.
33. 235 F. Supp. 2d at 586–87. The SEC had made the same argument in *Carley Capital v. Deloitte & Touche, LLP,* 27 F. Supp. 2d 1324 (N.D. Ga. 1998) and the court adopted it. However, in light of the Eleventh Circuit's later adoption of the bright line test in *Ziemba* (*supra* note 16), the SEC's test no longer governs in the Eleventh Circuit. The SEC also urged the adoption of its "creates a misrepresentation" test in its brief to the Third Circuit in the *en banc* hearing in *Klein v. Boyd,* but as discussed above (*supra* note 13), that case settled before the *en banc* hearing. *See In re Enron*, 235 F. Supp. 2d at 586 n.24.
34. *Id.* at 588–90 (quoting the SEC's *amicus* brief) (citations omitted).
35. *Id.* at 705.
36. *Id.*
37. *Id.* at 669–673.
38. *Id.* at 706.
39. *Id.* at 577–81.
40. *Id.* at 580.
41. *Id.* at 704–05.

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SLUSA Preemption and the PSLRA Discovery Stay: The Evolving Application of Federal Preemptive Concepts to Securities Class Action Claims

By Douglas C. Conroy

Inter-circuit and intra-circuit conflicts over the interpretation of fundamental liability concepts have pervaded federal securities litigation for at least the last twenty-five years. Developments since the passage of the Private Securities Litigation Reform Act ("PSLRA") in 1995 and the Securities Litigation Uniform Standards Act ("SLUSA") in 1998 prove that legislative initiatives simply provide additional opportunities for such conflicts. Congress, through passage of the PSLRA, sought to impose discovery limitations on securities plaintiffs which, in conjunction with stricter pleading standards, would lead to a higher incidence of early dismissals. In reaction to a perceived increase in state court filings in reaction to the PSLRA, Congress sought, through passage of SLUSA, to create preemption and removal mechanisms with respect to state law securities class action claims, and other state court filings, to assure that the perceived purpose of these discovery limitations was achieved and the predominance of other federal concepts in "covered class actions" was fully realized.

While practitioners readily acknowledge the dichotomies which the PSLRA created in the various circuits' approaches to the issue of what constitutes adequate pleading of scienter, similar variances exist with respect to many of the more procedural aspects of these "reforms" envisioned by the architects of the SLUSA and PSLRA. This discussion will highlight just two of the areas in which conflicts have arisen and have not been definitively resolved concerning the meaning and extent of these reforms: first, the extent and operation of SLUSA's removal and preemption provisions, and second, the continuing battles over discovery "fishing expeditions" which the PSLRA hoped to prevent.

I. The Evolving Impact of SLUSA

SLUSA was enacted in 1998 primarily in response to a marked increase in state court class action securities fraud filings following on the heels of the passage of the PSLRA.[1] One effect of these state filings was frequently to allow plaintiffs' counsel early discovery for later or parallel federal claims, and to avoid the impact of both Rule 9(b) of the Federal Rules of Civil Procedure and the heightened standards on pleading "scienter" which Congress had sought to implement by passage of the PSLRA. Additionally, plaintiffs' counsel had launched renewed efforts in state courts to seek recognition of the "fraud-on-the- market" presumption for purposes of state law class action claims.[2]

SLUSA operates through removal and preemption mechanisms, the thrust of which are to bring many, if not most, securities class actions under federal court supervision, control and standards.[3] SLUSA provides:

> No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging
>
> (A) a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security; or
>
> (B) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a security.[4]

As stated in *Behlen v. Merrill Lynch:*[5]

> Congress passed the SLUSA which . . . made federal court, with limited exceptions, the sole venue for class actions alleging fraud in the purchase and sale of covered securities. Congress further mandated that such class actions would be governed by federal law rather than state law. To that end, the SLUSA preempts certain state law claims, allows for removal of state actions to federal court, *and required immediate dismissal* of "covered lawsuits." (emphasis added).[6]

From a defendant's standpoint, the plaintiffs are subjected to both the PSLRA's stay of discovery and to the higher Rule 9(b) and PSLRA pleading standards employed in the federal courts. In addition, state law theories of recovery which may give rise to punitive damage claims, such as claims for breach of fiduciary duty, vanish based on SLUSA's preemptive mechanisms.

In practice, the dismissal is subject to the ability of plaintiffs, following removal, to state sufficiently detailed facts to constitute a federal securities fraud claim involving the purchase or sale of a "covered" security.

By its terms, SLUSA does not apply to cases pending in state courts before its effective date. It has been held to apply to pre-enactment conduct alleged in post-SLUSA filings.[7] However, the fact that there is conflicting case law on this issue within a single district amply illustrates the evolving and sometimes conflicting nature of SLUSA interpretation.[8]

There are exceptions that can arise because of the explicit requirement of 15 U.S.C. § 78bb(f)(i) that the misconduct be "in connection with the purchase or sale of a security." One recent California decision lays out one type of claim that may avoid SLUSA removal. The California Supreme Court, in *Small v. Fritz Companies, Inc.*,[9] held that common law fraud claims for securities fraud could be based on declines in value of stock that plaintiffs allege they continued to hold after purchase based on subsequent misrepresentations or failures to disclose. The court refused to adopt the rationale of *Blue Chip Stamps v. Manor Drug Stores*,[10] which requires purchases or sales in reliance for purposes of a Rule 10b-5 claim, as a prerequisite for a California common law securities fraud claim. However, the court also held that plaintiffs seeking such a recovery must allege actual reliance on misstatements or omissions with specificity, making class actions more difficult.[11] Institutional plaintiffs such as pension funds with large holdings of a California-based issuer would appear to be ideally situated to take advantage of the opening offered by this holding to bring actions in state court and argue against removal.[12]

Although the primary effect of SLUSA's preemption mechanism is to preempt state statutory and common law securities fraud claims that fall within its definitional scheme, it does so only with respect to certain "covered class actions" as defined in SLUSA.[13] The "covered class actions" involve both securities traded on national exchanges and NASDAQ[14] and other types of securities issued by listed companies, including debt securities which do not qualify for a registration exemption.[15] SLUSA also encompasses securities issued by registered investment companies even though not traded on a national exchange.[16] SLUSA apparently does not cover securities traded through such mechanisms as the "pink sheets," and there are other exceptions, including contractual actions between indenture trustees and issuers, individual actions, derivative actions, and the so-called Delaware "carve out."[17]

Under 15 U.S.C. § 78bb(f)(5)(B) "class actions" need not be denominated as such as long as they involve claims by or on behalf of 50 or more persons.[18] Under 15 U.S.C. § 78bb(f)(5)(D), partnerships, pension funds and other entities are generally treated as one person. Furthermore, 15 U.S.C. § 78bb(f)(5)(B) provides that state and municipal pension plans are exempt from SLUSA if they bring claims on behalf of similar plans *with those plans' authorizations*. These exceptions allow another opportunity for large sophisticated investors to take advantage of both state statutory and common law claims.

One of the evolving procedural questions posed by the SLUSA removal process is the extent to which traditional removal concepts apply in the SLUSA context. Is SLUSA an attempt by Congress to completely preempt certain types of state claims or, alternatively, should federal courts give deference to plaintiffs' pleadings under the "master of the complaint" doctrine recognized in *Caterpillar Inc. v. Williams*?[19] On the other side of the equation, plaintiffs are generally not allowed to avoid complete federal preemption through creative surgical pleading, and the courts have held that, in such instances, the courts may—and should—look beyond the pleadings.[20] This level of analysis is often critical since removing defendants have in effect only "one bite at the apple" to justify removal. It is settled that these types of remand orders are not reviewable by the appellate courts.[21]

Some decisions have found SLUSA preemption unavailable for state court claims for violations of only the 1933 Act, finding SLUSA did not preempt the concurrent jurisdiction for such claims provided by the original 1933 Act, as reflected in 15 U.S.C. § 77v(a). Here again, there are direct conflicts in the case law.[22] If one views SLUSA as a follow-on to the Reform Act and a reaction to the post-Reform Act migration to state courts by the plaintiffs' bar, which seldom filed 1933 Act claims in state courts prior to 1998, SLUSA removal of such claims seems to be the proper outcome and is consistent with the legislative intent.[23] The language of 15 U.S.C. § 78bb(f)(1)(A), which refers generally to "a misrepresentation or omission of a material fact," is also susceptible to a construction covering 1933 Act claims under sections 11 and 12(a)(2) of the Act.[24]

Plaintiffs have also used other stratagems to avoid preemption. Certain decisions have dealt with the issue of whether a removed case should be remanded because it did not seek damages. Courts seem to have seen through this stratagem and found removal proper, finding in effect that the failure to demand damages was an effort to use the state court action for discovery with the intent of amending later.[25] There is also an ongoing dispute as to which categories of defendants can take advantage of SLUSA's preemptive scheme, i.e., whether it applies to defendants other than issuers or their affiliates.[26] A significant number of cases hold that securities brokers can invoke SLUSA.[27]

What SLUSA has assured is the predominance of federal concepts in the vast majority of class actions against issuers, officers and directors, underwriters, other investment professionals, and auditors charging material misrepresentations or omissions in purchases or sales of securities. However, that has not lessened the initial extensive motion practice over whether the action is a "covered class action" for purposes of SLUSA. For purposes of making that determination, courts commonly look to the patchwork of conflicting case law defining the essentials of a Rule 10b-5 violation with all the potential problems inherent in reconciling those cases. A great deal of the SLUSA decisional law deals with these recurring issues.

II. Issues Commonly Litigated in SLUSA Removal Proceedings

A. The "In Connection With" Requirement

SLUSA removal regularly generates a variety of controversies concerning whether an action raises claims of misrepresentations or omissions "in connection with" the purchase or sale of a security. Satisfaction of the "in connection with" requirement is obviously critical for both a finding of federal jurisdiction under section 10(b) of the Exchange Act and SLUSA removal. Given the explicit language of 15 U.S.C. § 78bb(f)(i), many SLUSA opinions deal with the ongoing interpretation of leading Supreme Court decisions on Rule 10b-5 liability. Among these decisions are *Blue Chip Stamps v. Manor Drug Stores*,[28] dealing with the requirement that there be a purchase or sale in reliance and *Santa Fe Industries v. Green*,[29] which holds that mere claims of mismanagement or fiduciary breaches, without more, are insufficient to state 10b-5 claims. In 1971, the Supreme Court also admonished, in *Superintendent of Ins. v. Bankers Life & Cas. Co.*, that section 10(b) of the 1934 Act be read "flexibly, not technically and restrictively," and that the scope of the "in connection with" qualifier required that the plaintiff only need to have "suffered an injury as a result of deceptive practices touching its sale of securities. . ."[30] While these decisions provide general guidelines, the decisions of lower courts, both as to the "in connection with a purchase or sale" requirements and what constitutes a "fiduciary" claim, have left a great deal of room for disagreement.

In the intervening 25 to 30 years, a large body of jurisprudence has evolved around these cases, most particularly around the "in connection with" requirement. The Second Circuit recently summarized numerous cases from a variety of circuits interpreting *Bankers Life* as standing for the inherently vague proposition that the misrepresentations must at a minimum "affect or 'touch' the actual purchase made by plaintiffs."[31] Certainly, the Supreme Court's most recent pronouncement in *S.E.C. v. Zandford*,[32] albeit in the broker-customer context as will be discussed, appears to bring into serious question many of the earlier decisions discussed below which had found the "in connection with" requirement not satisfied. As a result, *Zandford* in particular may enable more frequent successful invocation of SLUSA removal and preemption. The ironic corollary is that plaintiffs' counsel will seek to narrow the application of *Zandford*.

Successful invocation of *Zandford* by defendants will prevent application of state securities laws, with sometimes lower thresholds of proof, to class actions. In addition, potentially more dangerous state law punitive damage claims are eliminated. What is critical to keep in mind is that a great deal of earlier case law, while not explicitly overruled by *Zandford*, is now problematic.

1. The Traditional "In Connection With" Interpretation

For purposes of Rule 10b-5, a misrepresentation or omission must be made "in connection with" the purchase or sale of the security. The definition of a "security" for purposes of removal analysis is far-reaching and generally beyond the scope of this article. A statement made after a purchase is, by definition, not "in connection with" that purchase. For that reason, a 10b-5 claimant cannot recover based upon a later misstatement.[33] Many cases held that there needed to be a "transactional nexus" between the purchase or sale in question and the allegedly misleading statement, while other cases used narrower language holding that the misrepresentation involved in the alleged fraud "must relate to the securities alleged to satisfy the purchase or sale requirement, and not just to the transaction in its entirety."[34] The rationale for requiring a misrepresentation as to the "value" of the shares was stated as follows:

> The purpose of § 10(b) and Rule 10b-5 is to protect persons who are deceived in securities transactions—to make sure that buyers of securities get what they think they are getting and that sellers of securities are not tricked into parting with something for a price known to the buyer to be inadequate or for a consideration known to the buyer not to be what it purports to be.[35]

Similarly, courts regularly held that the misrepresentation or omission must in some way relate to the value of the securities in question or the interest in the corporation the securities represent. The "misrepresentations must pertain to the value of securities purchased or sold."[36] Other cases framed the requirement in terms of the misrepresentation relating to the consideration received.[37]

The decision in *Manufacturers Hanover Trust v. Smith Barney*[38] was also instructive on the then-prevailing reasoning on this issue, summarizing and relying upon Second Circuit jurisprudence that narrowly construed the "in connection with" requirement. The court dismissed a Rule 10b-5 claim against a broker, Smith Barney, which allegedly assisted in perpetrating a fraudulent conversion of securities. The convertor was an employee of Manufacturers Hanover Trust, the transfer agent, which cancelled shares on the books and issued new certificates in the names of two confederates, who then sold the shares through accounts at Smith Barney. The plaintiffs argued that the "alleged scheme could not have been carried out without the transfers of the embezzled stock to [his confederates] as owners of record and the sale of the embezzled stock on the NYSE through the brokerage accounts." The court rejected this theory and dismissed the action against Smith Barney, holding that a plaintiff must plead "something more than a 'de minimis' relationship between the fraudulent scheme and the purchase or sale of securities."[39] The viability of these more traditional cases is questionable given the Supreme Court's holding in *Zandford*.

The Third Circuit espoused a broader, and arguably contrary, view which encompassed not only issues of value but also the "trading process "—which seems more consistent with the later *Zandford* approach.[40] The Seventh and Fourth Circuits adopted an "investment value" approach.[41] One lower court in the Fourth Circuit suggested several different possible approaches, construing the "in connection with" requirement as requiring "misrepresentations made in connection with the value of securities *or a course of dealings in securities*. . ."[42]

2. The "In Connection With" Requirement Under *Zandford*

The Supreme Court's recent decision in *S.E.C. v. Zandford*[43] has given a broader construction to the "in connection with" requirement in the broker-dealer/customer context, which seems to bring into question much of the earlier case law. *Zandford* involved a broker who was alleged to have breached his fiduciary duty and violated Section 10(b) by engaging in a fraudulent scheme in which he sold a client's securities for his own benefit. The broker argued the sales were lawful and that subsequent misappropriation of the proceeds, though fraudulent, did not have the requisite "connection." The Supreme Court, reversing, disagreed, holding that when a breach of fiduciary duty coincides with a sale of securities, the "in connection with" requirement is satisfied.[44] Courts have not limited *Zandford's* application to the broker-dealer context and have already picked up on this liberal interpretation of the "in connection with" requirement to deny remand following SLUSA removal.[45]

3. Allegations that Arguably Still Do Not Satisfy the "In Connection With" Requirement

The case law has also long recognized that simple allegations of mismanagement are not actionable under section 10(b) and Rule 10b-5 under the so-called *Santa Fe Industries* rationale.[46] Allegations of mismanagement, incompetence or "disarray" are usually treated similarly.[47] Nor may fiduciary duty claims be "bootstrapped" into 10b-5 claims by alleging merely a failure by directors to disclose such a breach.[48] Similar rationales have also been extended to claims under sections 11 and 12(a)(2) of the 1933 Act.[49]

Mere subsequent breaches of contract following the purchase or sale also usually do not satisfy the "in connection with" requirement absent a showing that a defendant entered into the agreement with no intention of honoring the promises made. *Zandford* has not undercut this analysis.[50]

Other cases have found the requirement for SLUSA preemption not satisfied because the allegations dealt only with holding securities—as opposed to purchases or sales—therefore not satisfying *Blue Chip Stamps*, or because the alleged misrepresentations followed a purchase.[51] Some cases find that the allegations sound in breach of fiduciary duty.[52]

4. The Impact of "In Connection With" Jurisprudence on SLUSA Removal

Numerous SLUSA decisions analyze removal from the perspective of whether a securities fraud claim is necessarily stated, finding, for a variety of miscellaneous reasons, that it is not.[53] Cases can also sometimes be the subject of more than one removal petition, depending on the evolution of the pleadings.[54] As a result, numerous extremely close and, arguably, contrary distinctions continue to be made by the district courts given the non-reviewability of remand orders, providing a ready stock of case law ammunition for most removal/remand disputes.[55]

Finally, even remand may not provide plaintiffs with a safe harbor and can on occasion provide the "second bite at the apple" not provided by appellate review of remand decisions. Recently, a state trial court, following receipt of a file based on a successful remand motion, found itself not bound to follow the earlier unappealable federal court order remanding the case.[56] It dismissed the remanded complaint based on its reading of SLUSA's provisions.[57]

III. The Impact of The PSLRA's Automatic Stay of Discovery on Threshold Motion Practice

A statutory development which permeates federal securities fraud litigation post-1995 is the creation by Congress, in the PSLRA, of a statutory stay of discovery during the pendency of motions to dismiss. 15 U.S.C. § 78u-4(b)(3)(B) provides:

> In any private action arising under this chapter, *all discovery* and other proceedings *shall be stayed* during the pendency of any motion to dismiss, *unless the court finds* upon the motion of any party that particularized discovery is necessary to preserve evidence or to prevent *undue prejudice* to that party. (emphasis added)

As noted, exceptions are provided where the court finds it necessary to prevent "undue prejudice" or to preserve evidence.

Congress also anticipated that the plaintiffs' bar might seek discovery in related state court actions. Section 15 U.S.C. § 78u-4(b)(3)(D) provides:

> Upon a proper showing, a court may stay discovery proceedings in any private action in a State court, as necessary in aid of its jurisdiction, or to protect or effectuate its judgments, in an action subject to a stay of discovery pursuant to this paragraph.

House Report 105-640 set forth the rationale behind this provision, stating, in pertinent part:

> [Section 78u-4(b)(3)(D)] amends Section 27(b) of the Securities Act of 1933 to include a provision to prevent plaintiffs from circumventing the stay of discovery under the Reform Act by using State court discovery proceedings in any private action in a State court as necessary in aid of its jurisdiction, to protect or effectuate its judgments. . . . Because circumvention of the stay of discovery of the Reform Act is a key abuse that this litigation is designed to prevent, the Committee intends that the courts use this provision liberally, so that the preservation of the State court jurisdiction of limited individual securities fraud claims does not become a loophole through which the trial bar can engage in discovery not subject to the stay of the Reform Act.

A stated purpose of this language was to eliminate cases in which plaintiffs engaged in "fishing expeditions," and imposed associated, and often astronomical, discovery costs on defendants. As recently stated by one court,[58] while allowing limited document production based on the "unique circumstances" before it:

> The legislative history of the PSLRA indicates that Congress enacted the discovery stay in order to minimize the incentives for plaintiffs to file frivolous securities class actions in the hope either that corporate defendants will settle those actions rather than bear the high cost of discovery, *see* H.R. Conf. Rep. No. 104-369, at 37 (1995), *reprinted in* 1995 U.S.C.C.A.N. 730, 735, or that the plaintiff will find during discovery some sustainable claim not alleged in the complaint, *see* S.Rep. No. 104-98, at 14 (1995), *reprinted in* 1995 U.S.C.C.A.N. 679, 693. *See also In re Lernout & Hauspie Sec. Litig.*, 214 F. Supp. 2d 100, 106 (D. Mass. 2002).

Many experienced practitioners will readily admit that the second problem was acute, particularly in accounting cases, with pre-PSLRA amended complaints often bearing only faint resemblance to the initial filings after plaintiffs' counsel combed through documents and often came up with different or additional violations.

This stay, unlike SLUSA preemption, has been held not to be limited to just class action claims. Here, again, there is disagreement among the courts. There are cases holding the stay applicable to individual securities claims, which is consistent with the language used in the PSLRA amendments.[59] However, there are cases limiting the stay to class actions or questioning its applicability to individual securities actions.[60]

From its inception, most courts have given the discovery stay a liberal reading.[61] However, some courts have distinguished between the status of various parties defendant in deciding on application of the stay, looking at which parties have triggered the stay by filing or intending to file, motions to dismiss, and whose motions remain undecided.[62] Courts have also, by and large, rejected efforts to find ways around the stay. This includes extending the stay to related state court proceedings and pendent state claims.[63] In at least one instance, the stay has been extended to related ERISA litigation.[64] However, exceptions have been made, particularly in more notorious situations, to require the production of documents previously provided to government agencies.[65]

There are many cases refusing to allow relief under the "undue prejudice" standard.[66] There are also cases applying the stay to evidence in the hands of a third party.[67] Nevertheless, as with other provisions of the PSLRA, conflicts have arisen and certain exceptions have been made, either by way of invoking the "undue prejudice" provision or a more narrow reading of the statute.[68] Even in cases where some relief from the automatic stay is allowed, the relief granted can be limited in scope and plaintiffs' counsel may encounter later problems with assertions that their discovery exceeded the bounds contemplated. In one recent case,[69] the court initially allowed discovery of third-party individuals where a confidentiality agreement executed in connection with merger negotiations had inhibited access. However, in an opinion a year later, dismissing all of the plaintiffs' amended claims, the court found their counsel had violated the narrow earlier order allowing discovery to add additional theories of recovery, which were, in any event, also found deficient as a matter of law.[70]

Other decisions may turn on the nature of related state claims, although this issue only comes up with individual securities actions not subject to SLUSA federal law preemption and, therefore, susceptible to additional state law claims.[71] One court discussed this issue in a non-class action context where both diversity jurisdiction and the federal securities laws were invoked as a basis for jurisdiction. The common law claims included fraud, breach of contract and other claims. The court found that discovery should go forward on the state claims under those circumstances, noting and disagreeing with a contrary opinion.[72]

While these exceptions have been carved out, and courts have disagreed on various constructions or applications of the PSLRA discovery stay provisions, the stay remains in effect in most cases. The practical effects of this stay, combined with the Reform Act provisions relating to scienter, have been multifaceted. The "race to the courthouse" mentality which characterized pre-PSLRA practice by plaintiffs' counsel has abated, and plaintiffs generally do more spadework in preparing their complaints to withstand the almost inevitable motion to dismiss. Complaints are longer and purport to be highly detailed, sometimes to the point where they raise issues of compliance with Rule 8 of the Federal Rules of Civil Procedure. As a corollary, motion practice at the pleading stage has become more important, and decisions voluminous and detailed, as judges see themselves occupying more of a legislatively-mandated gatekeeper function.

Endnotes

1. The history of SLUSA and purpose behind its enactment are described at some length in *Gutierrez v. Deloitte & Touche, L.L.P.*, 147 F. Supp. 2d 584, 589–90 (W.D. Tex. 2001). For an illustration of the types of challenges that faced defense counsel and their clients, pre-SLUSA and post-PSLRA, by reason of state court filings, often parallel to federal filings, see *Smith v. Lenches*, 263 F.3d 972 (9th Cir. 2001).
2. *See, e.g., Kaufman v. i-Stat Corp.*, 165 N.J. 94, 754 A.2d 1188 (2000) (rejecting application to New Jersey common law claims).
3. *Compare IDS Bond Fund, Inc. v. Gleacher Natwest, Inc.*, 2002 WL 373455, at *4–7 (D. Minn., Mar. 6, 2002); *Zuri-Invest AG v. Natwest Fin. Inc.*, 177 F. Supp. 2d 189 (S.D.N.Y. 2001) (both rejecting a comparable preemption argument based on the National Securities Markets Improvement Act of 1996 ("NSMIA")).
4. 15 U.S.C. § 78bb(f)(1).
5. 311 F.3d 1087, 1091–92 (11th Cir. 2002).
6. 311 F. 3d at 1091; *accord Paternaude v. The Equitable Life Assurance*, 290 F.3d 1020, 1023 (9th Cir. 2002). Several courts have held that the level of misconduct alleged for the state law claim to be removable need not rise to the level of fraud required for alleging a Rule 10b-5 claim, but may encompass negligence similar to that required for claims under sections 11 and 12(a)(2) of the 1933 Securities Act. *Kingdom 5-KR-41, LTD. v. Star Cruises PLC*, 2004 WL 444554, at *3 (S.D.N.Y., Mar. 10, 2004); *In Re WorldCom, Inc. ERISA Litig.*, 263 F. Supp. 2d 745, 768–772 (S.D.N.Y. 2003). A separate issue arises when attempts are made to remove state cases asserting only violations of the 1933 Act, as discussed *infra*.
7. *See Blaz v. Belfner*, 2004 U.S. App. LEXIS 7989 (5th Cir., Apr. 22, 2004); *Professional Mgmt. Associates, Inc. v. KPMG, LLP*, 335 F.3d 800 (8th Cir. 2003); *Winne v. Equitable Life Assur. Society*, 2003 WL 22434215, at *9 (S.D.N.Y. Oct. 27, 2003); *Gray v. Seaboard Sec., Inc.*, 241 F. Supp. 2d 213, 217–18 (N.D.N.Y. 2003) (discussing and applying majority view).
8. *See W. R. Huff Asset Mgmt. Co., LLC v. Kohlberg Kravis Roberts & Co., L.P.*, 234 F. Supp. 2d 1218, 1222–27 (N.D. Ala. 2002) (citing Judge Harmon's unreported decision in *In re Enron Corp. Sec., Derivative & "ERISA" Litig.*, MDL-1146, No. H-02-1150 (S.D. Tex., Aug. 16, 2002) and rejecting a contrary ruling in *W.R. Huff Asset Mgmt. Co. v. BT Sec. Corp.*, 190 F. Supp. 2d 1273, 1280–81 (N.D. Ala. 2001)).
9. 30 Cal. 4th 167, 184–85 (2003). *See* C. Evans Stewart, *Suitability Claims For Investors Who Hold: The California Bloom Is Off The Rose*, 35 BNA Sec. Reg. & Law Report No. 29, at 1211 (July 21, 2003) (discussing *Small* at length).
10. 421 U.S. 723 (1975).
11. This holding was consistent with its earlier holding in *Mirkin v. Wasserman*, 5 Cal. 4th 1082, 1090–98 (1993), refusing to adopt the "fraud-on-the-market" theory for common law claims.
12. *See Gordon v. Variable Ins. Products*, 2003 WL 23318666, at *2 (S.D. Fla., Dec. 4, 2003) (noting class alleged in complaint to exclude purchasers or sellers); *Dacey v. Morgan Stanley Dean Witter & Co.*, 263 F. Supp. 2d 706 (S.D.N.Y. 2003) (remanding "holder" claims but retaining "purchaser" claims). However, even "holder" cases can be removed on alternative grounds such as diversity. *See Rogers v. Cisco Systems, Inc.*, 268 F. Supp. 2d 1305 (N.D. Fla. 2003).
13. Constitutional attacks on SLUSA have been rejected. *See Riley v. Merrill Lynch, Pierce, Fenner & Smith*, 292 F.3d 1334, 1346–47 (11th Cir. 2002).

14. *See BT Sec. Co. v. W. R. Huff Asset Mgmt. Co., L.L.C.*, 2004 WL 818852 (Alabama Supreme Court, Apr. 16, 2004) (subsequent delisting from NASDAQ not of consequence since majority of wrongful conduct occurred earlier).

15. *See Zoren v. Genesis Energy, L.P.*, 195 F. Supp. 2d 598, 602-606 (D. Del. 2002); 15 U.S.C. § 78bb(f)(5)(E).

16. *See Kenneth Rothschild Trust v. Morgan Stanley*, 199 F. Supp. 2d 993, 1000 (C.D. Cal. 2002).

17. *See Greaves v. McAuley*, 264 F. Supp. 2d 1078 (N.D. Ga. 2003) (Delaware "carve out" requiring remand of all claims made, even though claims against one defendant not subject to "carve out"); *Alessi v. Beracha*, 244 F. Supp. 2d 354 (D. Del. 2003); (construing 15 U.S.C. § 77bb(f)(3)(I)) (Delaware "carve out"); *Arlia v. Blankenship*, 234 F. Supp. 2d 606 (S.D. W.Va. 2002) (derivative action); *Gibson v. PS Group Holdings, Inc.*, 2000 WL 777818, at *4–6 (S.D. Cal., June 14, 2000)(same); 15 U.S.C. § 78bb(f)(3)(A); 15 U.S.C. § 78bb(f)(5)(C).

18. *See Spehar v. Fuchs*, 2003 U.S. Dist. LEXIS 10406, at *16–30 (S.D.N.Y., June 17, 2003) (remanding common law fraud claims because number of named plaintiffs reduced to less than 50 following removal).

19. 482 U.S. 386, 393–95 (1987).

20. *See Spielman v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 332 F.3d 116, 123 n.5 (2d Cir. 2003); *Parino v. FHP, Inc.*, 146 F.3d 699, 704 (9th Cir.), *cert. denied*, 525 U.S. 1001 (1998) ("Because complete preemption often applies to complaints drawn to evade federal jurisdiction, a federal court may look beyond the face of the complaint to determine whether the claims alleged as state law causes of action in fact are necessarily federal claims."); *Galvez v. Kuhn*, 933 F.2d 773, 780 (9th Cir. 1991). *Compare Lippitt v. Raymond James Fin. Serv., Inc.*, 340 F.3d 1033 (9th Cir. 2003) (holding removal of claimed violations of California Unfair Competition Law based on marketing of "callable certificate of deposit" not warranted); *Jain v. Clarendon America Co.*, 304 F. Supp. 2d 1263 (W.D. Wash. 2004).

21. *See United Investors Life Ins. v. Waddell & Reed*, 360 F.3d 960, 964–67 (9th Cir. 2004); *Spielman v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 332 F.3d 116 (2d Cir. 2003); *Abada v. Charles Schwab & Co., Inc.*, 300 F.3d 1112 (9th Cir. 2002). *See also Beightol v. UBS Painewebber, Inc.*, 334 F.3d 187 (2d Cir. 2004) (finding unappealable an order allowing removal of securities fraud claims involving Global Crossing under the Bankruptcy Code's removal provisions).

22. The Second Circuit has recently ruled that the 1933 Act claims, standing alone, would not have been removable under SLUSA absent the ability to invoke the removal provisions of the bankruptcy laws, 28 U.S.C. § 1452(a). *California Public Employees' Retirement Sys. v. WorldCom, Inc.*, 2004 WL 1048203, at *6–9 (2d Cir., May 11, 2004). *See also Nauheim v. The Interpublic Group of Companies*, 2003 WL 1888843 (N. D. Ill., Apr. 15, 2003) (citing 15 U.S.C. §§ 77a, 77p(b) and 77p(c)); *In re Waste Mgmt. Sec. Litig.*, 194 F. Supp. 2d 590 (S.D. Tex. 2002) (a decision by Judge Harmon noting that only 1933 Act claims were pled in the state court action). There are at least two decisions reaching a contrary result. *Alkow v. TXU Corp.*, 2003 WL 21056750, at *1–2 (N.D. Tex., May 8, 2003); *Brody v. Homestore, Inc.*, 240 F. Supp. 2d 1122 (C.D. Cal. 2003).

23. *See* Andrew J. Morris & Fatima A. Goss, *Why Claims Under The Securities Act of 1933 Are Removable To Federal Court*, 36 BNA Sec. Reg. & Law Report No. 14, at 626 (Apr. 5, 2004).

24. *See also Patenaude v. The Equitable Life Assurance*, 290 F.3d 1020, 1025 (9th Cir. 2002); *Lander v. Hartford Life & Annuity Ins. Co.*, 251 F.3d 101, 108 (2d Cir. 2001); *Bertram v. Terayon Communications Sys., Inc.*, 2001 WL 514358, at *1 (C.D. Cal., Mar. 27, 2001); H.R. Conf. Rep. No. 105-803, at 14–15.

25. *See Bertram v. Terayon Communications Sys.*, 2001 WL 514358 (C.D. Cal., Mar. 27, 2001); *Gibson v. PS Group Holdings, Inc.*, 2000 WL 777818 (S.D. Cal., Mar. 8, 2000).

26. *See Gutierrez v. Deloitte & Touche, L.L.P.*, 147 F. Supp. 2d 584, 591 (W.D. Tex. 2001); *Prager v. Knight/Trimark Group, Inc.*, 124 F. Supp. 2d 229, 233 (D.N.J. 2000).

27. *See Kenneth Rothschild Trust v. Morgan Stanley*, 199 F. Supp. 2d 993, 1004 (C.D. Cal. 2002) (citing cases).

28. 421 U.S. 723 (1975).

29. 430 U.S. 462 (1977).

30. 404 U.S. 6, 12–13 (1971).

31. *Lawrence v. Cohn*, 325 F.3d 141, 154 (2d Cir. 2003). As discussed in Section IIA, this appears to be a looser standard than previously followed in the Second Circuit. However, the court did not discuss *S.E.C. v. Zandford*.

32. 535 U.S. 813, 122 S. Ct. 1899 (2002).

33. *See Meyer v. Dygert*, 156 F. Supp. 2d 1081, 1088 (D. Minn. 2001); *In re Staffmark Sec. Litig.*, 123 F. Supp. 2d 1160, 1177 (E.D. Ark. 2000); *Alpern v. Utilicorp United, Inc.*, 1994 WL 682861, at *2 (W.D. Mo., Nov. 14, 1994).

34. *Compare P. Schoenfeld Asset Mgmt. LLC v. Cendant Corp.*, 142 F. Supp. 2d 589, 595–603 (D.N.J. 2001) (on remand) with *Crummere v. Smith Barney*, 624 F. Supp. 751, 755 (S.D.N.Y. 1985), citing *Chemical Bank v. Arthur Andersen & Co.*, 726 F.2d 930 (2d Cir.), *cert. denied*, 469 U.S. 884 (1984); *U.S. v. Coriaty*, 2001 U.S. Dist. LEXIS 9870, at *19–25 (S.D.N.Y., July 16, 2001).

35. *Chemical Bank*, *supra*, 726 F.2d at 943. *But see S.E.C. v. Jakubowski*, 150 F.3d 675, 678–80 (7th Cir. 1998), *cert. denied*, 525 U.S. 1103 (1999) (citing *United States v. O'Hagan*, 521 U.S. 642 (1997) and *United States v. Naftalin*, 441 U.S. 768 (1979)).

36. *Crummere v. Smith Barney*, 624 F. Supp. 751, 756 (S.D.N.Y. 1985); *accord Kearney v. Prudential Bache Sec., Inc.*, 701 F. Supp. 416, 424 (S.D.N.Y. 1988).

37. *See Hoffman v. TD Waterhouse Investor Services, Inc.*, 148 F. Supp. 2d 289, 291–92 (S.D.N.Y. 2001); *Miller v. Asensio*, 101 F. Supp. 2d 395, 400–401 (D.S.C. 2000); *Prod. Res. Group, LLC v. Stonebridge Partners Equity Fund*, 6 F. Supp. 2d 236, 240 (S.D.N.Y. 1998).

38. 770 F. Supp. 176 (S.D.N.Y. 1991).

39. *Id.* at 181. *See also Pross v. Katz*, 784 F.2d 455, 459 (2d Cir. 1986) (dismissing complaint that alleged "no more than a conversion of property that happened to involve securities. We are unwilling to extend the reach of the securities laws to every conversion or theft of a security."). *Accord Bochiccio v. Smith Barney, Harris Upham & Co.*, 647 F. Supp. 1426, 1430 (S.D.N.Y. 1986).

40. *See In re Prudential Ins. Co. of American Sales Practices Litig.*, 975 F. Supp. 584, 607–608 (D.N.J. 1996) (discussing the views espoused in *Angelastro v. Prudential-Bache Secs., Inc.*, 764 F.2d 939, 942 (3d Cir.), *cert. denied*, 474 U.S. 935 (1985)).

41. *Gurwara v. Lyphomed, Inc.*, 937 F.2d 380 (7th Cir. 1991); *Head v. Head*, 759 F.2d 1172 (4th Cir. 1985).

42. *FS Photo Inc. v. Picturevision, Inc.*, 61 F. Supp. 2d 473, 479 (E.D. Va. 1999) (emphasis added).

43. *Zandford* was presaged to some degree by the Supreme Court's earlier decision in *The Wharf (Holdings) Ltd. v. United Int'l Holdings, Inc.*, 532 U.S. 588, 596, 121 S. Ct. 1776 (2001) which rejected a defense that a secret reservation not to permit exercise of an option did not relate to the value of the security or the consideration paid.

44. 122 S. Ct. at 1903.

45. *See Falkowski v. Imation Corp.*, 309 F.3d 1123, 1129–31 (9th Cir. 2002); *Araujo v. John Hancock Life Ins. Co.*, 206 F. Supp. 2d 277, 282–83 (E.D.N.Y. 2002).

46. *See, e.g., Santa Fe Indust., Inc. v. Green*, 430 U.S. 462, 479, 97 S. Ct. 1292, 1303–1304 (1977); *Herm v. Stafford*, 663 F.2d 669, 685 (6th Cir. 1982); *Arduini/Messina Partnership v. National Medical Fin. Serv. Corp.*, 74 F. Supp. 2d 352, 362 (S.D.N.Y. 1999); *Ciresi v. Citicorp*, 782 F. Supp. 819, 821 (S.D.N.Y. 1991). *Compare Suez Equity Investors v. Toronto-Dominion Bank*, 250 F.3d 87, 99 (2d Cir. 2001) (rejecting application on the facts before it and distinguishing *Field v. Trump*, 850 F.2d 938, 946 (2d Cir. 1988) as a failure to disclose that certain directors and officers "breached their fiduciary duty to the shareholders").

47. *See, e.g., Milman v. Box Hill Systems Corp.*, 72 F. Supp. 2d 220, 233–34 (S.D.N.Y. 1999). There are exceptions when issuer statements arguably put the question of management competence or conduct in play. *In re Premiere Tech. Inc. Sec. Litig.*, 2000 WL 33231639, at *14–15 (N.D. Ga., Dec. 8, 2000) (noting statements dealing with management infrastructure and personnel issues were put "in play" by company statements); *In re Donna Karan Int'l Sec. Litig.*, 1998 WL 637547, at *9 (E.D.N.Y. Aug. 14, 1998) (holding there may be liability for failure to disclose material facts resulting from mismanagement).

48. *See, e.g., Werner v. Werner*, 267 F.3d 288, 299 (3d Cir. 2001); *Kas v. Fin. General Bankshares, Inc.*, 796 F.2d 508, 513 (D.C. Cir. 1986).

49. *See Craftmatic Secs. Litig. v. Kraftsow*, 890 F.2d 628, 638 n.14 (3d Cir. 1990); *Charas v. Sand Tech Sys. Int'l, Inc.*, 1992 WL 296406, at *6 (S.D.N.Y., Oct. 7, 1992).

50. *See, e.g., Gurary v. Winehouse*, 235 F.3d 792, 801 (2d Cir. 2000); *First Lincoln Holdings, Inc. v. Equitable Life Assurance*, 164 F. Supp. 2d 383, 394 (S.D.N.Y. 2001); *IDT Corp. v. EGlobe, Inc.*, 140 F. Supp. 2d 30, 33–35 (D.D.C. 2001); *Gigliotti v. Mathys*, 129 F. Supp. 2d 817, 823–24 (D.V.I. 2001). *Compare The Wharf (Holdings) Ltd. v. United Int'l Holdings*, 532 U.S. 588, 592, 121 S. Ct. 1780 (2001) (preexisting intent proven).

51. *See Green v. Ameritrade, Inc.*, 279 F.3d 590 (8th Cir. 2002); *Xpedior Creditor Trust v. Credit Suisse First Boston (USA), Inc.*, 2004 WL 435058, at *3–7 (S.D.N.Y., Mar. 9, 2004) (finding state law claims not preempted by SLUSA in a case originally filed in District Court since they did not arise out of untrue statements or omissions of a material fact or use of a manipulative or deceptive device); *Shen v. Bohan*, 2002 U.S. Dist. LEXIS (C.D. Cal., Oct. 17, 2002) (no "purchase or sale" where claim that voting rights were diluted through adjustment of stock options). *Compare Korsinsky v. Salomon Smith Barney Inc.*, 2002 WL 27775, at *5–6 (S.D.N.Y., Jan. 10, 2002) (refusing to remand claims of purchasers of AT&T stock where purchases were made following public statements of leading telecommunications analyst, distinguishing *Hardy*, *infra*) *with Hardy v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.*, 189 F. Supp. 2d 14, 18–19 (S.D.N.Y. 2001) (finding that only one of three potential subclasses might satisfy that post-statement purchase requirement and dismissing, as opposed to remanding, in order to allow plaintiffs' counsel to limit class by excluding that group in any re-filed state court litigation).

52. *Gordon v. Buntrock*, 2000 WL 556763, at *3 (N.D. Ill., Apr. 28, 2000) (breach of fiduciary duty); *Lalondriz v. USA Networks, Inc.*, 68 F. Supp. 2d 285, 286 (S.D.N.Y. 1999) (same); and *Hines v. ESC Strategic Funds, Inc.*, 1999 WL 1705503, at *6 (M.D. Tenn., Sept. 17, 1999) (fiduciary duty breach *after* purchase of stock).

53. *See, e.g., MDCM Holdings v. Credit Suisse First Boston Corp.*, 216 F. Supp. 2d 257–58 (S.D.N.Y. 2002) (issuer's claim against underwriter founded only in breach of contract); *Coykendall v. Kaplan*, 2002 U.S. Dist. LEXIS 22483 (N.D. Cal., Aug. 1, 2002) (derivative action alleged); *Spielman v. Merrill Lynch*, 2001 WL 1182927, at *3–5 (S.D.N.Y., Oct. 9, 2001) (statements alleged concerned transaction fees); *Roskind v. Morgan Stanley Dean Witter & Company*, 165 F. Supp. 2d 1059, 1064–67 (N.D. Cal. 2001) (holding that allegations of failure to execute at best available price and "trading ahead" implicate state law fiduciary duty and that NASD rules not a "necessary element" of plaintiff's claims); *Shaw v. Charles Schwab & Co., Inc.*, 128 F. Supp. 2d 1270, 1272–74 (C.D. Cal. 2001) (ordering remand to challenge to online trading practices); *Abada v. Charles Schwab & Co., Inc.*, 127 F. Supp. 2d 1101 (S.D. Cal. 2000) (ordering remand for failure to satisfy "in connection with" requirement).

54. *Burns v. Prudential Sec., Inc.*, 116 F. Supp. 2d 917, 923–24 (N.D. Ohio 2000) ("*Burns I*") (to ordering remand of claim of unauthorized trading absent allegations of a larger scheme to defraud); *Burns v. Prudential Sec., Inc.*, 218 F. Supp. 2d 911 (N.D. Ohio 2002) (analyzing unsuccessful removal petition on the merits).

55. *Riley v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.*, 292 F.3d 1334, 1342–45 (11th Cir. 2002) (finding it sufficient that allegations covered both acquisition and retention of securities); *Ray v. Citigroup Global Markets, Inc.*, 2003 WL 22757761, at *5–6 (N.D. Ill., Nov. 20, 2003) (same); *Kenneth Rothschild Trust v. Morgan Stanley*, 199 F. Supp. 2d 993, 1003 (C.D. Cal. 2002) (distinguishing *Shaw, supra*); *McCullagh v. Merrill Lynch & Co.*, 2002 WL 362774 (S.D.N.Y., March 2, 2002) (denying remand of allegations based on analysts' buy recommendations); *Denton v. H & R Block Fin. Advisors, Inc.*, 2001 WL 1183292, at *3–4 (N.D. Ill., Oct. 4, 2001) (distinguishing *Burns I*, *supra*, and discussing case law extensively). *See also Behlen v. Merrill Lynch*, 311 F.3d 1087, 1092–96 (11th Cir. 2002) (rejecting contentions that state court had to certify class before removal and efforts to avoid removal through amendments deleting misrepresentation allegations); *Dudek v. Prudential Sec., Inc.*, 295 F.3d 875, 879–80 (8th Cir. 2002) (finding both failures to disclose and "deceptive device or contrivance").

56. *Shaw v. Charles Schwab & Company, Inc.*, 128 F. Supp. 2d 1270, 1272–74 (C.D. Cal. 2001).

57. *Shaw v. Charles Schwab & Company, Inc.*, 2003 WL 1463842 (Cal. Superior Court, Mar. 7, 2003). The state court also dismissed a state claim on SLUSA preemption grounds in *BT Sec. Co. v. W. R. Huff. Asset Mgmt. Co., L.L.C*, 2004 WL 818882 (Alabama Supreme Court, Apr. 16, 2004).

58. *In re WorldCom. Inc. Sec. Litig.*, 234 F. Supp. 2d 301, 305 (S.D.N.Y. 2002).

59. *See Benbow v. Aspen Tech., Inc.*, 2003 WL 1873910, at *3–4 (E.D. La., Apr. 11, 2003); *In re DPL Inc. Sec. Litig.*, 2003 U.S. Dist. LEXIS 3093, at *9 n.6 (S.D. Ohio, Feb. 25, 2003); *Tobias Holdings, Inc. v. Bank United Corp.*, 177 F. Supp. 2d 162, 166 n.4, 166–69 (S.D.N.Y. 2001) (finding stay applicable to individual actions but distinguishing discovery as to pendant claims asserted).

60. *See Lapicola v. Alternative Dual Fuels, Inc.*, 2002 WL 531545 (N.D. Tex., Apr. 5, 2002); *In re Transcrypt Int'l Sec. Litig.*, 57 F. Supp. 2d 836 (D. Neb. 1999).

61. *See Newby v. Enron Corp.*, 188 F. Supp. 2d 684, 709 (S.D. Tex. 2002); *In Re CFS-Related Sec. Fraud Litig.*, 179 F. Supp. 2d 1260, 1263–64 (N.D. Okla. 2001) (applying to all discovery where any defendant has filed a motion to dismiss); *In Re Carnegie Intern. Corp. Sec. Litig.*, 167 F. Supp. 2d 676, 682–83 (D. Md. 2000) (finding stay available where motion to dismiss not yet due to be filed and noting minority contrary authority); *Medical Imaging Centers of America, Inc. v. Lichtenstein*, 917 F. Supp. 717, 719–721 (S.D. Cal. 1996) (applying to action under Section 13(d) of the Exchange Act in context of proxy contest despite rapidly approaching board of directors election).

62. *Compare In re CFS-Related Sec. Fraud Litig.*, 213 F.R.D. 435, 442–47 (N.D. Okla. 2003) (applying to promised motions by third-party defendants to dismiss third-party claims but not to main action based on motions by defendants to dismiss cross-claims and counterclaims); *In re Lernout & Hauspie Sec. Litig.*, 214 F. Supp. 2d

100, 104–109 (D. Mass. 2002) (allowing discovery to proceed against defendants whose motions to dismiss were denied despite pendency of similar undecided motions by other defendants).

63. *See, e.g.*, *Newby v. Enron Corp.*, 338 F.3d 467 (5th Cir. 2003) (upholding District Court's authority to stay discovery in *any private, class or non-class, state* court *action*, and to force withdrawal of plaintiff's temporary injunction motions to freeze defendants' assets and to preserve documents); *In Re Bankamerica Sec. Litig.*, 263 F.3d 793, 802–03 (8th Cir. 2001) (issuing injunction as to discovery in state court proceedings); *SG Cowen Sec. Corp. v. United States District Court*, 189 F.3d 909, 913 (9th Cir. 1999) (refusing to distinguish between federal and pendent state claims and vacating order allowing limited discovery); *In re DPL Inc., Sec. Litig.*, 247 F. Supp. 2d 946 (S.D. Ohio 2003) (extending stay to state derivative action). *See also In re DPL Inc., Sec. Litig.*, 285 F. Supp. 2d 1053, 1061–63 (S.D. Ohio 2003) (refusing to terminate stay).

64. *See In re AOL Time Warner, Inc. Sec. and ERISA Litig.*, 2003 WL 22227945 (S.D.N.Y., Sept. 26, 2003).

65. *In re Royal Ahold N.V. Sec. & ERISA Litig.*, 220 F.R.D. 246, 250–53 (D. Md., Mar. 12, 2004); *In re AOL Time Warner, Inc. Sec. Litig.*, 2003 WL 715752 (S.D.N.Y., Feb. 28, 2003); *In re WorldCom, Inc. Sec. Litig.*, 234 F. Supp. 2d 301 (S.D.N.Y. 2002); *Compare In re Vivendi Universal, S.A. Sec. Litig.*, 2003 WL 21035383 (S.D.N.Y., May 6, 2003).

66. *In re Initial Public Offering Sec. Litig.*, 236 F. Supp. 2d 286 (S.D.N.Y. 2002) (refusing to lift stay despite argument that size and complexity of litigation and scope of discovery required met "undue prejudice" standard); *Log On America, Inc. v. Promethean Asset Mgmt. L.L.C.*, 210 F. Supp. 2d 291 (S.D.N.Y. 2001) (refusing to allow relief from confidentiality order in other litigation initiated by plaintiff to allow for use of certain disclosures in that litigation as basis of amended complaint following dismissal without prejudice of initial complaint); *In re CFS–Related Sec. Fraud Litig.*, 179 F. Supp. 2d 1260, 1265 (N.D. Okla. 2001); *Faulkner v. Verizon Communications, Inc.*, 156 F. Supp. 2d 384, 401–406 (S.D.N.Y. 2001) (denying relief from stay); *Hilliard v. Black*, 125 F. Supp. 2d 1071, 1084 (N.D. Fla. 2000).

67. *In re Carnegie Intern. Corp. Sec. Litig.*, 107 F. Supp. 2d 676 (D. Md. 2000) (applying stay to discovery sought from third-party accounting firm). *See also Neibert v. Monarch Dental Corp.*, 1999 U.S. Dist. LEXIS 22312, at *3–4 (N.D. Tex., Oct. 20, 1999); *In re Fluor Corp. Sec. Litig.*, 1999 U.S. Dist. LEXIS 22128, at *7 (C.D. Cal., Jan. 19, 1999). *Compare In re Grand Casinos, Inc. Sec. Litig.*, 988 F. Supp. 1270, 1272 (D. Minn. 1997).

68. *See In re WorldCom, Inc. Sec. Litig.*, 234 F. Supp. 2d 301, 305–06 (S.D.N.Y. 2002) (noting, among other factors, documents provided to other interested parties, including regulators and creditors' committee); *Vacold LLC v. Cerami*, 2001 WL 167704 (S.D.N.Y., Feb. 16, 2001); *In re Baan Co. Sec. Litig.*, 81 F. Supp. 2d 75, 81–84 (D.D.C. 2000) (discovery allowed on the issue of "minimum contacts" for jurisdictional purposes).

69. *Anderson v. First Sec. Corp.*, 157 F. Supp. 2d 1230, 1241–42 (D. Utah 2001).

70. *Anderson v. First Sec. Corp.*, 249 F. Supp. 2d 1256, 1271–72 (D. Utah 2002).

71. *Tobias Holdings, Inc. v. Bank United Corp.*, 177 F. Supp. 2d 162, 166–69 (S.D.N.Y. 2001).

72. The disagreement was with Magistrate Judge Pitman's conclusions in *In re Trump Hotel Shareholder Derivative Litig.*, 1997 WL 442135, at *2 (S.D.N.Y., Aug. 5, 1997); *Compare Rampersad v. Deutsche Bank Sec., Inc.*, 2003 WL 21074094 (S.D.N.Y., May 9, 2003).

Committee Report—Eliminating a Trap for the Unwary: A Proposed Revision of Federal Rule of Civil Procedure 50

By Gregory K. Arenson and Thomas McGanney

Introduction

Federal Rule of Civil Procedure 50, now entitled "Judgment as Matter of Law in Jury Trials; Alternative Motion for New Trial; Conditional Rulings" (hereinafter "Rule 50"), was extensively amended in 1991. The 1991 amendment eliminated the terminology of "directed verdict" and "judgment notwithstanding the verdict (hereinafter "judgment n.o.v.") and substituted the term "judgment as a matter of law" for both. The rule provides that "motions for judgment as a matter of law may be made at any time before submission of the case to the jury."[1] The motion is no longer required to be made when a party has completed its case and formally rested, but may be granted at any time when "a party has been fully heard on an issue."[2] It is relatively rare that such a motion is granted; the trial court usually either reserves decision or denies such a motion, and leaves the initial determination to the jury. "[A]ppellate courts have often indicated that in general the better and safer practice is for trial courts to wait for a verdict and rule on the sufficiency of the evidence in a post-verdict motion for judgment."[3]

The rule retains the requirement that, in order for judges to consider a motion for judgment made after the verdict, there must have been a motion made for judgment "at the close of all the evidence."[4] Thus, even if a party has made a motion for judgment at the end of the opposing party's case (or when the opposing party has been heard), but fails to renew it at the close of the evidence, such party cannot make a motion for judgment after the verdict is rendered. Instead, under the language of Rule 50, that party is limited to a motion for a new trial under Rule 59.

The Advisory Committee stated in 1991 that it is desirable for the motion for judgment to be made before the case is submitted to the jury "so that the responding party may seek to correct any overlooked deficiencies in the proof."[5] However, the Advisory Committee did not address why such a motion must again be made at the close of all the evidence, if it has already been made at a time when the responding party has been fully heard.

Numerous commentators have criticized the structure of Rule 50 in this regard as "a trap for the unwary."[6] Both New York and California have abolished the rule that a pre-submission motion must have been made as a prerequisite to entering judgment for a party despite a jury verdict in favor of the other party.[7] *California Procedure*[8] refers to the prior procedure as "a useless and annoying formality."[9] The New York Advisory Committee stated in its 1958 Report:

> The motion at the close of the evidence is a mere formality today which does not give either the court or litigants any fair notice in time to cure defects. It seems only a trap for the unwary or inadvertent which should not be an absolute condition for judgment notwithstanding the verdict.[10]

Perhaps more significantly, several federal appellate and trial courts have refused to enforce Rule 50 as written in this regard, finding that the procedure has no practical justification. Other courts do enforce the rule as written, creating uncertainty within and among the various circuits as to the state of the law.

The varied and unpredictable approach of the courts to the procedure under Rule 50 creates a problem that should be addressed. At least four significant alternatives present themselves:

(1) Rule 50 should be enforced as written.

(2) Rule 50 should be amended to eliminate the requirement for any pre-verdict motion to be made as a prerequisite to a post-verdict motion for judgment.

(3) Rule 50 should be amended to eliminate the need for making a motion for judgment "at the close of all the evidence" as a prerequisite to making a post-verdict motion, if a motion for judgment in accordance with Rule 50(a) has already been made prior to that time.

(4) The issue should be decided by weighing the prejudice to each side based on the facts of the case.

For the reasons discussed below, the Section concludes that alternative 3 should be adopted.

Discussion

A. Constitutional Background

The procedure under Rule 50 (and its predecessors) has been shaped by Supreme Court decisions interpreting the Seventh Amendment. The Supreme Court in 1913 held that a motion for judgment notwithstanding the verdict could not be granted in federal courts because its grant would have the effect of depriving the victorious party of his right to a jury trial. The Court found no analogue to the motion in the pre-Constitution common law procedure. The Court made specific reference to the

clause of the Seventh Amendment that provides that "no fact tried by a jury shall be otherwise re-examined in any court of the United States."[11] The Court did not hold in that case that the trial court had erroneously denied a directed verdict motion, but held that the appropriate remedy was a new trial.

Twenty-two years later, in *Baltimore & Carolina Line, Inc. v. Redman*,[12] the Court found a way around *Slocum*. The Court held that if the district court expressly reserved the point whether a directed verdict should be granted, both it and the appellate court were thereby empowered to enter judgment n.o.v., if they determined that the directed verdict motion should have been granted.

Rule 50(b), as it was promulgated in 1937, eliminated the need for a formal reservation by the district court. The Rule provided that the court was "deemed" to have reserved the determination of legal issues whenever a pre-verdict motion for a directed verdict was not granted. The language has been modified, but the same concept is embodied in the current version of Rule 50(b). The Supreme Court has upheld post-verdict judgment as a matter of law pursuant to Rule 50 as consistent with the Seventh Amendment.[13]

The Fed. R. Civ. P. 50, 1991 Advisory Committee Note to Subdivision (a) makes clear that the Advisory Committee considers the constitutional thinking of *Slocum* anachronistic:

> [A]ction taken under the rule is a performance of the court's duty to assure enforcement of the controlling law and is not an intrusion on any responsibility for factual determinations conferred on the jury by the Seventh Amendment. . . .

However, the historical development of the Supreme Court cases and Rule 50 does indicate that there may be a constitutional objection to eliminating the requirement that at least one pre-verdict motion for judgment be made. If such a motion has not been made at all, then there would be nothing upon which to base the fiction[14] that decision has been reserved. In light of this, alternative (2)—the procedure adopted in New York and California—cannot easily be adopted in the federal courts. The question remains as to whether there is any justification for requiring renewal of the motion if it has once been made.

B. The Advisory Committee's Rationale for Requiring Pre-Verdict Motions

The Advisory Committee in 1991 addressed the practical justification for requiring a pre-verdict motion in several places. In commenting on subdivision (a), the Advisory Committee Note states:

> Paragraph (a)(2) retains the requirement that a motion for judgment be made prior to the close of the trial, subject to renewal after a jury verdict has been rendered. The purpose of this requirement is to assure the responding party an opportunity to cure any deficiency in that party's proof that may have been overlooked until called to the party's attention by a late motion for judgment.

The Note also refers to the second sentence of Rule 50(a)(2), which requires that the moving party articulate the basis on which a judgment as a matter of law might be rendered. The Note goes on to say that the "revision thus alters the result in cases in which courts have used various techniques to avoid the requirement" that a pre-verdict motion be made as a predicate for a motion notwithstanding the verdict. This provision does require that at least one such pre-verdict motion be made; it does not, however, provide a rationale for the position that the motion, once made, has to be renewed. The Note then quotes from *Farley Transp. Co. v. Santa Fe Trail Transp. Co.*[15] and *Benson v. Allphin*,[16] both discussed below.

A similar comment is made by the 1991 Advisory Committee with respect to Subdivision (b):

> **Subdivision (b).** This provision retains the concept of the former rule that the post-verdict motion is a renewal of an earlier motion made at the close of the evidence. One purpose of this concept was to avoid any question arising under the Seventh Amendment. *Montgomery Ward & Co. v. Duncan,* 311 U.S. 243 (1940). It remains useful as a means of defining the appropriate issue posed by the post-verdict motion. A post-trial motion for judgment can be granted only on grounds advanced in the pre-verdict motion. *E.g., Kutner Buick, Inc. v. American Motors Corp*., 868 F.2d 614 (3d Cir. 1989).

Again, this statement does not address the issue of why it should be necessary to renew a motion for judgment at the close of all the evidence.

C. The Conflicting Case Law

Prior to the 1991 amendment, the then-Advisory Committee Reporter, Paul Carrington, in an article in the *University of Pennsylvania Law Review*,[17] commented on the status of the case law under Rule 50:

> The concern with Rule 50 is not that it sends too many or too few cases to a jury, or that too many or too few verdicts

are being disregarded at the point of judgment. The concern is rather that Rule 50 and the practice under it are anachronistic, too complex, and a trap for the unwary.

An old rule of questionable value requires a motion for directed verdict under Rule 50(a) as a predicate for a motion for judgment notwithstanding the verdict under Rule 50(b). The rule rests on the fiction that denial of a motion for directed verdict automatically reserves the issue for reconsideration when the post-verdict motion is made. Courts interpreted a 1913 decision to require the fiction, but a 1935 holding substantially undermined the 1913 ruling. Also questionable is the old rule, possibly abiding, that a party waives a motion for directed verdict by presenting evidence.

These otherwise anachronistic rules protected opposing parties from being surprised by a motion for a judgment notwithstanding the verdict based on a legal theory or a factual contention not previously raised or considered. Absent these provisions, parties might have been tempted to save an objection to the legal sufficiency of an adversary's case until it was too late to cure the defect by submission of additional evidence on a fact not previously recognized by the adversary as material.

On the other hand, requiring a formal motion for directed verdict has several unfortunate consequences. It is a trap: Failing to make a timely motion that a judge very likely would have denied could force a party to undergo a new trial. The refusal to consider a motion for judgment notwithstanding the verdict on the sole ground that the party did not make a motion for directed verdict is an empty formalism out of keeping with the Rules. Moreover, the requirement forces some parties to make motions contrary to their own tactical interests; in doubtful cases, litigants may prefer sending their cases to the jury in the hope of a favorable factual termination rather than risking a reversal of a directed verdict resulting in yet another trial. A number of courts have used techniques designed to avoid the effect of the requirement and in the process they have created some complex doctrine. (footnote omitted).

Despite Professor Carrington's views, the Advisory Committee maintained the requirement of a pre-verdict motion for making a post-verdict motion.

As Professor Carrington noted, one of the results of literal enforcement of the rule is that noncompliance can mean that a party, which may deserve judgment as a matter of law, is limited to seeking the relief of a new trial.[18] This result is intolerable to many courts, and they have devised ways to avoid this result.

As a practical matter, if a party is entitled to judgment as a matter of law, it makes little sense to require another trial to present factual evidence, when the result is foreordained by the resolution of the legal issue.

A note in the *Michigan Law Review* of March 1993[19] collects numerous cases and compares the approach of the various circuits to the requirements of Rule 50. This survey detailed five or six different rules applied in ten different circuits. No cases were then found in the D.C. Circuit or the Fourth Circuit. As further discussed below, since that time the Fourth Circuit has adopted a lenient approach to Rule 50, but the Seventh Circuit has criticized its previous decisions and adopted a strict approach.

(1) The Third and the Eleventh Circuits have taken a literal, strict approach. Even if a directed verdict motion is made, a post-verdict motion for judgment as a matter of law will not be considered if the motion is not renewed at the close of all the evidence.[20]

(2) Four circuits—the First, Sixth, Eighth and Tenth—have held that the post-verdict motion could be entertained, even if the directed verdict motion had not been renewed if two conditions were met: (1) the district judge, at the time of hearing the directed verdict motion, had somehow specifically indicated that the failure to renew the motion at the close of the evidence would not result in a waiver; and (2) the evidence put on by the moving party after denial of the directed verdict motion was not extensive.[21]

(3) The Fifth Circuit also permitted consideration of post-verdict motions where there has been no renewal of the directed verdict motion, but formulated the test somewhat differently: (1) the district judge need only have "reserved" decision on the motion—it was not necessary that the judge give specific assurance to the moving party that its rights were being preserved; and (2) the evidence introduced after

reservation of the directed verdict motion may be substantial, so long as it is essentially unrelated to the motion.[22]

(3A) The Second Circuit articulated a variant of the Fifth Circuit rule that: (1) required that the trial judge indicate that the movant's rights were preserved; but (2) phrased the test relating to the evidence introduced after the motion as being of such a nature that the opposing party could not "reasonably have thought that the moving party's initial view of the insufficiency of the evidence had been overcome and there was no need to produce anything more in order to avoid the risk of judgment n.o.v."[23] The Second Circuit has also held that it will not enforce the strict provisions of Rule 50 if the opposing party fails to raise the issue in the district court.[24]

(4) The Ninth Circuit has held that it was permissible to entertain a post-verdict motion for judgment, so long as the district court had taken an earlier motion for a directed verdict under advisement, rather than deciding it.[25] In a later case, the Ninth Circuit held that the motion had to be renewed at the close of the evidence, when the district court had denied a prior motion for judgment made after plaintiff's opening statement.[26] The court noted that plaintiff had called six witnesses and defendant one witness, after the motion was made.

(5) Prior to the 1991 amendments, the Seventh Circuit had adopted a rule that depended upon a showing of prejudice by the opposing party. If the movant had made a motion for a directed verdict, even if the district court had denied it outright, the movant was entitled to renew the motion post-trial if there was no prejudice to the other party.[27] However, in *Downes* v. *Volkswagen of America, Inc.*,[28] the Seventh Circuit held that since the Advisory Committee had the chance to revise Rule 50 in 1991, but instead had retained the requirement of renewing a pre-verdict motion for judgment, *Benson* should not be followed.[29] Other Seventh Circuit decisions have followed *Downes*.[30]

(6) The Fourth Circuit, which had not taken a position prior to 1991, adopted a lenient approach in *Singer* v. *Dungan*.[31] In that case, the court, after quoting from Moore's Federal Practice[32] and noting the decisions of various courts applying a limited approach to Rule 50(a), determined that defendant's motion for judgment should have been granted, despite defendant's failure to renew the motion at the close of the evidence, "because the spirit behind Rule 50 was served" in that case.[33]

One conclusion that can be drawn from this survey is that a large amount of judicial effort has been expended to determine whether the literal requirements of Rule 50(a) should be enforced, and as a result, this rule has quite different application in various federal courts throughout the United States.

Conclusion

In 1991, the Advisory Committee articulated a practical justification for the procedure of requiring a motion for judgment to be made before submission to the jury. It found the justification to be "that the responding party may seek to correct any overlooked differences in the proof." The Advisory Committee cited to decisions in the Ninth and Seventh Circuits[34] which had articulated these justifications. However, the holdings of both these cases were to excuse the failure to renew, before submission to the jury, a directed verdict motion.

The Advisory Committee's rationale does not support a requirement that a directed verdict motion must be renewed at the close of all the evidence, as Rule 50(b) now requires. At most, it supports the position that *at some time prior to submission* to the jury, a motion for judgment as a matter of law should be made and the basis for the motion clearly articulated. Such motions can be made after the non-moving party has been fully heard on the issue, or after it has rested.

We do not believe that the question of whether the motion should be reserved should be resolved on a case-by-case basis by weighing the comparative prejudice to each party. Nor do we believe that the complicated formulations adopted by some courts on this issue are helpful; indeed they seemed designed to encourage further litigation directed to procedural, not substantive, issues. There should be a clear rule which makes practical sense.

We thus suggest that the first sentence of Rule 50(b) be amended to add the italicized phrases:

> If, for any reason, the court does not grant a motion for judgment as a matter of law made *after the non-moving party has been heard on an issue or rested*, *or* at the close of all the evidence, the court is considered to have submitted the action to the jury subject to the court's later deciding the legal questions raised by the motion.

We believe that such an amendment satisfies the purpose of Rule 50—to give notice to the non-moving party of correctable deficiencies in its case—but lessens the potential of the rule to be simply a "trap for the unwary."

Endnotes

1. Fed. R. Civ. P. 50(a)(2) (hereinafter "Rule 50(a)(2)").
2. Fed. R. Civ. P. 50(a)(1)).
3. Moore's Federal Practice (3d ed.) § 50.02(2) at 50-14. *See Mattivi v. South African Marine Corp., "Huguenot,"* 618 F.2d 163, 166 n.2 (2d Cir. 1980).
4. *See* Fed. R. Civ. P. 50(b) (hereinafter "Rule 50(b)") and Fed. R. Civ. P. 50, 1991 Advisory Committee Note to Subdivision (b)).
5. Fed. R. Civ. P. 50, 1991 Advisory Committee Note to Subdivision (a).
6. Paul D. Carrington, *The Federal Rule–Making Process*, 137 U. Pa. L. Rev. 2067, 2110–2111 (1989).
7. *See* CPLR 4404 (McKinney 2003) (permitting a post-verdict motion by a losing party or on the court's own motion without requiring a pre-verdict motion.) and Cal. Civ. Proc. § 629.
8. 7 B.E. Witkin, 4th ed. 1997.
9. *Id.* at Section 448.
10. Advisory Comm. on Practice & Procedure, Second Preliminary Report, N.Y. Leg. Doc. No. 13 at 312 (1958).
11. *Slocum v. New York Life Ins. Co.*, 228 U.S. 364, 376 (1913) (5-4 decision).
12. 295 U.S. 654 (1935).
13. *Neely v. Martin K. Eby Constr. Co.*, 386 U.S. 317, 321 (1967).
14. There is no question that it is a fiction: "A judge may issue a definitive ruling denying the pre-verdict motion for judgment as a matter of law . . . yet that seemingly definitive ruling is somehow deemed to constitute nothing more than a reservation of decision on the motion." Moore's Federal Practice (3d ed.) ¶ 50.04(2) at 50.21.
15. 786 F.2d 1342 (9th Cir. 1986).
16. 786 F.2d 268 (7th Cir. 1986).
17. Paul D. Carrington, *The Federal Rulemaking Process*, 137 U. Pa. L. Rev. 2067, 2110–2111 (1989).
18. *See DeMarines v. KLM Royal Dutch Airlines*, 580 F.2d 1193 (3d Cir. 1978) (defendant moved for directed verdict at end of plaintiff's case, but failed to renew the motion at the close of all the evidence; held, although defendant deserved judgment as matter of law, failure to renew motion in accordance with Rule 50's terms, precluded such relief).
19. Note, Rollin A. Ransom, *Toward A Liberal Application of the "Close of all the Evidence "Requirement of Rule 50(B) of the Federal Rules of Civil Procedure: Embracing Fairness over Formalism*, 91 Mich. L. Rev. 1060 (1993).
20. *See Lowenstein v. Pepsi-Cola Bottling Co. of Pennsauken*, 536 F.2d 9 (3d Cir. 1976); *Mark Seitman & Assoc. Inc. v. R.J. Reynolds Tobacco Co.*, 837 F.2d 1527 (11th Cir. 1988).
21. *Bayamon Thom McAn, Inc. v. Miranda*, 409 F.2d 968 (1st Cir. 1969); *Boynton v. TRW Inc.*, 858 F.2d 1178, 1186 (6th Cir. 1988); *Halsell v. Kimberly-Clark Corp.*, 683 F.2d 285, 294 (8th Cir. 1982) (however, the Eighth Circuit has also required that a motion for judgment n.o.v. be renewed, without reference to the *Halsell* case, in *Duckworth v. Ford*, 83 F.3d 999, 1001 (8th Cir. 1996); *Armstrong v. Fed. Nat'l. Mortgage Ass'n*, 796 F.2d 366, 370 (10th Cir. 1986).
22. *Miller v. Rowan Cos.*, 815 F.2d 1021, 1024–25 (5th Cir. 1987). *See also Bay Colony, Ltd. v. Trendmaker, Inc.*, 121 F.3d 998, 1003 (5th Cir. 1997) ("Thus, this Court has not required strict compliance with Rule 50(b) and has excused technical noncompliance where the purposes of the requirements have been satisfied.").
23. *Ebker v. Tan Jay Int'l Ltd.* 739 F.2d 812, 824 (2d Cir. 1984).
24. *See Gibeau v. Nellis*, 18 F.3d 107, 109 (2d Cir. 1994).
25. *Farley Transp. Co. v. Santa Fe Trail Transp. Co.*, 786 F.2d 1342 (9th Cir. 1986).
26. *Patel v. Penman*, 103 F.3d 868 (9th Cir. 1996).
27. *Benson v. Allphin*, 786 F.2d 268 (7th Cir. 1986).
28. 41 F.3d 1132 (7th Cir. 1994).
29. *Id.* at 1139–40.
30. *See Mid-America Tablewares, Inc. v. Mogi Trading Co. Ltd.*, 100 F.3d 1353, 1364 (7th Cir. 1996) (collecting cases).
31. 45 F.3d 823 (4th Cir. 1995).
32. "[G]uided by the general principle that the Federal Rules are to be liberally construed, some courts have held that a motion for judgment under Rule 50(b) may be granted, despite the movant's failure to renew a previous motion under Rule 50(a) at the close of all the evidence, where the purposes of Rule 50 have been met in that both the adverse party and the court are aware that the movant continues to believe that the evidence presented does not present an issue for the jury."

    Moore's Federal Practice, 2d ed. 1994, ¶ 50.08, at 50-91 (footnote omitted). This statement does not appear in the third edition of *Moore's Federal Practice* (1997).
33. *Id.* at 828–829.
34. *Farley Transp. Corp. v. Santa Fe Trail Transp. Co.*, *supra*, and *Benson v. Allphin*, *supra*.

February 12, 2003

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Committee Report on Rule 30(b)(6)

By Gregory K. Arenson and James A. Beha II

Rule 30(b)(6) of the Federal Rules of Civil Procedure was introduced in 1970 to make specific changes in how information could be obtained from a corporation or other organization by deposition.[1] Where, previously, the examining party designated some officer or managing agent as the witness, taking the risk that the deponent might not have the desired information (and, incidentally, the risk that the person who did possess the information might not be an officer or managing agent whose testimony could "bind" the entity), Rule 30(b)(6) changed the process. The examiner's burden now is to identify by notice the topics on which testimony was sought with "reasonable particularity" (hereafter a "Notice"), at which point the burden shifts to the corporation to designate for examination one or more persons who would be prepared to convey the corporation's knowledge on the topics, speaking on behalf of the corporation (hereafter a "Corporate Witness").

This Report discusses the burdens on the examining party in terms of the specificity of the Notice and the obligation of the deponent corporation in terms of the preparation of the Corporate Witness. This Report also considers the proper scope of a Rule 30(b)(6) examination, particularly the extent to which it may be used to elicit contentions or trial positions of a corporate party, giving particular attention to the much-cited 1996 case of *United States v. Taylor*, decided by Magistrate Judge Eliason of the Middle District of North Carolina.[2] The Report also addresses the evidentiary significance of Rule 30(b)(6) testimony, the extent to which such testimony should be given preclusive effect, the attorney work-product issues that are often presented in the preparation and examination of a Rule 30(b)(6) witness, and current practice (as reflected in reported cases) with respect to the imposition of sanctions where the witness presented is unable to fulfill the testimonial duties imposed by the Rule.

The Report then sets forth a series of recommendations for practice under the Rule as well as a recommendation for amendment of the Rule to eliminate the use of such depositions as a device to discover legal arguments, contentions, and trial positions.

A. The Rule and An Overview of Common Practice Issues

Rule 30(b)(6) currently provides:

> A party may in the party's notice and in a subpoena name as the deponent a public or private corporation or a partnership or association or governmental agency and describe with reasonable particularity the matters on which examination is requested. In that event, the organization so named shall designate one or more officers, directors, or managing agents, or other persons who consent to testify on its behalf, and may set forth, for each person designated, the matters on which the person will testify. A subpoena shall advise a nonparty organization of its duty to make such a designation. The persons so designated shall testify as to matters known or reasonably available to the organization. This subdivision (b)(6) does not preclude taking a deposition by any other procedure authorized in these rules.

The Rule was adopted as "an added facility for discovery, one which may be advantageous to both sides as well as an improvement in the deposition process."[3] The Rule offers a streamlined procedure for extracting information that may be dispersed throughout a corporation, and, in practice, proves especially useful early in a case when locating particular information, identifying potential witnesses on particular points, or obtaining explanatory information about particular documents that may be essential to mapping out a pretrial plan. The requirement that the Corporate Witness *shall* "testify as to matters known or reasonably available to the organization" requires a well-prepared deponent, and thereby seeks to eliminate the prior situation in which an examining party had to proceed through a series of deponents who each professed that the person who knew the answer was someone else.[4] In complex cases, very specific Notices may also prove the only practicable method for extracting information about documents, policies or decisions that have emerged as significant in the case (such as accounting treatment of a particular event or a company policy), but for which individual deponents have not been knowledgeable or helpful. The burden on the corporation to produce a witness who "shall testify as to matters known or reasonably available to the organization" can be an invaluable tool for forcing a filling-in of blanks where memories seem to have failed the witnesses so far examined.

Anecdotal reports from practitioners indicate that Notices are often framed as seeking factual support for matter in the pleadings (e.g., "all facts that plaintiff contends support the allegations of paragraph x of the Complaint" or "the factual basis for defendant's asser-

tion of a defense of estoppel," etc.). Even where the Notice is not framed in evaluative terms, Corporate Witness responses (and witness preparation) in the context of a Rule 30(b)(6) deposition also constantly present issues about privileged communications and work product, since counsel handling the case typically has the most thorough knowledge of the facts.[5]

Occasionally, too, parties may seek to force a corporation to take a litigation position with respect to specific issues or events through the medium of a Rule 30(b)(6) deposition. Since the Corporate Witness must "speak" for the corporation on the designated topics to the extent information is "reasonably available" to the corporation, it is argued, the witness may be asked for the corporation's "position" on factual questions, including, where testimony from other witnesses at deposition has proven to be conflicting, which version of events the corporation credits.[6] (Q: I have presented you with the depositions of Witness One and Witness Two [both, say, former employees] with respect to the circumstances surrounding the denial of plaintiff's application for promotion. Which version of such events does the company adopt?)

Use of Rule 30(b)(6) to seek "positions" that might alternatively be sought by requests to admit or contention interrogatories effectively requires the corporation, through its witness, to map out litigation positions in an oral exchange with adversary counsel with only minimal assistance from counsel—who would have been heavily involved in framing responses to written discovery. Questions of specificity, scope and protection of work product are obviously interrelated: the more areas of inquiry and the more scope to ask about "positions," the more likely that counsel preparing a witness to answer "fully" will have to share not only factual information but counsel's assessment of the facts.

The *Taylor* decision and a number of others have approved the practice of seeking corporate "positions" from the Corporate Witness, often expressing a preference for compelling a corporation to speak through an individual employee rather than allowing counsel to present the corporation's position.[7] Other courts reject, or at least strongly disfavor, the use of a Rule 30(b)(6) deposition for this purpose, and Sinclair and Fendrich condemn the practice as a "very common misuse."[8] Although concerns about this practice may be mitigated by requiring very specific advance warning in the Rule 30(b)(6) notice, in the context of an ongoing deposition (and in the context of very strong judicial disfavor of instructions to a witness not to answer), counsel for the corporation—and the witness—can be at a great disadvantage in a factually complex case if such questions are permitted—a disadvantage several times compounded if the court treats the scope of Rule 30(b)(6) answers as preclusive of other evidence.[9]

Disputes about the use of Rule 30(b)(6) will surface in reported cases only in the context of motions to compel (or for sanctions), motions to preclude, or motions for protective orders.[10] Such cases will necessarily present a distorted view of practice under the Rule. Moreover, as some commentators have pointed out, analysis of decisions in such cases must sort out the court's general pronouncements about the Rule and the parties' obligations thereunder from the actual relief (including any sanctions) directed.

Common, often interrelated, subjects in such disputes include the following:

1. How specific must the Notice be, and to what extent may a Rule 30(b)(6) witness be examined on matters outside the scope of a designated topic?

2. Where the Corporate Witness lacks personal knowledge (or sufficient personal knowledge) on the designated topic for which the witness is proffered, how much preparation is required, particularly as to (i) details of information available somewhere within the corporation, and (ii) information that might be "reasonably available" if the corporation is required to obtain information from former employees or from third parties?

3. Must a witness be prepared when the information is available to the corporation only through the investigative work of counsel (including both work product and attorney-client communications from former employees); if a witness must be prepared, how can this be managed consistent with protection of attorney work product?

4. To what extent may the witness be asked to take a position for the corporation with respect to third-party testimony, to summarize the corporation's evidence on a particular point, to muster evidence in support of pleadings that have been framed by counsel, or to state the corporation's current "interpretation" of documents or events, or the like?

5. What should be the relationship of Rule 30(b)(6) questions and other discovery devices, particularly contention interrogatories?

Responses to these questions reflect a continuum of views, from a position that Rule 30(b)(6)'s central function is to provide reliable leads to the identity of persons with actual knowledge on the topic (and perhaps to provide specific factual information about corporate documents) to the position that Rule 30(b)(6) may be used to require the Corporate Witness to assemble all critical information about the corporation's case and

then to elicit corporate contentions and admissions limiting the proof at trial.

B. Particularity in the Notice and the Scope of the Examination

The requirement of *reasonable particularity* is the counterbalance to the corporation's duty of preparation and the role of the witness as spokesperson. When sanctions are sought for the shortcomings in the testimony of the Corporate Witness, courts are likely to start their analysis by testing the particularity of the Notice, concluding that if answers must be given "fully, completely, and unevasively" (the standard formulation), then "the requesting party must take care to designate, with painstaking specificity, the particular subject areas that are intended to be questioned, and that are relevant to the issues in dispute."[11]

It is perhaps not surprising that a number of courts have been asked to consider whether introducing the list of noticed topics with the phrase "including but not limited to" renders the entire notice defective. While perhaps the corporation's counsel could simply have announced that the list of topics would be deemed exclusive, courts have indeed stricken such notices.[12] This construction is necessary because, on the one hand, the corporation is only required to prepare the Corporate Witness with the "corporation's" knowledge with respect to noticed topics but, on the other hand, examiners generally are permitted to go beyond such topics where the witness has knowledge on other relevant matters.[13] The distinction generally made is that on such other lines of questioning the witness testifies in his individual capacity; the effect of such testimony depends on that capacity rather than the effect of this Rule.[14] Accordingly, counsel for the corporation properly insists that the notice be both reasonable and particular and during deposition may want to state positions as to whether a particular line of questions falls within the notice.[15] Thus, a Rule 30(b)(6) witness may be questioned on topics outside the scope of the Notice and thereby be required to give such information as the witness may have on such matters, but there is no duty to prepare the witness with the "corporation's" knowledge outside the enumerated topics.

A Rule 30(b)(6) Notice has been held unduly burdensome where it seeks a witness to identify relevant documents, and all nonprivileged documents that have already been produced. In Magistrate Judge Katz's felicitous phrasing:

> No Rosetta stone is necessary to unlock their mysteries. Defendant and his counsel can read them and determine which documents pertain to an allegation, and to what degree, directly or indirectly.[16]

Presumably a witness might still be required for authentication or to establish business record status, if not stipulated to, and a Rule 30(b)(6) examination might still seek additional information about specific documents, suitably identified in the Notice.

Requiring particularity also allows better consideration of the potential burden of the notice in the context of the litigation as a whole. The Rule does not set an express limit on the number of topics, but Rule 26 allows the court to limit all manner of discovery.[17]

The balancing of the variety of noticed topics and the burden of response takes on additional complications where there are presumptive limitations on the number of depositions.[18] The more complex the case, the more likely that different persons are the best source of information on particular topics, and the corporation may well prefer to designate several witnesses who have knowledge on different points rather than seek to prepare one witness for topics of which the witness is otherwise ignorant. On the one hand, the general rule has been that examination of multiple deponents produced in response to a single Rule 30(b)(6) notice is counted as one deposition. However, for purposes of the presumptive seven-hour time limit on a deposition[19] the Advisory Committee's position is that each witness supplied in response to a Rule 30(b)(6) Notice should be treated as a separate witness.

This situation provides an incentive for a corporation to prepare a single witness to be minimally adequate on all noticed topics (thus preserving the seven-hour limit), rather than provide several witnesses better qualified on different aspects of the Notice (thereby permitting the examiner multiples of seven hours for examination), an incentive which is inconsistent with the purposes of Rule 30(b)(6). Applying the presumptive seven-hour limit retains a meaningful restraint on the scope of the topics noticed, and it should not matter significantly to the examiner (who has, after all, chosen the topics) whether the corporation provides responsive information through one or more than one witness, so long as the witness is properly prepared as to the particular topic.[20] The examining party should, however, be allowed to reserve any unused time for subsequent Rule 30(b)(6) examinations.[21] Rule 30(d)(2) would still require the court to allow additional time whenever necessary "for a fair examination of the witness" or if the examination is impeded or delayed.

Finally on this point, the general practice appears to be that, where a witness is designated as a Rule 30(b)(6) representative and is also examined separately, the pre-

sumptive seven-hour limit applies separately to each portion of the examination.[22]

C. Sufficiency of Preparation of, and Performance by, the Corporate Witness

The Corporate Witness must be properly prepared by the corporation with the information reasonably available to the corporation. How do the courts assess the witness's performance—and by inference the sufficiency of preparation? A related question, addressed in a subsequent section, is what the consequences will be at trial if the corporation's counsel seeks to introduce evidence or arguments relating to the noticed topics which were not mentioned by the Corporate Witness.[23]

Although the rhetoric of the courts in setting out what is expected of the corporation and the Corporate Witness is stern and expansive, the decisions indicate that, with rare but important exceptions, the relief or sanctions ordered when the Corporate Witness falls short of the pronounced standards have been modest and mild. Sinclair and Fendrich exhaustively review cases under the Rule and repeatedly note that broad rhetoric is typically followed by narrowly focused, restrained relief. Where the witness is thoroughly unprepared to address noticed topics, courts may treat the situation as a failure to appear.[24] The case for sanctions may seem overwhelming in such circumstances, but even then, most reported cases seem to give the entity a second chance with only a warning so long as the witness adequately responded on at least some topics.

Review of reported cases suggests that the imposition of any procedural sanction other than ordering additional discovery has been rare. One court has commented:

> The Court should diligently apply sanctions under Rule 37 both to penalize those who have engaged in sanctionable conduct and to deter those who might be tempted to engage in such conduct in the absence of such a deterrent.[25]

Nonetheless, and notwithstanding the near-mandatory language of Rules 37(a)(4) and (d), Fed. R. Civ. P., monetary awards are quite uncommon. In some courts' view:

> In order for the court to impose sanctions, the inadequacies in a deponent's testimony must be egregious and not merely lacking in desired specificity in discrete areas.[26]

Where imposed at all, monetary awards usually are limited to either a modest allowance for the cost of the motion or some portion of the cost of unproductive time at the initial deposition.[27] Indeed, some reported monetary sanctions appear so light that it is difficult to imagine them serving as a deterrent,[28] and courts do not seem to have resorted at all to Rule 37(c), Fed. R. Civ. P. (allowing "other appropriate sanctions" for failures to disclose), in connection with unsatisfactory performances at Rule 30(b)(6) depositions.

Disputes about preparation of the witness tend to fall into three groups:

(1) whether the "most knowledgeable" witness must be produced and what remedies are available where the witness is sufficiently prepared to answer many of the questions posed but lacks information on some particulars;

(2) to what extent the witness must be prepared with information "reasonably available" to the corporation from outside sources, particularly former employees or existing discovery in the case; and

(3) how the preparation of the witness interplays with attorney work product and with privileges.

As Magistrate Judge Schenkier of the Northern District of Illinois advised practitioners in a recent article, "you can search high and low in Rule 30(b)(6) and not find a requirement that the corporation produce the 'most knowledgeable witness.'"[29] Indeed, there is no requirement that the corporation produce a witness with firsthand knowledge, even when it has one.[30] More generally, the examining party *cannot* select the witness to speak for and bind the Corporation by operation of Rule 30(b)(6) by naming a specific person in the Notice; the Rule plainly allows the corporation to select the witness to be tendered for these purposes.

What *is* required is that the witness have a sufficient grasp of the information available to the corporation to give responsive answers on the noticed topics. Where the court feels the corporation has not adequately prepared the witness, it may order a new examination with specific preparation mechanisms.[31] As the cases cited in the preceding footnotes demonstrate, however, if the witness can give responsive answers much of the time and point to other persons who can address very detailed questions, most courts will find that sufficient compliance; if the witness does well enough in most areas but lacks knowledge on a particular topic when the court considers the topic important and the record insufficient, a court is likely to direct production of an additional witness or the use of alternative discovery devices, but the court may well not impose any sanctions. Despite constant repetition of the "full" and "complete" tests, moreover, a number of decisions have denied sanctions and refused to order

additional preparation or a new witness where, although there were questions the witness could not answer, taking the deposition as a whole, the witness's knowledge on each topic appeared reasonably adequate and his testimony included leads about where more detailed information could be obtained.[32]

By the Rule's terms, the witness need only know of "matters known or reasonably available to the organization." What non-privileged information held by third parties or former employees is "reasonably available" to the corporation? Several cases indicate that if the only source of information on a topic is a former employee, the corporate designee must not merely provide that "lead," but attempt to gather the information from the employee. Indeed, a few cases suggest that if information pertaining to a topic has been made available elsewhere in discovery, in other depositions for example, the corporate designee must both be familiar with such testimony *and* be prepared to state the corporation's "position" with respect thereto (i.e., take a position as to the truthfulness, accuracy and completeness of the testimony). Several courts have stated that "reasonably available" information includes that which can be obtained from former employees.[33] This certainly implies that if the witness does not interview the former employees himself, he must be prepared with responsive information gathered by counsel.[34]

Cases recognize that even after exhausting what is "reasonably available," a corporation may have no information on topics counsel has included in the Notice, or have some information but be unable to answer as to some specifics. The resulting balancing act is demonstrated in an opinion involving discovery of the Iranian government:

> Iran has not proffered any witnesses regarding these items. If Iran is unable to locate, after a proper effort, any witnesses able to testify as to these issues, then so be it. However, the court may subject Iran to sanctions, such as a prohibition on the presentation of evidence on this issue, if Iran later discovers proper witnesses and fails to offer a sufficient explanation to the court. Accordingly, Iran should engage in a genuine and thorough effort to identify an adequate deponent with regard to these items.[35]

Setting the scope of "reasonable particularity" for the notice, on the one hand, and what is "reasonably available" to the corporation's witness (or witnesses), on the other hand, can take on an entirely different level of complexity when the information lies with third parties or former employees, or is "available" to the corporation solely through the investigations of counsel. Consider the following hypothetical posed by Sinclair and Fendrich:

> . . . assume that an entity has been noticed for a deposition under the Rule. The events giving rise to the claims, let us assume, are complex and involve the actions of any number of participants over a course of time. Assume further that the events which are central to the lawsuit occurred long ago, so that some number of the people who were agents of the entity are no longer under its control. Other participants in the events may be dead or missing. Still others are third parties who are not, and perhaps were never, under the control of the organization. Documents that bear upon the events are extremely voluminous, scattered, and often ambiguous—especially when their authors or recipients do not remember them, not to speak of when they are no longer available to interpret them. Counsel for the entity is now faced with the task of helping the client select and prepare one or more designees to testify on its behalf on what is "known or reasonably available" about the subjects which have been identified in a Rule 30(b)(6) notice.[36]

In such cases attorney work product is inevitably at risk, as may be privileged communications from former employees to counsel, since such information is in some sense "reasonably available" to the client. (We return to the subject of witness preparation and work product below in Part E).

This Report focuses on the use of Rule 30(b)(6) in discovery of a corporate party to a litigation, although much of the discussion about witness preparation, specificity, and privilege applies equally where the corporate deponent is a subpoenaed non-party. There is one distinction which should be noted at this point. Because the Corporate Witness testifies "on behalf" of the corporation, the deposition testimony is treated as admissible at trial against the corporation *even if* the testimony is given without direct personal knowledge (i.e., the witness is not personally competent but is conveying information supplied to the witness for purposes of the deposition).[37] What should be the admissibility of such incompetent or hearsay testimony gathered from a non-party corporation via Rule 30(b)(6)?

This question was presented very recently in the context of a summary judgment motion decided by Judge Casey, when the defendant moved to strike the testimony of a third-party Corporate Witness as not based on personal knowledge.[38] Judge Casey denied the motion to strike and referred to other decisions holding that a Rule 30(b)(6) witness is not required to have "personal knowledge on a given subject, so long as they are able to convey the information known to the corporation."[39] Judge Casey's opinion appears to be the only reported case on this point, and we must respectfully suggest that it is wrongly decided.

Cases certainly do routinely hold that the corporation may fulfill its Rule 30(b)(6) deposition obligations by providing a witness who can answer the pertinent questions but lacks personal knowledge. Hearsay testimony is obtained in all sorts of deposition contexts, however, and nonetheless will be admissible in court only if an evidentiary exception applies. Rule 30(b)(6) does not purport to create an evidentiary exception, although in almost all cases the fact that the corporate deponent is a party makes the testimony an evidentiary admission admissible *against that party* at trial. When the witness is not a party, however, or the testimony is otherwise offered against a party other than the corporation deposed (and thereby against a party that did *not* make the evidentiary admission), the rules about competence and hearsay should be applicable.

D. *Taylor* and the Trial Consequences of Rule 30(b)(6) Testimony

The decisions just discussed present a view of Rule 30(b)(6) as an exploratory tool of the examining party and focus on getting the examining party the information it reasonably needs. In this context, courts rarely consider what the consequences should be if the corporation seeks to offer at trial evidence not mentioned by its designee. Because that was one of the two considerations about Rule 30(b)(6) most famously discussed in *Taylor*, we turn now to a discussion of that case. Because so much is often made of *Taylor* as a seminal case on the application of this Rule, it is worth reviewing in considerable detail what actually happened in that case.

Union Carbide ("UCC") was a defendant in a CERCLA "Superfund" environmental clean-up case in which the government asserted that UCC was legally responsible both for its own contribution to the site's condition and for the conduct of a division, Grower Service, which had been sold years before the litigation commenced and as to which no current UCC employees had knowledge. Faced with a Notice from the government, UCC argued that it should only be required to provide its current internal corporate knowledge; to identify former employees who might have knowledge of earlier events; and to "leave it up to the government" to pursue that knowledge. UCC also sought to have the court rule in advance that UCC could call such witnesses (or others) at trial and argue from their evidence, even though the Corporate Witness had provided no information about the substance of such testimony.

Magistrate Judge Eliason held that it was UCC's obligation to gather all evidence reasonably available to it on the noticed topics, including information from past employees and information already available in discovery. Furthermore, Judge Eliason held that absent an explanation (such as later discovery of information despite initial due diligence), UCC would not be permitted to offer at trial evidence or argument, direct or rebuttal, on topics as to which its Corporate Witness had denied knowledge or not taken a position.[40] Thus, while most cases addressing Rule 30(b)(6) only consider whether the corporation has sufficiently "appeared" by a knowledgeable witness, Magistrate Judge Eliason took the further step of setting out a preclusive scheme that, absent explanation, limited the party's trial case to what was disclosed at the Rule 30(b)(6) deposition.

The Magistrate Judge expressly acknowledged that Rule 30(b)(6) testimony was not the equivalent of a judicial admission.[41] He cited earlier cases stating that a Rule 30(b)(6) witness must convey the "subjective beliefs and opinions" of the corporation and present its "opinion" on the noticed topics.[42] The Magistrate Judge also acknowledged that ascertaining a party's "position" might be handled by contention interrogatory and that deciding which method "is more appropriate will be a case-by-case factual determination."[43] Nonetheless the Magistrate Judge concluded that if a corporation

> wishes to assert a position based on testimony from third parties, or their documents, the designee still must present an opinion as to why the corporation believes the facts should be so construed. The attorney for the corporation is not at liberty to manufacture the corporation's contentions. Rather, the corporation may designate a person to speak on its behalf and it is this position which the attorney must advocate.[44]

Few would quarrel with the first basic premise of the *Taylor* opinion, that the information "reasonably available" to a corporation on a particular topic includes what can be learned from prior employees, whether in interviews or in deposition transcripts, at least where the notice has been sufficiently specific as to topic. But many would challenge the clear message that, within the confines of the Notice, the Corporate Witness must be prepared to recite every bit of evidence the party's attorney will offer and to explain and justify

every "position" counsel will take, even if such evidence was *never* known to the corporation until unearthed by counsel in discovery. That this was indeed how the Magistrate Judge viewed the situation is evidenced by the following response to UCC's argument that it could rely at trial on, or at least make arguments about, "the documents and testimony of others" where the Rule 30(b)(6) witness had offered "no knowledge or position":

> This suggested procedure assumes that the attorneys can directly represent UCC's interest on their own as opposed to merely being a conduit of the party. This, of course, is not true. If a corporation has knowledge *or a position* as to a set of alleged facts or an area of inquiry, it is its officers, employees, agents, or others who must present the position, give reasons for the position, and, more importantly, stand subject to cross-examination. . . . Otherwise, it is the attorney who is giving evidence, not the party.[45]

Most trial attorneys would not accept the proposition that they are "merely being a conduit of the party," but one can sense the point the Magistrate Judge was trying to make. Where most trial lawyers would surely disagree with the Magistrate Judge, however, is on the description of how the corporation's position will be presented at trial: most trial lawyers would agree that the corporation cannot call the Corporate Witness to testify as to topics or "positions" covered at the deposition outside the deponent's competent, personal knowledge. The corporation's counsel will have to call competent witnesses, and counsel will indeed present "positions" in the processes of briefing and jury presentations. Moreover, while the adversary may use the Rule 30(b)(6) testimony insofar as the Rules permit, we have located no case allowing the adversary to call the Corporate Witness at trial in order to cross-examine the witness about the hearsay bases for the "positions" taken.

As noted, *Taylor* did not introduce the reading of Rule 30(b)(6) as allowing questions about the corporation's "position." However, it arguably misread the earlier cases, and it surely did suggest that position-seeking be given a wider ambit than in any preceding case. Rule 30(b)(6) requires *testimony* and that testimony is supposed to convey educated corporate knowledge; nothing is said about "positions." The angry tone of the response by Sinclair and Fendrich suggests just how much is at issue in terms of how a case may be proved at trial:

> . . . there is no basis for imposing a requirement that the corporation take a "position" on all deposition testimony in a case. . . . [T]he proper mission of a deposition under the rule should be to provide the discovering party with advance warning about what persons within the entity know. It is not a device intended to provide *reactions to* or *assessments of* the myriad assertions in all depositions given by other witnesses . . .
>
> * * *
>
> There are obviously many cases in which there are competing and inconsistent pieces of evidence. The notion that when the corporation has no knowledge through employees and documents in its possession, custody, or control, the company must select from, say, three nonparty witnesses' versions of the events the one it adopts as its knowledge or position is glib at best. To require the deposition designee to consider adversary witness testimony as part of the corporation's knowledge base is even less defensible.[46]

To be fair, Magistrate Judge Eliason several times stated that a corporation is not obligated to take a "position" as to every "set of alleged facts or area of inquiry;" *his* position was only that if a corporation passed on a particular topic, it should not be allowed at trial to present evidence or argument on that topic. And in response to the Sinclair and Fendrich hypothetical, if the testimony of the three non-party witnesses concerns relevant conduct *of the corporation*, perhaps it is not unreasonable to require the corporation to take a "position" as to what it did or did not do that is informed by such evidence—although whether that position should be expressed in a deposition response or an interrogatory answer may be a different question.

Again, few would quarrel with the proposition that counsel should not be permitted to offer factual evidence on specific topics concerning the corporation's conduct where the deponent pleaded ignorance (e.g., Did the manager approve this advance? Who prepared this memorandum?) without a clear explanation why such information was not "reasonably available" to the corporation at the time of the deposition, or that it was only inadvertently omitted.[47] On the other hand, given the availability of contention interrogatories, it is difficult to see what purpose is served by limiting the scope

of trial evidence to what the Rule 30(b)(6) witness masters of the evidence, particularly evidence counsel expects to obtain from third parties who are not former employees, or limiting argument to "positions" taken by that witness on matters other than the factual characterization of the conduct of the Corporation. Nonetheless, in addition to the square holding in *Taylor*, several cases state in passing that the party will not be allowed to add information or "change its position."[48] Such blanket preclusive language appears inconsistent with the status of Rule 30 (b)(6) testimony as an evidentiary admission but *not* a judicial admission.[49]

There is an important distinction between the rules for interrogatory responses and those for depositions, moreover: the obligation to update the response. Rule 30(b)(6) imposes no obligations to follow up with information learned *subsequent* to the deposition, and many of these depositions occur at the early stages of a case. There is no provision for these (or other) depositions that is comparable to Rule 26(e)(2), Fed. R. Civ. P., dealing with the updating of responses to interrogatories, requests for production and requests to admit. Certainly, there could be disputes about whether the information had been "reasonably available" to the corporation at the time of the deposition, but there may be sound reasons why it was not.[50] A party may even conclude that the "position" taken by the witness was incorrect in light of subsequent information. This may be embarrassing at trial, but there appears to be no *requirement* that notice of the change of view be given (although one would expect that in practice something in the pretrial order would force disclosure).[51] A disclosure process (with *mea culpa*) is what Magistrate Judge Eliason put into place prior to resuming the Rule 30(b)(6) deposition process in *Taylor*—but perhaps, absent UCC forcing the issue early on, this would have been dealt with there too in the pre-trial order.

The more complex the case, the more dispersed the information, and the more mixed the matters of fact and law, the more difficult these questions become. We appreciate that many local rules, including S.D.N.Y. Local R. 33.3, place interrogatories about "claims and contentions" at the end of the case, whereas a litigant may feel it critical at an early stage in the case to nail down the bases for a particular claim by the adversary or to find out what position an adversary will take on a critical factual issue. This is not, we argue, a reason to allow questions at a Rule 30(b)(6) examination which, if propounded as interrogatories, would be deferred until the close of discovery; rather it is a good argument in the particular case for accelerating the use of interrogatories on those particular points.

There is, moreover, a bit of irony in the professed concern that trial counsel not be able to ambush an adversary at trial with evidence or arguments not revealed at the Rule 30(b)(6) deposition. As several courts have pointed out, there are several pretrial mechanisms for blunting this threat, including contention-type interrogatories and pretrial orders. The *real* unfairness lies in expecting a witness who lacks direct knowledge to retain comprehensive memory of, and accurately regurgitate in the context of oral questions and answers, all the witness has been told about a noticed topic in deposition preparation and perhaps also to handle questions, anticipated or unanticipated, about "interpretations," "opinions" or "positions" of the corporation in the litigation. At best, a miscue or misunderstanding becomes something that, once remedied, comes back as impeachment material, even though the witness had no direct knowledge and testified based on double hearsay. At worst, the statement has some preclusive effect.

Moreover, the practical reality is that it can be extremely difficult to put reasonable objections about scope (is the question within the notice or not, and therefore "binding" or not) or privilege before the court while a deposition proceeds, and it is usually easier to rule on the sufficiency of objections and answers (and perhaps give answers preclusive effect) when interrogatories have been carefully propounded and responsibly answered.

Many courts have adopted at least the language of Magistrate Judge Eliason's opinion in *Taylor*, and that case has been repeatedly cited and quoted in rulings on Rule 30(b)(6) issues.[52] For example, in one recent case Magistrate Judge Pittman wrote:

> The Rule 30(b)(6) designee does not give his personal opinions. Rather, he presents the corporation's "position" on the topic. Moreover, the designee must not only testify about facts within the corporation's knowledge, but also its subjective beliefs and opinions. The corporation must provide its interpretation of documents and events. The designee, in essence, represents the corporation just as an individual represents him or herself at a deposition. Were it otherwise, a corporation would be able to deceitfully select at trial the most convenient answer presented by a number of finger-pointing witnesses at the depositions. Truth would suffer.[53]

Magistrate Judge Pittman made similar statements about the scope of Rule 30(b)(6) in another case a few months later.[54] It should be noted that in neither of these cases did Magistrate Judge Pittman actually compel a corporate witness to take a "position," provide "subjective beliefs and opinions," or offer "interpreta-

tion of documents and events." In *Marvel*, a corporate witness was required to produce an additional deponent with knowledge relating to specific items about a subsidiary. In *AIA*, Magistrate Judge Pittman required a corporation to produce a Rule 30(b)(6) witness even though its "principal" had already been deposed, unless the corporation could show that "its corporate knowledge is no greater than that of its principals." However, other courts have followed similar language to the conclusion that "[g]enerally, inquiry regarding a corporation's legal positions is appropriate in a Rule 30(b)(6) deposition," at least where there are mixed "legal and factual component[s]."[55]

Such statements about the scope and use of Rule 30(b)(6) might be contrasted to these recent words from Judge Rakoff:

> In a nutshell, depositions, including 30(b)(6) depositions, are designed to discover facts, not contentions or legal theories, which, to the extent discoverable at all prior to trial, must be discovered by other means.[56]

This view finds strenuous support from Sinclair and Fendrich, who argue from analysis of the Advisory Committee Notes to the various 1970 amendments that the deposition device was a minor convenience being created to avoid unnecessary guesswork at the outset of a case when the party litigating against the entity may lack information as to which of many officers and employees has personal knowledge of topics relevant to the lawsuit.[57] Those authors contrast the discussion of this change in the 1970 Notes and related discovery reports to the "extensive discussion of the difficulties attending contentions in the Rule 33 amendments" considered and adopted at the same time, after "years of bickering over contention interrogatories," and concluded that, with nary a mention of contentions in the Notes to Rule 30(b)(6), the Committee could not have intended that oral depositions be used for this purpose.[58]

The corporation's "subjective beliefs and opinions" as these existed in connection with the controversy being litigated (e.g., evaluations of an employee, beliefs about the knowledge of the party with whom a contract was being negotiated, etc.) are themselves matters of fact at the time of trial. In the context just discussed, however, the discovery is directed to current beliefs, evaluation of the evidence of witness credibility or litigation positions. Rule 30(b)(6) should be amended to eliminate questioning of this sort, both because of the practical concerns discussed above and to protect attorney work product. This recommendation is discussed further after turning to the subject of work product.

E. Extent of Preparation—Work Product Considerations

Of course factual information possessed by corporate personnel is not privileged merely because it was communicated by counsel,[59] but often *only* trial counsel (or—very often—only trial counsel and the in-house attorneys with whom trial counsel is working) has gathered, and possesses, the information. It may well be that much of this factual information will eventually be disclosed in responding to interrogatories, but counsel in that context (i) only has to assist the client in responding to questions posed in advance, rather than having to prepare an otherwise uninformed witness with sufficient information to respond to a range of questions on a topic; and (ii) has the opportunity to craft good-faith responses, which minimize interference with privileges. Moreover, it is far more efficient to present the court with privilege issues in reviewing written responses to interrogatories than on the fly as oral questions are posed.

Rule 612(2), Fed. R. Evid., makes writings used prior to testifying "to refresh memory" discoverable "if the court in its discretion determines it is necessary in the interests of justice."[60] Assuming the Corporate Witness is not testifying from personal knowledge, one could argue that showing attorney work product (such as investigative or interview memoranda) *cannot* "refresh" his recollection. Some courts have opined that showing work-product documents to a Rule 30(b)(6) witness does not make those documents discoverable.[61] Certainly there would be an apparent unfairness in *requiring* counsel to educate the witness with the fruit of counsel's investigation and then holding that, by complying, counsel has waived protection for the work product used in the process.

If a Rule 30(b)(6) deposition is to be used to elicit "positions" on disputed issues of fact where direct corporate knowledge is limited, or to ascertain the "bases" for pleaded claims or defenses, particularity if the Notice becomes critical, because in practice the corporate witness (in a perversion of *Taylor*'s logic) must become the conduit for the attorney! As Sinclair and Fendrich note:

> In the case of litigation, the discovery and collation of what needs to be known is characteristically undertaken by lawyers. It is the lawyer who investigates the facts, reviews a mosaic of documents, weeds through recollections of participants in the central events, and then attempts to put together a coherent account of "what really happened."[62]

If the attorney is going to have to educate the witness not only on factual matters but also on "positions" the corporation will want to take at trial, attorney work product considerations will have to be parsed carefully. Requiring a very high level of specificity in the notice is reasonable in such circumstances to allow such considerations to be addressed in advance and to enable the court, if the corporate party seeks its aid, to determine whether the route of a contention interrogatory is preferable.

A number of decisions involving discovery of governmental agencies have denied Rule 30(b)(6) discovery of information gathered by attorneys or their investigators on behalf of the agency.[63] Private organizations, however, have been less successful in seeking protective orders on such grounds.[64] Sinclair and Fendrich question the assumption:

> that questions asking a witness about what facts she was aware of which supported a particular allegation in a claim or defense do not improperly tend to elicit the mental impressions of the entity's lawyers who participated in the preparation of the witness or advice to the company . . . [65]

Whether a fact "supports" a contention, claim, or defense is almost always a question that the witness can answer only by obtaining and revealing attorney work product. The Corporate Witness' view of what "supports" an allegation is almost certainly rooted in counsel's analysis of the case and counsel's selection of evidence and organization of issues. Addressing such questions to the witness is an "easy window into what the attorney for the entity thinks is important. . . ."[66] As one court pungently put it, either the attorney thought the fact important "or, presuming rationality, the attorney would not have communicated the fact to the client." [67]

The examining party is entitled to discover facts (whether or not, incidentally, those facts "support" a particular contention), but the examining party should not be able to force counsel to supply evaluative work product to the client or the client to reveal such work product in order to comply with Rule 30(b)(6). Hence, questions properly seeking facts should not be phrased in a manner that potentially calls for evaluative work product.

Questioning what "supports" a particular allegation or defense can usually be rephrased to reduce offense to the work-product protection while still eliciting the necessary factual information. Questions about "positions" or the legal significance of documents, however, really *are* seeking case strategies. By and large, to the extent trial counsel eventually decides to take certain positions *at trial*, such conclusions are discoverable before trial to avoid unfair surprise or "sandbagging." As Magistrate Judge Eliason recognized, however, there may be many factual or other issues as to which the corporation decides *not* to take a position at trial and therefore decides not to reveal counsel's analysis. Written discovery near the close of the process allows counsel to formulate "positions" or take a pass on an issue and live with the consequences. Oral depositions, and particularly such depositions early in the case, do not allow time for considered judgments before, what was work product, becomes a disclosed "position," and the deposition context makes it difficult in practice to seek the court's guidance on the line to be drawn. Other discovery tools provide a more balanced mechanism for spelling out claims and contentions, particularly if the responses are to have preclusive, or even impeachment, effect.

Rule 30(b)(6) should be amended to remove from the scope of such depositions questioning that evaluates the legal significance of facts, elicits positions or contentions, or pursues similar lines.[68] This change, coupled with greater flexibility in the timing of contention interrogatories where appropriate, will still permit appropriate and timely discovery of trial positions and contentions without the awkwardness, and potential prejudice, of pursuing such information in an oral deposition where the person who is charged with shaping trial strategy—the party's counsel—cannot properly assist the witness.

In the absence of such an amendment, questioning of this sort should be disfavored and permitted only where the nature of the questions had been clearly specified in the Notice so that the corporation's counsel will have had an opportunity to raise work product concerns with the court.

F. Recommendations

Our recommendations fall into four general categories: (a) notices and burden of preparation; (b) sanctions; (c) the use of Rule 30(b)(6) to elicit a party's "positions" in contradistinction to contention interrogatories; and (d) the potential preclusive effect of Rule 30(b)(6) testimony.

(a) Notices and Preparation

(1) Absent stipulation or order, all Rule 30(b)(6) examinations of a party should be treated as one deposition with a presumptive cumulative limit of seven hours, whether the corporation tenders one or multiple witnesses to respond on its behalf and whether only one or more than one

such deposition is sought during the course of discovery.

(2) When the phrase "including but not limited to" is used in a Notice, the words "but not limited to" should be deemed surplusage.

(3) The obligation of Rule 30(b)(6) witness preparation should not generally extend to the review of testimony or documents from other parties or non-parties unless these are from present or former employees or agents of the corporation. Notwithstanding this, the examining party should be permitted to direct attention in the Notice to specific testimony about, or documents concerning, the corporation's conduct.

(b) Sanctions

(4) Courts should impose meaningful sanctions where counsel (i) routinely instructs a deponent not to answer questions directed to factual information because the deponent learned the factual information from counsel, and (ii) where the Corporate Witness is ill-prepared to answer factual questions about a noticed topic for which the witness was tendered.

(c) "Positions" and Contentions

(5) Rule 30(b)(6) should be amended to insert the word "factual" before "matters" in the fourth sentence and thereby establish that such depositions should not be a vehicle for seeking discovery of legal arguments, "contentions" or "positions" that are not simply factual statements, but seek evaluations of the legal significance of facts. In order to allow parties timely disclosure of litigation positions or contentions, this change may require greater flexibility in allowing contention-style interrogatories at early stages of discovery, but this is preferable to allowing contentions to be explored by oral examination of a witness.

(6) Even in the absence of the proposed amendment, Rule 30(b)(6) notices should be stricken (and questions at such examinations should be deemed presumptively improper) as violative of the protection of attorney work product where it seeks evaluation of the evidentiary significance of factual information (e.g., "support," "prove," etc.), as it bears on a claim or defense. Examining counsel is entitled to full disclosure of factual information, but competent counsel can find many other avenues to elicit factual information relevant to a particular topic without framing questions that depend on the adversary counsel's evaluation of the facts.

(7) While Rule 30(b)(6) examinations may properly inquire about a corporation's "subjective opinions" insofar as these constitute facts relevant to the litigation, the use of this discovery mechanism for inquiring into litigation positions and the application of law to the facts conveyed, even in the absence of the proposed amendment, should be disfavored. In the absence of the proposed amendment, this should not preclude the examining party from specifically identifying in the Notice a factual issue on which the corporation's position or version of events is sought. Such advance specification allows the corporation, if it chooses, to offer alternative mechanisms of response (e.g., voluntarily tendering a statement to be treated as an interrogatory answer or response to written question) or to seek the court's intervention as to the discovery device.

(d) Preclusion

(8) So long as the court is persuaded that the Rule 30(b)(6) witness was properly prepared to provide responsive answers, Rule 30(b)(6) testimony generally should not be treated as preclusive with respect to either evidence or arguments. Rule 30(b)(6) testimony is not a judicial admission (and hence may be contradicted or rebutted), and the failure of a Corporate Witness to mention particular information, absent bad faith, should not be grounds to preclude the subsequent proffer of such information. Whether an omission was inadvertent or the evidence was only subsequently developed, the better view of a Rule 30(b)(6) deposition is that it is an exploratory tool, and other devices are better suited to limiting the evidence at trial. Notwithstanding this, because Rule 30(b)(6) testimony constitutes an admission, the omission of information or interpretations from a Corporate Witness's response may still be probative at times, e.g., to evidence when the corporation became aware of certain information or first took a certain position.

(9) If the Corporate Witness inadvertently omitted factual information that was reasonably available to the corporation at the time of the deposition, and this information is not otherwise disclosed during the discovery process (or if a court concludes that the omission or the extent of the delay in providing the information was a deliberate litigation tactic), the court should then consider preclusive sanctions under Rule 37(c), Fed. R. Civ. P., particularly where other parties have been prejudiced.

Endnotes

1. Rule 30(b)(6) applies to a variety of entities ("a public or private corporation, or a partnership, or association, or governmental agency"); we use "corporation" here as a shorthand. In 1971, Rule 30 was further amended to make clear that deposition discovery of third-party entities by subpoena would follow a parallel procedure.
2. *United States v. Taylor*, 166 F.R.D. 356 (M.D.N.C.) (Eliason, M.J.), *aff'd*, 166 F.R.D. 367 (M.D.N.C. 1996) ("*Taylor*").
3. Rule 30(b)(6) Advisory Committee's Notes (1970 Amendments).
4. *Id.* (referring to the practice as "bandying"). *See generally* Jerold Solovy & Robert Byman, *Discovery: Invoking Rule 30(b)(6)*, NAT'L L.J., Oct. 26, 1998, at B13 (arguing that if a witness is not properly prepared and lacks knowledge, which others in the corporation do have (e.g., as to what happened in a negotiation), the corporation should thereafter be bound by the professed lack of knowledge—in opposing summary judgment, for example.)
5. *See*, *e.g.*, *Protective Nat'l Ins. Co. of Omaha v. Commonwealth Ins. Co.*, 137 F.R.D. 267, 279–80 (D. Neb. 1989) ("*Protective Nat'l*") (although documents may be protected work product, a Rule 30(b)(6) witness must be prepared with "facts" contained in them and divulge such facts at deposition; questions as to which facts "support" particular allegations did not necessarily seek counsel's mental impressions, and a deposition rather than contention interrogatories was an acceptable method insofar as it addressed allegations that were not simply legal conclusions). *But see Am. Nat'l Red Cross v. Travelers Indem. Co.*, 896 F. Supp. 8, 13 (D.D.C. 1995) (in a complex case with extensive document discovery, requiring a description of documents that "support" affirmative defenses was barred by work-product doctrine).
6. *See* Kent Sinclair & Roger P. Fendrich, *Discovering Corporate Knowledge and Contentions: Rethinking Rule 30(b)(6) and Alternative Mechanisms*, 50 ALA. L. REV. 651, 699 (1999) ("Sinclair & Fendrich").
7. *See*, *e.g.*, *Canal Barge Co. v. Commonwealth Edison Co.*, 2001 WL 817853, at *2 (N.D. Ill. July 19, 2001) ("*Canal Barge*") ("Generally, inquiry regarding a corporation's legal positions are appropriate in a Rule 30(b)(6) deposition" (citing *Taylor*); although in some cases contention interrogatories may be the preferred method, in this case "there is both a legal and factual component to the interpretation of these contracts," so that a deposition was preferred); *Ierardi v. Lorillard, Inc.* 1991 U.S. Dist. LEXIS 11887, at *5 (E.D. Pa. Aug. 20, 1991) ("*Ierardi*") (with respect to documents, plaintiffs were "entitled to discover the interpretation [defendant] intends to assert at trial" and since such "interpretation" was factual, a Rule 30(b)(6) deposition was preferable to contention interrogatories).
8. Sinclair & Fendrich, 50 ALA. L. REV. at 700.
9. *See* Solovy & Byman, *supra* note 4 (arguing for this result). *Compare Taylor*, 166 F.R.D. at 365 (Rule 30(b)(6) testimony precludes additional evidence or argument absent showing of "extremely good cause" for omission from testimony) *with Arkwright Mut. Ins. Co. v. Nat'l Union Fire Ins. Co.*, 1993 U.S. Dist. LEXIS 1163, at *8 (S.D.N.Y., Feb. 4, 1993) (Francis, M.J.) ("*Arkwright*") (Rule 30(b)(6) testimony would not limit trial evidence since witness need not have "comprehensive" knowledge; contention interrogatories would be used to ensure full disclosure prior to trial).
10. Reported cases that consider the preclusive effect of Rule 30(b)(6) testimony appear to be extremely rare. The issue was presented in *Taylor* only because the corporation sought an advance ruling that its Corporate Witness's testimony would not limit the scope of proof and argument at trial.
11. *Prokosch v. Catalina Lighting, Inc.*, 193 F.R.D. 633, 638 (D. Minn. 2000) ("*Prokosch*").
12. *See*, *e.g.*, *Reed v. Nellcor Puritan Bennett & Mallinckrodt*, 193 F.R.D. 689, 692 (D. Kan. 2000). *See also Innomed Labs, LLC v. Alza Corp*, 211 F.R.D. 237, 240 (S.D.N.Y. 2002) (Ellis, M.J.). Wasteful disputes about such terminology might be avoided by a Local Rule deeming "but not limited to" to be surplusage for purposes of a Notice.
13. *See*, *e.g.*, *Detoy v. City and County of San Francisco*, 196 F.R.D. 362, 366–67 (N.D. Cal. 2000).
14. *See*, *e.g.*, *Primavera Familienstifung v. Askin*, 130 F. Supp. 2d 450, 551 (S.D.N.Y. 2001) (Sweet, J.) (corporation "not limited" by testimony of Rule 30(b)(6) witness on topic outside specifics of notice). There seems to be disagreement as to whether the binding effect of Rule 30(b)(6) testimony is simply that accorded any "officers, directors, or managing agents" of a corporation (whether or not the Corporate Witness is one), or is to some degree more preclusive. *See*, *e.g.*, *In re Vitamins Antitrust Litig.*, 216 F.R.D. 168, 174 (D.D.C. 2003) ("While the government submissions constitute admissions by Bioproducts, its Rule 30(b)(6) deposition is a sworn corporate admission that is binding on the corporation."); *but see In re Puerto Rico Electric*, 687 F.2d 501, 503 (1st Cir. 1982) (noting misconception that Rule 30(b)(6) testimony is conclusively binding). *See also* Sinclair & Fendrich, 50 ALA. L. REV. at 730; S.I. Schenkier, *Deposing Corporations and Other Fictive Persons: Some Thoughts on Rule 30(b)(6)*, LITIGATION, v. 29 note 2 (American Bar Ass'n, Winter 2003) 20, 62 (citing cases in both directions). *See also* discussion of *Taylor* in Part D below.
15. Counsel may also want to ensure in preparing the witness that counsel has only conveyed additional information to the witness with respect to the specific topics in the notice. Thus, if the questioner strays outside the notice the deponent may truthfully convey only such information as the witness already possessed. In one case, the notice called for "a witness to testify as to any statement of fact set forth in the amended complaint to which defendant has denied," and the court struck the notice for insufficient particularity. *Skladzien v. St. Francis Reg'l Med. Ctr.*, 1996 U.S. Dist. LEXIS 20621, at *2 (D. Kan., Dec. 19, 1996).
16. *United States v. Dist. Council*, 1992 U.S. Dist. LEXIS 12307, at *43 (S.D.N.Y., Aug. 14, 1992) (Katz, M.J.) ("*Brotherhood of Carpenters*").
17. *Cf.* Sinclair & Fendrich, 50 ALA. L. REV. at 682 (urging use of the "balancing and triage provisions of Rule 26 when considering the appropriate scope of burdens" on the corporation).
18. Rule 30(a)(2)(A).
19. Rule 30(d)(2).
20. An alternative, counting examination of multiple Rule 30(b)(6) witnesses provided in response to a single Notice as multiple depositions, each of a presumptive-seven hour length, would encourage tactical maneuvers by the corporation to eat into the presumptive ten-witness limit of Rule 30(a)(2)(A). A balance must be struck here, and the one presented in the text seems preferable.
21. It is often good practice to seek additional Rule 30(b)(6) examinations at later stages in a case where very specific questions about documents or events have not been resolved by other witnesses.
22. *See*, *e.g.*, *Sabre v. First Dominion Capital L.L.C*, 2001 U.S. Dist. LEXIS 20637, at *4 (S.D.N.Y., Dec. 12, 2001) (Pittman, M.J.).
23. *Cf.* Rule 37(c), Fed. R. Civ. P. (failures to disclose).
24. *See*, *e.g.*, *Resolution Trust Corp. v. Southern Union Co.*, 985 F.2d 196 (5th Cir. 1993).
25. *T&W Funding Company XII, L.L.C. v. Pennant Rent-a-Car Midwest, Inc.*, 210 F.R.D. 730, 733 (D. Kan. 2002) (affirming award of both motion costs and expenses of new deposition).

26. *Zappia Middle East Constr. Co., Ltd. v. Emirate of Abu Dhabi*, 1995 U.S. Dist. LEXIS 17187 at *25–26 (S.D.N.Y., Nov. 17, 1995) (Francis, M.J.).

27. *See*, *e.g.*, *In re Vitamins Antitrust Litig.*, 216 F.R.D. at 174–75 (costs of motion); *Mattel, Inc. v. Robard's Inc.*, 139 F. Supp. 2d 487, 498 (S.D.N.Y. 2001) (ordering an additional deposition and awarding expense of motion); *Arctic Cat, Inc. v. Injection Research Specialists, Inc.*, 210 F.R.D. 680, 683–84 (D. Minn. 2002) (small portion of costs of first deposition). However, in *Turner v. Hudson Transit Lines, Inc.*, 142 F.R.D. 68, 78–80 (S.D.N.Y. 1991), Judge Leisure awarded full motion costs plus the time and expense of the initial deposition and made counsel jointly liable with the client for payment of the sanctions.

28. *See*, *e.g.*, *Koken v. Lederman*, 2001 U.S. Dist. LEXIS 628, at *1 (E.D. Pa., Jan. 22, 2001) ($350 sanction for wrongfully terminating Rule 30(b)(6) deposition when questioning was proper).

29. Schenkier, *supra* note 14, at 20.

30. Solovy & Byman, *supra* note 4. *See Gucci America Inc. v. Exclusive Imports Int'l*, 2002 WL 1870293, at *10 (S.D.N.Y., Aug. 13, 2002) (Casey, J.) (upholding Magistrate Judge Maas's determination that, where a witness was "marginally adequate," plaintiff was not required to produce a witness with actual knowledge); *Cruz v. Coach Stores, Inc.*, 1998 U.S. Dist. LEXIS 18051, at *17 (S.D.N.Y., Nov. 18, 1998) (Rakoff, J.) (finding that rule requires prepared witness, not one who is "most knowledgeable"). *But see Reilly v. Natwest Mkts. Group Inc.*, 181 F.3d 253, 268–69 (2d Cir. 1999) (although defendant produced a Rule 30(b)(6) witness, it was proper for the trial court to preclude testimony from other witnesses not produced in response to a Notice).

31. *See*, *e.g.*, *Federal Deposit Ins. Corp. v. C.H. Butcher*, 116 F.R.D. 196, 201–202 (E.D. Tenn. 1986) (FDIC to redesignate witnesses and provide them as part of their preparation with responsive documents including extensive investigative memorandum); *Paul Revere Life Ins. Co. v. Jafari*, 2002 U.S. Dist. LEXIS 5594, at *8 (D. Md., Mar. 28, 2002) (ordering new deposition at plaintiff's expense).

32. *Cf. Equal Opportunity Comm'n v. Am. Int'l Group, Inc.*, 1994 WL 376052, at *3 (S.D.N.Y., July 18, 1994) (Ellis, M.J.) (Rule 30(b)(6) examination is not a "memory contest"); *Barron v. Caterpillar Inc.*, 168 F.R.D. 175, 178 (E.D. Pa. 1996) (in absence of bad faith, shortcomings would be handled by other discovery devices); *United States v. Mass. Indus. Fin. Agency*, 162 F.R.D. 410, 412 (D. Mass. 1995) ("*Massachusetts Finance*") (same).

33. *See*, *e.g.*, *Bank of New York v. Meridian Biao Bank Tanzania, Ltd.*, 171 F.R.D. 135, 151 (S.D.N.Y. 1997) (sources for matters reasonably available include "documents, past employees, or other sources"); *Prokosch*, 193 F.R.D. at 639. Several cases raise the threshold by stating that witness preparation on noticed topics must include prior fact witness deposition testimony, although—except in *Taylor* itself—results do not seem to turn on whether preparation went that far.

34. *See Calzaturficio S.C.A.R.P.A., s.p.a. v. Fabiano Shoe Co., Inc.*, 201 F.R.D. 33, 37 (D. Mass. 2001) (reciting that requirement).

35. *McKesson Corp. v. Islamic Republic of Iran*, 185 F.R.D. 70, 81 (D.D.C. 1999) ("*Republic of Iran*").

36. Sinclair & Fendrich, 50 ALA. L. REV. at 699 n.259.

37. In substance, the deposition testimony is treated as an evidentiary admission of the corporate party (but not a judicial admission). *See* note 41 below for discussion.

38. *Gucci America, Inc. v. Ashley Reed Trading Inc.* 2003 WL 22327162 (S.D.N.Y., Oct. 10, 2003).

39. *Id.*, 2003 WL 22327162 at *3 (internal citation omitted).

40. The opinion does not provide much information about the content or particularity of the Notice.

41. The court described it as "a statement of the corporate person which, if altered, may be explained and explored through cross examination," but noted that the designee could make admissions against interest "which are binding on the corporation." *Taylor*, 166 F.R.D. at 361 n.6. In many cases (including *Taylor*) the use of the term "binding" only heightens confusion, since the testimony of a corporate designee under Rule 30(b)(6) is *already* admissible as the statements of an officer or managing agent; whether such are evidentiary admissions "against interest" (Fed. R. Evid. 804(b)(3)) would seem to be beside the point. *See also Industrial Hard Chrome, Ltd. v. Hetran Inc.*, 92 F. Supp. 2d 786, 791 (N.D. Ill. 2000) (Rule 30(b)(6) testimony "is not a judicial admission that ultimately decides an issue"; it can be both contradicted and used for impeachment); *W.R. Grace v. Viskase Corp.*, 1991 WL 211647 at *2 (N.D. Ill., Oct. 15, 1991) (Rule 30(b)(6) testimony is an evidentiary, not a judicial, admission and may be contradicted).

42. *Id.* at 361. *Taylor* cited *Lapenna v. Upjohn Co.*, 110 F.R.D. 15, 20 (E.D. Pa. 1986), for the proposition that a Rule 30(b)(6) inquiry could reach the corporation's "subjective beliefs and opinions," but the comment in *Lapenna* is an abbreviated aside and does not make clear whether this means relevant beliefs and opinions held in the context of the initial dispute (e.g., what did Y's supervisor think of Y's job performance) or opinions reached in the litigation (e.g., which witness is telling the truth). *Ierardi* is cited for the proposition that the corporation "must provide its interpretation of documents and events," but in fact *Ierardi* said merely that when the defendant argued that a document "could be interpreted in different ways . . . plaintiffs are entitled to discover the interpretation [defendant] *intends to assert* at trial" 1991 U.S. Dist. LEXIS 11320, at *5 (emphasis added). Finally, although *Massachusetts Finance* is cited for the proposition that a Corporate Witness must provide the corporation's "position," the case does not stand for that proposition and used the term "position" only when ordering a defendant to "clarify its position in response to certain interrogatories." 162 F.R.D. at 412.

43. 166 F.R.D. at 362 n.7.

44. *Id.* at 361–62.

45. *Id.* at 362–63 (emphasis added).

46. 50 ALA. L. REV. at 694–95 (emphases in original).

47. An interesting variation on this point is presented in *Newport Elect., Inc. v. Newport Corp*, 157 F. Supp. 2d 202, 219–20 (D. Conn. 2001). There, the corporate defendant opposed summary judgment with an affidavit from the person who had been its Rule 30(b)(6) designee; the affidavit supplied information on topics of which, at the deposition, the witness said he lacked knowledge. The court cited the Second Circuit practice that on a Rule 56 motion a material issue of fact cannot be created by affidavit testimony that contradicts the affiant's previous deposition testimony; and concluded that the Rule 30(b)(6) witness "was not at liberty to delay reviewing information on these topics until after the deposition" and later contradict his then-proffered lack of knowledge.

48. *Canal Barge*, 2001 WL 817853, at *2; *Ierardi*, 1991 WL 158911, at *8. *See* Solovy & Byman, *supra* note 4 (arguing that where information available to a corporation is omitted by a Corporate Witness the corporation should be prevented from offering other testimony on the point). By contrast, in *Massachusetts Finance* the court ruled that the defendant would be allowed at trial to present "its position through witnesses who have already been deposed by the United States," even though the deponent apparently had not "sorted out" that testimony. 162 F.R.D. at 412. In *Arkwright*, Magistrate Judge Francis concluded that the testimony of a sufficiently prepared Rule 30(b)(6) witness would not limit the corporation's presentation of evidence at trial because the witness need not have "comprehensive" knowledge; other discovery devices could be used to nail down the

corporation's positions prior to trial. 1993 U.S. Dist. LEXIS 1163, at *8. *See also In re Ind. Serv. Org. Antitrust Litig.*, 168 F.R.D. 651, 654 (D. Kan. 1996) (discovering "supporting facts" and marshalling proof not an appropriate use of Rule 30(b)(6); any legitimate discovery interests best accommodated by other methods).

49. See cases cited at note 41.

50. *Cf. Republic of Iran*, 185 F.R.D. at 81, where the court warned of potential sanctions "if Iran later discovers proper witnesses and fails to offer a sufficient explanation" as to why these witnesses had not been consulted "in a genuine and thorough effort" to respond to the Notice.

51. In *Otis Eng'g Corp. v. Trade & Dev. Corp.*, 1994 U.S. Dist. LEXIS 3132, at *2–3 (E.D. La., Mar. 16, 1994), the Corporate Witness was the lead design engineer, a person with knowledge. Some months after her testimony, Otis informed defendant of a change in her view about the cause of the machine failure. Denying a motion to preclude the deponent from offering testimony at trial that differed from the deposition, the court held that the trier of fact should deal with credibility; the witness could be impeached with her prior testimony, but would not be precluded from changing it.

52. By contrast, the actual remedy adopted in that case—barring a corporation from offering evidence obtained from third parties in counsel's trial preparation to the extent such evidence was not disclosed at the Rule 30(b)(6) deposition absent an *in limine* showing of good cause—does not appear to have been adopted by other courts. Sinclair and Fendrich describe *Taylor* as "setting a record for expansive reading of the rule." 50 ALA. L. REV. at 746.

53. *A.I.A. Holdings, S.A. v. Lehman Brothers, Inc.*, 2002 U.S. Dist. LEXIS 9218, at *15–16 (S.D.N.Y., May 20, 2002) (citations omitted).

54. *Twentieth Century Fox Film Corp. v. Marvel Enter. Inc.*, 2002 U.S. Dist. LEXIS 14682, at *6–7 (S.D.N.Y., Aug. 6, 2002).

55. *Canal Barge*, 2001 WL 817853 at *2.

56. *J.P. Morgan Chase Bank v. Liberty Mut. Ins. Co.*, 209 F.R.D. 361, 362 (S.D.N.Y 2002).

57. 50 ALA. L. REV. at 718.

58. *Id.*

59. *Upjohn Co. v. United States*, 449 U.S. 383, 395–96 (1981). Sinclair & Fendrich, 50 Ala. L. Rev. at 719; Wright, Miller & Marcus, Federal Practice and Procedure: Civil 2d § 2023 at 330–33 (1994) (collecting cases).

60. The House Judiciary Committee wrote that it intended "that nothing in the Rule be construed as barring the assertion of a privilege with respect to writings used by a witness to refresh his memory." Notes of the Committee on the Judiciary, H.R. Rep. No. 650, 93rd Cong., 1st Sess. 8 (1973), *reprinted in* 1974 U.S. Code Cong. & Admin. News 7051, 7086.

61. *See, e.g., Federal Deposit, Ins. Corp. v. Butcher*, 116 F.R.D. at 200. *Butcher* appears consistent with the cases that hold generally that attorney work product communicated to a witness, including the selection of documents, is not discoverable—although, it bears repeated emphasis, factual information that thereby becomes known to the witness will be discoverable. *See, e.g., Sporck v. Peil*, 759 F.2d 312 (3d Cir. 1985) (selection of documents); *Ford v. Philips Electrs. Instruments Co.*, 82 F.R.D. 359 (E.D. Pa. 1979) (may obtain witness knowledge but not counsel's impressions or evaluation of significance of facts); *but see, e.g., James Julian, Inc. v. Raytheon Co.*, 93 F.R.D. 138, 144, 146 (D. Del. 1982) (binder of selected documents used to educate company's witnesses discoverable; work-product protection waived), and Sinclair & Fendrich 50 ALA. L. REV. at 7226 ("the argument exists that the examining counsel has a basis for requesting to know what material was reviewed").

62. 50 ALA. L. REV. at 656.

63. *SEC v. Rosenfeld*, 1997 U.S. Dist LEXIS 13996, at *6 (S.D.N.Y., Sep. 10, 1997) (Patterson, J.) (where examinations of a Rule 30(b)(6) deponent prepared by SEC legal staff would reveal counsel's "legal and factual theories as regards the alleged violations . . . and their opinions as to the significance of documents," work product protection should be afforded); *SEC v. Morelli*, 143 F.R.D. 42, 47–48 (S.D.N.Y. 1992) (Leisure, J.) (Notice impermissibly sought attorney work product when it "intended to ascertain how the SEC intends to marshall the facts" and defendant sought to discover inferences SEC believes "properly can be drawn from the evidence it has accumulated"); *Brotherhood of Carpenters*, 1992 U.S. Dist. LEXIS 12307 at *43. *But see Federal Deposit. Ins. Corp. v. Butcher*, 116 F.R.D. at 200 (if only way to prepare FDIC deponent was to use protected investigative memoranda, FDIC nonetheless must prepare a witness and prepare that witness to answer "fully").

64. *See, e.g., Protective Nat'l*, 137 F.R.D. at 280 (appropriate to ask deponent for facts learned from counsel); *In re Vitamins Antitrust Litig.*, 216 F.R.D. at 172 (corporation obligated to educate witness on facts even if facts are in documents that are attorney work product).

65. 50 ALA. L. REV. at 720.

66. *Id.*

67. *Protective Nat'l*, 137 F.R.D. at 280.

68. Again, opinions or evaluations that existed in connection with the events being litigated (such as employee evaluations) are facts in the context of the later litigation.

February 12, 2004

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DVD/VIDEO REVIEW:

Preparing the Lay Witness for Deposition

With David A. Sonenshein and John Chesney
National Institute for Trial Advocacy, 114 Minutes, DVD or Two Videotapes

Reviewed by Michael S. Oberman

If a picture is worth a thousand words, how many words should a two-hour DVD be worth? It is precisely this sort of question that led me to major in history rather than in math—but it is a question that I must confront to complete this review.

NITA has released on DVD a program called *Preparing the Lay Witness for Deposition*, originally issued in 2002 on videotape. The running time is close to two hours. The program features David A. Sonenshein, Professor of Law at Temple University, and John Chesney, a partner at Drinker Biddle & Reath. Included with the DVD or videotapes is a 57-page, double-spaced brochure called "Video Support Materials."

The program focuses almost entirely on the standard instructions given to a lay witness in deposition preparation. As listed in NITA's press release, the subject areas include:

- "A general description of the deposition process, the physical setting and basic rules
- Explaining the goals of the witness
- The theory of the case
- Objections, instructions and lawyer's tricks
- Correcting errors in testimony
- Consulting with your lawyer during the deposition
- How to handle documents
- Covering a witness's personal history
- Redirect examination
- 'Moot court' practice time"

The program offers both demonstrations of how to prepare a witness and commentary about witness preparation, in alternating segments. It is a filmed CLE presentation, not an interactive product. Sonenshein plays the part of a lawyer preparing a witness. There are about a dozen separate scenes set in a conference room, showing Sonenshein in shirtsleeves meeting with a witness. After the demonstration of a topic (e.g., how to handle documents), Sonenshein and Chesney—sitting side-by-side in what appears to be a reception area—give pointers on how to cover that topic with a witness as a reinforcement and an amplification of what the demonstration teaches.

As the lawyer preparing the witness in the mock vignettes, Sonenshein is an excellent role model. He comes across as confident, courteous, approachable, articulate and attentive to the witness. The standard witness instructions are provided with great clarity. They include helpful guidance on how to testify at a videotaped deposition. Sonenshein ably shows how to engage the witness in the preparation session, both by maintaining a pleasant demeanor and by asking the witness about any concerns she might have about the upcoming deposition.

Sonenshein's treatment of each topic with the witness is extremely thorough: the viewer will surely take away all that might be said to a witness about a particular topic. Yet—as recommended in the course brochure—attorneys who try to follow this program might want to condense some of the instructions, for the mock discussion of the topics takes in the aggregate about an hour.

What the vignettes do not include is the substance of witness preparation. While the program begins with a case hypothetical, the facts of the case are incidental to the demonstrations. This program does not show, for example, how to help a witness deal with the difficult contents of a particular document (as opposed to showing us how to tell the witness to read a document before answering questions). Nor does the program demonstrate how to help a witness give nuanced answers (by drawing on details of a case). This program is pure and simple "Deposition Preparation 101"—witness preparation guidelines. I do not mean to minimize the importance of these guidelines, but I do mean to say that the presentation of these guidelines is often not the most important part of witness preparation. Because the vignettes do not focus on the facts of the hypothetical case, neither the demonstrations nor the commentary reaches the often challenging strategy and ethical issues inherent in preparing a witness to testify about what occurred.

The commentary by Sonenshein and Chesney, coming between each vignette, tells the viewer what Sonen-

shein was attempting to accomplish with the witness. This helps nail down the points to be absorbed. There are some useful suggestions in how to deal with different witnesses. Chesney explains, for example, that it is often more difficult to get a senior executive (as opposed to a lower-level corporate employee) to accept the need to answer questions by saying "I don't know" or "I don't recall" and to accept that his role is not to try to win the case in the deposition—placing the executive in a role at variance with the command position he occupies on a daily basis.

There are a few times where I think the commentary teaches a better lesson than the demonstration. Sonenshein tells us in the commentary that it is helpful to teach a witness how not to volunteer by framing an example from the facts of the case, to make the example memorable. On the other hand, in the demonstration, the question Sonenshein uses is, "Where did you go to college?" The witness says: "I got an associate's degree from NITA Community College in 1982." The witness is kindly chided for volunteering the year of graduation. As suggested in the commentary, I think a witness is better assisted by showing how excessive information related to the merits of the case could lead to extended questioning, rather than focusing on a piece of background information which the witness probably shares in her actual life outside the deposition room.

The commentary also includes important reminders about trends in litigation. In one mock session, Sonenshein takes the witness through every imaginable objection that he might make at the deposition, explains the reason for that type of objection, and expressly and repeatedly tells the witness how the statement of the objection at the deposition (e.g., objection; lacks foundation) will provide a clue for the witness. The brochure explains that this detailed discussion of the grounds for objections is now needed since "speaking objections" are generally prohibited. The commentary cautions that, in some jurisdictions, even the statement of the basis for objections—which might serve to coach a witness—is no longer permitted. Similarly, the commentary admonishes attorneys to check local rules to determine whether it is permissible to speak to the witness about the substance of the testimony during the course of the deposition, since some rules now prohibit any substantive discussion, even during breaks or overnight, once the deposition has begun and until it is concluded. The commentary does not go on to explain how these recent trends affect the overall process of witness preparation—such as the heavier burden on the role of preparation when consultation during the deposition is prohibited.

The commentary in the program largely matches the text of the brochure, and I did not find that the oral presentation was more effective than the written word. In part, this relates to the production of the video. The background set for the commentary has an oversized oriental vase separating Sonenshein and Chesney, which sometimes appears as the focus of the picture. And the way Sonenshein and Chesney are positioned side-by-side interferes with any sense of a free-flowing conversation between them. While the camera shows Chesney talking on the left side of the screen, for example, the camera also catches Sonenshein on the right side of the screen nodding vigorously and, at least to me, excessively. Sonenshein and Chesney also repeat each other too often; the brochure is more concise (except for a surplus of footnotes).

The DVD or videotapes cost $400, which is expensive for training materials on deposition conduct. But one factor offsets the price: attorneys eligible to receive CLE credit for self-study can earn 2.2 credits for completing this program, and NITA will sign certificates for no extra cost for each firm lawyer who completes the program. Although the DVD format does permit the viewer to quickly get to any desired topic from the main menu, the DVD has none of the special features that are now common on movie DVDs. For example, the DVD could contain the program as videotaped with the commentary, and a separate version of the preparation sessions presented in sequence without the commentary. In this way, a viewer could read the brochure and watch or re-watch all or some of the demonstrations without having to fast-forward or scroll past the commentary.

Is this video program worth more than a standard text on witness preparation? Words in a handbook can only tell a lawyer how to conduct a witness preparation; a video program allows the lawyer to see how it is done. For a lawyer who has had no chance to observe a more experienced lawyer prepare a witness, this program should provide a useful teaching tool. For the novice deposition defender, the DVD is worth more than a deposition handbook. For more experienced attorneys, an article on pointers for deposition preparation would be a more efficient way of obtaining the few nuggets of information that might be new and of interest to veteran litigators.

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BRIEFLY NOTED:

Taking and Defending Depositions

By Stuart M. Israel
American Law Institute—American Bar Association, 2004, 321 Pages

Reviewed by Michael S. Oberman

ALI-ABA has just released into the crowded field of deposition "how-to" books a new title, *Taking and Defending Depositions*, by Michigan lawyer and mediator Stuart M. Israel. According to its forward, "*Taking and Defending Depositions* is an easy-to-read, handy guide for anyone who litigates. This book will help all lawyers—from recent law school graduates and trial practice novices to more seasoned pros—succeed in handling depositions . . . Stuart Israel gives real-world advice concerning depositions and practical guidance about how to avoid common errors. Readers will particularly benefit from his detailed lists." Does the book deliver on the promises of its forward?

1. The book is easy to read; I completed its 252 handbook-sized pages of text during part of a transcontinental flight. However, I found one facet of its style to be distracting (although others might be amused): Israel too often injects jokes in the middle of practical advice. For example, in writing that the deposition of a party may be used at trial for any purpose under Fed. R. Civ. P. 32(a)(2), he adds: "Well, not quite *any* purpose—you can't roll up the transcript and smack a party, as much as he may deserve it." (P. 21). Similarly, in discussing what circumstances might warrant additional time above one day of seven hours, Israel offers the following: "[J]ust to prime the pump, I suggest they may include earthquakes, tsunamis, terrorism, pestilence, locusts, and sewer back-up." (P. 66).

2. I would not recommend this book as my first choice to "recent law school graduates and trial practice novices." For a basic how-to manual with extensive practical guidance, I continue to prefer *The Deposition Handbook—Fourth Edition*, by Dennis R. Suplee and Diana S. Donaldson (reviewed in *NYLitigator,* Winter 2003 at 28). Many of the chapters in *Taking and Defending Depositions* appear to be stand-alone articles presenting a compilation of points—such as "Seventeen Deposition Objectives" and "Nine Advantages and Five Drawbacks of Depositions." *The Deposition Handbook* does a better job of taking the reader's hand and walking him through each step of a deposition, and it provides citations to cases and secondary authorities. Some parts of Israel's book are too advanced for a beginner (e.g., a lengthy exploration of memory and truth, drawing on the writings of psychologists). However, a young lawyer would do well to read Chapter 11 ("Taking Depositions (Part 1)—Organization and Mechanics, Client Participation, and Beginning Depositions") and Chapter 12 ("Taking Depositions (Part 2)—Questions, Transcript Awareness, Objections, Problem Witnesses, And Ending Depositions") of Israel's book, which provide a very good introduction in narrative form and "real-world advice" on how to prepare for and then conduct a deposition.

Nor would I recommend this book to the most experienced litigators. For a book published in 2004, *Taking and Defending Depositions* virtually ignores important practice challenges with which veteran lawyers are currently grappling, such as the most effective use of synchronized videotaped depositions and transcripts at trial; the evolving law on Rule 30(b)(6) depositions; and the implications of court rules limiting the phrasing of objections or conferring with a witness during a deposition.

There is, on the other hand, a large group to whom I would recommend this book: litigators who are skilled in the basics and are stretching to master the art of taking or defending a deposition. For this group, Israel's compilations of points might click. And sections of the book present with clarity and insight subjects that any seasoned litigator must consider. In particular, Chapter 7 ("Truth, Memory and the Ethical Boundaries of Coaching") and Chapter 8 ("Witness Anxiety") warrant close study—articles about aspects of deposition practice that are always present but are less-often treated with equal sophistication in "how-to" deposition guides.

3. This brings me to the "detailed lists": Israel gives us most notably "The 162 Essential Rules for Deponents" as well as "Sixty-Seven Suggestions for Defending Discovery Depositions." Those who enjoy Israel's jokes might appreciate how he slices standard witness guidelines into 162 pieces and then follows with an explanation of why he omitted from the list "Do not spit tobacco juice into a Styrofoam cup while testifying." (P. 148). The lists surely give a litigator enough to work with, but I found the length of the lists excessive for sharing with a witness or even for use as a checklist. Certain items provide insufficient guidance (e.g., "33. Don't volunteer. 34. When appropriate, volunteer."), while others are simply overwritten (e.g., "45. Give short concise answers. Don't be long-winded, prolix, otiose, or pleonastic. Eschew the superfluous, extraneous, duplicative, redundant, superrogatory, and unnecessary. Be succinct. Be brief."). The DVD *Preparing the Lay Witness for Deposition* (see the review on page 86 in this issue) is a better guide for less-experienced litigators on how to teach a witness the standard guidelines.

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BOOK REVIEW:

Electronic Discovery and Evidence

By Michael R. Arkfeld
Law Partner Publishing, 2003, 418 Pages

Reviewed by Heather Kamins

Surely by now every litigator grasps the make-or-break impact a smoking-gun e-mail can have on a case. Think Microsoft, Monica Lewinsky and Arthur Andersen. But finding that e-mail amid the haystack of messages a company sends and receives each day or protecting your clients in the face of such an inflammatory e-mail can be a harrowing task given that current evidentiary rules have yet to adjust to accommodate the electronic age.

Discovering electronic evidence may be an especially daunting task for the novice computer user still skeptical that sent e-mail will arrive at its designated destination. It is these computer-green litigators who stand to benefit most from Michael R. Arkfeld's new practice manual, *Electronic Discovery and Evidence*, which the author markets as a resource in navigating the uncharted territories of electronic discovery.

The book's forward offers no promises, but plainly sets forth the challenges litigators face in discovery now that "we have changed from a paper-based to an electronic-based information society." Arkfeld writes, "As practitioners, we are being challenged to apply procedural rules and case law to the discovery and subsequent admission of electronic information. It will not be an easy transformation." He continues to spell out the specific hurdles lawyers face: understanding how electronic information is generated, stored and retrieved; deciphering authentication, hearsay and other obstacles for admission; and managing disclosure and duty to retain.

The author closes the preface with a statement of his modest vision for the text. He writes, "Without a doubt, electronic discovery is here to stay. We will not be going back to earlier paper-based discovery—we are firmly entrenched in the future. My hope is this book will assist, in some way, to lessen the changeover obstacles to electronic discovery. If so, then my efforts will have been rewarded." If this was his aim, then it is fair to say Arkfeld's efforts have been successful. The book offers a broad foundation of technical knowledge for the computer neophyte and a solid starting point for the more computer-savvy litigator commencing the conversion to electronic discovery.

The text presents a broad overview of the electronic discovery process, starting with understanding the components of a computer to the admissibility of electronic evidence. Arkfeld is a civil litigator practicing in Arizona, serves on the Electronic Discovery Committee for the State Bar of Arizona, and is a self-described computer enthusiast. His depth of computer knowledge is evidenced by the text's detailed anatomical discussion of computers and other electronic devices, to which more than one-third of the book is dedicated. The first three sections lay out the what, why and how of electronic discovery, explaining the new crucial role electronic evidence plays in litigation and providing a comprehensive and clear discussion of how electronic evidence is created and stored. Arkfeld states that in order to understand how electronic evidence can most effectively be utilized in the discovery process, lawyers will have to understand how electronic information is generated, stored and retrieved. Thus, he begins with the basics—the definition of hardware—and continues logically for the next 120 pages with detailed yet understandable explanations of virtually every feature of a computer. Even the novice computer user will quickly be able to distinguish between bits and bytes and WAM and LAN.

The book continues with an explanation of the role computer forensic experts and "electronic discovery" experts can play in assisting, gathering and deciphering the electronic information requested during discovery; establishing the chain of custody; and testifying to its authenticity. Arkfeld provides a lengthy list of issues to consider when choosing a forensic expert and includes information on how to locate an expert.

The second half of the book explains how to "harvest" electronic information, how to produce your own client's electronic information in response to discovery requests and how to use electronic information at trial. These sections make up the legal core of the book, and they include discussions of how to manage evidentiary issues as well as case-specific examples that document innovative ways to use electronic discovery to reduce discovery costs, recover lost data and simplify the task of quantifying damages.

Overall, Arkfeld's writing is clear and straightforward, although at times it is a bit repetitive. At its best, the book is a cheerleader and motivator, encouraging litigators to understand the fundamentals of computers, to welcome the progress electronic discovery brings, to create comprehensive electronic discovery procedures and to maximize the beneficial elements of electronic data. Each chapter includes relevant case citations and "Discovery Pointers," which include practical advice for making requests and ensuring electronic data is not destroyed or altered. The case law presented is certainly not exhaustive, but offers a good starting point for further research. In addition, Arkfeld provides purchasers of the book a free one-year subscription to a member-protected website, offering content updates, practice forms and additional case summaries.

Arkfeld dedicates too many pages to laying out the Federal Rules of Evidence, and should shorten or at least better integrate those sections. For example, he discusses the evidentiary rules of hearsay for six pages, but includes only one paragraph that applies the rule to electronic evidence. In this context, further discussion of how different types of electronic evidence fall under hearsay exceptions would be more helpful.

My only other suggestion for the book comes from the book's preface. Arkfeld states in the preface that "[e]ventually, electronic discovery standardization will occur. Just as standards and procedures were developed for the taking of videotaped depositions, so will the discovery and disclosure process for electronic discovery." Arkfeld presents case law to suggest how courts are construing the unique problems related to the advent of electronic discovery, including, for example, the ability to recover deleted e-mails. This discussion is extremely valuable for the practitioner, and further delineation of where and how current discovery law will have to bend would be of great interest to the reader.

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