ASSOCIATION OF BUSINESS TRIAL LAWYERS

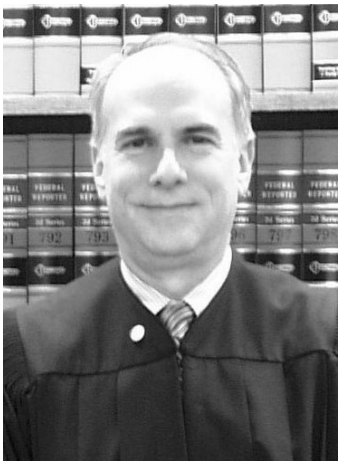
abtl REPORT

ORANGE COUNTY

Volume VIV No. 4 Winter 2007/2008

Q&A with the Hon. Robert N. Block

By Linda A. Sampson



[Editor's Note: This judicial interview is with United States District Court Magistrate Judge Robert Block. Prior to his appointment in February 1995, Judge Block was a successful general business litigator at Mitchell, Silberberg & Knupp.]

Q: *You have been a magistrate judge in Los Angeles for over 12 years. What made you decide to move to Orange County?*

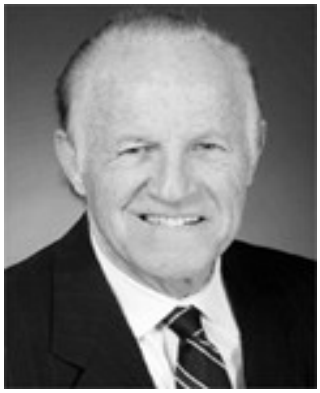
A: It was a combination of timing and personal reasons. The Court decided that a third Magistrate Judge position in our Southern Division was warranted based on the number of District Judges assigned to Orange County, and I requested that I be allowed to fill that third position. The personal reasons included the fact that my tenure as

-Continued on page 5-

-IN THIS ISSUE-

Why Clients Change Lawyers in the Middle of a Case

By Thomas R. Malcolm and John A. Vogt



For a lawyer, being fired by your client is a difficult and humbling experience, particularly where you have spent months or years working on a matter or investing in what you hoped would be a long-term client relationship. The lawyer, however, has it easy. Put yourself in the shoes of the client who must make the decision whether to change counsel midstream. What factors should a client dissatisfied with its counsel consider? There are several, and this issue has undoubtedly caused clients and general counsel many a sleepless nights.

First of all, the costs can be steep. The new counsel who are brought into a case will require a learning curve, and the client will find itself paying twice for the same work as the new lawyers spend time reviewing the file and bringing themselves up to speed. The more complex the case, and the higher the stakes, the higher these costs will be. Complex cases can often involve millions of pages of documents and files that fill an entire room. All of this information must be physically and mentally transitioned from the old counsel to the new. New counsel will also need to establish and/or repair relationships with opposing counsel and, depending upon how the matter has gone, may also have to rehabilitate the client's image with the court. Finally, the replaced lawyer usually is entitled to be paid for work already done. For lawyers

-Continued on page 8-

The President's Message

By James G. Bohm

As I muse over what to write about in my last President's report, I can't help but reflect back on last year — both the challenges and the accomplishments for the ABTL Orange County Chapter. I really can't believe that my term is over already; it seems like it just began. I was very fortunate to take over the reigns of the organization from outgoing President Gary Waldron. Gary left the organization is such good order that it was easy to assume responsibility. He is a shining example of all the positive attributes of a great business trial lawyer (with particular emphasis on the word "trial"). Gary has significant trial experience ending his term as president nearly simultaneously with obtaining a $20 million judgment in favor of his client. Thank you Gary for leaving the ABTL in such good shape.

Shortly after being installed as President, I received news that our long time executive director Becky Cien was resigning to relocate with her family to Texas. We were all thankful for her many years of service and wished her and her family well in their new endeavors. We then undertook the laborious task, along with the Los Angeles chapter, to find a replacement. We were fortunate enough, after more interviews than I care to count, to have found Adrienne King who stepped into the role as the executive director of both the Orange County and Los Angeles chapters. Adrienne undertook this new role with enthusiasm and I thank Adrienne for all her hard work and her great attitude.

One of the things the ABTL Orange County Chapter is long known for is its support of the Public Law Center. Every year, we have exceeded our previous year's donation. This year was no exception. We have been told by PLC that we are the single largest contributor. Thank you everyone for making this year's PLC dinner such a success by attending the program, purchasing wine and raffle tickets, making direct donations and supporting the cause. I particularly want to thank Kathleen Peterson for taking the lead on organizing the event. Because the PLC dinner has been such a success, the Board wanted to extend its charitable endeavors. Last year we had the first annual Orangewood benefit. We were successful in col-

-Continued on page 8-

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ABTL: Setting High Standards in the Community

By Hon. Sheila B. Fell

It has been two years since I had the honor of serving as the seventh President of our ABTL chapter. Since turning over the gavel to Gary Waldron, we have continued to grow and set a high standard in the legal community.

During my presidency, I submitted my humble opinions on matters relating to integrity and professionalism. The time since my tenure has confirmed my belief that our association is characterized by the assembly of ethical, professional leaders of the Orange County Bar.

The professional education programs that we have enjoyed from members and guest presenters are each designed to share professional experiences and techniques of litigation. We have shared these techniques honed by many years of winning courtroom endeavors.

I recall discussions with other Bench Officers relating to the legal results obtained by skilled litigators handling cases in their courts. The competence and credibility of our members is well recognized in the judgments awarded as a consequence of the competency in advocacy. The success of our members has also translated into financial rewards directly related to the professional management of the legal issues related to their cases.

The ABTL envisions a collegiality of Judicial Officers and the ABTL members. The cordiality is designed to enhance the professional interaction in the court system; a relationship which inures to the benefit of the litigants.

From the judge's perspective on the bench, those times when we are the triers-of-fact, we thoroughly enjoy the trial product of experienced and competent counsel. We can also recognize the tangible results returned by jurors who can understand and rule on the evidence presented by competent counsel.

We have all joined in this partnership of legal participation to strive for professional excellence in our practice. This participation of lawyers and judges in our na-

-Continued on page 11-

Autumn "Brown Bag Lunch" Series with the Hon. Andrew Banks, Corey Cramin and David Velasquez

By Jacqueline Beaumont and Adrianne Marshack

This fall, we had the opportunity to meet with several judges from the Orange County Superior Court as part of a series of lunch discussions sponsored by the ABTL.

The Hon. Andrew Banks
and
the Hon. Corey Cramin

On Wednesday, October 17, 2007, the Honorable Andrew P. Banks hosted a discussion for several attorneys in his courtroom, with a surprise guest—the Honorable Corey S. Cramin. Judge Banks began his judicial career in the Municipal Court in 1997, and was elevated to the Orange County Superior Court in 1998. Judge Cramin was appointed to the Municipal Court in 1992 and elevated to the Orange County Superior Court in 1997.

We were fortunate to have both judges present to compare their perspectives on various stages of litigation. Addressing oral argument, the Judges stressed that an attorney should tailor her choices to the individual judge presiding over the case. Judge Banks admitted that he prefers attorneys to use two simple words at oral argument: "I submit." He remarked that he usually only wants oral argument if there is a new case directly on point. Judge Banks advised us that in the rare situation where he does not make a "tentative" ruling, it is for one of two reasons: either (1) he is perturbed by the arguments made and does not want to embarrass an attorney in public, or (2) there is an issue he wants to discuss at oral argument.

Judge Cramin said that attorneys appearing before him should speak up at oral argument if they believe he missed something in his tentative

-Continued on page 13-

Increasing Your Chances of Reversing an Unfavorable Trial Court Result

By Robert M. Dato

When you're preparing a case for trial – or actually trying it – it's often difficult to see how someone else might view it on appeal in a year or two. Or in a writ proceeding a few months later. But if things turn sour for your client in the trial court, you'll want to raise and preserve as many issues as you can that might convince an appellate court to reverse the trial judge. Here are a few particularly "hot" issues to look for in business litigation and suggestions for how to raise them:

Discovery Issues.

Most appellate review of discovery issues occurs via writ proceedings. Traditionally, such review has been difficult to obtain. But there are at least two areas concerning discovery that have recently generated considerable appellate activity:

A. Precertification Discovery in Class Actions.

In class actions, under what circumstances should discovery be allowed before the class is certified? This general question produced no less than three published decisions in 2007. In *Pioneer Electronics (USA), Inc. v. Superior Court* (2007) 40 Cal.4th 360, our Supreme Court held that class counsel could obtain personal information of consumers from Pioneer where those consumers had complained to Pioneer about the product was at issue in the class action. In *First American Title Ins. Co. v. Superior* Court (2007) 146 Cal.App.4th 1564 and *Cryoport Systems v. CNA Ins. Cos*. (2007) 149 Cal.App.4th 62, the Courts of Appeal held that a "class representative" with no individual standing could not use precertification discovery to identify a more appropriate class representative. In each of these cases, the defendant challenged precertification discovery early and often, fleshing out the issues not only for the trial court but for the reviewing court as well.

-Continued on page 9-

A WORD FROM OUR SPONSOR: Business Valuation Issues Involving Subchapter S Corporations

By Daniel C. Curren

In recent years, the valuation of subchapter S corporations has been one of the most controversial issues facing the business appraisal profession. The primary issue at hand involves whether or not a Subchapter S corporation (or an interest in it) is worth more than an otherwise identical C corporation. This issue arises because the earnings of a Subchapter S corporation "pass through" to shareholders who are taxed at individual rates, while C corporation earnings are taxed at the corporate level first, and then taxed again at the shareholder level, when received as dividends.

Generally speaking, practitioners used to tax-affect S corporation earnings as if they were a C corporation when using publicly traded stock market information to derive a discount or capitalization rate. While tax-affecting S corporation earnings was the generally accepted practice for years, the benefits of single taxation related to S corporations has been long debated. The continuing debate regarding S corporation valuation issues combined with a dramatic increase in the number of S corporations (800,000 in 1986 and 3,400,000 by 2003) led to the issues coming to a head in the case Walter L. Gross, Jr., et ux, et al v. Commissioner. (T.C. Memo. 1999-254, No. 4460-97 (July 29, 1999), aff'd. 272 F.3s333 (6th Cir. 2001).)

In the Gross case, the expert for the taxpayer tax-affected the earnings and the expert for the IRS did not. When using a combined state and federal entity level tax rate of 40% for a C corporation, the IRS method of valuation (not tax-affecting) yields a value approximately **65% higher** than the value derived with tax-affected earnings. The following numerical example (simplified) presents the value difference of a company based on tax-affecting vs. not tax-affecting earnings.

-Continued on page 16-

ABTL OC: Rising and Shining
By The Hon. Andrew J. Guilford

It was sometime in the seventies. Gerald Ford was President. I was a callow youth sitting in a high-rise in downtown L.A. answering interrogatories and thinking there must be something more to being a trial lawyer. As the sun was setting over Santa Monica in the distance, senior partner Bill Masterson stuck his head in my office and invited me to an ABTL dinner. I marched off to the dinner, at the Broadway Plaza as I recall. There, for the first time in my life, I met many judges. It was clear that my future success as a trial lawyer depended largely on these judges (and on the partner I rode in with). At first the judges seemed like alligators in Old Spice (with not enough women judges), but after chatting a bit, they were actually very nice.

All in all, it was a good evening: needed time with my assigned partner, a good time with some judges, a good program on trials, my first taste of not too rubbery chicken, booze and a bottle of wine freely chitted to Sheppard Mullin, and a chance to be social – even human – with opposing counsel who had seemed demonic in a recent telephone conversation where I requested more time to answer interrogatories. Over my years in Los Angeles, that's what the ABTL was: a chance to meet judges, learn about trials, and break bread with lawyers in my firm and beyond.

Over time, the idea of lawyers and judges getting together to talk about trials has become even more important to me. I fear that today young lawyers become too isolated in glass towers. Too often, they deal with opposing counsel impersonally, and therefore rudely, in telephone calls and emails that are less likely to be productive and professional than when they have broken bread together. They lose touch with the important bottom line of our work: trials. Their answers to interrogatories therefore sometimes reflect irrelevant gamesmanship rather than practical answers with a focus on the trial. Sadly, young associates can even become isolated from their assigned partners. An ABTL dinner helps alleviate all these problems.

-Continued on page 6-

-Q&A: Continued from page 1-

Chief Magistrate Judge was winding down, and I was ready to try something different; my best friend on the court (and ski buddy), Judge Nakazato, was here in Orange County and encouraging me to make the switch; at the time, my son was attending a private school in Anaheim, which was in the opposite direction from our house as downtown Los Angeles; I knew from having sat down here a couple of times that the daily commute from my home, while equal mileage-wise, would be less stressful than the daily commute to downtown Los Angeles; and I loved the Santa Ana courthouse and the judges' chambers.

Q: *How has the transition been?*

A: From my perspective, extremely smooth and satisfying. I particularly enjoy having contact with all the other judges down here on a regular, if not daily, basis, and being able to maintain a general sense of what's going on in the courthouse. My sense is that the change has been akin to what I would have experienced going from a large law firm to a small law firm, which is something that I always was curious about.

Q: *Why did you originally decide to leave the practice of law to become a magistrate judge? Do you have any regrets?*

A: After 16 years, I no longer found the practice of law as fun as I had found it in my earlier years. Or, put another way, I no longer looked forward to going to work each day. One of the sitting Magistrate Judges, Judge Eick, who had been in my class at the firm and who was a close friend, encouraged me to apply for one of the vacant Magistrate Judge positions because he loved the job and thought I'd like it as well. He was right.

Q: *Any early influences leading to a career in law?*

A: I had no lawyers in my family, but my grandmother let me know early on that she expected me to become either a lawyer or a doctor. I liked watching Perry Mason more than Dr. Kildare.

Q: *Are there any particular types of matters that you are working on?*

A: Like the other Magistrate Judges, I spend the majority of my time working on three types of cases: habeas petitions brought by state prisoners, pro se civil rights

-Continued on page 6-

-Shining: Continued from page 5-

After growing with the ABTL in L.A. during my younger years, I moved to Orange County, which did not have an ABTL chapter. A partner predicted my career would necessarily collapse at "the beach" (as Pasadena partners liked to call the OC). The partner was wrong. Orange County provided a closely knit legal community, a good life, and a chance for a young guy to try lots of cases before friendly judges. It was also a vibrant, growing county. In a 1991 *President's Page*, called "Pride and Prejudice," I wrote:

> We are a community of about 2,500,000 people, making us the fifth largest county in the United States. Our economic output exceeds the GNP of all but 25 *nations* in the world. Want to make some money during half-time of Monday Night football? Ask your friends at the bar which of the following has the highest economic output: Orange County, Chile, New Zealand, Portugal, Israel, or . . . Iraq. The answer is Orange County, with twice the output of Chile! As a follow-up question for sports fans, ask which of the following won more gold medals at the 1988 Olympics: Orange County, Britain, France, China, Japan, or Canada. Again, the answer is Orange County, with twice as many as Japan and Canada! You can look it up. Someday soon, the N.B.A. and even the World Series will show up in Orange County. Really.
>
> And beyond the stats and sports are a spirit and quality of life in Orange County that cannot be quantified. Instead, it is reflected in artistic performances at places like SCR, the Grove Shakespeare Festival, and the Laguna Playhouse. It shines in glowing new creations such as the Performing Arts Center and the Orange County Airport. . . .
>
> The high *quality* of our judges and lawyers matches the high *quantity* of lawyers in Orange County. There are now more lawyers in Orange County than in most states! Stacked on top of each other, we lawyers would be about eight times higher than Saddleback Mountain. (Or nine times higher if

-Continued on page 12-

-Q&A: Continued from page 5-

actions, and social security appeals. I am assigned as the discovery judge on 1/3 of the cases filed here in the Southern Division, but that does not result in very many discovery motions or settlement conferences. I also serve as the criminal duty judge 1/3 of the time, which mostly involves conducting initial appearances and the post-indictment arraignment calendar, and issuing search warrants and arrest warrants.

Q: *Is your caseload different now that you are in Orange County?*

A: Not really. Habeas, civil rights, and social security cases are assigned off a district-wide wheel. The Court has a means of insuring that the number of discovery case assignments to the Magistrate Judges is equalized district-wide. On days when I serve as the criminal duty judge, the volume of work is much lower down here, but I serve as criminal duty judge six times as often, so the amount of time spent on criminal duty computes out to about the same as it was in Los Angeles.

Q: *What is the biggest mistake attorneys make before you?*

A: Here's one that comes to mind. Repeating arguments from their papers that my tentative ruling indicates I already have considered and rejected, instead of being responsive to my tentative ruling.

Q: *What are your pet peeves about the lawyers who practice before you?*

A: I've been asked this question before when I've sat on a civil practice panel. Here's my current list:

1. Filing ex parte applications where the attorney's own lack of diligence has created the urgency.

2. Asking me to do things which only the District Judge can order (e.g., extending the discovery cut-off date; issuing case dispositive sanctions).

3. Noticing motions in front of the District Judge which should have been noticed in front of me in the first place (which invariably results in me having less time to react).

4. Filing discovery motions without even purporting to comply with LR 37 (e.g., no attempt to meet

-Continued on page 7-

-Q&A: Continued from page 6-

and confer first; motion not presented in the form of a joint stipulation and no declaration of counsel explaining why not).

5. Filing discovery motions while purporting to comply with LR 37, but not really (e.g., sending a "meet and confer" letter which does not specify which responses are being disputed and why; demanding that the other side meet and confer at a specified time and place (invariably less than 10 days); not making a good faith effort at the conference to obviate the necessity for the motion by compromising (the "capitulate to my position or else" mentality); merely tacking two separate memoranda together and calling that a joint stipulation; failing to specify in the joint stipulation with respect to each issue in dispute how the party proposed to resolve the dispute at the conference; sandbagging the other side and the court by holding back legal arguments supporting that party's position until the supplemental memorandum (by which time I frequently already have worked up the motion)). If I perceive that counsel did not make a sufficient good faith effort to resolve their discovery dispute without court intervention, it is my practice to require lead counsel of record to appear before me to meet and confer further under my auspices.

6. Relying on the wrong substantive law (e.g., in a case where federal law will govern the privilege issues because there are federal claims involved, predicating your position on California cases when the federal rule is different; in diversity cases assuming that California law will govern, when there is a choice of law issue).

7. Citations without jump cites.

8. Being late to court.

Q: *Do you have any general guidelines for ruling on discovery motions that you'd like to share?*

A: When ruling on a discovery motion, I start from the following propositions: *First*, I will disregard any allegations by the defendant regarding the supposed frivolousness of the plaintiff's claims. My sole concern is whether the discovery sought falls within the scope of permissible discovery.

-Continued on page 17-

Thank You for Making Our First Annual ABTL Holiday Gift Giving Program a Success.

The Orange County Chapter of the ABTL collected gift cards totaling $1, 320.00 for donation to the Orangewood Children's Foundation. In early December, David Glidden (Orangewood's Executive Director) very gratefully accepted the gift cards from Jim Bohm and Justice Kathleen O'Leary.

We also had a wonderful showing of support for the Orange County Superior Court's adoption program. As you can see, we collected a very large number of stuffed animals. Thank you all.

-President: Continued from page 2-

lecting thousands of dollars in gift certificates and large bags of stuffed animals for these underprivileged children. I particularly want to thank Justice Kathleen O'Leary and Linda Sampson for playing such an important role in this event. I also want to thank Presiding Judge Nancy Stock for assisting with the collection of the stuffed animals so judicial officers can provide them to the children.

Keeping in line with one of our primary functions, we had some incredible programs last year. Gerry Klein did an exceptional job recruiting some of the top lawyers and most highly regarded judges in the field of business litigation to put on programs that were both informative and entertaining. Linda Sampson did a terrific job editing the ABTL Report which is also an important part of our organization's educational efforts. It is a lot of work and she did it cheerfully. I also want to thank each and every board member for their participation last year. Every single person made a significant contribution and their efforts were greatly appreciated. I particularly want to thank all judicial board members and advisory board members. One of the most attractive aspects of the organization is the opportunity for lawyers to interact with the judges on a less formal basis. Our organization has been very fortunate to have a significant attendance from the judiciary and we are all very grateful for that.

Finally, I want to thank the executive committee—Martha Gooding (this year's president), Sean O'Conner and Rich Grabowski. Each of these individuals contributed significantly in their time and effort in assuring that last year was such a success for the organization. We had regular in person meetings throughout the year and were in constant communication via email. There really isn't enough I can say about how great of a job they each did and how much easier they made my job. Any of the three of them could be counted on at any time to step up to the plate to handle any task. There aren't enough pages in this report to detail all that they have done for the organization. Thank you Martha, Sean and Rich.

In closing, I leave the presidency with the peace of mind of knowing that it is in the very able hands of Martha Gooding. Late last year she was busily organizing and planning for this year. She is committed to being an exceptional president and her early actions are certainly indicative of that. As a final thank you, I want to thank everyone who was involved in the organization last year in anyway. It certainly was a memorable experience for me and I am very grateful to have been a small part of such a highly regarded organization and to have worked with so many talented lawyers and judges. Thank you everyone!

♦ *James G, Bohm is a partner at Bohm, Matsen, Kegel & Aguilera.*

-In-house: Continued from page 1-

who had been working on a contingency fee basis, the client may be required to pay the former lawyer a reasonable hourly rate for time spent on the case plus costs and expenses.

Second, the client is taking an enormous gamble by replacing the lawyers who have lived with and know the case with newcomers who are strangers to the litigation. Will opposing counsel try to take advantage of the situation and will your new counsel ever be able to catch up? Depending upon when the decision to change counsel is made, new counsel may never be able to develop the same level of knowledge and the same comfort level with the facts that the original lawyers had. Employees who may have helped educate prior counsel may now be gone, relationships that were formed between these employees and other witnesses with your prior counsel will be lost, and new counsel may not have an opportunity to see firsthand how witnesses (both yours and theirs) perform at depositions. This may be less of a concern if the depositions were videotaped and can be viewed by new counsel, but even a video tells only part of the story. The client, who is ultimately responsible for the outcome, must balance the reasons for replacing counsel with the potential harm to the case.

Of course, changing counsel can also bring benefits. A new lawyer to a case can, and often times will, take a fresh look at the facts and law, and may develop legal strategies that had been overlooked or were not given the attention they deserve. New counsel also can bring new credibility to a matter and may possibly give the client a fresh start with the court in a case that has so far gone poorly.

Although these considerations are important, in the end, the client must decide whether the lawyer can still be trusted to serve as the client's advocate. As in-house counsel interviewed for this article have explained, a breakdown in a lawyer-client relationship typically stems from a breakdown of the foundations of that relationship—what this article refers to as the four pillars: (i) open and candid communication; (ii) managing client

-Continued on page 9-

-In-house: Continued from page 8-

expectations; (iii) loyalty; and (iv) managing costs. In varying words and form, these four pillars of the lawyer-client relationship are expressed in legal ethics textbooks, the ABA Model Rules, and the rules of professional responsibility in each state. In simpler terms, we all learned these rules in kindergarten—don't lie; don't cheat; treat others with respect; and do your homework.

Changing lawyers in the middle of a case is one of the last things most clients want to do. But when a lawyer breaks one or more of the four pillars of this relationship — such as repeatedly failing to return client phone calls or e-mails, giving a client incomplete or misleading information, making promises to the client the lawyer cannot keep, putting one client's priorities ahead of others, and overcharging for legal work—clients often will begin weighing the costs of replacing existing counsel with the benefits that new counsel can bring. These are tough issues to deal with and, ultimately, even tougher choices to make. Yet, as this article demonstrates, these are decisions facing consumers of legal services (both large and small) each day in the public and private sectors.

"My Lawyer Does Not Communicate With Me."

Understandably, all clients get steamed when their lawyer fails to return their phone calls, facsimiles or e-mails, when the lawyer is too busy to communicate with them, or when the lawyer is not candid about the case and its progress. This growing sentiment is expressed by the State Bar of Florida:

> From feeling uninformed or misinformed about matters at the support staff level, to being surprised by the size of the bill at the client level, poor communication is one of the legal profession's most pressing problems. Communication is a learned skill which most attorneys believe they are good at. However, signs of poor communication are everywhere. Failure to communicate with clients is one of the most frequently found charges included in Bar disciplinary complaints.

(See J.R. Phelps, "Keys to Maintaining a Successful

-Continued on page 10-

-Appellate: Continued from page 4-

B. Inadvertent Disclosure.

Two cases in the California Supreme Court – one just decided and the other still pending – deal with fundamental questions about inadvertent disclosure during discovery. In *Rico v. Mitsubishi Motors Corp*. (Dec. 13, 2007, S123808) ___ Cal.4th ___, one of plaintiff's attorneys inadvertently received a document prepared by defense counsel that included confidential work product, then extensively reviewed the document with the attorneys representing other plaintiffs and with plaintiffs' expert witnesses. The trial court disqualified the attorney and our Supreme Court affirmed: "[A]n attorney who receives privileged documents through inadvertence . . . may not read a document any more closely than is necessary to ascertain that it is privileged. Once it becomes apparent that the content is privileged, counsel must immediately notify opposing counsel and try to resolve the situation." (*Id*. at p. ___ [typed opn. at p. 1].

In a related case, *Jasmine Networks, Inc. v. Marvell Semiconductor, Inc.* (No. S124914), deferred pending resolution of *Rico*, Jasmine obtained a transcript of a conversation among Marvell's lawyers and officers that was recorded on Marvell's voicemail system; it showed that Marvell did not intend to abide by the terms of its contract. The recording was made by accident; the lawyers and officers called one of the corporation's employees, left a message, then continued their conversation without hanging up the speakerphone. In both matters, the discovery was seen as "making or breaking" the case. Often times, however, the importance of such evidence isn't all that clear at the time. Objecting to production is necessary to preserve appellate review.

JNOV vs. JMOL.

Both state and federal practice allow a losing party to file a post-trial motion seeking to enter judgment in its favor. But they are critically different in at least one respect. In state practice, "[a] party does not have to move for a directed verdict or nonsuit and have the judge deny that motion before moving for JNOV." (Cal. Judges Benchbook: Civil Proceedings – After Trial (CJER 1997) § 2.59, citing *Rollenhagen v. County of Orange* (1981) 116 Cal.App.3d 414, 417.) But not so with a JMOL motion in federal court; a party must make that motion under FRCP 50(a) at the close of evidence before it can "renew" the motion under FRCP 50(b) after trial.

-Continued on page 10-

-Appellate: Continued from page 9-

The failure to make the rule 50(a) motion means that judgment in favor of the losing party cannot be entered; a new trial is the only relief available. (See, e.g., *Cummings v. General Motors Corp*. (10th Cir. 2004) 365 F.3d 944, 951; *Rice v. Community Health Ass'n* (4th Cir. 2000) 203 F.3d 283, 285.) And the converse is also true: Failure to make a rule 50(b) motion following denial of a rule 50(a) motion precludes a Court of Appeals from entering judgment in the losing party's favor. (*Fuesting v. Zimmer, Inc.* (7th Cir. 2006) 448 F.3d 936, 938.)

However, it has long been held that the form of the motion is not crucial. (See, e.g., *Ryan Distributing Corp. v. Caley* (3d Cir. 1945) 147 F.2d 138, 140.) Thus, even an oral motion referencing a previously-denied motion has been deemed sufficient, so long as the grounds for the motion are accurately stated. (See, e.g., *Maine Rubber Int'l v. Envtl. Mgmt. Group*, 324 F.Supp.2d 32, 34.) So particularly in federal court, make challenges to the sufficiency of your adversary's case early and often.

New Trial Motions; Not Always Required, But . . . .

"Generally speaking, . . . an error may be raised on appeal although it could have been made the basis for a motion for new trial." (9 Witkin, Cal. Procedure (9th ed. 1995) Appeal, § 397, p. 449.) But there are at least two important exceptions to this rule. The first is that a challenge to the excessiveness or adequacy of damages must be raised in a new trial motion. (See, e.g., *City of Los Angeles v. Southern California Edison Co*. (2003) 112 Cal.App.4th 1108, 1121.) This includes the always-popular topic of punitive damages; a proper motion for new trial allowed our Supreme Court to reduce a $1.7 million punitive damages award to $50,000. (*Simon v. San Paolo U.S. Holding Co., Inc.* (2005) 35 Cal.4th 1159, 1170, 1189.)

The second is juror misconduct, assuming that you don't find out about it until after the verdict is rendered. (See *Weathers v. Kaiser Foundation Hospitals* (1971) 5 Cal.3d 98, 103 [right to new trial waived where party was aware of misconduct at earlier stage of trial but failed to move for mistrial or admonition].) Thus, if juror misconduct is uncovered for the first time in a post-trial investigation, it must be asserted in a new trial motion so that the trial court has an opportunity to correct the error.

-Continued on page 11-

-In-house: Continued from page 9-

Law Practice," Florida Bar's Law Office Management Assistance Service.)

The statistical evidence in other jurisdictions certainly bears out this poignant observation: In the most recent Discipline System Report of the State Bar of California, for example, of the 11,647 state bar inquiries opened in 2006, an overwhelming 34% of the complaints concerned lawyer performance (e.g., failure to perform, failure to communicate). (2006 Report on the State Bar of California Discipline System.) From 2002 though 2006, the majority of complaints the State Bar of California received regarding lawyers concerned their performance—including, specifically, a lawyer's failure to communicate.

Every lawyer knows that they have an ethical obligation to communicate with their clients. The ABA Model Rules, for example, require lawyers to "act with reasonable diligence and promptness in representing a client." (Rule 1.3.) ABA Model Rule 1.4 expands upon this duty, and requires a lawyer to: (i) promptly inform the client of any decision or circumstance with respect to which the client's informed consent is required; (ii) reasonably consult with the client about the means by which the client's objectives are to be accomplished; (iii) keep the client reasonably informed about the status of the matter; (iv) promptly comply with reasonable requests for information; (v) consult with the client about any relevant limitation on the lawyer's conduct when the lawyer knows that the client expects assistance not permitted by the Rules of Professional Conduct or other law; and (v) explain a matter to the client to the extent reasonably necessary to permit the client to make informed decisions regarding the representation. (Rule 1.4.)

Why, then, does this breakdown in communication occur?

Many times it is because lawyers and clients are not on the same page. For the client, the call to his/her lawyer asking about the status of a case may be their most important call of the day. The client expects the lawyer to promptly call back. The lawyer, however, may be juggling dozens of cases at a time, attending court hearings or trials in other matters, preparing for and taking other depositions, and so on. The lawyer may view the client's call as a low priority when compared to these other more immediate obligations. But, as the clients interviewed for this article have expressed, the lawyer who ignores their own client does so at his own peril. Clients expect regular and consistent communication from their counsel.

-Continued on page 11-

-In-house: Continued from page 10-

Lawyers must balance responsiveness to clients with their duties to other clients. If the lawyer is not able to return a phone call or e-mail, he or she should arrange to have someone else in their office do so. No matter how busy they are, a lawyer has a professional duty to communicate with their clients in an open and candid manner. Ultimately, clients are responsible for the consequences of their case, not the lawyer—a sentiment expressed by many clients interviewed for this article. The client must, therefore, have faith and confidence that a matter is being handled properly. Not returning phone calls, e-mail, or otherwise keeping clients fully informed about the progress of a case is a primary reason why clients lose confidence and decide to change lawyers. These lawyers may not only be fired by the client, they may face disciplinary action if complaints are filed with state bar associations. This is a primary (and avoidable) reason for client dissatisfaction. The statistics do not lie.

"My Lawyer Does Not Manage My Expectations."

Another principal cause of a breakdown in the lawyer-client relationship is where a lawyer fails to manage the client's expectations—a key aspect of providing competent representation. A lawyer's job is not telling the client what they want to hear or making promises to win a beauty contest that the lawyer cannot keep. A frequent cause for complaint among in-house counsel interviewed for this article is: (i) lawyers who make promises and assurances on which they fail to deliver; and (ii) when asked "what went wrong" they cannot provide a satisfactory explanation. The State Bar of Florida summed up the issue this way:

> Failure to reach a clear understanding of what the client wants, how soon it is expected, and how services are to billed and paid leads to many problems. Even a cursory review of the grievances filed by clients indicates that clients and lawyers often have vastly differing viewpoints on what was to be accomplished. Lawyers need to reach a clear understanding with clients early in the relationship of what the client really expects.

(See J.R. Phelps, "Keys to Maintaining a Successful Law Practice," Florida Bar's Law Office Management Assistance Service.)

-Continued on page 12-

-High Standards: Continued from page 3-

tion's history dates back to the foundation of our nation.

I was particularly impressed at a recent judicial conference in Philadelphia to be reminded of the assembled drafters of our Constitution, many of whom were lawyers and judges. The lasting language that those legal heroes crafted in that historic document has served our nation well through peace and war for centuries.

As our members already know, the way to a juror's heart (and vote) is through engagement and rapport. The engagement is developed by the art of communication and convincing argument. ABTL members, by-and-large, have brought home consistent awards for their clients. We like to believe that the success of our members (through jury awards) is a validation of our theme of professionalism and integrity in the conduct of courtroom presentations.

I envision many decades of success for our organization. I am so happy to have been a part of its leadership.

♦ *The Honorable Sheila Fell was the Orange County Chapter's seventh president.*

-Appellate: Continued from page 10-

Final Thought.

It is often a good idea to "embed" an appellate attorney – or at least someone not involved with the day-to-day litigation – in order to help define and present potential issues that may arise on appeal. It may increase your chances of reversing an unfavorable trial court result.

♦ *Robert M. Dato is an appellate lawyer at Buchalter Nemer. Mr. Dato wished to thank Harry Chamberlain and Efrat Cogan, the other two appellate specialists at Buchalter Nemer, for their assistance with the section on discovery issues.*

-Shining: Continued from page 6-

> we were all as tall as Stu Waldrip.) Laid out head to foot, we would reach from the Pacific Ocean along the 55 Freeway almost to the 5 Freeway.
>
> * * *
>
> A legal community such as ours deserves more than we are getting. We deserve more state and federal judges and justices. We deserve real state courtrooms, not converted department stores. We deserve real federal courtrooms, not ugly, trailer-like buildings. And we deserve these federal courtrooms in whatever federal district can provide them. . . . We deserve an accredited public law school.

So back in 1991 Orange County had almost everything, and most of what we didn't have we would eventually get. Rather than getting a losing Clipper franchise, we got a Stanley Cup winner with the Anaheim Ducks. We got a World Series, and the Anaheim Angels won it. We got our federal courthouse. We got more judicial officers. We're getting our public law school.

And Orange County finally got an ABTL chapter. In the early nineties, ABTL leaders from Los Angeles kindly asked if we were interested, but at the time they were told existing OC bar groups were sufficient. By 1997, this had changed, and with the persistent leadership of Bob Fairbank from L.A., an ABTL chapter was formed in Orange County. As most everyone knows, except maybe a certain baseball mogul, ***we are not L.A.*** And our ABTL chapter in Orange County allows us to uniquely explore our craft surrounded by the great lawyers and judges of our community. As an extra bonus, we contribute to the important work of the Public Law Center in providing everyone access to our courts.

We've had many great programs, and led some events for all the ABTL chapters meeting together. At one such event at the Quail Lodge, ABTL leaders defined their mission: to do programs about trials with a quality that would attract judges and lawyers and thus allow ourselves to identify together with the important common purpose we have. That's what I saw in the seventies in L.A., and that's what we're doing in the oughts in OC. Oh, and the food and drink have improved since the Ford Administration.

♦ *United States District Court Judge, the Hon. Andrew J. Guilford was our chapter's fourth president.*

-In-house: Continued from page 11-

Just like the duty to communicate, lawyers know they have an ethical obligation to provide competent representation to a client. The ABA Model Rules, for example, make this duty explicit, and require all lawyers to "provide competent representation to a client." (Rule 1.1) Under the ABA Rules, competent representation "requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation." (*Id*.) According to in-house counsel interviewed for this article, promising results that cannot be achieved is not competent. Even worse, when the lawyer makes promises, but fails to deliver on them, a client's confidence in the lawyer will be seriously tested.

Ultimately, clients who lose confidence in their lawyers will make a change. For example, inadequate performance—when a lawyer simply "lets you down"—has led current Los Angeles County Counsel, Raymond G. Fortner, Jr., to change counsel in the middle of on-going litigation. Mr. Fortner explains that the decision to replace counsel can be an expensive proposition—indeed, a "wrenching experience"—because "you have invested a lot of money in a case, but the firm has made significant missteps." One of the main reasons why Mr. Fortner has decided to change counsel in the middle of a case is when an important motion was lost, and the lawyer's explanation of why the motion was lost, including the lawyer's strategy regarding how to move the case forward, simply was unconvincing. Under that circumstance, the prospect of continuing the case with current counsel is outweighed by the potential benefits of bringing in a new lawyer, even if the learning curve with retaining new counsel will have an associated cost.

In that regard, Mr. Fortner explains that the costs of finding replacement counsel to take over a case, and to get up to speed in learning every aspect of the litigation, can be steep. Nonetheless, in Mr. Fortner's experience, "you need to have confidence in your lawyer," and that is the bottom line. When he has made a decision to replace counsel midstream, Mr. Fortner will generally turn to lawyers with whom he has worked in the past and in whom he has confidence.

Mr. Fortner recalled one instance in which he made the decision to switch outside counsel—which turned out to be the right choice. While Mr. Fortner initially thought the current outside counsel was the "right team" for the case, when they lost a motion and raised the judge's ire because of a failure to develop a compelling strategy of the case, it was apparent to him that something needed to change or the County would soon lose

-Continued on page 14-

-Brown Bag: Continued from page 3-

ruling. Otherwise, making the same arguments orally that were in the papers will have little or no effect.

Both Judges were sympathetic to the reality that clients want attorneys to argue zealously on their behalf; and may be uncomfortable with counsel who "submits." If this is the case, they advise attorneys to inform them when a client is sitting in the courtroom. Judge Banks said he would tailor his discussion in court to "give cover" to the losing lawyer, though a client's presence would have no effect on the ultimate ruling.

A sign posted behind Judge Banks's bench which reads "It's okay to go to trial" sparked discussion on the Judges' philosophies on trials and settlements. Judge Banks said that the sign is a statement to the Bar not to apologize for trying a case. He posts the sign because he trusts and respects the adversarial system of justice, and will not *force* parties to settle. Both Judges remarked upon the value of a good-faith settlement discussion between parties, and encourage opposing counsel to meet in an environment that will foster collegiality, such as a lunch in a nice restaurant. Judge Cramin emphasized that parties should not have to rely on a formal settlement conference with the judge playing referee.

Finally, Judge Banks and Judge Cramin offered their insight on trial. They advised the trial attorney to remember that she can easily lose a case based upon how the jury perceives her, but she can almost never win based solely on skill. Judge Banks told us to remember that at trial, "The lawyer is the director, not the actor, and never the star."

The Hon. David C. Velasquez

On Wednesday, October 17, 2007, the Honorable David C. Velasquez treated several attorneys to a discussion in his courtroom and a tour of his chambers. Judge Velasquez began his judicial career in the Municipal Court in 1998, and was elevated to the Orange County Superior Court in 1990. He is currently the Supervising Judge of the Complex Panel, where he has been assigned for roughly four years.

Judge Velasquez began the conversation by explaining that, during his tenure on the Complex Panel, class actions have displaced construction defect cases as the largest component of the panel's case load. He likened the role of the judge presiding over a class action to that of a watchdog, saying it was the judge's job to protect absent class members who are bound to decisions in the case. Judge Velasquez believes that it is especially important that judges guard against collusive actions on the part of parties' counsel, such as the motivation of plaintiffs' attorneys to collect fees, and that of defendant's attorneys to release their clients from the case. However, Judge Velasquez said that his default position is to presume that any proposed settlement that crosses his desk for approval is fair and reasonable. Situations in which he might not approve a class action settlement typically involve some sort of procedural defect, such as where notice to the class is not distributed fairly, or if the scope of the release is too broad or requires class members to waive future claims that do not relate to those settled by the class action.

Attorneys who practice before the Complex Panel will be happy to know that they enter the courtroom with goodwill. According to Judge Velasquez, the Complex Panel expects to see "the cream of the crop." Attorneys that do not live up to this expectation stand out, and not in a good way. Judge Velasquez advised attorneys who practice before him to feel comfortable suggesting next steps in the litigation process, as the purpose of a distinct Complex Panel is to develop innovative strategies in handling complex litigation. He recognizes that there is usually more cooperation between adversaries in the context of complex litigation, and encourages attorneys to get creative in terms of designing their own case management.

Perhaps the message Judge Velasquez most strongly wanted to convey to the lunchtime audience was the importance of electronic presentation. The Judge's courtroom is uniquely "wired" and up to date with modern technological capabilities. He pointed out the widescreen computer monitors mounted on the walls and at counsel tables, and the courtroom's wireless internet capabilities. The Judge even took us into the jury deliberation room to show us the computers that jurors may use to review exhibits electronically during their discussions. Judge Velasquez noted that cases before the Complex Panel are designated "complex" for a reason. They often involve large numbers of parties or novel issues, and the few cases that go to trial usually last for quite a while. Anything an attorney can do to grab the jury's attention or make their life (and the life of the judge) easier, will go a long way in helping her establish her case.

As Harper Lee said in *To Kill a Mockingbird*, "You never really understand a person until you consider things from his point of view." As attorneys who are always trying to understand what judges want, being able to learn directly from those on the other side of the bench

-Continued on page 18-

-In-house: Continued from page 12-

the entire case. At this juncture, which was early on in motion practice, Mr. Fortner made the decision to hire a different firm to handle the case, hoping that with new counsel, the County could regain the judge's trust and put forth the County's case in the best light possible. In the end, this is exactly what happened, and the County prevailed.

For Peter Zeughauser, who served as General Counsel to the Irvine Company for 15 years, firing outside counsel was never an easy experience. Many times, in Mr. Zeughauser's experience, it is "often the most unlikely cases that go to trial." Where lawyers are not accurately managing expectations it can cause clients to make assumptions that certain matters will never reach trial. When they do go to trial, however, the dynamics of the case change, and clients often weigh the need to bring in more experienced trial counsel. As Mr. Zeughauser explained, this decision to fire outside counsel who had invested years of hard work is not because of poor performance, but because the case was never expected to go to trial—again, managing expectations.

Of course, this is not always the lawyer's fault and, as Mr. Zeughauser opined, sometimes "not all clients are good clients." Mr. Zeughauser said he had seen many instances of what he referred to as "in-house malpractice"—poor decision making by in-house counsel as to which outside counsel to hire because they had simply assumed a particular matter would settle. For example, often times, said Mr. Zeughauser, he had seen in-house counsel fail to press outside counsel hard enough when making the decision to hire them about important factors such as trial experience. Overlooking trial experience, which initially may appear remote or unnecessary, can have costly consequences down the road when a last-minute decision is made to substitute new counsel on the eve of trial.

Further, in-house counsel, Mr. Zeughauser explained, may often be "pennywise and pound foolish." They may not permit outside counsel to invest the necessary time and money to thoroughly investigate a particular matter, challenge the client's assumptions, and fully understand the dynamics of the case. "It is very hard to manage expectations if you don't know the case well. Learning the case is hard to do if clients perceive litigation as expensive and do not want to spend a lot of money initially. You can scrimp at the beginning, but this often winds up costing more."

Mr. Zeughauser agreed that switching counsel is a difficult decision to make. "Almost always, you have [as General Counsel] personal relationships with outside lawyers. Firing them is the hardest part, because no matter why you made the decision, they almost always think it's a reflection on them." Moreover, "being fired is disruptive for outside counsel in their firm." At the end of the day, however, the General Counsel "gets paid to make those tough decisions."

To underscore the experience of Messrs. Fortner and Zeughauser, the State Bar of Arizona publishes literature regarding the reasons why many clients lose confidence in their lawyers, and what lawyers can do to avoid the problem. The Arizona Bar explains that, while "[l]awyers care deeply about their work and their responsibilities to their clients[,] [m]any attorneys get into trouble with discipline not because they ignore their clients or abandon their responsibilities." (Arizona Bar Counsel Insider, Clients and Communication.) Instead, according to the Arizona Bar, lawyers "get into trouble [with clients] because they work intensely to help a client and get overextended or lose perspective in the representation." (*Id.*)

The Arizona Bar provides a good example of an attorney who misses a deadline or fails to respond to a motion: "Instead of saying simply, 'I screwed up, this is what I will do to fix it,' the lawyer deflects responsibility by blaming the opposing attorney or the court, or he simply does not tell the client. The attorney continues to try to fix the problem without telling the client. Inevitably, the client finds out and feels betrayed." (*Id.*) According to the Arizona Bar, "[a]n act that may be just a malpractice issue turns into a bar complaint and possibly a sanction." (*Id.*)

As the Arizona Bar suggests, the "cure" to this problem "is communication." (*Id.*) Promptly sharing information with the client "often will prevent or minimize problems for the attorney." Furthermore, lawyers should "[m]anage client expectations, deliver bad news promptly, admit mistakes and tell the client what you will do to fix them." According to the Arizona Bar, "[t]his approach may not insulate one fully, but a client appreciates an attorney who communicates in an open and honest manner."

In short, when a lawyer fails to manage a client's expectations, a client's confidence in that lawyer will be tested and, ultimately, a lack of confidence will lead to a change in counsel.

"Where Are My Lawyer's Loyalties?"

All lawyers owe their clients a duty of loyalty—even in the smallest or most routine legal matters. Clients will

-Continued on page 15-

-In-house: Continued from page 14-

replace lawyers who they do not believe are putting their interests first, or who fail to properly manage potential conflicts between clients.

Mr. Zeughauser recalled a situation where a prominent firm representing an affiliate of the Irvine Company—in a matter for which the Irvine Company was paying the firm's bills—went on to file suit against the Irvine Company on another matter. The firm claimed that the entity the firm represented was not the Irvine Company itself, but merely an affiliate, and therefore the firm should not be conflicted out of representation in the second case. To Mr. Zeughauser's surprise, the court held the firm could sue the Irvine Company without a conflict. Immediately after the ruling came out, Mr. Zeughauser fired the firm. "Why should we keep on paying a firm who turns around and sues us?" Ironically, the Irvine Company was a far larger client for the firm than the entity it represented in the second case. This situation could have been avoided if the firm had consulted with Mr. Zeughauser and attempted to address his concerns by, for example, screening mechanisms to ensure that lawyers representing the affiliate would not work on the matter against the Irvine Company or that confidential information would not be shared.

It is never a good idea for a law firm to be defending motions to disqualify brought by its own clients. The lesson for all lawyers is to identify for the client as many potential conflicts as possible at the outset of a case and to obtain any necessary prospective waivers or consent. That way, the client is not surprised down the road, and does not feel betrayed. Client loyalty is critical. Ultimately, lawyers who take these simple steps will make a client's decision to change counsel over non-disqualifying conflicts a much more difficult one.

"<u>That Motion Cost What</u>?"

There is no reason for lawyers to charge their clients unreasonable fees or expenses in the delivery of legal services. (See, e.g., ABA Model Rule 1.5.) Clients will replace lawyers when the client thinks that the lawyer's fees and expenses are unreasonable or unjustified.

Lawyers' fees are a frequent cause of complaint to state bar disciplinary offices. In Massachusetts, approximately 10% of the 6,000 complaint received annually involve fee disputes. (See Nancy E. Kaufman and Constance V. Vecchione, "The Ethics of Charging and Collecting Fees," Massachusetts Office of Bar Counsel.) While fee disputes can often be prevented by clear communication between lawyers and clients regarding how fees are calculated, there exist unique problems when a client discharges an attorney midstream, and hires replacement counsel. This can be a particularly challenging problem in contingency fee cases, and raise several important issues: (i) how are fees allocated between the first and second lawyers; and (ii) who pays the first lawyer's fees?

For example, when a client who changed lawyers had signed a one-third contingent fee agreement with each lawyer, the second lawyer, who resolved the case, is holding the client's proceeds, and wants to take her full contingent fee from those proceeds before making distribution to the client. (See Susan Strauss Weinberg, "Contingent Fees and the Discharged Lawyer," Massachusetts Office of Bar Counsel.) But the discharged lawyer, whose work on the case may have contributed in large part to the successful outcome, also wants to be paid for their services. The typical outcome is that the discharged lawyer will be unable to collect a contingent fee. But the discharged lawyer is entitled to be paid in quantum meruit for the reasonable value of their services, typically figured on an hourly basis. (*Id*.)

Of course, the replacement counsel will have to live up to equally high expectations. The client will usually explain that original counsel was fired because they were too expensive, and that the replacement counsel are expected to keep costs down. Ms. Weisberg describes the second lawyer's obligations well:

> Before taking over representation, the new lawyer should also have a full and frank discussion with the client about the compensation issue, provide adequate information to allow the client to ascertain the client's best interests, and reach a specific agreement with the client on who will be responsible to pay the former lawyer. This discussion is required as part of the new lawyer's obligations to provide advice sufficient for the client to make fully informed decisions about the representation . . . and to communicate adequately the basis for the fee . . . . The agreement about the prior lawyer's fee should be in writing and should unambiguously identify the party responsible for the payment.

While Ms. Weisberg specifically reference the Massachusetts Rules of Professional Conduct, this is good advice for replacement counsel in any state.

In fact, "[l]awyers who ignore these issues do so at their peril because, absent express discussion and agree-

-Continued on page 16-

-In-house: Continued from page 15-

ment, the client will simply assume that both lawyers will be paid out of the same contingent fee without any appreciation of the potential for a larger obligation." (Id.) Ignoring these rules is a risky proposition also in part because they risk the filing not only of a disciplinary complaint when suing a client for fees, but also of a counterclaim for malpractice with a potential judgment on the counterclaim that is more than the fee sought. (See Kenneth Luke & Alison Mills Cloutier, "Why Not Arbitrate Fee Disputes?" Massachusetts Board of Bar Overseers.)

In non-contingent cases, lawyers must ensure that their bills are accurate and provide enough information for the client to determine how and why the fees were incurred. Clients should not be surprised when they see a bill, and this can be avoided by regular communication concerning the status of the case and the services being performed. A client should not learn that hundreds of hours were spent drafting a summary judgment motion the client knew nothing about.

Today, of course, many clients have sophisticated in-house counsel who closely monitor legal bills and require regular budgets from outside counsel. Although the law is still a profession and the quality of legal services is still paramount, cost considerations may lead clients to change lawyers particularly where the lawyer does not follow the expected billing protocols and procedures or fails to keep the client adequately informed.

Conclusion

Open and candid communication, managing client expectations, loyalty, and managing costs are the k to a successful lawyer-client relationship. Although there are real and significant disadvantages to changing counsel in the middle of a case, clients will do so where the foundation of the attorney-client relationship breaks down.

Returning phone calls and e-mail, communicating honestly, making candid assessments of a case, identifying potential conflicts up-front, and keeping a close eye on legal bills will go a long way to maintaining client relationships. On the other hand, failing to do one or more of these things may result in an unhappy client deciding to fire their lawyer in the middle of a case—an outcome both the lawyer and the client would prefer to avoid.

♦*Thomas R. Malcolm and John A. Vogt are both at Jones Day's Irvine office.* *Both would like to thank Tamar Tal, a colleague who assisted with this article, and the in-house counsel interviewed for this article, who provided their invaluable input and expertise.*

-Sponsor: Continued from page 4-

	Tax-Affecting	**No Tax-Affecting (IRS Position in Gross Case)**
Pre-Tax Net Income	1,000,000	1,000,000
Corporate Taxes	40%	N/A
After Tax Net Income	400,000	1,000,000
Capitalization Rate	25%	25%
Value Of Company	2,400,000	4,000,000

Percentage Increase In Valued Based On Not Tax-Affecting = 67%

Over the years following the Gross case, valuation professionals have pointed out that there are many problems with the IRS approach in the Gross case and that many issues are involved when valuing S corporations.

The following are several of the issues that may need to be addressed in the valuation of an S corporation:

- Is the subject interest a 100% interest (are you valuing the entire company or some other interest).
- Is the subject interest a fractional interest (less than 100%)?
- Is the subject interest a minority interest (less than 50%)?
- Is the subject interest a controlling interest?
- Is the subject interest a non-controlling interest?
- How long has the company been an S corporation?
- Can the subject interest "break" or change the S corporation status?
- Does the S corporation distribute its net income?
- How much of the S corporation's net income is distributed?
- How long had the S corporation been distributing its net income?
- What are the marginal corporate tax rates?

-Continued on page 17-

-Sponsor: Continued from page 16-

What are the capital gains rates of the marginal investor?

What are the personal tax rates of the marginal investor?

What is the likely pool of buyers for the subject company/interest?

If income exceeds the amount distributed, the S Corp shareholder will receive an increase in the tax basis of the investment by the difference between net income and the amount distributed.

A buyer of an S Corp may pay a premium (the premium being the benefit to the existing S Corp shareholder) to receive a stepped up basis.

Asset Sale (or Stock Sale accompanied by a 338 election) - the tax basis of the assets are "stepped up" to the transaction price. Acquirer obtains higher depreciation and amortization tax shield.

Stock Sale without 338 election - No step up in basis. The lower tax basis is carried over.

It appears that the largest debate since the Gross case involves the valuation of a minority (non-control) interest in an S corporation as opposed to a majority (control) interest.

Many practitioners agree that the value of a minority interest in an S corporation can be greater than an otherwise similar interest in a C corporation. The greater value would result from the single-taxation of S corporations, consistent historical distributions of earnings, as well as other factors.

The same practitioners that agree a minority interest in an S corporation can be greater than an otherwise similar C corporation interest (under certain circumstances) typically also agree that a minority interest in an S corporation can be worth less than a similar interest in a C corporation if certain circumstances exist. These circumstances could include the lack of historical distributions (thus leaving a minority shareholder with a tax burden each year and no distribution with which to pay this burden).

Over the years following the Gross case, four models for valuing interests in S corporations have been developed. These models were developed by the following individuals:

Daniel R. Van Vleet
Chris D. Treharne
Z. Christopher Mercer
Roger J. Grabowski

In addition to the models developed by these individuals, as of the writing of this article a new "Guide to the Valuation of Subchapter S Corporations" is available. ("Fannon's Guide To The Valuation of Subchapter S Corporations", Nancy J. Fannon, Business Valuation Resources, LLC.)

The point of this article was not to delve into the underpinnings of models/methods available to value subchapter S corporations, but rather create awareness as to issues involved with one of the most debated issues in the valuation community in recent years. As this issue recently arose in a divorce case (The Supreme Judicial Court of Massachusetts had to determine if it was appropriate to tax-affect the value of an S-corporation Bernier v. Bernier) it is possible that issues relating to the valuation of subchapter S corporations will arise more frequently and in different arenas.

♦*Daniel C. Curren is a member of Zamucen, Curren, Holmes & Hanzich. He is an Accredited Senior Appraiser (ASA) in the business valuation discipline of the American Society of Appraisers, as well as a Certified Business Appraiser (CBA) under the Institute of Business Appraisers.*

-Q&A: Continued from page 7-

Second, the scope of permissible discovery has been narrowed by the amendments to the Federal Rules of Civil Procedure which became effective December 1, 2000. Under Fed. R. Civ. P. 26(b)(1), as amended, the scope of discoverable information no longer is any unprivileged matter which is relevant to the subject matter involved in the pending action and/or reasonably calculated to lead to the discovery of admissible evidence. Rather, the scope of discoverable information has been narrowed, and now may be stated as follows: any unprivileged matter relevant to the claim or defense of any party, and/or relevant information reasonably calculated to lead to the discovery of admissible evidence. Accordingly, counsel should not be relying on older cases where the courts cited or applied the former, broader standard for discovery.

Third, the failure of a party to serve a timely response to a properly-served set of interrogatories, document pro-

-Continued on page 18-

Brown Bag: Continued from page 17-

has been an invaluable experience. We would like to sincerely thank Judge Banks, Judge Cramin, and Judge Velasquez for taking the time to share their points of view, thoughts, and insights with us.

♦ *Jacqueline Beaumont and Adrianne Marshack are litigation associates at Morrison & Foerster.*

-Q&A: Continued from page 17-

duction requests, and/or requests for admission constitutes a waiver of all objections to the particular discovery request (including any objections to any interrogatory, document production request, and/or request for admission contained therein). This includes objections on the ground of the attorney-client privilege and even on the ground of the Fifth Amendment privilege.

Fourth, the failure of a party to interpose a timely particular objection to a particular interrogatory, document production request, and/or request for admission constitutes a waiver of that particular objection to that particular interrogatory, document production request, and/or request for admission. Thus, particular objections asserted for the first time in a party's portion of the Joint Stipulation (or opposition) will not be considered.

Fifth, notwithstanding a party's waiver of objections in general or waiver of particular objections, I will not order a party to provide a further response to any interrogatory, document production request, and/or request for admission which on its face (a) does not seek information within the scope of permissible discovery, or (b) is so vague and ambiguous that I am unable to discern whether the interrogatory, document production request, and/or request for admission seeks information within the permissible scope of discovery.

Sixth, when a timely relevance objection has been interposed, I subscribe to the view that the burden of demonstrating relevance rests with the party seeking discovery. Accordingly, if the propounding party merely makes the conclusory assertion in its portion of the Joint Stipulation that the discovery sought clearly is relevant to the claims or defenses of the parties, or if the propounding party otherwise fails to convince me of the relevance of the discovery sought to the claims or defenses of the parties, I will sustain the relevance objection and deny the motion to compel with respect to that particular request.

Seventh, I will not order a party to produce documents that the party already has produced in this or a previously-pending action between the same parties, whether produced informally, or pursuant to its voluntary disclosure obligations, or in response to a previous discovery request.

Eighth, I will not order a party to produce documents which the party represents either never existed or no longer exist, unless the propounding party convinces me that the representation has not been made in good faith and/or that the responding party did not make a reasonably diligent effort to locate responsive documents before making the representation.

And *ninth,* if the dispute is over the sufficiency of a response already served, I will not order a further response to a particular interrogatory, document production request, and/or request for admission that the moving party failed to reference in the meet and confer letter sent to opposing counsel pursuant to Local Rule 37-1.

Q: *What is your philosophy on awarding sanctions?*

A: I have no predilection against awarding sanctions. I remember doing a survey of my discovery rulings once, for a panel I was getting ready for in LA. For the period of time I looked at, I found that one or both of the parties had requested sanctions about 40% of the time, and I actually had awarded sanctions in about half of those cases. If either or both sides requests sanctions, I have to rule on that issue, and I will just follow the standard set forth in Federal Rule 37(a)(4). Where the discovery motion has been granted in part and denied in part, the issue of sanctions is governed by Fed. R. Civ. P. 37(a)(4)(C), which accords me the discretion to apportion the reasonable expenses incurred in relation to the motion among the parties and persons in a just manner. In that situation, my normal practice is to order the parties to bear their own attorneys fees and costs, unless I conclude that sanctions are warranted against one of them pursuant to Local Rule 37-4 for violating Local Rule 37-1 and or 37-2.

That's my approach when either or both sides requests sanctions. If neither side requested sanctions, I normally will defer and not raise the issue *sua sponte*. The only exception would be if I believed that sanctions were warranted against one side pursuant to Local Rule 37-4. In that situation, it's usually my practice to raise the sanctions issue, and then let the party who would otherwise be

-Continued on page 19-

awarded sanctions submit a declaration of their attorneys fees and costs if they want sanctions. I would always afford the prospective sanctionee the opportunity to be heard in that situation.

Q: What c*an you tell us about the new pilot program for magistrate judges that the Central District is in the process of implementing?*

A: The program is based on a successful program that the Court ran in Riverside for a couple of years with Judge Larson, while he still was a Magistrate Judge. We are going to be expanding the program district-wide. Each Magistrate Judge will be directly assigned two cases a month off the civil assignment wheel. When a Magistrate Judge's name is randomly drawn as the judge on the case, no District Judge's name will be drawn. Assuming no other triggering event occurs such as the filing of a substantive motion, if both parties have not consented within a certain time frame (which has not yet been determined for the pilot, but in the Riverside program was the time the Rule 26 joint statement was filed), the case will be reassigned to a District Judge and the Magistrate Judge's card will go back into the deck. We contemplate that certain types of cases will be exempt from assignment to Magistrate Judges, such as cases where a TRO or preliminary injunction request is filed along with the complaint, bankruptcy appeals, and class actions. Our Rules Committee is in the process of drafting proposed new Local Rules to implement this program, and we hope to publish those proposed rules for public comment some time in the next few months.

Q: *If you could have dinner with a famous person -- living or dead -- who would it be and why?*

A: I think I would choose Abraham Lincoln. I would find it fascinating to hear about his experiences in the practice of law, in politics, and as President during the Civil War. I also would be very interested in discussing with him modern issues such as the war on terror, pervasive gang crime, and illegal immigration.

Q: *What do you enjoy doing when you are not working?*

A: My family took up the sport of golf about a year and a half ago; suffice it to say that "working on our game" consumes a lot of my spare time. At this time of year, I like to go skiing a lot (snow permitting). I also enjoy working out, watching sports on TV, and reading fiction (including books-on-tape during my daily commute).

Q: *If you could choose any job in the world other than a judge or lawyer, what job would you choose?*

A:I can't think right now of any job I'd rather have than my current job as a Central District Magistrate Judge. But I recall that, when I was in college, I liked accounting and believed I had a pretty good aptitude for it. So, if I had to choose something else, I think I would choose working for one of the big accounting firms.

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