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What Can a Competitor Do?

The Dividing Line Between Permissible Competitive Behavior and Tortious Interference With Contract

by Glen Banks

Also in this Issue

NEW YORK STATE BAR ASSOCIATION
Journal

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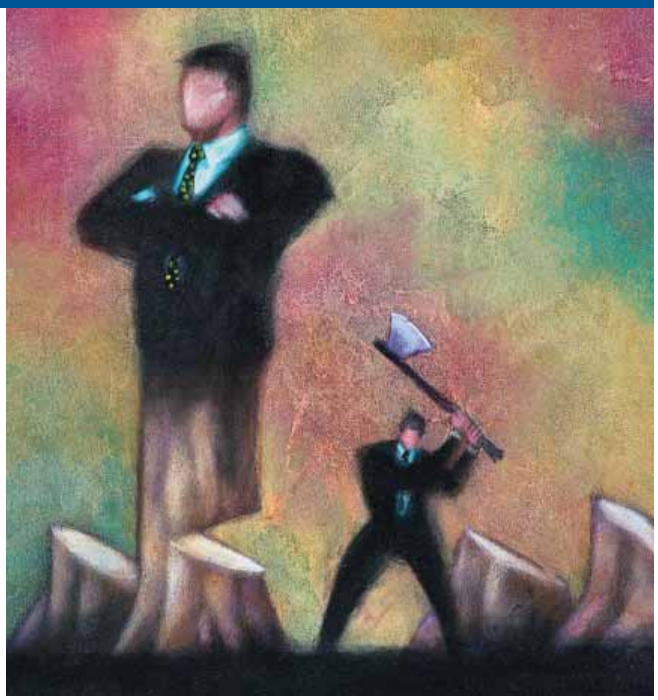

DEPARTMENTS

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KATHRYN GRANT MADIGAN

Join the Voices for Recovery

He was just a couple of days sober, barely holding on. Fortunately he called NYSBA's Lawyer Assistance Program (LAP) hotline. Our LAP Director, Pat Spataro, put out a call for help to local volunteers and within hours, 10 lawyers had offered to call him, meet with him, take him to a 12-Step meeting, whatever it took to help him through those early, tenuous days and weeks of sobriety. This story of hope, and recovery, is what motivates the hundreds of LAP volunteer judges and attorneys, many of whom have triumphed over their own problems with substance abuse, gambling, depression or other mental health issues, or debilitating stress.

Lawyers, by nature, can be highly competitive, driven, A-type personalities, and more susceptible to the addictive behaviors and depression that often accompany overpowering stress. The statistics are grim. Attorneys suffer from alcoholism and depression at twice the rate of the general population. An ABA study of attorney disciplinary cases in New York and California found that up to 70% involved alcoholism. In its 2005 and 2006 annual reports, the New York Lawyers' Fund for Client Protection reported that alcohol and substance dependency is a "significant contributing factor" in client losses. Other causes are mental illness and gambling. In addition, one out of every four lawyers suffers from stress; and, according to a landmark Johns Hopkins study, lawyers rank first in depression among 105 occupations. Most disturbingly, a disproportionate number of our colleagues commit suicide each year. And it's not just lawyers and judges. Our law school and college populations show a sharp rise in binge drinking, prescription drug abuse, Internet gambling and depression. The good news? All these problems are treatable.

Since 1990, the State Bar's Lawyer Assistance Program has provided career- and life-saving services to attorneys, judges and law students who are affected by alcohol and drug abuse, overwhelming stress, depression and other mental health issues, and the health, family and work-related problems that often result. LAP also provides collateral services to family members. NYSBA's LAP is guided by the dedicated volunteers serving on our Lawyer Assistance Committee under the inspirational leadership of its Chair, the Honorable Sallie Kraus. This past year, with financial support from the New York State Lawyer Assistance Trust, we hired a LAP Coordinator for the Fourth Department, Paul Curtin. He has already made an enduring difference by strengthening the local Lawyers Helping Lawyers (LHL) Committees, including regionalization of programs among the smaller bar associations. Paul and Al Lampert, the newly hired Second Department Coordinator, joined an already committed statewide team of lawyer assistance professionals.

In April, I had the pleasure of hosting a regional LHL meeting at Levene Gouldin & Thompson, which brought together bar association leaders and staff in the Southern Tier. Our goal was to plant the seed for a coordinated, regional effort to promote lawyer wellness services by establishing a regional LAP Committee. As a result, the Broome County Bar Association revitalized its LAP, and both Broome and Chemung Counties now have a solid and growing connection with the vibrant LHL program in Tompkins County.

Statewide collaboration is contagious. In Erie County, Dan Lukasik, an attorney with depression, created a Web site specifically for attorneys – www.lawyerswithdepression.com. Dan also started a support group for attorneys with depression. This support group initiative is being replicated this fall in Rochester and Albany. These are shining examples among many of the growth of peer-assisted volunteer programs across the state.

In May, the annual NYSBA LAP Retreat and Wellness Weekend was held in Silver Bay, Lake George. As an avid work/life balance and wellness advocate, I looked forward to participating in the retreat, but I did not expect it to be life altering, which is the only way to describe the experience. Together with new and old friends and colleagues in an idyllic setting, we honored Hon. A. Gail Prudenti for her unstinting support and involvement with Lawyer Assistance Programs, particularly in the First and Second Departments. Another LAP champion

KATHRYN GRANT MADIGAN can be reached on her blog at http://nysbar.com/blogs/president.

Barbara F. Smith, Executive Director of the Lawyer Assistance Trust, was presented with the first ever Extraordinary Service Award.

We shared with open hearts powerful stories told by those among us, of their darkest moments, their personal and often miraculous paths to recovery. As LAP Director Pat Spataro noted afterward, "we re-emerged changed forever" by the stories, which were a "gift to all of us." As I drove down the Northway the next morning, reflecting on that profound and transcendent experience, I knew that I too must become a voice for healing and the spirit of recovery.

Whatever impairment or problem you, a family member or colleague may be confronting today, please know that you, and they, are not alone. Resist the temptation to suffer alone in silence or to ignore a colleague who shows signs of struggling with an addiction, depression or mental health issue. Let us help you help yourself. Your confidentiality is guaranteed and all services are free. Our staff and volunteers are waiting to help you on your path to healing and recovery. Call 800-255-0569 or connect to our Web site www.nysba.org/lap. ■

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FROM THE NYSBA BOOKSTORE

October 2007

Attorney Escrow Accounts, Second Edition

The Second Edition offers comprehensive coverage of the most common situations involving client funds and clearly discusses the legal and ethical issues encountered.
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This classic text provides detailed guidance in the field of debt collections and enforcement of money judgments. Completely updated with the cumulative supplement.
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Construction Site Personal Injury Litigation — New York Labor Law §§ 200, 240(1), 241(6)

Perhaps no single scheme of statutory causes of action has initiated more debate. This text provides a road map through this at-times confusing area of law. Includes a summary of key case developments.
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This detailed text covers all aspects of depositions. Topics include pre-trial discovery schedules, appropriate and inappropriate behavior at depositions, and motions for protective orders.
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This manual contains a collection of the forms and protocols that provide the necessary predicate or foundation questions for the introduction of common forms of evidence and the examination of witnesses.
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Legal Manual for New York Physicians, Second Edition

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NEW!

NYS Physician's HIPAA Privacy Manual

Designed to be a hands-on tool for health care providers and their legal counsel, this new publication provides guidance for a physician's office to respond to routine, everyday inquiries about protected health information.
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Real Estate Titles, Third Edition

An all-time bestseller, this 2007 Edition is edited by James M. Pedowitz, Esq., a nationally renowned expert in real estate law and title insurance, and authored by some of the most distinguished practitioners in the field. This edition, consisting of 27 chapters, is an essential guide to the many complex subjects surrounding real estate law. Includes the new ALTA policies and TIRSA endorsements.
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A comprehensive reference that covers the myriad legal concerns of people with disabilities. It is the ideal reference for those who want a "one-stop" source for a thorough overview of the legal framework affecting individuals with disabilities.
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This landmark text is the leading reference on public sector labor and employment law in New York State. All practitioners will benefit from the comprehensive coverage of this book, whether they represent employees, unions or management. Practitioners new to the field, as well as the nonattorney, will benefit from the book's clear, well-organized coverage of what can be a very complex area of law.

December

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NYSBA CLE Partial Schedule of Fall Programs

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The New York State Bar Association Has Been Certified by the New York State Continuing Legal Education Board as an Accredited Provider of Continuing Legal Education in the State of New York.

Update 2007
Live Sessions
October 5 Syracuse
October 19 New York City
+Video Replays (do not qualify for MCLE credits for newly admitted attorneys)
October 24 Binghamton
October 25 Utica
October 30 Albany; Buffalo
November 1 Rochester
November 7 Ithaca; Plattsburgh; Saratoga
November 8 Jamestown; Suffern
November 15 Uniondale, LI; Tarrytown
November 16 Canton
November 28 Poughkeepsie
November 30 Loch Sheldrake; Watertown

Practical Skills: Basic Matrimonial Practice
October 10 Albany; Buffalo; Melville, LI; New York City; Rochester; Syracuse; Westchester

The Lawyer as Employer (half-day program)
October 10 New York City
October 17 Uniondale, LI

+Second Corporate Counsel Institute (two-day program)
October 11–12 New York City

Handling a No-Fault Case: The Fundamentals and Strategies for Representing Plaintiffs and Defendants
October 11 New York City
October 12 Albany
October 18 Syracuse
October 19 Melville, LI
November 1 Buffalo

Handling the Failure to Diagnose Breast Cancer Medical Malpractice Case
October 12 New York City

Construction Site Accidents: The Law and the Trial
October 12 Uniondale, LI
October 19 Syracuse
November 15 New York City
November 16 Buffalo

+Real Estate Titles
October 12 New York City
October 26 Tarrytown
November 1 Albany
November 2 Melville, LI
November 14 Rochester

A Day in Discovery – Win Your Case Before Trial with Jim McElhaney
IMPORTANT NOTE: CLE Seminar Coupons and Complimentary Passes CANNOT be used for this program.
October 16 Syracuse
October 17 Buffalo
November 7 Melville, LI
November 8 New York City

Risk Management for Attorneys – Don't Make Malpractice Your Nightmare (half-day program)
October 16 Buffalo
November 2 New York City
November 13 Uniondale, LI

+ Does not qualify as a basic level course and, therefore, cannot be used by newly admitted attorneys for New York MCLE credit.

Prosecuting and Defending Medical Malpractice Claims
October 17 Syracuse
October 19 Buffalo
October 26 Albany
November 1 Plainview, LI
November 2 Rochester
November 7 New York City

A Primer on Human Subject Research; Federal and State Law
October 19 New York City

Practical Skills: Introduction to Estate Planning
October 23 Albany; Buffalo; Melville, LI; New York City; Rochester; Syracuse; Westchester

New York Appellate Practice
October 25 Rochester
November 2 Tarrytown
November 8 Hauppauge, LI
November 28 Albany
December 7 New York City

+Ninth Annual Institute on Public Utility Law
October 26 Albany

+New York's Fault Divorce Law at Age 40: Pleading and Proving Your Grounds Case (half-day program)
October 26 Buffalo
November 2 Albany
November 16 Melville, LI
December 7 Syracuse
December 14 New York City

Special Education Law Update 2007
October 26 Buffalo
November 16 New York City
November 28 Albany

+At the Ramparts: Challenges in Representing and Litigating with Public Companies in the Post-DURA/IPO/Sarbanes-Oxley Environment
October 30 New York City

Preparing and Drafting Organizational Documents for New York LLCs and Corporations (half-day program)
November 7 Rochester
November 16 Albany
December 7 Uniondale, LI
December 11 New York City

+Fifth Annual Sophisticated Trusts and Estates Institute
IMPORTANT NOTE: CLE Seminar Coupons and Complimentary Passes CANNOT be used for this program. (two-day program)
November 8–9 New York City

Practical Skills: Purchases and Sales of Homes
November 13 Albany; Buffalo; Hauppauge, LI; New York City; Rochester; Syracuse; Westchester

Engaging and Working with Investigative Consultants (half-day program)
November 14 New York City

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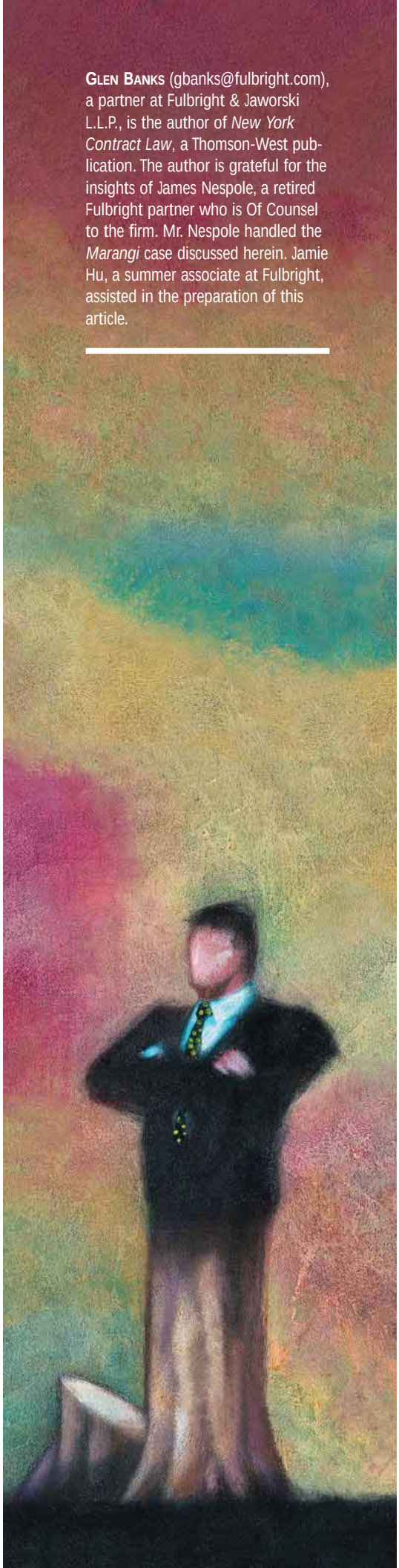
What Can a Competitor Do?

The Dividing Line Between Permissible Competitive Behavior and Tortious Interference With Contract

By Glen Banks

When a contract is breached, the resulting litigation may involve more than the contracting parties. The non-breaching party may bring a claim for tortious interference with contract against a third party whose actions allegedly induced the breach.

Glen Banks (gbanks@fulbright.com), a partner at Fulbright & Jaworski L.L.P., is the author of *New York Contract Law*, a Thomson-West publication. The author is grateful for the insights of James Nespole, a retired Fulbright partner who is Of Counsel to the firm. Mr. Nespole handled the *Marangi* case discussed herein. Jamie Hu, a summer associate at Fulbright, assisted in the preparation of this article.



As the Second Circuit has noted, economists believe that breaches of contract that are efficient and wealth-enhancing should be encouraged and that such "efficient breaches" occur when the breaching party will still profit after paying damages to compensate the other party to the contract for its expectation interest.[1] Efficient breach is consistent with a contract party's freedom to choose whether to perform or breach its contract.[2] Because, at least in theory, this kind of breach makes society better off, the law does not treat it as disfavored.[3] As one Circuit Court of Appeals has stated, the "whole notion of an 'efficient breach' is that a party *should* abrogate its contractual responsibilities if a more profitable opportunity comes along."[4]

The New York Court of Appeals has noted that a claim against a competitor is a "subset" of the "amorphous" law of tortious interference and "presents a wide range of possibilities."[5] An interesting question arises when a party breaches a contract because it has been offered better terms by a competitor of the non-breaching party. In such instance, an arguably efficient breach has occurred in that the breaching party has exercised its right to breach and pay damages in the belief that it will be better off doing business on the terms offered by a competitor. In this situation, which economists would view as beneficial and wealth-enhancing, should a court impose liability upon the competitor for tortious interference with contract?

In *White Plains Coat & Apron Co. v. Cintas Corp.*,[6] the Court of Appeals considered the intersection of society's interest in the benefits that result from robust competition and the protection of contract rights. The Court was asked to decide whether a company's generalized economic interest in soliciting business for profit provided it with a defense to a claim for tortious interference with contract arising from its solicitation of business from customers with whom the company had no prior relationship, and who were under contract with a competitor. The Court ruled that the company did not have an economic interest defense to the tortious interference claim.

The Court's opinion, however, left uncertain the line between permissible conduct by a company seeking business and conduct that would tortiously interfere with a competitor's contract. The language of the opinion could be used to argue that the Court retreated from the bright-line position that tortious interference occurs when a breach of contract results from a company soliciting business by offering better terms to customers it knows to be under contract to a competitor.

This article will first give an overview of New York law on tortious interference with contract and the economic interest defense to such a claim. It will then discuss the *White Plains Coat* case. Finally, it will address the import of the opinion of the Court of Appeals in that case.

Tortious Interference With Contract

A tortious interference with contract claim has its roots in the 1853 English decision in *Lumley v. Gye*,[7] where the court held actionable the enticement of a well-known opera singer to refuse to perform an engagement. It took some time, however, for the claim to be recognized by New York courts.

In its 1872 decision in *Ashley v. Dixon*, the Court of Appeals noted that if A contracted to sell land to B, absent fraudulent conduct C was free to induce A to violate the contract and sell the land to C.[8] The Court stated that although "moral law" would obligate C to abstain from interference with the contract, this moral obligation "is one of those imperfect obligations which the law, as administered in our courts, does not undertake to enforce."[9]

In 1918, in *S.C. Posner Co. v. Jackson*, the Court stated that *Ashley* should be limited to its particular facts because once the *Ashley* Court concluded the plaintiff had not presented evidence that the defendant had instigated the breach, there was no need for the Court to engage in further discussion.[10] The *Posner* case involved a defendant's alleged willful and malicious acts to interfere with a contract between a plaintiff and one of the plaintiff's employees. The Court ruled that if a person knowingly and intentionally interfered with the express contract rights of an employer, with the purpose and intent of injuring it, the person would be liable for injury that his or her actions caused the employer.

Two years later, in *Lamb v. S. Cheney & Son*,[11] the Court adopted a general rule that if one "maliciously" interferes with a contract between the two parties, and induces one of them to breach the contract, to the injury of the other, the injured party can maintain an action against the interfering party. The Court considered the word "malicious" as not meaning actual malice or ill will, but the intentional doing of a wrongful act without legal justification. The Court viewed the gist of a tortious interference claim as not being an intent to injure the non-breaching party, but to interfere, without justification, and with knowledge thereof, with that party's contractual rights.

In *Campbell v. Gates*, the Court noted that if A and B have a contract and C "intentionally and knowingly, and without reasonable justification or excuse" causes B to breach the contract, C would be liable to A for damages caused by the breach.[12] The Court continued to apply that standard in ruling that tortious interference with contract occurs when the defendant, with knowledge of an existing valid contract between the plaintiff and a third party, acts intentionally and "without justification" to procure the third party's breach of that contract.[13] The defendant's actions affecting the contract "must be intentional, not merely negligent or incidental to some other, lawful, purpose."[14]

Some Second Circuit panels have viewed a tortious interference with contract claim under New York law as requiring a showing that a third party, with knowledge of a valid and existing contract, "intentionally *and improperly* procured its breach."[15] This language was used in the Second Circuit's decision in *Finley v. Giacobbe*,[16] where the court cited the decision of the N.Y. Court of Appeals in *Israel v. Wood Dolson Co.*[17] and that of the First Department in *Kaminski v. United Parcel Service*.[18] Both these cases, however, require only that a defendant intentionally acted to procure the breach. There was no requirement that the plaintiff show the defendant acted improperly.

This moral obligation "is one of those imperfect obligations which the law does not undertake to enforce."

The language in *Finley* differs from that articulated in other Second Circuit cases where the court has stated that a plaintiff must show the "defendant's knowing and intentional interference with the contract without reasonable justification."[19] The Second Circuit has not explained the difference, if any, between showing a defendant's actions were "without justification" and that a defendant acted "improperly."

Guard-Life and the Restatement (Second)

The difference in language between "without justification" and "improperly" is due to the language in the Restatement (Second) of Torts. Before its issuance in 1977, courts had noted that a liability for tortious interference with contract would be imposed when a defendant acted "without justification." In contrast, Restatement (Second) states that the tort occurs when the defendant "intentionally and improperly interferes" with a contract.

The Court of Appeals in its 1980 decision in *Guard-Life Corp. v. S. Parker Hardware Manufacturing Corp.* noted that the law in tortious interference with contracts was still in its formative stage and had not yet "fully congealed."[20] The Court discussed the Restatement (Second), noting:

> The American Law Institute in the Restatement of the Law of Torts 2d, adopted May, 1977, has stated the fundamental principle: "One who intentionally and improperly interferes with the performance of a contract (except a contract to marry) between another and a third person by inducing or otherwise causing the third person not to perform the contract, is subject to liability to the

other for the pecuniary loss resulting to the other from the failure of the third person to perform the contract." (§ 766.) The keystone of the statement is the adverb "improperly" a term selected in preference to the phrase "without justification" appearing frequently in judicial decisions and giving rise to questions of burden of proof the definition of which is inconstant and mutable, drawing its substance from the circumstances of the particular situation at hand. Section 767 of the Restatement sets out several factors for consideration in determining whether an intentional interference with a contract is "improper," accompanied by the observation that "[t]he issue in each case is whether the interference is improper or not under the circumstances; whether, upon a consideration of the relative significance of the factors involved, the conduct should be permitted without liability, despite its effect of harm to another. The decision therefore depends upon a judgment and choice of values in each situation" (Comment b). Included among the factors to be considered are the nature of the conduct of the person who interferes (a chief factor in determining whether conduct is improper), the interest of the party being interfered with (whether in an enforceable contract or in a contract voidable and thus unenforceable or terminable at will), [Fn.1] and the relationship between the parties [Fn. 2].

[fn. 1] The Restatement recognizes that these two types of contracts present similar situations. In each there is a valid and subsisting relation until opposition to enforcement is raised or termination is effected (Restatement, Torts 2d § 766, Comments f, g).

[fn. 2] Other factors include the motive and interests sought to be advanced by the one who interferes, the social interests in protecting the freedom of action of that person as well as the contractual interests of the party interfered with, and the proximity or remoteness to the interference of the conduct complained of.[21]

In *Guard-Life*, the Court noted that New York law provided greater protection to an interest in an existing contract (as to which respect for individual contract rights outweighs the public benefit to be derived from unfettered competition) than to the less substantive, more speculative interests in a prospective relationship (as to which liability will be imposed only on proof of more culpable conduct on the part of the interferer).[22] Consistent with this distinction, the Court noted that when a contract is not for a definite term – *e.g.*, when it is terminable at will – there can be no claim for tortious interference with contract, but a claim for tortious interference with economic relations may be asserted if the alleged interfering party used wrongful means to procure the termination.[23]

In *NBT Bancorp Inc. v. Fleet/Norstar Financial Group, Inc.*,[24] the Court elaborated on the distinction between existing contracts and prospective relations, noting that a party can be liable for tortious interference with contract even if its behavior was entirely lawful; but the party could be liable for tortious interference with prospective relations only if it used wrongful means to cause a third party not to enter into an agreement with the plaintiff. In both *Guard-Life* and *NBT*, the Court viewed "wrongful means" as conduct such as physical violence, fraud or misrepresentation, civil suits and criminal prosecutions, and some degree of economic pressure, but not persuasion alone, even if knowingly directed at having a third party not deal with the plaintiff.[25]

The *Guard-Life* Court stated that "status as a competitor does not protect the interferer from the consequences of his interference with an existing contract."[26] The Court believed that with respect to a contract for a definite term, persuasion to breach alone, as by an offer of better terms, had been sufficient to impose liability on one who thereby interferes with performance.[27] For this point, the Court cited *Gold Medal Farms, Inc. v. Rutland County Co-op Creamery, Inc.*[28] and *Gonzales v. Reichenthaler.*[29]

In *Gold Medal*, the plaintiff had a contract to acquire all the milk produced by the defendant Rutland Creamery. The plaintiff alleged that Vermont Milk & Cream Company, a competitor, tortiously interfered with its contract with Rutland. In response, Vermont argued that to prevail on the tortious interference claim, the plaintiff had to show some additional wrong, such as actual malice, fraud or deceit, independent of the actual inducement of the breach. The court rejected this contention, saying that it would be sufficient for the plaintiff to show that Vermont, with actual knowledge of the existence of the contract between Rutland and the plaintiff, "intentionally made an offer of better terms to Rutland with the intent of persuading it to breach its contract."[30] The court believed that the plaintiff's tortious interference claim could proceed to trial because there was sufficient evidence to allow the trier of fact to conclude that Vermont "with full knowledge of the facts, intentionally made a better offer to Rutland with the intent of bringing about a breach of the [plaintiff's] contract."[31] The plaintiff also had advanced evidence that shortly after Rutland breached its contract, Vermont loaned Rutland a very substantial sum, without interest, which was to be repaid from "premiums" over and above the contract price Vermont paid for Rutland's milk.

The *Gold Medal* decision is consistent with the Fourth Department's earlier decision in *Elk Street Market Corp. v. Rothenberg*.[32] There, the court stated: "It is fundamental that no person has a right to persuade a party to a binding contract to repudiate, abandon, or break it."[33] *Gold Medal* has been followed by the First Department, which has held that a tortious interference claim lies if a defendant, with knowledge of the plaintiff's contract with a third party, intentionally makes an offer of better terms to the third party, with the intent of persuading it to breach its contract with the plaintiff.[34]

In *Gonzales v. Reichenthaler*, the plaintiff leased an arcade game from defendant Kentucky Derby Co., the contract provided that Kentucky Derby would not provide the game to other parties for use at Coney Island. The plaintiff claimed that with knowledge of this contract, defendant Reichenthaler persuaded Kentucky Derby to provide him with a similar game for use at Coney Island.

The Second Department noted that there was a "serious question of law" as to whether Reichenthaler could be held liable for inducing Kentucky Derby to breach its contract with the plaintiff.[35] Relying upon *Posner* and *Lamb*, the court believed that such a claim could be asserted against Reichenthaler. Without addressing the tortious interference issue, the Court of Appeals affirmed the Second Department's decision.[36]

The "Economic Interest" Defense

Procuring the breach of a contract in the exercise of an equal or superior right justifies what would otherwise be an actionable wrong.[37] A defendant acts with justification when it acts to protect its "economic interest."[38]

The economic interest defense has its roots in *Felsen v. Sol Café Manufacturing Corp.*,[39] a case decided prior to the promulgation of the Restatement (Second) of Torts. In that case, plaintiff Felsen was employed by defendant Sol Café pursuant to the terms of a written contract; defendant Chock Full O'Nuts owned all the stock of Sol Café. After Sol Café terminated Felsen's contract, he sued for breach of contract and asserted a claim against Chock Full O'Nuts for tortious interference with his employment contract. The jury returned a verdict for Felsen, finding that Chock Full O'Nuts had intentionally interfered with his employment contract without just cause or excuse. The Court of Appeals ruled that the tortious interference claim should have been dismissed because Chock Full O'Nuts, as the sole stockholder of Sol Café, had an existing economic interest in the affairs of Sol Café and protection of that interest permitted it to take action with respect to the plaintiff's employment with Sol Café. *Felsen* established economic interest as a defense to a claim for tortious interference with contract in that the Court recognized that a defendant was justified in taking action if it had a significant ownership interest in the breaching party, such as where a parent-subsidiary relationship exists.[40]

The Court also has recognized that the defense would cover corporate agents, such as directors, accused of tortiously interfering with the corporation's contracts.[41] The imposition of liability in spite of a defense of economic interest requires a showing of either malice on the one hand, or fraudulent or illegal means on the other.[42]

The defense of justification is not automatically applicable simply because the defendant has an economic interest.[43] The defendant must show that its allegedly interfering actions were taken to protect that interest.[44]

Courts have found, in a wide array of circumstances, that a defendant has an economic interest defense. Decisions in recent years have found:

- A creditor may act to protect its secured interest;[45]
- A franchisor who is a creditor of a franchisee may take action with respect to the franchisee's loan agreements with a financial institution;[46]
- A controlling (83% interest) shareholder may act with respect to the controlled corporation's contracts;[47]
- A party may act to protect its contractual rights;[48]
- A defendant who has a managerial contract with a third party may have an economic interest defense to a claim that it caused the third party to breach a contract;[49]
- A copyright owner may protect its copyright by alerting a third party that the copyright is being infringed;[50]
- A defendant may take action with respect to the contracts of a company that the defendant has a contract right to acquire;[51]
- A corporation may seek to prohibit its major shareholders and directors from dealing with an executive it had terminated until after disputes between the corporation and the executive have been resolved;[52]
- A corporation may take action with respect to the contracts of an affiliate sister company;[53]
- A party to litigation may advise others of its adjudicated rights;[54] and
- A party may take reasonable and appropriate actions to correct an error that it made.[55]

The defense, however, had not been extended to a company that would attempt to further its economic interest by persuading customers under contract with a competitor to breach their contract and give their business to the company. The Court of Appeals has noted that a party could be liable for damages if its lawful behavior caused a third party to breach its contract with a plaintiff.[56] In the same opinion, the Court also noted that scholarly commentary supported the contrary position – that "lawful competition" should not give rise to liability for tortious interference.[57] In the *White Plains Coat* case, the Court was asked to address whether a company had an economic interest defense that protected it from a claim for tortious interference with contract arising from its solicitation of business from customers it knew were under contract to a competitor and with whom it had no prior relationship.

The Facts in *White Plains Coat*

White Plains Coat and Apron Co., Inc. (WP) rented napkins, tablecloths and other laundered items to restaurants and other businesses. WP had written contracts with its customers obligating the customer, during the term of the agreement, to rent exclusively from WP, which agreed to supply the customers' needs.

Cintas Corp. ("Cintas"), a competitor of WP, allegedly induced dozens of customers it knew to have contracts with WP to breach their agreements with WP and enter into agreements with Cintas. WP contended that Cintas trained its sales representatives how to convince WP's customers to abandon prematurely their agreements with WP and give their business to Cintas.

WP sent a letter to Cintas that identified the customers that WP had under contract and demanded that Cintas cease its practice of soliciting business from these customers. In response, Cintas visited many of these customers and attempted to have them certify that Cintas had not infringed existing contracts the customer may have had with other providers. Such a certification had been included in agreements Cintas had entered into with its customers.

WP sued Cintas in the Southern District of New York alleging, *inter alia*, tortious interference with contract. At the close of discovery, Cintas moved for summary judgment.

The District Court's Decision

The District Court's Judge Charles L. Brieant granted summary judgment, dismissing WP's tortious interference claim. It reasoned that Cintas had a legitimate economic interest as a competitor to seek business from WP's customers. It believed that the interest of Cintas to solicit business and make a profit provided a defense to the tortious interference claim. The court ruled that the tortious interference claim failed because the plaintiff failed to rebut the defendant's economic interest defense by advancing evidence that the defendant's actions were malicious or illegal.

WP moved for reconsideration, arguing that the economic interest defense did not apply because Cintas had no economic relationship with the customers it solicited. The court adhered to its ruling, believing that the defense was not limited to those situations where the party accused of tortious interference had an interest in the breaching party.

WP appealed the dismissal of its claim. It argued that the court erred in extending the economic interest defense to protect the general economic interest of a competitor to solicit business and make a profit.

The Second Circuit's Opinion

The Second Circuit noted that under New York law when a party procures the breach of a contract in the exercise of an equal or superior right, it acts with just cause and has a justification defense to what would otherwise be an actionable wrong.[58] The court believed that while the consequences of triggering the economic interest defense were relatively clear, the type of economic interest that would trigger the defense was not. It observed that courts had applied the defense in an inconsistent manner and

The Court of Appeals's opinion raises three points.

that precisely what constituted a sufficient economic interest for the purpose of relying upon the defense had not been established. The court noted that there was authority to support the proposition that when a competitor, with knowledge of the contract, takes an active part in persuading the party under contract to breach it by offering better terms or other incentives, it unjustifiably interferes with the contract.

The court viewed the question of whether a company's general business interest in luring customers from a competitor triggered the economic interest defense as an important recurring issue that potentially touched on a wide range of commercial behavior. It believed New York law did not clearly identify the type of economic interest that could be asserted as a defense to a tortious interference claim. Accordingly, it certified to the Court of Appeals the issue of whether a competitor had an economic interest defense to a tortious interference with contract claim. In doing so, the court noted the underlying competing policy issues of protecting WP's valid contracts with its customers and in allowing Cintas to engage in robust competition. Striking the appropriate balance between the protection of contracts and the protection of competition was a task best left to the Court of Appeals. The Second Circuit certified to the Court the question of whether a generalized economic interest in soliciting business for profit constitutes a defense to a claim of tortious interference with an existing contract for an alleged tortfeasor that had no previous economic relationship with the breaching party.

The Court of Appeals's Ruling

The Court of Appeals answered the certified question in the negative. In addressing the issue, it acknowledged that New York law on tortious interference had generated a spate of decisions with somewhat varying views, as courts struggled to strike a balance between protection of enforceable contracts, which lends stability and predictability to business dealings, and promotion of robust competition in the marketplace.

The Court stated that the plaintiff asserting a claim for tortious interference must show (1) the existence of its valid contract with a third party, (2) the defendant's knowledge of that contract, (3) the "defendant's *intentional and improper procuring* of a breach" and (4) damages.[59] In "response" to such a claim, the defendant "may raise the economic interest defense."[60] The defense, said the Court, applies when a party acts to protect its own legal or financial stake in the breaching party's business such as where a defendant (1) was the corporate parent or held an interest in the breaching party, (2) was the breaching party's creditor, or (3) had a managerial contract with the breaching party.

Cintas could not assert an economic interest defense, said the Court. Its mere status as WP's competitor did not constitute a legal or financial stake in the breaching party's business that permitted it to induce a breach of contract. The Court noted that New York's Pattern Jury Instructions states:

> When the defendant is simply a competitor of the plaintiff seeking prospective customers and plaintiff has a customer under contract for a definite period, defendant's interest is not equal to that of plaintiff and will not justify defendant's inducing the customer to breach the existing contract.[61]

The Court, however, concluded its opinion by noting protection of existing contractual relationships does not negate a competitor's right to solicit business. What is actionable is the "*improper* inducement of a third party to breach its contract."[62] Citing comment m to the Restatement (Second) of Torts § 766, the Court stated that regular advertising and solicitation of business in the normal course would not constitute such improper inducement. Instead, a competitor's liability would depend on a showing that it acted improperly, in that its conduct exceeded a minimum level of ethical behavior in the marketplace.

The Import of *White Plains Coat*

The Court of Appeals's opinion raises three points that are likely to impact future litigation involving tortious interference claims. The first concerns the pleading standard for a tortious interference with contract claim. The Court quoted Restatement (Second) of Torts § 766 for what it called the "familiar proposition" that liability for tortious interference may be imposed upon a defendant who "intentionally and improperly interferes" with a contract. The "plaintiff must show," *inter alia*, the defendant's "improper procuring of a breach." In support of its recitation of the elements of a tortious interference claim, the Court cited three cases. None of the three cases, however, uses the term "improper." In *Lama Holding v. Smith Barney, Inc.*,[63] the Court ruled "intentional procurement" of the breach "without justification" was a necessary element of a tortious interference claim. In *NBT Bancorp*,[64] the Court stated that a defendant's "deliberate interference," which results in a breach, would be actionable. In *Israel v. Wood Dolson Co.*,[65] the Court said a defendant's "intentional procuring of the breach" would support a tortious interference claim.

The Court's recitation of what the "plaintiff must show" should not be read as affecting the pleading standard for a tortious interference with contract claim. A plaintiff should be allowed to generally allege that the defendant's actions were improper. A court should not require a plaintiff to plead specific facts because such facts might be solely

within the knowledge of the defendant and be unknown to the plaintiff until discovery is completed.

The second point of *White Plains Coat* is the decision's impact upon the burden of proof. Prior decisions have noted that once the plaintiff shows that the defendant's action resulted in a breach, "the burden shifts to the defendant to plead and prove justification."[66] This is consistent with the introductory notes to the portion of the Restatement (Second) of Torts dealing with tortious interference claims.

If economic interest or status as a competitor is merely a factor to be taken into account in determining whether the plaintiff has met the burden of proving that the defendant acted improperly, then arguably there should be no shifting of the burden to the defendant to prove that its actions were justified or fell within the economic interest defense. Economic interest might no longer be a defense to a tortious interference with contract claim but, rather, a factor to be taken into account in determining whether a plaintiff has met its burden of proving that the defendant acted improperly.

A balance may be struck between the protection of contract rights and the promotion of robust competition by shifting the burden of production in a manner similar to that employed in civil rights cases.[67] A plaintiff's presentation of evidence that the defendant, with knowledge of the contract, intentionally took action that resulted in its breach, would shift to the defendant the burden of producing evidence that its actions were justified. If the defendant advances such evidence, the plaintiff would have the burden of persuading the trier of fact that, when all the evidence is considered, a determination should be made that the defendant's actions were improper. If the defendant does not advance such evidence, the plaintiff still has the burden to prove that the defendant's actions were improper.

Imposing upon a plaintiff the burden of proving that a defendant's actions were "improper" would reduce the protection that New York courts have provided to existing contracts, because the general consensus of prior cases was that when a defendant knowingly and intentionally interfered with a contract, in the absence of the defendant advancing evidence that its actions were justified, the trier of fact could conclude such actions were improper. A requirement that the plaintiff show the defendant's actions were "improper" would be a change from the standard reiterated by the Court of Appeals as recently as 2004: "[W]here there is an existing enforceable contract and a defendant's deliberate interference results in a breach of that contract, a plaintiff may recover damages for tortious interference even if defendant was engaged in lawful behavior."[68]

The third point raised by the decision is, what meaning should be given to the language in its last paragraph – that protecting existing contractual relationships does not negate a competitor's right to solicit business, provided the solicitation is not an "improper inducement" to breach an existing contract? This language was not necessary for the Court to answer the certified question and to rule that the economic interest defense did not extend to a competitor. The Court's statement appears at odds with its earlier statement in *Guard-Life* that, with respect to a contract for a definite term, "persuasion to breach alone, as by an offer of better terms has been sufficient to impose liability on one who thereby interferes with performance."[69] The Court's opinion did not address that apparent inconsistency. It also left for another day the question of when soliciting business would constitute "improper inducement" to breach a contract, indicating only that inducement would be improper when the defendant's conduct fell below the minimum level of ethical marketplace behavior. The Court said nothing as to what that minimum level might be.

Guidance for Competitors

A key issue after the *White Plains Coat* decision is what guidance can counsel give to a client who inquires whether it can solicit business from customers under contract with a competitor? Where are courts likely to draw the boundary line between permissible competitive behavior and "improper inducement" to breach a contract? Guidance on this issue can be gleaned from a close examination of the authorities the Court of Appeals cited in the portion of its opinion discussing "improper inducement."

In speaking of "minimum level of ethical behavior," the Court cited Chief Judge Cooke's dissent in *Guard-Life*,[70] and referenced the decision in *V. Marangi Carting Corp. v. Judex Enterprises, Inc.*[71]

Chief Judge Cooke noted that the *raison d'etre* of a tortious interference claim was the ethical precept that one competitor must keep his hands off the contracts of another. He believed that the law of tortious interference did not merely balance protection of contract rights versus freedom to compete, but also took account of society's weighty interest in insuring a minimum level of ethical behavior in the marketplace. His opinion stated that the law long ago decided "that enforcement of certain market morals is a societal interest worthy of protection."[72]

In *Marangi*, upon analysis of the applicable sections of the Restatement (Second) of Torts, the court concluded that the law did not permit a finding of tortious conduct merely upon proof that a defendant "offered better terms" to the plaintiff's customer.

Marangi presented an interesting fact situation. The plaintiff had entered into contracts with its customers, pursuant to which it would pick up and remove the customers' trash. The defendant, a competitor carting company, circulated brochures offering the trash pick-up service at a rate lower than that charged by the plaintiff. The complaint alleged that the brochures were given to

customers that the competitor knew to be under contract with the plaintiff. When a customer breached its contract with the plaintiff and gave its business to the defendant competitor, the plaintiff sued for tortious interference with contract.

The *Marangi* court viewed the issue before it as what, if anything, may a competitor safely communicate to a prospective customer under contract with another. The court believed that not all of a competitor's conduct toward prospective future customers would constitute tortious interference with contractual relations; rather, that a court must ensure that the freedom to conduct normal business is not unduly hampered by the existence of a tortious interference claim. In this regard, it is critically important to clarify the type of "offer of better terms" which is necessary to support a finding of liability.

The court stated that blind adherence to older authority, the *Gold Medal* and *Gonzales* cases cited in *Guard-Life*, should be avoided. It distinguished *Gold Medal* and *Gonzales* on the ground that they concerned conduct toward a particular, targeted competitor in order to induce the breach of a specific contract.

The *Marangi* court, like the Court of Appeals in *White Plains Coat*, believed that it should be guided by § 766 of the Restatement (Second) of Torts and comment m thereto. Section 766 states that liability will be imposed upon a party who "intentionally and improperly" interferes with the performance of a contract. Comment m to that section states that A does not interfere with B's contract with C merely by offering B better terms than C, but would be liable for tortious interference if it advised B that its terms were specially set to allow B to terminate its contract with C, settle C's claim for breach of contract and still make money. The court also noted that the competitor could tortiously interfere with the contract by "sweetening" its offer with "something extra" to induce the customer to breach its existing contract. It recognized that the substantial, interest-free, loan in *Gold Medal* could be viewed as such a sweetener.[73]

In evaluating whether actions improperly interfered with a contract, a court also is likely to look at the factors set forth in Restatement (Second) of Torts § 767, which were noted in *Guard-Life*.[74] These factors include:

- the nature of the actor's conduct;
- the actor's motive;
- the interests of the party whose contract is breached;
- the interests sought to be advanced by the actor; and
- the relation between the parties.

Citing a comment to that section, the *Guard-Life* Court noted that in determining whether an action impacting a contract was improper, the question is whether, upon a consideration of the relative significance of the factors involved, the conduct should be permitted without liability, despite its effect of harm upon the party whose contract is breached.[75]

Given the above discussion, two points can be made with certainty. A company will not be held liable for tortious interference with contract merely because, as part of a general solicitation, it communicated its standard prices and terms to a customer it knew had a contract with a competitor and the customer thereafter breached its contract. Second, because the law provides greater protection to an existing contract than interests in a prospective relationship, a company can be liable for tortious interference with contract even if its interaction with the competitor's customer was entirely lawful and neither malicious nor wrongful.

Courts are likely to focus upon the extent to which the defendant's actions may be viewed as aimed at having specific customers abandon their existing contracts.

In determining when a competitor's conduct becomes "improper" and a tortious interference with a contract, courts are likely to focus upon the extent to which the defendant's actions may be viewed as aimed at having specific customers abandon their existing contracts and give their business to the defendant, as opposed to a broad-based solicitation. In this regard, a court should consider whether:

- The solicitation specifically targeted the plaintiff's customers;
- The price/terms in the solicitation were what the defendant commonly used, as opposed to special terms for purposes of the solicitation;
- The solicitation in any way disparaged the competitor or its products/services;
- There was any unfair comparison between the soliciting company's product/service and that of the competitor;
- The solicitation offered an incentive not made available to other prospective customers; and
- A side-deal existed between the defendant and the breaching party which "sweetened" the defendant's terms.

In determining whether a broad general solicitation is consistent with a minimum level of ethical behavior

in the marketplace, a court should consider whether:

- The defendant used wrongful means in an effort to have the customer abandon its existing contract;
- The defendant's actions were motivated by malice;
- The defendant's actions were contrary to a standard or guideline prescribed for the industry in which the parties compete;
- The defendant's actions were inconsistent with general trade practice in the particular field;
- The price/terms in the solicitation were "predatory";
- The solicitation contained false or misleading statements; and
- The solicitation expressed opinions that had no reasonable basis in fact.

Attention should be paid to § 772(a) of the Restatement (Second) of Torts, which provides that there is no improper interference in communicating "truthful information" to a party under contract. Other states, for example, New Jersey,[76] have recognized this principle.

Also to be considered are the comments to Restatement § 766 that improper conduct does not occur merely by entering into an agreement with a party under contract, knowing that the party cannot perform both contracts (comment n) and that the defendant's conduct "must be intended to affect the contract of a specific person" (comment p).

Restatement § 768 and comment h thereto should be taken into account. These provisions note that a defendant's mere status as the plaintiff's competitor does not shield it from a charge that it tortiously interfered with the plaintiff's contracts. Comment e to § 768 notes that if the interfering party diverts business from the competitor by virtue of superiority in matters relating to the competition, such action may be permitted so as to encourage competition. The comment further notes that if business is diverted for reasons

unrelated to the competition, superior efficiency is not furthered.

Unwarranted litigation brought in bad faith with no belief in its merit can constitute improper conduct that can tortiously interfere with a contract.[77]

A court also may consider how courts in other jurisdictions have addressed the claim of tortious interference with contract. For example, the First Circuit, applying Rhode Island law, endorsed a jury instruction that tortious interference could be found "only if the competitor uses methods of competition which are beyond those which competitors must expect to occur in the marketplace, that is, by competition which is based upon illegal [or] illegitimate means."[78] The Ohio Supreme Court, citing Restatement (Second) of Torts § 768, stated competition is proper "if (a) the relation between the actor . . . and his or her competitor . . . concerns a matter involved in competition between the actor and the other, and (b) the actor does not employ wrongful means, and (c) his action does not create or continue an unlawful restraint of trade, and (d) his purpose is at least in part to advance his interest in competing with the other."[79] In Massachusetts, tortious interference liability may be imposed when the defendant had "improper motives" or used "improper means."[80]

In sum, in determining whether competitive conduct improperly interferes with a contract, a court should carefully consider the particular facts before it, in light of three values: the interest in promoting robust competition, the protection of contracts and the preservation of a minimum level of ethical behavior in the marketplace. Ultimately, as noted in *Guard-Life* and Restatement (Second) of Torts § 767, comment b, the court must decide whether the competitive conduct of the alleged interferer should be permitted without liability, despite the harm it causes to the party whose contract is breached. ■

1. *Thyssen, Inc. v. S.S. Fortune Star*, 777 F.2d 57, 63 (2d Cir. 1985).

2. 3 Farnsworth, Contracts § 12.8 at 194-95 (2d ed. 1990).

3. *Stop-N-Go, Inc. v. Uno-Ven Co.*, 184 F.3d 672, 680 (7th Cir. 1999).

4. *U.S. v. Blankenship*, 382 F.3d 1110, 1133–34 (11th Cir. 2004), *cert. denied sub nom. Glover v. U.S.*, 126 S. Ct. 42 (2005).

5. *NBT Bancorp Inc. v. Fleet/Norstar Fin. Group, Inc.*, 87 N.Y.2d 614, 621, 681 N.Y.S.2d 581 (1996).

6. 8 N.Y.3d 422, 835 N.Y.S.2d 530 (2007).

7. 2 El. & Bl. 216, 118 Eng. Rep. 749 (1853).

8. 48 N.Y. 430, 432 (1872).

9. *Id.*

10. 223 N.Y. 325, 333, 119 N.E. 573 (1918).

11. 227 N.Y. 418, 422, 125 N.E. 817 (1920).

12. 236 N.Y. 457, 460, 141 N.E. 914 (1923); *accord Hornstein v. Podwitz*, 254 N.Y. 443, 448, 173 N.E. 674 (1930).

13. *See, e.g., Lama Holding Co. v. Smith Barney, Inc.*, 88 N.Y.2d 413, 424, 646 N.Y.S.2d 76 (1996).

14. *Alvord & Swift v. Stewart M. Muller Constr. Co.*, 46 N.Y.2d 276, 281, 413 N.Y.S.2d 309 (1978).

15. *TVT Records v. Island Def Jam Music Group*, 412 F.3d 82, 88 (2d Cir. 2005), *cert. denied*, 126 S. Ct. 2968 (2006); *Albert v. Loksen*, 239 F.3d 256, 274 (2d Cir. 2001) (emphasis added).

16. 79 F.3d 1285, 1294 (2d Cir. 1996).

17. 1 N.Y.2d 116, 120, 151 N.Y.S.2d 1 (1956).

18. 120 A.D.2d 409, 412, 501 N.Y.S.2d 871 (1st Dep't 1986).

19. *Jews for Jesus, Inc. v. Jewish Cmty. Relations Council*, 968 F.2d 286, 292 (2d Cir. 1992); *accord Int'l Minerals & Resources, S.A. v. Pappas*, 96 F.3d 586, 595 (2d Cir. 1996).

20. 50 N.Y.2d 183, 189–90, 428 N.Y.S.2d 628 (1980).

21. *Id.*

22. *Id.* at 191.

23. *Id.* at 194.

24. 87 N.Y.2d 614, 641 N.Y.S.2d 581 (1996).

25. *Id.* at 624; *Guard-Life*, 50 N.Y.2d at 191.

26. 50 N.Y.2d at 190–91; *see also Flash Elecs., Inc. v. Universal Music & Video Distribution Corp.*, 312 F. Supp. 2d 379, 404 (E.D.N.Y. 2004) ("defendants are not afforded the excuse that they were acting as business competitors in procuring the breach"); *Hidden Brook Air, Inc. v. Thabet Aviation Int'l Inc.*, 241 F. Supp. 2d 246, 278 (S.D.N.Y. 2002) ("it is always improper for a competitor to induce a party to breach an existing contract").

27. 50 N.Y.2d at 193.

28. 9 A.D.2d 473, 195 N.Y.S.2d 179 (3d Dep't 1959).

29. 233 N.Y. 607, 135 N.E. 938 (1922).

30. 9 A.D.2d at 479.

31. *Id.* at 480.

32. 233 A.D. 243, 251 N.Y.S. 259 (4th Dep't 1931).

33. *Id.* at 247.

34. *State Enters., Inc. v. Southridge Co-op. Section 1, Inc.*, 18 A.D.2d 226, 238 N.Y.S.2d 724 (1st Dep't 1963).

35. 197 A.D. 277, 189 N.Y.S. 783 (2d Dep't 1921), *aff'd*, 233 N.Y. 607, 135 N.E. 938 (1922).

36. 233 N.Y. 607, 135 N.E. 938 (1922).

37. *Foster v. Churchill*, 87 N.Y.2d 744, 750, 642 N.Y.S.2d 583 (1996); *Felsen v. Sol Café Corp.*, 24 N.Y.2d 682, 687, 301 N.Y.S.2d 610 (1961).

38. *Foster*, 87 N.Y.2d at 750.

39. 24 N.Y.2d 682.

40. *Id.* at 687.

41. *Foster*, 87 N.Y.2d at 750.

42. *Id.*

43. *Ives v. Guilford Mills, Inc.*, 3 F. Supp. 2d 191, 198 (N.D.N.Y. 1998).

44. *Foster*, 87 N.Y.2d at 750–51.

45. *Ultramar Energy Ltd. v. Chase Manhattan Bank, N.A.*, 179 A.D.2d 592, 579 N.Y.S.2d 353 (1st Dep't 1992).

46. *Wilmington Trust Co. v. Burger King Corp.*, 34 A.D.3d 401, 826 N.Y.S.2d 205 (1st Dep't 2006), *leave denied*, 8 N.Y.3d 806, 832 N.Y.S.2d 488 (2007).

47. *Hirsch v. Food Resources, Inc.*, 24 A.D.3d 293, 808 N.Y.S.2d 618 (1st Dep't 2005).

48. *RBFC One, LLC v. Zeeks, Inc.*, 367 F. Supp. 2d 604, 628 (S.D.N.Y. 2005), *aff'd*, 171 Fed. Appx. 902 (2d Cir. 2006).

49. *Don King Prods., Inc. v. Smith*, 47 Fed. Appx. 12 (2d Cir. 2002).

50. *P. Kaufman, Inc. v. Americraft Fabrics, Inc.*, 232 F. Supp. 2d 220, 225 (S.D.N.Y. 2002).

51. *E.F. Hutton Int'l Assocs., Ltd. v. Shearson Lehman Bros. Holding, Inc.*, 281 A.D.2d 362, 723 N.Y.S.2d 161 (1st Dep't), *leave denied*, 97 N.Y.2d 603, 735 N.Y.S.2d 492 (2001).

52. *Barrett v. Toroyan*, 39 A.D.3d 366, 833 N.Y.S.2d 497 (1st Dep't 2007).

53. *MTI/The Image Group, Inc. v. Fox Studios East, Inc.*, 262 A.D.2d 20, 690 N.Y.S.2d 576 (1st Dep't 1999).

54. *Night Hawk Ltd. v. Briarpatch Ltd., LP*, 2003 WL 23018833, *6 (S.D.N.Y. Dec 23, 2003).

55. *Bankboston (Guernsey) Ltd. v. Schupak*, 2000 WL 423526 (S.D.N.Y. Apr. 18, 2000), *aff'd*, 4 Fed. Appx. (2d Cir. 2001); *Drummond v. Morgan Stanley & Co.*, 1996 WL 631723 (S.D.N.Y. Oct. 31, 1996).

56. *NBT*, 87 N.Y.2d at 621.

57. *Id.* at 624 n.2.

58. *White Plains Coat & Apron Co. v. Cintas Corp.*, 460 F.3d 281 (2d Cir. 2006).

59. *White Plains Coat & Apron Co. v. Cintas Corp.*, 8 N.Y.3d 422, 426, 835 N.Y.S.2d 530 (2007) (emphasis added).

60. *Id.* at 426.

61. PJI 2d 3:56, at 507–08 (2007).

62. *Id.* (emphasis in original).

63. 88 N.Y.2d at 424.

64. 87 N.Y.2d at 620.

65. 1 N.Y.2d 116, 120, 151 N.Y.S.2d 1 (1956).

66. *Bogoni v. Friedlander*, 197 A.D.2d 281, 286, 610 N.Y.S.2d 511 (1st Dep't), *leave denied*, 84 N.Y.2d 803, 617 N.Y.S.2d 317 (1994); *see also Fallon v. Wall Street Clearing Co.*, 182 A.D.2d 245, 250, 586 N.Y.S.2d 953 (1st Dep't 1992). Although the law in most states puts the burden upon the defendant to prove any defense based on justification or privilege, some states place the burden upon the plaintiff to show defendant acted without justification. *See, e.g., Super Sulky, Inc. v. U.S. Trotting Ass'n*, 174 F.3d 733, 742 (6th Cir.), *cert. denied*, 528 U.S. 871 (1999) (Ohio law); *Bakare v. Pinnacle Health Hosps., Inc.*, 469 F. Supp. 2d 272, 294 (M.D. Pa. 2006) (Pennsylvania law); *Cordry v. Vanderbilt Mortgage & Fin., Inc.*, 370 F. Supp. 2d 923, 933 (W.D. Mo. 2005), *aff'd*, 445 F.3d 1106 (8th Cir. 2006) (Missouri law).

67. *See McDonnell Douglas Corp. v. Green*, 411 U.S. 792 (1973).

68. *Carvel Corp. v. Noonan*, 3 N.Y.3d 182, 189, 785 N.Y.S.2d 359 (2004) (quoting *NBT*, 87 N.Y.2d at 622).

69. 50 N.Y.2d at 194 (citation omitted).

70. 50 N.Y.2d at 200.

71. 171 Misc. 2d 820, 823, 655 N.Y.S.2d 832 (Sup. Ct., N.Y. Co. 1997). (Fulbright & Jaworski L.L.P. acted as counsel for the party accused of tortious interference.)

72. 50 N.Y.2d at 200.

73. The Court of Appeals's cite to *Marangi* is interesting in light of the fact that in almost identical fact situations involving the same plaintiff and alleged interferer, two other Supreme Court Justices concluded that persuasion to breach alone, as when a competitor offers better terms, could give rise to liability for tortious interference. *V. Marangi Carting Corp. v. Riccardo's Catering Inc.*, N.Y.L.J., Nov. 6, 1996, p. 29, col. 6 (Sup. Ct., Queens Co.). *V. Marangi Carting Co. v. Levona Pastries, Inc.*, Index No. 10245/95 (Sup. Ct., N.Y. Co. Dec. 5, 1995).

74. 50 N.Y.2d 183.

75. *Id.* at 190 (quoting Restatement (Second) of Torts § 767, comment b).

76. *East Penn Sanitation, Inc. v. Grinnell Haulers, Inc.*, 294 N.J. Super. 158, 682 A.2d 1207 (Super. Ct. 1996).

77. *Missigman v. USI Northeast, Inc.*, 131 F. Supp. 2d 495, 515 (S.D.N.Y. 2001).

78. *Ocean State Physicians Health Plan, Inc. v. Blue Cross & Blue Shield of RI*, 883 F.2d 1101, 1114 (1st Cir. 1989).

79. *Fred Siegel Co., L.P.A. v. Arter & Hadden*, 85 Ohio St. 3d 171, 180, 707 N.E.2d 853 (1999).

80. *United Truck Leasing Corp. v. Geltman*, 406 Mass. 811, 816, 551 N.E.2d 20 (1990).

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"Take My Evidence . . . Please!"

This morning I fired my associate.

As I walked into the office through the reception area this morning, performing my due diligence by casting a glance at the headlines in the *Law Journal*, an attorney who looked familiar exited the conference room, nodded familiarly towards me, and strode onto the elevator I had just exited. She had a large envelope tucked under her arm. As the elevator doors closed, my associate came out of the conference room, coffee and half-eaten bagel in hand.

I asked, "Who was that?"

"Jane Jones, the defense attorney on the Smith case."

Now the Smith case is a medical malpractice case where my office represents the plaintiff, a woman whose radiologist, the defendant, failed to detect breast cancer on a mammogram he reviewed. As a result, there was a substantial delay in diagnosing my client's breast cancer. The plaintiff returned to the defendant's office after her diagnosis to collect her original mammogram films for her new physician to review. Later, when she consulted with me about a possible case, she left the original films with me so I could have an expert review them. My office has maintained custody of them since then.

"What was she doing here?"

"She came to pick up the original mammogram films so the defense expert can review them."

The room seemed to go black. As I gradually became aware of my surroundings again, I experienced an excruciating pain throbbing across my forehead, accompanied by waves of nausea I had not felt since my college days.

"You what?" I sputtered, followed by "How could you do such a thing?"

My associate's upper lip trembled slightly, only increasing my anger. His response sent me through the roof: "She said she will return them next week."

"Sure she will. What if they are lost, damaged, altered or destroyed?" My associate said nothing, only enraging me more.

"Do you realize what this means? It means the loss of our case, professional discipline, and a malpractice lawsuit." I paused, vaguely aware that I was paraphrasing George Bailey in *It's a Wonderful Life*, in the scene where he berates Uncle Billy for losing the Building & Loan's bank deposit. Still, it's hard to stop once I get worked up, so I continued ranting and raving until I was spent. My final words were "Get out, and don't come back!"

I walked into my office, slammed the door, and sunk dejectedly into my ergonomically correct chair. I spent the rest of the morning calling my cadre of lawyer buddies, bemoaning the foolishness of my associate. All commiserated, and all agreed that turning over the crucial evidence in the case was, at best, a huge mistake, and, at worst, a fatal blow to the case.

Around lunchtime, I heard a noise outside my door, and noticed a paper being slipped underneath. I hauled myself up from my chair, walked over to the door, and picked up the paper.

"*Olexa v. Jacobs*,"[1] I read, "Second Department, January 23, 2007."

I opened my office door a crack, peered out, and saw my associate, shoulders slumped, walking towards the elevator with a cardboard box filled to overflowing with diplomas and office knickknacks.

I closed my door, sat down in my chair, and continued reading the decision. I read that the defendants, a physician and radiology group, had appealed a trial court order

> which granted that branch of their motion which was to compel the plaintiff to turn over certain original mammograms only to the extent of directing the plaintiff to turn over the mammograms for two periods of 72 hours each, and conditionally striking their answer if they failed to return the original mammograms.[2]

The order appealed from was reversed by the Second Department.

Of course, I thought. What was the trial court thinking in ordering the plaintiff's counsel to turn the original films over to the defendants?

I read on:

> [T[hat branch of the motion which was to compel the plaintiff to turn over the original mammograms is granted that to the extent the plaintiff is directed to turn over the original mammograms to the appellants for two periods of 10 consecutive business days.[3]

What?

This can't be right, I thought. After all, the mammogram films taken and misread by the defendants in a failure to diagnose breast cancer case are, without question, the key evidence in

the case. What about chain of custody? What about the possibility of spoliation? What was going on?

The body of the decision was brief and un-illuminating:

> With respect to the production of the subject mammograms, while it is clear that "[t]he supervision of discovery, and the setting of reasonable terms and conditions for disclosure, are within the sound discretion of the Supreme Court," the Supreme Court herein erred in placing overly-restrictive limits on the appellants' time and opportunities to review the original mammograms. Because there is no dispute that the original mammograms are crucial to the defense of this action, we direct the plaintiff to turn over the original mammograms to the appellants for two periods of 10 consecutive business days.
>
> The striking of a pleading may be an appropriate remedy for the negligent or intentional loss or destruction of crucial evidence. However, the court should not have ordered that the appellants' answer would be stricken if they "fail[ed] to return" the original films. Such a remedy was premature without the proper showing for the striking of a pleading based on the destruction of evidence.[4]

A trial court's discretion to set the terms and conditions of disclosure was a concept I was familiar with. The two cases cited by the Second Department in *Olexa*, one quoting the other, explained the scope of the trial judge's role:

> The supervision of discovery, and the setting of reasonable terms and conditions for disclosure, are within the sound discretion of the Supreme Court. The Supreme Court's discretion is broad because it is familiar with the action before it, and its exercise should not be disturbed on appeal unless it was improvidently exercised.[5]

Putting aside, for now, the fact that both the trial and appellate court had no hesitation in ordering the plaintiff's counsel to turn the films over to defense counsel, something my gut told me was wrong, why was it an "improvident exercise" of discretion for the trial court to permit the defendants to review the films for three days, rather than 10?

It is a simple thing to find decisions where an appellate court finds, or fails to find, that a trial court improvidently exercised its discretion.[6] Try and find a decision where the appellate court explains why the trial court improvidently exercised its discretion – that's harder. Try and find a decision where the facts, as explained in the decision, square with the facts you have in a particular case in your office, and you are generally off on a quixotic quest.

Partly, this is the nature of the beast. In a different context, the Second Department, while reviewing under an abuse of discretion standard a trial court's decision to allow evidence of a prior conviction in a rape case, referred to "these well-recognized but deliberately imprecise guidelines."[7] Not surprisingly, you begin to feel like you are in the world of pornography's "I know it when I see it," standard. Still, I was confused.

In *Olexa*, the Second Department characterized the "original mammograms [as] crucial to the defense of the action."[8] By parity of reasoning, they are also crucial to the plaintiff's ability to prove the action. So why was it improper for the trial court to have issued a conditional order striking the answer imposing a penalty if the films were not returned?

The cases cited by the Second Department in *Olexa* simply offer examples where both the plaintiffs and the defendants were, and were not, entitled to a spoliation sanction. None appear to involve a conditional order.

After all, if the defendants failed to return the original mammogram

films as directed by the trial court, they would, *per se*, have spoliated the films and would be in violation of the court's disclosure order. In that case, the trial court would have available all of the disclosure penalties set forth in CPLR 3126, including striking the defendants' answer, as well as a common law spoliation penalty.[9] Since the key evidence in the case is the original mammogram films, striking the answer of the party that spoliated that evidence would be a perfectly appropriate penalty. So, why did the appellate court hold that the remedy in the conditional order was premature?

Conditional orders pre-date the enactment of the CPLR, and were, according to one early CPLR decision, "the usual procedure adopted by most Judges when providing for imposition of possible penalties under the Civil Practice Act."[10] With a conditional order, "the sanction is not effective if compliance is forthcoming within a stated time after the court's order is made."[11] So, why wouldn't the appropriate penalty for failing to return the original mammogram films be striking the defendants' answers?

The claim that the conditional order was premature is perplexing since a party may be relieved of the penalty contained in a conditional order. A violation of a conditional order may be forgiven if the defaulting party proffers a reasonable excuse for the default and demonstrates a meritorious case.[12] I was still confused.

Now, my main issue with the *Olexa* decision was apparently not an issue for either the trial or appellate court. I simply cannot fathom why the plaintiff's counsel was ordered to turn over the original mammogram films. I don't understand why the defendants' expert could not review the films in the plaintiff's counsel's office or, alternatively, bring the films to the defendants' expert's office for a review under the watchful eye of the plaintiff's counsel?[13]

True, this might entail disclosing the identity of the defendants' medical expert; CPLR 3101(d)(1)(i) permits the defendants to withhold the identity of their medical expert. However, the Second Department has made it clear that the incidental disclosure of a medical expert's identity when disclosing the expert's credentials does not trump the demanding party's right to full disclosure of the expert's credentials.[14] So the fact that the expert's identity might be disclosed in the course of reviewing the original films does not seem to be an issue.

What about chain of custody concerns?

Professor Richard Farrell offers a concise definition of, and descriptions of problems involving, chain of custody:

> The proponent of an item of real evidence must demonstrate its genuineness by clear and convincing evidence (authentication merely requires "evidence sufficient to support a finding that the matter in question is what its proponent claims"). If the thing offered is capable of being replaced or altered, the proponent must provide evidence of its identity and integrity, usually by showing a chain of custody tracking the item from its acquisition to its presentation at trial. Gaps or discrepancies in the chain of custody need not require the Trial Judge to exclude the evidence if, on the whole, the proponent's evidence provides reasonable assurance of the identity and unaltered condition of the thing. However, breaks in the chain of custody may be considered in assessing the weight of the evidence. As to the destruction of dangerous drugs, see CPL art 715; CPL 60.70. In other words, if the real evidence is not fungible "strict proof of the chain of custody [is] not required."
>
> If the item of real evidence is such that any changes in it would be clearly evident, the proponent may rest admissibility on the testimony of any witness familiar enough with the thing to identify it.[15]

Where do the original mammogram films in my case fall within this continuum? The plaintiff has the burden of demonstrating the films' genuineness and, while the films are not fungible, they may be capable of being altered, so the plaintiff should be prepared to establish chain of custody. While a gap in the chain of custody is not fatal if the plaintiff establishes its "identity and unaltered condition," it does go to its weight, and what if there is a claim by one or both sides that the films were altered?

Absent a compelling need for the defendants to take custody of the original films, which is not mentioned in the *Olexa* decision, wouldn't it have been better to avoid any potential problems with the films' chain of custody, authenticity, and unaltered condition by having the defendant's expert review them while under the control of the plaintiff's counsel?

Well, I have been overruled many times before. I have also learned that, when it comes to relying on my gut in figuring out what the law is, I should trust, but verify.

I'm still confused by the *Olexa* decision, but have no doubts about my decision to fire my associate.

This evening I re-hired my associate. ■

1. 36 A.D.3d 776, 829 N.Y.S.2d 564 (2d Dep't 2007).
2. *Id.*
3. *Id.*
4. *Id.* at 777 (citations omitted). *See* CPLR 3101(a), 3120(1)(i).
5. *Ito v. Dryvit Sys., Inc.*, 5 A.D.3d 735, 773 N.Y.S.2d 599 (2d Dep't 2004) (quoting *Provident Life & Cas. Ins. Co. v. Brittenham*, 284 A.D.2d 518, 727 N.Y.S.2d 142 (2d Dep't 2001)).
6. *See, e.g., Olexa*, 36 A.D.3d 776.
7. *People v. Shields*, 58 A.D.2d 94, 98, 395 N.Y.S.2d 476 (2d Dep't 1977).
8. *Olexa*, 36 A.D.3d at 777.
9. Spoliation penalties are available both under CPLR 3126 and the common law. *See, e.g.*, LexisNexis AnswerGuide New York Civil Disclosure, Chapter 26.
10. *Burbell v. Burman*, 44 Misc. 2d 749, 255 N.Y.S.2d 56 (Sup. Ct., Bronx Co. 1964).
11. 1-20 Weinstein, Korn & Miller CPLR Manual § 20.08.
12. *Gorokhova v. Belulovich*, 267 A.D.2d 202, 699 N.Y.S.2d 314 (2d Dep't 1999).
13. I can't bring myself to address a related issue, why a defense expert would need 10, or even three, days to review a mammogram film. Having deposed many radiologists, I have learned that a typical mammogram film is reviewed in a matter of minutes, not hours or days.
14. *Thomas v. Alleyne*, 302 A.D.2d 36, 752 N.Y.S.2d 362 (2d Dep't 2002).
15. Prince, Richardson on Evidence § 4-203 (citations omitted).

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Are They Still Enforceable?

Non-compete Agreements Revisited

By Gary M. Fellner

Many employers use written agreements to secure an employee's promise not to compete with the employer if the employee leaves the company. Today, with many people changing jobs frequently, an employer's need to protect its information can be vital. This is especially true when the employee acquires confidential information that could harm the company if it fell into competitors' hands.

Non-compete agreements, also known as restrictive covenants, address this need and will be enforced by the courts if they are reasonable to protect the employer's legitimate business interests. What do courts deem reasonable? What factors do courts consider when ordering an employee to refrain from competing under a non-compete agreement? What, if anything, can a company do to make it more likely that the agreement will be enforced? This article discusses some recent cases in New York and New Jersey addressing these questions.

It should be noted that non-compete agreements remain useful tools to protect the employer's business interests. But, as is true with any legal agreement, non-compete agreements should be tailored to each specific situation, and drafted by counsel familiar with the employer's business and governing precedents.

What Is Considered Reasonable?

In New York State, courts will deem non-compete agreements reasonable if the evidence establishes that the covenant: "(1) is *no greater* than is required for the protection of the *legitimate interest* of the employer, (2) does not impose an undue hardship on the employee, and (3) is not injurious to the public."[1] The employer's interests are limited to misappropriation of the employer's trade secrets or confidential client lists, or protection from competition by a former employee whose services are unique or extraordinary.[2]

The courts in New Jersey similarly hold that a non-compete agreement is reasonable if it protects the legitimate interests of the employer, imposes no undue hardship on the employee and is not injurious to the public.[3] Matters that merit protection need not be characterized as trade secrets; the courts in New Jersey will protect information held by a departing employee so long as it is treated by the employer as confidential and not generally known to others, such as the employer's customers' buying habits, the cost and mark-up structure, merchandising plans, sales projections, and business strategies.[4] If the departing employee possesses confidential information, the court will consider whether the restrictive covenant itself is reasonable.

Two primary areas of concern are the restrictive covenant's geographic reach and duration. Given the expansive territories into which companies conduct business today, regardless of where the business or employee is physically located (particularly in light of the computer revolution that permits people to work ubiquitously), limiting the non-compete agreement to a certain mile-radius is not as meaningful as it is for companies whose

customer-base is geographically limited. For instance, physicians and real estate brokers may still successfully maintain that restricting employment beyond 20 or 30 miles from the employer's place of business is unnecessary to protect the employer's legitimate business interests.[5] By contrast, where the employer conducts business globally, a restrictive covenant's geographic boundaries become less significant. In *Mansol Industries, Inc. v. Singh*,[6] the agreement said:

> [T]he employee will not during his/her employment, or after the termination thereof . . . have an interest in or be connected in any way with any person, firm or corporation engaged in the same or a similar business as the company's within the geographical territories in which the company has transacted business.[7]

The court held that

> the geographical and temporal scope of the [c]ovenant [n]ot to [c]ompete . . . is not unreasonable in light of the relevant market. The [relevant] industry involves a world-wide market and focuses upon a very narrow specialized niche within which separable geographic zones are indistinguishable. As such, the covenant being world-wide in focus is not unreasonable.[8]

Similarly, in *Pathfinder, LLC v. Luck*,[9] the employer provided consulting services to the chemical industry. The restrictive covenant at issue provided that the officer agreed not to "seek, encourage, and/or accept direct or indirect employment with a client of the Company for a period of one year following the termination of employment or membership with the Company."[10] With respect to the officer's argument that the covenant was overly broad because it applied anywhere in the world, the court held that "because the restrictive covenant was limited to clients, for a limited duration, it is not unreasonable merely because the geographical limits were open-ended."[11]

As to a time restriction imposed under a restrictive covenant, courts are usually faced with covenants restricting employment anywhere from one to three years. Two years is commonly considered reasonable.[12] In *Greystone Staffing, Inc. v. Goehringer*,[13] the court enforced a non-compete agreement signed between Greystone Staffing, a personnel company, and its account manager. The agreement stated that the manager would not: (1) competitively work in the staffing business for a period of one year after his employment ended; or (2) solicit or divert Greystone's customers, employees or temporary personnel for a period of one year after his employment ended. By contrast, in *Mansol Industries*, a case involving a manufacturer of glass and ceramic, the court found that it was "satisfied . . . that the three-year non-competition restriction is reasonable in light of the standards in the industry . . . and the fact that [the plaintiff's] price and cost information can have a lifespan of three years."[14] The durational reasonableness of a non-compete agreement is often judged by the length of time for which the employer's confidential information will be competitively valuable.[15]

To protect the employer against unfair competition even when the agreement's language may be deemed too broad, courts may reduce any duration stated in the non-compete agreement to make it reasonable. *Estee Lauder Companies, Inc. v. Batra*[16] concerned Shashi Batra, who had been employed as general manager of Estee Lauder. When Batra was hired, he signed an agreement that restricted him from working for any competitor for one year after his termination. The agreement covered all geographic regions in which he had responsibility; it was undisputed that he had worldwide responsibility involving many aspects of the business. In discovery, it was shown that Batra, while still employed by Estee Lauder, had used work time and Estee Lauder computers to help a competitor. Batra then resigned to become global manager for that competitor. The court wrote:

> [U]nder the facts of this case, it is determined that the period of time set forth in the agreement and advanced here is greater than necessary to adequately protect Estee Lauder's trade secrets and to protect the interests of Batra. While, as Estee Lauder points out, some of the trade secrets to which Batra was privy arguably have a durational life of as much as two to three years, the evidence presented with respect to Estee Lauder's general behavior surrounding the enforcement of restrictive covenants suggests that such a length of time is generally unnecessary, and it is deemed unnecessary here. . . . [I]n accordance with the authority to grant partial enforcement, a five-month period of enforcement is deemed reasonable.[17]

In addition to reducing the covenant to make it reasonable, courts may, under the principles of partial enforcement, enforce selected parts of the agreement. In *Portware, LLC v. Barot*,[18] the employer moved for an injunction against Barot, a former account manager. Barot sold Portware products and managed customer relationships. The non-compete agreement contained non-competition, non-solicitation, and confidentiality covenants, including the commitment that, for one year after termination of employment with Portware, Barot would not "engage in any business or other commercial activity" that would be "competitive in the United States" with Portware's business activities. After Barot resigned from Portware, he soon began working as a sales manager for FlexTrade Systems, Inc., a direct competitor, where Barot was responsible for identifying potential customers for FlexTrade's software. Portware asked the court to enjoin Barot for one year from soliciting customers whose accounts he managed while at Portware, or transacting business with any customers or potential customers of Portware. The court enforced the agreement in part, observing that

> [p]artial enforcement may be justified when the unenforceable portion is not an essential part of the agreed exchange, and where the employer demonstrates an absence of overreaching, coercive use of dominant bargaining power, or other anti-competitive misconduct, and did not know that the covenant was overly broad and has in good faith sought to protect a legitimate business interest.[19]

The court found that Portware had a legitimate interest in preventing Barot from disclosing or using confidential information that he learned at Portware, but that it had "no legitimate interest in preventing Barot from disclosing or using non-confidential information."[20] Ultimately, the court did not prevent Barot from working at FlexTrade, as the court was ultimately not persuaded that Barot was engaging in unfair competition or that working at FlexTrade would, in and of itself, damage Portware.

What Factors Do Courts Consider?

In *Estee Lauder Companies, Inc. v. Batra*, Estee Lauder availed itself of expedited discovery. As discussed above, the employee, Shashi Batra, resigned to become global manager for Perricone, a competitor. Estee Lauder quickly established that Batra (1) had actively solicitied other employees, while employed by Estee Lauder, to leave with him to join Perricone; (2) possessed trade secrets of Estee Lauder; and (3) had been responsible for product lines at Estee Lauder that were in direct competition with Perricone. In granting Estee Lauder a preliminary injunction to prevent Batra from competing, the court held:

> Even where a trade secret has not yet been disclosed, irreparable harm may be found based upon a finding that trade secrets will inevitably be disclosed where, as here, "the movant competes directly with the prospective employer and the transient employee possesses highly confidential or technical knowledge concerning marketing strategies, or the like." . . . [I]f Batra does misappropriate Estee Lauder's trade secrets, it would be "very difficult to calculate the monetary damages that would successfully redress the loss," given the difficulty in ascertaining empirically how much of a competitive advantage such information gives Perricone and/or how much detriment it might cause to the future profitability of [Estee Lauder].[21]

By contrast, in *Intarome Fragrance & Flavor Corp. v. Zarkades*,[22] the court denied the employer injunctive relief for lack of proof of unfair competition. Intarome employed Zarkades as vice president of sales from 1997 to 2006 in connection with its business of manufacturing fragrances. He was responsible for directing Intarome's nationwide sales force. Zarkades entered into a non-compete and stock subscription agreement that prohibited him from competing with Intarome for a period of one year after his employment terminated. After Zarkades's termination in 2006, he began working for E.T. Horn Company as vice president. Intarome then received an e-mail in January 2007 from Genlabs, one of its customers, sent in error to Zarkades, indicating that Zarkades had been competing with Intarome at E.T. Horn and soliciting its clientele. The court denied the employer's motion for injunctive relief because the evidence was insufficient to show that Zarkades had breached the non-compete agreement:

> [Zarkades] claims that he has not competed against [Intarome], that his current employer, E.T. Horn, is not a competitor of Intarome, and that the two companies are in two entirely different lines of business. Zarkades argues that "[a]s such, any information about the sales of Intarome . . . have no application or significance to the pricing and sales of the broad range of chemicals and specialty ingredients sold by E.T. Horn. [Zarkades] contends that the alleged breach of the Non-Compete Provision revolves around Genlabs, which was a shared client of both Intarome and E.T. Horn. [Zarkades] claims that shortly after he was terminated, and for several months thereafter, Intarome began having difficulties serving its west coast customers.[23]

The court thus concluded that Zarkades gave a plausible explanation based on his long-standing business relationship with Genlabs.

In *Emerging Vision, Inc. v. Main Place Optical, Inc.*,[24] a case involving a franchise for eyewear, Emerging Vision, Inc., requested that the court enjoin employee-optometrists from violating a covenant not to compete. The franchise agreement's covenant not to compete provided that, for a period of two years from the assignment, termination or expiration of the franchise agreement, the defendants would not engage individually or as shareholders, partners or owners of any business which is engaged in the sale of contact lenses, prescription and non-prescription eye-wear and eye care products within a five-mile radius of EVI's location.

Although the court found that the restrictive covenant was enforceable, it nevertheless denied the motion to enjoin the optometrists from violating the covenant because of insufficient evidence that they were engaging in unfair competition:

> EVI has failed to make a *prima facie* showing of entitlement to a preliminary injunction. EVI seeks enforcement of the covenant not to compete against Osiak, Boryszak and Tarbell on the grounds that they threaten to take action which are in violation of [its] rights. *While the covenant not to compete may be reasonable as to scope and duration, EVI has failed to present any evidence that Osiak, Boryszak or Tarbell have engaged in or are threatening to engage in unfair competition by using EVI's trade secrets or confidential information.*[25]

Improving the Odds of Enforcement

Drafting the non-compete agreement to provide that the employee agrees that he or she will be acquiring confidential information and generally describing its nature

will bolster the conclusion that the specific employee has information worthy of protection. The agreement should also provide that the employee consents to injunctive relief after termination and that he or she acknowledges the information's confidentiality.

As to the evidence required, establishing that the information at issue is truly a trade secret, as opposed to information otherwise available, is essential. Further, obtaining discovery from the former employee, customers, and new employer will increase the chance of success.

Employers may also consider giving the employee additional consideration for signing the non-compete agreement. This can be in the form of a bonus, salary, or stock. A court will likely view such additional consideration favorably, if and when the employee argues against a restrictive covenant's enforceability.

In *Morris v. Schroder Capital Management*,[26] the New York Court of Appeals reaffirmed the employee-choice doctrine. That doctrine applies where an employer gives the employee benefits upon compliance with the employer's restrictive covenant. In that situation, the reasonableness of the covenant will not even be examined because the doctrine rests upon the premise that if the employee is given the choice of preserving his or her rights under the contract by refraining from competition or competing, there is no unreasonable restraint upon an employee's liberty to earn a living.

Conclusion

Non-compete agreements remain viable tools to protect employers against unfair competition. They will be carefully scrutinized by the courts and will be enforced where the provisions are reasonable and the employee possesses information that justifies protection. When appropriate, the court may vary the agreement's terms as the court deems reasonable, including reducing the duration or scope of the non-compete provisions to fit the facts involved. To enjoin an employee from competing, courts look at the nature of the employer's and the competitor's businesses and whether they are direct competitors; what information the employee has acquired; what the employer has done to safeguard the information; and how expansive the restrictive covenant is. The validity and enforceability of a covenant against competition is a fact-sensitive inquiry and is determined in light of the facts of the particular case.[27] Each situation merits its own considerations, and for that reason, non-compete agreements should be tailored to address each accordingly. ■

1. *BDO Seidman v. Hirschberg*, 93 N.Y.2d 382, 388–89, 690 N.Y.S.2d 854 (1999) (emphasis in original).

2. *Id.* at 389.

3. *Maw v. Advanced Clinical Commc'ns, Inc.*, 179 N.J. 439 (2004) (citing *Ingersoll-Rand Co. v. Ciavatta*, 110 N.J. 609 (1988)).

4. *Ingersoll-Rand Co.*, 110 N.J. at 683; *Platinum Mgmt., Inc. v. Dahms*, 285 N.J. Super. Ct. Law Div. 274 (1985).

5. For example, in *Cmty. Hosp. Group, Inc. v. More*, 183 N.J. 36 (2005), the New Jersey Supreme Court held that restricting the physician-employee from competing within 30 miles from the medical facility was unreasonable given the shortages of neurosurgeons, and upon remand, directed that the court impose a restriction not to exceed 13 miles, since the doctor in question had staff privileges at a nearby hospital 13 miles away.

6. 1996 U.S. Dist. LEXIS 22823 (D.N.J. Sept. 25, 1996).

7. *Id.* at *10.

8. *Id.* at *33.

9. 2005 U.S. Dist. LEXIS 44782 (D.N.J. May 20, 2005).

10. *Id.* at *5.

11. *Id.* at *20.

12. *Cmty. Hosp. Group, Inc. v. More*, 365 N.J. Super. Ct. App. Div. 84 (2003), *rev'd*, 183 N.J. 36 (2005) (covenants containing a two-year period of restriction have generally been upheld as reasonable) (citing *Schuhalter v. Salerno*, 279 N.J. Super. Ct. App. Div. 504, *cert. denied*, 142 N.J. 454 (1995) (covenant restricting accounting partners from servicing each other's clients for two years found reasonable and enforceable)); *A.T. Hudson & Co. v. Donovan*, 216 N.J. Super. Ct. App. Div. 426 (1987) (covenant restricting principal from soliciting business from consulting firm for two years held enforceable); *Mailman, Ross, Toyes & Shapiro v. Edelson*, 183 N.J. Super. Ct. Ch. Div. 434, 441 (1982) (finding that two-year restrictions are generally reasonable).

13. 14 Misc. 3d 1209(A), 836 N.Y.S.2d 485 (Sup. Ct., Nassau Co. 2006).

14. *Mansol Indus., Inc. v. Singh*, 1996 U.S. Dist. LEXIS 22823 (D.N.J. Sept. 25, 1996).

15. *Estee Lauder Cos., Inc. v. Batra*, 430 F. Supp. 2d 158, 180 (S.D.N.Y. 2006).

16. *Id.*

17. *Id.* at 181–82.

18. 11 Misc. 3d 1059(A), 815 N.Y.S.2d 495, 2006 WL 516816 (Sup. Ct., N.Y. Co. Mar. 2, 2006).

19. *Id.* at *3.

20. *Id.* at *4.

21. *Estee Lauder Cos.*, 430 F. Supp. 2d at 174 (citations omitted).

22. 2007 WL 979882 (D.N.J. Mar. 29, 2007).

23. *Id.* at *4.

24. 10 Misc. 3d 1071(A), 814 N.Y.S.2d 560, 2006 WL 118364 (Sup. Ct., Nassau Co. Jan. 11, 2006).

25. *Id.* at *6 (emphasis added).

26. 7 N.Y.3d 616, 825 N.Y.S.2d 697 (2006).

27. *Graziano v. Grant*, 326 N.J. Super. Ct. App. Div. 328 (1999).

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Going Beyond the Will

A Primer on Legacy Planning for Attorneys

By Scott E. Friedman and Dr. Alan G. Weinstein

Traditionally, and appropriately, lawyers focus their estate planning initiatives on the thoughtful disposition of their clients' tangible assets, so as to insure a well-managed and efficient transfer of these material possessions upon death. A useful adjunct to this traditional focus can be a similarly thoughtful plan for the transfer of important intangible assets. This may be accomplished by helping clients create a written or recorded "Legacy." Thoughtfully and carefully prepared, a Legacy can be a lasting treasure for family members, friends, and even communities. What follows is offered as a primer for lawyers who wish to assist their clients in adding a Legacy to the estate plan.

The Need for Advance Legacy Planning

The notion of seeking to transmit wisdom and experience to others in anticipation of one's passing is as old as the Bible, which contains passages referencing the value of such a practice.[1] More recently, the history of 9/11 is replete with poignant messages left in anticipation of imminent death, such as the one by Ceecee Lyles, a 33-year-old flight attendant on Flight 93, who left a message on an answering machine asking that her children be told that she loved them very much. Another was left by Captain Walter Hynes of the New York City Fire Department, while on his way to the World Trade Center. He recorded, "I don't know if we'll make it out. I want to tell you that I love you and I love the kids."[2] Numerous other last-minute communications were sent that day to deliver messages of love, forgiveness and other heartfelt emotions.

Not all such messages have their origins in dark times. The well-known columnist Art Buchwald recorded a video months before he died in January 2007, which was released moments after his passing. Buchwald's video combined his sense of humor (it began with the statement "Hi, I'm Art Buchwald and I just died") along with his views of the world and important personal observations.

One of the many important differences between the 9/11 messages and Buchwald's message is that his was the result of careful planning. Buchwald recognized his impending death, and had the luxury of both time and materials to thoughtfully prepare every aspect of his message: how (video), where (his vacation home on Martha's Vineyard), what (a combination of humor and serious reflection), when (released moments after his death), and to whom (widely over the Internet). By stark contrast, those who died on 9/11 had no such opportunity. As a result, their messages, though important to and cherished by their loved ones, were inevitably constrained by lack of time.

Since the precise time of one's death is unpredictable, we believe it can be helpful to prepare a statement well in advance, as Buchwald elected to do. Such advance preparation can help insure that clients will have the opportunity to say whatever they want to say – to whomever they would like to say it. This is the advantage of what is referred to here as Legacy Planning.

Contents of a Legacy

Because a Legacy is a vehicle for expressing deeply held personal beliefs, and for relaying a lifetime's worth of experiences and observations, there is almost no limit to the type (or amount) of information that can be included: insights into happiness, business success (or failure), strategies for working through difficult times or with dif-

ficult people. It can be created for one or many people, typically family members and friends, but sometimes even for organizations with which the client was affiliated.

Historical family information that might otherwise be forever lost can be transmitted. This might include, for example, the circumstances surrounding meeting a spouse, the birth of a child, overcoming some particular adversity, or simply recounting memories from a particular trip or other moment in time. Major life decisions, and why those decisions were made, might also be shared. A Legacy can be used to ask for forgiveness, or to forgive someone else. It might contain burial instructions or instructions to forgo a traditional burial service in lieu of something less traditional but more meaningful, such as a party to celebrate the author's life.

Lawyers can assist their clients in preparing powerful and meaningful Legacies by asking them to consider a wide variety of subjects for possible inclusion. For example, in addition to the subjects referred to above, a Legacy can contain a variety of "practical" information: the location of all (or particular) assets; helpful resources for everything ranging from wealth management to liquidating unique assets (*e.g.*, a rare wine collection); and non-binding advice on which assets to keep or sell.

Lawyers might also prompt their clients to consider including thoughts from the following list:

- their core values and examples of how these were actually used to help make difficult decisions;
- lessons passed along from other loved ones, including parents, grandparents, a spouse, and friends;
- hopes for the future;
- advice on anything from parenting and marriage to how to prepare an old family recipe;
- important events in life; and
- favorite books, movies, songs, Web sites, quotations, and places to visit.

Those who take the time to prepare a Legacy discover not only a unique way to share important perspectives and insights with their loved ones but also learn something very important about themselves. Working on a Legacy can be a very positive emotional experience for clients, often providing unexpected clarity as to what is most important in their lives, and even giving them a sense of "completion," particularly as parents. For many, it is clear that the gifts transmitted in a Legacy are a wonderful complement to the assets transferred in their wills. (There can even be a side-benefit for the attorney: the client's experience of working on such a constructive project can help foster a deeper respect and commitment to his or her lawyer.)

The Legacy as Adjunct to Family Business Planning

A Legacy can be a useful resource for family businesses where the client was a (or "the") key participant. Following an ownership and management transition, surviving members typically struggle to find a new equilibrium. For a combination of reasons, such efforts are not always successful, resulting in the inability of the family to keep the business going.[3]

This inability may be caused by poor communications and unhappy family dynamics. Some family business leaders contribute to these problems by remaining completely silent on succession issues. This can create a confusing leadership vacuum in which children inevitably focus on their own self-interest. In other instances, leaders might share some of their thinking, but not fully, or very clearly. Instead, they give greater attention to traditional estate planning documents, which are concerned more with "what happens" than with "why." In the absence of prior and clear communications from the now-departed client, surviving family members can be left with little guidance about how to lead the company.

A Legacy can help fill this void, and may serve as a useful adjunct to a leader's family business succession plan. It can provide important additional background and context to major decisions made by him or her; it can include perspective on why it makes more sense for a particular member to assume (or forgo) a leadership role. Complementing the traditional estate planning documents, which determine the mechanics of how ownership interests in a business are to be transferred, a Legacy can explain why those interests are being transferred in a particular way. It can also serve as a means of sharing the leader's hopes for how decisions regarding the company's operations might be made in the future under the new leadership.

This form of communication may be critical in helping to build collaboration and family unity. Moreover, the act of preparing a Legacy may help a leader more clearly think

through his or her own desires and intentions. The effort may prove to be invaluable to surviving family members.

In short, a Legacy can be used by a senior member of the family business to share his or her intentions about leadership, succession, ownership and governance of the family business, and to provide insight and wisdom to the next generation. It may even improve the chances that surviving members will accept the plan found in the more traditional documents, and thereby reduce the potential for intra-family conflict.

Sharing Values and Personal Feelings

Another reason for preparing a Legacy is to facilitate a sharing of core principles and values, so that children can have a better understanding of what guided a parent's decision-making throughout his or her life – why a particular career path was or was not followed, how a balance between work and family was achieved (or was at least attempted), and the nature of the client's relationships with his or her own parents and grandparents and any other persons who were influential.

In addition, a Legacy can be a "last chance" to say some things that should have been said, but never were. While many people are excellent communicators when it comes to "matters of the mind," they can be much less adept at expressing emotions or "matters of the heart." As a result, such individuals may never have shared their feelings fully or well, and may have lost opportunities to say what they would like to have said during the course of their lives. In other instances, people may have experienced an "emotional cutoff" from loved ones or friends, and they have drifted apart, or even have become completely estranged. Creating a Legacy offers a chance to express difficult emotions, as well as to bring closure to unfinished personal business. Such closure may be meaningful to the recipient of a message, as well as being therapeutic for the person delivering the message.

Preparation Tips

There is no one "right" or "wrong" way to prepare a Legacy; each is unique unto itself. However, certain approaches are worthy of consideration to insure that a Legacy achieves maximum effectiveness.

Letters have been the most widely used medium for Legacies. Traditionally, they are provided to the intended recipients upon the author's death. A better approach may be to urge the client to review a Legacy with the recipients while he or she is still alive. This creates a better learning opportunity for the beneficiaries, who can ask questions of the writer, and thereby gain enhanced clarity and understanding.

As is done with traditional wills, it can be useful to update and edit the Legacy, and perhaps add to it, over the years, as one's thoughts, knowledge and insight continue to sharpen as time passes. Legacies can be revisited throughout life to help clarify core values and guiding principles, as they can and should be statements of those values and principles. Such statements might be helpful to couples as they enter into marriage, to children upon the divorce of their parents, or at any other point where the client feels inspired to share insight, experience and wisdom.

While a Legacy could conceivably be transmitted orally, lawyers can help construct more permanent expressions of thought by assisting clients to prepare some type of tangible document. While this often takes the form of a letter, the current wide access to new forms of technology means that a Legacy can be prepared on a CD or DVD, with all the accompanying "bells and whistles" – video clips, photographs, sound bites, music, etc. It is even possible to engage professional writers, interviewers, photographers, and production companies for those interested in preparing a more thoughtful, dynamic or even professional-quality Legacy. Such technology might help your client share not just the content of a message, but the appropriate tone and emotion as well. Whether simply written on the back of a napkin, or recorded with the most advanced technology, a Legacy represents one of the surest tools available to transfer wisdom, values and emotional expression.

Finally, it is important to emphasize that a Legacy should not be considered a legally enforceable instrument. If there is anything in a Legacy that a client would like to make enforceable, such as a succession plan in a family business, it should be included in other documents, such as a will or shareholders' agreement.

Conclusion

An oft-cited cliché tells us that it is better to teach a person how to fish than to give that person a fish. Accepting the premise that education can create self-sufficiency, a parent's knowledge, insight and wisdom are among the most important assets that can be transferred to a child. A Legacy Plan can be the mechanism for that transfer, and may provide families with a context and explanation of purpose to an estate plan that traditional wills and trust documents do not. Legacies can also foster family and/or organizational continuity by tying together past, present and future generations with shared knowledge and experience. For these reasons, all lawyers should consider incorporating Legacy Planning into their professional practices. The Legacies that result will surely be treasured for years to come. ■

1. *See, e.g.*, Genesis, Chapter 49. *See also* The Book of John, Chs. 15–18.

2. As quoted in "The Sounds That Still Echo From 9/11," by Peggy Noonan, in the *Wall Street Journal*, Sept. 9, 2006.

3. *See generally* Scott E. Friedman, The Successful Family Business (1998); Michael Friedman & Scott E. Friedman, How to Run a Family Business (1994).

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Derivative Standing for New York LLC Members – The Conflict Continues

By Laurence A. Steckman, Dennis M. Rothman and Yoko Yamamoto

Introduction

On February 5, 2007, Judge Joseph Bianco, in *Pennacchio ex rel. Old World Brewing Co. v. Powers*,[1] held that members of limited liability companies (LLCs) lack standing to file derivative suits against fellow members under the New York Limited Liability Company Law (NYLLCL). Relying on a decision of the Second Department,[2] and trial-level state precedents,[3] he became the first federal judge to reject the position, taken by the Southern and Eastern Districts,[4] that New York grants standing to LLC members to sue derivatively. In an interesting juxtaposition, just three days later, the First Department, in *Tzolis v. Wolff*,[5] relying on the federal cases Judge Bianco had just rejected, reached the opposite conclusion, becoming the first state court to grant standing to LLC members to assert derivative claims, contrary to then-existing state authorities.

At present, conflicts on the LLC derivative standing issue exist between New York's First and Second Departments of the Appellate Division, New York's Southern and Eastern Districts and between judges in the Eastern District.

To say the law is confused is an understatement.

In the first section of this article we discuss certain features of LLCs, comparing them to corporations and partnerships, the policies for and against LLC member derivative standing, and cases, commentary and NYLLCL legislative history on derivative rights for LLC members. Next, we discuss cases that have held or stated in dicta that LLC members lack standing to file derivative suits, and then turn to cases that have held LLC members do have standing to file derivative suits. We assess competing arguments in the last portion of the article, identifying the sources of confusion among the courts, and conclude that the courts holding New York LLC members have standing to file derivative suits have the more compelling arguments.

LLC Structure, Pros and Cons of Derivative Rights and Legislative History

LLC Structure and the Pros and Cons of Derivative Rights

Limited liability companies are "hybrid" business entities, considered a "cross-breeding of the corporate form and the partnership form."[6] LLCs share the feature of limited liability protection for their owners, called "members," with the corporations, but, like partnerships, provide members with a greater degree of operating flexibility.[7] LLC members may directly manage LLCs, and they owe fiduciary duties to other members in running the LLC.[8]

Essentially, LLC derivative suits, like other derivative suits, provide a vehicle by which members can vindicate the rights of the LLC by suing managers engaged in wrongdoing who refuse to sue themselves.[9] Such suits facilitate fiduciary breach claims against those persons who control the firm's decision to sue.[10] Derivative remedies are granted explicitly in the LLC statutes of most states, and where they are not so provided, courts have frequently implied the right of members to sue derivatively under common law.[11] The NYLLCL provisions governing duties and liabilities of managers, including fiduciary duties, follow corporate concepts for directors, and track, almost word-for-word, provisions in N.Y. Business Corporation Law § 717, for directors.[12]

The New York Court of Appeals has said of shareholder derivative actions that they serve the important purpose of protecting corporations and minority shareholders against officers and directors who, in discharging their official responsibilities, place other interests ahead of those of the corporation.[13]

The public debate on the NYLLCL dedicated substantial time to derivative rights. The reasons why those rights were salutary and important were enumerated by Howard Lefkowitz, then Chair of the Committee on Corporation Law of the Association of the Bar of the City of New York, in his testimony before the New York State Assembly. Lefkowitz noted that equity courts had provided the holder of an interest in an entity, such as corporate shareholders, the right to question the decision making of those in control of the entity by bringing a derivative action, that this right was recognized in New York as early as 1832 and that the Supreme Court had, by then, outlined the standards of derivative suits, the majority of which remain virtually unchanged.[14]

He also explained the primary, two-fold justification for derivative rights. First, because a corporation is an entity distinct from its members, derivative actions permit claims to be brought in the name of the entity to recover for wrongs to the entity rather than harm to the individual plaintiff or class of plaintiffs. Second, they provide the shareholders or partners with a means of overseeing the actions of the company's managers to ensure they are acting wisely and in good faith in performing their fiduciary duties. Shareholders need such a device, he stated, to ensure their interests are satisfactorily protected. He also observed that derivative actions serve as a substantial deterrent to improper activity by those entrusted with the rights and powers of management, who refuse to sue themselves.[15]

Notwithstanding these salutary purposes of derivative actions, some commentators have criticized LLC derivative rights. For example, one notes that although a suit by a single member arguably is appropriate in public corporations (because the members are generally passive and uninvolved in management and, in any event, are too numerous to coordinate effectively for action against errant managers), the derivative suit mechanism in the LLC context opens the door to suits that are more self-interested strikes for attorney fees than legitimate grievances.[16] Some commentators have argued that LLC derivative suits are costly and unnecessary, given other remedies available to LLC members, including the power to sue directly in their own right.[17] Because the derivative action potentially subjects the LLC to litigation costs and possible liability for claims of fiduciary breach, LLC derivative suits have often been met with hostility.[18] By and large, such criticism has been disregarded and many states have enacted LLC statutes expressly providing derivative rights for members.

The Legislative History of the NYLLCL as to Derivative Rights

Derivative rights were an issue for legislators when the NYLLCL was being considered. Early drafts of the law provided for member derivative rights but that provision, proposed Article IX, was not incorporated into the final version of the law. As the practice commentary to the NYLLCL (the "Commentary") in McKinney's notes:

> In the initial draft [Article IX] had covered the rights of members to institute derivative actions. Because some legislators raised questions as to the derivative rights provisions, to avoid jeopardizing passage of the Law, Article IX was excised. . . . The battle to include derivative rights in the [NYLLCL] may be fought at some future date.[19]

While each court that has held that LLC members lack standing to file derivative suits has focused on this piece of the Commentary, the Commentary is not the only source for the legislative history. The NYLLCL legislators also heard detailed testimony that, even if they did not provide a derivative right in the statute, the right would exist nonetheless under New York's common law: "[T]he assembly solicited testimony on the matter at a public hearing on the proposed NYLLCL and was told that an LLC member would have the common law right to bring a derivative suit on behalf of the LLC whether or not the statute contains such an express right."[20]

In his testimony, Howard Lefkowitz explained that the courts have permitted derivative suits in the partnership context without express statutory authority, and that New York state and federal courts have long permitted derivative actions by a limited partner without statutory authority, analogizing a limited partner to a shareholder, neither of whom would otherwise have the right to bring an action on behalf of the business entity. The existence of a derivative right is rooted in the law of trusts, that beneficiaries have the right on general principles of equity, *independent of statutory provisions*, to sue for the benefit of the trust on a cause which belongs to the trust or where

the trustee has an adverse interest, a right codified in 1968 in § 115-a of the N.Y. Partnership Law.[21] Lefkowitz addressed how the rules would apply to LLCs based on their similarity to limited partnerships:

> Applying these principles to a limited liability company . . . to the extent that members of a limited liability company are analogous to a minority shareholder or a limited partner . . . *such member would, as a matter of common law precedent, have the right to bring a derivative action on behalf of a limited liability company whether or not the statute contains such an express right*.[22]

Addressing proposed Article IX directly, Lefkowitz stated that LLC members would have the right to bring derivative suits even if Article IX were not enacted: "Article IX of the Assembly bill specifically addresses the situation that I have described and is consistent with the statutory framework for derivative actions for other entities in New York. *In fact, if such statute is silent, in my view, the members would still have such a right*."[23] Thus, the Assembly was told expressly that the common law provides derivative rights for similar business entities, that LLC derivative rights would exist under the common law based on analogy to limited partnership rights, and that those rights would exist even if they were not written into the statute. This testimony, however, has not been cited in any of the cases holding that LLC members may not sue derivatively.

The Commentary now states:

> A preliminary question may be whether the claim would be a direct claim by the member for wrongs he suffered or a derivative claim for wrongs to the LLC. The LLCL does not include a specific provision permitting a member to bring a derivative action on behalf of the LLC of which he is a member. Early drafts of the proposed LLCL had included an Article IX with provisions governing the institution of derivative actions on behalf of LLCs. Because some legislators had raised questions about the derivative rights provisions, to avoid jeopardizing passage of the balance of the law, Article IX was dropped. *The absence of an Article IX from the LLCL was a conscious omission, not a typographical error, as the decision to omit derivative rights occurred late in the legislative session*.[24]

The Commentary makes no mention of the testimony that derivative rights would exist by force of common law, even in the absence of an express statutory grant and emphasizes only that the Legislature omitted derivative rights intentionally, which is the basis for the rationale of the "no standing" case holdings.

The "No Standing" Cases

The first New York state case to address the NYLLCL derivative standing issue is *Schindler v. Niche Media Holdings, LLC*.[25] Citing only the Commentary, the court held that because the Legislature enacted the NYLLCL without the express grant of derivative rights, the claim had to be dismissed as unauthorized.

> The public debate on the NYLLCL dedicated substantial time to derivative rights.

The next year, in *Hoffman v. Unterberg*,[26] the Second Department held that LLC members have no right to sue derivatively: "[P]laintiff, an alleged owner/member of a limited liability company, does not have the right to bring a derivative action on behalf of the company."[27]

In January 2006, in *Lio v. Zhong*,[28] the court, relying on *Hoffman* and *Schindler*, suggested, in *dicta*, that the "no standing position" was correct, stating that "most courts have held that the deliberate omission of such a remedy in the statute means that there is no such right at all." The court concluded that the "more persuasive authority is that there is no such right."[29] The phrase "most courts" referred to *Schindler* and *Hoffman*, both of which relied solely on the Commentary,[30] and although the pro-standing position in *Weber v. King*[31] was cited, the *Lio* court provided no analysis as to why the state cases were "more persuasive."

Two months later, in *Tzolis v. Wolff*,[32] the trial court noted that the NYLLCL legislators had made a "conscious decision" to eliminate the right of LLCs' individual members to bring derivative actions. Although *Weber* had held the Legislature's failure to include such a right did not prevent a court from implying a common law right to do so, *Hoffman*, *Lio* and *Schindler* all held there was no such right. Absent a First Department decision on the issue, the court held itself bound by those decisions.

In October 2006, in *Caprer v. Nussbaum*,[33] the Second Department, in *dicta*, observing the dissonance between *Weber*[34] and *Hoffman*, relied on the Legislature's refusal to enact derivative rights to reach a "no standing" position.

In February 2007, Judge Bianco, in *Pennacchio ex rel. Old World Brewing Co., Inc. v. Powers*,[35] adopted the "no standing" position. The "plain language" of the statute did not provide for derivative actions and such rights were deleted when the statute was enacted, supporting the conclusion that derivative suits could not be brought. Legislative intent may be inferred from the omission of substantive provisions and the "specific rejection of language authorizing derivative actions" effectively meant that there was no such right.[36]

Judge Bianco distinguished *Klebanow v. New York Produce Exchange*,[37] in which the Second Circuit had found that derivative rights existed for limited partners under New York common law, even absent a statutory grant.[38] The history of the NYLLC law was significantly different from the partnership law. It was not just "silent" as to whether there was a derivative right; the Legislature specifically and explicitly rejected proposed Article IX during the law making process.[39] This "provided a clear

understanding of the legislature's intent and is likely to be viewed as sufficient by the New York Court of Appeals to overcome any common law right to bring a derivative action here on the basis of the similarities between LLCs and corporations or limited partnerships, which both have such a right."[40]

These state decisions found no derivative standing and found that the common law could not be invoked because of the "clear mandate" from the Legislature to preclude LLC derivative rights. Either, as stated in *Lio*, there is no common law right to bring such suits because the "deliberate omission" of such a remedy in the statute "means that there is no such right at all" or, as stated in *Pennachio*, the Legislature's "clear intent" would "overcome" any common law right that might otherwise have existed.

Because the common law provided such rights for other business entities with similar characteristics, this suggests that derivative rights exist, despite the omission from the statute's text.

Decisions Favoring LLC Derivative Standing

Weber v. King,[41] decided in 2000, was the first federal case to address whether New York LLC members have standing to bring suits on behalf of their business entities. Judge Mishler, after identifying similarities between corporate entities, partnerships and LLCs, explained why the Legislature's decision to delete the grant of derivative rights did *not* determine whether such rights existed under New York common law.

He observed that in *Klebanow*, the Second Circuit had recognized a right of limited partners to sue derivatively on behalf of a partnership prior to the passage of N.Y. Partnership Law § 115-a, which provides limited partners the statutory right to sue derivatively on behalf of the partnership. That court analogized limited partners to corporate shareholders and concluded that limited partners share key traits with corporate shareholders, including an expectation of a share of the profits and immunity from personal liability for partnership debts, save for their original investment. Limited partners, like shareholders, are not thought to be owners of partnership property; LLC members share that characteristic.[42] Because the common law provided such rights for other business entities with similar characteristics, this suggests that derivative rights exist, despite the omission from the statute's text.

In *Cabrini Development Council v. LCA-Vision, Inc.*,[43] another 2000 decision, the defendants relied on the Commentary but Judge Chin rejected their arguments, relying on *Weber*, which had just been decided, concluding it was not unreasonable to believe derivative standing existed for LLC members.[44] The Second Circuit, reviewing *Cabrini*, remanded to permit the filing of a more detailed complaint, stating:

> The district court held that LCA does not have standing to assert these claims because they do not represent a direct injury to LCA. Rather, the district court concluded, these claims properly belong to Excimer and thus could only be asserted by LCA in a derivative action on Excimer's behalf.[45]

In 2006, in *Bischoff v. Boar's Head Provisions Co., Inc.*,[46] Judge Chin examined the derivative standing issue in greater detail. By the time *Bischoff* was decided, the state courts in *Schindler*, *Hoffman*, *Lio* and *Tzolis* had issued holdings conflicting with *Weber/Cabrini*. Judge Chin observed first that derivative actions on behalf of corporations have long existed at common law, that the action existed as a species of equitable suit, and that such suits had been recognized, without statutory authorization, since the 1800s.[47] The common law right to sue derivatively is rooted in the law of trusts, pursuant to which a beneficiary has the equitable right, independent of statute, to bring a cause of action that belongs to the trust, but upon which the trust refused to act.[48]

Unlike the state judges who considered the Legislature's intentional deletion of derivative right to have resolved the issue, Judge Chin, citing *Weber* and *Cabrini*, reached the opposite conclusion, observing that there was no clear indication why Article IX was left out of the statute. Although the Commentary stated the derivative rights provision was left out to avoid jeopardizing passage of the balance of the law, courts could also look to common law in permitting derivative actions on behalf of LLCs.[49]

Since shareholders could bring derivative suits under common law before such actions were codified,[50] and because the Second Circuit, in *Klebanow*, had held limited partners could sue derivatively under common law, without statutory authority,[51] Judge Chin refused to view the "statutory silence" as a *prohibition* on derivative suits. Because limited partners share important characteristics with corporate shareholders including the expectation of profit-sharing, immunity from personal liability, and no ownership of partnership property, they, like shareholders, could maintain a derivative action under the common law.[52]

Hoffman and *Schindler* had relied solely on legislative omission; in *Tzolis*, the trial court found itself bound by *Hoffman*.[53] The trial court in *Lio* mentioned that the common law might provide a derivative right, but it did not

analyze the issue because it thought "most courts" hold the deliberate omission of this remedy in the statute "means there is no such right at all." Judge Chin noted that common law can only be displaced by a statement of "clear and specific legislative intent." The Legislature's failure to expressly provide for derivative suits in the NYLLCL did not "necessarily signify an intent" to eliminate derivative rights that undoubtedly existed under the common law. While change to proposed legislation is one factor in discerning legislative intent, this omission does not imply an intent to abrogate derivative rights altogether; the common law is never abrogated by implication.[54]

Departing from the prior state and federal cases, Judge Chin found a basis for derivative rights in the Legislature's receipt of testimony that derivative rights would exist under common law even in the absence of an express statutory grant:

> [I]t is to be presumed that legislation takes place "against a background of common-law adjudicatory principles.". . . Thus, legislators were aware that the right to bring derivative suits on behalf of similar entities existed at common law. Indeed, *the assembly solicited testimony on the matter at a public hearing on the proposed NYLLCL and was told that an LLC member would have the common law right to bring a derivative suit on behalf of the LLC "whether or not the statute contains such an express right."* . . . Had the legislature intended to preclude derivative claims by LLC members, it easily could have written an explicit prohibition into the law.[55]

Although the state cases relied on that part of the legislative history that the Commentary presented, neither the Commentary nor those cases relying on it mentioned the actual, extensive testimony the legislators heard on the persistence of common law derivative standing. That testimony shows the legislators were aware that their decision not to include an express derivative right would not preclude the right. Their decision was not "the clear indication" of an intent to preclude such suits, as found by most state courts.

Given the "clear existence" of a common law right allowing similar business entities to file derivative suits, and given what the legislators were told regarding the persistence of derivative rights, Judge Chin concluded the onus was on the Legislature to have provided an explicit written prohibition on such suits. He opined that the New York Court of Appeals, on this basis, would hold a member of a New York LLC could properly bring a derivative suit on behalf of the LLC, under New York common law.

In 2007, in *Brownstone Investment Group, LLC. v. Levey*,[56] Judge Marrero held that where an LLC was harmed, the LLC could bring suit derivatively.[57] Although he noted that the NYLLCL does not expressly authorize derivative lawsuits, and that whether New York LLC members may bring derivative actions is unsettled, he stated that Judge Chin's *Bischoff* decision supported his conclusion – the suit could be brought.[58]

In February 2007, on appeal in *Tzolis*,[59] the First Department became the first state court to break ranks with the "no standing" position. It began by observing, in the absence of First Department authority, that New York's trial courts had previously followed the Second Department decision in *Hoffman* – but that all of them had relied solely on the Commentary's "conscious omission" discussion. The First Department rejected that argument expressly stating that it declined to follow the Second Department given the historic judicial recognition of the common-law right to bring a derivative action on behalf of a corporation or a limited partnership and principles of statutory construction, which provide that only a clear statement of legislative intent may override the common law.

The court reasoned that similarities between LLCs, corporations and partnerships, and the pre-statute, common law existence of derivative rights for corporations and partnerships, justified, *a fortiori*, the existence of derivative rights in LLCs. There is no reason to deprive members of LLCs of the same important right to bring a derivative action that is possessed by the members of limited partnerships and corporations, and there is "nothing inherent in the limited liability company structure, operation, purpose, status, or benefits that would call for treating its members any differently, on the issue of standing, from the shareholders of corporations or the members of limited partnerships."[60]

Under this part of the First Department rationale, LLCs may sue derivatively because (1) the right at issue is an "important right," (2) such a common law right pre-existed statutory codification, and (3) there is nothing about the structure or purpose of LLCs that provides any reason why such rights should not be recognized. The absence of a specific statutory grant of such rights was not fatal to the plaintiffs' derivative claims because not only were stockholders and limited partners afforded such rights, but courts had historically allowed individuals, ranging from trust beneficiaries to condominium owners, to advance derivative claims notwithstanding the lack of express statutory authority.[61] Also, federal courts applying New York law had found such rights under the reasoning in *Weber* and *Bischoff*. The First Department rejected as "unpersuasive" the argument that the Legislature's omission of a clause expressly providing for derivative rights for LLC members justified the "no standing" position:

> We believe the statute's silence on this issue cannot be construed as a specific legislative intent to override the common law, nor do we perceive any reason to do so (*see Bischoff*, 436 F.Supp.2d at 631-632; *see also* Callison and Sullivan, Limited Liability Companies: A State-by-State Guide To Law and Practice § 4.7 [2006 ed.] [even when right to bring a derivative claim is

> not available under the Limited Liability Company statute, court may recognize common law right for members to sue derivatively]). We are aware of that portion of the Practice Commentary (Rich, Practice Commentaries at 6), which explains the absence of language affording limited liability company members a right to bring a derivative action and suggesting that the statute's silence was a strategic compromise to increase the likelihood of the passage of the "balance of the law." As seductive as that circumstance may appear as a basis for the theory adopted by the Second Department in *Hoffman v. Unterberg*, 9 A.D.3d 386, 780 N.Y.S.2d 617, *supra*, we respectfully disagree with that holding, because we believe it to be at odds with the longstanding rules of statutory construction requiring a clear expression of legislative intent to overrule a common law principle.[62]

This is consistent with Lefkowitz's testimony that a common law right to sue derivatively would persist, notwithstanding the deletion of Article IX from the statute.

The First Department, on March 27, 2007,[63] confirmed its position, holding that LLC members may bring derivative suits on behalf of LLCs, citing *Tzolis*, and nothing else.

Conclusions

Courts that have considered derivative standing disagree whether the "express rejection" of a derivative rights statutory provision in the NYLLC should be construed as a "clear and specific" or "express rejection" of derivative rights. The authors believe the courts that have found in favor of derivative standing for New York LLCs have the better arguments.

First, each of the "no standing" courts relies on a very selective reading of the NYLLCL's legislative history. They merely cite the Commentary, which makes no reference to the testimony regarding the persistence of common law derivative rights even if Article IX were not enacted. Instead, they focus only on the fact that Article IX was not enacted, albeit to assure passage of the balance of the law.

Second, the "no standing" courts assume the decision not to include Article IX "means" the Legislature did not want LLC members to have any derivative rights. These are completely different things, as Judges Mishler and Chin, and now the First Department, have made clear.

Third, the "no standing" courts assume that merely because omission of a text is relevant to understanding legislative intent, it is dispositive. But, here, the omission from the LLC law was only partially explained by the Commentary's highly selective statement. The NYLLCL legislative history on derivative rights actually supports the opposite position.

Critics of LLC derivative rights are uncomfortable with *Bischoff*. In an interesting blog, one critic, who titled his blog commentary on *Bischoff*: "LLC derivative suits: a dreadful NY federal case," sets forth reasoning particularly interesting for what it does not say:

> [M]y award for the worst unincorporated business case of 2005-2006 goes to . . . *Bischoff v. Boar's Head Provisions Co., Inc.*, 2006 WL 1793653 (S.D.N.Y. June 29, 2006. Here a federal court, purportedly exercising diversity jurisdiction, held that a member of a New York LLC could bring a derivative action on behalf of the LLC despite the absence of NY state authority supporting this result. It gets worse. . . . *The court noted that while a proposed version of the New York LLC act provided for derivative suits, the provision was omitted from the final law, "purportedly to ease passage of the balance of the statute." There's a suggestion here of the court's disdain for mere state politics*. . . . Judge Chin might have been forgiven for relying on this federal authority. But the four state decisions the judge cited came after the federal authority. Doesn't NY get to clarify its own law?. . . . NY courts and legislatures have made the judgment against derivative suits.[64]

The above critic does not mention that the Legislature, as Judge Chin stated, may have concluded that such rights would exist for LLC members even if legislators did not enact Article IX. The critic fails to mention the legislative history that was the very basis of *Bischoff*, a history which directly challenges his critical view of LLC derivative rights, as expressed in his LLC treatise[65] and in his blog.[66] Judge Chin's analysis in *Bischoff* does not show a "disdain for mere state politics"; rather, his careful review of the NYLLCL's legislative history shows exactly the opposite. The critic's commentary plainly does not do justice to Judge Chin's rationale.

Interestingly, the Commentary, updated to discuss *Bischoff*, also fails to mention the legislative history upon which *Bischoff* was largely based. The Commentary re-emphasizes the Legislature's rejection of Article IX, adding to prior text only the fact that elimination of proposed Article IX from the final version was a "conscious decision." Implicitly and wrongly, it suggests the Commentary's prior statement that the Legislature did not enact Article IX because doing so "jeopardized" enactment of the balance of the legislation was and is sufficient to inform inquiry as to what the legislators understood about the persistence of common law rights,

Conflicts and inconsistencies on derivative standing continue to split the courts.

under New York law. Conflicts and inconsistencies on derivative standing continue to split the courts.

The authors believe that the courts finding LLC derivative standing have the better arguments. In light of *Bischoff* and recent First Department holdings on this issue, the authors expect the Second Department will, when the opportunity presents itself, reverse its position or the issue will find its way to the Court of Appeals. If the latter, New York's highest court should conclude that the cases finding derivative standing for New York LLC members are correctly decided. ■

1. 2007 WL 446355 (E.D.N.Y. 2007).

2. *Hoffman v. Unterberg*, 9 A.D.3d 386, 780 N.Y.S.2d 617 (2d Dep't 2004).

3. *See Schindler v. Niche Media Holdings, LLC*, 1 Misc. 3d 713, 772 N.Y.S.2d 781 (Sup. Ct., N.Y. Co. 2003); *Lio v. Zhong*, 10 Misc. 3d 1068(A), 814 N.Y.S.2d 562, 2006 WL 37044 (Sup. Ct., N.Y. Co. 2006); *Tzolis v. Wolff*, 12 Misc. 3d 1151(A), 819 N.Y.S.2d 852, 2006 WL 1310621 (Sup. Ct., N.Y. Co. 2006), *aff'd*, 39 A.D.3d 138, 829 N.Y.S.2d 488 (1st Dep't 2007). *See also Caprer v. Nussbaum*, 36 A.D.3d 176, 825 N.Y.S.2d 55 (2d Dep't 2006) (*dicta*).

4. *See Bischoff v. Boar's Head Provisions Co.*, 436 F. Supp. 2d 626, 630 (S.D.N.Y. 2006); *Weber v. King*, 110 F. Supp. 2d 124, 130–32 (E.D.N.Y. 2000); *Cabrini Dev. Council v. LCA-Vision, Inc.*, 197 F.R.D. 90, 94–95 (S.D.N.Y. 2000), *appeal dismissed in part, vacated in part, sub nom. Excimer Assocs., Inc. v. LCA Vision, Inc.*, 292 F.3d 134, 139 (2d Cir. 2002) (implicitly affirming derivative rights are permissible for LLCs).

5. 39 A.D.3d 138.

6. Rich, McKinney's Practice Commentary, N.Y. LLCL (1)(A) (2006).

7. *Id.*

8. *See Tzolis*, 2006 WL 1310621, at *7 ("[m]anaging members have statutory and common-law fiduciary duties to the members of the company") NYLLCL § 409; *Salm v. Feldstein*, 20 A.D.3d 469, 799 N.Y.S.2d 104 (2d Dep't 2005); *Nathanson v. Nathanson*, 20 A.D.3d 403, 799 N.Y.S.2d 83 (2d Dep't 2005).

9. *See* Larry E. Ribstein & Robert R. Keatinge, Ribstein and Keatinge on Limited Liability Companies, § 10.3, Derivative Suits, text at n.5 (2006).

10. *Id.*

11. *Id.*

12. Rich, McKinney's Practice Commentary, N.Y. LLCL 5(C) (2006) (Duties and Liabilities of Managers).

13. *Bansbach v. Zinn*, 1 N.Y.3d 1, 769 N.Y.S.2d 175 (2003).

14. *Public Hearing on Limited Liability Company Legislation*, N.Y. Ass. 133 (1992) (statement of Howard N. Lefkowitz, Chair of the Committee on Corporation Law, The Association of the Bar of the City of New York) ("Public Hearing"), at 131.

15. *Id.* at 131–32. Other witnesses made similar statements. *See, e.g., id.* at 27–29 (comments of Brian L. Schorr, co-chair of the Association of the Bar of the City of New York and the NYS Bar Association Joint Drafting Committee of the Proposed New York State Limited Liability Company Act) (more modern states have LLC statutes providing for derivative rights; such rights are especially important in manager-operated LLCs where the existence of a right to sue derivatively acts as a "substantial deterrent to improper activity by those who are entrusted with the rights and powers of management and refuse to sue themselves."); *id.* at 52–53 (Bar Association and the Joint Drafting Committee believe derivative rights are important in manager-operated LLCs where the powers of certain members are limited, arguing derivative rights should be expressly included in the statute).

16. Ribstein & Keatinge, *supra* note 9.

17. *Id.* (notes omitted).

18. *See, e.g., id.*

19. Rich, McKinney's Practice Commentary, N.Y. LLCL (G).

20. *Bischoff v. Boar's Head Provisions Co.*, 436 F. Supp. 2d 626, 632–33 (S.D.N.Y. 2006) (Public Hearing *supra* note 14. This testimony is discussed in more detail in connection with the case analysis of *Bischoff, infra.*

21. Public Hearing, *supra* note 14 at 132–33.

22. *Id.* at 133 (emphasis added).

23. *Id.* at 134.

24. Rich, McKinney's Practice Commentary, N.Y. LLCL (G) (emphasis added).

25. 1 Misc. 3d 713, 772 N.Y.S.2d 781 (Sup. Ct., N.Y. Co. 2003).

26. 9 A.D.3d 386, 780 N.Y.S.2d 617 (2d Dep't 2004).

27. *Id.* at 388.

28. 10 Misc. 3d 1068(A), 814 N.Y.S.2d 562, 2006 WL 37044 (Sup. Ct., N.Y. Co. 2006).

29. *Id.* at *3 (plaintiff withdrew the derivative claims under threat of sanctions).

30. In fact, if New York federal courts *Weber*, *Cabrini* and *Excimer* were counted as of the date the decision, most courts favored the view that derivative standing existed under the common law.

31. 110 F. Supp. 2d 124 (E.D.N.Y. 2000).

32. 12 Misc. 3d 1151(A), 819 N.Y.S.2d 852, 2006 WL 1310621 (Sup. Ct., N.Y. Co. 2006).

33. 36 A.D.3d 176, 825 N.Y.S.2d 55 (2d Dep't 2006).

34. *See Weber*, 110 F. Supp. 2d 124.

35. 2007 WL 446355 (E.D.N.Y. 2007).

36. *Id.* at *5 (citing *Lio*, 10 Misc. 3d 1068(A)).

37. 344 F.2d 294 (2d Cir. 1965).

38. *Id.* at 298–99.

39. *Pennachio*, 2007 WL 446355 at *5.

40. *Id.*

41. 110 F. Supp. 2d 124 (E.D.N.Y. 2000).

42. *Id.* at 131 (discussing *Klebanow*, 344 F.2d 294 (2d Cir. 1965)).

43. 197 F.R.D. 90 (S.D.N.Y. 2000), *appeal dismissed in part, vacated in part, sub nom. Excimer Assocs., Inc. v. LCA-Vision, Inc.*, 292 F.3d 134 (2d Cir. 2002).

44. *Cabrini Dev. Council*, 197 F.R.D. at 94–95.

45. *Excimer Assocs., Inc.*, 292 F.3d at 139.

46. 436 F. Supp. 2d 626 (S.D.N.Y. 2006).

47. *Id.* at 629.

48. *Id.*

49. *Id.* at 630.

50. *Id.* (citing N.Y. Bus. Corp. Law § 626; N.Y. P'ship Law § 115-a(2), (3)).

51. *Id.* at 630 (citing *Klebanow v. N.Y. Produce Exch.*, 344 F.2d 294 (2d Cir. 1965)).

52. *Id.*

53. *Id.* at 631.

54. *Id.*

55. *Id.* at 632–33 (citation omitted) (emphasis added) (quoting Public Hearing, *supra* note 14).

56. 468 F. Supp. 2d 654 (S.D.N.Y. 2007).

57. *Id.* at 662.

58. *Id.*

59. 39 A.D.3d 138, 829 N.Y.S.2d 488 (1st Dep't 2007).

60. *Id.* at 143.

61. *Id.* (citing cases).

62. *Id.* at 143.

63. *Bischoff v. Boar's Head Provisions Co.*, 38 A.D.3d 440, 834 N.Y.S.2d 22 (1st Dep't 2007).

64. Larry E. Ribstein, "LLC Derivative Suits: a dreadful NY federal case," Ideoblog, July 20, 2006, <http://busmovie.typepad.com/ideoblog/2006/07/llc_derivative_.html> (emphasis added).

65. Ribstein & Keatinge, *supra* note 9, at § 10.3 (New York is an "exception" – one of the few states not having provided for LLC derivative rights).

66. Ribstein, *supra* note 64.

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A Defense Lawyer's Guide to No-Fault Litigation in New York State

By Mitchell S. Lustig and Jill Lakin Schatz

The Civil Court of the City of New York and the District Courts in Nassau and Suffolk Counties have been inundated with lawsuits filed by medical providers seeking reimbursement for payment of first-party no-fault benefits rendered to injured claimants.[1] These lawsuits are commenced by medical providers as assignees of injured claimants.

Many counties have created Special Parts to handle the burgeoning caseload. It is not uncommon for motions in some counties to be adjourned up to eight months. Because the dollar amount of most no-fault lawsuits is relatively small and discovery is typically not extensive, counsel for the medical providers often move for summary judgment soon after the action is commenced. This article will function as a primer on how to successfully defend a no-fault lawsuit commenced by a medical provider, with particular emphasis on defending a motion for summary judgment.

Prima Facie Case

In order to establish a prima facie case of entitlement to no-fault benefits, the medical provider must demonstrate the following: (1) it possesses an assignment of benefits from the injured claimant; (2) it completed a statutory proof of claim, such as an NF-3; (3) it mailed the claim to the insurer; and (4) the claim was not paid or was denied within 30 days of the insurer's receipt of the claim.

Over the past few years the courts have issued decisions that have made it relatively easy for the provider to satisfy this burden.[2] The medical provider is not required to prove the medical necessity of the services provided to the claimant as part of its prima facie case.[3] Primarily for this reason, medical providers recently have routinely opted for litigation over American Arbitration Association (AAA) arbitration; some arbitrators, relying on an opinion letter from the New York State Insurance Department dated January 11, 2000, have issued decisions requiring

that the medical provider prove the medical necessity of the services rendered even in cases in which the insurer has issued a late denial.

Despite the general trend of the case law, which liberally interprets the provider's burden, there has been a spate of recent decisions from the Appellate Term, Second Department denying summary judgment to medical providers for failure to establish a prima facie case. In these decisions the court has held that the documentary evidence submitted by the provider in support of the motion constituted "inadmissible hearsay," because the affidavit of the plaintiff's corporate officer failed to establish that the officer possessed personal knowledge of the provider's business practices and procedures "so as to lay a proper foundation for the admission, as business records, of the documents annexed to plaintiff's moving papers."[4] It remains to be seen what impact, if any, these decisions will have in curtailing the current litigation explosion.

Assuming that the medical provider has established a prima facie case, the burden then shifts to the insurer to come forward with proof, in admissible form, to refute the plaintiff's evidence and demonstrate a material issue of fact sufficient to defeat the provider's motion for summary judgment.[5]

30-Day Rule

The no-fault insurer is required, by both statute[6] and regulation,[7] to pay or deny a claim within 30 days of receipt of the claim. An insurer may extend this 30-day period if, within 15 business days after receipt of the claim, the insurer sends a request for verification.[8] If the demanded verification is not received within 30 days, the insurer must issue a follow-up request within 10 calendar days of the insured's failure to respond.[9] The 30-day period does not begin to run until all demanded verification is received.[10] If a lawsuit is commenced while there is an unanswered outstanding verification request, it will be dismissed as premature.[11]

If the insurer fails to deny the claim within 30 days of receipt of either the bill or the requested additional verification, the insurer is precluded from asserting most defenses to the cause of action, including lack of medical necessity.[12] An untimely denial, however, does not preclude an insurer from asserting a lack of coverage defense premised on fraud (the insurer alleges that the claimed injury did not arise out of the insured accident[13] or that the accident was a deliberate event caused in furtherance of an insurance fraud scheme[14]). In a rather bizarre interpretation of the regulations, the courts have held that a defense predicated upon a provider's fraudulent scheme to obtain no-fault benefits, such as a provider that bills for services or supplies not rendered or provided to the injured assignor, is precluded by an insurer's untimely denial of the claim.[15]

When invoking the defense of fraud, the insurer has the burden to come forward with proof, in admissible form, to establish "the fact" or the "evidentiary foundation" for its belief that the patient's treated condition was unrelated to the automobile accident or that the alleged accident was an event staged to defraud the insurer.[16] Unsupported conclusions and suspicions as well as unsubstantiated hypotheses and suppositions are insufficient to raise a triable issue of fraud.[17] To raise a triable issue of fraud, the insurer must submit an affidavit from an individual with personal knowledge of the facts, such as a special investigator or claims specialist.[18] An affirmation from an attorney or a bare conclusory statement of a claims representative is insufficient.[19]

One major issue that has been litigated extensively is how specific must the insurer's denial be. For example, when an insurer denies a claim for lack of medical necessity based upon a peer review, is it sufficient for the insurer to simply state on the denial of claim form (NF-10) that all benefits are denied based upon the peer review of "Dr. Smith"? Or is the insurer required to recite the factual basis and medical rationale of the peer review doctor's conclusion or attach a copy of the peer review report to the NF-10?

The medical providers have argued that a denial of claim form that fails to either attach a copy of the peer review report or set forth the factual basis and medical rationale of the peer reviewer's doctor's conclusions is facially defective and precludes the insurer from raising the defense of medical necessity. The relevant insurance department regulation does not appear to support this position. 11 N.Y.C.R.R. § 65-3.8(b)(4) provides that if a no-fault claim is denied in whole or in part based upon a peer review report requested by the insurer, "the insurer shall release a copy of that report to the applicant . . . upon written request."

The insurers have asserted that this regulation only obligates the insurer to send the peer review report to the provider if requested in writing and does not require the insurer to attach the medical report to the denial. The insurers have further argued that there is no textual basis in the regulation to support the draconian remedy of preclusion where the denial did not recite the factual basis and medical rationale of the peer review doctor's conclusions.

In a series of cases involving denials based upon a peer review, the Appellate Term, Second Department firmly sided with the medical providers and summarily voided the insurers' denials. In *A.B. Medical Services v. Liberty Mutual Insurance Co.*,[20] the Appellate Term, Second Department held that an NF-10, although timely mailed, was defective where it merely stated that the claim was being denied based upon a peer review, without attaching a copy of the peer review or reciting the factual basis and medical rationale of the peer review doctor's conclusions. The court asserted that the insurer was precluded from asserting the defense of lack of medical necessity

because the "denial of claim form fails to set forth with particularity the factual basis and medical rationale for its denial based upon lack of medical necessity."

A.B. Medical v Liberty Mutual was quickly followed by *A.B. Medical Services v. Geico Casualty Co.*[21] and *A.B. Medical Services v. Clarendon National Insurance Co.*,[22] where the Appellate Term, Second Department also voided denials based upon peer reviews where the denials were determined to be "nonspecific." As the court noted in *A.B. Medical Services v. Clarendon National Insurance Co.*:

> To preserve the defense of lack of medical necessity, defendant's denial of claim forms must assert, with the requisite specificity, the necessary facts and medical rationale to establish such defense, thereby satisfying the NF-10 form's requirement that the basis of any denial be "fully and explicitly" set forth. Herein, the denials were factually insufficient and thus, while timely, did not avoid preclusion.[23]

In *Contempo Medical Care, P.C. v. Travelers Indemnity Insurance Co.*,[24] the same court extended the reasoning of the *A.B. Medical* cases to a denial premised upon an IME report. According to the court, "[t]he denial of claims forms submitted herein were insufficient on their face for vagueness in that they merely indicated that the denials were based upon independent medical examinations (IMEs) with no indication that the reports of [the] IMEs were annexed thereto or sent to the plaintiff under separate cover within the 30-day claim period."

AAA arbitrators also rigidly followed the reasoning of the *A.B. Medical* line of cases. The first question typically asked at arbitrations where a denial of benefits was premised upon a peer review or IME report was whether the doctor's report was attached to the NF-10. If the doctor's report was not attached to the NF-10, the arbitrator would routinely find in favor of the applicant without considering the issue of medical necessity.[25]

Based upon these decisions, insurers were compelled to settle thousands of cases that would have otherwise been defended and/or tried on the issue of medical necessity. Then, on April 24, 2007, the Appellate Division, Second Department reversed the decisions of the Appellate Term, Second Department in *A.B. Medical Services v. Liberty Mutual Insurance Co.*[26] and *A.B. Medical Services v. Geico Casualty Insurance Co.*,[27] holding that the insurer did not have to attach a copy of the peer review report to the denial or set forth, with particularity, the factual basis and medical rationale of the peer review doctor's conclusions. As the Second Department noted in *A.B. Medical Services v. Geico Casualty Insurance Co.*:

> [W]e disagree with the Appellate Term's conclusion that the defendant's denial of claim forms were insufficient because they failed to set forth with sufficient particularity the factual basis and medical rationale upon which they were based. The applicable regulations provide that if a no-fault claim is denied in whole or part based upon a medical examination or peer review report requested by the insurer, then the insurer shall release a copy of that report to, among others, the applicant or its attorney, upon written request. Had it been the intent of the Department of Insurance to require the carrier to set forth a medical rationale in the prescribed denial of claim form, it would have so provided.

As a result of this stunning reversal insurers will no longer be precluded from raising the defense of medical necessity because the denial of claim form was "nonspecific." Consequently, insurers will now be in a position to defend many more cases and/or settle cases on more favorable terms. It should be noted, however, that a denial of claim form that omits numerous items of information or is otherwise incomplete will still be held to be defective and the medical provider will be awarded summary judgment.[28]

Moreover, as a result of the reversal by the Second Department, courts will now be required to directly confront the issue of medical necessity. The key inquiry will change from whether the language set forth in the denial contains the necessary specificity to whether the peer review or IME report provides a sufficient factual basis and medical rationale for the doctor's conclusions that the services provided were not medically necessary.

A number of courts have already held that a peer review is insufficient if it is unsupported by evidence of "generally accepted medical/professional practice."[29] These decisions are predicated upon the firmly established principle that the burden is on the insurer to prove that the medical services provided were not medically necessary.[30] However, these decisions were rendered after trials where the trier of fact must make a final determination as to the medical necessity of the services in question. In the context of a motion for summary judgment, the standard for judging whether the peer review or IME report suffices to raise an issue of fact as to the medical necessity of the services rendered, should be more relaxed.

Proof of Mailing

One of the major issues that continues to confound the defense practitioner opposing a medical provider's motion for summary judgment is the nature of the evidence the insurer is required to submit to demonstrate that it mailed the denial or NF-10 within 30 days of receipt of the claim.

The question of mailing is of vital importance to the no-fault insurer. As noted above, a no-fault insurer is required to deny a claim for no-fault benefits within 30 days of its receipt of the claim.[31] Not only must the insurer demonstrate that it generated the NF-10 within 30 days of receipt of the bill but it must also prove that it mailed the denial within the 30-day period.[32] If the insurer's proof of mailing of the NF-10 is deficient, the

denial will be deemed untimely and the medical provider will be awarded summary judgment.[33]

In order to establish proper proof of mailing, the insurer must satisfy the common-law test for mailing that requires proof of "actual mailing or a standard office practice and procedure designed to ensure that the items [NF-10] are properly addressed and mailed."[34]

It is virtually impossible for the insurer to prove "actual mailing" of the NF-10 as this would require the affidavit of the first-level clerical employee who actually placed the envelope containing the NF-10 in the mail. Typically, this person cannot be identified by the insurer or is no longer employed by the insurer at the time the validity of the denial is challenged. Moreover, determining whether the insurer followed "a standard office practice or procedure" is highly subjective and is given wide interpretation depending on one's predisposition to favor either the medical provider or the insurer.

The insurer might satisfy the common-law test by submitting an affidavit from its claims examiner stating the following: (1) it is the normal custom and practice of the insurer to mail the NF-10 to the medical provider on the same day the NF-10 is generated and signed; (2) a clerical employee places the NF-10 into an envelope and checks the name and address on the envelope to ensure that it matches the provider's name and address as indicated on the NF-10; and (3) the same clerical employee places the envelope in the outgoing mail bin where it is mailed that same day. If this is all that is necessary, it is a fairly easy standard to meet.

However, recent case law has added the further requirement that a no-fault insurer must establish proof of mailing the NF-10 by "competent evidence." According to these decisions, proof of an office practice or procedure must be established by someone with the "duty . . . to ensure compliance" with the office practices and procedures or with "actual knowledge that they were complied with."[35]

The competent evidence standard represents a significant departure from the three-pronged test described above and places an almost insurmountable burden upon the insurer. The claims examiner is primarily responsible for determining the validity of a claim submitted by the provider and is not typically charged with a duty to "ensure compliance" with the office practices and procedures for mailing the NF-10. Nor can the claims examiner possibly be expected to have "actual knowledge" that those practices and procedures were "complied with."

To satisfy the competent evidence test, the insurer is required to submit two separate affidavits to defeat a provider's motion for summary judgment – in particular, one from the claims examiner setting forth the legal basis and timeliness of the insurer's denial and a second affidavit from the supervisor of the mail room who is responsible for ensuring compliance with the insurer's mailing procedures. This second affidavit must set forth, in detail, the precise procedures followed by the insurer in mailing the NF-10.

Some courts, adopting a more relaxed view of the insurer's burden, have held that although the affidavit submitted by the claims examiner was insufficient to entitle the insurer to summary judgment dismissing the provider's claim, the affidavit nevertheless raised a triable issue of fact as to whether the insurer timely denied the claim sufficient to defeat the motion for summary judgment.[36] These decisions are predicated upon the fact that, in defending a motion for summary judgment, the insurer is only required to show that there are disputed issues of fact.[37]

A stringent application of the common-law test for mailing can have an adverse effect.

Due to the subjective nature of the common-law test for proof of mailing, it is not surprising that the courts have rendered inconsistent decisions on the question of mailing.[38] It is the opinion of the authors that too many otherwise valid denials have been rejected by the courts on the largely trivial issue of the insurer failing to demonstrate proper proof of mailing of the NF-10.[39]

It should also be noted that a stringent application of the common-law test for mailing can adversely affect the medical provider. As part of establishing its prima facie case of entitlement to summary judgment, the provider is required to prove that it mailed the claim to the insurer.[40] Recent decisions have denied summary judgment to medical providers where they failed to submit an affidavit from an officer or employee with knowledge of the standard office practice and procedures for mailing claim forms.[41] Moreover, two other recent decisions have denied a provider's motion for summary judgment where the provider failed to establish proof of mailing of the claim forms by "competent evidence."[42]

Abandonment of the current common-law test for proof of mailing in favor of requiring the insurer to obtain a Certificate of Mailing properly endorsed by the post office when it mails an NF-10 would resolve the problem of inconsistent decisions and provide predictability to the practitioner. Section 313 of the Vehicle and Traffic Law requires a Certificate of Mailing when an insurer mails a notice to the insured canceling a private passenger automobile policy. This requirement provided uniformity to a previously problematic area of the law where courts had been deluged with a multitude of hearings, trials and motions regarding proof of mailing.[43]

A Certificate of Mailing is a document that separately lists the names and addresses of individuals or companies to which items (NF-10s) are mailed. The insurer pays an additional fee of 30 cents in addition to the postage for each item mailed. The clerk at the post office is required to check the names and addresses on the mailing list against the envelopes to ensure that they match. The Certificate of Mailing is then date stamped or endorsed by the postal clerk.

Section 313(1)(b) of the Vehicle and Traffic Law provides that a copy of the notice of cancellation and the Certificate of Mailing, when kept in the regular course of the insurer's business, shall constitute "conclusive proof of compliance" with the mailing requirements. If the same requirement is extended to the no-fault arena, once the insurer produces a copy of the NF-10 and the Certificate of Mailing, it would foreclose all questions relative to the timely mailing of the NF-10. Medical providers should also be required to obtain a Certificate of Mailing when submitting a no-fault claim to the insurer.

Of course, for this to take effect the Legislature would have to amend § 5106 of the Insurance Law and/or the Superintendent of Insurance would have to amend the regulations. Although this will impose an additional cost and administrative burden on the insurer and the provider alike, ample benefits will inure to both. The insurer will have the comfort of knowing that its denial will not be challenged on the largely trivial issue of mailing. The provider, in turn, will know that its claim has been validly submitted, thereby shifting the burden to the insurer to prove the validity of any subsequent denial. ■

1. *See* Shlomo S. Hagler & Aaron H. Hauptman, *First Party No-Fault Benefit Actions*, N.Y.L.J., Oct. 8, 2004, p. 4, col. 4; Karen B. Rothenberg & Jennifer R. Rappaport, *No-Fault – The Litigation Epidemic*, N.Y.L.J., Jan. 5, 2004, p. 4, col. 4.

2. *Mary Immaculate Hosp. v. Allstate Ins. Co.*, 5 A.D.3d 742, 774 N.Y.S.2d 564 (2d Dep't 2004); *Inwood Hill Med., P.C. v. Allstate Ins. Co.*, 3 Misc. 3d 1110(A), 787 N.Y.S.2d 678 (Civ. Ct., N.Y. Co. 2004); *Vinings Spinal Diagnostic, P.C. v. Liberty Mut. Ins. Co.*, 186 Misc. 2d 287, 717 N.Y.S.2d 466 (Dist. Ct., Nassau Co. 2000).

3. *Amaze Med. Supply, Inc. v. Eagle Ins. Co.*, 2 Misc. 3d 128(A), 2003 N.Y. Slip Op. 51701(U) (N.Y. Sup. App. Term 2003).

4. *See Infinity Chiropractic, P.C. v. N.Y. Cent. Mut. Ins. Co.*, 14 Misc. 3d 138(A), 836 N.Y.S.2d 493 (N.Y. Sup. App. Term 2007); *Delta Diagnostic Radiology, P.C. v. Mercury Cas. Co.*, 14 Misc. 3d 138(A), 836 N.Y.S.2d 492 (N.Y. Sup. App. Term 2007); *Delta Diagnostic Radiology v. Allstate Ins. Co.*, 14 Misc. 3d 137(A), 836 N.Y.S.2d 492 (N.Y. Sup. App. Term 2007); *Dan Med. P.C. v. N.Y. Cent. Mut. Fire Ins. Co.*, 14 Misc. 3d 44, 829 N.Y.S.2d 404 (N.Y. Sup. App. Term 2006).

5. *Kings Med. Supply Inc. v. Country-Wide Ins. Co.*, 5 Misc. 3d 767, 783 N.Y.S.2d 448 (Civ. Ct., Kings Co. 2004).

6. N.Y. Ins. Law § 5106(a).

7. 11 N.Y.C.R.R. § 65-3.8 (a)(1).

8. 11 N.Y.C.R.R. § 65-3.5(b).

9. 11 N.Y.C.R.R. § 65-3.6(b). If the insurer fails to issue a follow-up request, any resulting denial would be defective. For example, if an insurer requests that a claimant attend an IME, the insurer is required to send a follow-up notice if the claimant fails to appear at the first IME. *See Vitality Chiropractic. P.C. v. Kemper Ins. Co.*, 14 Misc. 3d 94, 831 N.Y.S.2d 637 (N.Y. Sup. App. Term 2006).

10. 11 N.Y.C.R.R. § 65-3.8(a)(1).

11. *Nyack Hosp. v. State Farm Mutual Auto. Ins. Co.*, 19 A.D.3d 569, 796 N.Y.S.2d 538 (2d Dep't 2005).

12. *Presbyterian Hosp. in the City of N.Y. v. Md. Cas. Co.*, 90 N.Y.2d 274, 660 N.Y.S.2d 536 (1997).

13. *Cent. Gen. Hosp. v. Chubb*, 90 N.Y.2d 195, 659 N.Y.S.2d 246 (1997).

14. *Metro Med. Diagnostics, P.C. v. Eagle Ins. Co.*, 293 A.D.2d 751, 741 N.Y.S.2d 284 (2d Dep't 2002).

15. *Careplus Med. Supply Inc. v. State-Wide Ins. Co.*, 11 Misc. 3d 29, 812 N.Y.S.2d 736 (N.Y. Sup. App. Term 2005); *Fair Price Med. Supply Corp. v. Travelers Indem. Co.*, 9 Misc. 3d 76, 803 N.Y.S.2d 337 (N.Y. Sup. App. Term 2005), *aff'd*, No. 2006-02763, 2007 WL 1704621 (2d Dep't 2007).

16. *Mount Sinai Hosp. v. Triboro Coach, Inc.*, 263 A.D.2d 11, 699 N.Y.S.2d 77 (2d Dep't 1999). It has been held that a "low impact study," accompanied by an affidavit of the technical consultant/accident reconstructionist who prepared the report, is sufficient to raise a triable issue of fact that the assignor's alleged injuries did not arise out of the insured incident. *See A.B. Med. Servs., PLLC v. N.Y. Cent. Mut. Fire Ins. Co.*, 12 Misc. 3d 140(A), 824 N.Y.S.2d 760 (N.Y. Sup. App. Term 2006).

17. *A.B. Med. Servs., PLLC v. Eagle Ins. Co.*, 3 Misc. 3d 8, 776 N.Y.S.2d 434 (N.Y. Sup. App. Term 2003).

18. *Ocean Diagnostic Imaging, Inc. v. Utica Mut. Ins. Co.*, 6 Misc. 3d 131(A), 800 N.Y.S.2d 351 (N.Y. Sup. App. Term 2005); *A.B. Med. Servs., PLLC v. State Farm Mut. Auto. Ins. Co.*, 5 Misc. 3d 138(A), 799 N.Y.S.2d 158 (N.Y. Sup. App. Term 2004).

19. *Ocean Diagnostic Imaging P.C. v. Allstate Ins. Co.*, 6 Misc. 3d 134(A), 800 N.Y.S.2d 351 (N.Y. Sup. App. Term 2005). For an excellent discussion of what an

insurer must demonstrate to establish a defense of fraud, see Shlomo Hagler, *Recent Developments in First-Party, No-Fault Benefit Actions*, N.Y.L.J., Aug 4, 2005, p. 4, col. 4.

20. 10 Misc. 3d 128(A), 2005 N.Y. Slip Op. 51902(U) (N.Y. Sup. App. Term 2005).

21. 12 Misc. 3d 30, 816 N.Y.S.2d 821 (N.Y. Sup. App. Term 2006).

22. 12 Misc. 3d 143(A), 824 N.Y.S.2d 760 (N.Y. Sup. App. Term 2006).

23. *Id.* (citations omitted).

24. 12 Misc. 3d 139(A), 2006 N.Y. Slip Op. 51338(U) (N.Y. Sup. App. Term 2006).

25. *See E. Med. Care P.C a/a/o Erika Pace v. N.Y. Cent. Mutual Fire Ins. Co.*, AAA Case No.: 412006033713.

26. 39 A.D.3d 779, 2007 N.Y. Slip Op. 03636 (2d Dep't 2007).

27. 39 A.D.3d 778, 2007 N.Y. Slip Op. 03635 (2d Dep't 2007).

28. *Nyack Hosp. v. Metro. Prop. & Cas. Ins. Co.*, 16 A.D.3d 564, 791 N.Y.S.2d 658 (2d Dep't 2005).

29. *Williamsbridge Radiology & Open Imaging v. Travelers Indem. Co.*, 14 Misc. 3d 1231(A), 2007 N.Y. Slip Op. 50224(U) (Civ. Ct., N.Y. Co. 2007); *Delta Med. Supplies v. N.Y. Cent. Mutual Ins. Co.*, 14 Misc. 3d 1231(A), 2007 N.Y. Slip Op. 50241(U) (Civ. Ct., Kings Co. 2007); *Bajaj v. Progressive Ins. Co.*, 14 Misc. 3d 1202(A), 2006 N.Y. Slip. Op. 52387(U) (Civ. Ct., N.Y. Co. 2006); *Jacob Nir, M.D. v. Allstate Ins. Co.*, 7 Misc. 3d 544, 2005 N.Y. Slip Op. 25090 (Civ. Ct., Kings Co. 2005).

30. *Kings Med. Supply Inc. v. Country-Wide Ins. Co.*, 5 Misc. 3d 767, 783 N.Y.S.2d 448 (Civ. Ct., Kings Co. 2004).

31. *See* 11 N.Y.C.R.R. § 65-3.8(a)(1).

32. *Damadian MRI in Canarsie, P.C. v. Countrywide Ins. Co.*, 194 Misc. 2d 708, 755 N.Y.S.2d 585 (N.Y. Civ. Ct. Queens Co. 2003).

33. *Nyack Hosp. v. Metro. Prop. & Cas. Ins. Co.*, 16 A.D.3d 564, 791 N.Y.S.2d 658 (2d Dep't 2005).

34. *See Allstate Soc. Work & Psychological Servs. PLLC v. Geico Gen. Ins. Co.*, 6 Misc. 3d 1010(A), 800 N.Y.S.2d 341 (Civ. Ct., Kings Co. 2005); *S & M Supply Inc. v. Geico Ins.*, 2003 WL 21960343, 2003 N.Y. Slip Op. 51192(U) (N.Y. Sup. App. Term 2003); *Residential Holding Corp. v. Scottsdale Ins. Co.*, 286 A.D.2d 679, 729 N.Y.S.2d 776 (2d Dep't 2001).

35. *See Harbor Med. & Diagnostic, P.C. v. Allstate Ins. Co.*, 11 Misc. 3d 1063(A), 816 N.Y.S.2d 696 (Civ. Ct., Queens Co. 2006); *Contemporary Med. Diag. & Treatment, P.C. v. Government Employees Ins. Co.*, 6 Misc. 3d 137(A), 800 N.Y.S.2d 34 (N.Y. Sup. App. Term 2005).

36. *Response Med. Equipment v. General Assurance Co.*, 13 Misc. 3d 129(A), 824 N.Y.S.2d 758 (N.Y. Sup. App. Term 2006); *Chiropractic Neurodiagnosis, PC v. Travelers Indem. Co.*, 11 Misc. 3d 1057(A), 815 N.Y.S.2d 493 (Civ. Ct., N.Y. Co. 2006); *Kings Med. Supply, Inc. v. Hereford Ins. Co.*, 5 Misc. 3d 55, 785 N.Y.S.2d 270 (N.Y. Sup. App. Term 2004).

37. *Sillman v. Twentieth Century-Fox Film Corp.*, 3 N.Y.2d 395, 165 N.Y.S.2d 498 (1957).

38. *E.g., cf., Harbor Med. & Diagnostic, P.C.*, 11 Misc. 3d 1063(A) (insurer's affidavits insufficient to establish that the insurer followed a standard office practice and procedure regarding the mailing of the NF-10) *with Kings Med. Supply, Inc.*, 5 Misc. 3d 55 (affidavit submitted by insurer's adjustor sufficiently set forth "the routine procedure and practice of her office, in the regular course of its business, which indicated that the denial had been duly mailed" to the provider).

39. *See Westchester Med. Ctr. v. AIG*, 36 A.D.3d 900, 829 N.Y.S.2d 180 (2d Dep't 2007).

40. *First Help Acupuncture, P.C. v. Lumbermens Mut. Ins. Co.*, 9 Misc. 3d 1127(A), 2005 N.Y. Slip Op. 51815(U) (Civ. Ct., Kings Co. 2005).

41. *N.Y. & Presbyterian Hosp. v. Allstate Ins. Co.*, 29 A.D.3d 547, 814 N.Y.S.2d 687 (2d Dep't 2006); *Magnezit Med. Care, P.C. v. N.Y. Cent. Mut. Fire Ins. Co.*, 11 Misc. 3d 135(A), 816 N.Y.S.2d 697 (N.Y. Sup. App. Term 2006).

42. *Vista Surgical Supplies, Inc. v. Liberty Mut. Ins. Co.*, 12 Misc. 3d 114, 820 N.Y.S.2d 396 (N.Y. Sup. App. Term 2006); *Gribenko v. Allstate Ins. Co.*, 10 Misc. 3d 139(A), 814 N.Y.S.2d 566 (N.Y. Sup. App. Term 2005).

43. *See Holmes v. Utica Mut. Ins. Co.*, 92 A.D.2d 1045, 461 N.Y.S.2d 549 (3d Dep't 1983); *Felician v. State Farm Mut. Ins. Co.*, 113 Misc. 2d 825, 830–31, 449 N.Y.S.2d 887 (Sup. Ct., Queens Co. 1982).

BY GARY A. MUNNEKE

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Why Practice Management?

Lawyers think of themselves as living in a world apart. The legal profession, with its Socratic method of education, arcane mores, and perquisites of self-regulation, views itself as unique. It is our strength and weakness. Not even doctors have the gall to refer to all those in the population who have not attended medical school as non-doctors. Lawyers perceive themselves as independent professionals, exempt from the laws of commerce and business, impervious to the depredations of economic cycles, and above the rules of the free market where providers of goods and services compete for patrons.

There may have been a time when the practice of law did not require lawyers to understand principles of business management. Private practice was conducted individually and inexpensively. Competition among lawyers and with other professions was limited. It was not difficult for lawyers to earn a comfortable income, attain respect in the community and maintain control of their personal destiny.

Today, however, lawyers must regard the practice of law as a business, inasmuch as they earn their livelihood from the practice of law. The marketplace for legal services is a competitive one; not only has the size of the profession more than quadrupled in the past 50 years, but other professions and businesses have also begun to perform services traditionally restricted to lawyers. For example, accounting firms have encroached on tax litigation, banks in the trusts and estates area, and financial planners in estate planning. In a series of cases, the United States Supreme Court has made it clear that lawyers cannot prevent the development of this competition from both within and without the legal profession.

Furthermore, the technological advances of recent decades have forever changed the way lawyers deliver legal services to clients. If you were to look into a law office circa 1965, and compare it to a law office in 2007, the transformation would be mind-boggling. Hardly any aspect of the office would not have undergone major transformation (from telephones, to computers, to knowledge management systems). Lawyers who fail to understand this evolution cannot hope to succeed in the emerging practice of the future.

My first appreciation of the fact that the practice of law was undergoing a fundamental sea change occurred in 1974 when, scarcely six months out of law school, I attended a conference called "Salvation for the Solo Practitioner." The speakers at that program talked about the delivery of legal services as a cottage industry, where most work was performed piecemeal by individuals, who operated much like tailors, cutting each suit individually. There was consensus among the speakers that lawyers needed to develop systems – routine ways to complete regularly recurring transactions – in order to practice efficiently and profitably. Their message suggested that in order to survive in the future, lawyers needed to change the way they conduct business.

Survive! No one ever told me in law school that the issue was survival – economic survival. No one ever said that anyone who knew how to "think like a lawyer" might fail at the practice of law, or explained the economic realities of practicing law that I would need to know in order to make it in my chosen profession. Students today may have more of a sense that they are entering a competitive environment, but with notable exceptions no one is talking about what they need to do to survive (and even thrive) as practitioners.

Even in 2007, many practitioners seem to approach the future with their heels firmly planted in the past. They either ignore the changes that are transforming the practice of law or they react slowly and resentfully to the evolving professional landscape. In truth, lawyers of all ages and experience levels deal with changes in the legal profession and society every day. Some just try to survive, while others try to excel by staying ahead of the curve.

The practice of law in the United States is a multibillion-dollar industry, indispensable to the functioning of modern society. The delivery of legal services by lawyers to the people they represent is fundamental to the process of dispute resolution, and ultimately to the legitimacy of the justice system in this country. Although the law itself

is constantly changing, a truth that all lawyers and law students implicitly understand, the fact that the practice of law is constantly evolving may be under-appreciated by those in the business of delivering legal services. Certainly, longtime practitioners will readily admit that practice has changed over the course of their careers, but most have not stopped practicing long enough to examine the implications of change on their day-to-day work. If anything, most practicing lawyers are reactive rather than proactive.

Actually, most lawyers are ill-equipped to run a business organization efficiently and profitably. Some of this is due to self-selection. If most of us had wanted to go into business, we would have gone to business school. Instead, we made a conscious decision to practice law, only to find out when we graduate that we have to run a business in order to pursue our chosen career.

Some critics charge that lawyers are greedy, and that money clouds lawyers' professional judgment. In reality, most lawyers work hard and expect a fair return on their investment, but very few get rich practicing law and fewer still are outright crooks. If a law firm can provide legal services more efficiently, both clients and lawyers will benefit through lower costs for the services and a better return to the providers.

Disciplinary authorities confirm that lawyers who get into trouble over financial matters often are experiencing economic difficulties that tempt them to cut corners or take other inappropriate actions. Thus, it should not be too much of a stretch to say that a well-run legal business is also likely to be a professional practice.

One of the reasons that lawyers are not prepared for the business aspects of practicing law is that their legal education does not adequately prepare them for the business of practicing law. The law school curriculum is heavily weighted in favor of teaching a vast amount of substantive information and developing a narrow range of legal skills through a traditional pedagogical framework based upon the so-called Socratic method, euphemistically referred to as "learning to think like a lawyer." This approach would have been unrecognizable to Socrates, but more important, it has very little in common with the actual work of lawyers. It is sometimes said that recent bar examinees know more law and less about what to do with it than anyone in the profession.

Many legal educators are re-examining the structural, traditional notions and approaches to the legal education and preparation of lawyers. The traditional framework of legal education remained relatively unchanged for generations, but the changing realities of law practice and society have forced legal educators to re-think some of their basic assumptions. Law schools today universally offer clinical and lawyering skills courses, and individual professors are experimenting with different teaching methods in traditional courses.

In 1991, the *Report of the American Bar Association Task Force on Legal Education and the Profession: Narrowing the Gap* (also known as the MacCrate Report) described a set of fundamental lawyering skills and values necessary to professional success. These skills and values are acquired over a continuum of experience beginning long before law school and continuing throughout one's professional career. Although reasonable minds might differ over what skills should be included in this list, or the relative importance of certain skills compared to others, the basic idea that practicing law requires the application of some set of professional skills is hard to escape. Included in this list of fundamental lawyering skills was a skill identified as "organization and management of legal work." More recently, the ABA

amended its *Standards for the Approval of Law Schools* to incorporate a requirement that all law schools "shall require that each student receive substantial instruction" in management and organization of legal work.

The proposed New York Rules of Professional Conduct define "competence" in Rule 1.1 as "legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation." This Rule demonstrates that professional competence requires more than knowledge of the law. Knowledge, without the skill to apply it, is a hollow quality. In more practical terms, if practicing lawyers cannot skillfully use their knowledge for the benefit of clients, they bring little value to society and will not succeed financially.

The MacCrate Report, the ABA *Standards for Approval of Law Schools*, and the proposed ethics rules all recognize that competence as a lawyer goes far beyond the ability to "think like a lawyer." Although competence is a complex concept, "organization and management of legal work" is one of the core skills of lawyering. Legal educators and practitioners sometimes point fingers at each other for not doing enough to prepare lawyers for the practice of law. In truth, the responsibility for teaching new lawyers the basic skills and knowledge necessary to practice competently is a shared obligation.

Professional skills are critical to successful lawyering, and practice management is one of the critical skills. As lawyers, we must recognize that we are not prepared for the business side of law practice by education, experience or inclination. At the same time, in order to succeed in our chosen profession, we need to possess the business acumen to deliver the legal work product to our clients consistent with their expectations for quality service and the professional standard of care.

For the past 20 years, I have taught a course at Pace Law School called Law Practice Management, which aims to integrate the skills associated with managing a practice professionally into the education of students before they enter – ill-equipped – the practice of law. It is time for other law schools to recognize that they have a responsibility to teach all their students the fundamental skill of law practice management. And it is time for the organized bar to insist that all lawyers know how to manage a law practice, because more professional error is caused by management error than any other reason.

Management principles have been addressed in the literature of many fields, outside of law, in business and industry, where thinking about how to improve efficiency and productivity is a central concern. Managers and executives in most large companies and many small ones study business in college, and those who did not receive business degrees during their undergraduate education often return to graduate business programs for MBAs or other advanced degrees. Over the years, academics in business schools have provided an intellectual framework for management by conducting research and writing on how organizations work.

Business schools have explored the management of professional services firms for generations. The literature, both academic and popular, surrounding the science of management is both extensive and sophisticated, yet ignored by most lawyers. Publications such as the *Harvard Business Review*, and other academic journals, are replete with case studies of professional service firms in general and law firms in particular.

We can learn from our colleagues in the business world. Despite the myriad changes facing the legal profession, the basic principles of effective law practice and office management, strategic planning, and organizational systems are not novel. Dwight McCarthy in 1927, Reginald Heber Smith in 1942, and a number of other legal writers since have articulated a variety of themes that recur in present day law practice. Despite rapid changes in technology and other aspects of practice, many of the basic principles of sound management have not changed over the years.

As the French say, *Toujours le change; toujours le même*. Lawyers have always had a need to know how to manage the business side of the practice, and probably have always been as uncomfortable with the demands of that side of their work as they are today. Why practice management? The simple answer is because we must, in order to survive in a competitive marketplace, to thrive economically and to sustain professional standards in the practice of law. ■

The literature, both academic and popular, surrounding the science of management is both extensive and sophisticated, yet ignored by most lawyers.

"Point taken. There's no need to get all constitutional on me."

ATTORNEY PROFESSIONALISM FORUM

To the Forum:

I read with great interest your Forum each month in the *Journal*. Thus far, the questions have dealt with specific fact situations where professionalism issues arise. That is all well and good and provides useful guidance. However, I would like to hear your thoughts on the general problem of lawyer bashing, particularly in the media. There are a whole lot of really good lawyers out there.

Sincerely,
Frustrated in Fredonia

Dear Frustrated:

"First you kill all the lawyers." That oft-repeated line from Shakespeare has been used as a mantra by those who view members of the legal profession as slick characters concerned only with collecting large fees, winning cases on hyper-technicalities, and manipulating the law to their clients' advantage. In fact, that so very misused passage from *Henry VI* was said as part of a plan to throw aside the court system, dismantle social institutions, and create anarchy. It seems that in Shakespeare's day, just as now, lawyers were viewed as the guardians and gatekeepers of justice.

But, fast forward to the 1990s, and beyond. We've weathered the O.J. and the McDonald's coffee cases, and, more recently, the paternity suit over Anna Nicole Smith's baby daughter. The media have been saturated with "extra-ordinary" lawyers taking on these "extra-ordinary cases," and the many, many lawyers participating in the seemingly endless and mind-numbing commentaries. Yet, gratefully, this is only a snapshot of the legal profession.

We have had little opportunity to see or hear about the "ordinary" lawyers who every day, day after day, diligently and quietly give devoted, competent and trustworthy service to their clients. These are the attorneys who unravel the mysteries of our tax, trust and health laws to assist senior citizens terrified of losing their lifetime savings to health and custodial care costs. These are the attorneys who assist penniless entrepreneurs in setting up new businesses. These are the attorneys who generously volunteer their time to represent the poor and the homeless. These are the attorneys who zealously, for little or nothing when assigned by the court, defend people accused of criminal acts. And yes, as much as some of us may not understand or like it, these are the attorneys who help ensure that even the "guilty" are not denied their inalienable rights to due process, rights that protect us all.

Lawyers have not lately embraced service and duty. Their efforts are steeped in a long-standing tradition of the bar. More than two centuries ago, 24 of the signatories to our Constitution, men of position and financial means – and lawyers – risked it all in the name of justice and liberty. These "ordinary" lawyers were hounded, tortured, their properties seized, they were left penniless – all for putting principle before convenience.

Current public attitude toward both lawyers and the justice system is as contradictory, inconsistent and often mercurial as the public attitude is toward every other institution. Examine any one of the myriad polls and studies taken over the past decade, and you can find one that confirms your personal bias, from: *I am very satisfied with my own lawyer, but distrust all others;* to: *I distrust all of them*. Why is it that we do not see TV news clips about the many thousands of lawyers who collectively donate millions of hours each year to represent the poor and disadvantaged? Why is it that we hardly ever see in print a feature about all those lawyers who serve pro bono as directors of hospitals, scouts, United Ways, colleges, museums, orchestras, and cancer, kidney, and other nonprofit health-related organizations and foundations? Why is it that we never hear radio commentators talk about lawyers who perform legal work, at no charge, for their churches, synagogues and mosques? No other professional group is more collectively generous with its time than the legal profession.

Perhaps it's the byproduct of living in a jaded, fearful, and skeptical age. Perhaps it's a barometer that tells us that in a time of communication overload it's just too convenient, too easy, to make instant judgments and wholesale indictments of any group based on sound bites and media "snapshots."

Despite our best efforts, we will never be able to convince the small minority of "bad guys" in the profession to clean up their act. We also will not be able to convince every reporter and TV commentator that the overwhelming majority of our colleagues are decent, hard-working, admirable and concerned professionals. However, we will continue to insist on a fair hearing from the media.

But, no matter. While we cannot ensure that every person, regardless of ability to pay, will always receive adequate legal representation, we will continue our efforts on behalf of the

The Attorney Professionalism Committee invites our readers to send in comments or alternate views to the responses printed below, as well as additional hypothetical fact patterns or scenarios to be considered for future columns. **Send your comments or questions to: NYSBA, One Elk Street, Albany, NY 12207, Attn: Attorney Professionalism Forum, or by e-mail to journal@nysba.org.**

This column is made possible through the efforts of the NYSBA's Committee on Attorney Professionalism. Fact patterns, names, characters and locations presented in this column are fictitious, and any resemblance to actual events or to actual persons, living or dead, is entirely coincidental. These columns are intended to stimulate thought and discussion on the subject of attorney professionalism. The views expressed are those of the authors, and not those of the Attorney Professionalism Committee or the NYSBA. They are not official opinions on ethical or professional matters, nor should they be cited as such.

public. We will seek to reform the justice system as needed, to make positive changes in the way our profession functions, to advocate in the best interests of our clients, and – even when our efforts are not appreciated – to defend the rule of law, and support an independent judiciary.

The Forum, by
Miriam M. Netter
Member, NYSBA Committee on Attorney Professionalism
Subcommittee on Attorney Professionalism Award
Delmar, N.Y.

In January of 2008, our organization will present its 9th Annual Attorney Professionalism Award. With this award we honor one among us who has demonstrated outstanding service to clients, a commitment to promoting respect for the legal system in pursuit of justice and the public good, exemplary ethical conduct, good judgment, integrity and civility, Past winners of the Award are: Barry Kamins, Brooklyn (2000); Lucille A. Fontana, White Plains (2001); Carlton F. Thompson, Binghamton (2002); Anne Reynolds Copps, Albany (2003); James M. Conboy, Albany (2004); George J. Nashak, Jr., Glendale (2005); Terrence M. Connors, Buffalo (2006); Frank E. Yannelli, Garden City (2007).

QUESTION FOR THE NEXT ATTORNEY PROFESSIONALISM FORUM:

I am the managing partner of a fairly large firm in New York City. As if meeting associates' sharply rising salary expectations is not enough, we have a challenging new issue facing us.

Increasingly, we are being pressured by important and longstanding clients to meet certain "diversity targets" as a condition for continuing to represent them. Clients are demanding that the racial, gender and ethnic composition of our firms' associates and partners more closely mirror the profession's diversity. Others require that our engagement teams on their matters reflect diversity in a meaningful way, with minority and women lawyers having important roles to play at all levels. We are required to fill out detailed questionnaires and disclose information that, frankly, is of a proprietary nature: where we recruit, how many white and minority candidates we interview and hire, etc.

At the same time, we are facing client pressures from another direction. At least one government official has suggested that clients exert their economic influence by pulling back their work from law firms doing pro bono work for the Guantanamo detainees.

These actual and suggested demands by our clients – to whom we owe a duty of loyalty and whose business we both want and need – about who we are and what we do apart from our representation of them, raise troubling issues that challenge our independence as professionals. What advice do you have for us?

Sincerely,
A Besieged Firm Leader

Continued from Page 64

yers who write to or for New York State courts.

The Bluebook is wrong about official citations. The Bluebook tells users to cite the unofficial N.E.2d for Court of Appeals cases instead of the official N.Y.3d. It also tells users to cite the unofficial N.Y.S.2d instead of the official A.D.3d or Misc. 3d for decisions from other courts. An example from The Bluebook is *Palsgraf v. Long Island Railroad Co.*, 162 N.E. 99 (N.Y. 1928).[9] Why The Bluebook favors the unofficial reports is a mystery. Unofficial reports are often inaccurate, and New York requires official citations for decisions appearing in the Official Reports and in practitioners' appellate papers.[10]

The Bluebook is also wrong about parallel citations and what New York's "local" rules demand. The Bluebook properly directs that "[i]n documents submitted to state courts, all case citations should be to the reporters required by local rules."[11] The Bluebook correctly refers its readers to Table BT.2, which commendably cites the Tanbook, the CPLR, and Court of Appeals and Appellate Division rules as the sources of New York's local rules.[12] But The Bluebook gets it wrong from there. The Bluebook explains that "[l]ocal rules often require citation to both the official state reporter *and* the unofficial regional and/or state-specific reporter"[13] and cites *Kenford Co. v. County of Erie*, 73 N.Y.2d 312, 537 N.E.2d 176, 540 N.Y.S.2d 1 (1989),[14] as an example of the supposed New York local rule requiring parallel citations.

That rule doesn't exist. According to the CPLR and New York court rules, parallel citations to New York cases aren't required for New York lawyers. Nor are they helpful to New York judges, who rely, and properly so, on official citations only. As the 2007 Tanbook explains, "Parallel unofficial citations are not used for officially reported New York State cases."[15]

The Bluebook is wrong, moreover, in directing writers to cite New York's intermediate courts' departments or districts only when that information "is of particular relevance."[16] The Bluebook cites as examples *Schiffman v. Corsi*, 50 N.Y.S.2d 897 (Sup. Ct. 1944), and *Schiffman v. Corsi*, 50 N.Y.S.2d 897 (Sup. Ct. N.Y. County 1944).[17] Both the rule and the examples are wrong. Legal writers should always give the department or district, for intermediate appellate courts and for trial courts, to tell readers whether the authority is binding or persuasive and, if persuasive, how persuasive. Additionally, The Bluebook's citation to *Schiffman* isn't from an intermediate appellate court, like New York's Appellate Division or Appellate Term. It's from a court of first instance: Supreme Court, Special Term. And *Schiffman* really does have intermediate appellate history. The Bluebook should have given this citation: *In re Schiffman v. Corsi*, 182 Misc. 498, 50 N.Y.S.2d 897 (Sup. Ct. N.Y. County), *aff'd mem. sub nom. In re Schiffman v. Murphy*, 268 App. Div. 765, 50 N.Y.S.2d 132 (1st Dep't 1944), *rev'd sub nom. Schiffman v. Corsi*, 294 N.Y. 305, 62 N.E. 81, *cert. denied*, 326 U.S. 744 (1945).

The Bluebook continues to be wrong about the New York Law Journal. The Bluebook offers two ways to cite the Law Journal. Both are wrong. In one place, The Bluebook tells us that the Law Journal publishes opinions from the federal district court in Massachusetts and that dates of decision, in addition to publication dates, are available for citing. Neither is true. The Bluebook example is *Charlesworth v. Mack*, N.Y. L.J., Dec. 5, 1990, at 1 (D. Mass. Dec. 4, 1990).[18] Sixty-one pages later, The Bluebook contradicts itself — it gives a consecutively paginated way to cite the Law Journal (124 N.Y. L.J. 1221 (1950)) that will allow no one to find the reference.[19]

The New York Rules of Citation

The only way for New York lawyers to use The Bluebook is to fix it with the New York Rules of Citation, published by St. John's University School of Law. Now in its fifth edition, revised in late 2005 to incorporate The Bluebook's eighteenth-edition revisions, the Rules of Citation explains The Bluebook's deficiencies and tells lawyers, law students, and law-journal editors how to correct them. If you must use The Bluebook, combine it with the Rules of Citation. The Rules of Citation is prepared by St. John's law librarian William H. Manz, who also wrote Gibson's New York Legal Research Guide (3d ed. 2004), which dedicates many pages to comparing Bluebook, ALWD, and Tanbook citing.

New York judges who want to publish their opinions in the Official Reports must cite Tanbook-style.

ALWD

The ALWD citation manual is designed by legal-writing experts to substitute for the inordinately complex Bluebook. ALWD has succeeded in its mission: It's much easier to use than The Bluebook. For example, it eliminates the unnecessary distinction between citing for law reviews and law journals and citing in practitioners' legal documents.

Experts doubt whether ALWD will ever rival The Bluebook in popularity. The subtle distinctions in citing between ALWD and The Bluebook are noticeable to experienced practitioners and recent graduates from law review and moot court. They will assume that those who cite ALWD-style don't know how to use The Bluebook.

In terms of New York citations, ALWD, in its third edition, is a vastly

improved product. In its first edition, every ALWD example for New York law was wrong. ALWD now refers its New York readers to the Tanbook.[20] For its national readers, ALWD still makes too many mistakes about New York. In one place, ALWD, like The Bluebook, uses unofficial citations instead of official citations and tells writers to add "App. Div.," even though all New Yorkers know that "2d Dept." means the Appellate Division: 634 N.Y.S.2d 740 (App. Div. 2d Dept. 1995), *aff'd*, 679 N.E.2d 1035 (N.Y. 1997).[21] Later, ALWD, in its parallel-citing section, omits the "App. Div." reference: *People v. Glanda*, 18 A.D.3d 956, 794 N.Y.S.2d 712 (3d Dept. 2005).[22]

ALWD also errs the one time it gives an example of a rule. Calling New York's ethics rules a "uniform law," ALWD offers this citation: "N.Y. Code of Prof. Resp. DR 4-101(c)(2) (1999). [New York version of the Model Code of Professional Responsibility DR 4-101(c)(2)]."[23] This is all wrong. New York has not adopted the Model Code. And if one cites DR 4-101(c)(2), one must also add its 22 NYCRR parallel citation, because the Code of Professional Responsibility is binding only to the extent that the departments of the Appellate Division have adopted it. The correct way to cite the rule according to the Tanbook: (Code of Professional Responsibility DR 4-101 [c] [2] [22 NYCRR 1200.19 (c) (2)].).

2007 Tanbook Revisions

The 2007 Tanbook re-works the 2002 edition, which itself was updated by some amendments in 2004.[24] It's the best Tanbook yet. In her foreword to the Tanbook's 2002 edition, Chief Judge Judith S. Kaye wrote that the 2002 changes, encouraging "clearer, cleaner, more readable" legal writing, "ma[de] my heart jump with joy."[25] The Chief Judge's 2007 foreword explains that the current revision — she calls it "updating" — "is more akin to filling crevices than bridging chasms . . . . Always the movement, happily, is toward more readable text."

Revisions for 2007 include rules requiring writers to add years of decision to case-law authority, eliminating "supra" usage, and new rules aiding writers' use of electronic formats and making it easier to quote. The 2007 Tanbook offers new abbreviations, fewer capitalizations, and excellent guidance on gender-neutral writing and writing in plain English, such as avoiding Latinisms and legalisms. It also offers advice on reducing excessive hyphenation and italics. The 2007 revisions incorporate revisions from 2004, including eliminating asterisks "* * *" in favor of ellipses ". . ." and forbidding commas after signals like "see" and "contra."

The 2007 Tanbook still includes two relics: Citations surrounded by disconcerting parentheses and brackets. The original view was that citations should be placed into but set off from the text. Parentheses and brackets satisfied that mandate. Today they are an anachronism, included, perhaps, only because the LRB must change citation usage incrementally, not wholesale. Another problem with the Tanbook is that it gives writers too much discretion in citing cases and secondary authority. Writers and readers want and need to be told what to do. As lawyers, we are confused when we have too many choices.[26] That discretion includes whether a citation will be part of the sentence or a separate sentence.

Despite the Tanbook's relics and excessive permissiveness, New York lawyers, trained in The Bluebook and, increasingly, ALWD, would be smart to keep the 2007 Tanbook on their desks. The 2007 Tanbook is user-friendly in organization. It is accurate and comprehensive in legal research. It is progressive and informative on usage and style. It's the best of the options by far. It's for New Yorkers, by New Yorkers.

Some say you get what you pay for. Not so the 2007 Tanbook, available for free online. Other than the LRB's free online case-law publication service, it's the best free legal resource in New York.

> New York lawyers, at their best when they make it easy for judges to rule for their clients, should cite Tanbook-style.

In the next issue, the Legal Writer will continue with its series on Legal Writing Do's, Don'ts and Maybes. ■

1. Compounding the problem is that many publications use their own citation systems. These publications include all State Bar publications, such as the *Journal*. State Bar publications use their own Bluebook variant. *See* http://www.nysba.org/Content/NavigationMenu/Publications19/Bar_Journal/Article_Submission22/Article_Submission.htm (last visited Aug. 14, 2007). Everyone, it seems, wants to set a different uniform citation method, including the American Association of Law Libraries, which has developed its Universal Citation Guide for courts designing medium-neutral citation schemes, or citation schemes that cite print and electronic sources the same way and which cite to paragraphs, not pages. *See* http://www.aallnet.org/committee/citation/ucg/index.html (last visited Aug. 14, 2007) (offering prior Universal Citation Guide version 2.1).

2. *See* http://www.legalbluebook.com (last visited Aug. 14, 2007).

3. ALWD is so-named because it's written by the Association of Legal Writing Directors and Darby Dickerson, Stetson University College of Law's dean. *See* http://www.alwd.org/publications/citation_manual.html (last visited Aug. 14, 2007). ALWD is published by Aspen Publishers, which has a helpful Web site that offers charts, appendixes, and updates. *See* http://www.alwdmanual.com/books/dickerson_alwd/default.asp (last visited Aug. 14, 2007).

4. Competing for the moniker "Tanbook" is LexisNexis's New York Landlord-Tenant Law (Tanbook), currently in its 2007 edition.

5. For the Law Reporting Bureau's Web site, go to http://www.nycourts.gov/reporter (last visited Aug. 14, 2007). The LRB's editors who prepared the 2007 Tanbook are Gary Spivey, the State Reporter, and Charles A. Ashe, William J. Hooks, Michael Moran, Katherine D. LaBoda, Chilton B. Latham, Kathleen B. Hughes, and Cynthia A. McCormick.

6. *See* http://www.nycourts.gov/reporter/Decisions.htm (last visited Aug. 14, 2007).

7. Tanbook Preface at v.

8. ALWD Appendix 2, at 425 (citing 2002 Tanbook and quoting Gerald Lebovits, *New Edition of State's "Tanbook" Implements Extensive Revisions in Quest for Greater Clarity*, 74 N.Y. St. B.J. 8 (Mar./Apr. 2002)).

9. Bluebook Rule B5.1.5, at 11. This cite also contradicts Bluebook rules. "Railroad" must be abbreviated as "R.R." Bluebook Rule T.6, at 336.

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LANGUAGE TIPS

BY GERTRUDE BLOCK

Question: On the op-ed page of the *Boston Globe*, in an article about presidential privilege, the verb *flaunt* seems to have been mistakenly used to mean *flout* in the sentence, "Flaunting subpoenas is not permitted." What is your opinion?

Answer: Unless the White House adviser was waving the subpoenas from the windows of the White House, the correct verb is *flout*. The verbs *flaunt* and *flout* are often used incorrectly and interchangeably, but the op-ed writer probably knows the difference now, after hearing from numerous *Globe* readers. Both *flaunt* and *flout* are transitive verbs (that is, they require a direct object to complete their meaning), but the similarity ends there. The verb *flaunt* means "exhibit ostentatiously, show off," as in, "He flaunted his knowledge of Greek philosophy." The verb *flout* means, "openly and ostentatiously scorn," as in, "The president flouted Congress's demands."

When words that look alike differ in meaning, they are often mistaken as synonyms. If that happens often enough, one of the two words disappears. This is happening with the adjectives *disinterested* (which means "objective or unbiased") and *uninterested* ("not interested").

Because *disinterested* has come to mean *uninterested*, the word *uninterested* is disappearing from the language, and the word *disinterested* has lost its original meaning, which seems a pity.

Similarly, the verb *lend* has virtually disappeared. The noun *loan* has become popular as a verb as well as a noun, so there is no longer a need for an exact synonym in *lend*. Several more pairs could be cited, among them the intransitive verb *lie*. Almost exclusively, we now *lay* down instead of *lie* down, but neither of those losses are – in my opinion – worth bemoaning. Comments, readers?

Question: I am the secretary of the founding partner of a New York law firm. He is old-fashioned and set in his ways about language. For example, he insists that the word "problematic" means "questionable," not "a problem." I worry that he will be misunderstood by his clients. He reads your columns, so perhaps you can straighten him out.

Answer: Although you are right that *problematic* means "a problem," so is your boss, because the adjective *problematic* can mean either "questionable" or "a problem." The original meaning of *problematic* is the one your boss insists on, but as you say, he is likely to be misunderstood because the newer meaning, "a problem," is widely used.

To explain why *problematic*, a word that looks like *problem*, originally meant "questionable" involves an explanation of the etymology of the English language through the years. The English noun *problem* is derived from the Greek verb *probaillein*, which meant "to throw or put forward." Then *probaillein* became the Greek noun *problēma*, which meant "projection, or projecting wall." The noun was adopted into Latin as *problema*, and then during or before the 11th century became the Middle French noun *probleme*.

The noun *problem* came into Middle English in 1066, introduced by French invaders under William, Duke of Normandy, who was determined to become the successor of the childless Edward the Confessor by thwarting the newly elected king Harold. The story is that during a crucial battle, Harold was pierced in the eye by a Norman arrow, and when the English retreated, having lost their leader, William the Conqueror pillaged and burned villages in the south of England, wiped out the English nobility, and conquered England.

For the ensuing 200 years, the language of the English upper classes was French, and although the language of the English masses was eventually restored, the many French borrowings greatly enlarged the English wordstock, changing it forever.

The word *problem*, having dropped its final *e* is one of those borrowed words. It is not clear when *problem* gained its present figurative meaning, but words typically come into a language with their literal meaning, adding figurative meanings after they become popular. So *problēma*, the Greek "protecting wall," eventually became a figurative type of protection, "an excuse." From "excuse," it was a short step to the earliest (now obsolete) meaning of *problem*: "a formal public disputation based on a question proposed for academic discussion."

Problem still means "a question raised for inquiry, consideration, discussion, decision, or solution." It also means "an unsettled question that demands a solution." In chess, a *problem* "is a certain constructed position in which a specified result – perhaps checkmate – is to be accomplished in a specific number of moves." In Logic, *problematic* is "a proposition that enunciates or supports what is not necessarily true," as in "a problematic judgment about the existence of unicorns."

So when your boss insists that *problematic* means "questionable," he is no doubt thinking of that last definition. But the average English speaker is not. Influenced by the resemblance of *problematic* to the word *problem*, the average person almost certainly thinks of a *problem* as a "difficulty." If you explain the etymology of the noun, perhaps your boss will change his mind.

The etymology of the word *problem* is continuing. As I have noted previously in this space (under the heading "Where have all our problems gone?"), Americans seem to be substituting the noun *issue* as a euphemism for *problem*. The word *issue*, whose meaning has, until recently, been "a question which, when resolved, will solve a problem," has now become the *problem* itself. ■

Gertrude Block is lecturer emerita at the University of Florida College of Law. She is the author of *Effective Legal Writing* (Foundation Press) and co-author of *Judicial Opinion Writing* (American Bar Association). Her most recent book is *Legal Writing Advice: Questions and Answers* (W. S. Hein & Co., 2004).

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10. *See, e.g.*, *Disenhouse Assocs. v. Mazzaferro*, 135 Misc. 2d 1135, 1137 n.*, 519 N.Y.S.2d 119, 120 n.* (Civ. Ct. N.Y. County 1987) (urging attorneys not to cite "the unofficial reports only") (citing CPLR 5529(e), which provides that in their appellate briefs, attorneys who cite New York cases must cite the Official Reports, if available); *People v. Matera*, 52 Misc. 2d 674, 687, 276 N.Y.S.2d 776, 789 (Sup. Ct. Queens County 1967) ("[W]e are required, in the rendition of our opinions, to cite New York decisions from the official reports, if any, as the counsel themselves are bound to do in their briefs on appeal.").

11. Bluebook Rule B5.1.3, at 9 (bold omitted).

12. *Id.* Rule BT.2, at 38.

13. *Id.* Rule B5.1.3, at 9 (emphasis in original).

14. *Id.*

15. Tanbook Rule 2.2 (b)(1), at 14.

16. Bluebook Rule 10.4(b), at 90.

17. *Id.*

18. *Id.* Rule 10.1, at 80.

19. *Id.* Rule 16.5(c), at 141.

20. *See supra* text and accompanying note 8.

21. ALWD Rule 11.3(g), at 56.

22. *Id.* Rule 12.4(d)(3)(g), at 82.

23. *Id.* Rule 27.4(f), at 243.

24. The 2002 Tanbook, accessible in HTML and PDF versions, is found at http://www.courts.state.ny.us/reporter/Styman_Menu.htm (last visited Aug. 14, 2007). It is reviewed and compared to The Bluebook (17th ed. 2000) and ALWD (1st ed. 2000) in Lebovits, *supra* note 8.

25. Tanbook Foreword at iii.

26. An earlier Bluebook competitor, The University of Chicago's Maroonbook, failed because it offered too much discretion. Bryan A. Garner, *Practice Strategies: Legal Writing, available at* http://www.abanet.org/genpractice/newlawyer/2003/nov/strategies2.html (last visited Aug. 17, 2007) (discussing The Bluebook, ALWD, New York's Tanbook, and other citation schemes). The Tanbook's built-in audience and team of experts who keep it current will assure its success.

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Larose, Stuart J.
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McClusky, James P.
Mitchell, Richard C.
Pellow, David M.
Peterson, Margaret Murphy
Priore, Nicholas S.
Richardson, M. Catherine
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Giorgio, Frank, Jr.
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Walsh, Owen B.
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Dietz, John R.
Goldblum, A. Paul
Haskel, Jules J.
James, Seymour W., Jr.
Leinheardt, Wallace L.
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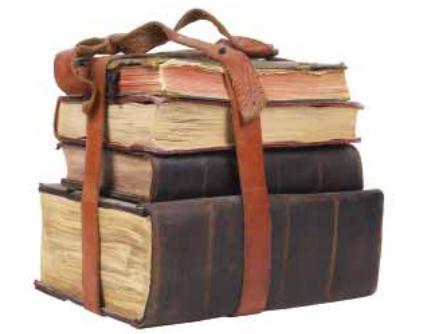
BY GERALD LEBOVITS



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