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To Talk, or Not to Talk . . . That is the Question: Communications with Potential Class Members



I. Introduction.

Defendants involved in class-action litigation often overlook a potentially invaluable resource: the potential class members. When faced with class actions, it may be in a defendant's best interest to reach out to potential class members to garner information, negotiate settlements, or otherwise investigate the case. But many defendants fail to involve potential class members in their fact-finding efforts due to fear of reprisals from the court. This can be a significant oversight because valuable information may be obtained by communicating with potential class members.

This article discusses the legal and ethical considerations applicable to contact with absent class members.

II. Formal discovery versus informal communications.

Courts are generally hesitant to order formal discovery from unnamed class members. A defendant seeking formal discovery from unnamed class members prior to certification generally must make a showing of need. *Manual for Complex Litigation*, (3d ed.) ¶ 21.14 (1995). One of the underlying goals of class actions is to promote judicial economy by allowing a single party to represent others who share a common interest but whose joinder is unmanageable. Requiring potential class members—who likely were completely uninvolved in the decision to bring the suit—to respond to formal discovery may be seen by the court as invasive. Courts may be reluctant to force absent class members to answer interrogatories or be deposed.

This fact often leads defense attorneys to believe that no information may be obtained from potential class members. But the key distinction is the invasiveness and burden formal discovery may be viewed as imposing on potential class members. As opposed to noticing someone for a deposition, procuring information through voluntary informal communications is minimally intrusive and may be terminated at the discretion of the class member. Indeed, it may be appropriate to memorialize such information in an affidavit. Because cooperation is at the discretion of the class member, informal discovery does not pose the burdens associated with formal discovery. As such, court approval is not necessarily needed to informally communicate with class members. Defendants should strongly consider using such informal discovery methods.

III. Communications with potential class members are legal and ethical.

In *Gulf Oil Co. v. Bernard*, the United States Supreme Court addressed whether parties in an uncertified class action could communicate with

potential class members. *Gulf Oil Co. v. Bernard*, 452 U.S. 89 (1981). The Court stated that, although a district court has the authority to limit certain communications to prevent frustration of the policies embodied in class-action rules, the district court “may not exercise the power without a specific record showing by the moving party of the particular abuses by which it is threatened.” *Id.* at 102. The Court further noted that any restrictive order should be narrowly tailored to address specific abuses and should clearly identify those abuses. In compliance with *Gulf Oil*, courts have routinely recognized that parties attempting to restrict another party’s communication with potential class members must present an evidentiary showing of actual or threatened abuse by the party sought to be restrained. See, e.g., [Payne v. Goodyear Tire & Rubber Co.](#), 207 F.R.D. 16, 20 (D. Mass. 2002); [Jenifer v. Del. Solid Waste Auth.](#), No. Civ. A.98-270MMS, Civ. A.98-565MMS, 1999 WL 117762, at *4 (D. Del. Feb 25, 1999).

More recently, the American Bar Association Committee on Ethics and Professional Responsibility issued a formal opinion on April 11, 2007, titled “Contact by Counsel with Putative Members of Class Prior to Class Certification.” ABA Comm. on Ethics and Prof’l Responsibility, Formal Op. 07-445 (April 11, 2007). The Committee, recognizing the majority rule, stated, “putative class members are not represented parties for purposes of the Model Rules prior to certification of the class and the expiration of the opt-out period.” ABA, Op. 07-445, at 3 (emphasis added).

Because potential class members are not represented, both plaintiffs’ and defense counsel are governed by the Model Rules of Professional Conduct Rule 4.3, which addresses communications with unrepresented persons. Plaintiffs’ counsel’s right to contact potential class members is also subject to the limits on communicating with prospective clients under Rule 7.3. Rule 4.3 does not limit factual inquiries, but rather requires attorneys to refrain from giving legal advice other than the advice to engage counsel, if necessary. *Id.* at 5-6. The pertinent section of Rule 4.3 provides, “[t]he lawyer shall not give legal advice to an unrepresented person, other than the advice to secure counsel, if the lawyer knows or reasonably should know that the interests of such person are or have reasonable possibility of being in conflict with the interests of the client.” The information sought from potential class members may include facts that are relevant to class certification. *Id.* at 5.

To avoid the issuance of a protective order, parties must not engage in activities that are abusive of class-action rules or coercive in nature. Practices that have been found sufficient to warrant protective orders include communications that coerce prospective class members into excluding themselves from the litigation; see, e.g., *Payne*, 207 F.R.D. at 21 (discussing other cases in which courts found that a defendant’s ex parte communication with class members was coercive where the defendant was seeking to encourage opt-outs); communications that contain false, misleading, or confusing statements; see, e.g., [Basco v. Wal-Mart Stores, Inc.](#), No. Civ.A. 00-3184, 2002 WL 272384, at *3 (E.D. La. Feb. 5, 2002); and communications that undermine cooperation with or confidence in class counsel; see [Hampton Hardware, Inc. v. Cotter & Co.](#), 156 F.R.D. 630, 632 (N.D. Tex. 1994). However, the “mere possibility of abuse” is insufficient to support a ban on communications. *Gulf Oil*, 452 U.S. at 104. Also, there is no requirement that the communications be “objective and/or neutral.” *Babbitt v. Albertson’s*, No. 92-1883, 1993 WL 150300, at *3-4 (N.D. Cal. 1993).

IV. Settlements with putative class members are acceptable.

The law has long encouraged settlements as a means of avoiding the burdens and costs of the legal system. Although class-wide settlements of certified classes require judicial approval, individual settlements with potential class members prior to class certification are permissible and do not require court approval. *Manual for Complex Litigation*, at ¶ 30.24; [Jenifer](#), 1999 WL 117762, at *3. Like any settlement, the potential class members should be made aware of the claim they would be foregoing. [Jenifer](#), 1999 WL 117762, at *7. Also, defendants must scrupulously avoid using false or misleading information or undue influence to procure settlements. *Manual for Complex Litigation*, at ¶ 30.24. It should further be noted that in certain situations settlements may be subject to scrutiny. For instance, settlements of claims involving the Fair Labor Standards Act (FLSA) may not be binding on the Department of Labor. See, e.g., *Lynn’s Food Stores, Inc. v. U.S.*, 679 F.2d 1350, 1355 (11th Cir. 1982) (to be valid, settlements of such claims must be either “supervised by the Department of Labor” or be a “stipulated judgment entered by a court”). Similarly, settlements with individuals who have claims of discrimination, or are “piggy-backing” on the claims of others, will not bind the administrative enforcement agency.

Settlements are an important starting point, because in order to settle a dispute, the parties must communicate. So communications will clearly be necessary and are allowable. Also, the ability to settle claims should further place courts’ reluctance to order formal discovery in perspective. While courts generally do not like to order formal discovery from potential class members, they allow settlements with these members. Because settlement disposes of the individual’s claim, it would seem to pose a far greater risk of abuse and the use of intrusive tactics than mere contact with a potential class member to develop factual information relevant to the lawsuit. That defendants could contact class members to settle claims but not contact them for information related to whether the case is maintainable as a class action would be inconsistent. Indeed, many forms of communication are permissible and available for defendants to use against class-action claims.

V. Interviews and affidavits.

Interviews and affidavits are not the only permissible communications between defendant and potential class members but may be particularly useful in defeating class certification and addressing the merits of plaintiffs’ claims. Several courts have allowed defense counsel to interview potential class members and secure affidavits from them that are used to oppose class certification. See, e.g., *Greisler v. Hardee’s Food Systems, Inc.*, No. 71-2731, 1973 WL 79, at *1 (E.D. Pa. 1973); [Basco](#), 2002 WL 272384, at *4. Defendants may find it desirable to interview potential class members; interview of potential class members have been most frequently utilized in employment contexts. See, e.g., *Babbitt*, 1993 WL 150300, at *1; *Pruitt v. Chicago, Dept. of Aviation*, No. 03-C-2877, 2004 WL 1146110, at *3 (N.D. Ill. 2004). Conducting interviews or

securing affidavits allow defendants to properly evaluate and investigate the claims and potential defenses in the case. Information gained from affidavits and/or interviews may be used to defeat class certification or to prevail on the merits.

In one class action involving claims of racial discrimination, the defendant obtained affidavits from other minority employees stating that they had not been subjected to, nor witnessed any discrimination or harassment. *Pruitt*, 2004 WL 1146110, at *3. Twelve potential class members signed such affidavits, while another eight declared that they did not want to participate in the lawsuit. *Id.* at *6. The court, over plaintiff's objections, admitted the affidavits and declarations because there was no evidence of abuse or misleading communications. These affidavits contributed to the court's decision that the class was not so numerous as to justify class certification. *Id.* at *8. Had the case been certified, these affidavits would have also been valuable for rebutting the plaintiffs' claims.

In another case, 47 of 53 potential class members signed affidavits stating why they believed the purported class representative's interests were not aligned with theirs. *Shulman v. Ritzberg*, 47 F.R.D. 202 (D.D.C. 1969). The court found the statements in these affidavits to be relevant to the issue of adequacy of representation. *Id.* at 208. However, the court questioned, but did not decide, whether the affidavits could be used to allow plaintiffs to opt out of the class under Fed. R. Civ. P. 23(c)(2). Because Rule 23(c)(2) controls the procedure for opting out of class actions in order to avoid the *judicata* effect of the judgment, the opt-outs contained in the affidavits may not have been effective for opt-out purposes. *Id.*

In a wage-and-hour case, plaintiff moved to exclude employee declarations that supported the employer's opposition to class certification. *Bell v. Addus Healthcare, Inc.*, No. 06-5188, 2007 WL 2752893, slip op. at *1 (W.D.Wash. Sept. 19, 2007). The employer had conducted employee interviews to obtain declarations in its effort to oppose certification. The court held that there was no showing of abusive or coercive conduct, and that the employer "ha[d] a right to fully investigate the case." *Id.* at *3. As such, the court refused to place limitations on defendant's communications with the potential class members.

VI. Good practices for communicating with potential class members.

As a preliminary note, defense lawyers may want to consider what their clients can do before litigation has arisen. Professional hockey legend Wayne Gretzky once remarked, "A good hockey player plays where the puck is; a great hockey player plays where the puck is going to be." A lawyer who focuses on developing trends among the plaintiffs' bar, identifies potential class claims against their clients, and audits the company's practices – taking interviews and affidavits along the way – may be well poised to respond with a Rule 11 letter in the event litigation is threatened. Memberships in organizations such as Defense Research Institute, keeping a pulse on class action and collective action developments, and being able to stop class actions before they are filed distinguish the good defense lawyers from the great ones.

There are several things to consider before engaging in systematic communications with potential class members. First, some courts have held that the best practice is to provide the court with information regarding such communications before engaging in the communications. *Matarazzo v. Friendly Ice Cream Corp.*, 62 F.R.D. 65, 69 n.4 (E.D.N.Y. 1974). However, another court expressly rejected the need to seek judicial approval. *Parris v. The Superior Court of Los Angeles County*, 109 Cal. App. 4th 285, 290 (Cal. Ct. App. 2003). In the interest of not drawing the court's ire, it may be advisable to inform the court that you intend to communicate with potential class members. Individual practitioners should also familiarize themselves with the court's local rules or practice.

Next, it should be noted that some courts have considered ongoing-business relationships to be potentially coercive. See, e.g., *Fraleigh v. Williams Ford Tractor and Equip. Co.*, 5 S.W.3d 423, 436 (Ark. 1999); *Hampton Hardware*, 156 F.R.D. at 633; but see *In re Winchell's Donut Houses*, 1988 WL 135503, at *1 (Del. Ch. Dec. 12, 1988) (protective order particularly inappropriate when defendant and plaintiffs have a continuous business relationship). Coercion is more likely to be found where the defendant is in a position of power over potential members of the class. This will turn on the nature of the relationship between the parties. For instance, if potential members of the class are employed by the defendant, then there is the possibility that the defendant could exert undue influence over potential class members. Similarly, there could be disparity of power where the class members depend on the defendant as the sole provider of information, supplies, or credit. *Ralph Oldsmobile Inc. v. Gen. Mot. Corp.*, No. 99 Civ 4567, 2001 WL 1035132, at *4 (S.D.N.Y. Sept. 7, 2001). However, coercion is much less likely to exist if the potential class members are merely customers who buy or rent products from the defendant. In such situations, the defendant would rely on the class members for their business, and the potential for coercion is much lower.

In situations that are particularly likely to be coercive, the court may grant a protective order without a finding that a particular abuse occurred. *Hampton Hardware*, 156 F.R.D. at 633. But while an actual harm need not be shown in these situations, there must be evidence that potential for serious abuse exists. *Burrell v. Crown Cent. Petroleum, Inc.*, 176 F.R.D. 239, 244 (E.D. Tex. 1997). The record of threatened abuses must be clear so as to justify an interference with the defendant's speech. The mere existence of a potentially-coercive relationship alone is insufficient to bar communications. *Basco*, 2002 WL 272384, at *4. Indeed, one court has stated that, "[p]articularly where the class is comprised of persons with whom the defendant has an ongoing commercial relationship, it would seem distinctly ill-advised to attempt to require the defendant to deal with what may be an important aspect of a commercial relationship only through the channel of a self-appointed class action plaintiff." *In re Winchell's Donut Houses*, 1988 WL 135503, at *1.

With those concerns in mind, defendants should proceed with caution in commercial settings. It is important to evaluate the relationship between the defendant and the potential class members. This relationship will impact how defendants should approach class members. Defendants should also take time to consider exactly what sort of information they will seek from potential class members.

Before conducting interviews or seeking affidavits, defendants may want to prepare a disclosure statement relevant to the information sought for potential class members to sign. Although there is no rule requiring a disclosure statement, having one can rebut any later allegations by a potential class member claiming that they were ambushed or otherwise unaware of their rights. *Addus Healthcare*, 2007 WL 2752893, at *3. The following are some points that a defendant may want to include in a disclosure statement. These sample statements come largely from *Addus Healthcare, Inc.*

- A. A statement (1) identifying the lawsuit; (2) identifying the defendant(s); and (3) stating that the signor is a potential class member.
- B. A statement that defendant is investigating facts to evaluate and defend against the lawsuit, and that any information provided may be used in the lawsuit.
- C. A statement that the potential class member is not obligated to speak with the defendant, and will not be retaliated against if they decide not to participate.
- D. A statement that the defendant will not reward any potential class member for choosing to speak, nor has the defendant promised anything to encourage the potential class member to speak.
- E. A statement explicitly stating that the defendant will not attempt to influence the potential class member's decision to opt out of the potential class action.

The appropriateness of these sample statements will greatly depend both on the kind of information sought and from whom it is sought. For instance, if the defendant is not seeking information that would jeopardize a potential class member's claim, there may be no need to disclose the existence of the case. See *Jenifer*, 1999 WL 117762, at *7; *Carnegie v. H & R Block*, 687 N.Y.S.2d 528, 531-32 (N.Y. Sup. Ct. 1999). Similarly, including language about retaliation is probably more important in relationships that have the potential to be coercive, such as an employee-employer relationship, than in less coercive business settings. If there is little the defendant could do to retaliate against a class member, then there is probably no need for that statement. There also may be less need for a disclosure statement with affidavits, as some of the content could be incorporated into the affidavit itself.

The disclosure statements will help remove any appearance of coercion or deception from the process of obtaining information from class members. In providing a clear explanation of the communications' purpose and the rights of the potential class member, defendant should be able to avoid any later effort by plaintiff to exclude evidence or information collected. Also, these statements will provide documentation of the communications between the defendant and class members that relate to the case. This is important because, if defendants have a potentially coercive relationship with class members, the court may order production of communications between the defendant and the class members regarding the case. *Manual for Complex Litigation, Fourth* § 21.12 (2004). The court may order such production to ensure that no coercion was used to obtain the information. This would not abridge any otherwise privileged documents or work product but would merely relate to actual communications between the parties.

VII. Conclusion.

Potential class members are an often-overlooked avenue of information for defendants in class actions. Before certification, defendants should take advantage of the relationships they have with potential class members to prepare a defense to the suit. Information obtained through communications with potential class members can assist defendant in defending both class certification and the merits of the case, or at least lead to less costly individual settlements. However, candor and fair play are paramount. The appearance of unfair dealings may draw the scrutiny of the court. By utilizing disclosure statements, defendants can further ensure that they will be able to gain valuable information about the class action with little risk of it being excluded.

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Forum Selection Clauses under the Puerto Rico Dealer Statute: Is the Statute's Provision invalidating such Clauses still Enforceable?



The Puerto Rico Dealer Statute provides that a contractual clause that mandates litigation in a forum outside Puerto Rico shall be null, as violating the public policy behind the statute. See 10 L.P.R.A. § 278b-2. Specifically, the statute states in pertinent part: `<code>xml:namespace prefix = o ns = "urn:schemas-microsoft-com:office:office" />`

Any stipulation that obligates a dealer to... litigate any controversy that comes up regarding his dealer's contract outside Puerto Rico... shall be... considered as violating the public policy set forth by this chapter and is therefore null and void.

`<code>xml:namespace prefix = st1 ns = "urn:schemas-microsoft-com:office:smarttags" />`

The Puerto Rico Supreme Court has not rendered a decision enforcing or rejecting this provision. The United States Court of Appeals for the First Circuit, on the other hand, has upheld a forum selection clause mandating litigation outside Puerto Rico in a case involving the Dealer Statute. See *Royal Bed and Spring Co., Inc. v. Famossul Industria e Comercio de Moveis Ltda.* 906 F.2d 45, 50 (1st Cir. 1990). In *Royal Bed*, the court of appeals affirmed the district court's dismissal of the complaint under a forum selection clause mandating litigation in Brazil. Even though it was a diversity case where the movant sought dismissal, the court used the "federal principles" of the *forum non conveniens* analysis, rather than Puerto Rico law, to render its decision. *Id.* To this end, the court cited with approval an Eighth Circuit case that "held that the enforceability of a forum clause... is clearly a federal procedural issue and that federal law controls," and stated that "state forum non conveniens laws 'ought not to be' binding on federal courts in diversity cases." *Id.* (citations omitted). Following *Royal Bed*, the United States District Court for the District of Puerto has consistently upheld outside forum selection clauses in cases brought under the Dealer Statute. See e.g., *Antilles Cement Corp. v. Aalborg Portland A/S* 526 F. Supp.2d 205 (D.P.R. 2007) (upholding England forum selection clause); *D.I.P.R. Mfg., Inc. v. Perry Ellis Intern., Inc.*, 472 F. Supp.2d 151 (D.P.R. 2007) (upholding Florida forum selection clause); *Díaz-Rosado v. Auto Wax Co., Inc.*, 2005 WL 2138794 (D.P.R. 2005) (Unpublished Opinion) (upholding Texas forum selection clause); *Outek Caribbean Distributors, Inc. v. Echo, Inc.*, 206 F. Supp.2d 263, 270 (D.P.R. 2002) (upholding Illinois forum selection clause). The district court has stated that "local public policy on forum-selection clauses is certainly not a significant factor" when deciding whether to enforce a forum selection clause. *Outek*, 206 F. Supp.2d at 270. The court has also stated that "[t]he fact that a Puerto Rico statute [precludes] the applicability of forum selection clauses does not mean that the Court will automatically disregard the parties' freely-negotiated contractual obligations." *Díaz-Rosado*, 2005 WL 2138794, *2.

These courts were not dissuaded by the plain letter of the Dealer Statute, which expressly invalidates forum selection clauses under public policy principles. Their decisions are preceded by two relevant Supreme Court decisions: *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972), and *Stewart Org., Inc. v. Ricoh Corp.*, 487 U.S. 22 (1988). In *M/S Bremen*, the Supreme Court upheld the validity of an England forum selection clause. There, an American corporation had contracted with a German corporation to tow the former's sea drilling rig from Louisiana to a point off the coast of Italy. While the rig was being towed in international waters, a storm caused serious damage to the rig, and the owner commenced a suit in admiralty in the United States District Court in Florida. The defendant moved to dismiss for lack of jurisdiction and *forum non conveniens*. The Supreme Court held that forum selection clauses "are prima facie valid and should be enforced unless enforcement is shown by the resisting party to be 'unreasonable' under the circumstances." *Id.* at 10. Under *M/S Bremen*, the burden is upon the party resisting the forum selection clause to "show that enforcement [of the clause] would be unreasonable and unjust, or that the clause was invalid for such reasons as fraud or overreaching." *Id.* at 15. The Court underscored, however, that "[a] contractual choice-of-forum clause should be held unenforceable if enforcement would contravene a strong public policy of the forum in which suit is brought, whether declared by statute or by judicial decision." *Id.* This is significant, given the Dealer Statute's public policy against outside forum selection clauses.

On the other hand, in *Stewart*, the Supreme Court rejected the notion that the district court had to take into consideration Alabama law that looks unfavorably upon forum selection clauses before deciding a motion to transfer the case. The Court stated: “[w]e hold that federal law, specifically 28 U.S.C. § 1404(a), governs the District Court’s decision whether to give effect to the parties’ forum-selection clause and transfer this case[.]” 487 U.S. at 32, and *see* n. 9 (“Our determination that § 1404(a) governs the parties’ dispute notwithstanding any contrary Alabama policy makes it unnecessary to address the contours of state law.”) There, an Alabama copy machine dealer brought a diversity action against a New York manufacturer. The manufacturer sought to enforce a Manhattan contractual forum selection clause and moved to transfer the case under that clause. The Supreme Court left no doubt that, when faced with a motion to transfer a case under Section 1404(a), district courts should only apply federal law to their determination of the proper forum pursuant to a forum selection clause and disregard any state public policy against enforcement of forum selection clauses.

The *Stewart* decision eliminated the weight given by *M/S Bremen* to state public policy considerations in forum selection disputes, but only as it applies to motions to transfer under 28 U.S.C. § 1404(a), not necessarily motions to dismiss. Indeed, the United States District Court for the District of Puerto Rico has stated that *M/S Bremen* applies to state cases where the moving party seeks dismissal or federal cases where the moving party seeks dismissal under an international forum selection clause, and *Stewart* applies to cases where the moving party seeks a transfer under Section 1404(a). *See Antilles Cement Corp.*, 526 F. Supp.2d at 207. Thus, a state court faced with an outside forum selection clause, or a federal court faced with a motion to dismiss under an international forum selection clause, still could consider the public policy caveat expressed in *M/S Bremen* and hold the forum selection clause unenforceable in accordance with the public policy declared by the Dealer Statute.

The Puerto Rico Supreme Court has not considered whether, in light of *M/S Bremen*’s public policy caveat, an outside forum selection clause should be rendered invalid under the Dealer Statute and its strong public policy. In a different context, the Puerto Rico Supreme Court has stated that forum selection clauses fulfill their own significant public policy of not imposing obstacles in interstate and international commerce, as well as “vital interests of the system of justice.” *See Unisys P.R. v. Ramallo Bros. Printing, Inc.*, 128 D.P.R. 842, 856-57 (P.R. 1991) (translation provided). This public policy, however, conflicts with the public policy behind the Dealer Statute, which favors litigation in Puerto Rico regardless of whether the dispute arises from “interstate” or “international” commerce.

In view of these conflicting public policies, the *M/S Bremen* Court’s reasoning that a forum selection clause “should be held unenforceable if enforcement would contravene a strong public policy of the forum in which suit is brought, whether declared by statute or by judicial decision,” warrants a balancing test between the public policy declared by the Dealer Statute and the public policy declared by the *Unisys* decision before a court decides the fate of a motion to dismiss under a forum selection clause in a Dealer Statute case. *See M/S Bremen*, 407 U.S. at 15. Such a case could be dismissed if the court decides that the public policy behind the statute does not outweigh the public policy explained in *Unisys*. This balancing test, however, has not been conducted.

The United States District Court for the District of Puerto Rico has noted the public policy caveat stated in *M/S Bremen*. *See e.g., Antilles*, 526 F. Supp.2d at 208-09. But it has not afforded weight to the Dealer Statute’s public policy because the “policy has yielded to clauses covered by the Federal Arbitration Act... as well as those falling within the ambit of § 1404(a)...” and previous decisions “bypassed the Law 75 forum limitations while applying federal common law.” *Id.* at 209 (citations omitted).

In sum, there is no Puerto Rico reported decision dismissing a complaint under a forum selection clause where the court engaged in a balancing test between the public policy behind the Dealer Statute and the public policy explained in *Unisys*. This balancing test could trump the forum selection clause provision of the Dealer Statute completely, or it could tilt in favor of the public policy behind the statute. In this regard, the Dealer Statute’s provision barring outside forum selection clauses could, at least in theory, still be enforceable in situations where the moving party seeks dismissal rather than a transfer. As it stands, however, the provision is hanging by a thin thread. Indeed, even in *M/S Bremen*, decided over thirty years ago, the Supreme Court admonished that “the forum clause should control absent a strong showing that it should be set aside.” 407 U.S. at 15. Although the Court acknowledged that state public policy considerations could trump otherwise valid forum selection clauses, such public policy considerations are taking a back seat to public policies that support global trade and commercial expansion “[i]n the light of present-day commercial realities and expanding international trade[.]” *See id.*

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June 30, 2008

From the Chair

Accomplishments and Challenges



We thought it might be interesting to share with you some information about the growth of this Committee. Thanks to our Board Liaison, [Chuck Cole](#), from crunching these figures.xml:namespace prefix = o ns = "urn:schemas-microsoft-com:office:office" />

This past month, the Commercial Litigation Committee has exceeded 1300 members, and we are now the sixth largest substantive law committee in DRI. Looking over the past four years, no other substantive committee has approached our level of growth, which has averaged almost 6% per year. We have grown almost 20% since 2004, and are less than 100 members behind the fourth largest committee. Looking back further, at the end of 2001, we had 838 members; thus, we've seen a growth of almost 500 members in that time.

What does this mean? First, kudos are due not just to our past leaders, but to all the members of this Committee who have worked to recruit new members, develop our publications and programs, and enhance the Committee's presence and content. It would appear that we are doing *something* right, and we should keep at it. Thanks, also to the support of DRI leadership in this effort..

More importantly, we can keep growing and broadening the Committee. As I have reported in prior months, we have many initiatives in play – our SLGs, teleseminars, publications, and regional seminars; our [DRI Annual Meeting CLE](#); our September 4-5, [2008 IP Litigation Seminar](#); and our in-the-works 2009 seminar – which offer commercial litigators of all stripes, and their clients, great opportunities to participate, learn, and network. If you aren't involved – or even if you are but want to enhance or change what you do within the Committee – contact me or one of our other leaders and let us know what you would like to do.

At a minimum, plan on attending the Chicago IP Litigation seminar and/or the DRI Annual Meeting. Both are great opportunities to get CLE, network with your colleagues and, as a side benefit, have a great time. If you're interested in learning IP nuts and bolts, plan on signing up for one or more of our IP 101 Teleconference series; the first, Patents 101, is scheduled for June 26 from 3:00 to 4:30 Eastern time. Trademarks and copyrights will follow.

Lastly, Chuck has suggested – and I concur – that we should make it a goal to move our Committee into the ranks of the top five substantive law committees by the time of our September seminar. To do that, each of us should try to recruit at least one non-DRI attorney (whether inside your firm, in another firm, an in-house counsel, or a recent law school graduate) to join DRI and our Committee. They should know that unlike many other organizations, our members get the opportunity to get involved immediately. If folks in your firms are transitioning their practices to a more business-oriented litigation focus, suggest that they add our Committee to their DRI involvement.

We have some great opportunities in the next 18 months to expand this Committee tremendously. I encourage each of you to participate, and to use the Committee's activities as a way to build our network, reach out to existing or potential clients, and grow both the Committee and your practice.

As always, if you have any thoughts, comments, or suggestions (including where the Yankees can find some pitching), please let me know.

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June 30, 2008

From the Editor

Half-time Report



Here we are, second quarter tax payments already posted to the government, baseball in full season, kids being shuttled to overnight camps, and it is tempting to just kick back and take it easy in the heat. But the Commercial Litigation Committee never sleeps. We've got seminars to plan, teleconferences to schedule, articles to write, and compendia to publish.

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The ambitious Trade Secret/Non-Compete Compendium will be "knee high by the 4th of July", as they say in the Midwest. We heartily appreciate all the efforts of the many, many authors and the volunteer regional editors. We'll be rounding the curve to the finish line on this in the next month and it will be available for purchase in the late summer.

We're also moving right along with the Business Suit in Review. For those of you who recall that you saw an really good article somewhere in some publication in the last two years (meaning you have no idea where you saw it), this is the perfect desk reference copy, nicely indexed so you can actually find the most valuable and interesting articles written anywhere on earth. Thanks go to Kelly Kosek for shepherding this project.

Finally, a compendium of articles from the committee's SLG's is off to a start, albeit a slow one. This is a project for which we are calling on the SLG members to prepare articles on a variety of topics of general interest to the committee members. We've solicited the SLG chairs to ask their members for proposals and we've received some but the ideas have not rolled in at quite the pace we'd hoped. This is an excellent opportunity to have an article on a topic you want to write about published in a book that is available for purchase. We hope to have this on the market by the fall. But we need your help to accomplish this. So if you have an idea, please contact your SLG chair or SLG publications sub-chair and let him or her know.

About the Author Christine Mast is a partner at Hawkins & Parnell, LLP in Atlanta, Georgia. Her practice focuses on professional liability defense work and licensing matters, insurance coverage and bad faith, and commercial litigation disputes. Christine can be reached at cmast@hplegal.com.

June 30, 2008

Leadership Spotlight



This month's spotlight shines on Christy Mennen, an associate at Halleland Lewis Nilan & Johnson, PA in Minneapolis, Minnesota. Christy practices in the areas of commercial litigation and product liability. She serves as the Young Lawyer liaison to the Commercial Litigation Committee and is the vice-chair of the Young Lawyers Membership Committee.xml:namespace prefix = o ns = "urn:schemas-microsoft-com:office:office" />

1. Describe your practice:

My practice consists primarily of commercial litigation and product liability defense work. I am licensed in Minnesota and Wisconsin and regularly serve as both national and local counsel.

2. What's the most interesting case you have handled:

A few years ago I spent nine months defending a patent infringement case involving serial-to-Ethernet connectors. It was my first introduction to intellectual property law and not only challenging (when I started I had no idea what a Markman hearing was), but extremely interesting to dive into the electrical engineering world. Perhaps the greatest accomplishment of all was proving to my husband, an electrical/software engineer, that despite my strictly liberal arts major, I really could master the technology.

3. What's the most amusing client story . . . ?

I was defending a medical device company in a product liability action when my client called to point out that the pro se plaintiff, an inmate in Florida state prison, had filed an Amended Complaint. We couldn't help but laugh when we realized the plaintiff had amended his Complaint to specify exactly how he wanted to receive his alleged damages -- he wanted \$2 million dollars, and he wanted it paid to him in \$5 bills (so he could use them in prison commissary).

4. How did you get involved with the DRI Commercial Litigation Committee?

My colleague, Cynthia Arends, is on the Commercial Litigation Steering Committee and on the Executive Committee for Young Lawyers. After she suggested that I become involved, I sought out the young lawyer vice-liaison position in 2006-2007. I am now the young lawyer liaison to the committee.

5. Have you gotten any benefits from being involved with the DRI Commercial Litigation Committee?

Absolutely. I have met a great group of commercial litigators practicing all over the country, have consulted with them on cases, referred work to them and been hired as local counsel.

6. Tell us something about you that we might now know, but which you are passionate about:

Do I dare? Let's see . . . I am pretty passionate about party flair. It must have started with my mom decorating the entire house for my birthday when I was a kid. Let's just say I have a lot of creativity when it comes to parties, holidays, pub crawls, you name it. Some of you probably remember that I brought wigs and masks to the seminar in Phoenix last fall. I mean, a conference on Halloween? I simply couldn't resist.

Other things? Live music; college football; running; and my two adorable kids – Haley (3) and Will (1) – for ensuring that I take time to “play” every day.

7. Why did you become a lawyer?

My dad and my two brothers are plumbers and my mom is a nurse. Honestly, I don't know a thing about plumbing (except that it is really expensive to get a plumber to make a house visit), and I have always been scared of hospitals. After taking government in high school, I started thinking about becoming a lawyer, but it wasn't until college, when I met two lawyers playing pool in a martini bar that it all came together for me. When they told me their legal secretary was moving to Arizona, I convinced them I could do the job. They were definitely surprised when I called the next morning for an interview, but they offered me the job on the spot. I worked for them for a year and then went straight to law school.

8. What do you like about practicing law?

I have two small children and I would be lying if I said it wasn't difficult to juggle being a mom and being a litigator. But I cannot imagine not practicing law. I work with a group of extremely intelligent, talented and fun lawyers who are committed to my professional development. I am

so fortunate that straight out of law school, I started working at a firm that is the right fit for me. Also, I love that every new case requires me to delve into a new area of law, learn about a new product or industry, or analyze business decisions I wouldn't have otherwise considered. I always loved school and for me, practicing law is like continuing my education – every new case is a new learning opportunity.

9. What don't you like about practicing law?

I really dread encountering people who don't understand how the legal system works and because of a bad experience with one lawyer, have concluded that all lawyers are evil. These are usually the same people who refuse to believe I don't defend criminals, regardless of how many times I tell them I am a commercial litigator. The legal profession is an admirable one, and it's unfortunate that not everyone realizes that.

June 30, 2008



William Frank Carroll, a member of the Cox Smith Matthews law firm's Dallas office was recently elected as a member of the American Law Institute. The Institute is responsible for the preparation of the Restatements of Law. Frank has been appointed to the committees working on the Restatement of the Law Third-Restitution and Unjust Enrichment, and Principles of the Law of Aggregate Litigation.

June 30, 2008

DRI MEMBER SCORES TKO A KNOCKOUT



DRI member Christopher T. Sheean and Matthew Garrett, partners with WILDMAN, HARROLD, ALLEN & DIXON LLP, successfully defended software developer Tech King Operations, Inc. ("TKO"), against claims of trade secret misappropriation brought by competitor Verotix Systems, Inc., in an eight day trial in March in Joliet, Illinois.

In 2002, Follett Library Resources sought bids for the upgrade and expansion of its warehouse and conveyor system in Illinois. TKO and several other companies bid for the supply of the warehouse management software component, including the existing vendor, Plaintiff Verotix Systems, Inc. TKO was awarded the software subcontract and configured its CHAMP(r) system for the project.

Verotix subsequently filed suit in Will County, Illinois against TKO and Follett alleging that Follett had supplied TKO with confidential drawings, flow charts, source code and software relating to the plaintiff's warehouse management software. The court in *Verotix Systems, Inc. v. Tech King Operations, Inc., et al.*, Case No. 02 CH 2041, rejected plaintiff's claims and found in favor of TKO, as well as its co-defendant, Follett. In defeating the claims, counsel for the defense was able to establish that several of the alleged trade secrets came from well-known sources in the public domain or from Follett's request for proposal document itself. The court ruled in TKO's favor and found no evidence of any misappropriation of trade secrets.

June 30, 2008

Eliminating Copyright Infringement As to On-Line Content Without Litigation



The internet poses a major concern as to copyright infringement, particularly given the ease of posting content and the often lackluster policing as to possible violations of intellectual property rights. In many instances, litigation is not the first choice option.xml:namespace prefix = o ns = "urn:schemas-microsoft-com:office:office" />

Initial efforts focus on the “cease and desist” type letter, and that letter is often initially directed to the site registrant. The preferred Whois service can assist tracking down the registrant information if not otherwise apparent. Thus, Whois.domaintools.com provides useful information as to the registrant’s contact information. This typically includes the registrant’s name, e-mail address and organization.

A second step, if the “cease and desist” letter to the registrant is not successful, or in tandem with that request, is to contact the on-line services provider (the “OSP”) to request that it notify or take down/disable the disabling site. The Digital Millennium Copyright Act (“DMCA”) provides some assistance to this end as it helps protect the OSP from legal action by the alleged infringer when it has responded to a take-down notice.

In order to track down the OSP, the Whois can be again helpful. It will identify the server which hosts the site. The OSP is identified in the server data box. In the OSP’s headquarters are not clearly identified, then its website, or failing that, the US Copyright list of designated agents for OSPs should provide contact information.

The Copyright Office maintains designated agents as to many of the OSPs. Clicking on the OSPs name reveals contact information.

The take down notice to the OSP is fairly straightforward. The most important Identifiers are of course, the information as to the specific material being infringed, the absence of any permission, and the basis for copyright ownership.

Chillingeffects.org database has some examples of takedown notices. They have a database of such notices.

If the OSP is situated outside the United States, that is clearly a complication. However, even with an off-shore OSP, it may worth a look to see whether the other Jurisdiction has any set procedure for takedown notices.

In the event that contacting the OSP is not effective, a further step would be send a takedown notice to the company that registers the URL. Many registrars also disable domains that engage in copyright infringement. Thus, once you determine who it is, you can send the registrar a DMCA takedown notice as well.

In order to determine the domain registrar, Whois generally provides information sufficient to find the registrar’s website. It is often advisable to address a letter to both the hosting company and the registrar to provide notice.

A takedown notice to the search engine can also be attempted. Each of the major Search engines, e.g. Google, Yahoo, MSN, have their own policy as to copyright infringement.

If the copyright infringement occurs in connection with sale of merchandise on a website, which will often be coupled with trademark infringement, notice to the host site, including any fraud detection officer, may put some pressure to enforcement. While companies such as E-Bay assert that it is a virtual impossibility for them to police their sites for the purpose of purging the sites of counterfeit or otherwise infringing product, there has been increasing media attention and thus, pressure on these sites to be reactive, if not always proactive, in dealing with identified infringement.

While none of these steps will prevent litigation in the more virulent cases, some infringement claims can be effectively resolved on this basis; and absent such resolution, litigation always remains an option.

About the Author Craig Aronson is a co-editor of DRI’s intellectual property column. He is a principal at Berger, Kahn, xml:namespace prefix = st1 ns = "urn:schemas-microsoft-com:office:smarttags" />Orange County, CA, and specializes in intellectual property and trade secrets issues.

June 30, 2008

The Puzzling Situation of Lloyd’s: Is One of the “World’s Best Known Insurance Companies,” Not Really An Insurer At All?



Lloyd’s is one of the preeminent insurance names in the world. It has a long history of dealing with commercial risks. However, those who have litigated against Lloyd’s know that it takes the position that it is not an insurer at all.xml:namespace prefix = o ns = "urn:schemas-microsoft-com:office:office" />

Lloyd’s has a colorful history and an enigmatic present. The Lloyd’s coffeehouse aka Edward Lloyd’s coffeehouse originated

in xml:namespace prefix = st1 ns = "urn:schemas-microsoft-com:office:smarts" / London on Tower Street in 1688. As befitted the times, the primary gatherers at the coffee shop were merchants, seamen, and shippers. Given the risks of long journeys by sea, and uncertainty of cash flow given commodities lost in nautical perils, the need for insurance arose to cover the needs of the shipping industry and merchants. Additionally, at the time many of the boats were involved in slave trade, which presented a high risk of piracy. Between 1688 and 1807, Lloyd's carved out a niche in insuring slave ships, specifically, and shippers generally.

From its inception through the 1970s, Lloyd's developed a broader based commercial presence in the insurance industry and became an anchor for Britain in the commercial insurance market. For reasons that have more to do with the tax system in England than with any particular interest of insureds, the backing for Lloyd's insurance increasing became based on a system of passive investors. The tax rate in England for the 1970s has been listed as, for top earners, 40% on capital gains, 83 percent on earned income and 98% on investment income. Accordingly, at least one factor encouraging the passive investor backing of policies for Lloyd's may well have been the tax structure at the time.

Another factor that underlies a distinctive origin of Lloyd's is that it has been continually the subject of the acts of Parliament. Thus, in 1982, the Lloyd's Act defined the rules and regulations governing the Lloyd's of London insurance market. The Lloyd's council normally has six working, six external and six nominated members. The appointment of nominated members, including that of the Chief Executive Officer, is confirmed by the Governor of the Bank of England. The working and external members are elected by Lloyd's members. The Chairman and Deputy Chairmen are elected annually by the Council from among the working members of the Council. All members are approved by the Bank of England.

There are essentially two sides to the Lloyd's operation. There is the funding side, whereby essentially so-called syndicates of members finance the insurance policies; and the marketing side, the agents and brokers that are a buffer between Lloyd's, the managing agents, and the public. Lloyd's brokers deal with the public: Outsiders, whether individuals or other insurance companies, cannot or do not do business directly with Lloyd's syndicates. They must hire Lloyd's brokers, who are the only customer-facing companies at Lloyd's. They are therefore often referred to as 'intermediaries'. Lloyd's brokers shop customers' policies among the syndicates, trying to obtain the best prices and terms.

However, herein lies part of the conundrum. As a financing vehicle and business, Lloyd's thrives as it historically has, by having interested investors so-called members front/finance the policies. These certain underwriters and members of syndicates are, at least from Lloyd's perspective, the financial reality as to who has ultimate responsibility to pay the loss.

The business reality though for dealing with the insureds is different, the

Lloyd's name carries the day, and individual syndicate members, remain as to the policy holders nameless and faceless individuals, perhaps identified by a vague reference to a syndicate number on page 25 of a policy that bears Lloyd's names.

Lloyd's reputation carries the day in marketing. Insureds want a Lloyd's policy, not a policy written by syndicate number 720. Lloyd's writes broad commercial coverage for major businesses and is known for creative policies, such as a policy on Celine Dion's voice, on Jimmy Durante's nose and Tina Turner's legs. The fact that the policies are brokered by Lloyd's agent, on a policy that on the cover page has Lloyd's name is instrumental to the policy sales; as many insureds whether celebrity or commercial would probably not feel inclined to have insurance with just an unnamed syndicate.

For those who deal with Lloyd's though, and are in litigation with Lloyd's, there are some unique problems. Lloyd's takes the position that the insured's relationship is with the syndicates identified by numbers. Thus, tender is not to be made generally to Lloyd's but to the syndicate or its representative for receipt of service. Payment of claims is not to be made by Lloyds as an insurer but by the syndicate as backers. The writer is interested in the experiences of others presently dealing with Lloyd's and its position that it has no responsibility as an insurer or general agent on the policies, and that the true policy insurer is the syndicate.

However, this situation creates something of an unworkable dynamic:

The apparent agent/insurer on the policy, the name that the insured banks on is Lloyd's, but the economic reality as conveyed by Lloyd's is the syndicate. Does this mean though, for example, that if a commercial insured has multiple policies with Lloyd's, tender to Lloyd's or to a Lloyd's agent is not sufficient, as the tender should be directed to the interested syndicate or its agent, which agent may vary from syndicate to syndicate? This apparently is a position that has been taken by Lloyd's attorneys.

Thus, the Lloyd's conundrum is whether in effect, as gauged by the standard of the presumptively typical insured, it can both be the great insurer, and not an insurer at all. And, if Lloyd's is just acting as an agent, can it disclaim any obligations on policies as a general agent, and require that matters be taken up with individual syndicates?

Thus, the ultimate question may be whether a company perceived and understood as one of the world's great insurance companies can present itself as a non-insurer and place obligations vis-à-vis its insureds with the syndicates and their agents only. Clearly, this will be an issue of ongoing concern and litigation.

About the Author Craig Aronson has advised concerning and litigated major insurance cases for the past twenty years and a special interest in coverage issues related to intellectual property and commercial claims.

June 30, 2008

The View from the Couch: What I Learned from Reality TV.



The Digital Age has brought many changes to the practice of law—the cell phone, the BlackBerry, e-mail, and wireless internet. Technology's leaps and bounds are truly dazzling. But one technological breakthrough stands head and shoulders above the rest: TiVo. `<xml:namespace prefix = o ns = "urn:schemas-microsoft-com:office:office" />`

If you have a TiVo, you understand. If you aren't a card-carrying TiVo owner or DVR user, I direct you to former FCC-chairman Michael Powell's revelation that "TiVo is God's Machine."

I love the flexibility that TiVo provides. I can work late and schedule evening events without fear of missing a Very Special Episode of [insert your favorite show here]. No more struggling to program the VCR to record my favorite show. And, more frequently, I find that my TiVo frequently is recording Reality TV.

Now, I know what you're thinking. *Reality TV is bottom-of-the-barrel television fare. It's mindless drivel giving brain-dead twits more than their allotted fifteen minutes of fame.* I respectfully disagree. Lawyers can benefit a great deal from (as well as be entertained by) Reality TV. In fact, I've discovered that every reality show contains lessons that every attorney—especially junior attorneys—should learn.

Project Runway.

The Project Runway contestants are asked to take less-than-optimum materials and a short amount of time to construct a stunning, fashionable, wearable work of art. Fashion moguls and trendsetters judge the resulting clothes. Some contestants breakdown or sloppily finish their garments – sometimes with tape or staples. Other contestants plan a course of action, sketch the envisioned design, and carefully gauge what can actually be accomplished given the constraints of the task. Tim Gunn, the contestants' advisor, employs a catchphrase to encourage his fledgling designers: "Make It Work!"

In the legal world, we've all been faced with a deadline that seems insurmountable. We're given "bad facts," contrary law, and less time to prepare for the big brief or hearing than we want or need. But, taking Tim Gunn's advice, an able attorney makes it work. Keeping your cool, planning the attack, and focusing on making the best use of the limited time may just get you to "Fashion Week."

Survivor.

After 16 seasons of Survivor, contestants have learned one thing: make alliances early. The same holds true for attorneys. Get to know your fellow associates, the partners at your firm, your colleagues in the community, the court's staff, and your firm's staff. Identify allies in your own tribe *and* in your competitor's tribe. In the end, success may be judged by your former alliance members—so be wary of how you treat your competitors *and* your allies.

Amazing Race.

The Amazing Race receives a lot of kudos for being a "smart" reality show. The concept of the show is straightforward. Teams of two embark on a globe-trotting mission to solve puzzles and complete mental and physical tasks. The last team to complete each leg of the race is eliminated. Certain legs of the trip have a *Fast Forward* task that teams may choose to complete. The *Fast Forward* task is typically a daring physical task, but only one team can capitalize on the *Fast Forward*. That team—the one that successfully completes the *Fast Forward*—is rewarded by being able to skip forward to the finish line for that leg of the race. Once a team completes the *Fast Forward* task, any other team waiting to try the *Fast Forward* must return to the normal tasks—often far behind the other teams that did not consider taking the *Fast Forward*.

Obviously, taking the *Fast Forward* is risky. A team never knows whether another team has decided to take the *Fast Forward*. Getting to a *Fast Forward* after another team can be disastrous. For attorneys, the lesson is clear—great risk can yield great reward. But sometimes even though taking the long way may not be exciting, it is a sure-fire way to cross the finish line.

American Idol.

American Idol has become an American institution. Families watch American Idol religiously. Yet even with all of the contestants who have come before, the new contestants still make the same mistakes over and over. Repeatedly, contestants take on songs that are “too big” for them. This theme often surfaces when a contestant decides to take on a Whitney Houston song and the judges are forced to remind the wannabe singer that she or he is no Whitney.

The lesson in law? Just because Whitney sang it, doesn’t mean that you have to. Problems can be solved in a number of different ways. Don’t be afraid to be creative and solve a problem in an original way. Also, when you’re drafting a motion, don’t be a slave to those who’ve come before you. Make smart changes and edits that improve upon the original.

The Apprentice.

Donald Trump’s The Apprentice showcases up and coming business talent (or C-list celebrities) vying for a job working for Donald Trump. To become the Apprentice, candidates must complete in two teams. The teams will be given a challenge—often creating, selling, or marketing products. After the challenge, one team is declared the winner. The other team faces Donald Trump in the board room, where Donald Trump will fire one of the losing team’s members. Ultimately, Donald Trump alone decides who is “fired” or “hired.” His reasons are not always apparent. In fact, his decision can be difficult because the best project leader is disadvantaged with a poor team member or bad location.

In the practice of law, cases can be like Apprentice tasks. A project leader’s or attorney’s effort does not necessarily equal a victory. But, sometimes, the effort can save you. Just think—in Celebrity Apprentice, Donald Trump decided not to fire anyone because the losing team did so well. While that’s not going to happen in the legal world, the extra effort may give you some bargaining power down the road.

The Mole.

The Mole is one of the first great Reality TV shows. (ABC cancelled it, but is resurrecting it this year.) The Mole features a “double agent” who secretly sabotages the rest of the contestants. The contestants collectively earn money for completing tasks, but lose money for certain infractions. The Mole must be friendly enough with the rest of the contestants to avoid detection, but successful enough to keep money out of the pot. In past seasons, contestants have found that befriending The Mole could be dangerous or beneficial, depending on the situation.

In the legal world, we often know our opponent. Our opposing counsel may be difficult to work with, but he or she may also be friendly. Following The Mole’s lead, it is important to know your opponent and leverage the relationship when you can. But beware—if you underestimate your opponent, elimination may be on the horizon.

So what are you waiting for? Program your TiVo and bulk up on Reality TV. Just think what you might learn from “What Not To Wear” or “Hell’s Kitchen.” I guarantee there’s a Reality TV marathon on next weekend (or the weekend after that!). Go ahead. Enjoy some TV—it may not be as mindless as you thought.

About the Author

Kelly A. Kosek is an associate with Hahn Loeser & Parks LLP in its Cleveland, `xml:namespace prefix = st1 ns = "urn:schemas-microsoft-com:office:smarts" />Ohio office. Kelly’s practice focuses on commercial litigation and class actions. She also has experience in product liability and premises liability litigation. Kelly currently serves as the Young Lawyer Vice-Liaison to the Commercial Committee.`

June 30, 2008

First Circuit Update



- **Agreement to Chinese arbitration enforceable by non-signatory**`xml:namespace prefix = o ns = "urn:schemas-microsoft-com:office:office" />`

- **Alleged employee poaching by strategic partners subject to arbitration**

- **Unilateral pricing unreasonable despite being non-discriminatory**

Agreement to Chinese arbitration enforceable by non-signatory

A recent First Circuit decision suggests that close attention to the international nature of a client's contractual partners is warranted in evaluating the potential scope of an arbitration clause. In Sourcing Unlimited, Inc. v. Asimco Int'l, Inc., plaintiff outsourced some of its manufacturing capability to Asimco Technologies, Inc. ("ATL"), a Delaware corporation headquartered in China. -- F.3d --, 2008 WL 2132838 (1st Cir. 2008). Defendant Asimco is a subsidiary of ATL. Id. at *1. The outsourcing and profit sharing agreement between plaintiff and ATL was contained in a written partnership agreement ("the ATL Agreement"), which required ATL to collect from customers and pay plaintiffs a portion of the profits, also contained an arbitration clause requiring that "[a]ny action to enforce, arising out of, or relating in any way to, any of the provisions of this agreement shall be brought in front of a P.R. China arbitration body." Id. Defendant Asimco was not a party to the ATL Agreement. Id. In its complaint alleging that it had been significantly underpaid, plaintiff claimed that it had entered into an oral agreement with Asimco, contemporaneously with the Agreement, identical in all respects except for the omission of any arbitration requirement. Id. at *2. Asimco's motion to dismiss in favor of arbitration had been denied by the District Court. Id. at *3.

The First Circuit's reversal relied in large part on the Federal Arbitration Act ("FAA"), specifically on that portion of the FAA implementing the Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Id. at *2. Cursorily distinguishing decisions from the Tenth and D.C. Circuits supporting plaintiffs' position that the court did not have jurisdiction to allow an interlocutory appeal on substantive arbitrability by a non-signatory to the arbitration agreement, the court noted that the international component of the FAA (Chapter 2) was broader than its domestic counterpart (Chapter 1). Id. at *4-5. Whereas Chapter 1 of the FAA allowed district court compulsion of arbitration "under *awritten agreement* for arbitration," Chapter 2 provides that a court "may direct that arbitration be held in accordance with the agreement at any place therein provided for." Id. at *4, 5 (citing 9 U.S.C. §§4 and 206) (emphasis added). The court also noted the expansive definition of an arbitration agreement under Chapter 2 as "arising out of a legal relationship, whether contractual or not, which is considered as commercial . . ." Id. at *5.

Placing significance on the fact that plaintiff signed a written arbitration agreement (albeit with ATL) and was now trying to avoid arbitration, the court held that the central question was whether "the issues the nonsignatory is seeking to resolve in arbitration are intertwined with the agreement that the estopped party had signed." Id. at *6. Finding both that plaintiffs' claims continually referred to the ATL Agreement and that any substantive terms in an oral contract with Asimco were identical to the ATL Agreement, the court remanded with instructions to grant Asimco's motion to compel arbitration and dismiss the suit. Id. at *8.

Alleged employee poaching by strategic partners not subject to arbitration

Where a Maine corporation was "subject to a spate of mass resignations" whereby its employees were hired by an Alaskan former strategic partner, the First Circuit found that an arbitration clause in one agreement did not compel arbitration in a dispute regarding a second, contemporaneous contract. The parties in Combined Energies v. CCI, Inc. had entered into 1) a Teaming Agreement ("TA") related to the submission of a bid to the U.S. Navy; 2) a Strategic Alliance Agreement ("SAA"), and; 3) a Purchase Order Agreement ("POA"), the latter of which contained an arbitration clause and dealt with the "standard terms and conditions applicable to each party's performance of the Navy contract." 514 F.3d 168, 170 (1st Cir. 2008). Plaintiff alleged various claims for tortious interference, equitable relief, and breach of contract, referencing only the TA and SAA. Id. Applying the Federal Arbitration Act ("FAA") to plaintiffs claims, the court noted that its decision on defendant CCI's motion to compel arbitration depended solely on "whether the dispute is of a kind that the parties had agreed to submit to arbitration." Id. at 171.

CCI argued that the POA arbitration clause, requiring that the parties arbitrate "[a]ll claims, disputes and matters in question arising out of, or relating to, this POA or the breach thereof," mandated dismissal of Combined Energies' ("CE") claims in favor of arbitration. Defendant also sought to apply the arbitration clause of the POA to the two other agreements via the POA's definition of the Contract Documents to include both the TA and SAA. Id. at 173-174. Rejecting both arguments notwithstanding the relatedness of the contracts and underlying transactions, the court first relied on the POA's requirement that a dispute arise out of or relate *to the POA*, noting that none of CE's claims alleged problems with the performance of the Navy contract. Id. at *172-*173 (observing that CE's allegations "would stand regardless of the parties rights and responsibilities as defined by [the POA]."). Second, the court noted that the clause within the POA defining "Contract Documents" also specifically identifies the POA as one of those documents, frustrating CCI's effort to apply that contract's arbitration requirement to all of the Contract Documents. Id. at *173-*174. Accordingly, the court affirmed the prior denial of CCI's motion to compel arbitration. Id. at *174.

Unilateral pricing unreasonable despite being non-discriminatory

In Marcoux v. Shell Oil Products Co., LLC, gasoline producers appealed a decision in favor of Massachusetts gasoline dealers regarding the termination of sales-based lease discounts and unreasonable gas prices under franchise agreements. 524 F.3d 33 (1st Cir. 2008). Although

the central claims, and much of the First Circuit's opinion, turned on interpretations of the federal Petroleum Marketing Practices Act, an ancillary issue was whether the producer/defendants violated a U.C.C. requirement for open price term contracts. Under their agreements, the price which the plaintiff dealers paid for gasoline was periodically determined by defendants "who calculated it by assessing the street prices of other competing gasoline stations in the area, and reducing those prices by the taxes levied on gasoline and an Estimated Industry Margin to approximate the wholesale price of the defendants' competitors." *Id.* at 38.

While adjudicating a dispute which arose in 2000, the court dealt with plaintiffs' claim that defendants' pricing structure violated the U.C.C.'s requirement that open price term contracts be administered in good faith under the timely heading "Unreasonable Gas Prices" *Id.* at 50. Surveying interpretations of Section 2-305(2) of the U.C.C., the court acknowledged that other courts had found that pricing did not breach the "good faith" requirement so long as it was nondiscriminatory. *Id.* at 50-51. Nevertheless, the court rejected defendants' argument that nondiscriminatory pricing insulated them against any "good faith" challenge, holding that the "good faith" requirement required a substantive analysis of how prices were set in order to avoid the "uncommercial" result of allowing one party unfettered control over pricing *Id.* at 51. The court concluded by rejecting defendants' challenge that plaintiffs' evidence regarding reasonable wholesale gasoline prices was limited to an unduly localized range of other retailers' prices by pointing out that plaintiffs' method "is the same benchmark that the defendants used in their [] pricing model," under the disputed contract. *Id.*

About the Author Sean D. Magenis is an associate with Friedman Gaythwaite Wolf & Leavitt in Portland, Maine where he focuses on litigating, arbitrating and mediating commercial disputes.

June 30, 2008

Federal Circuit Update



- **Federal Circuit Rejects Change of Counsel as Justification Warranting Review of Argument Raised for First Time on Appeal**
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- **Federal Circuit Holds Certificate of Correction Effective Even If Secured After Accused Activity Began**

- **Federal Circuit Says TSM Test Remains Applicable to Unobviousness Analysis Under *KSR* Standards**

- **Federal Circuit Rejects Change of Counsel as Justification Warranting Review of Argument Raised for First Time on Appeal**

Federal Circuit Rejects Change of Counsel as Justification Warranting Review of Argument Raised for First Time on Appeal

Golden Bridge Technology, Inc. v. Nokia, Inc., ___ F.3d ___ (Fed. Cir. xml:namespace prefix = st1 ns = "urn:schemas-microsoft-com:office:smarttags" />May 21, 2008)

In *Golden Bridge*, the Federal Circuit emphasized the impropriety of raising arguments not considered by the trial court and rejected the notion that a change of counsel on appeal was a circumstance meriting appellate review of such a new argument. In the case before it, the District Court had granted summary judgment of invalidity based on anticipation. On appeal the patentee, represented by new appellate counsel, argued that the anticipatory reference lacked a synchronization feature required by the claims. This argument had never been raised below; rather:

Golden Bridge unequivocally admits that its factual contention is an entirely new argument raised for the first time on appeal and never presented to the district court.

Moreover, Golden Bridge did not argue that it had been prevented from making the argument below. Indeed, Golden Bridge had had many opportunities to present the argument, but had chosen to argue other distinctions over the cited reference. The Federal Circuit declined to review the newly made argument because:

We cannot sanction the iterative process Golden Bridge would like to pursue. It would be unfair to allow Golden Bridge to bring some arguments distinguishing the Hakkinen reference during proceedings at the district court and then, only after those arguments have been completely rejected, bring entirely different arguments on appeal for the first time.

The Federal Circuit reaffirmed that review of newly raised arguments on appeal is proper in only limited circumstances, such as changed legislation, changes in controlling precedent, or to apply the correct law to an issue properly before the court. And the Federal Circuit expressly rejected a change of counsel as a justification for appellate review of a newly raised issue:

The only explanation offered by Golden Bridge for why this court should consider this new argument on appeal is that it has new appellate counsel. Substitution of new appellate counsel is not one of, or even in proportion to, the limited circumstances outlined in *Forshey*. New appellate counsel does not present an exceptional case or circumstance in which our declining review will result in injustice. To hold otherwise would open the door to every litigant who is unsuccessful at the district court to simply hire new counsel and then argue he should get to raise new issues on appeal.

Federal Circuit Holds Certificate of Correction Effective Even If Secured After Accused Activity Began

E.I. du Pont de Nemours & Co. v. MacDermid, Inc., ___ F.3d ___ (Fed. Cir. May 14, 2008)

In *du Pont*, the patentee had secured a certificate of correction to correct the patent's continuity data. Specifically, the patent as originally issued did not reference a provisional application as the priority date of the patent.

The certificate was secured after the accused activity began, but before the lawsuit was filed. In finding the certificate had been properly secured, despite the patentee's failure to correct the error either during prosecution or in the published application, the Federal Circuit stated:

It is, of course, desirable to have applicants correct the PTO's mistakes in pending applications as soon as possible so that the correct information is reflected in published applications and issued patents. Nevertheless, nothing in the statute conditions eligibility for a certificate to correct PTO error on the applicant's diligence in correcting the mistake, and the statute does not set any time limit for seeking such corrections. . . . Additionally, because there is a requirement that such certificates issue only if the mistake is "clearly disclosed by the records of the [PTO]," the chance that competitors will be harmed by any delay is minimal.

In addition, the Federal Circuit found the certificate was effective against the accused infringer despite having been secured after the infringing activity began. The Federal Circuit found that *Southwest Software Software, Inc. v. Harlequin, Inc.*, 226 F.3d 1280 (Fed. Cir. 2000), which held that a certificate of correction is effective only for causes of action arising before it issues, was distinguishable, both because the certificate in *du Pont* was only being applied to acts of infringement that occurred after the certificate issued and because it had been secured before the lawsuit was filed.

Federal Circuit Says TSM Test Remains Applicable to Unobvious Analysis Under *KSR* Standards

Ortho-McNeil Pharmaceutical, Inc. v. Mylan Laboratories, Inc., ___ F.3d ___ (Fed. Cir. March 31, 2008)

In *Ortho*, the patent contained claims directed to topiramate, an epilepsy drug that had been discovered while the inventor was engaged in a search for antidiabetic drugs. Topiramate was a reaction intermediate in the synthesis of the drugs being researched for antidiabetic activity.

Because there was no proof that a skilled person would have started with the chosen material, would have selected the synthesis route that led to the intermediate, would have stopped at that intermediate or would have tested it for epilepsy, the Federal Circuit concluded "This clearly is not the easily traversed, small and finite number of alternatives that *KSR* suggested might support an inference of obviousness."

The Federal Circuit concluded that teaching, suggestion or motivation (TSM) test remains key to an obviousness analysis even under *KSR*:

As this court has explained, however, a flexible TSM test remains the primary guarantor against a non-statutory hindsight analysis such as occurred in this case. *In re Translogic Tech., Inc.*, 504 F.3d 1249, 1257 (Fed. Cir. 2007) ("[A]s the Supreme Court suggests, a flexible approach to the TSM test prevents hindsight and focuses on evidence before the time of invention."). The TSM test, flexibly applied, merely assures that the obviousness test proceeds on the basis of evidence – teachings, suggestions (a tellingly broad term), or motivations (an equally broad term) – that arise before the time of invention as the statute requires. As *KSR* requires, those teachings, suggestions, or motivations need not always be written references but may be found within the knowledge and creativity of ordinarily skilled artisans.

About the Author Terri Gillis is a partner in the New York office of Howrey LLP. She specializes in intellectual property litigation, including both trials and appeals. She has handled litigation in many technologies, including medical imaging, pharmaceuticals, digital cameras, diagnostic methods and medical devices.

June 30, 2008

Fifth Circuit Update



• Novation Requires an Existing Prior Obligation and Clear and Unequivocal Evidence of Intent

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• An Arbitration Agreement is Illusory if One Party Retains the Unilateral, Unrestricted Right to Terminate It

• Unambiguous Contractual Provisions Providing Interpretive Authority to a Party are Enforceable Unless Interpreting Party is Shown to Have Acted in Bad Faith.

• No Exception to Texas's Economic Loss Rule for Post-Sale Negligence Claims

Novation Requires an *Existing* Prior Obligation and Clear and Unequivocal Evidence of Intent.

Langhoff Properties, LLC v. BP Products North America, 519 F.3d 256 (5th Cir. 2008), began as a lawsuit to recover damages for contamination of Langhoff Properties, LLC's ("Appellants") leased property and possible contamination of its adjacent property. Specifically, in 1966, Plaintiffs-Appellants, directly or through their predecessors in interest, leased immovable property in New Orleans, Louisiana to Defendant-Appellee BP Products North America, Inc., formerly American Oil Company or Amoco ("BP Products"), its successors and assigns, for BP Products to operate a fuel and automotive service station there. Appellants appealed the district court's grant of summary judgment in favor of BP Products, which the district court grounded solely in its conclusion that a subsequent lease of the same property signed by Appellants and Star Enterprise ("Star") on August 12, 1996 but effective August 15, 1996 (the "Star Lease") constituted a novation of the prior lease (the "Amoco Lease"), which had been executed in 1966 by Appellants and BP Products, had been extended from time to time, and had expired on August 14, 1996. The district court further ruled that an effect of this novation was to release BP Products from any duties that it might have owed to Appellants *in solido* with Star, the last assignee of the lessee's interest under the Amoco Lease and the original lessee under the Star Lease.

Under Louisiana law, the Amoco Lease constituted an "obligation" between Appellants and BP Products, specifically a conventional obligation or contract. By virtue of this legal relationship, Appellants and BP Products each possessed particular rights and owed particular duties with respect to one another. Novation under the Louisiana Code refers to the substitution of a new obligation for an existing one, rather than any substitution of the correlative rights and duties attendant on the old or new obligations. Within this framework, Appellants insisted that the Star Lease could not constitute a novation of the Amoco Lease because (1) the Amoco Lease expired by its own terms before the Star Lease took effect, and (2) BP Products failed to meet its Civil Code-imposed burden of proving Appellants' "clear and unequivocal" intention to novate.

Louisiana Civil Code article 1879 defines novation as "the extinguishment of an existing obligation by the substitution of a new one." In its analysis of whether the Star Lease constituted a novation of the Amoco Lease, the Fifth Circuit analyzed:

It is foundational, then, that for a novation to even occur, there must be an existing obligation for the new one to replace. As such, the basic code definition of novation eschews a holding that the Star Lease constituted a novation of the Amoco Lease: The Amoco Lease was one obligation; it expired (albeit with particular duties of the parties remaining to be performed); the Star Lease came into effect after the Amoco Lease expired; *ergo* the Star Lease was not a novation of the Amoco Lease but a wholly new obligation, with all rights and duties of the parties thereto on a going-forward basis only.

Louisiana Civil Code article 1880 states that “[t]he intention to extinguish the original obligation must be clear and unequivocal. Novation may not be presumed.” Further, Louisiana law recognizes that the intention to novate may be determined from the express terms of the agreement in question, the nature of the transaction, and the facts and circumstances surrounding the transaction. The burden of proving novation lies with the party insisting that one occurred.

BP Amoco insisted that the merger clause of the Star Lease provided clear and unequivocal evidence of the parties’ intent to novate. However, the Fifth Circuit held that the boiler plate merger clause of the Star Lease was in no way probative of the parties’ intent concerning a novation and should never have entered into the district court’s contract construction calculus. Rather, the merger clause should have been given nothing more than its widely recognized meaning, *viz.*, ensuring that all of the issues negotiated by the parties to the Star Lease were incorporated into the written lease agreement and that no prior communications during the negotiations, written or oral, could be used subsequently to alter the rights and duties set forth therein. The Fifth Circuit further held:

As a conventional obligation under the Civil Code, the Amoco Lease was “dead and gone” - and thus legally unsusceptible of novation - by the time the Star Lease came into existence ... [T]he Star Lease was a new obligation, intended to govern the parties’ rights and duties going forward and not affecting any prior obligations between these parties and any third parties.

In so doing, the Fifth Circuit reversed the district court’s grant of summary judgment in favor of BP Products, held that the Star Lease was a new contract and not a *novation* of the expired Amoco Lease, and remanded for further proceedings consistent with its opinion.

An Arbitration Agreement is Illusory if One Party Retains the Unilateral, Unrestricted Right to Terminate It.

In *Morrison v. Amway Corporation*, 517 F.3d 248 (5th Cir. 2008), Appellants’ (collectively, “Distributors”) complaints center upon their relationships with Appellee Amway Corporation and distributorships within Amway Corporation (collectively, “Amway”), a multinational seller of household products in existence since 1959. In order to distribute Amway products, every Amway distributor signs Amway’s standard distributorship agreement, which “confer[s] a right to distribute Amway products, and the right to receive sales commissions or ‘bonuses’ on any products sold, for a period of one year.” Among other things, the distributor agrees to pay an annual fee and to abide by Amway’s Code of Ethics and Rules of Conduct “as amended and published from time to time in official Amway literature.” This agreement must be renewed annually, “no later than December 31” for the following calendar year. In September 1997, Amway informed Distributors it was amending the Rules of Conduct to include an arbitration program, communicating through publication in its official magazine, the Amagram, and other media sent directly to distributors. The arbitration provision, added to the 1998 Rules of Conduct, provided for arbitration for “any ... claim or dispute arising out of or relating to [an] Amway distributorship, the Amway Sales and Marketing Plan, or the Amway Rules of Conduct (including any claim against another Amway distributor, or any such distributor’s officers, directors, agents or employees, or against Amway Corporation, or any of its officers, directors, agents or employees).” There is no dispute that all Distributors renewed their distributorship agreements after Amway gave notice of implementation of the arbitration program.

On January 8, 1998, a group of Distributors sued Amway and other defendants in Texas state court alleging a number of federal and state law claims, ranging from defamation to RICO. Amway (and the other defendants) on February 6, 1998 timely removed the case to the district court under 28 U.S.C. § 1441(b), and then filed a motion to stay the suit pending arbitration. Distributors argued against the stay, contending *inter alia*, that the Arbitration Agreement was not binding on them. On October 15, 1998, the district court granted Amway’s motion and stayed the suit pending arbitration.

On May 18, 2001, the Distributors requested arbitration under the arbitration agreement. On June 14, 2001, Amway and other defendants filed counterclaims in the arbitration. On August 17, 2001, the Distributors filed a motion for “Summary Disposition” in the arbitration, contending, *inter alia*, that there was no valid agreement to arbitrate, that if there were such an agreement it did not apply, or could not properly apply, to disputes, such as those involved in the instant proceeding, which arose and were ongoing and known to Amway prior to the September 1997 amendment to Amway Rules of Conduct which introduced the arbitration program, and, further, that the arbitration program “is inherently unfair” because Amway “selected and trained the arbitrators” and “hold[s] the exclusive power to remove unwanted” arbitrators. Amway and the other defendants filed a response and their own motion for summary disposition. On October 15, 2001, the arbitrator Anne Gifford denied (without explanation) both motions for summary disposition.

JAMS, the arbitration services provider for Amway, provided the parties with the names and biographical information of five neutrals “who had ‘completed the training course for Arbitrators offered by [JAMS/Endispute], and conducted by Amway and the Amway Distributors Association [ADA].” From among those listed, the parties ultimately selected Anne Gifford to arbitrate the dispute, and she was appointed as Arbitrator. On October 9, 2001, Gifford disclosed to the parties that she had attended a 1998 training session conducted by Amway and had subsequently conducted mediation training of certain Amway employees.

On January 13, 2005, Gifford ruled in favor of the Distributors on all of Amway’s claims and in Amway’s favor on all of Distributors’ claims; fees

and costs were awarded to each prevailing party, thereby resulting in an award of \$7 million to Amway offset by an award to Distributors of \$1 million. The ruling contains no analysis and states no reasons. Distributors moved in the district court to vacate the award alleging *inter alia*, Gifford's partiality and corruption as well as the unenforceability of the arbitration agreement. Amway and the other defendants moved the district court to confirm the award and enter judgment on it. The district court ultimately denied the motion to vacate and confirmed the award. Distributors moved for rehearing which the district court denied. Distributors filed their notice of appeal to the Fifth Circuit.

The Distributors assert that the district court erred in its October 15, 1998 order staying their suit pending arbitration. In this respect, the Distributors contend, among other things, that the district court erred by compelling arbitration because an enforceable arbitration agreement never existed. There is no disagreement that there was a written arbitration policy in effect between the Distributors and Amway at the time the suit was filed. However, Distributors claim the arbitration agreement was not valid and enforceable.

In reviewing the arbitration agreement, the Fifth Circuit found that there was nothing in any of the relevant documents which precluded Amway's amendment to the arbitration program - made under Amway's unilateral authority to amend its Rules of Conduct - from eliminating the entire arbitration program or its applicability to certain claims or disputes so that once notice of such an amendment was published, mandatory arbitration would no longer be available even as to disputes which had arisen and of which Amway had notice prior to the publication. Citing to the Texas Supreme Court in *J.M. Davidson, Inc. v. Webster*, 128 S.W.3d 223, 230 n.2 (Tex. 2003), the Fifth Circuit set forth the rule that "if a party retains the unilateral, unrestricted right to terminate the arbitration agreement, it is illusory." Ultimately, the Court held that the Amway arbitration agreement was illusory and unenforceable under *Davidson*. The Fifth Circuit reversed the district court's October 15, 1998 order staying the case pending arbitration and the district court's September 15, 2005 final judgment, and remanded the case for further proceedings.

Unambiguous Contractual Provisions Providing Interpretive Authority to a Party are Enforceable Unless Interpreting Party is Shown to Have Acted in Bad Faith.

In *Kern v. SITEL Corporation*, 517 F.3d 306 (5th Cir. 2008), Kern was hired by SITEL as Vice President, Business Development in 2003. His contract included a base salary of \$110,000.00 and the possibility of earning an incentive payment based on his sales performance. Specifically, the contract stated that Vice Presidents, Business Development receive incentive compensation for new SITEL services business sold to new accounts and new SITEL services sold to existing accounts. Vice Presidents, Business Development were to be compensated for all SITEL services that are invoiced to clients during the fiscal year. In sum, the incentive payment was based on the budgeted target revenue: if a vice president reached 100% of their target revenue, they were entitled to 100% of their incentive payment. The incentive payments could reach up to 250% of their base salary if sales were twice the target revenue.

In 2004, Kern's target revenue was eight million dollars (\$8,000,000.00) and he generated a total invoiced revenue of \$16,846,659.50. Accordingly, Kern argued that he was entitled to 250% of his base salary, because his invoiced revenue was twice the amount of the target revenue. However, SITEL interpreted the incentive payment provisions differently and capped Kern's incentive payment at \$150,000.00. Kern sued SITEL seeking the remaining \$125,000.00 in additional incentive pay.

The parties rely on the language of two provisions of Kern's contract: sections 6.0 and 20.0. First, section 6.0 states that the Business Unit President and Vice President of Human Resources Representative will resolve disputes over interpretation of any aspects of this plan and such decision of the Business Unit President shall be final. Section 20.0 states that all Vice Presidents, Business Development, the maximum incentive payment that can be received in one fiscal year for any one account contract is \$150,000.00. However, there was no limit to the number of large account contracts that can be sold by any one Vice President, Business Development.

Kern argues that the 20.0 "one account contract" language unambiguously means that incentive payments are maxed out for any one sales contract. Kern also argues that SITEL's interpretive powers under section 6.0 cannot be triggered if the language of the contract is unambiguous. Conversely, SITEL argues that its "one account contract" interpretation must stand, because it was contractually given the right to interpret Kern's contract. SITEL further argued that unless its interpretation was made with fraud, in bad faith, or with gross mistaken exercise of judgment, SITEL's interpretation is final.

In addressing both parties' arguments, the Fifth Circuit first determined whether section 20.0 was unambiguous. A contract is ambiguous when its meaning is uncertain and doubtful or it is reasonably susceptible to more than one meaning. SITEL argues that "one account contract" language in section 20.0 means one "client" and that this phrase caps the incentive bonus Kern can receive on all sales to a particular client. Kern argues that "one account contract" caps the incentive bonus he can receive on any one individual sale. So, Kern's interpretation is that a Vice President, Business Development cannot earn more than a \$150,000.00 incentive payment on any one sale/contract, but there is no limit on the number of sales/contracts he can make to any one client. The Court agreed with Kern's argument, because SITEL's interpretation was unreasonable. SITEL's interpretation that "one account contract" refers to an individual client would render the second part of section 20.0 meaningless. Therefore, the Court held the "one account contract" language unambiguous.

The Court then determined the effect of section 6.0 and SITEL's interpretive rights. Kern argues that because the 20.0 language is unambiguous, SITEL has no right to interpret a different meaning than its plain meaning. The Court notes that no Texas case law has addressed the effect of a contract provision granting interpretation rights and its effects if the contract is unambiguous. However, prior Fifth Circuit case law addressed a similar issue involving a Trustee and a pension plan that stated "all decisions of the Trustees in administering the Plan shall be final." The Court held that such language did not accord complete and unbridled discretion to the Trustee, but found that Texas law required such a provision to be given effect unless there was a showing that the Trustee acted in bad faith.

Accordingly, the Court held that prior Fifth Circuit cases required the Court to honor SITEL's interpretive rights under section 6.0 so long as SITEL did not act in bad faith. Therefore, even though SITEL erred in its interpretation of "one account contract" in section 20.0, unless this error was made in bad faith, SITEL retains final interpretive authority over "any aspect" of the contract. As a result, SITEL's determination that Kern is owed only \$150,000.00 in incentive pay must stand.

The Court finally addressed whether SITEL acted with bad faith in its interpretation of the incentive pay. Bad faith may be established by direct evidence or indirect evidence such as unreasonable requirements, refusal to consider favorable information, or the use of standards more strict than those applied to others similarly situated. SITEL argued that Kern put forward no evidence of bad faith and that SITEL consistently interpreted section 20.0 and applied this provision equally to other Vice Presidents. Therefore, the Court held SITEL did not act in bad faith, SITEL retains interpretive authority under section 6.0, and Kern is entitled only to the \$150,000.00 incentive pay SITEL awarded.

No Exception to Texas's Economic Loss Rule for Post-Sale Negligence Claims

In *Memorial Hermann Healthcare System, Inc. v. Eurocopter Deutschland, GMBH*, 2008 WL 1113339, (5th Cir. 2008), Memorial Hermann Healthcare Systems, Inc. ("Memorial Hermann") and United States Aviation Underwriters, Inc. ("USAU") appeal the dismissal of their post-sale negligence claim against Eurocopter Deutschland ("Eurocopter"). Memorial Hermann and USAU (collectively, "Appellants") claim that the district court erred when it refused to carve out an exception for post-sale negligence claims to Texas's economic loss rule. Specifically, Memorial Hermann owned and operated a Eurocopter BK 117 helicopter that it bought from the manufacturer, Eurocopter. The helicopter's left door separated from the helicopter and struck its rotor blades. The impact severely damaged the helicopter but caused no additional harm or injuries. Memorial Hermann brought suit against Eurocopter for post-sale negligence. Memorial Hermann claimed that, by voluntarily issuing safety warnings and updates to its customers, Eurocopter assumed a duty to warn its customers of defects to its products. According to Memorial Hermann, Eurocopter breached this duty when it negligently failed to warn Memorial Hermann of a potential door defect even though it had prior knowledge of a similar accident involving another BK 117 helicopter.

Eurocopter subsequently moved to dismiss on two grounds: (1) Eurocopter contended that it did not have a duty to warn its customers of defects discovered after the helicopter was manufactured; and (2) Eurocopter claimed that, even if it had this duty, Texas's economic loss rule barred Memorial Hermann from recovering only economic losses. The district court agreed with Eurocopter that Texas's economic loss rule precluded recovery and dismissed Memorial Hermann's claim.

The Fifth Circuit analyzing the Texas economic loss rule found that, no duty in tort exists when plaintiffs have suffered only economic losses. Therefore, in Texas, the economic loss rule bars plaintiffs from recovering economic losses resulting from a defective product based on a negligence theory. Moreover, citing the seminal case of *Jim Walter Homes, Inc. v. Reed*, 711 S.W.2d 617, 618 (Tex. 1986), the Fifth Circuit wrote that the Texas Supreme Court has unequivocally adopted a broad interpretation of the economic loss rule. According to the Texas Supreme Court, "the nature of the injury" may preclude plaintiffs from seeking relief in tort, and "[w]hen the injury is only the economic loss to the subject of a contract itself, the action sounds in contract alone." *Id.* Further, the Court found that implicit in the economic loss rule is the premise that the tort concern with safety is reduced when an injury is only to the product itself. Therefore, despite Appellant's request, the Fifth Circuit refused to carve out an exception to Texas's economic loss rule for post-sale negligence claims. Ultimately, the Fifth Circuit affirmed the district court's dismissal.

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June 30, 2008

"On Point" is a great legal news blog which can be found at <http://www.onpointnews.com/>. The site, edited by Matthew Heller, covers serious cases reported on by national news outlets, such as the removal of children from the FLDS compound in Texas, but also a large assortment of less widely-reported cases, such as the \$1M fraud case filed by an Ohio woman against a psychic who allegedly falsely promised to resolve the woman's "personal problem". On Point also recently wrote about a Minnesota appellate court which ruled in favor of an insurer which had denied coverage for the death of a homeowner's guest which was caused by an overdose of methamphetamine provided by the homeowner and a settlement reached between a New York restaurant and the woman its manager kicked out of its women's restroom for looking too much like a man. There is plenty of coverage of legal news, such as the litigation between Rob Lowe and his former nannies, and the numerous parties who have filed suit against actor Sacha Baron Cohen over the filming and release of the blockbuster movie "Borat".

The sections of On Point entitled "On File", "On Trial", and "On the Docket" are also a quick and fun read, featuring humorous or significant recently-filed documents, recent verdicts and noteworthy hearings and court appearances. The "Extra Points" section also provides quick links to timely decisions in cases such as the recent reversal of the \$32M Vioxx verdict and the answer recently filed by You Tube in litigation brought by Viacom.

About the Author Erin K. Russell is an associate in the Atlanta, Georgia office of Hawkins & Parnell, LLP. Erin specializes in complex litigation matters in the areas of professional liability, transportation and products liability litigation. She can be reached at (404) 614-7554 or erussell@hplegal.com.

June 30, 2008

For a less serious site poking fun at our species, check out www.thepartyofthefirstpart.com. Really a blog, it is written by a recovering litigator and author, and contains some of the most ridiculous pieces of legalese we've ever seen.

June 30, 2008

SAVE THE DATE! On September 4-5, 2008, the Commercial Litigation Committee will present its Intellectual Property Seminar at The Drake Hotel in Chicago, Illinois. A lineup of blockbuster speakers will address common IP issues, from trademarks to trade secrets, as applied to the video presentation of a unique hypothetical. Complete with fantastic social events and networking opportunities, this is one Seminar you don't want to miss!

June 30, 2008

How Can I Get Involved in the Committee?

Join a Specialized Litigation Group!

Our Committee has 9 practice area specialized litigation groups. Each has a chair whose email address is listed below. Click and join:

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The Commercial Litigation welcomes articles from our membership for the Business Suit. Your article should be of interest to your fellow committee members and have a national focus. Submit completed articles for consideration to our Business Suit editors, Christine Mast cmast@hplegal.com, Bill Ireland wireland@hbblaw.com and Rob Bodzin rbodzin@burnhambrown.com. Click [here](#) for some practical tips to successfully publish with the committee.

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Defense Library Series - Suggest And Write for a Compendia!

Our Committee regularly publishes a compendia of articles unified by a theme. These can be a great way to get published and get active in the Committee. If you have an idea, please email Publications Chair Christine Mast [Christine Mast](#). Click [here](#) for past compendia and [here](#) for writer's guidelines. Plans are also in the works for a new yearly compendium of articles from the members of each of the SLGs. We'll be soliciting articles from the members of each SLG each year to form a collection. Email [Christine Mast](#) or your SLG Chair if you have article ideas.

Publish in The Voice?

Our Committee publishes a lead article in The Voice approximately quarterly. If you have an idea for an article that would cover a current, substantive legal issue that is relevant to our Committee and engage other DRI members, please send ideas to our Publications Chair [Christine Mast](#). Click [here](#) for Voice writer's guidelines.

For the Defense Articles

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In-House Defense Quarterly

On occasion, our Committee submits singlet articles to In-House Defense Quarterly. If you have ideas for a stand-alone article, please send ideas to our Publications Chair [Christine Mast](#).

July 02, 2008

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These webconferences will provide participants with a solid foundation in the basics of patent, trademark and copyright law and litigation. Designed for litigators and in-house counsel who are not typically involved with these types of IP disputes, the courses provide a primer for navigating the sometimes mysterious documents in the IP world.

July 03, 2008



DRI's newest magazine, ***In-House Defense Quarterly (IDQ)***, addresses the specific needs of in-house defense counsel with feature articles written by experienced DRI members. Each issue is loaded with substantive information and reports acquired from leading content providers. Read about the latest trends and hot topics vital to in-house counsel. **IDQ** is a free benefit to corporate members. All others can receive this valuable resource for just \$20 per year. To begin your subscription, simply [click here](#) to fill out and return the subscription form.

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