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Journal

BREAKING UP LLCs

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EDITORIAL OFFICES
One Elk Street
Albany, NY 12207
(518) 463-3200
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ON THE COVER

This month's cover was prepared to symbolize the questions likely to arise when the founders of limited liability companies reach the point where they need to seek a judicial dissolution. As the accompanying article asks, will the relevant statutes and case law decisions be up to the task?

Cover Design and Photo by Lori Herzing.

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President's Message

Lorraine Power Tharp

The Paths We Take

"Mamma, don't let your babies grow up to be cowboys . . . let 'em be doctors and lawyers and such."[1] No doubt many of you are concerned that we have gone from an association president who was trained as an opera singer to one who quotes from country-and-western songs (for the record, I enjoy opera but I truly love *good* rock and, yes, country and western).

We as lawyers receive mixed messages. The public continues to be fascinated with us—as stated in an article in *The New York Times* (May 12, 2002), "We now live in a culture obsessed with lawyers and judges." Another article in a local paper recently featured a 15-year-old musician, whose plans are to sing and play guitar, but whose back-up plan is to be a lawyer. During the recent Winter Olympics, when Jack Shea of Lake Placid, a former Olympic Gold Medalist, was interviewed concerning his life (which shortly after the interview was tragically ended in a car crash), he stated that his one disappointment in life—now, remember this was an Olympic Gold Medalist—was that he had *not* become a lawyer.

With those who did realize a dream—or followed Willie's admonition—and entered the legal profession, our lives are not without angst. The media portrayal and public perception that is reported is often unkind. The daily challenges to meet deadlines, know the substantive law and work within the ethical framework can take its toll. We need, and are fortunate to have, an association to help.

The paths we take and the perspectives we hold have much to do with the words and actions of people who have made an impression on us. Think of the power of communication. Consider the impact of your words of explanation to clients and others in the community, and your example and encouragement to younger colleagues. Contemplate the possibilities to open and change minds by a more concerted outreach, as an association and as individuals. Especially in the hands of people skilled in counseling and advocacy, there is enormous opportunity to make progress. As we know from the pervasive problems of public perception of the justice system and the profession, the need and importance of taking these actions are considerable.

My journey to the law and to the New York State Bar Association began at the kitchen table. My father, a private practitioner, justice of the peace and then St. Lawrence County district attorney, spoke with passion about the law, its history, its meaning and its process. I had the benefit of seeing his efforts to counsel people and examine the issues at hand as he sought to put the law into action. I watched how he applied his legal skills in community service and how he encouraged and helped forge opportunity for other members of the bar to advance. He appointed the first woman as an assistant district attorney in St. Lawrence County. Dad was delighted when I was designated as president-elect of the NYSBA, and I know he would have followed every aspect of my presidency, as a proud parent and as a committed colleague of the bar.

Few have such a personal introduction to the value of the justice system and to the dedication of the people in the profession. I also was fortunate early on in my career to have colleagues who spoke of the importance of bar association and community activity and encouraged my participation. They demonstrated that this effort not only helps the individual to grow, but that it can be a rewarding means of serving the profession and society.

Using the power of words and action and the strength of the collective knowledge and energy of our membership, one of my initiatives this year will be for the association to work to redouble its outreach and communication—in essence, take every opportunity to touch lives by:

• Educating the public, from young people to senior citizens, about the legal process, the rule of law, rights and responsibilities, the importance of judicial independence, and the roles of lawyers and judges. Look for us to maximize use of our new Web site, as well as forums, education materials, classroom experiences and other means.

Also look for us to enhance our already stellar youth education program in more areas and involving more volunteer members of the bench and bar. Just spend a few minutes with the students who participate in our Law, Youth & Citizenship Program to see the positive results of our law-related education work in the schools; talk for a few moments with the members of our Committee on Citizenship Education and the volunteer attorney coaches for the statewide high school mock trial to feel the depth of their dedication.

• Increasing our contact with the media, identifying needed changes in the law and procedure, presenting our

Lorraine Power Tharp can be reached at Whiteman Osterman & Hanna, One Commerce Plaza, Albany New York 12260, or by e-mail at lptharp@woh.com.

positions and proposed actions based on our practical experience, and serving as a background resource for reporters.

• Building our legislative action program in analyzing pending legislation and regulations, proposing measures, and making our voice heard. We are implementing the steps recommended by the Special Committee on Legislative Advocacy and working with sections and committees.

• Ensuring access to justice for all New Yorkers, including indigent, working poor and middle-income persons, and small businesses. This is an ongoing pursuit where collaboration, innovation, and persistence are key to making progress. Our legislative proposal for a simplified civil case resolution option in matters of modest levels, proposed by the Commission on Providing Legal Services for Middle Income Consumers, is an excellent example of how we can bring creative approaches to challenging issues. This also is demonstrated by our concerted effort in seeking adequate resources for programs providing legal counsel to the poor in criminal and civil matters, through our President's Committee on Access to Justice, Committee on Legal Aid, Criminal Justice Section, and other committees and sections.

• Enhancing our outreach and promoting active involvement in the Association, to reflect the diversity of the profession. This is critical to maintain a vibrant organization in tune with the needs of the profession and the needs of people that we serve. It is equally important to evaluate the opportunities available for members to participate and grow within the association, and the work of our Governance Committee and our Committee on Women and the Law will play a vital role in these efforts.

• Enhancing diversity in the judiciary, to reflect the profession and society. To that end, I have appointed a Task Force on Increasing Diversity in the Judiciary, which will undertake research, possibly communicate with "How to Become a Judge" workshops, and then make recommendations.

• Being a resource for our members in effective and efficient law practice management methods, from the best use of technology to client communication in these fast-paced times when it is a challenge to take a moment for quiet contemplation. These efforts must go beyond initiatives to enhance practice performance. We also must work to ensure that there is opportunity for bar association involvement and other professional and community service collaborations—and personal quality of life. Activities beyond the case at hand are rewarding, enriching and help us view issues from many perspectives. These are vital elements in maintaining our passion for the profession and our collegiality with one another. We will be working with our committees and sections and talking with law office representatives on these challenging concerns.

• Expanding our dialogue with law school administrators and educators on preparing students on the values and skills needed to be a member of the profession in its fullest sense. Do we do enough in the area of counseling law students as to the various areas of practice, and the merits of each? I think not.

The need to enhance communication, through our association and as individuals, is demonstrated in opinion surveys released in the past few months. The results, showing low levels of public confidence in the justice system and profession and confusion about procedures in engaging a lawyer, are consistent with prior research that identified problems of public perception. This research also indicates opportunities for education to demystify the legal process, dispel misperceptions, and demonstrate the valuable work of lawyers. The American Bar Association Section on Litigation's Public Perception of Lawyers survey, for example, found that after the September 11 attack, confidence levels in the justice system and the profession increased in the wake of the tremendous bench and bar *pro bono* and disaster relief efforts. Also, the good news continues to be that individual members of the public have confidence in their *own* lawyer.

Each of the above areas of action relates to and presents opportunities to build public understanding. In the months ahead, I will be discussing these issues with you—through this column, in section, committee and bar association meetings across the state. I had terrific conversations with section officers last month at our Section Leaders Conference on means of advancing these efforts in the various fields of practice. I will be having similar discussions with committee chairs through the summer, and fall.

At these various meetings, I urge you to share your counsel with me on how we can make inroads and overcome obstacles. Please do not wait for such an occasion to talk about these subjects, other issues of concern, and what you would like to see your Association doing to assist you in your work, the profession, and our efforts in public service. I am just an e-mail away. Back to our opera-trained president. All of us owe our collective thanks to Steven C. Krane for his guidance and strength, particularly after September 11. I will always remember being in Albany that day with Steve, our new executive director, Patricia Bucklin, other bar leaders and judges. We gathered in horror and responded with leadership. Although minor in the scheme of things, I too will never forget then-President Krane's voice leading our House of Delegates in November for the first time ever in the singing of "God Bless America." It was not opera, nor country and western—it was all of us, lawyers from around the state, looking to reaffirm our values, our beliefs and our solidarity behind a country that is based on the rule of law.

1. With all due credit to Willie Nelson.

When Limited Liability Companies Seek Judicial Dissolution, Will The Statute Be Up to the Task?

By Peter A. Mahler

In the years since New York authorized limited liability companies in 1994, the statistics on new business entity filings demonstrate a growing recognition of the significant tax and organizational advantages that limited liability companies (LLCs) offer when compared with other available corporate or partnership options for closely held business entities. The trend has led some to predict that "before too long the LLC may largely render the partnership, limited partnership and closely held corporation obsolete."[1]

Now that many thousands of LLCs have been formed and the natural life cycles are running their course, the question arises whether New York's statute governing proceedings for judicial dissolution of LLCs is up to the task.

This article examines New York law concerning LLC dissolution and concludes that the governing statute does not adequately empower the courts to resolve LLC "business divorce" litigation. The statute's provisions for member dissociation and dissolution were drafted to assure that LLCs would receive favorable tax treatment as partnerships under then-existing IRS regulations, which were subsequently scrapped. The legislature responded with amendments establishing corporation-style default rules for dissociation and dissolution, but without revising the judicial dissolution provision. This article recommends amending the statute to assimilate the statutory scheme for judicial dissolution of closely held business corporations under the Business Corporation Law (BCL).

Tax Policy and the LLC Movement

The approach of the Limited Liability Company Law (LLCL) to dissolution has its roots in federal tax policy, as do many other key features of LLCs.

The modern tax era began in 1913 with ratification of the 16th Amendment authorizing the income tax.[2] Under the first Revenue Act passed that same year, Congress imposed taxes on the net income of every corporation or "association . . . not including partnerships." This dual classification scheme—entity-level taxation of corporations and unincorporated organizations classified as "associations," and pass-through taxation of partnerships—remains in place and plays a critical role in entity selection.

For almost 50 years after the adoption of the federal income tax, regulations generally classified and taxed unincorporated entities as non-partnership "associations" whenever they shared the corporate trait of limited liability. In 1960, the IRS adopted new regulations making it harder for unincorporated entities to be treated as associations.[3] Under the 1960 regulations, an unincorporated organization is classified for tax purposes as a partnership if it lacks at least two of four corporate characteristics: (1) continuity of life, (2) centralization of management, (3) limited liability and (4) free transferability of interests.[4]

Over the following two decades, shifts in the relative tax rates for individuals and corporations, together with a surge of independent oil producers and other partnership syndications needing to pass through tax losses to investors, made conditions ripe for the invention of a new business form that combined limited liability and pass-through tax benefits, but without the constraints of the subchapter S corporation.[5]

The breakthrough came in 1977 when Wyoming enacted the first domestic LLC statute at the request of the Hamilton Brothers Oil Company. In 1980, Hamilton obtained from the IRS a private letter ruling confirming that the LLC qualified for federal tax treatment as a partnership. About the same time, however, the IRS proposed new, contrary partnership classification rules that would treat the LLC as a corporation for tax purposes.

Peter A. Mahler is a partner at Derfner & Mahler, LLP, in New York City (e-mail mailerlaw@aol.com). He practices in the area of business litigation, including shareholder, partnership and LLC membership disputes. A graduate of U.C. Santa Barbara, he received his J.D. from New York University School of Law.

Under heavy criticism, the IRS withdrew the proposed regulations in 1983 and embarked on a five-year study of the issue. In the interim, Congress passed major tax reform that severely curtailed partnership syndications and raised corporate tax rates, thereby generating even greater interest in business and legal circles for partnership tax treatment for LLCs.[6]

By 1988, due to the tax uncertainty only one other state (Florida) had adopted LLC legislation and less than 100 businesses had organized as domestic LLCs.[7] That all changed in 1988 with Revenue Ruling 88-76, in which the IRS recognized partnership tax classification for the Wyoming LLC. The ruling established that limited liability alone would not require corporate taxation for unincorporated organizations, and that the four corporate characteristics would be weighed equally.[8]

New Business Corporations and LLCs 1994–2001

Year	New Business Corporations	New LLCs	Conversions to LLCs
1994	70,691	1,133*	124*
1995	72,433	7,063	824
1996	73,866	9,427	858
1997	74,397	12,238	771
1998	72,568	15,149	608
1999	75,276	18,007	510
2000	75,992	20,818	364
2001	73,410	21,913	377
Totals	588,633	105,748	4,436

*LLC filings became effective on 10/24/94

Source: New York Department of State

Revenue Ruling 88-76 triggered an avalanche of LLC legislation. Between 1990 and 1996, the remaining 48 states and the District of Columbia all enacted LLC legislation, some of it modeled on a prototype LLC act sponsored by the American Bar Association.[9] From 1988 through the end of 1995, more than 200,000 new LLCs were organized nationwide.[10]

In New York, by 1991 various bar association drafting committees organized to take up the LLC cause. LLC legislation was introduced in the 1992 and 1993 legislative sessions without success, apparently due to concern over loss of corporate tax revenues. In the end, fear of losing business to surrounding states with LLC statutes overcame revenue concerns, and in July 1994 Governor Cuomo signed the LLCL, made effective October 24, 1994.[11]

Dissociation and Dissolution in New York

Revenue Ruling 88-76 essentially dictated the original dissociation and dissolution provisions of the LLCL by requiring drafters to establish default rules that would cause the LLC to fail the test for continuity of life. They achieved that objective by mimicking the dissociation and dissolution provisions for limited partnerships. The supporting memorandum submitted by one of the proposed legislation's sponsors, Senator John Daly, declared that many of its dissolution and winding-up provisions would be adapted, with minor modifications, directly from the Revised Limited Partnership Act (RLPA).[12]

The provisions of the law for member dissociation and dissolution are contained in three sections: LLCL § 606, governing member withdrawal; § 701, setting forth events of dissolution; and § 702, authorizing actions for judicial dissolution.

LLCL § 606 The original version of § 606 permitted a member to withdraw from the LLC upon the happening of any events specified in the operating agreement, or in accordance with the operating agreement or, unless otherwise provided in the operating agreement, with the consent of two-thirds of the other members. Unless prohibited by the operating agreement, a member could still withdraw even without the other members' consent upon six months' prior written notice. A withdrawal in violation of the operating agreement, however, entitled the LLC to recover any damages for breach that could be offset against any distributions due the withdrawing member. Under LLCL § 509, a withdrawing member is entitled to receive, within a reasonable time after withdrawal, the fair value of his or her membership interest.

LLCL § 701 As originally enacted, LLCL § 701 mandated dissolution of LLCs upon the first to occur of five enumerated events, including a decree of judicial dissolution under § 702. The other dissolution events fell into two general categories: (1) contractual or other consensual events expressly contemplated in the articles of organization and operating agreement, or (2) non-consensual events including the bankruptcy, death, dissolution, expulsion, incapacity or withdrawal of a member, subject to the remaining members' right to continue the LLC within 180 days pursuant to vote or a right to continue stated in the operating agreement.

LLCL § 702 This section authorizes a member to apply for a decree of judicial dissolution of an LLC "whenever it is not reasonably practicable to carry on the business in conformity with the articles of organization or operating agreement." The quoted language is borrowed from RLPA 121-802, which authorizes dissolution of a limited partnership whenever it is "not reasonably practicable to carry on the business in conformity with the partnership agreement." The latter section, in turn, is a truncated version of Partnership Law § 63(d) which, among other grounds, permits dissolution of a general partnership when a partner "wilfully or persistently commits a breach of the partnership agreement, or otherwise so conducts himself in matters relating to the partnership business that it is not reasonably practicable to carry on the business in partnership with him."

LLCL § 702 also closely tracks the language in § 902 of the ABA Prototype LLC Act, the 1992 commentary to which states that the "'not reasonably practicable' language probably includes at least some of the causes of dissolution provided for in partnership law, particularly partner misconduct."[13] The same commentary also suggests a deliberate avoidance of the typical grounds for dissolution found in corporate dissolution statutes, on the ground that "disgruntled members" of an LLC "would be encouraged to make this sort of allegation in limited liability company breakups."[14]

"Check-the-Box"

Shortly after New York's LLCL went into effect, the IRS gave notice that it was considering the adoption of radically simplified regulations that would allow unincorporated business organizations, including LLCs, to elect either partnership or association tax treatment without regard to application of the four-factor test for corporate characteristics.[15] Under the so-called "check-the-box" regulations, which went into effect in 1997, a new unincorporated entity with two or more members automatically is classified as a partnership unless it elects a different status, and a new one-member entity is disregarded for tax purposes absent an election otherwise.[16]

Prior to check-the-box, the default provisions of LLC statutes were carefully drawn to avoid the corporate characteristic of continuity of life. The new regulations rendered non-continuity of life essentially meaningless for tax purposes. For business purposes, continuity of life is more attractive to LLC investors, third-party lenders and contract partners because it removes the uncertainty associated with events of dissolution and simplifies the operating agreement. Accordingly, states including New York responded to the new regulations by reversing the default rules governing member withdrawal and dissolution.

The 1999 LLCL Amendments

Chapter 420 of the Laws of 1999, which went into effect August 31, 1999, included important amendments to LLCL § 606 and § 701. The previous default rights of members to withdraw upon consent of the other members or, absent consent, unilaterally upon six months' notice, were eliminated from § 606 and replaced with a default prohibition barring withdrawal prior to dissolution except as otherwise provided in the operating agreement.[17]

The default rules for dissolution under § 701 were amended to provide the LLC with "perpetual existence" absent a limited-duration provision in the articles of organization and operating agreement.[18] The previous default rule under § 701, requiring dissolution of the LLC upon the death, retirement, resignation, expulsion, bankruptcy or dissolution of any member unless the remaining members vote to continue, also was eliminated. In its place, the amended section states that such dissolution events shall not cause the LLC to be dissolved unless within 180 days a majority of the remaining members agree to dissolve.[19]

Senator John Marchi's memorandum in support of the proposed amendments explained that the changes in the default rules for withdrawal were designed to codify "the likely expectations of the parties forming" the LLC "to have rights similar to those of a shareholder of a business corporation." It went on to note that shareholders would "not have a right of withdrawal or redemption absent an express agreement" and that it would therefore be "appropriate" to treat LLCs "similarly to corporations in this area." The memorandum also commented that "the dissolution provisions of the LLCL that were designed to meet [previous] IRS regulations may be changed to conform with the likely expectations and preference of LLC members."[20]

Partnership vs. Corporate Exit Rules

The 1999 amendments to LLCL § 606 and § 701 jettisoned the partnership model in favor of the corporate model, but left LLCL § 702 untouched. Can a partnership-modeled judicial dissolution statute adequately address membership disputes of the type found in closed corporations?

Over the last several decades, a vast body of literature and case precedent has grown around the problem of squeeze-out and other forms of minority shareholder oppression in closed corporations.[21] Historically, partnership squeeze-out cases are rare not only because of the partners' equal management rights, but also because of the relative ease of exit under partnership law.[22] In the absence of any agreement to the contrary, a partner can dissolve the partnership at any time and receive his or

CONTINUED ON PAGE 12

Dissolution Provisions Of Limited Liability Companies Law

§ 701. Dissolution.

(a) A limited liability company is dissolved and its affairs shall be wound up upon the first to occur of the following:

(1) the latest date on which the limited liability company is to dissolve, if any, provided in the articles of organization, or the time specified in the operating agreement, but if no such date is provided in the articles of organization and if no such time is specified in the operating agreement, then the limited liability company shall have a perpetual existence;

(2) the happening of events specified in the operating agreement;

(3) subject to any requirement in the operating agreement requiring approval by any greater or lesser percentage in interest of the members or class or classes or group or groups of members, the vote or written consent of at least a majority in interest of the members or, if there is more than one class or group of members, then by at least a majority in interest of each class or group of members;

(4) at any time there are no members, provided that, unless otherwise provided in the operating agreement, the limited liability company is not dissolved and is not required to be wound up if, within one hundred eighty days or such other period as is provided for in the operating agreement after the occurrence of the event that terminated the continued membership of the last remaining member, the legal representative of the last remaining member agrees in writing to continue the limited liability company and to the admission of the legal representative of such member or its assignee to the limited liability company as a member, effective as of the occurrence of the event that terminated the continued membership of the last remaining member; or

(5) the entry of a decree of judicial dissolution under section seven hundred two of this article.

(b) Unless otherwise provided in the operating agreement, the death, retirement, resignation, expulsion, bankruptcy or dissolution of any member or the occurrence of any other event that terminates the continued membership of any member shall not cause the limited liability company to be dissolved or its affairs to be wound up, and upon the occurrence of any such event, the limited liability company shall be continued without dissolution, unless within one hundred eighty days following the occurrence of such event, a majority in interest of all of the remaining members of the limited liability company or, if there is more than one class or group of members, then by a majority in interest of all the remaining members of each class or group of members, vote or agree in writing to dissolve the limited liability company.

(c) A limited liability company whose original articles of organization were filed with the secretary of state and effective prior to the effective date of this subdivision shall continue to be governed by this section as in effect on such date and shall not be governed by this section, unless otherwise provided in the operating agreement.

§ 702. Judicial dissolution.

On application by or for a member, the supreme court in the judicial district in which the office of the limited liability company is located may decree dissolution of a limited liability company whenever it is not reasonably practicable to carry on the business in conformity with the articles of organization or operating agreement. A certified copy of the order of dissolution shall be filed by the applicant with the department of state within thirty days of its issuance.

Continued from page 10

her rightful share of the liquidation proceeds. If the business as a going concern is worth more than its liquidation value, the partners are highly motivated to negotiate a buyout. The Revised Uniform Limited Partnership Act also contains liberal exit rules, permitting general partners to cash out for fair value so long as their departure does not trigger dissolution, and permitting limited partners to receive fair value upon six months' notice.[23]

In contrast, "[c]orporate law norms are conducive to minority squeeze-outs in a closely held firm."[24] Majority shareholders exercising control of the board of directors have any number of ways to impair minority shareholder interests, *e.g.*, barring participation in management decisions, reducing salary, terminating employ-

ment, removing a shareholder from the board of directors, altering dividend policy, or paying the controlling shareholders excessive salaries.

At the same time, unlike partnership default rules, corporate law does not provide non-controlling shareholders of closed corporations with any easy means of egress that would permit them to recoup their investment. For this reason most states, including New York in 1979, enacted laws giving minority shareholders the right to seek judicial dissolution for oppressive actions or other misconduct by controlling shareholders. These laws typically also provide for a statutory buyout of the minority shareholder's stock and empower the courts to fashion other forms of relief short of dissolution.[25]

Time will tell whether the LLCL's 1999 amendments will lead to increased litigation of disputes between LLC members. The most likely candidates are post-amendment LLCs without operating agreements and therefore governed by the LLCL's new default rules.[26] A member of such an LLC has no right to withdraw and no right to receive fair value for his or her interest. An action for judicial dissolution may be the only way out.

The Developing Case Law

To date, only a handful of court decisions have involved judicial dissolution of New York LLCs. The decisions are striking in two respects. First, they make no meaningful attempt to construe or apply the specific language of LLCL § 702. Second, almost all of them either explicitly or implicitly treat LLCs as business corporations subject to the same dissolution standards and remedies available under BCL Article 11, without any acknowledgment of the statutory differences and without offering any rationale for doing so.

The one officially reported New York decision thus far to address LLC dissolution in anything approaching a substantive fashion is *In re Roller (W.R.S.B. Development Co., LLC)*,[27] in which the Fourth Department affirmed the denial of a motion to dismiss the petition. Practitioners should not expect much guidance from the *Roller* opinion's meager four sentences. The court merely states that the petitioners' ownership of membership interests in the two subject LLCs on the date the proceeding was commenced gives them standing to bring the proceeding, and that "the petition adequately states a cause of action for judicial dissolution" under LLCL § 702.[28]

What allegations in *Roller* sufficed to state a § 702 claim? A look at the *Roller* petition shows that there were two subject LLCs organized by four members to develop shopping centers.[29] The three petitioning members owned 75% of one LLC and 45% of the other. The petition alleges that the respondent member "excluded" them from the companies' business affairs; that there is "internal dissension" and "irreconcilable conflict" such that dissolution "would be beneficial to the membership"; that the respondent breached his fiduciary duty by denying petitioners access to company records and by managing the businesses to his sole benefit; that dissolution would not injure the public; and that all of the foregoing renders it "no longer reasonably practicable to carry on the business of the companies in conformity with the operating agreement of each."

Veterans of corporation business divorce litigation recognize the *Roller* allegations as classic grounds for dissolution under BCL §§ 1104 and 1104-a, for deadlock and oppression. While such grounds may indeed point to the need for dissolution of an LLC, by its express terms § 702 requires something else: a showing that "it is not reasonably practicable to carry on the business in conformity with the articles of organization or operating agreement." Conspicuously missing from the *Roller* petition is any reference to the provisions of the operating agreement or articles of organization which, in light of the conduct alleged, make it impracticable for the business to carry on in conformity therewith.

The unspoken reliance on BCL dissolution standards in *Roller* comes out into the open in an unreported lower court ruling in *RRA Limited Partnership v. A Space Place, Centereach, LLC*.[30] The case involved four related LLCs formed to acquire and improve real property for use as self-storage space. The petitioner was the majority owner of two of the LLCs and 50% owner of the other two. Both sides agreed that the companies were operating successfully and that they intended to sell all the assets.

The petitioner sought dissolution after the failure of a proposed sale to a third party. The petitioner explicitly relied on BCL § 1104(a)(3) in support of dissolution, based on "numerous incidents of divisiveness between the parties" such that dissolution "may be beneficial to the shareholders [*sic*]."[31] The court's determination to deny the respondent's dismissal motion likewise paraphrases the standards for dissolution under BCL §§ 1104 and 1104-a, several subsections of which the court cites along with several case precedents under those statutes. As in *Roller*, the specific prerequisite for dissolution stated in LLCL § 702 is given nominal regard.

Several other unreported trial court decisions likewise apply BCL Article 11 to LLC dissolutions without any discussion of the basis for, or implications of, doing so. In *In re O'Brien (Academe Paving, Inc.)*,[32] the petitioner sought to dissolve two related entities—one a business corporation and the other an LLC—under BCL § 1104-a for minority shareholder oppression. The respondents served an election under BCL § 1118 to purchase the petitioners' "shares" in both entities for fair value, after

Provisions of Operating Agreement Can Minimize Dissolution Contests

The freedom that limited liability companies have to form the agreements that govern their operation allows the founders to include provisions that would, in effect, constitute a kind of prenuptial agreement to avoid a messy business divorce when the LLC members wish to break up.

With few exceptions, LLCL § 417(a) permits members to adopt a written operating agreement that contains "any provisions not inconsistent with law or its articles of organization" relating to the LLC's business affairs and the rights and duties of LLC members and managers. The LLCL's articles dealing with membership, management, contributions and distributions, function as default rules that govern only when the operating agreement is silent on the issue. As the Delaware Chancery Court put it, "LLC members' rights begin with and typically end with the Operating Agreement."[1]

So, too, with member dissociation and dissolution. In this regard, LLC operating agreements and shareholder agreements for business corporations can serve the same purpose. Courts routinely deny petitions for judicial dissolution of closely held corporations based on provisions in shareholder agreements that, for example, require surrender of stock with or without consideration upon any termination of the shareholder's employment,[2] or deem the commencement of a dissolution proceeding as an offer to sell at a fixed price or under a predetermined formula.[3] Courts also can be relied on to deflect LLC dissolution petitions based on mandatory arbitration clauses in operating agreements, just as they do with arbitration clauses in shareholder agreements.[4]

The inclusion of such provisions in an operating agreement will depend on many factors. These include the nature of the business and its capital structure; the number of members and the resources or talents each contributes; whether the LLC is family-owned; the magnitude of any possible threat to the LLC's liquidity posed by a member buyout; and the relative bargaining power of the parties to the operating agreement. So long as the particular mechanism adopted reflects the parties' voluntary agreement to avoid dissolution and to carry on the business notwithstanding the alleged detriment to the complaining LLC member, an application for judicial dissolution under LLCL § 702 is not likely to succeed.

1. *Walker v. Resource Dev. Co., LLC*, 791 A.2d 799 (Del. Ch. 2000).
2. *See In re Apple (Apple Rubber Prod., Inc.)*, 224 A.D.2d 1016, 637 N.Y.S.2d 534 (4th Dep't 1996).
3. *See Doniger v. Rye Psychiatric Hosp. Ctr., Inc.*, 122 A.D.2d 873, 505 N.Y.S.2d 920 (2d Dep't 1986).
4. *See Alleman v. Sunrest Health Facilities, Inc.*, 176 A.D.2d 287, 574 N.Y.S.2d 216 (2d Dep't 1991).

which the court stayed the dissolution and ordered a valuation hearing.

At first blush, nothing about *O'Brien*'s enforcement of the respondents' § 1118 election seems amiss, especially if the petitioner's consent to the election is assumed. Upon closer examination, however, the incorporation of BCL buyout rights is highly problematic. BCL § 1118(a) specifically limits the statute's application to proceedings for shareholder oppression and other misconduct under BCL § 1104-a. This express statutory limitation has led courts repeatedly to preclude § 1118 buyouts in deadlock proceedings under BCL § 1104.[33]

The LLCL does not authorize a buyout of the interest of the member seeking dissolution. If BCL § 1118 cannot reach across the small gap between BCL §§ 1104 and 1104-a, certainly it cannot bridge the chasm separating BCL § 1104-a and LLCL § 702.

Other recent examples of courts applying BCL Article 11 to LLC dissolutions include *In re Rodriguez (Zoros Limited)*[34] and *In re Honig (JM Marketing, LLC)*.[35] In *Rodriguez*, the court denied a motion to dismiss a dissolution proceeding involving a foreign LLC on the ground that BCL § 1104 empowered the court, if not to actually dissolve the LLC, to declare the parties' rights of ownership, order a winding up and, if called for, order the parties to file dissolution papers in the foreign jurisdiction. In *Honig*, the court ordered a hearing on the petition to dissolve an LLC after acknowledging the dearth of reported decisions interpreting LLCL § 702. The *Honig* court concluded on the basis of BCL Article 11 case law that the proper focus is "assurance to the petitioner seeking dissolution that a fair return on his investment in company securities can be obtained whether through a buy-out option, if available, or by the sale of the shares to other share holders."[36] It is impossible to locate any basis in LLCL § 702 for this BCL-derived standard.

At least one unreported LLC dissolution decision, *In re Quinn (David Rose Perennials, LLC)*,[37] is more attuned to the statutory constraints of LLCL § 702. *Quinn* involved a two-member LLC. The petitioner was the managing member who ran the retail business while the respondent member and majority owner was responsible for the business plan and finances. The petitioner left

the business and formed a new business after the respondent refused to increase her compensation.

The court denied the petitioner's motion for a preliminary injunction on the ground that the operating agreement gave the respondent a controlling voting interest in the company. As viewed by the court, the petitioner's departure resulted from "a disagreement as to the apparently proper exercise of discretion" in determining her compensation and not from any wrongdoing by respondent.

Quinn's focus on whether the complained-of conduct conforms to the operating agreement is consistent with the language of LLCL § 702. At the same time, it highlights § 702's inherent limitations as a remedial statute. LLC members wielding majority control under the operating agreement will almost always be able to use their control to the disadvantage of the minority owners for whom employment with the LLC may be the primary if not sole source of return on their investment. Majority curtailment of the minority's employment benefits is a classic squeeze-out technique which can often occur without appreciable impact on the business, and therefore without running afoul of LLCL § 702. As one commentator succinctly noted, "it is often possible to carry on the business while freezing a minority interest out of any return."[38]

So long as the language of the statute forces courts to focus primarily on the inability of the LLC to carry on its business in conformity with the operating agreement or articles of organization, and only secondarily on the conduct of the members or the effect on a particular membership interest, there are bound to be cases in which LLC members will be denied relief under circumstances where a similarly situated corporation shareholder would succeed.[39]

A contrary argument could be made based on the notion that the BCL is a statute of general application to all species of business entities, including LLCs. However, BCL § 103 expressly limits the application of the statute to domestic "corporations" and foreign "corporations" authorized or doing business in New York. LLCL § 102(m) defines an LLC as an "unincorporated organization . . . other than a partnership or trust." The statutory schemes governing business corporations and LLCs, and their authorized business and ownership structures, are like day and night.

In addition, the Court of Appeals has observed that, historically, New York courts were considered divested of equity jurisdiction to order dissolution of corporations, as statutory prescriptions were deemed "exclusive."[40] There is no more reason to conclude that courts have a general, non-statutory power to augment the LLCL's prescriptions for dissolution by incorporating what are essentially alien BCL provisions.

A Proposal to Amend LLCL § 702

It is possible that in years to come, a stand-alone jurisprudence for judicial dissolution of LLCs will take root, flourish and mature into a well-developed body of law from which the business and legal communities can draw guidance. So far the signs are not promising. The LLCL's narrow standard for exercise of the dissolution power, based on outdated partnership exit rules, does not seem adequate to the task. In the meantime, the uncertainty resulting from the absence of authoritative case law can only serve as a deterrent to greater use of the LLC as one among several competing business entities.

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A number of other states have taken the lead in adopting the "modern, liberal corporate model" for judicial dissolution of LLCs.[41] Section 801 of the Uniform Limited Liability Company Act (1996) (ULLCA), which so far has been enacted by eight states and one territory,[42] permits judicial dissolution whenever "the managers or members in control of the company have acted, are acting, or will act in a manner that is illegal, oppressive, fraudulent, or unfairly prejudicial to the petitioner."[43] California permits judicial dissolution of LLCs whenever it is "reasonably necessary for the protection of the rights or interests of the complaining members" or when controlling members "knowingly countenanced persistent and pervasive fraud, mismanagement, or abuse of authority."[44] The ULLCA and California standards are more liberal than those governing dissolution of closely held New York business corporations, and have been criticized as "creat[ing] too many opportunities for oppression of the majority by the minority."[45]

Amendment of LLCL § 702 need not go as far as the ULLCA and California law. Rather, the legislature should amend § 702 by incorporating the existing, more modest standards for dissolution under BCL §§ 1104-a and 1104.

Since its enactment in 1979, BCL § 1104-a has permitted a 20%[46] or more shareholder to seek dissolution where the directors or those in control of the corporation engage in "illegal, fraudulent or oppressive actions" or where corporate property and assets are being "looted,

wasted, or diverted for non-corporate purposes." An extensive body of interpretive case law has grown around these provisions, with "oppressive actions" garnering the overwhelming share of judicial attention.[47]

BCL § 1104 and its predecessor statutes, in place for more than 70 years, authorize a 50% shareholder to petition for dissolution based on management or ownership deadlock and dissension.[48] These provisions likewise have been construed in numerous cases, giving clarity and predictability to deadlock-based disputes.[49]

As a matter of public policy, there seems little reason to distinguish between LLCs and closely held business corporations when it comes to the grounds for business divorce. The reliance of New York courts on BCL statutory and decisional law in the early LLC dissolution cases discussed above underscores the similarity of the internal forces that contribute to dissension and oppression among co-owners of both LLCs and business corporations. Amending LLCL § 702 to incorporate the grounds for dissolution in BCL §§ 1104 and 1104-a will place these respective proceedings on a par where they belong, and will provide LLC members and their counsel with a ready-made, extensive body of decisional law from which to draw guidance in designing operating agreements and in regulating member conduct.

LLCL § 702 also should be amended to incorporate buyout rights akin to those found in BCL § 1118.[50] The latter provision gives the respondent shareholders or the corporation the right to elect, within 90 days of the petition, to purchase the petitioner's shares for fair value. If the parties are unable to agree on fair value, upon application the court will stay the dissolution and determine the fair value as of the day prior to the date on which the petition was filed.

There is every reason to expect that granting respondent LLC members the right to stay dissolution in favor of a buyout will have the same salutary effect the proceedings under BCL Article 11. It will also likely induce organizers of LLCs to include mandatory buyout provisions in an operating agreement, which will promote two important goals. First, parties entering into an LLC venture will be encouraged to enter into consensual arrangements that fix their rights and financial expectations in the event of dissociation. Second, by doing so, LLC members will be far less likely to burden the courts with business divorce litigation.

1. F. Gevurtz, *Squeeze-Outs and Freeze-Outs in Limited Liability Companies*, 73 Wash. U. L.Q. 497, 497 (1995) ("Gevurtz, *Squeeze-Outs*"). A former IRS commissioner recently noted that "[n]o rational, reasonably well-informed tax professional would deliberately choose subchapter S [corporation] status over an LLC when there is a choice, and 99% of the time there is a choice." D. Alexander, *Tax Practice*, July 17, 2000, *quoted in* 1 Ribstein and Keatinge on Limited Liability Companies § 2.01 (2001).
2. *See* S. Hamill, *The Origins Behind the Limited Liability Company*, 59 Ohio St. L.J. 1459, 1478–1504 (1998) ("Hamill, *Origins*").
3. The 1960 regulations were adopted in response to the decision six years earlier in *United States v. Kintner*, 216 F.2d 418 (9th Cir. 1954), where the court sided with a medical partnership that purposefully structured itself with certain corporate characteristics to gain tax treatment as an association and thereby to obtain pension benefits not then available to partnerships. *See* S. Hamill, *The Taxation of Domestic Limited Liability Companies and Limited Partnerships: A Case for Eliminating the Partnership Classification Regulations*, 73 Wash. U. L.Q. 565, 573 (1995).
4. Former Treas. Reg. § 301.7701-2. The factors are drawn from the decision in *Morrissey v. Commissioner*, 296 U.S. 344 (1935), where the Supreme Court held that a business trust with corporate characteristics could be taxed as a corporation. *See* C. Goforth, *The Rise of the Limited Liability Company: Evidence of a Race Between the States, But Heading Where?*, 45 Syracuse L. Rev. 1193, 1200 (1995) ("Goforth, *Rise of LLC*").
5. *See* 1 Ribstein and Keatinge on Limited Liability Companies § 16.02; Hamill, *Origins*, *supra* note 2, at 1509–16.
6. *See* Hamill, *Origins*, *supra* note 2, at 1516–18; Goforth, *Rise of LLC*, *supra* note 4, at 1199–1201.
7. *See* Hamill, *Origins*, *supra* note 2, at 1469.
8. *Id*. at 1469–70.
9. *See* Goforth, *Rise of LLC*, *supra* note 4, at 1206, 1222–62.
10. *See* Hamill, *Origins*, *supra* note 2, at 1477–78.
11. *See* K. Walker, New York Limited Liability Companies and Partnerships § 1.1.1 (2002) ("Walker, NY LLCs").
12. Senate Introducer Mem. in Support, Bill Jacket, 1994 N.Y. Laws ch. 576, at 8.
13. ABA Prototype LLC Act § 902, commentary at 64.
14. *Id*.
15. Notice 95-14, 1995-14 CB 297; *see* 1 Ribstein and Keatinge on Limited Liability Companies § 16.02.
16. Treas. Reg. § 301.7701-2(c). *See* Walker, NY LLCs, *supra* note 11, §§ 2.2–2.3. The new regulations replaced Treas. Reg. §§ 301.7701-1, 301.7701-2, 301.7701-3.
17. Under LLCL § 606(b) as amended, an LLC whose original articles of organization were filed prior to August 31, 1999, shall continue to be governed by the pre-amendment version of the statute unless otherwise provided in the operating agreement.
18. LLCL § 701(a)(1).
19. LLCL § 701(b).
20. Senate Introducer Mem. in Support, Bill Jacket, 1999 N.Y. Laws ch. 420, at 5–6.
21. The leading treatise on the subject is F. O'Neal & R. Thompson, O'Neal's Oppression of Minority Shareholders (2d ed. 1999).
22. Gevurtz, *Squeeze-Outs*, *supra* note 1, at 501–502; *see* D. Karjala, *Planning Problems in the Limited Liability Company*, 73 Wash. U. L.Q. 455, 471 (1995) ("Karjala, *Planning Problems*").
23. Gevurtz, *Squeeze-Outs*, *supra* note 1, at 501–504.
24. *Id*. at 501.

25. *Id*. at 498–501; *see* 1 Ribstein and Keatinge on Limited Liability Companies § 2.06.
26. LLCL § 417(a) states that every LLC "shall adopt a written operating agreement" but does not address the consequences (if any) of failure to do so and does not require the operating agreement to be filed. LLCL § 417(c) states that the operating agreement "may" be entered into before, at the time of or within 90 days after the filing of the articles of organization. For an example of the litigation complexities that can arise in the absence of an operating agreement, see *Child Care of Irvine, LLC v. Facchina*, 1998 Del. Ch. LEXIS 114 (Del. Ch. July 15, 1998) (denying plaintiffs' motion for summary judgment in action to uphold termination of defendant member as LLC's general manager where factual issues arose from the parties' failure to execute an operating agreement).
27. 259 A.D.2d 1012, 689 N.Y.S.2d 897 (4th Dep't 1999). In *Roller* and all of the unreported LLC dissolution cases discussed in this article, dissolution was sought by way of petition in a special proceeding notwithstanding the absence of any authorization in LLCL § 702. CPLR 103(b) mandates that "[a]ll civil judicial proceedings shall be prosecuted in the form of an action, except where prosecution in the form of a special proceeding is authorized." The use by counsel of the special proceeding form in LLC dissolutions is yet another manifestation of the prevailing treatment of LLC dissolutions as governed by BCL Article 11 which mandates a special proceeding for dissolution proceedings under that article.
28. *Roller*, 259 A.D.2d at 1012.
29. Petition, *In re Roller (W.R.S.B. Development Co., LLC)*, Index No. 10012/97 (Sup. Ct., Erie Co. Nov. 25, 1997) (on file with author, courtesy of Melissa Hancock Nickson, Esq.).
30. Index No. 00-26634 (Sup. Ct., Suffolk Co., June 8, 2001).
31. *Id.,* slip op. at 2.
32. Index No. 99-2594 (Sup. Ct., Broome Co., Aug. 24, 2000).
33. *See In re Sternberg (Osman)*, 181 A.D.2d 897, 582 N.Y.S.2d 206 (2d Dep't 1992). In *In re Cristo Brothers, Inc.*, 64 N.Y.2d 975, 976, 489 N.Y.S.2d 35, 36 (1985), the Court of Appeals commented that "the legislative history of Business Corporation Law § 1118 contains nothing to indicate why it accorded a buy-out privilege in any proceeding brought pursuant to section 1104-a but not with respect to a dissolution proceeding under Business Corporation Law § 1104."
34. N.Y.L.J., Jan. 18, 2001, p. 29, col. 5 (Sup. Ct., N.Y. Co.).
35. Index No. 6405/00 (Sup. Ct., Nassau Co. Oct. 19, 2000).
36. *Id*., slip op. at 5 (citations omitted).
37. N.Y.L.J., Apr. 20, 2000, p. 32, col. 6 (Sup. Ct., Nassau Co.).
38. Karjala, *Planning Problems*, *supra* note 22, at 471.
39. *See McConnell v. Hunt Sports Enterprises*, 132 Ohio App. 3d 657, 694, 725 N.E.2d 1193, 1220 (Ohio Ct. App. 1999) (where the court held that while it is not "necessary" under Ohio's LLC dissolution statute to find wrongful conduct, it is "possible that wrongful conduct is the underlying reason for it no longer being practicable to carry on the business of a company" in conformity with the articles of organization and operating agreement).
40. *In re Kemp & Beatley, Inc. (Gardstein)*, 64 N.Y.2d 63, 69, 484 N.Y.S.2d 799 (1984).
41. Karjala, *Planning Problems*, *supra* note 22, at 472.
42. The ULLCA jurisdictions are Alabama, Hawaii, Illinois, Montana, South Carolina, South Dakota, U.S. Virgin Islands, Vermont and West Virginia.
43. ULLCA § 801(a)(4)(v). Section 801 also authorizes judicial dissolution whenever (i) the economic purpose of the company is likely to be unreasonably frustrated; (ii) another member has engaged in conduct relating to the company's business that makes it not reasonably practicable to carry on the company's business with that member; (iii) it is not otherwise reasonably practicable to carry on the company's business in conformity with the articles of organization and the operating agreement; and (iv) the company failed to purchase the petitioner's distributional interest under § 701, which requires the LLC to purchase a dissociated member's distributional interest for its fair value under certain circumstances.
44. Cal. Corp. Code § 17351(a)(2), (5).
45. R. Keatinge & J. Reynolds, *Advisors' Report on the Uniform Limited Liability Company Act* § 4, submitted Mar. 13, 1995, to the Committee on Partnerships and Unincorporated Business Organizations of the Business Law Section of the American Bar Association.
46. New York is in the minority of states that condition standing to seek dissolution for oppressive or other misconduct on a minimum stock ownership percentage. Given that LLCL § 702 at present contains no similar requirement, it would make little sense to include this feature of BCL dissolution in any amendment of § 702.
47. *See In re Kemp & Beatley, Inc.*, 64 N.Y.2d 63, 484 N.Y.S.2d 799 (1984) (adopting a "reasonable expectations" standard under which oppression should be deemed to arise only when the majority conduct substantially defeats expectations that, objectively viewed, were both reasonable under the circumstances and were central to the petitioner's decision to join the venture). For a comprehensive review of judicial dissolution proceedings under BCL § 1104-a, see Peter A. Mahler, *Twenty Years of Court Decisions Have Clarified Shareholder Rights Under BCL §§ 1104-a & 1118*, N.Y. St. B.J., Vol. 71, No. 5 at 28 (1999); Peter A. Mahler, *Decisions Have Set Parameters for Establishing "Fair-Value" of Frozen-Out Shareholder Interests*, N.Y. St. B.J. Vol. 71, No. 6 at 71 (1999); Peter A. Mahler, *Reviewing Shareholder "Freeze-Out" Cases of 2001*, N.Y.L.J., Feb. 8, 2002, p. 1; Peter A. Mahler, *Reviewing Shareholder "Freeze-Out" Cases of 2002*, N.Y.L.J., Jan. 3, 2001, p. 1; Peter A. Mahler, *Annual Review of Shareholder "Freeze-Out" Cases*, N.Y.L.J., Feb. 25, 2000, p. 1.
48. The grounds for dissolution under BCL § 1104 are:

    > (1) that the directors are so divided respecting the management of the corporation's affairs that the votes required for action by the board cannot be obtained; (2) that the shareholders are so divided that the votes required for the election of directors cannot be obtained; or (3) that there is internal dissension and two or more factions of shareholders are so divided that dissolution would be beneficial to the shareholders.

49. *See In re Radom & Neidorff*, 307 N.Y. 1, 119 N.E.2d 563 (1954); *In re Seamerlin Operating Co.*, 307 N.Y. 407, 121 N.E.2d 392 (1954); *In re Gordon & Weiss, Inc.*, 32 A.D.2d 279, 301 N.Y.S.2d 839 (1st Dep't 1969).
50. *See* S. Bahls, *Application of Corporate Common Law Doctrines to Limited Liability Companies*, 55 Mont. L. Rev. 43, 84–90 (1994) (arguing in favor of buyout remedy in LLC dissolution proceedings).

Decisions on Liability for Debts Are Inconsistent for Corporations Dissolved for Unpaid Taxes

By Michael A. Siskin and Richard E. Miller

Companies incorporated in New York State that fail to file annual corporate tax reports[1] for two consecutive years or pay corporate franchise taxes[2] owed to the state for any two years may be involuntarily dissolved, automatically, without notice, by proclamation of the Secretary of State.[3] A corporation so dissolved is authorized only to wind up its affairs, and may not carry out other business.[4]

Either through ignorance of the corporation's dissolution or knowingly, some shareholders and officers of dissolved corporations carry on the business of their corporations, entering into agreements with other businesses and incurring debts in the names of these corporations, as if they had not been dissolved. In some, if not all such circumstances, the shareholders and officers may be held liable for debts incurred in the name of the dissolved corporation.

To date, the Court of Appeals has not addressed this issue, despite an apparent split in authority between state and federal court decisions applying New York State law. Last year, however, the Supreme Court[5] and the Civil Court[6] of New York County followed state precedent and ignored a line of federal cases in holding the shareholders of two dissolved corporations liable for debts incurred after the corporations were involuntarily dissolved by action of the Secretary of State. This article discusses the historical basis for those decisions and the reasoning behind them.

Liability Issues

In 1941, in *Poritzky v. Wachtel*,[7] a state supreme court decision first addressed the issue of the liability of individuals for the debt of a corporation dissolved pursuant to § 203-a of the New York Tax Law for failing to pay franchise taxes. The corporation had no assets when the action was initiated. Thus, if the plaintiff creditor could not collect from the individual, the corporation's president, who entered into the debt, then the debt could not be collected.[8] The court charged the president of the corporation with knowledge of the corporation's dissolution, whether or not he had such actual knowledge.[9] Given that knowledge, the court reasoned that the president "had no further right to obligate the corporation or to continue its business while it remained dissolved."[10] The court held the president personally liable for debts incurred while the corporation was dissolved, reasoning that to hold otherwise "would encourage fraud and abuse."

> [A] former officer of a dissolved corporation could obtain credit and then upon subsequent discovery of the non-existence of the corporation, by merely paying arrears in franchise taxes, could shift the personal liability which the law would otherwise impose upon him back to the corporation.[11]

In 1986, in *Prentice Corp. v. Martin*,[12] the District Court for the Eastern District of New York rejected the holding in *Poritzky*. Unlike the corporation at issue in *Poritzky*, the corporation in *Prentice* had been reinstated sometime after entering into two contracts with the plaintiff.[13] Although the District Court recognized that *Poritzky* was the only case on point,[14] it chose to follow what it perceived as *dictum*.[15] The District Court adopted the reasoning of the New York Court of Appeals, in another context, that individual shareholders and officers are shielded from personal liability, absent a

Michael A. Siskin is an associate at Agovino & Asselta, LLP in Mineola. He graduated from the University of California at Berkeley and received his J.D. degree from the University of Minnesota Law School.

Richard E. Miller is a partner at Kurzman Karelsen & Frank, LLP in New York City. He graduated from New York University and received his LL.B degree from Yale University Law School.

showing of fraud, because a dissolved corporation that continues its business becomes a *de facto* corporation—that is, an entity that is still recognized as a corporation due to its good faith attempts at reinstatement or good faith efforts to maintain its corporate status, but is without the legal status of a *de jure* corporation as a result of some unintentional defect. In addition, the Federal Court opined that the New York legislature would have explicitly created a private remedy had it intended for individuals to become liable.[16]

Two Lines of Reasoning Emerge

In 1987, in *J.M. Lynne Co. v. Geraghty*,[17] the Supreme Court of Connecticut, applying New York law, chose to follow *Poritzky* and rejected *Prentice*. It found that the federal district court's disregard of *Poritzky* in *Prentice* was "critically suspect."[18] The court expressed its concern that the *Prentice* decision was based on cases factually distinguishable.[19] Moreover, it found that the "policy concerns underlying *Poritzky* of discouraging fraud and abuse are certainly legitimate considerations and are as important today as they were in 1941, the year *Poritzky* was decided."[20]

"Fraud and abuse would be encouraged if an officer of a dissolved corporation were allowed to conduct business in the corporate name."

Two years later, the Appellate Division, Second Department, in *Brandes Meat Corp. v. Cromer*, without reference to *Poritzky* or *J.M. Lynne*, rejected the concept of *de facto* existence of a corporation dissolved pursuant to Tax Law § 203-a, and held the individual purporting to act as an agent of the corporation personally liable for the obligations incurred.[21] The court observed that the corporation had not been reinstated, and also found it significant that the transactions at issue were not part of the process of winding up the corporation's affairs.[22] The appellate panel held that the corporation therefore lacked the capacity to be sued and held the individual defendant liable for the obligations.[23]

In *Annicet Assocs. v. Rapid Access Consulting*,[24] in 1997, the Supreme Court in Rockland County specifically followed the holdings in *Poritzky*, *J.M. Lynne* and *Brandes*, and rejected the holding in *Prentice*. The court based its decision on the analysis in *J.M. Lynne* and, "[t]he salient premise of the *Poritzky* case . . . that fraud and abuse would be encouraged if an officer of a dissolved corporation were allowed to conduct business in the corporate name."[25]

In 1999, the U.S. Court of Appeals for the Second Circuit, in *L-Tec Elecs. Corp. v. Cougar Elec. Org., Inc.*,[26] followed the *Prentice* opinion. Curiously, it did so without mention of the growing New York case law on personal shareholder and officer liability. Instead, the Second Circuit discussed a number of factually distinguishable New York State cases concerning recognition of *de facto* corporations, and concluded that reinstatement retroactively validated those contracts entered into during the corporation's period of dissolution.[27]

Just four days after the Second Circuit's decision, in *WorldCom, Inc. v. Sandoval*[28] the Supreme Court in New York County chose to follow the holdings in *Poritzky* and *J.M. Lynne*: "The Connecticut Supreme Court, in applying New York law, concluded that New York courts today would still follow *Poritzky*. The court agrees with that conclusion."[29] The court noted that *Prentice* had been criticized, and rejected it as a proper statement of New York law on this subject.[30] Following *Poritzky*, the court held the individual defendants personally liable for the contractual obligations of the dissolved corporation.[31]

In February 2001, in *Department 56, Inc. v. Bloom*,[32] a Supreme Court decision in Richmond County cited *Prentice* with approval. *Department 56*, however, involved a factual twist. The corporation at issue was a dissolved New Jersey corporation that was being run during its dissolution by its president, who was a New York resident. The decision relied upon the reinstatement of the dissolved corporation in rejecting what it recognized to be the undisputed New York law as articulated in *Poritzky*.[33] The court distinguished *Brandes* on the sole basis that "it involved a corporation that had been dissolved but not reinstated."[34] Despite the court's focus on *Poritzky* and *Prentice*, however, the corporation at issue was not dissolved pursuant to Tax Law § 203-a, but pursuant to New Jersey law. Notwithstanding the New York residence of the corporation's president, the court ultimately found "no merit in plaintiff's contention that New York law should control," and applied the law of New Jersey, thus transforming its opinion on New York case law into *dicta*.[35]

Decisions in 2001

On September 25, 2001, in *Digital Nation Media, Inc. v. Ploni & Assocs., Inc.*,[36] the Civil Court of New York County held, counter to the holding in *Department 56*, that New York law applied when a Delaware corporation doing business in New York was voided for failure to pay taxes. Citing *Poritzky* and its progeny, and ignoring *Prentice*, *L-Tec Elecs.* and *Department 56*, the Civil Court held without further discussion: "In New York State, shareholders and officers of a corporation involuntarily dissolved, are personally liable on contracts consummated while the corporation was in dissolution."

One day after the *Digital Nation Media* opinion, the New York County Supreme Court issued its opinion in the case of *Klein v. Guglielmi*.[37] Citing to *Brandes*,[38] the supreme court held that the dissolved corporation had neither a *de jure* nor a *de facto* existence. The court recognized a split in authority when corporations have been reinstated,[39] but held the individual shareholders personally liable for the debts incurred in the name of the dissolved corporation as a matter of law, because there was no dispute that the corporation had not been reinstated.

De Facto Corporations

The distinction in the case law between reinstated and dissolved corporations can most easily be explained by an understanding of *de facto* corporations. A federal court has stated: "In every decision treating a business as a *de facto* corporation despite the absence of *de jure* corporate status, the business either inadvertently failed to meet the requirements of the law or was operated with the formalities of a corporation and was attempting to achieve legal status."[40] Similarly, the Appellate Division, Second Department states:

> *De facto* recognition requires both a good-faith exercise of corporate powers and colorable compliance with the enabling statute [citations omitted]. A delinquent corporation lacks both prerequisites. There is neither a good-faith exercise of corporate duties, nor compliance with statutes requiring the payment of franchise taxes for the privilege of conducting business in the corporate form.[41]

The reasoning is that when the corporation has been reinstated, by payment of its unpaid franchise taxes, penalties and interest, it has arguably been acting in good faith as a corporation and within "colorable compliance with the enabling statute."

Thus, in *L-Tec Elecs.,* despite its holding, the Second Circuit realized that, "some Appellate Division cases . . . hold that a corporation dissolved for failure to pay taxes has no *de facto* existence."[42] The Second Circuit noted, however, that New York courts often recognize the significance of acting to reinstate the dissolved corporation.

> [E]ven those cases recognize that where the corporation later pays its taxes and is reinstated, its corporate status is restored nunc pro tunc, and any contracts into which it may have entered are retroactively validated. Thus, the district court did not err when it held that reincorporation relieved the individual defendants of any personal liability.[43]

This is seemingly consistent with the language of Tax Law § 203-a that reinstatement procedures "shall have the effect of annulling all of the proceedings theretofore taken for the dissolution of such corporation."[44]

The Split in Authority

The true split in authority in this area is with those cases concerning reinstated corporations. Whereas in *WorldCom* and *Poritzky* the individuals are held liable, the individuals are shielded from liability in *L-Tec Elecs.* and *Prentice*. It is not merely federal courts that believe that individuals should be protected from liability when corporations have been reinstated. Although expressed in *dicta*, the state court in *Department 56* makes it clear that it would have shielded the individuals from liability even if it found that New York law applied.

Parsing out the factual differences between these cases sheds little light on the different outcomes. Although it is interesting to note that the corporations in both *WorldCom* and *Poritzky* were not reinstated until after the complaint had been filed against them, and that, in the *L-Tec Elecs.* and *Prentice* opinions, it is not apparent whether the corporations were reinstated before or after commencement of the actions against the individuals, the corporation in *Department 56* also was reinstated only after the dissolution "was brought to [the president's] attention by plaintiff."[45] Further, none of the opinions rely on this fact in their analysis.

Analyzing the Split in Authority

It is difficult, if not impossible, to reconcile these decisions. There is no hint of significant factual differences. These decisions contain little, if any, discussion of the circumstances that led to the dissolution of the corporations. To attempt to understand these cases, it is helpful to look to case law involving corporations dissolved for failure to comply with the corporate tax laws, but where the issue was not whether individuals may be held liable for the debts of dissolved corporations.

Where defendants seek to deny the existence of corporations to avoid corporate liability, state courts tend to find *de facto* existence and hold the corporations liable. For example, a corporation that was dissolved for non-payment of taxes and continued its business under a new name could not plead dissolution in order to avoid its obligations.[46] "Any other conclusion would enable [the dissolved corporation] to profit by its own nonpayment of taxes."[47] More obviously, where, prior to default, a company made all payments necessary for reinstatement of the corporation, except the payment of a $55 reinstatement fee, the company was found to be in colorable compliance with the statute and, thus, a *de facto* corporation, and liable for its remaining debt.[48]

In one case where the corporation sought to prove its *de facto* existence in order to collect on a fire insurance policy, the Second Department, Appellate Division, even found that, absent reinstatement, a dissolved corporation has no capacity to sue for matters arising outside of the course of winding up the corporation's affairs.[49]

An individual aware of the dissolution of the corporation may not, for his or her own advantage, enforce an agreement entered into by that individual on behalf of the nonexistent corporation.[50] This is because the individual "knew, or should have known, that the Agreement was invalid, and cannot now complain that it should be enforced for his benefit."[51]

Even in the unusual situation where an individual sought to deny the existence of a corporation in order to avoid personal liability, the courts have held that the company was a *de facto* corporation and found the individual liable. Thus, where a guarantor on a line of credit, opened by a corporation that had previously been dissolved in Florida for failure to pay its franchise taxes, sought to avoid personal liability for sums still due, the corporation was found to have opened the line of credit as a *de facto* corporation, and the guarantor was held liable.[52]

The trend of these state cases is to provide a means for creditors to collect on their debts, but limit the ability of individuals and corporations to manipulate the status of the corporation for their own benefit. In other words, wrongdoers do not benefit from their own misdeeds.

Following this logic, one should expect, in the context of a reinstated corporation, that if the courts determine that the debts were incurred without knowledge of the corporation's dissolution, and such dissolution occurred innocently and without neglect or carelessness, perhaps as evidenced by attempts to rectify the temporary lapse in compliance, and not in an attempt to use the Tax Law for personal gain, such individuals will not be held liable. Otherwise, they will.

It may be argued that "colorable compliance" should be determined at the time when the debts are incurred. Such a rule would be consistent with the purpose of recognizing *de facto* corporations, which is to avoid penalizing innocent shareholders and officers in situations where the only intent is to act as a corporation, but corporate status fails through some inadvertent defect. How a corporation acts before and after the period of dissolution seems irrelevant to its actions while it was dissolved. The issue is, or should be, whether the shareholder can justify the failure to keep the corporation in good standing.

If a corporation has made substantial efforts to pay its franchise taxes, but, for example, the check never arrived at its intended destination, and debts were incurred while the shareholders and officers were ignorant of such dissolution because they thought they were in compliance, *de facto* existence should be recognized for the period prior to reinstatement. If, however, corporations simply do not pay their taxes, whether purposefully or through carelessness, and are dissolved by proclamation therefor, all "colorable compliance" occurring after the fact, including reinstatement, should not transform the faulty actions of the corporation at the time that debt is incurred.

To deny individual liability would be to encourage unscrupulous shareholders and officers to stop paying their franchise taxes in order to receive free goods and services from unsuspecting companies.

One reason for allowing collection from individual defendants is revealed in *dicta* in *Animazing Entertainment, Inc. v. Louis Lofredo Associates*.

> It would be inequitable to allow individuals who form contracts on behalf of nonexistent corporations to avoid liability because their misrepresentations resulted in a contractual defect. The plaintiffs in those cases believed that they had entered into valid contracts with corporations and since those corporations did not exist, had no remedy except against the individuals who acted as agents of those purported corporations.[53]

To deny individual liability would be to encourage unscrupulous shareholders and officers to stop paying their franchise taxes in order to receive free goods and services from unsuspecting companies that have no reason to know whether their customers have been dissolved by proclamation. Further, "[r]ecognition of *de facto* status would directly subvert the effectiveness of the sanctions for franchise tax delinquency, removing all incentive for a dissolved corporation to seek reinstatement."[54] To prevent fraud and abuse, it must be the rule that individuals be held responsible for debts they incur in the name of dissolved and insolvent corporations. If a company can prove that dissolution was truly inadvertent and not due to neglect, however, and it quickly rectified the default by seeking reinstatement, creditors must be left to rely on the solvency of their customers.

1. *See* Tax Law § 192.
2. *See* Tax Law §§ 180–207-b.
3. Tax Law § 203-a.
4. BCL § 1005(a)(1), expressly incorporated by Tax Law § 203-a(10).
5. *Klein v. Guglielmi*, N.Y.L.J., Oct. 18, 2001, p. 20, col. 4.
6. *Digital Nation Media, Inc. v. Ploni & Assocs., Inc.*, N.Y.L.J., Oct. 4, 2001, p. 19, col. 2.
7. 176 Misc. 633, 27 N.Y.S.2d 316 (Sup. Ct., Putnam Co. 1941).
8. *Id.* at 635.

9. *Id.* at 634.
10. *Id.*
11. *Id.*
12. 624 F. Supp. 1114 (E.D.N.Y. 1986).
13. *Id.* at 1114.
14. *Id.* at 1115.
15. *Id.* at 1115–16 (discussing *Garzo v. Maid of the Mist Steamboat Co.*, 303 N.Y. 516, 104 N.E.2d 882 (1952)). Significantly, in *Garzo*, the corporation inadvertently expired according to its charter, and was not involuntarily dissolved for failure to comply with the Tax Law. This distinction is critical in that one requirement for *de facto* corporation status is "colorable compliance with the enabling statute." The corporation in *Garzo* apparently complied with all of its statutory requirements, unlike corporations which are dissolved for failure to file reports or pay taxes.
16. *Prentice*, 624 F. Supp. at 1116.
17. 204 Conn. 361, 528 A.2d 786 (1987).
18. *Id.* at 371.
19. *Id.* at 372.
20. *Id.* at 374.
21. *Brandes Meat Corp. v. Cromer*, 146 A.D.2d 666, 667, 537 N.Y.S.2d 177 (2d Dep't 1989).
22. *Id.* at 666.
23. *Id.* at 667.
24. 171 Misc. 2d 861, 865, 656 N.Y.S.2d 152 (Sup. Ct., Rockland Co. 1997).
25. *Id.* at 864.
26. 198 F.3d 85 (2d Cir. 1999).
27. *Id.* at 87.
28. 182 Misc. 2d 1021, 701 N.Y.S.2d 834 (Sup. Ct., N.Y. Co. 1999).
29. *Id*. at 1025.
30. *Id.*
31. *Id.* at 1026.
32. 186 Misc. 2d 901, 720 N.Y.S.2d 920 (Sup. Ct., Richmond Co. 2001).
33. *Id.* at 903–905.
34. *Id.* at 904.
35. *Id.* at 905.
36. Index No. 21715 CV 01, 2001 N.Y. Misc. LEXIS 1020 (Civ. Ct., N.Y. Co. Sept. 25, 2001).
37. Index No. 100471/00, 2001 N.Y. Misc. LEXIS 755 (Sup. Ct., N.Y. Co. Sept. 26, 2001).
38. *Brandes Meat Corp. v. Cromer*, 146 A.D.2d 666, 667, 537 N.Y.S.2d 177 (2d Dep't 1989).
39. The supreme court observed that individual shareholders and officers were held liable for corporate debts incurred while corporations were dissolved by proclamation even though the corporations were later reinstated in *WorldCom, Inc. v. Sandoval*, 182 Misc. 2d 1021, 701 N.Y.S.2d 834 (Sup. Ct., N.Y. Co. 1999), and *Poritzky v. Wachtel*, 176 Misc. 633, 27 N.Y.S.2d 316 (Sup. Ct., Putnam Co. 1941), but were shielded from such liability in *Department 56*, 186 Misc. 2d 901, *L-Tec Elecs. Corp. v. Cougar Elec. Org., Inc.*, 198 F.3d 85 (2d Cir. 1999), and *Prentice Corp. v. Martin*, 624 F. Supp. 1114 (E.D.N.Y. 1986) (wherein the district court held that individual shareholders could be held liable upon a showing of fraud or bad faith).
40. *Animazing Ent., Inc. v. Louis Lofredo Assocs.*, 88 F. Supp. 2d 265, 269 (S.D.N.Y. 2000).
41. *Lorisa Capital Corp. v. Gallo*, 119 A.D.2d 99, 110–11, 506 N.Y.S.2d 62 (2d Dep't 1986) (citations omitted); *see De George v. Yusko*, 169 A.D.2d 865, 867, 564 N.Y.S.2d 597 (3d Dep't 1991).
42. *L-Tec Elecs.*, 198 F.3d at 87.
43. *Id.*
44. Tax Law § 203-a(7).
45. *Department 56 v. Bloom*, 186 Misc. 2d 901, 902, 720 N.Y.S.2d 920 (Sup. Ct., Richmond Co. 2001).
46. *D & W Cent. Station Alarm Co. v. Copymasters, Inc.*, 122 Misc. 2d 453, 471 N.Y.S.2d 464 (Civ. Ct., Queens Co. 1983).
47. *Id.* at 457.
48. *Ludlum Corp. Pension Plan Trust v. Matty's Superservice, Inc.*, 156 A.D.2d 339, 548 N.Y.S.2d 292 (2d Dep't 1989).
49. *Lorisa Capital Corp. v. Gallo*, 119 A.D.2d 99, 111, 506 N.Y.S.2d 62 (2d Dep't 1986).
50. *Animazing Ent., Inc. v. Louis Lofredo Assocs.*, 88 F. Supp. 2d 265, 271 (S.D.N.Y. 2000).
51. *Id.*
52. *National Bank of N. Am. v. Paskow*, 75 A.D.2d 568, 427 N.Y.S.2d 262 (1st Dep't 1980), *aff'd*, 53 N.Y.2d 953, 441 N.Y.S.2d 443 (1981).
53. *Animazing Ent.*, 88 F. Supp. 2d at 271.
54. *Lorisa Capital Corp.*, 119 A.D.2d at 111. But see *Department 56 v. Bloom*, 186 Misc. 2d 901, 904, 720 N.Y.S.2d 920 (Sup. Ct., Richmond Co. 2001), concluding that, since the problem only arises when corporations have insufficient funds to pay their debts, they may also have insufficient funds for reinstatement, and thus, the individual shareholders or officers cannot expect to be shielded from liability. The court seems to ignore the reasonable possibility that a shareholder having the thousands of dollars necessary to pay the back taxes and penalties could incur substantially higher debts in the name of the corporation, and avoid substantial personal debt merely by reinstating the corporation at his or her own expense. The court in *Department 56* further suggests that the creditor who is shielded from seeking recompense from the individual shareholder and officers would be in the same position with an insolvent reinstated corporation as it would be with an insolvent corporation that was never dissolved. Of course, the corporation that was never dissolved has not attempted to manipulate the tax laws in order to avoid payment to its creditors.

Correction

In the March/April 2002 issue of the *Journal* the article entitled *Enhanced Notice Requirements in Property Tax Foreclosure Cases Give Owners More Protection* (p. 48) states that the amendment to RPTL § 1125 requires that notice of a tax foreclosure must now be sent by certified mail, return receipt requested. In fact, the change adds only the requirement of a certified mailing, and *not* the use of a return receipt card.

RPTL § 1125 also states: "The failure of an intended recipient to receive any such notice shall not invalidate any tax or prevent the enforcement of the same as provided by law" (§ 1125(3)(b)), which makes it clear that no greater burden of proof has been placed on the municipality.

A review of the legislative history shows that the original proposal did include the return receipt requirement but it was subsequently omitted.

Black Mold Suits Yield Some Large Personal Injury Verdicts, But Their Future Is Uncertain

By Brian Del Gatto and Robert J. Grande

In the scientific community and courtrooms across the nation, a new debate is emerging about the health risks from exposure to certain types of mold. This debate has spurred many plaintiffs' attorneys to sue for exposure to mold. These suits have resulted in some generous verdicts to certain plaintiffs, prompting the insurance industry and residential building owners to re-think their policies concerning mold.

New York has not been immune to this debate. In the New York County Supreme Court, 495 apartment residents of the Henry Phipps Plaza in Manhattan sued Phipps Plaza South and Phipps Housing Services, Inc., the entities in charge of maintenance of the buildings, for nearly $9 billion in damages.[1] According to the plaintiffs' attorney, Steven Goldman, residents suffered skin rashes, infected lungs and mouths, and bleeding from noses and gums, and in some cases short-term memory loss, constant fatigue and death.[2] Plaintiffs claimed that the building management did nothing to notify the plaintiffs of the danger of the condition and ignored the requests of residents to eliminate the mold problem.[3] According to Goldman, water leakage spurred the growth of the mold.[4]

In August 2001, Justice Louise Gans denied the plaintiffs' motion for class certification, but agreed to a joint trial of seven cases.[5] After the trial began, the court issued a gag order. On November 29, 2001, after several weeks of an expected two-month trial involving only seven of the residents, the parties reached a confidential settlement.[6] The *New York Post* reported that the total settlement amount for all 495 residents was approximately $1.18 million.[7] Unless definitive scientific evidence substantiating or refuting these claims becomes available, the Henry Phipps lawsuit is not likely to be the last.

Background

The controversy concerning "toxic mold" apparently began in Cleveland about seven years ago. Between 1993 and 1996, at least 34 Cleveland area infants were purportedly made ill by exposure to a greenish-black mold known as *stachybotrys atra* (also known as *stachybotrys chartarum*).[8] At the time, infants were coughing up blood and subject to chronic cough and congestion, among other symptoms.[9] Ultimately, several children in the Cleveland area developed pulmonary hemorrhage and 10 died.[10]

The U.S. Centers for Disease Control and Prevention (CDC) sent researchers to the Cleveland area to conduct tests. Initially, the CDC released a study that suggested a causal connection between *stachybotrys chartarum* and pulmonary hemosiderosis. However, in 1999, the CDC admitted that its study was flawed due to small sample size and improper testing procedures, among other reasons.[11]

Stachybotrys atra "can grow on material with a high cellulose and low nitrogen content, such as fiberboard, gypsum board, paper, dust and lint. Growth occurs when there is moisture from water damage, excessive humidity, water leaks, condensation, water infiltration and flooding. Constant moisture is required for its growth."[12] The most common health complaints from mold infestation include hay-fever-like allergic symp-

Brian Del Gatto is a member of the law firm of Wilson, Elser, Moskowitz, Edelman & Dicker LLP (e-mail delgattob@wemed.com). He litigates and tries high exposure cases in both New York and Connecticut, where his practice is focused on products/general and environmental defense litigation. He graduated from Brooklyn College and Quinnipiac School of Law.

Robert J. Grande is an associate at the White Plains office of Wilson, Elser, Moskowitz, Edelman & Dicker LLP. His practice is focused on general/environmental liability and employment law. He graduated from Boston College and Suffolk University Law School.

toms.[13] However, as with the infants in Cleveland, some claim that mold has been responsible for more serious health conditions such as pulmonary hemorrhage, memory loss and death.

It has been reported that perhaps 50% of all homes may have some level of *stachybotrys* infestation.[14] Unfortunately, there are no federal standards for detecting what constitutes a "dangerous" level of exposure.[15] The CDC maintains at the present time that there is no proven causal link between certain fatal conditions and mold exposure, but acknowledges that moldy homes are unhealthy.[16] Although proving such claims may be difficult, the infestation is so common that there is the potential for almost anyone to claim that mold is responsible for illness.

Property Damage

Aside from personal injury claims, interrelated or independent claims for property damage are also possible. The New York City Department of Health's Bureau of Environmental & Occupational Disease Epidemiology has produced the "Guidelines on Assessment and Remediation of Fungi in Indoor Environments."[17] This is not a legal mandate but a document with many useful recommendations to building engineers and management. The guidelines urge that the presence of mold, water damage, or musty odors be addressed immediately. In all instances, any source(s) of water must be stopped and the extent of water damage determined. Water-damaged materials should be dried and repaired.

Removal of mold can often become a complicated and expensive task. The guidelines recommend respiratory protection, gloves and eye protection. Extensive contamination—particularly if heating, ventilating, air conditioning (HVAC) systems or large occupied spaces are involved—should be assessed by an experienced health and safety professional and remediated by personnel with training and experience handling environmentally contaminated materials. Lesser areas of contamination can usually be assessed and remediated by building maintenance personnel. Contaminated materials that cannot be cleaned must be removed in sealed plastic bags.

A case in Texas demonstrates how costly some of these claims can be if an insurer or home owner does not act expeditiously to remove materials damaged by mold. According to the facts, Mary Melinda Ballard had a bathroom plumbing leak. When the wood did not dry, her contractor advised removing the floor because of the potential of mold. Ballard contacted her insurer and advised of the potential for mold infestation. Ballard's insurer refused to pay for the removal of the floor. Eventually, the damage spread to windows, door frames, stairs and walls. Her family vacated the home. Ballard's insurer agreed to settle the lawsuit for more than $100,000, but the plaintiff's contractor claimed that the damage exceeded this amount. In June 2001, despite exclusion of experts' testimony concerning personal injury, a Texas jury awarded Ballard $32 million in her bad faith lawsuit against her insurance company.[18]

Testimony on Causation

At present, proving physical injury from toxic mold requires expert testimony. The long-standing approach in New York to resolving the problem of ensuring reliability of expert testimony has been the application of the "*Frye*" rule or the "general acceptance" test.[19] Under this approach, expert testimony based on scientific principles or procedures is admissible in New York only after such principles or procedures have gained general acceptance in the relevant discipline.[20] It is an open question how New York courts will consider expert testimony in toxic mold cases.

The guidelines of the New York City Department of Health provide support for claims involving allergic symptoms related to mold. The executive summary of the document provides in relevant part that

> [f]ungi in buildings may cause or exacerbate symptoms of allergies (such as wheezing, chest tightness, shortness of breath, nasal congestion, and eye irritation), especially in persons who have a history of allergic diseases (such as asthma and rhinitis). Individuals with persistent health problems that appear to be related to fungi or other bioaerosol exposure should see their physicians for a referral to practitioners who are trained in occupational/environmental medicine or related specialties and are knowledgeable about these types of exposures.

Although many scientists may claim that mold exposure can cause some illnesses, it seems inappropriate for courts to conclude at this time that there is a "general acceptance" of the concept that mold is responsible for serious respiratory problems. Nevertheless, several courts appear to be headed in this direction.

The Supreme Court of Nebraska recently held that it was an abuse of discretion to refuse to admit expert testimony bolstering claims of severe asthma attacks due to mold, requiring hospitalization. In *Mondelli v. Kendel Homes Corp.*,[21] the plaintiffs sought to introduce testimony from a toxicologist about the high level of mold and the potential that repeated exposure could result in permanent lung damage. The trial court had held that the toxicologist could not testify regarding causation because no standards existed in the scientific community concerning the level of mold that is acceptable in a house. The supreme court reversed, acknowledging that there is no acceptable standard for mold levels, but finding that such testimony is admissible because the scien-

tific community has generally accepted the principle that a connection exists between the presence of mold and health.

Similarly, the Supreme Court of Delaware upheld a verdict against a landlord for almost $1 million that was supported by expert testimony after two tenants with leaks and mold in their apartments started experiencing health problems.[22] According to the facts alleged by the plaintiffs, plaintiff Elizabeth Stroot had suffered from allergies and asthma since childhood. However, the frequency and severity of her asthma attacks significantly increased after she moved to her apartment, requiring hospitalization on several occasions. Despite other potential causes for the plaintiff's health problems, including being a smoker and the owner of a dog even though she was allergic to dogs, the court concluded that the methodology used by the plaintiffs' experts had been reviewed by peers and was generally accepted in the scientific community. The court opined, "The foundation for an expert's causation opinion need not be established with the precision of a laboratory experiment."[23] Any other factors that could have caused the plaintiffs' injuries went to the weight of the evidence, not admissibility.

The same characteristics that make toxic mold claims attractive to litigious hypochondriacs make it especially difficult for an individual with potentially legitimate adverse health effects from mold to detect or prove.

The same characteristics that make toxic mold claims attractive to litigious hypochondriacs make it especially difficult for an individual with potentially legitimate adverse health effects from mold to detect or prove. As indicated above, mold exposure could manifest itself merely by allergic reactions. Decisions in the Appellate Division, Third Department, dealing with "sick building" claims demonstrate the difficulty of proving the causal link between mold exposure and compensable illness, at least before the Workers' Compensation Board. In *Nicholson v. Mohawk Valley Community College*,[24] a secretary allegedly began experiencing headaches, nosebleeds, rashes, itching and chronic cough when her work site was moved to a newly renovated building. She filed a workers' compensation claim alleging exposure to dust and other allergens. Initially, a Workers' Compensation Law judge and a panel of the Workers' Compensation Board found that the claimant had proved a claim for "sick building syndrome." The full Workers' Compensation Board reversed this decision, however, and the Appellate Division affirmed. Although the claimant had several physicians testify that her symptoms were caused or exacerbated by poor air quality at work, none could identify a specific allergen that was present in the claimant's work environment and had caused her symptoms. Her allergies to dust, mold and other common allergens could not be exclusively confined to her workplace environment.

In *Knapp v. Vestal Central School District*,[25] a claimant alleged that "multiple chemical sensitivity," including aches, pains, headaches and memory loss resulted from her employment in a "sick building." A Workers' Compensation Law judge held that the claimant had failed to prove that she had been exposed to any type of chemical in her work environment sufficient to trigger the development of "multiple chemical sensitivity." The Appellate Division affirmed, noting that the claimant had admitted to experiencing fatigue and other symptoms in her work environment for more than 20 years. She had also admitted that she experienced similar problems in other locations, thereby undercutting any claim that the building where she worked was a sick building.

New York Statute of Limitations

Aside from any issues of causation, New York's statute of limitations may bar many potential claims. Civil Practice Law and Rules section 214-c(2) (CPLR) provides in relevant part that the three-year period to commence a lawsuit caused by the latent effects of exposure to any substances or combination of substances must be computed from "the date of the discovery of the injury by the plaintiff or from the date when through the exercise of reasonable diligence such injury should have been discovered by the plaintiff, whichever is earlier." If the discovery of the cause of the injury occurred less than five years after the discovery of the injury, a plaintiff must commence litigation within one year of the discovery of the cause of the injury.[26] Indeed a potential plaintiff exposed to mold may have common allergic responses to the mold, but will not believe that the symptoms are adequate to commence litigation. When more serious symptoms manifest themselves, a lawsuit may be too late.

In *Chavious v. Tritec Asset Management, Inc.*,[27] the plaintiffs alleged that they were exposed to certain chemicals or other toxic substances during their employment at a radiation oncology treatment center.[28] The court granted the defendant's motion for summary judgment, concluding that the action was barred by the statute of limitations. Although the plaintiffs claimed

that their symptoms worsened and became a permanent condition at a later date, evidence showed that the plaintiffs had been suffering from symptoms for over three years.

Similarly, in *Harley v. 135 East 83rd Owners Corp.*,[29] the plaintiff started experiencing symptoms shortly after leaks were discovered in her apartment in 1987. It was not until March 1990 that the plaintiff's chronic condition was attributed to mold flourishing in her damp apartment. Nevertheless, the court concluded that the lawsuit, not filed until January 28, 1993, was untimely because it was begun more than three years after the discovery of her injury and more than one year after the discovery of the cause of her injury.

Conclusion

With the possibility of large verdicts, New York can expect a proliferation in the number of lawsuits claiming injury due to toxic mold. Although there will be numerous obstacles for any plaintiff to achieve success, including problems with proof of causation and the running of the statute of limitations, the potential rewards to successful plaintiffs for scientifically questionable claims may be too hard to resist. For some plaintiffs, black mold may in fact be black gold, while for others it may be "fools' gold," where much time and expense is spent for modest or no returns on that investment.

1. *Confidential Settlement Reached in New York Apartment Case,* Mealey's Litig. Rep.: Mold, Vol. 1, No. 12 (Dec. 2001).
2. *Toxic-Mold Case is Settled by Landlord, Tenants*, *available at* <http://www.moldupdate.com/articles/0102e.htm> (visited May 8, 2002).
3. Paul H.B. Shin & Derek Rose, *Having a Mold Complex*, N.Y. Daily News, Sept. 10, 2001 at 3.
4. Helen Peterson, *Mold Suit Nets Tenants 1G*, N.Y. Daily News, Dec. 16, 2001 at 48.
5. *See supra* note 1.
6. Dareh Gregorian, *Kips Bay 'Toxic Mold' Suit Settled*, N.Y. Post, Dec. 12, 2001 at 22.
7. *Id.*; *see supra* note 1.
8. *Pulmonary Hemorrhaging: CDC: Mold Not Cause of Mid-90s Ohio Infant Deaths*, NewsRx. Mar. 20, 2000, at 27.
9. *Id*.
10. *Id*.
11. Mark Moran, *Answers Prove Elusive in Mold-Linked Deaths* (July 26, 2000), *available at* <http://www.ehw.org/Healthy_House/HH_Toxic_Mold.htm.>
12. Questions and answers on *stachybotrys chartarum* and other molds are avalable at <http:www.cdc.gov/nceh/airpollution/mold/stachy.htm> (last updated Mar. 30, 2002).
13. *Id.*; Victoria L. Chase, *Mold Litigation is Likely to Spread*, The Legal Intelligencer, Sept. 20, 2001, *available at* <http://www.mgklaw.com/articles/moldlitigationis likelytospread.htm> (visited May 8, 2002).
14. *News 10 Close-up: Toxic Mold: Frequently Asked Questions*, <http://www.kxtv10.com/news-special/close-up/mold/questions.htm> (visited May 8, 2002).
15. *See supra* note 13.
16. *See supra* note 12.
17. The guidelines can be found online at <http://www.nyc.gov/html/doh/html/epi/moldrpt1.html>.
18. *Jury Awards $32 Million to Texas Homeowner in Mold Coverage Case*, Mealey's Litig. Rep.: Mold, Vol. 1, No. 6 (June 2001).
19. *See Frye v. United States*, 293 F. 1013 (D.C. Cir. 1923); *People v. Wesley*, 83 N.Y.2d. 417, 611 N.Y.S.2d 97 (1994).
20. *See Wesley*, 83 N.Y.2d at 422; *Collins v. Welch*, 178 Misc. 2d 107, 678 N.Y.S.2d 444 (Sup. Ct., Tompkins Co. 1998).
21. 262 Neb. 263, 631 N.W.2d 846 (Neb. 2001).
22. *See New Haverford P'ship v. Stroot*, 772 A.2d 792 (Del. 2001).
23. *Id*. at 800.
24. 274 A.D.2d 677, 711 N.Y.S.2d 542 (3d Dep't 2000).
25. 247 A.D.2d 667, 668 N.Y.S.2d 718 (3d Dep't 1998).
26. *See* CPLR 214-c(4).
27. 284 A.D.2d 362, 726 N.Y.S.2d 676 (2d Dep't 2001).
28. It is uncertain whether this is a toxic mold case. However, in the court's opinion there is a reference to an expert's affidavit that indicated that the air and mildew levels were found to be within acceptable levels.
29. 238 A.D.2d 136, 655 N.Y.S.2d 507 (1st Dep't 1997).

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Should Mediation Be Available as An Option to Reduce Litigation in Contested Guardianship Cases?

BY LEONA BEANE

The New York practice of commencing guardianship proceedings as an adversarial process[1] has the advantage of protecting the due process rights of the "alleged incapacitated person" (AIP), but it also encourages litigation that can become extremely contentious. That was not the intent of the Law Revision Commission when it recommended that Article 81 of the Mental Hygiene Law (MHL) be adopted, nor was it the intent of the legislature[2] when it enacted the commission's proposals.

Nevertheless, in the years since April 1, 1993, when Article 81 replaced the old Articles 77 and 78 that provided for "conservators" to assist with financial needs and "committees" for incompetents, experience has provided numerous examples of how contentious guardianship litigation can get out of hand. That raises the question of whether there is a better way to handle guardianship proceedings.

Mediation Tool

One solution is to consider mediation[3] as a tool to assist in the resolution of a litigated guardianship proceeding. The facilitative mediation model, where an experienced mediator acts as facilitator,[4] is one possibility for guardianship disputes. The mediator should be required to have an understanding of the issues that arise in guardianship law and be in a position to help parties assess their options and recognize alternatives.

Currently, the states of Michigan[5] and Washington[6] have statutes that provide for mediation in guardianship proceedings. In Utah, a local rule[7] provides for mediation in all contested probate cases. Mediation in contested guardianship proceedings has been studied extensively at the Center for Social Gerontology in Ann Arbor, Mich. The center has been providing training for attorneys, mediators and others involved in guardianship proceedings, and has set up pilot programs in four different cities.[8]

In the *Adult Guardianship Mediation Manual*, it states: "A court is limited to statutory solutions. . . . The emphasis is on naming a guardian, not on resolving the problem. Mediation, on the other hand, focuses on solving the problem. Mediation allows the persons involved to search for more creative responses."[9]

Mediation is widely used in the New York court system's ADR programs.[10] Situations that make mediation appropriate include the need or desire of the disputing parties to protect an ongoing relationship, improve communication, bring emotional issues into the open, and create a unique solution without being bound by legal constraints.[11] Mediation can offer available alternatives that are not typically used by a court. Courts rarely have the time to work with parties to explore alternatives that would avoid guardianship or develop personalized limited guardianships.[12]

Issues to Consider

Before appointing a guardian, the court must determine the appointment is necessary to provide for the personal needs (including food, clothing, shelter, health care, or safety) and/or to manage the property and financial affairs of the AIP, and in addition, that the AIP agrees[13] to the appointment, or that the AIP is "incapacitated."[14] Mediation may assist in obtaining the agreement of the AIP and the other parties. The determination of "incapacity" is based on clear and convincing evidence that the AIP is likely to suffer harm because the AIP is unable to provide for personal needs and/or property management and cannot adequately understand and appreciate the nature and consequences of such inability.[15] Although this may appear to be a simple and straightforward standard,[16] in many situations it can become embroiled in convoluted contentious liti-

LEONA BEANE, a professor emeritus at Baruch College (CUNY), taught law for 21 years and is a practicing attorney. She has written and lectured extensively on matters relating to guardianships, in particular the provisions of Article 81 of the Mental Hygiene Law, and is chair of the Article 81 Sub-Committee of the Legal Problems of the Aging Committee of the Association of the Bar of the City of New York. A graduate of City College, she received her law degree from New York Law School.

Current Article 81 Procedures

Although the guardianship procedure established by Article 81 of the N.Y. Mental Hygiene Law attempted to anticipate the difficult personal circumstances that are often present in these proceedings, conflicts and unresolved issues continue to pose problems.

A few of the issues involve the roles of the court evaluator and the court-appointed counsel for the alleged incapacitated person (AIP) and the interaction between them. The issues become more difficult when "interested parties" also retain counsel.

The court evaluator, as an investigator for the court, is obliged to meet with the AIP and explain the nature and possible consequences of the proceeding (in a manner the AIP can reasonably be expected to understand). The evaluator should also advise the AIP of her or his rights, including the right to counsel, and describe the duties of a guardian. The evaluator must write a report to the court, providing responses to 17 different questions listed in the statute.[1]

Legal counsel must be appointed if the petition seeks a temporary guardian, injunctive relief such as the freezing of a bank account, or if several other circumstances apply.[2] The role of legal counsel is to be an advocate for the AIP, ensure that the AIP's point of view is presented to the court, and offer arguments to protect the AIP's rights.[3] If unable to communicate or obtain clear direction from the AIP, counsel should still advocate for the AIP and protect the AIP's rights in the proceeding. In such situations, experience has shown that some counsel will vigorously oppose the proceeding while others take a "best interests" position. It is not clear which approach is the correct one.

If counsel is appointed, the court may dispense with a court evaluator, often in an effort to reduce the expense for the AIP. If the case appears to be complex, however, the judge may well appoint both so that the court will have the benefit of the evaluator's neutral report and conclusions.

Most courts permit the court evaluator (who is an attorney) to cross-examine witnesses and introduce evidence and present witnesses. Some do not, however, claiming that the evaluator is the court's witness. The Court of Appeals has ruled the court evaluator is not a party to the proceeding,[4] and thus is not able to appeal.

The court evaluator's report should be an independent evaluation,[5] not a "rubber stamp" of the way others see the AIP. The report may include inferences and conclusions that are negative and adverse concerning some of the parties. In the adversarial situation, the court evaluator may thus be harassed by others who disagree with aspects of the report.

The court evaluator's report may be admitted into evidence[6] (even though it may contain hearsay) if the court evaluator testifies and is subject to cross-examination. In the hands of a litigious attorney, this aspect of the proceeding may become highly confrontational and convoluted, and may subject the court evaluator to extensive vexatious cross-examination, particularly if an attorney for the AIP or a family member is intent on obstruction.

The court may order disclosure of the AIP's medical, psychological and/or psychiatric records, notwithstanding the physician/patient privilege, if the court determines such records are likely to contain information that will assist the evaluator in completing the report.[7]

At the hearing, any party to the proceeding has the right to present evidence, call witnesses, cross-examine witnesses, and be represented by counsel of her or his choice.[8] Many of the AIP's relatives must be served with the petition and order to show cause, even if they have not had contact with the AIP for many years, but it is not clear whether all of them are "parties to the proceeding" and have the right to present evidence, call witnesses, cross-examine witnesses, and be represented by counsel. A person known to have a power of attorney (and perhaps being accused of financial abuse) would also need to be served, but should that person have all the rights of a "party"?

The hearing must be conducted in the presence of the AIP,[9] either at the courthouse or where the AIP resides so that the court can obtain its own impression of the AIP's capacity. If there is uncontested evidence that the person could not meaningfully participate in the hearing, some judges will waive the requirement.

At the hearing, the court may waive the rules of evidence for good cause.[10] If litigious attorneys are involved, they are likely to raise objections. A determination that the person is incapacitated must be based on clear and convincing evidence,[11] a very high standard. Litigious attorneys typically raise numerous objections to prevent the standard from being met, even where the AIP needs assistance and is at risk.

1. MHL § 81.09(c)(5).
2. *See* MHL § 81.10(c).
3. *See* McKinney's Law Revision Commission Comments, MHL § 81.10.
4. *In re Lula XX*, 88 N.Y.2d 842, 644 N.Y.S.2d 683 (1996).
5. McKinney's Law Revision Commission Comments, MHL § 81.09.
6. MHL § 81.12(b).
7. MHL § 81.09(d). But see *In re Tara X*, N.Y.L.J., Sept. 18, 1996, p. 27 (Suffolk Co.), where Justice Prudenti denied the court evaluator's request to review medical records because the AIP objected. This decision also explains the conflicting interaction that may be present between the court evaluator and legal counsel.
8. MHL § 81.11(b).
9. MHL § 81.11(c).
10. MHL § 81.12(b).
11. MHL § 81.12(a).

gation, with numerous objections along the way, thus obstructing the orderly flow of the guardianship proceeding.

The issue of incapacity itself should *not* be decided by mediation, because that is a legal issue requiring a decision by a judge.[17] Thus, there must be a court determination of incapacity before a guardian is appointed. But, if all the other issues are resolved by a mediated agreement, any necessary hearing should proceed quite smoothly.

At the court hearing, the judge must determine whether there is sufficient evidence that the person meets the legal definition of incapacity, and this must be proven by clear and convincing evidence.[18] In mediation, a legal finding of incapacity is not the issue, and thus, a mediator could focus instead on the needs of the AIP and possibly the needs of other family members.

If the court determines the person is incapacitated and that appointment of a guardian is necessary, the court makes its findings on the record.[19] The judge then has three dispositional alternatives: to dismiss the petition, to provide for protective arrangements and single transactions, or to appoint a guardian.[20]

Mediation Alternatives

With the use of mediation, there may be other alternatives for the court, such as a very limited guardianship. Although the law provides for protective arrangements, authorizations for single transactions and the appointment of "special" guardians, that occurs only after a determination of incapacity.[21] However, via a mediated agreement, there could be a very limited-purpose guardian, authorized to provide whatever is needed to assist the AIP, and nothing further.

A mediated agreement leading to the appointment of a specific named guardian with specific tailored powers could have great value when the issues might otherwise foster highly contentious litigation, reflecting a "power struggle" among members of a dysfunctional family seeking to acquire "control" over the elderly or disabled person. Quite frequently, there are many ongoing disputes among the family members. The legal issues presented in court are usually not the underlying issues causing the family turmoil. Sometimes there are no contested legal issues, but there are still family disputes or concerns that need to be addressed.[22]

Mediation can be most effective, both in reaching a solution and in allowing parties to hear and understand each other, if they try mediation early in the process, before positions have been staked out, and if possible, even before any court proceeding has been commenced.[23] In some family disputes, the disputes and controversy in the family continue, sometimes requiring further court intervention (after a guardian is appointed) because guardianship deals with continuing inter-personal relationships. The family members may need the opportunity "to vent." Mediation may be the tool to use in attempting to resolve the continuing interpersonal disputes, and in such situations, mediation is usually a better tool for a long-term solution.

Mediation in Michigan Guardianship Proceedings

Pursuant to the applicable Michigan statute, the court appoints a guardian *ad litem*[24] to protect the rights and interests of the disabled ward. The statutory provision imposes a duty upon the guardian *ad litem* to report to the court whether a disagreement or dispute related to the guardianship might be resolved through court-ordered mediation.[25] This sets the immediate groundwork for the court to order the parties to mediation. According to John N. Kirkendall, the probate judge of Washtenaw County (where Ann Arbor is located), guardians *ad litem* receive training by the court about what to look for so they can recommend, at the outset, those proceedings where they believe mediation will be of assistance.[26]

The participation of the proposed ward (respondent), to the full extent possible, is crucial.[27] The mediator should make a decision about the extent of the participation by the proposed ward at the mediation session,[28] depending on the person's capacity. It is also important that the proposed ward has representation[29] (or a support person or a surrogate, such as a guardian *ad litem* or legal counsel appointed) at the mediation session(s).

The mediation session is confidential—that is a basic fundamental of mediation. A conflict may arise regarding the guardian *ad litem*'s role in the mediation since a guardian *ad litem* is required to report to the court. One possible way[30] to resolve this conflict is for the guardian *ad litem* to complete the report before the mediation, then participate in the mediation to protect the rights and interests of the proposed ward, with the hope a mediated agreement will be reached. Thus, it will not be necessary for the guardian *ad litem* to report on any confidential information brought into the open at the mediation session(s). If no mediated agreement is reached, it may be necessary for the court to appoint legal counsel for the proposed ward or a successor guardian *ad litem* for the hearing.

In a videotape describing the program,[31] Judge Kirkendall states that, although judges are trained in resolving legal issues and making legal rulings on standards of proof and evidence, a mediator's training is different. A mediator focuses on the needs of the parties. Thus, the result can be a broader-based settlement that might not be available from a judge in a courtroom setting. The mediated settlement may result in more creative solutions. According to Judge Kirkendall, mediation has

assisted in resolving 85% of the guardianship cases before him.[32]

Should Mediation Be Available Under Article 81?

In the article titled "Court-Annexed ADR on the Rise,"[33] some advantages of mediation are described:

> Mediation . . . provides a more flexible and informal atmosphere than litigation. As a result, the parties can discuss certain confidential information with the mediator that they would not otherwise discuss with the other party or a judge. A skilled mediator can uncover, through this confidential exchange, underlying interests and settlement options that would not have been explored in direct negotiations, litigation or even a typical settlement conference. Mediation, therefore, often results in substantial savings in litigation costs and creative solutions tailored to the specific interests of the parties.

Many of the same issues raised in court cases . . . can be resolved in mediation, and thus possibly leave no need for the appointment of a guardian and the attendant legal finding of incapacity.

Many times guardianship proceedings contain highly litigated issues interrelated with strong heated emotions of who should be the guardian and what powers should be granted. These proceedings can be highly confrontational, particularly those involving dysfunctional families. Each member of the family brings to the table the "baggage" of the sibling rivalry that has been brewing among them during the past 30 years. Family dynamics may be such that old communication patterns block constructive decision making. Many of the same issues raised in court cases—safety and autonomy, living arrangements, financial management, and planning for the future—can be resolved in mediation,[34] and thus possibly leave no need for the appointment of a guardian and the attendant legal finding of incapacity.

In a family situation, even though there may be many disputes between the siblings or other relatives (nieces, nephews, cousins, *etc.*), they may still prefer to keep it "private"—they don't want to air all their family disputes in a courtroom in a litigated court proceeding. Many of these individuals have never been involved in any court proceeding, and this is their first encounter—involving, *e.g.*, guardianship for their mother. In such situations, mediation may provide the necessary tool to address the concerns of all the family members.

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1. This article is written specifically referring to Article 81 of the Mental Hygiene Law under which proceedings are commenced for the appointment of a guardian (for property matters and/or for personal needs) of an incapacitated person. Abbreviated references to the law as simply "Article 81" are common among practitioners in the field.

   Article 81 is used most often to provide for the needs of the elderly, but can be used for persons of all ages in many different types of situations involving many types of disability. It may also be used for young individuals, generally when a substantial sum of money from a source such as a personal injury settlement must be managed or the person meets the definition of incapacity. In other circumstances that require guardians for children, for the mentally retarded and for those with specific developmental disabilities, proceedings for a guardian may be commenced in the surrogate's court under Article 17 and Article 17-A of the Surrogate's Court Procedure Act. They are entirely different types of proceedings.
2. MHL § 81.01 states specifically that the objective was to make available to persons with incapacities "the least restrictive form of intervention which assists them in meeting their needs but, at the same time, permits them to exercise the independence and self-determination of which they are capable."
3. Mediation is defined as an informal "process in which a trained neutral assists disputants in framing issues in dispute, enhances communication between parties, helps parties develop possible solutions, and aids them in reaching mutually acceptable agreements." Erica Wood, *Dispute Resolution and Dementia: Seeking Solutions*, 35 Ga. L. Rev., 785, 800 (2001) ("Wood, *Dispute Resolution and Dementia*").
4. In the facilitative model the mediator encourages the parties to generate their own settlement options, and does *not* suggest the settlement terms. Facilitative mediation is "the intervention into a dispute or negotiation by an acceptable, impartial and neutral third party, who has no authoritative decision-making power, to assist disputing parties in voluntarily reaching their own mutually acceptable settlement of issues in dispute." Susan Hartman, Adult Guardianship Mediation Manual 8, 44 (1996) (definition adapted from Christopher W. Moore, The Mediation Process 14 (1986)) ("Hartman, Adult Guardianship Mediation Manual").
5. Court-ordered mediation is provided through two court rules (both effective August 1, 2000): MCR 2.411 court-ordered mediation in civil cases and MCR 5.143 probate cases are subject to the same process. *See* Mich. Comp. Laws § 700.5305 (eff. June 1, 2001).
6. See Washington statute, Wash. Rev. Code § 11.88.090(2), which provides that the court may order parties in a guardianship case to participate in mediation, establish the terms of the mediation, and allocate the cost of the mediation.
7. *See* Utah Third District Court (Salt Lake City) at <http://www.courtlink.utcourts.gov/mediation/adr_prob.htm>.
8. The first such program (conducted over three years) was in Washtenaw County, MI, originally undertaken in 1991. Thereafter, the four pilot sites were in Chicago, IL; Tampa, FL; Denver, CO; and Albuquerque, NM, all administered with the support of several grants.

9. Hartman, Adult Guardianship Mediation Manual, *supra* note 4, at ii.
10. Ann Pfau & Daniel Weitz, *Court-Annexed ADR on the Rise*, N.Y.L.J., Apr. 12, 1999, p. 1.
11. Susan Gary, *Mediation and the Elderly: Using Mediation to Resolve Probate Disputes over Guardianship and Inheritance*, 32 Wake Forest L. Rev. 397, 413 (1997). *See* Mary Radford, *An Introduction to the Uses of Mediation and Other Forms of Dispute Resolution in Probate, Trust, and Guardianship Matters*, 34 Real Prop. Prob. & Tr. J. 602, 636–42 (Winter 2000).
12. Hartman, Adult Guardianship Mediation Manual, *supra* note 4, at 24.
13. MHL § 81.02(a)(1), (2). There may be some situations where the AIP agrees to the appointment of a guardian with certain specified powers, in which case, the court would *not* have to make a finding of "incapacity." The court should be sure the AIP has the capacity to "agree," and the AIP should be questioned by the court.
14. MHL § 81.02(a)(1), (2).
15. MHL § 81.02(b).
16. Whether this is simple and straightforward is questionable as this author has seen some very unusual interpretations in the attempt to prove incapacity. In this author's opinion, the definition of incapacity as per MHL § 81.02 is *not* clear, and appears to be a convoluted series of phrases. Erica Wood, in *Dispute Resolution and Dementia*, *supra* note 3, at 793, stated that incapacity under guardianship statutes may be vaguely defined, vaguely interpreted, and subject to misuse.
17. Wood, *Dispute Resolution and Dementia*, *supra* note 3, at 807, as reported by Hartman, Adult Guardianship Mediation Manual, *supra* note 4, at 12.
18. MHL § 81.12(a).
19. MHL § 81.15(b), (c).
20. MHL § 81.16(a), (b), (c).
21. Per MHL § 81.16(b), if the AIP is found to be incapacitated, the court may appoint a "special" guardian to assist in completing single transactions and making protective arrangements.
22. Hartman, Adult Guardianship Mediation Manual, *supra* note 4, at 23.
23. *Id*.
24. The Michigan statute calls for the appointment of a "guardian *ad litem*" to protect the rights and interests of the disabled ward and report to the court. The guardian *ad litem* does not have to be an attorney. Mich. Comp. Laws § 700.5305(i)(b), (c), (e). The New York statute, by contrast, appoints a court evaluator, who does not have to be an attorney, to independently investigate and provide a written report for the court. *See* MHL § 81.09.
25. Mich. Comp. Laws § 700.5305(ii).
26. Videotape: Adult Guardianship Mediation: A Judge's Perspective (The Center for Social Gerontology 1997) ("Videotape").
27. Judge John Kirkendall, Videotape, *supra* note 26.
28. *See ADA Mediation Guidelines*, Cardozo Online J. Conflict Resol. (Feb. 16, 2000), available at <http://www.cardozo.yu.edu/cojcr/new_site/index.htm> (last updated Mar. 16, 2001). The mediator should determine a party's capacity to mediate "on a case by case basis, if and when a question arises" and that "[a]n adjudication of legal incapacity is not necessarily determinative of capacity to mediate," as such party may still be able to participate in mediation. *See also* Wood, *Dispute Resolution and Dementia*, *supra* note 3, at 808–809.
29. *See supra* note 28. Even if the proposed ward-respondent is not present, a representative on behalf of the proposed ward (respondent) such as a guardian *ad litem* or legal counsel should be present at each mediation session. *See ADA Mediation Guidelines*, *supra* note 28, at 8. (Note, if mediation is adopted for guardianship proceedings in New York, the court evaluator can provide this role.)
30. As reported by Susan Hartman at the Guardian Mediation Training Program, Center for Social Gerontology, in Ann Arbor, MI, June 3–5, 2001.
31. Videotape, *supra* note 26.
32. *Id*.
33. Pfau & Weitz, *supra* note 10.
34. *See* Hartman, Adult Guardianship Mediation Manual, *supra* note 4, at 25.

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In a Suit Based on Intentional Acts, Defendant May Attempt to Raise Comparative Fault Under CPLR 1411

BY JAMES A. BEHA II

Plaintiff, a male model moonlighting as a bartender, serves the already intoxicated defendant yet again, and then speaks disparagingly about defendant's nearest and dearest. Defendant then beats plaintiff with a chair, scarring him for life and substantially reducing his future earning potential. When plaintiff sues, may defendant reduce the damages he owes, as found by the jury, by reason of plaintiff's own provocative actions?

If a commercial lender fails to supervise adequately the safety of its collateral (say, a shipment of bicycles), may a third party who converts the collateral (and, of course, no longer has possession when sued) reduce what it must pay the lender because the lender's negligence made the conversion possible?

Finally, if a party in a commercial transaction bribes an employee of the other party to extract better financial terms, may the bribe-payer later argue in defending a fraud suit that negligent supervision of the employee by the bilked plaintiff, as well as the failure of the plaintiff to follow industry procedures in reviewing contract terms, contributed to the loss and hence should reduce any damage award?

Every plaintiff naturally contends that the intentional wrongdoer should pay in full for the injuries inflicted. Each defendant pleads that, whatever his wrong, plaintiff should not be excused from the consequences of his own actions. Which party holds the correct view? The answer (such as it is) lies in the courts' interpretation of CPLR 1411, New York's comparative fault statute.

Should Intentional Tortfeasors Benefit?

CPLR 1411, enacted in 1975, seems to say that *every* tort defendant may have the benefit of a "comparative fault" defense in reduction of damages. However, for the better part of two decades the prevailing wisdom has been that a "comparative fault" defense was not available to the intentional tortfeasor, just as an intentional tortfeasor could not, under prior law, plead contributory negligence as a defense to liability. Some recent cases, however, support a more universal application of CPLR 1411, leaving a plaintiff to bear the cost of his own mistakes, whatever the nature of the wrong done to him.

At first glance, the opening section of CPLR Article 14-A appears to resolve the debate, stating that in "any action to recover damages for personal injury, injury to property, or wrongful death, the culpable conduct attributable to the claimant" shall proportionally diminish the damages otherwise recoverable.[1] The "bar" of contributory negligence—which often disabled a recovery premised on negligence—was swept away by this 1975 legislation; one might also conclude that a rule of comparative fault (or comparative causation of fault) now applied to *all* tortious behavior. This view is reinforced by the 1975 Judicial Conference Report: "The defendant's culpable conduct may include, but is not necessarily limited to, negligence, breach of warranty, a violation of a statute giving rise to civil liability, conduct giving rise to liability upon a theory of strict liability and *intentional misconduct*." (emphasis supplied). Because "intentional misconduct" by defendant is expressly mentioned, one might conclude that CPLR 1411 applies in litigation concerning an intentional tort like assault, fraud, breach of fiduciary duty, or conversion.

But woe to those who read statutes without checking the case law annotations! A number of cases applying New York law have determined (or, in some instances, assumed) that CPLR 1411 does *not* apply to intentional tort cases at all, and thus is not available as an aid to an intentional tortfeasor. The leading case for this contrary result is a 1990 decision by the Appellate Division, First Department in *City of New York v. Corwen*.[2]

Before *Corwen* was decided, a series of Fourth Department cases had taken conflicting approaches to the applicability of CPLR 1411 in cases based on intentional

JAMES A. BEHA II is a partner in the New York office of Winston & Strawn. A graduate of Princeton University, he holds a J.D. from Harvard Law School and a Ph.D. from Harvard University. His partner, Steven M. Schwartz, assisted in the evaluation of the cases discussed and in the preparation of this article.

torts, and in each instance there had been little substantive discussion. In *Comeau v. Lucas*,[3] CPLR 1411 was applied in a case that included an assault claim, and in *Jordan v. Britton*,[4] defendant, convicted of manslaughter, was entitled to apportionment of damages for wrongful death where decedent's culpable conduct contributed to his injuries or death. In *Anderson v. WHEC-TV*,[5] however, the court said CPLR 1411 is not available to intentional tortfeasors who could not have asserted contributory negligence. Results elsewhere in New York reflected competing policy considerations and, again, reached conflicting answers.[6]

In *Corwen*, the First Department came down on the side of limiting the application of CPLR 1411: "In the past, contributory negligence clearly has not been regarded as a defense to intentional torts [citation omitted] and that appears to remain the rule with respect to comparative negligence (see, *Anderson v. WHEC-TV*, 92 A.D.2d 747)." Although the "appears to" language sounds equivocal, the result was that a defense of comparative fault was stricken, and *Corwen* has since been repeatedly cited for the proposition that CPLR 1411 is not available to a defendant found to be an intentional tortfeasor. As will be seen, however, the soundness of that proposition is far from clear.

Early Case Law vs. Legislative History

The rationale for excluding intentional tortfeasors from the benefits of CPLR 1411 is said to lie in the impetus for that 1975 legislation: to abrogate the "bar" to recovery in negligence actions posed by contributory negligence of the plaintiff. Some plaintiffs successfully argued that this remedial purpose—to "liberate" a negligent plaintiff—should limit the scope of the statute. Since contributory negligence had never been a bar to recovery in the case of an intentional tort, they reasoned, CPLR 1411 should not be read to reduce the recovery available to the victim of an intentional tort.[7]

This argument—that CPLR 1411 was intended to liberate a negligence plaintiff, not reduce the recovery available to the victim of an intentional tort—has emotional appeal. It also finds some support in the very title of § 1411, which says it applies "where contributory negligence is . . . established"; under prior law, contributory negligence would not be addressed, and thus never "established" in an intentional tort case. This position does not, however, have any express support in the legislative history. That history concluded with the sweeping restructuring of tort damages law begun by *Dole v. Dow Chemical Co.*,[8] the enactment of Article 14, and the amendment of N.Y. General Obligations Law § 15-108.

The only Court of Appeals decision to address the scope of CPLR 1411 as a defense, *Arbegast v. Board of Education of South Berlin Central School District*,[9] did so in a rather different context, that of the doctrine of assumption of risk. *Arbegast* reviewed at some length the history behind the enactment of CPLR 1411, both the prior common law of contributory negligence and assumption of risk, and the legislative history. The Court concluded that legislative history "made clear that 'this article is applicable not only to negligence actions, but to all actions brought to recover damages for personal injury, injury to property or wrongful death whatever the legal theory on which the suit is based.'" It specifically noted that by using the phrase "culpable conduct" rather than negligence, the legislature wanted to ensure that the statute would be broadly applicable to all conduct contributing to a plaintiff's damages, not just "negligent" conduct,[10] concluding as follows: "What the statute requires comparison of is not negligence but conduct which, for whatever reason, the law deems blameworthy, in order to fix the relationship of each party's conduct to the injury sustained."[11]

The reference to *any* action in CPLR 1411 and its legislative history regarding intentional misconduct can also be contrasted to CPLR 1601 and 1602. They too deal with apportionment of damages, although only in personal injury actions. The legislature expressly excluded from *those* apportionment provisions actions requiring proof of intent.[12] It did not do so in CPLR 1411.

Several of the New York lower court decisions addressing the scope of CPLR 1411, including all the Fourth Department opinions mentioned above, had predated *Arbegast*. The 1986 *Haran* decision[13] by Justice Winick in Nassau County, however, recognized the implications of *Arbegast*, concluding that CPLR 1411 did indeed apply to intentional torts. When the First Department addressed this issue in 1990 in *Corwen*, it had *Arbegast* cited to it as precedent. Nevertheless, the panel answered the question in the negative, citing the earlier Fourth Department *Anderson* opinion, and not mentioning *Arbegast* or *Haran*.[14]

Current State of the Law

The failure of the *Corwen* opinion to discuss, let alone distinguish, *Arbegast* leaves the bar somewhat at sea. It should be noted that defendant Corwen was charged with commercial bribery, a felony. The trial court had focused on this aspect of the case, interpreting the Court of Appeals decision in another case, *Barker v. Kallash*,[15] to mean that the defense of comparative fault cannot be raised by those in "serious violation of the law." (While *Barker* actually said nothing about defenses—being a decision about whether a *plaintiff* is barred from bringing suit because of the illegal character of plaintiff's own conduct—it does perhaps suggest that a party whose conduct is a serious crime should not be allowed to use CPLR 1411 to limit its responsibility.) This seemed to imply that a defendant who committed an intentional

act that was somehow not a "serious" violation of the law might be able to raise plaintiff's comparative fault. However, the First Department opinion did not express any such reservation or cite *Barker* as part of the panel's rationale.

After *Corwen*, some courts seem to have taken the exclusion of intentional torts from CPLR 1411 as a given. For example, in *Scott v. Dime Savings Bank of New York*,[16] Judge Chin cited *Corwen* and stated, without discussion, that the jury's finding of comparative fault (which had been applied to a negligence award) would not reduce the damages awarded on plaintiff's breach of fiduciary duty claim.[17] (It should be noted that there is no indication in the opinion that the defendant had even *argued* that CPLR 1411 should apply to the fiduciary duty claim.) Over the years, *Corwen* was also recognized in several other federal decisions as stating New York law.[18] Nevertheless, some recent decisions conclude that CPLR 1411 relief can be available to defendants liable for intentional torts.

Finding a "blameworthy" breach of duty by the plaintiff who has suffered an intentional wrong is not an easy task for a jury.

In *Coty v. Steigerwald*, the Fourth Department touched on this question again after a dozen years of silence.[19] The panel stated that it "agree[d] with defendants that comparative fault principles may be applied to a cause of action for breach of fiduciary duty," but held that the facts did not permit such an application in the case before it. The panel cited *Arbegast* in support of its view, but made no mention of prior Fourth Department precedent—not even a word about the 1983 *Anderson* opinion to the contrary!

Two decisions by Judge McKenna of the Southern District of New York squarely address this topic. In a case dealing with loans to an oil company (AroChem) that subsequently collapsed, two syndicate lenders sued the lead bank (represented by the writer), alleging breach of fiduciary duty, fraudulent inducement and other intentional torts. The lead bank protested its innocence and asserted that plaintiffs' losses were the result of AroChem's criminal fraud and of plaintiffs' own failures of diligence. Plaintiffs moved to dismiss the CPLR 1411 defense, relying on *Corwen* and other cases mentioned above.

Judge McKenna's decision, *Bank Brussels Lambert v. The Chase Manhattan Bank, N.A.*,[20] is the only opinion to discuss the application of CPLR 1411 to intentional torts in more than cursory fashion since the *Haran* decision in 1986. While recognizing "the lack of firm and unequivocal guidance in the New York case law construing CPLR 1411," Judge McKenna concluded, "albeit *dubitante*, that the New York Court of Appeals would find that CPLR 1411 is available to defendant in the present case as to plaintiffs' claims of intentional tort, *i.e.*, fraud, gross negligence and breach of fiduciary duty."

Judge McKenna found that the New York Court of Appeals' thorough analysis of the legislative history of Article 14-A in *Arbegast* made it clear that the Court endorsed an expansive view of the statute's scope; further, the Court's construction of CPLR 1411 in that case, which was focused on causation, suggested no reason to automatically exclude the statute's availability to a defendant who might be an intentional tortfeasor. Judge McKenna also stated that there was no logical reason why, where an intentional tort was only a partial cause of a plaintiff's loss, that the plaintiff should nevertheless recover fully for a loss caused in part by its own negligence.

Judge McKenna did not feel bound by *Corwen*, as it was a decision of an intermediate appellate court, but he did distinguish it:

> Public policy considerations arising out of the fact that the defendants in *Corwen* had engaged in bribery, relied on by the court below, may also be considered to have been a part of the ground for the affirmance. Such a factor is not present here where plaintiffs' claims, including those sounding in fraud, are asserted under the common law of New York.[21]

The same issue later arose before Judge McKenna in a related AroChem case, resulting in another opinion on the subject, *Bank Brussels Lambert v. Credit Lyonnais (Suisse) S.A.*[22] Here, the same plaintiffs had sued a bank outside the syndicate for fraudulent interference with their AroChem loan and for conversion of collateral securing the lender group. Defendant responded that plaintiffs were themselves responsible for their injuries, alleging, among other things, that plaintiffs had failed to monitor their collateral properly.

Plaintiffs contended that even if CPLR 1411 applied to intentional torts in general (as Judge McKenna had already ruled), it should not apply to the tort of conversion, as to which the owner's negligence had never been permitted as a defense. Their argument ran as follows: If I leave my watch on the table and walk away, my negligence should not reduce your obligation to return the watch (or pay me the fair value of the watch) after you have taken it.[23] Judge McKenna did not tie his answer to the specifics of the AroChem fact pattern, but simply stuck to his reading of *Arbegast* and indicated that CPLR Article 14-A modified any rule that negligence is not a defense to conversion.[24]

Other Considerations

Can this really mean that the wrongdoer does not have to pay in full for the watch (or bicycle) he took? Can the bribe-maker keep some of the benefit of his wrongly obtained contract because the victim was not vigilant? Although such questions were not reached in either of the decisions by Judge McKenna, the writer would suggest that the answer might well come in two parts.

First, CPLR 1411 refers to the "*culpable* conduct of the claimant." (emphasis supplied). Nothing in the legislative history tells us if "*culpable*" was intended to mean more than that the conduct also "caused the damages," but in *Arbegast* the Court of Appeals focused the analysis on "conduct which, for whatever reason, the law deems blameworthy."[25] Case law makes clear that in assessing the extent to which conduct is "culpable," the jury properly considers not only the strength of the causal link but also the magnitude of each party's fault.[26] As the New Jersey Supreme Court commented in deciding that its state's comparative fault statute also applied where defendant's conduct constituted an intentional tort:

> The different levels of culpability inherent in each type of conduct will merely be reflected in the jury's apportionment of fault. By viewing the various types of tortious conduct in that way, we adhere most closely to the guiding principle of comparative *fault*—to distribute the loss in proportion to the respective *faults* of the parties causing that loss.[27] (emphasis supplied).

Finding a "blameworthy" breach of duty by the plaintiff who has suffered an intentional wrong is not an easy task for a jury, even though society (and shareholders) expect certain levels of diligence and vigilance in the conduct of business and personal affairs. Nonetheless, "blame" is precisely what the jury is weighing when it weighs the "culpable" nature of plaintiff's own conduct.

How does this question of blame relate to the question at hand? In the law of torts, "fault" and "blame" have been flexible, evolving concepts, ones usually linked to the concept of duty, particularly the duty of care. In the bicycle conversion hypothetical at the beginning of this article, one might argue that, as to the loss of the goods taken, the owner's negligent conduct should not be deemed "blameworthy," whatever its causal relevance. Put somewhat differently, and with a nod to *Hartford Accident* and its watch analogy, the law does not impose on plaintiff any offsetting "duty" of care in the context of a remedy for theft. And in the commercial bribery hypothetical (reminiscent of *Corwen*), might not one argue that, in the context of righting the wrong, the law simply should not impose a "duty" on the victim to have foreseen the crime? These are essentially public policy considerations; they resonate in a case such as *Coty,* with its ambiguous holding that CPLR 1411 did not apply because "plaintiff had no duty" which was breached.

A second route to an answer in a given case emerges from considering the remedies sought for a particular wrong. New York law distinguishes between *direct* and *consequential* compensatory damages; New York also distinguishes between the award of compensatory damages and the remedy of recoupment. One who took property of another should neither be excused from giving the property (or its full value) back, nor allowed to profit from his wrong. CPLR 1411 should not be read or applied to impair this particular form of recovery. Outright theft of property does not neatly fall within "*injury* to property" at all (the property may not have been "injured"—it is *possession* that has been affected), and the standard remedy for conversion is really a variety of recoupment.

Much of damages analysis (and particularly damage analysis in commercial cases) is not about the immediate, direct impact of tortious conduct, but about its *consequences*—the loss of future revenues, the kingdom lost because of a shoe (or a bicycle), the overpriced investment that turned far worse. As to foreseeable *consequences* of the tort (beyond the direct loss) it is a fair question whether a plaintiff is to be immunized from his own errors because the others who harmed him did so intentionally rather than negligently. Applying CPLR 1411 to consequential damages of an intentional tort like conversion does not "enrich" the defendant but rather limits its liability for additional consequences for which the plaintiff shares some blame.

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1. CPLR 1411 states:

   > § 1411: Damages recoverable when contributory negligence or assumption of risk is established:
   >
   > In any action to recover damages for personal injury, injury to property, or wrongful death, the culpable conduct attributable to the claimant or to the decedent, including contributory negligence or assumption of risk, shall not bar recovery, but the amount of damages otherwise recoverable shall be diminished in the proportion which the culpable conduct attributable to the claimant or decedent bears to the culpable conduct which caused the damages.

2. 164 A.D.2d 212, 565 N.Y.S.2d 457 (1st Dep't 1990).
3. 90 A.D.2d 674, 455 N.Y.S.2d 871 (4th Dep't 1982).
4. 128 A.D.2d 315, 515 N.Y.S.2d 678 (4th Dep't 1987).
5. 92 A.D.2d 747, 461 N.Y.S.2d 607 (4th Dep't 1983). Taken aback by discovery of this line of cases, our plaintiff might now check the McKinney's commentary, the venerated Siegel treatise, and the exhaustive reaches of Weinstein-Korn-Miller. Not only do none of these say that CPLR 1411 does not apply to intentional torts, but the Weinstein treatise echoes the Judicial Conference Report: "When determining the total culpable conduct that caused the damages, the trier of fact must consider the conduct of both defendant and the claimant. . . . *The de-*

fendant's conduct may include, but is not limited to, negligence . . . and intentional misconduct." 2A Weinstein-Korn-Miller, *New York Civil Practice* § 1411.05 at 14A-19 (emphasis supplied). Notwithstanding the treatise language, in *Blue Cross and Blue Shield of New Jersey, Inc. v. Phillip Morris, Inc.*, 36 F. Supp. 2d 560, 575 (E.D.N.Y. 1999), Judge Weinstein commented that "contributory or comparative negligence is not a defense to fraud." While plaintiff's fault was never a *bar* to a claim for fraud, as an intentional tort, if CPLR 1411 is to be given effect in reduction of damages, New York law requires that it be pleaded as a *defense*. Thus, if the treatise view is correct then CPLR 1411 would be a "defense" in a fraud case.

6. *See Haran v. New York Metropolitan Baseball Club, Inc.*, 131 Misc. 2d 392, 393–94, 500 N.Y.S.2d 485 (Sup. Ct., Nassau Co. 1986) (earlier cases discussed statute applied to intentional torts).
7. *See, e.g.*, *Leiner v. First Wythe Ave. Serv. Station, Inc.*, 121 Misc. 2d 559, 468 N.Y.S.2d 302 (Civ. Ct., Kings Co. 1983), *aff'd*, 127 Misc. 2d 794, 492 N.Y.S.2d 708 (App. Term, 2d Dist. 1985) ("[w]here the tort complained of does not allow for a defense of contributory negligence, the adoption of CPLR 1411 will not be the instrument of its creation").
8. 30 N.Y.2d 143 (1972).
9. 65 N.Y.2d 161, 166–67, 490 N.Y.S.2d 751 (1985). One earlier Court of Appeals decision had dealt with the availability of CPLR 1411 to certain categories of *plaintiffs*. In *Barker v. Kallash*, 63 N.Y.2d 19, 479 N.Y.S.2d 201 (1984), the Court of Appeals held that CPLR 1411 did not overturn the common law doctrine that a plaintiff injured while involved in "substantial violation of the law" could not sue others for his injury (*Barker* involved the construction of a bomb).
10. *Arbegast*, 65 N.Y.2d at 166–67. *Cf. Lippes v. Atlantic Bank of New York*, 69 A.D.2d 127, 137-38, 419 N.Y.S.2d 505 (1st Dep't 1979) ("Use of the term culpable conduct in CPLR 1411, rather than 'negligent conduct'" suggests legislative intent to reach "any breach of legal duty or fault by the defendant").
11. *Arbegast*, 65 N.Y.2d at 168. The Court of Appeals' sense of the breadth of CPLR 1411's reach has had its limits. In *Mullen v. Zoebe, Inc.*, 86 N.Y.2d 135, 630 N.Y.S.2d 269 (1995), the Court held that notwithstanding CPLR 1411 "the culpability of an injured or deceased firefighter in contributing to the happening of the injury-producing accident" could not be invoked by defendant property owner in a statutory suit brought by a firefighter brought against the owner for creating hazardous conditions that violated fire safety laws (General Municipal Law § 205-a). The Court explained that § 205-a presents an express legislative allocation of fault-based recoveries: the statute prohibits a remedy for firefighters where the owner is merely negligent and allows firefighters a recovery only in circumstances of illegality (*e.g.*, code violations). The Court concluded that allowing comparison of fault in the instances where the firefighter is permitted a remedy would be inconsistent with the statutory purpose of placing "full responsibility" on the defendant in the case of a code violation. *Mullen*, 86 N.Y.2d at 140. *See also Bland v. Manocherean*, 66 N.Y.2d 452, 497 N.Y.S.2d 880 (1985), holding that CPLR 1411 is not available as a defense in actions brought under Labor Law § 240(1).
12. *See Siler v. 146 Montague Assocs.*, 228 A.D.2d 33, 652 N.Y.S.2d 315 (2d Dep't 1997).
13. *See supra*, note 6.
14. The appellate record shows that the passages of *Arbegast* dealing with the scope of CPLR 1411 were brought to the *Corwen* panel's attention. The *Haran* opinion apparently was not cited in the *Corwen* appellate briefs. Lance Gotthoffer of Oppenheimer, Wolff and Donnelly LLP brought this portion of the *Corwen* record to my attention when he and the author briefed opposing sides of this issue as collegial adversaries in a litigation mentioned later in this article.
15. 63 N.Y.2d 19, 479 N.Y.S.2d 201 (1984).
16. 886 F. Supp. 1073 (S.D.N.Y. 1995), *aff'd*, 101 F.3d 107 (2d Cir. 1996) (table).
17. *Scott*, 886 F. Supp. at 1081. If the point had been argued, a Second Department opinion subsequent to *Corwen* might have raised additional questions about this result. *See Mafoud v. City of New York*, 200 A.D.2d 561, 562, 606 N.Y.S.2d 309 (2d Dep't 1994) (action for personal injuries; theory not stated; opinion includes statement that CPLR 1411 applies to all tort actions, whatever their theory; hence "the statute does not merely require a calculation of the comparative degrees of negligence of the parties but rather requires a calculation of the comparative degrees of all types of culpable conduct giving rise to damages").
18. Judge Weinstein's *Blue Cross* opinion, *supra* note 5, also relies on *Corwen* in this regard, as does *Long Island Savings Bank v. Bigman*, 89 Civ. 0927, 1991 WL 144224 (E.D.N.Y. June 25, 1991) (if plaintiff had been negligent in not inspecting property [which the Court held plaintiff was not], that finding "would not be a defense to a charge of fraud"). *See Brockton Sav. Bank v. Peat, Marwick, Mitchell & Co.*, 771 F.2d 5, 13 (n. 10) (1st Cir. 1985) (an earlier case construing CPLR 1411 as not applicable where defendant found liable for intentional tort).
19. 262 A.D.2d 946, 692 N.Y.S.2d 556 (4th Dep't 1999).
20. 93 Civ. 6876, 1999 WL 710778 (S.D.N.Y., Sept. 10, 1999).
21. *Id.* at *2.
22. 94 Civ. 2713, 2000 WL 1364272 (S.D.N.Y. Sept. 20, 2000), reconsideration granted and original determination adhered to, 2000 WL 1694308 (S.D.N.Y. Nov. 13, 2000).
23. *See Hartford Accident & Indem. Co. v. Walston & Co.*, 21 N.Y.2d 219, 287 N.Y.S.2d 58 (1967) (presenting the watch analogy) (citing earlier cases). The defendant argued that this analogy did not match the alleged conversion, or conversion damages, actually at issue in the case, and that CPLR 1411 applied to *any* action for injury to property.
24. 2000 WL 136472 at *2. Perhaps Judge McKenna, by omission, did take account of the fact pattern: plaintiffs had argued that the conversions at issue should be considered as felonies and be subject to the "policy considerations" about criminal conduct discussed by the Court of Appeals in *Barker*. Judge McKenna found *Barker* inapplicable because *Barker* dealt with criminal conduct of the *plaintiff* (barring compensation to plaintiff) whereas this defendant was not seeking compensation but merely reduction in damages. Judge McKenna passed over in silence his own prior grounds for distinguishing *Corwen*, *i.e.*, that Corwen was alleged to have committed criminal bribery, a rationale that the *Corwen* lower court had premised on *Barker*.
25. *See supra* note 10.
26. *See Kreppain v. Celolex Corp.*, 969 F.2d 1424, 1426–27 (2d Cir. 1992).
27. *Blazavic v. Andrich*, 124 N.J. 90, 107, 590 A.2d 222 (1991).

New Federal Regulations Expand Protections For Privacy of Health Records

BY JANE F. CLEMENS

For the first time ever, New Yorkers have a comprehensive set of rules that govern the privacy of health records.[1] Regulations issued by the federal Office of Civil Rights of the Department of Health and Human Services (DHHS) under the Health Insurance Portability and Accountability Act of 1996 (HIPAA)[2] exceed any existing requirements of New York law by:

- Expanding the categories of people and entities required to maintain confidentiality of health information.
- Specifying in detail the steps an entity subject to the regulations must take to insure that confidentiality of an individual's health history is preserved.
- Limiting the release of health information to the minimum reasonably needed for the purpose of the disclosure.
- Detailing the rights individuals have to gain access to their own records and have their records corrected.
- Providing for civil and criminal penalties that exceed any remedy provided by current New York law.

The regulations issued by DHHS preempt state law only if state law is less protective of an individual's right to require that his or her own health records be kept in strict confidence.[3] To the extent that current New York rules provide greater privacy protections to an individual, those rules continue to apply.[4] Therefore, in any situation, whether a request for disclosure by an individual for a copy of his or her own health record, a request by an individual to correct a health record or a request by a third party for an individual's health record, both the federal and state law must be analyzed.

The New York Public Health Law and the New York Mental Hygiene Law are the principal statutory sources of New York law that require health information to be held in confidence. Special additional statutes are in effect covering specific situations, *e.g.*, HIV and AIDS patients,[5] disclosure of records in litigation,[6] and the collection of statistical information by various governmental agencies.[7] This article is limited to examining the impact the new federal regulations have on records subject only to the Public Health Law or the Mental Hygiene Law.

Expansion of Entities Covered

HIPAA expands the kinds of entities that must keep health records confidential.

Both the state Public Health Law and the state Mental Hygiene Law generally apply only to facilities licensed by the Department of Health, the Office of Mental Health, or the Office of Mental Retardation and Developmental Disabilities.[8]

A new term of art, "covered entity," is included in the HIPAA regulations. Covered entities are health care providers,[9] health plans,[10] and health care clearinghouses[11] that transmit or maintain any health information[12] via electronic media[13] in connection with a transaction covered by the regulations. The definition of health plan includes: group health plans (except certain employee-sponsored plans) as defined in ERISA (with either 50 or more participants or ones that are administered other than by the employer who maintains the plan and employee welfare benefit plans established for two or more employers), health insurance issuers, HMOs, Medicaid programs, Medicare programs, and long-term care policies. Included among covered health plans are limited-scope dental and vision health plans, and excluded from the applicability of the statute are worker compensation programs, property and casualty insurance programs, and disability insurance programs. In addition, nursing home fixed indemnity policies are excluded, although issuers of all other long-term plans are included.

JANE F. CLEMENS is a partner in the corporate department of Underberg & Kessler LLP in its Buffalo office. A graduate of Oberlin College, she received her J.D. from the law school at the State University at Buffalo. Ms. Clemens acknowledges the assistance of Amber Barney, an associate in the corporate department of Underberg & Kessler LLP.

The term "health care provider" incorporates the Medicare definitions of provider but is broader than that set forth in the New York Public Health Law because in addition to the practitioners and institutions identified in the New York statute, a variety of technicians, aides and suppliers of durable medical equipment are also covered.

Kinds of Information Protected

HIPAA expands the kind of information protected.

The Public Health Law applies to patient information except for mental health information and information received from certain sources or under certain conditions.[14] It protects "any information concerning or relating to the examination, health assessment for insurance and employment purposes" as well as information concerning the "treatment of an identifiable subject maintained or possessed by a health care facility or health care practitioner who has provided or is providing services for assessment of a health condition," except: (1) Clinical records subject to the provisions of § 23.05 or § 33.13 of the Mental Hygiene Law. (2) Personal notes of the health care practitioner if those notes were not disclosed by the practitioner to any person after January 1, 1987. (3) Information maintained by the practitioner and received from another practitioner. (4) Information disclosed to the practitioner by a third party on condition that it would not be disclosed to the patient.[15]

The Mental Hygiene Law protects only what is in the record, which the regulations prescribe as "including data pertaining to admission, legal matters affecting the patient or client, records and notation of course of care and treatment, therapies, restrictions on patient's or client's rights, periodic examinations, and such other information as he or she may require."[16] Clinical record means "information concerning or relating to the examination or treatment of an identifiable patient or client maintained or possessed by a facility which has treated or is treating such patient or client."[17]

HIPAA protects:

All Information Regardless of Source With limited exceptions, the new regulations apply to all individually identifiable health information in any form held or transmitted by a covered entity.[18]

All Information Regardless Who Created It The information protected is information whether oral or recorded and whether received or created by a "health care provider, health plan, public health authority, employer, life insurer, school or university, or health care clearinghouse."[19]

Physical and Mental Health Information Protection extends to information about the physical as well as mental health conditions of an individual.[20] The information may relate "to past, present, or future physical or mental health or condition of an individual; the provision of health care to an individual; or the past, present, or future payment for the provision of health care to an individual."[21] Psychotherapy notes are treated specially and subject to a higher standard of confidentiality.

Individually Identifiable Information The information protected must be identifiable—that is, information from which a person can identify the person to whom it relates, whether or not the person's name is included.[22] The regulations provide that if certain specified information is removed, information is presumed non-identifiable if the entity has no reason to believe that the anticipated recipient of the information could use the information either alone or in conjunction with other information to ascertain the identity of the individual involved.[23]

Information that can be removed to satisfy the non-identifiable part of the test includes name, address, birth date, telephone and fax numbers, e-mail addresses, medical record number, health plan beneficiary number, account number, photographs, fingerprints, Web URL, *etc*. Although the regulations provide an objective test of information that can be removed to make information presumed to be non-identifiable, determining in hindsight whether an organization had a reason to believe the recipient could use the information to ascertain the identity of the individual involved is very subjective and will depend upon an analysis of the circumstances surrounding the disclosure.

Access to Patient Information

HIPAA clarifies who has access to patient information.

The Public Health Law mandates disclosure to "qualified persons" who are: (1) The patient upon the patient's written request. (2) The committee for an incompetent person appointed under Article 78 of the Mental Hygiene Law or a guardian appointed under Article 81. (3) A parent or guardian of a minor with special restrictions.[24]

The Public Health Law then provides that disclosure to certain types of entities or in certain circumstances does not constitute disclosure. For example, a disclosure to another practitioner as part of the consultation or referral of the patient does not constitute a disclosure. Likewise, the term "treatment" excludes certain exceptions.[25]

The Public Health Law does not require an individual to be notified if his or her health record is disclosed, but rather, if the disclosure is authorized by law, simply a notation in the patient's record of the name and address of the third party and the purpose for disclosure is necessary.[26] If a disclosure is made to a governmental agency or insurance company, the note needs to be made only upon the first disclosure.[27] The statute re-

Summary of Privacy Regulations

The federal privacy standards established under the Health Insurance Portability and Accountability Act differ from the New York law in several important respects. The most significant differences are:

Individually Identifiable Information HIPAA and the Public Health Law both protect individually identifiable health information whereas the Mental Hygiene Law protects clinical records. The Public Health Law requires the information to be identifiable to a particular person without detailing what is to be considered in determining identifiable. The HIPAA regulations enumerate factors that will be considered in deciding whether information is identifiable.

Scope of Information The Public Health Law protects any information about examination, assessment or treatment. HIPAA adds protections for information relating to payment for health care. The state statute excludes information received from another practitioner or information disclosed by a third party on condition that it will not be disclosed. HIPAA protects information regardless of the source. The Public Health Law also excludes notes of the health care practitioner if those notes were not disclosed by the practitioner to any person after January 1, 1987; HIPAA makes no similar exclusion. New York has differing standards for physical and mental health records but HIPAA does not.

Use and Disclosure of Information HIPAA requires an individual's consent for use during treatment; neither the Public Health Law nor Mental Hygiene Law do. All three of the statutes permit disclosure without an individual's authorization to some third parties in some circumstances.

Administrative Requirements HIPAA specifies exactly how a covered entity must safeguard confidentiality and includes requirements for employee training and contractual safeguards; similar provisions do not exist under New York law.

Scope of Disclosure HIPAA restricts the disclosure to that which is necessary under the circumstances. The Mental Hygiene Law has a similar provision, but the Public Health Law does not.

Procedure for Correcting Records Neither the Public Health Law nor the Mental Hygiene Law includes a procedure by which an individual may correct what he or she believes to be mistakes in the health or mental health records although they both include a limited remedy by requiring an individual's request for correction to be attached to his or her records. HIPAA, on the other hand, includes a procedure by which the individual's record may be corrected.

Accounting for Disclosures Under the Mental Hygiene Law and the Public Health Law, a notation of all disclosures must be kept in the record, except for disclosures made to some recipients. HIPAA requires an accounting of all disclosures.

Penalties Penalties for failure to comply with the confidentiality provisions range from civil penalties not exceeding $1,000 for every violation under the Public Health Law, to civil and criminal penalties of up to $250,000 and jail up to 10 years under HIPAA.

Privacy of health information is now federally regulated with supplemental state regulation. Health care providers or others having health information must increase their vigilance to prevent disclosure to others. Although New York has historically protected health information, individuals will now have greater control over the content and use of their health information.

quires that the disclosure made to the insurance company or governmental agency be "limited to that information necessary in light of the reason for disclosure" and further, that the information be kept confidential by the person receiving the information.[28]

The Mental Hygiene Law follows a pattern similar to the Public Health Law and prohibits release of clinical records of an individual, with enumerated exceptions.[29]

Disclosures allowed must be restricted to the information necessary for the purpose for which disclosure is sought. Thus a licensed mental health care provider is required to exercise judgment in redacting some of the applicable patient or client files.[30] Any other disclosures to a third person require a court order.[31]

Excepted from disclosure is data disclosed to the treating practitioner in confidence by another person on the express condition that such data would never be disclosed to the patient or client and provided that the data has never been so disclosed.[32] The term disclosure does not include disclosures identified under MHL § 33.13 above. Requests for access to the record can be made by the individual client or patient, a committee appointed under Article 78 or guardian under Article 81 of the Mental Hygiene Law, a guardian or parent of a minor, or the parent, spouse or adult child of an adult patient.[33]

HIPAA does not draw fine distinctions about what constitutes a disclosure. Rather, it sets out clear guidelines for the circumstances under which disclosure is or is not permitted.

Consent Generally, an individual has the right to restrict use or disclosure of identifiable health information.[34] The regulations require covered entities to obtain an individual's written consent for the use of his or her health information for treatment, payment, and health care operations.[35]

A limited emergency exception exists where the provider is required by law to provide treatment or where there are substantial communication barriers, such as language differences, and the health care professional believes treatment should be given.[36] In addition, providers who have an indirect relationship with the individual (*i.e.*, do not see the patient) and providers providing services to inmates need not obtain the patient's consent to treatment.[37] In a press release, the Secretary of Health and Human Services said guidelines to be issued will clarify how patient care will not be "unduly hampered by the confusing requirements surrounding consent forms."[38]

Authorization If an individual initiates a request for disclosure of health information to a third party, he or she must sign a written authorization, in plain English, that identifies the items to be disclosed.[39] The individual may restrict which health care provider discloses the information and may also restrict the permitted recipient of the disclosure.[40]

The form of authorization is prescribed by the regulations and must include an expiration date, a manual signature and date of signature,[41] as well as statements about the individual's right to revoke the authorization, and a notice that the individual understands that if disclosure is made to an entity that is not a covered entity, the information will no longer be protected by HIPAA.[42] All health care providers need to examine the form of authorization for release of medical records in light of these requirements.

If a covered entity initiates the disclosure, it must have the individual sign a written authorization including all of the above plus statements about the purpose for the requested disclosure and identification of the intended recipient.[43] The request must limit the information to be disclosed to the minimum necessary for the particular question presented.[44] In an effort to address the growing use of direct mail and the selling of mailing lists, if the covered entity will receive a financial benefit from the disclosure, it also must disclose this fact to the individual on the authorization form.[45]

Disclosures Permitted Without Authorization The regulations detail permitted uses and disclosures of protected health information, without individual authorization, which are similar to permitted disclosures on items that are not considered disclosures under the state's Mental Hygiene Law and Public Health Law. These include disclosures in connection with public health activities, health oversight activities, judicial and administrative proceedings, investigations by coroners or medical examiners, law enforcement purposes (including health care fraud), governmental health data systems, directory information systems, banking and payment processing, research, certain emergency situations, to next of kin (who has apparent authority to make health care decisions with respect to the individual) and for certain specialized uses, in connection with military, veteran affairs, the intelligence community and the department of state.[46] All of these permitted disclosures are accompanied by special conditions and restrictions.

Procedures for Denial of Access

Under the Public Health Law, a provider may refuse access if the provider determines that the requested review "can reasonably be expected to cause substantial and identifiable harm to the subject or others which would outweigh the qualified person's right to access to the information"[47] or the information requested is personal notes and observations.[48] The statute gives a nonexclusive list of factors that may be taken into account in reaching that determination: (1) The need for continuing care. (2) The extent to which the knowledge of the information may be harmful to the health or safety of the patient or others. (3) Whether the information contains sensitive material furnished by third parties. (4) Whether the information contains sensitive materials disclosed by the patient, except when the patient is requesting the information. (5) In the case of a minor, as previously noted.[49]

The person denying access to the records must inform the person making the request and must state the basis upon which such denial is made only if based upon the reasons set forth in (1), (2) and (5) above.[50] In addition, the person making the request must be notified of the right to a review of the denial by a medical records access review committee.[51] The statute goes on to provide time periods within which the provider must notify the medical record access review committee of a request for review and the procedure for that review.[52] The statute does not include a time frame within which the requestor must submit the request.[53]

The committee must make a written determination of the basis for which access should be granted or denied.[54] If denial is made only upon the basis that disclosure would cause substantial and identifiable harm to the patient or others, or have a detrimental effect upon the minor's relationship with the provider, the requesting person has the right to seek judicial review.[55] The person has 30 days within which to start a special proceeding seeking disclosure and the court is instructed only to determine "whether there exists a reasonable basis for the denial of access."[56]

Under the Mental Hygiene Law, upon receipt of notice of a request for inspection the facility is to notify the treating practitioner.[57] If the treating practitioner determines that the "requested review of the clinical record can reasonably be expected to cause substantial and identifiable harm to the patient or client or others which would outweigh the qualified person's right of access," access may be denied.[58]

The Mental Hygiene Law and the Public Health Law use the same factors to determine whether the requested access would have a "substantial and identifiable harm to the patient or client." In the case of a minor, the age of the patient also is to be considered.

The statute goes on to provide a process by which the person requesting access to the information may have the clinical record access review committee review the request; the chairman of the committee is to perform an *in camera* review of the materials and make a determination.[59] If the request continues to be denied either in whole or in part, the person requesting the review may request judicial review within 30 days of receiving the written notice of the decision by commencing a special proceeding in the supreme court.[60] The court is required to perform its own *in camera* review of the materials provided, provide an opportunity for all to be heard and determine whether a reasonable basis exists for the denial of access.[61] The only relief is a judgment requiring access if the court determines there is not a reasonable basis to deny access.[62]

The clinical record access review committees are government-appointed committees, appointed by the commissioner of mental health, the commissioner of mental retardation and the commissioner of alcoholism and substance abuse services.[63] Annual reports are required regarding the number of requests for committee review and determinations thereon.[64]

Process Under HIPAA The regulations detail the process for denial, which includes providing the individual with written reasons for the denial.[65] In all cases, access must be denied for psychotherapy notes or information prepared for a trial or proceeding.[66] In addition, there are certain other unreviewed grounds for denial and reviewable grounds for denial if the licensed health care professional determines access is "reasonably likely to endanger the life or physical safety" of a person, or "cause substantial harm" to the patient or other person.[67] If access is denied, the regulations also spell out the procedure by which an individual can contest the decision.

Corrections

Under the HIPAA requirements, all individuals are entitled to amend the contents of their health information by means of a process detailed in the regulations.[68] The process includes a provision to deny the individual's application to amend the record.[69]

On the other hand, under the Public Health Law, a qualified person may challenge the accuracy of the information and may require a written statement prepared by the qualified person to be included in the record.[70] A health care facility may reasonably restrict the time and frequency of challenges to the accuracy of the information included in the record.[71]

Under the HIPAA requirements, all individuals are entitled to amend the contents of their health information by means of a process detailed in the regulations.

Likewise, under the Mental Hygiene Law, challenges to accuracy of materials contained in a clinical record may be made by a patient or client providing a brief written statement, which is then included in the record.[72] As with public health records, the required statement must address "factual statements and shall not include a provider's observation, inferences or conclusions."[73] The provider is not under an obligation to actually correct the record.[74]

Confidentiality Requirements

HIPAA imposes new requirements to safeguard confidentiality.

Regulations issued under the Public Health Law applicable only to hospitals prescribe the manner of assuring safeguards to ensure security and confidentiality by requiring each hospital to: (1) Assign, as appropriate, a unique identifier that is assigned in a confidential manner. (2) Certify in writing by the hospital's designee and the user that each identifier assigned is confidential and is available and accessible only to the person authorized to use the electronic or computer authentication system. (3) Develop policies and procedures to ensure the security of electronic or computer equipment from unwarranted access. (4) Develop policies and procedures that restrict access to information and data to those individuals who have need, reason and permission for such access. (5) Develop the implementation of an audit capability to track access by users.[75]

Regulations applicable to nursing homes, however, simply provide: (1) The facility shall safeguard clinical record information against loss, destruction, or unauthorized use. (2) The facility shall keep confidential all information contained in the resident's record, regardless of the form or storage method of the records, except when release is required by (a) transfer to another health

care institution; (b) law; or (c) the resident. (3) The facility shall permit each resident to inspect his or her records and obtain copies of such records.[76]

The operator of a residential health care facility for adult health care is to maintain a health record for each resident, which also includes non-medical information consisting of: (a) all details of the referral and registration; (b) identification of next of kin, family and sponsor; (c) the person or persons to be contacted in the event of an emergency; (d) accident and incident reports; (e) non-medical correspondence and papers pertinent to the resident's participation in the program; and (f) a fiscal record including copies of all agreements or contacts.[77]

The regulations also require the operator to keep "confidential and make available only to authorized persons all medical, social, personal and financial information relating to each registrant," but otherwise does not specify in detail what must be done.[78] Thus, depending upon the type of facility involved, New York provides differing standards on what must be included in a medical record and the specific steps necessary to be taken to protect confidentiality.

Facilities licensed by the Department of Mental Health are given no specific mandate about the mechanics of prescribing confidentiality.

The HIPAA regulations mandate that a covered entity implement specific practices to safeguard information.[79]

Privacy Official The covered entity must designate a privacy official and a contact person responsible for receiving complaints.[80]

Information Practices The entity must adopt information practices.[81]

Training The entity must provide training to all members of its work force who may have access to health information and must establish appropriate "administrative, technical and physical safeguards to protect the privacy of protected health information."[82]

Safeguards include verification procedures pursuant to which the entity must verify the identity of the person requesting health information, the person's authority for requesting and the basis upon which the request was made, the procedure pursuant to which an individual may complain that information was used or disclosed improperly, that an employee had improperly handled information, that the person had been wrongfully denied access to his or her information or that the notice described in this article and required by HIPAA did not adequately describe the actual practices of the entity.[83] The two specific requirements are the identification of a contact person to whom a complaint should be submitted and the maintenance of a record of complaints that are filed and the resolution of the complaints.[84]

Notice The entity must notify the individuals of the information policies and procedures of the entity.[85]

The regulations specify that the notice must be in plain English and also mandate the contents of the notice: the notice must describe the use and disclosure of information that will be made without individual authorization and distinguish between uses and disclosures the entity makes that are required by law and those that are permitted but not required by law.[86] The notice must include the name and telephone number of a contact person.[87]

Policies and Procedures The entity must adopt written policies and procedures to respond to an individual's request for access to his or her own health information.[88] The individual is only able to access information included in a "designated record set," which is the only record from which information is retrieved by individually identifying information.[89]

Sanctions A covered entity is required to implement sanctions if any of its employees violates the employer's policies and procedures.[90]

Additional Protections

The federal privacy regulations require additional protections to individuals.

All Disclosures Must Be Accounted For With exceptions including disclosures made for treatment, payment and health care operations, all individuals are entitled to an accounting of all disclosures of their health information for the previous six years.[91]

Obligations Imposed on Attorneys, Auditors and Consultants The regulations prohibit disclosures of protected health information to "business associates" of a covered entity except for disclosures when the covered entity has achieved "satisfactory assurance from the business associate that it will appropriately safeguard the information."[92] A business associate of a covered entity is any person doing business with the covered entity except for another health care provider providing treatment to the individual; the regulations specifically give as examples not only billing firms, data processing firms, and the like, but also attorneys, auditors, and consultants.[93]

The regulations envision that except for certain governmental agencies and health plans, the way to achieve safeguard assurance is to have a written contract with the business associate that includes the following provisions:[94]

• The business associate will not use or disclose the information other than as permitted or required by law.

• The business associate will use safeguards to prevent the use or disclosure of the information.

• The business associate will report to the covered entity any use or disclosure of the information not provided for by contract.

• The business associate will ensure that it has contracts with any of its subcontractors or agents that include similar provisions.

• The business associate will make available the protected health information to individuals in accordance with the regulation.

• The business associate will make available to the Department of Health and Human Services its internal practices and records "relating to the use and disclosure of protected health information."

• The business associate will return to the covered entity or destroy all the protected health information and retain no copies of such information at termination of the contract.

• The business associate will amend or correct the protected health information when notified pursuant to the regulations.

• A provision permitting the covered entity to terminate the contract if the covered entity determines that the business associate has violated a material term of the contract.

Penalties Are Potentially Severe

Penalties for failure to comply are potentially severe under HIPAA.

Penalties for failure to comply with the Public Health Law are $1,000 per day not to exceed $2,000 per violation.[95] Although there is no similar comparable provision in the Mental Hygiene Law, the common law of New York recognizes a cause of action for damages if the Mental Hygiene Law is violated.[96] Penalties for violation of the HIPAA are severe: up to one year in jail or a $5,000 fine per violation.[97] In addition, criminal penalties of up to 10 years in jail and $250,000 may be imposed for certain wrongful disclosures of information.[98]

The regulations do not, however, contemplate a private cause of action, but rather provide that the Secretary of Health and Human Services will develop policies and procedures in order to receive individual or group complaints that a covered entity has not complied.[99] The regulations permit, but do not require, the Department of Health and Human Services to investigate and resolve complaints, and also give the department authority to refer a complaint to the Department of Justice for prosecution.[100]

Relation With Other Laws

The statute and regulations provide that HIPAA preempts state law except to the extent state law relating to privacy of individually identifiable health information is more "stringent."[101] The regulations say that the criteria for determining whether state law is "more stringent" include:

• If relating to use or disclosure: provides more limited use or disclosure.

• With respect to rights of individuals to access their own records: permits greater right of access.

• Provides greater penalties.

• If related to furnishing an individual information about the proposed use or disclosure: provides greater information.

• If related to authorization: provides requirements which narrow the scope or duration or increase the difficulty of obtaining authorization.

• With respect to record keeping or accounting requirements: provides for record keeping in more detail or keeping information for a longer duration.

• In general provides "greater privacy protection for the individual."

Thus, in any particular situation facing a covered entity, an analysis will be required to be made of both New York law and federal law and a judgment made as to which is "more stringent."[102]

Transition Rules

The transition rules permit until April 14, 2003, for compliance with the statute, except for small health care plans which have until April 14, 2004.[103]

1. 45 C.F.R. pts. 160, 164. This article is a summary only and is qualified in its entirety by the regulations themselves. Amendments to the regulations have been proposed, 67 Fed. Reg. 14775 (Mar. 27, 2002).
2. Pub. L. No. 104-191, 110 Stat. 1936 (1996).
3. *Id*.
4. 45 C.F.R. § 160.202.
5. N.Y. Public Health Law § 2134 (PHL).
6. In a court proceeding in New York, specific providers (physicians, dentists, podiatrists, chiropractors, nurses, professional corporations, medical corporations, university faculty ("person authorized to practice medicine")) are not permitted to disclose information which was acquired in attending the patient and which was necessary to enable him to act in the capacity. Civil Practice Law & Rules 4504 (CPLR). The statute has two parts to the test and is limited in its application. CPLR 2306 governs the production of medical records and permits disclosure upon service of a subpoena. Special conditions apply to the disclosure of a mental or physical condition of a deceased patient.
7. Exceptions to the general requirements of confidentiality apply to statistical information required by law. For example: birth and death certificates must be filed with the custodian of vital statistics (PHL §§ 4130(2), 4140(1)); a list of names of fathers and mothers and fetal death cases must be maintained by the Commissioner of Health for the State of New York (PHL § 4100(2)(g)); reports of communicable diseases are required to be filed with the local health district (PHL § 2101); Alzheimer's disease must be reported to the Department of Health (PHL § 2001); HIV infections or AIDS or HIV-related diseases must be reported to the Commissioner of Health of the State of New York (PHL § 2130); all controlled substances dis-

pensed must be reported to the Department of Health (PHL § 3329); report detailing all required immunizations and exclusions to the local health authority and/or the Commissioner of Health (PHL § 2164); and all incidents of cancer are reported to the health officer of the health district (PHL § 2401). Section 3371 of the PHL prohibits disclosure of the record except to another "person employed by the department, . . . pursuant to judicial subpoena or court order in a criminal investigation or proceeding . . . to an agency, department of government, or official board authorized to regulate, license or otherwise supervise a person who is authorized . . . to deal in controlled substances, or . . . to a central registry established" by the health department.

8. Health care practitioners include physician assistants, chiropractors, dentists, dental hygienists, physical therapists, nurses, podiatrists, optometrists, psychologists, social workers, occupational therapists, speech language pathologists and audiologists licensed under various sections of the N.Y. Education Law. N.Y. Mental Hygiene Law § 33.13 (MHL).

9. 42 U.S.C. § 1320d(3) defines a "health care provider" as "a provider of services . . . , medical or other health services . . . , and any other person furnishing health care services or supplies." Regulations provide: "[h]ealth care provider means a provider of services (as defined in section 1861(u) of the Act, 42 U.S.C. § 1395x(u)), a provider of medical or health services (as defined in § 1861(s) of the Act, 42 U.S.C. § 1395x(s)), and any other person or organization who furnishes, bills, or is paid for health care in the normal course of business." 45 C.F.R. § 160.103.

10. 42 U.S.C. § 1320d(5) defines a "health plan" as "an individual or group plan that provides, or pays the cost of, medical care." Health plans include, but are not limited to Medicare, Medicare supplemental, Medicare + Choice, and Medicaid plans; SCHIP plans; state high risk pools; group health plans with 50 or more participants (except employee-sponsored plans); HMOs; health insurers (except group health plans); long-term care policies; employee welfare benefit plans or like organizations; military and veterans health plans; Civilian Health and Medical Program of the Uniformed Services (CHAMPUS) plans; Indian health services plans; and Federal Employees Health Benefit Plan (FEHBP). *See* 45 C.F.R. § 160.103.

11. 42 U.S.C. § 1320d(2) defines a "health care clearinghouse" as "a public or private entity that processes or facilitates the processing of nonstandard data elements of health information into standard data elements." Regulations provide a clearer definition:

    > Health care clearinghouse means a public or private entity, including a billing service, repricing company, community health management information system or community health information system, and "value-added" networks and switches, that does either of the following functions:
    >
    > (1) Processes or facilitates the processing of health information received from another entity in a nonstandard format or containing nonstandard data content into standard data elements or a standard transaction
    >
    > (2) Receives a standard transaction from another entity and processes or facilitates the processing of health information into nonstandard format or nonstandard data content for the receiving entity.

    See 45 C.F.R. § 160.103.

12. "Health information" is

    > information, whether oral or recorded in any form or medium, that—
    >
    > (A) is created or received by a health care provider, health plan, public health authority, employer, life insurer, school or university, or health care clearinghouse; and
    >
    > (B) relates to the past, present, or future physical or mental health or condition of an individual, the provision of health care to an individual, or the past, present, or future payment for the provision of health care to an individual.

    42 U.S.C. § 1320d(4); 45 C.F.R. § 160.103.

13. "Electronic media means the mode of electronic transmission. It includes the Internet (wide-open), Extranet . . . , leased lines, dial-up lines, private networks, and those transmissions that are physically moved from one location to another using magnetic tape, disk or compact disk media." 45 C.F.R. § 162.103.

14. PHL § 18(1)(e).

15. *Id.*

16. MHL § 33.13.

17. MHL § 33.16(a)(1).

18. Pub. L. No. 104-191, 110 Stat. 1936 (1996). The only exception is for health information contained in education records governed by the Family Educational Right and Privacy Act and records of students over 18 held by post-secondary institutions used exclusively for treatment and which the student requests not be disclosed. 45 C.F.R. § 164.501.

19. 42 U.S.C. § 1320d(4); 45 C.F.R. § 160.103.

20. *Id*.

21. *Id*.

22. 45 C.F.R. § 164.501.

23. 45 C.F.R. § 164.514.

24. PHL § 18(2). For treatment provided with the consent of the parent or guardian or for emergency treatment which was the result of an accident or unexpected illness, unless the health care provider determines that access to the information "would have a detrimental effect on the provider's professional relationship with the infant, or on the care and treatment of the infant, or on the infant's relationship with his or her parents or guardian."

25. The term "disclosure" does not include disclosures:

    > a. To other practitioners as part of a consultation or referral of the patient,
    >
    > b. To persons reviewing information or records in the course of ensuring the providers are in compliance with applicable quality of care, licensors or accreditation standards,
    >
    > c. To an employee of a federal, state or local agency who is conducting an audit of the provider,
    >
    > d. To the statewide planning and research cooperative system,
    >
    > e. Pursuant to a court order,
    >
    > f. To governmental agencies, insurance companies or others requiring information necessary for payments to be made,
    >
    > g. To qualified researchers,
    >
    > h. To the state board for professional medical conduct,
    >
    > i. To an insurance carrier insuring or attorney consulted by a health care provider,

j. To a health maintenance organization,

k. To the committee or court pursuant to provisions of Section 18 of the Public Health Law.

PHL § 18(1)(e).

26. PHL § 18(6).
27. *Id*.
28. *Id*.
29. MHL § 33.13(c) excepts the following:
    1. Statistical information reported to the Commissioners (except for names).
    2. Court ordered disclosure—the court must find that "the interests of justice significantly outweigh the need for confidentiality . . ."
    3. To the Mental Hygiene Legal Service.
    4. To attorneys representing the client or patient if the patient's or client's involuntary hospitalization is at issue.
    5. To the Commission on Quality of Care.
    6. To the Medical Review Board of the State Commission of Correction.
    7. To an individual or law enforcement agency when the treating psychiatrist or psychologist "has determined that a patient or client presents a serious and imminent danger to that individual."
    8. To the State Board for Professional Medical Conduct upon request.
    9. To certain governmental agencies, insurance companies, agencies needing information to locate missing persons, governmental agencies in connection with criminal investigations (restricts disclosure only to information required to satisfy the matter under investigation).
    10. Qualified researcher.
    11. Coroners, county medical examiners, or similar persons investigating the death of the patient or client.
    12. Persons "necessary to prevent imminent serious harm to the patient or client or another person."
    13. To the district attorney in connection with a criminal investigation of patient or client abuse.
30. MHL § 33.13(f).
31. MHL § 33.13(c)(1).
32. MHL §§ 33.13, 33.16.
33. MHL § 33.16.
34. 45 C.F.R. § 164.508.
35. 45 C.F.R. § 164.506.
36. *Id.* A covered health care provider should, in an emergency situation, obtain consent as soon as reasonably practicable after the delivery of such emergency treatment.
37. *Id.*
38. Tommy G. Thompson, Statement Regarding the Patient Privacy Rules (Apr. 12, 2001).
39. C.F.R. § 164.506.
40. *Id*.
41. *Id.*
42. *Id*.
43. *Id*.
44. 45 C.F.R. §§ 164.502(b), 164.514(d).
45. 45 C.F.R. § 164.508.
46. 45 C.F.R. §§ 164.502, 164.512.
47. PHL § 18(3).
48. The exemption of personal notes and observations does not apply once the litigation has been started, the subject of which is the patient's health history. *Magee v. Paul Revere Life Ins. Co.*, 172 F.R.D. 627 (1999).
49. PHL § 18(3)(d).
50. PHL § 18(3)(f).
51. *Id*.
52. *Id*.
53. *See* PHL § 18.
54. PHL § 18(3)(f).
55. *Id*.
56. *Id*.
57. MHL § 33.16(c).
58. *Id*.
59. *Id*.
60. MHL § 33.16(c)(5).
61. *Id*.
62. *Id*.
63. MHL § 33.16(d).
64. MHL § 33.16(e).
65. 45 C.F.R. § 164.524.
66. *Id*.
67. *Id*.
68. 45 C.F.R. § 164.526.
69. *Id*.
70. PHL § 18(8).
71. *Id*.
72. MHL § 33.16(g).
73. *Id*.
74. *See id*.
75. 10 N.Y.C.R.R. § 405.10(c)(4).
76. 10 N.Y.C.R.R. § 415.22.
77. 10 N.Y.C.R.R. § 415.30(d), (e).
78. 10 N.Y.C.R.R. § 425.21.
79. 45 C.F.R. § 164.530.
80. *Id*.
81. *Id*.
82. *Id*.
83. 45 C.F.R. § 164.520.
84. *Id*.
85. 45 C.F.R. § 164.520(a).
86. 45 C.F.R. § 164.520(b)(2)(i).
87. 45 C.F.R. § 164.520(b)(1)(vii).
88. 45 C.F.R. § 164.524.
89. 45 C.F.R. §§ 164.501, 164.524(e).
90. 45 C.F.R. § 164.530(e)(1).
91. 45 C.F.R. § 164.528.
92. 45 C.F.R. § 164.504(e).
93. 45 C.F.R. § 160.103.
94. 45 C.F.R. § 164.504(e)(ii)(2).
95. PHL § 12.
96. *City of New York v. Bleuler Psychotherapy Ctr., Inc.*, 181 Misc. 2d 994, 695 N.Y.S.2d 903 (Sup. Ct., N.Y. Co. 1999).
97. Pub. L. No. 104-191, 110 Stat. 1936 (1996).
98. *Id*.
99. 45 C.F.R. § 160.306.
100. *Id*.
101. 45 C.F.R. § 160.202.
102. *Id*.
103. 45 C.F.R. § 164.534.

View From Abroad

Turkey Embraces Arbitration as Step Toward Global Economic Integration

BY TOM GRANT

Turkey, a strategic and commercial ally in the Near East, reached a milestone this April in the development of its legal system. For the first time, parties chose arbitration to resolve a major dispute involving foreign direct investment and the Turkish public sector.

New Jersey-based PSEG Global and Texas-based North American Coal Corporation, with Turkish partner Konya Ilgin Uretim Ticaret, initiated arbitral proceedings against the Ministry of Energy on April 2, 2002, before the International Centre for Settlement of Investment Disputes (ICSID). With $300 million in dispute, the proceedings over the Konya Ilgin thermal power plant constitute a show of confidence in recent pro-arbitration reforms painstakingly enacted at the constitutional and statutory level.

As this and a smaller dispute over a telecommunications joint venture progress toward final awards, Turkey apparently stands ready to cement its commitment to the culture and institutions of arbitration and, in tandem, to move a critical step further toward integration in the global economy.

Taken so much for granted in the United States and most of the West, arbitration continues to struggle uphill in other parts of the world. Where it has gained a toehold, it all too often remains simply the pet project of some small corner of the bar. But the government bankers I met in Ankara demonstrate that, in Turkey, this dispute resolution technique concerns people well beyond the confines of the legal profession; it rests on foundations that pre-date the lobbying by the International Monetary Fund and the Organization for Economic Cooperation and Development in the midst of the recent economic challenge. Turks widely recognize arbitration as a foundation stone in their country's economic progress. And the economic progress of Turkey—by far the strongest and most diversified Muslim economy in the Near East not wedded to oil exports—must continue, if that vital ally in the war against terrorism is to remain secure.

Personal Experience with Arbitration

The striking awareness of the importance of arbitration was brought home to me vividly one afternoon at the beginning of the economic crisis that Turkey is only now beginning to reverse. Visiting Ankara, I spoke in the boardroom of the Central Bank of the Republic. It was February 21, 2001, and the *lira*, Turkey's national currency, earlier that day had entered a steep slide, precipitating the country's worst financial crisis in over half a century. The bad news from the markets—by noon the Istanbul Stock Exchange had already begun its own crash on word of the currency debacle—left me certain that my intended audience would be detained elsewhere, struggling to contain the crisis. I apprehended the prospect of a non-event. After all, what did international arbitration have to do with currency stability, economic health, or any of the other matters weighing so heavily on my banker hosts that day?

In the broad view, however, international arbitration has *everything* to do with Turkey's present concerns, and the bankers, although more at home with debt negotiations and currency statistics than litigation and contractual text, showed that they recognize this as much as anyone. They turned out in number, crowding the governor's boardroom atop the high-rise bank headquarters as a sleeting rain fell outside. Seated at the head of the table in the place usually reserved for the governor of the bank himself, I fought back concerns and stuck to the topic. And, to my surprise, the audience listened more than just attentively, but with a gradually increasing spark and enthusiasm that helped part the gloom of the day.

Turkey in 2001 hit a bump on the road to development. With the Istanbul Stock Exchange ultimately suf-

TOM GRANT is the Warburg Research Fellow at St. Anne's College, Oxford University, where he concentrates on public international law and international dispute resolution. A graduate of Harvard College and Yale Law School, he is a member of the bars of Massachusetts, Washington, D.C., and New York. He is a member of the International Environmental Law Committee of the New York State Bar Association.

fering an 18% decline as the currency lost one-third of its value (in what local media called a "dark week" in winter) that year, the bump was jarring. But emerging markets elsewhere have experienced similar or worse, and Turkey, exemplary among countries grappling with economic reform, has taken steps to make itself a good place to invest. Regulatory roll-backs and privatizations rank as the best-known changes in Turkey's investment environment and, indeed, have stimulated growth. A lesser-known reform in Turkey's constitutional and legal framework, however, opens the way to international arbitration of investment disputes; and this, as much as other reforms, bodes well for investment in the biggest economy of the Balkan and Near East regions.

Equally deserving of attention have been Turkey's bold steps toward building a constitutional and legal framework for international commercial arbitration.

Starting in the 1980s, Turkey made an historic transition. Decades of military rule began to give way to civilian government, and, in turn, democratic accountability achieved standards rarely matched in the important regions Turkey straddles. Economic reforms were initiated in earnest. Regulatory burdens were reduced and privatization initiated. Bureaucratic foot-dragging and corruption were curbed, and, starting in January 2000, disciplined budgetary and inflation policies were put in place. Turkey, as recent developments make clear, is open for business. Foreign investors have verified this by committing billions.

Building a New Framework

Equally deserving of attention have been Turkey's bold steps toward building a constitutional and legal framework for international commercial arbitration. As most basically defined, arbitration is a means by which parties can resolve a dispute pursuant to contractual undertakings, without recourse to court. Instead of winding its way through one or more national judicial systems, the dispute goes to private, non-governmental decision makers, who produce a binding award enforceable in the courts of virtually any important trading nation on earth. For multiple reasons, major investors—especially those engaged in the biggest projects—find arbitration a reassuring alternative to litigation in court.

Arbitration increases neutrality, because its decision-making personnel are not government-appointed—a particular reassurance to private investors when doing business with a government or with a government-owned entity. Arbitration decreases uncertainty because, through a contract to arbitrate, the parties agree not to initiate duplicative proceedings in national courts, which might produce contradictory decisions. Speed and efficiency can increase, in comparison to court-based litigation, when parties to an arbitration agree to limit discovery. Moreover, arbitration benefits parties by its flexibility. Rules systems, the place of arbitration, and the identity of arbitrators are party-controlled, allowing the parties to tailor a dispute settlement machinery to their particular circumstances. Its advantages can be as marked as those of a bespoke suit from Saville Row over an off-the-rack suit from a discount men's store and yet be cheaper than the one-size-fits-all court-based alternative.

Unfortunately, many countries have hesitated to adopt arbitration wholeheartedly. The United States itself, now at the federal level one of the most pro-arbitration of jurisdictions, took years to find a comfortable balance between concerns over lost sovereignty and fairness on the one hand and the benefits of arbitration on the other. Emerging market countries now visit many of these same concerns anew. Despite the inherent difficulty in getting the balance right—and the high political costs of getting it wrong—Turkey's leaders have moved to the fore in promoting arbitration.

Introducing arbitration to Turkish law required deft political footwork. During summer 1999, Prime Minister Bulent Eçevit championed reform to pave the way for arbitration, but he faced opposition. Labor unions—natural allies of the left-leaning Eçevit—begged to differ with him on arbitration. In fact, they protested its introduction vehemently. So did some members of the Turkish bar associations, expressing concern that extra-judicial dispute resolution would strip away Turkey's sovereignty. And, not at all trivially in a country proud of its past, historians complained that arbitration sounded like the judicial "capitulations" that the Ottoman state in the 19th century had granted European merchants, exempting them from local legal process and standards.

Eçevit countered by noting that some people simply fear progress.[1] Getting to the heart of the matter, the prime minister explained that foreign investors' confidence in Turkey would increase if arbitration were introduced—and erode if it were not. In particular, foreign investors contemplating a stake in newly privatized industries would fear litigating against the Turkish state or state-owned entities in Turkish courts. (Turkish businesses, it might be added, would have good reason to

worry about litigating in American courts, with their reputation for runaway juries and bankruptcy-inducing punitive damage awards.) Thanks to effective presentation of the case for reform—and some tenacious bargaining—the necessary 368 out of 550 deputies in parliament joined in August 1999 to amend Article 125 of the constitution and thus open the way to arbitration.

Parliament took advantage of this strategic opportunity and passed, in June 2001, an arbitration bill, setting up the detailed statutory framework for private dispute resolution in key sectors of foreign investment. Pro-arbitration constituencies in Turkey, aided by urgent calls from the IMF and OECD, crafted the bill to address all key aspects of its subject, while averting a showdown with skeptics. Under the law, parties may incorporate an arbitration agreement into the body of a larger contract or draft it as a freestanding instrument. Parties may choose arbitrators themselves or, at the election of a party, may delegate this responsibility to a magistrate's court. Other provisions address procedure, choice of seat and language, and review and enforcement of awards.

Role of Courts

Any effective national arbitration law needs to reserve for courts those areas of policy that a country's citizens believe must remain in public hands. Turkey's opinion leaders at one point had urged that *all* matters concerning investment in the energy sector be "non-arbitrable"—that is, reserved to domestic public organs for adjudication. Energy, however, is one of the sectors in Turkey most requiring foreign investment. The Council of State—the "Danistay"—would have retained full and final say over energy sector investment disputes, if the value of arbitration had not been effectively explained. Luckily, in the compromise finally reached, the Danistay retains some but not all jurisdiction over the review of energy sector arbitrations—enough to address legitimate concerns over national sovereignty, not so much as to hollow out arbitration.

The balance resembles that struck in many countries where leaders with competing interests have wrestled over the roles of public and private institutions in resolving disputes—not least resembling the balance struck in the United States, where matters of public policy such as antitrust and race and gender discrimination have marked the edge of the legal territory where arbitration may acceptably be given free rein.

Among the vital development projects that arbitration will facilitate in Turkey are some two dozen power plants, construction of which is valued at $4.2 billion and output of which will top 15 billion kilowatt hours per year. It is no coincidence that the Konya Ilgin ICSID arbitration is attracting the interest of energy sector analysts. Other major programs that will benefit from international confidence in Turkey's arbitration system include new sea container terminals, urban water supply projects, a railroad between the Mediterranean cities of Alanya and Antalya, and a third bridge over the Bosphorus.[2]

International Assistance

Treasury Secretary Paul O'Neil, after the onset of the economic crisis in 2001, called on the IMF to assist Turkey. In the form of Deputy Secretary of Defense Paul Wolfowitz, Turkey has another friend in the present administration. Intervention makes sense in Turkey if it does anywhere. A crucial zone of stability and economic progress, the country has long supported the United States as a strategic NATO ally and brought a calming influence to its region. In the wake of the September 11 atrocities, Turkey renewed and reaffirmed the relationship, by pledging units of its elite commando force to help with the war against terrorism and even to take over the bulk of peace-keeping duties in Afghanistan, after the initial phases of the conflict make the transition to longer-term "nation-building" tasks.

Among the vital development projects that arbitration will facilitate in Turkey are some two dozen power plants, construction of which is valued at $4.2 billion.

Foreign capital last year fled Turkey in amounts disruptive to the economy and political system, and painful to the ordinary citizen. Prospects ahead however remain bright. Public disagreements between the president, Ahmet Sezer, and the prime minister, Bulent Eçevit, seemed to exacerbate the financial crisis, yet the peaceful return of normal relations within the government testify that democratization has anchored itself firmly. Relationships within the civilian government, and between it and the military-led National Security Council in some aspects still require clarification, but a presidential-prime ministerial tussle of February 2001, even coinciding with a "dark week," gave rise to no noticeable disquiet. At the nadir of the crisis, incidents certainly occurred—perhaps the most publicized involving an angry shopkeeper heaving an empty cash register at the prime minister. But the tone in the streets of Ankara and Istanbul remained through the worst of the crisis essentially business-like, as a hard-working populace plowed ahead. More than a

year later, and amidst yet greater volatility in the Near East at large, calm prevails in Turkey, and a cautious optimism begins to buoy spirits, markets, and foreign investment.

Arbitration requires more than just changes in constitutional text. The national legislature and regulators must take a higher level of advantage of the opportunities afforded by pro-market and pro-arbitration reforms. Even with that accomplished, the judiciary and bar must adapt themselves to the institution of arbitration, for, without judges and counsel ready and able to use the institution, its mere presence on the books is unlikely to amount to much. Turkey has taken the first two steps—constitutional reform and appropriate rules at the statutory and regulatory level—and is well on the road to the final step, establishing the requisite human infrastructure. Key indicators point to Turkey succeeding in this crucial concomitant to its far-reaching program of economic and political reform. The past decade-and-a-half have witnessed reduced corruption, improved human rights, and greater political stability. One of the most ambitious privatization drives in the developing world rounds out the picture. As these reforms and supporting institutions take root and key players in Turkey continue to recognize well their importance, Turkey's short-term challenges should give way to its already-realized, and continuing, promise.

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1. Kemal Balci, *Arbitration Issue Causes Confusion*, Turkish Probe, Aug. 9, 1999.
2. Middle East Econ. Dig., Feb. 4, 2000.

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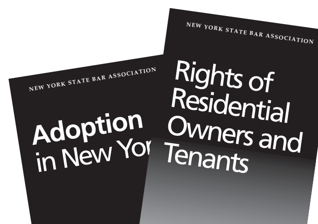

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Meet Your New Officers

President

Lorraine Power Tharp, a member of the law firm Whiteman, Osterman and Hanna in Albany, has taken office as president of the New York State Bar Association (NYSBA). She is the third woman, the first from the Capital District, elected to head the nation's largest voluntary state bar association.

A graduate of Smith College, Tharp earned her law degree from Cornell Law School. She has been a member of the state bar's Executive Committee since 1994, and served four terms as its secretary. She served as president-elect, chaired the House of Delegates and co-chaired the President's Committee on Access to Justice. A past chair of the Real Property Law Section and a past member of the Committee on Women in the Law, Tharp was the project chair of the subcommittee that drafted the NYSBA's report and model policy on sexual harassment. She is also a past member of the Unified Court System's Continuing Legal Education Board. She is a Fellow of The New York Bar Foundation.

Tharp, a native of Massena, recently joined the Whiteman firm. Previously, she had been a partner at another Albany law firm, McNamee, Lochner, Titus & Williams, P.C. She and her husband, Russell, who practices law in Glens Falls, live in Saratoga Springs. Active in community affairs in both Albany and Saratoga, in 2002, Tharp was selected Woman of the Year by the Saratoga Soroptimist Club. She is the immediate past chair of the Saratoga Springs Planning Board and currently serves on the Saratoga Hospital Board of Trustees, The Hyde Collection Art Museum Board of Trustees and the Empire State College (SUNY) Foundation Board of Directors.

Elected to the American College of Real Estate Lawyers, Tharp has lectured and written extensively in the area of real estate law practice for such organizations as the NYSBA, National Business Institute, and New York University Real Estate Institute programs.

President-Elect

A. Thomas Levin, a shareholder and director of the Mineola law firm of Meyer, Suozzi, English & Klein, P.C, is the president-elect of the New York State Bar Association (NYSBA). As president-elect, he is chair of the House of Delegates and co-chair of the President's Committee on Access to Justice. He will become Association president in June 2003.

A graduate of Brown University, Levin holds a J.D. and an LL.M., both from New York University School of Law.

Levin has served on the Association's Executive Committee since 1995, first as a Member-at-Large, then as 10th Judicial District Vice President, and since 2001, as Secretary of the Association. He chaired the Task Force on "Pay to Play" Concerns and the Committee on Bylaws. A member of the House of Delegates for more than 13 years, Levin is a Life Fellow of The New York Bar Foundation and a past chair of the New York State Conference of Bar Leaders. In addition, he is a past president of the Nassau County Bar Association and a past member of the ABA's House of Delegates; he is a Fellow of the American Bar Foundation.

Levin was counsel to the New York State Assembly Judiciary Committee and the Joint Legislative Committee on the State's Economy and law secretary to state Supreme Court Justice Bertram Harnett. By appointment of the Chief Judge of the State of New York, Levin served on the Unified Court System Task Force on the Profession and the Courts, and the Committee of Lawyers to Enhance the Jury Process.

The author and editor of numerous articles and publications on various legal subjects, Levin frequently lectures on such issues as professional ethics, law office management, municipal, environmental, and civil rights law. Since 1972, he has provided free legal services as general counsel to the Day Care Council of Nassau County and the Rosa Lee Young Childhood Center, Inc.

Treasurer

Kenneth G. Standard, special counsel in the labor and employment law practice group at the Manhattan law firm of Morgan, Lewis & Bockius, is Treasurer of the Association.

Standard received his undergraduate degree from Harvard College and earned his law degree from Harvard Law School. In addition, he holds an LL.M degree from New York University School of Law.

Prior to joining Morgan Lewis, Standard served as Assistant General Counsel for Labor Relations, Environmental and Benefit Plans at Consolidated Edison Company (ConEd) of New York City. In addition, he is a former director of the Office of Legal Services for the New York City School System and was vice-president of the Products Division of Bristol-Myers Company.

Standard is a former Member-at-Large of the Association's Executive Committee and Vice-President representing the First Judicial District. He has served on numerous Association committees, including Judicial Selection, Law Governing Firm Structure and Operation (MDP), and Association Governance. A sustaining member of the Association, Standard is a Fellow of both The New York and American Bar Foundations. He also serves on the NYSBA's House of Delegates.

Active in community affairs, Standard is the immediate past president of the Harvard Club of New York City, is a director of the Visiting Nurse Service of New York City, and is the former vice-chairman of the Aspirin Foundation of America.

Secretary

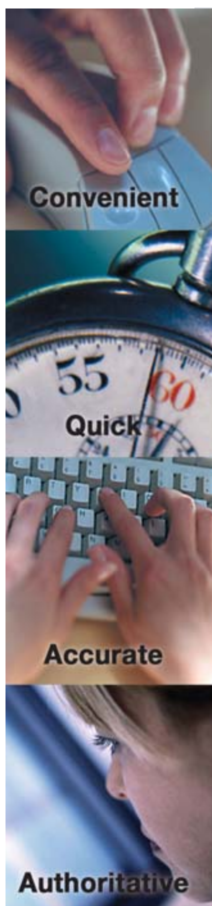
A. Vincent Buzard, a partner in the Rochester offices of Harris Beach LLP, is Secretary of the Association.

During the past 20 years, Buzard has held various leadership positions in the Association, including Member-at-Large of the Executive Committee and Vice President, representing the Seventh Judicial District. He serves on the House of Delegates, and has chaired the New York State Conference of Bar Leaders and co-chaired both the Lawyers in the Community and Medical Malpractice Committees. Currently, Buzard chairs the Special Committees on Legislative Advocacy and Cameras in the Courtroom.

A resident of Pittsford, he is a past president of the Monroe County Bar Association; he received the Adolph J. Rodenbeck Award for outstanding contribution to the community and the profession. He served as corporation counsel to the city of Rochester, and on the American Bar Association's House of Delegates, the National Conference of Bar Presidents and Chief Judge Judith S. Kaye's Special Committee on the Establishment of Commercial Courts in the State of New York. Buzard is a member of the Governor's Fourth Department Judicial Screening Committee and a referee for the New York State Judicial Conduct Commission.

A practicing trial lawyer for more than 30 years, Buzard focuses on complex civil litigation including representing people who are seriously injured, with a particular emphasis on those who have suffered brain injuries. He is a past president and a former board member of the New York State Head Injury Association.

Buzard is a regular contributor to numerous publications and is a legal and political commentator for local radio and television stations. He earned his undergraduate degree from Wabash College of Indiana and his law degree from the University of Michigan Law School.



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POINT OF VIEW

The HP Proxy Fight: Circus Or Governance Paradigm?

BY JOHN C. WILCOX

The Hewlett-Packard proxy contest deserves to be remembered, along with the Enron scandal, as a corporate governance milestone. Indeed, HP and Enron are true counterpoints, illustrating the best and the worst that the U.S. corporate governance system can produce.

HP's proxy fight was built on the populist model and embraced all the company's public constituencies, treating them to a full display of American corporate democracy in action, complete with a town meeting and a political-style campaign. Enron hid from its constituents, and its collapse reveals everything that can go wrong when company insiders assume they know best, evade governance responsibilities and mislead the investing public.

Given these contrasts, it was surprising to see the negative spin that built up during the HP contest. Some news stories went out of their way to paint a picture of a seamy, personal struggle with "smashmouth politics," backbiting and dirty tricks.

These negative characterizations did not do justice to the merits of the contest. Both HP management and dissident director Walter Hewlett deserve commendation for conducting campaigns that kept shareholders focused on the issues. The result was a textbook proxy fight and a genuinely effective shareholder referendum on key questions of business strategy. Although not a contest for control, HP ranks as one of the most visible and hard-fought contests in recent years. With the dismissal of claims of coercive tactics, it also ranks as one of the cleanest.

By contrast, the headlines of advertisements from famous past proxy contests screamed "DROP DEAD!" (RJR Nabisco), "Show Us the Money" (ITT), "Don't Be Conned By Kahn" (ICN Pharmaceuticals) and, the most famous of all, "The Directors of Sears, Roebuck & Co.—NON-PERFORMING ASSETS" (Sears/Robert Monks). Referring to Walter Hewlett as an academic and musician, or revealing details of Carly Fiorina's proposed pay package, are mild by comparison.

The negative spin on HP may simply reflect the media's tendency to embellish business stories with celebrity and big money angles. But there is a deeper cause, arising from the American public's love-hate relationship with democratic processes. We insist on the politics of inclusion, but at the same time we are resentful and slightly ashamed of the spectacle and the mess that result.

Given this ambivalence and the long-standing negative perception of proxy contests, HP should help us recognize that proxy fights can be a legitimate, practical and effective tool of good corporate governance.

Despite their notoriety, proxy contests are underutilized. During last year's proxy season there were just 40 proxy fights, out of a universe of nearly 10,000 annual meetings of U.S. publicly traded companies. (Since our firm started keeping records more than 20 years ago, the record number of contests was 41 in 1989, and the lowest was three in 1993.) What accounts for their scarcity? Dissatisfied investors often express reluctance to take their case to shareholders because they believe proxy fights are "impossible to win," "expensive," "time consuming," "risky," "unpredictable" or "the cards are stacked in favor of management." But in today's environment virtually all of these concerns are either illusory or readily overcome.

A case in point is the successful proxy fight earlier this year by investment manager Orbimed against Pharmacopeia Inc. Like HP, this contest opposed a merger proposal. But unlike the HP dissidents, Orbimed waged a low-profile communication campaign that targeted the largest accounts and avoided SEC filing requirements by not seeking direct proxy voting authority. Shareholders were simply asked to vote no on the management proxy. Orbimed's "clean" campaign, like HP's, focused on business and financial considerations. But unlike HP, Orbimed's success came with minimal public fanfare and at a reasonable cost.

The HP contest was on an entirely different scale, and it compels us to face the two criticisms of proxy fights that are raised most often—their cost and inefficiency.

When an Orbimed-style campaign will not suffice, the out-of-pocket costs, regulatory requirements and potential liabilities of a large solicitation deter all but the richest, best-organized and most committed dissidents. However, as a form of self-selection, this may not be altogether a bad result. Of greater concern are the basic inequities in the financing of solicitation campaigns. Company managers can use corporate (*i.e.*, shareholder) money and insurance, while dissidents are denied access to corporate resources. On the other side of the argument, the U.S. regulatory structure clearly works to the advantage of shareholders. The proxy rules keep managers in lockstep formation like British redcoats, while dissident freedom fighters are granted the flexibility to wage targeted low-cost guerrilla campaigns. The win-loss records are revealing. In recent years dissident successes have ac-

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Lawyer's Bookshelf

Inside/Outside: How Businesses Buy Legal Services by Larry Smith, ALM Publishing, www.lawcatalog.com; 379 pages, $34.95. Reviewed by Lori Tripoli.

Hot-shot lawyers and top-notch law firms might have spent the last years of the va-va-voom, dot-com-boom '90s branding, niche-marketing, perfecting their PowerPoint pitches and developing multi-paged Web sites with really cool yet appropriately serious graphics, but, for all the marketing mania the Clinton ("it's all about the spin") years brought us, the overblown and too early celebrated millennium has gotten off to a slow start.

Those fast-flying firms that just a short while ago could dismiss a client unwilling to throw an ever-rising threshold of legal fees their way might just be finding themselves having to fish for new business. And no matter how expensive the fishing rod or late-model the gear, the lawyer looking to reel in clients today has got to know what will make them bite. Which is exactly what Larry Smith explains in his new book, *Inside/Outside: How Businesses Buy Legal Services*.

Smith, a principal in Levick Strategic Communications and the long-time editor of *Of Counsel*, a law firm management report, has done an exhaustive study of the buying process, interviewing hundreds of insiders at Fortune 100 companies as well as start-ups. In discussions with general counsels, he has found out which companies like to keep all the truly challenging legal work in-house for themselves while farming out the more routine, who really makes the decision to retain a given firm (it's not just in the general counsel's hands at McDonald's and Caterpillar, where the hiring decision has been delegated downward), and what truly impresses the judges in all those beauty-contest pitches.

An enormous amount of material is crammed into a book that features case study after case study and a look at seemingly every business trend that's surfaced over the past 15 years or so and in-house counsels' responses to them. Smith writes about the development of mega-firms and why some companies like them and others don't; he talks about the encroachment of multidisciplinary practices and tells why all that buzz about law-firm branding was, in the end, a bit overblown; and he reveals how some firms cannily edged out their competition in unexpected ways.

Vinson & Elkins, for instance, a Texas-based law firm with a stellar reputation (at least before its representation of Enron became well-known), was willing to get its foot in the door at Motorola by performing lower tier legal work as regional counsel for Motorola's semiconductor operation based in the Lone Star State. Stamford, Conn.-based Cummings & Lockwood, a firm known for its trusts and estates practice, leapt at the opportunity to shore up its corporate practice when high-tech corporations (think Priceline) began popping up in the region. Smith also talks about how some New York-based firms may have overlooked an opportunity to grow their Silicon Valley, Calif. branches when young dot-coms with growth potential but relatively low fee revenue thresholds were shopping for legal representation.

Always, the merit of Smith's work is in both the broad strokes depicting the legal business he paints and in the details he adds. Practitioners should glean plenty from discussions of convergence, or the winnowing of the number of law firms a large corporation is willing to do regular business with, at companies like DuPont, Prudential, and Ultramar Diamond Shamrock. Smith doesn't just speak of how the process worked and why some law firms won out but also mentions when some of those corporations are willing to look beyond their established relationships and hire off-list.

Clearly knowledgeable about his subject matter, Smith has done an outstanding job presenting an enormous amount of material in readable, well-organized form. That said, an index would have been enormously helpful, as would a list of sources interviewed, as Smith tends to revisit interviewees introduced early on. Smith's treatment of a potentially dry subject is typically engaging as he manages to illustrate his points with specific examples culled of any extraneous detail. It takes a gift, and a well-honed writing style, to merge such a comprehensive discussion into interesting narrative interspersed with plenty of good quotations and contrasting examples.

While Smith's style is engaging, it does on occasion veer toward pretentiousness. Negotiations between buyer and seller don't reach a dead end but a *cul-de-sac*, an unfortunate mix of lawyers is a *mélange*, changes to GE's legal department weren't complete but a *fait accompli*, and nothing is "commonplace," it's *de rigueur*. Even if you are pitching to the ten-dollar-word crowd, Smith's fluency in "Franglais" is, well, *passé*.

That said, it's a *petit* quibble with an otherwise necessary work. Lawyers looking to stay ahead of the curve, or to figure out a way to get there, would do well to read it.

Lori Tripoli is a freelance journalist in Westchester County whose work has appeared in numerous legal and business publications. She received her law degree from the Georgetown University Law Center in 1989.

Language Tips

By Gertrude Block

Question: I recall a rule that one *compares with*, but *contrasts to*. Is that rule still in effect?

Answer: The rule the reader refers to is stated in the *American Heritage Dictionary* (1982 edition). It goes like this: When stating the similarity of two things, use *compared to*. For example, "The human brain has been compared to a computer." Thus, *compared to*, under that rule, is synonymous with *likened to*. But when *compared* means "worthy of comparison," comparing both similarities and differences, use *compared with*. For example, "This year's economy can be compared with last year's."

As you can attest, the rule is not often observed, and because even educated speakers don't make the distinction, dictionaries now ignore it. The 1987 unabridged *Random House Dictionary* says, "Following . . . *compared*, either *to* or *with* is used regardless of whether differences or similarities are stressed." But because there is also no rule that you must avoid the distinction in your own usage, you can continue to do so.

There is a rule, however, regarding the preposition to use after the word. Use *with* after the verb and *between* after the noun, unless you want to stress opposition in your use of the noun. Illustrations of the rule follow:

- The response of the administration to student sit-ins contrasts *with* that of the previous administration. (Here *contrasts* is a verb.)
- Television has reduced the contrast between the dialects of eastern and southern United States. (Here *contrast* is a noun.)
- In contrast to Senator Quagmire's previous stand against a tax increase, he now proposes to raise taxes again. (Here *to* is selected, to show contrast.)

But if you ignore that rule, you are like many educated users, and because wide, current use eventually determines what is correct, dictionaries will eventually also ignore the "rule."

From the Mailbag I:

In the February "Language Tips," Fordham Law School professor Michael Martin argued that *hereinafter* parentheticals are often unnecessary, except in contracts or in footnotes to articles. Professor Martin also argued that in all other cases they are not only unnecessary but fail to give the reader sufficient credit for being able to connect the abbreviation to the full name. He added that "hereinafter parentheticals" exemplify the gobbledygook lawyers learn in their legal training. I suggested that other lawyers should write to agree or disagree with Professor Martin's comments.

Attorney Kathryn McCary e-mailed her disagreement. While noting that *hereinafter* may not always be necessary, she argued that parenthetical identification of a short form that will later be used in place of the full name of a statute or other documents is a matter of common courtesy.

Her practice is primarily in education law, in the subfield special education law, which "revolves around the abominably named federal statute, the Individuals with Disabilities Education Act, or IDEA." Parents of disabled children, lay advocates and attorneys fall into the habit not only of referring to the statute as IDEA, but of using other acronyms within the field as if they were words in common usage (for example, FAPE, IEP, FBA—pronounced "fibba"—and even Edgar—Education Department General).

This, Ms. McCary points out, is confusing and frustrating to the uninitiated, which, she believes, is a significant reason for using the acronyms. Not only does the language make the user appear "an initiate into mysteries beyond the comprehension of the general public," but it is rude and contrary to today's requirement that legal speech and writing should be clear and comprehensible.

Ms. McCary agrees that the anticipated audience is a factor in deciding whether to use "hereinafter parentheticals." When preparing a memorandum of law for a New York State Supreme Court Justice, she would use abbreviations like CPLR without writing out the full name of the statute.

From the Mailbag II:

Rochester lawyer Anna Catalani (who prefaced her comment with the question, "Can you "stomach" another interpretation of *agita*?") wrote that when her Italian relatives came down with agita, they were referring to *acido*, commonly known as acid indigestion. She wrote that Americans have "tortured" *acido* into *agita*. Americans have also mispronounced other Italian words such as *bruschetta*, which should be pronounced with a *k*, not a *sh* sound, and other menu items. Ms. Catalani adds, "It gives me acido just to think about it."

My thanks to Attorney Catalani for her comment. But because I do not want to cause my New York readers either *agita* or *acido*, this will probably be my last word on the subject.

Gertrude Block is the writing specialist and a lecturer emeritus at Holland Law Center, University of Florida, Gainesville, FL 32611. Her e-mail address is Block@law.ufl.edu.

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1/1/02 - 5/31/02 __________4,423

NEW LAW STUDENT MEMBERS
1/1/02 - 5/31/02 ____________714

TOTAL REGULAR MEMBERS AS OF
5/31/02 ________________58,325

TOTAL LAW STUDENT MEMBERS AS OF 5/31/02_______________3,967

TOTAL MEMBERSHIP AS OF
5/31/02 ________________62,292

POINT OF VIEW
CONTINUED FROM PAGE 54

celerated to the point where they are very nearly on a par with incumbents'—an indication that financing inequities are at least partially neutralized by dissidents' regulatory and tactical advantages.

The so-called inefficiency of proxy contests is in the eye of the beholder. To the business community, proxy fights are unfamiliar territory—they just don't fit into spreadsheets. Proxy fights are undeniably about economic value, but they are also about power and ideas. The medium is votes, not dollars, which introduces an element of imprecision that makes both financial and legal advisors uncomfortable. Proxy contests bring with them unwelcome reminders that corporations belong to ordinary people and that these people may have opinions not entirely aligned with deal term sheets and pro forma financial statements. "Inefficiency" is inevitable when business goals are tied to democratic processes. In the United States we would not have it any other way.

Proxy fights will always be a remedy of last resort. They cap a regulatory system that is constantly struggling to balance conflicting goals—investor protection and market efficiency. Either too many or too few proxy fights could disrupt this balance. The continuing tension between the power of proxy fights and the barriers to using them should ensure that the right balance is maintained.

JOHN C. WILCOX is an attorney who serves as vice chairman of Georgeson Shareholder Communications Inc., which represented Hewlett-Packard in the proxy fight involving its merger with Compaq.

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In Memoriam

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Howard Vinokur
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THE LEGAL WRITER
CONTINUED FROM PAGE 64

Football fans take heart: Sports metaphors in legal writing do not come only from baseball. In its final sentence, the dissenting opinion in Florida's *Gore v. Harris*,[8] later *Bush v. Gore*, quoted football coaching legend Vince Lombardi's touchdown: "We didn't lose the game, we just ran out of time." The Seventh Circuit[9] also relied on a football metaphor to reverse its chief judge's judgment:

> Football fans know the sickening feeling: your team scores a big touchdown but then a penalty flag is tossed, wiping out the play. Universal Bancard Systems, Inc. knows that feeling firsthand after seeing not one, but two big touchdowns called back. The referee who waved off the first—a $7.8 million verdict—and then the second—a $4.1 million jury verdict after a second trial—was the Honorable Richard A. Posner, the circuit's chief judge who in this case was wearing, by designation, the robe of a district judge. Like the instant replay official, we now review the decisions of our colleague—using the voluminous record rather than a television monitor and recognizing that our review in 1999 of a case that began in 1993 is a far cry from instant.

A beautiful metaphor, from Judge Learned Hand: "Juries are not leaves swayed by every breath."[10]

A metaphor on the cutting edge: "Language is the lawyer's scalpel. If he cannot use it skillfully, he is apt to butcher his suffering client's case."[11]

A galloping metaphor: "Public policy is a very unruly horse, and when you once get astride it you never know where it will carry you."[12]

A musical metaphor: "A minor participant in the orchestra of a conspiracy is as much as part of it as is the concert master."[13]

A metaphoric clause that will drive you to drink: "After you have brushed the foam off the beer, the plaintiff's argument concerns only one item—money."[14]

A metaphor that contains some real nuggets:

> In the case of inexperienced pro se litigants, it is better to err on the side of admitting an ore-heap of evidence in the belief that nuggets of truth may be found amidst the dross, rather than to confine the parties to presenting assayed and refined matter which qualifies as pure gold under the rules of evidence.[15]

Next Month: Allegories, similes, and combinations with metaphors.

1. 248 N.Y. 339, 352 (1928) (Andrews, J., dissenting).
2. Aristotle, The Rhetoric of Aristotle 188 (Lane Cooper trans., 1932).
3. James D. Hopkins, *Notes on Style in Judicial Opinions*, 8 Trial Judges J. 49, 50 (1969), *reprinted in* Robert A. Leflar, *Quality in Judicial Opinions*, 3 Pace L. Rev. 579, 585 (1983). For a tribute to Justice Hopkins's legal writing, see Margaret Mary Fitzpatrick & John J. Sherlock, *Portrait of a Judge as an Artist (with Apologies to James Joyce)*, 3 Pace L. Rev. 495 (1983).
4. *Berkey v. Third Ave. Ry. Co.*, 244 N.Y. 84, 94 (1926). For some independent thoughts about metaphors in legal writing, see Haig Bosmajian, Metaphors and Reason in Judicial Opinions (1992); Bernard J. Hibbitts, *Making Sense of Metaphors: Visuality, Aurality, and the Reconfiguration of American Legal Discourse*, 16 Cardozo L. Rev. 229, 235 (1994).
5. *Pavlicic v. Vogtsberger*, 390 Pa. 502, 507, 136 A.2d 127, 130 (1957) (Musmanno, J.).
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GERALD LEBOVITS is a judge of the New York City Civil Court, Housing Part, currently assigned to Brooklyn and Staten Island. An adjunct professor and the Moot Court faculty advisor at New York Law School, he has written numerous articles and *Advanced Judicial Opinion Writing*, a handbook for New York State's trial and appellate courts, from which this column is adapted. His e-mail address is Gerald.Lebovits@law.com.

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THE LEGAL WRITER

Not Mere Rhetoric: Metaphors and Similes

BY GERALD LEBOVITS

Good legal writers apply law and fact in an organized, grammatical way. But the best legal writers use occasional rhetorical flourishes, tropes from the figures of speech learned in high school. To go to the head of your class, add metaphors and similes to your prose.

Experienced writers embrace metaphors, which implicitly compare unlike things that have something in common. The law is filled with effective, memorable metaphors that make abstract concepts concrete.

Metaphors have their place in legal writing: ambits, four corners of the record, marketplace of ideas, on its face, penumbras, safe harbors, sliding scales, slippery slopes, streams of commerce, zones of privacy.

Metaphors add color to legal writing: black-letter law, blue-sky laws, bright lines, color of title, golden parachutes, greenmail, grey-market goods, red lining, silver-platter doctrine, white knights, yellow-dog contracts.

Metaphors make legal readers sit down and take judicial notice: Covenants "run with the land," litigants have "standing," lawyers "move" and "advance" arguments. Not surprisingly, whether on a "high" court or a "lower" court, judges "sit." With all that movement, thank goodness lawyers have long-arm statutes to help them stay within the reach of the law and to cite cases on all fours without going on fishing expeditions or opening the floodgates of litigation.

Perhaps the most famous metaphor in the law comes from the New York Court of Appeals in *Palsgraf v. Long Island Railroad Co.*,[1] in which Judge Andrews analogized flowing water to the doctrine of proximate cause:

> The spring, starting on its journey, is joined by tributary after tributary. The river, reaching the ocean, comes from a hundred sources. No man may say whence any drop of water is derived. Yet for a time distinction may be possible. Into the clear creek, brown swamp water flows from the left. Later, from the right comes water stained by its clay bed. The three may remain for a space, sharply divided. But at last, inevitably no trace of separation remains. They are so commingled that all distinction is lost.

Metaphors are richest when they are subtle and unexpected. Metaphors are poorest when they are corny, vague, intricate, lengthy, unoriginal, forced, trivialized, or overused.

Never mix your drinks or your metaphors. Mixed metaphors are like not letting your right hand know that it is lucky to break a leg. Mixed metaphors result from stringing clichés. If you do not use clichés, you will not mix metaphors.

Aristotle, the master of metaphors, explained that "metaphors . . . must not be far-fetched; rather, we must draw them from kindred and similar things; the kinship must be seen the moment the words are uttered."[2] New York's Second Department Justice Hopkins agreed that metaphors should not be arcane: "Metaphors illuminate, yet may also be delusive. Be sure that they truly fit the pattern illustrated, and are not so remote in their bearing that the reader loses his way in underbrush."[3]

Do not rely on metaphors to substitute for independent thought. As Judge Cardozo (as he then was) explained, "Metaphors in the law must be narrowly watched, for starting as devices to liberate thought, they end up often enslaving it."[4]

Do not use inappropriate tone in metaphors. Consider this extended, self-indulgent metaphor, from the Supreme Court of Pennsylvania:

> A gift given by a man to a woman on condition that she embark on the sea of matrimony with him is no different from a gift based on the condition that the donee sail on any other sea. If, after receiving the provisional gift, the donee refuses to leave the harbor,—if the anchor of contractual performance sticks in the sands of irresolution and procrastination—the gift must be restored to the donor. *A fortiori* would this be true when the donee not only refuses to sail with the donor, but, on the contrary, walks up the gangplank of another ship arm in arm with the donor's rival.[5]

Metaphors make legal readers sit down and take judicial notice.

How 'bout them Yankees? If you want to hit a home run—and avoid striking out—use metaphors accurately.[6] A favorite baseball metaphor comes from the federal court in Oregon:[7]

> As I read the June 23 opinion of the Court of Appeals, the plaintiffs assert eight claims of error in my ruling. The Court found reversible error in five, but affirmed on three. In baseball, a batting average of .375 is enviable indeed. Judiciary wise, such an average sends one to the showers in a hurry.

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