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Letter from
the President

It is a pleasure to serve as ABTL's new president. ABTL was started over twenty years ago to deal with the unmet needs of business trial lawyers. I have one goal: to keep up our tradition of identifying and meeting the needs of our members. Despite the recent proliferation of CLE programs, no other group has ABTL's focus on the business trial lawyer. I enlist your help to sharpen our unique focus.



Karen Kaplowitz

The following are opportunities for your involvement:

Dinner Programs. Mark your calendars for dinner programs on the following Tuesday nights:

- December 10, 1996
- February 11, 1997
- April 8, 1997
- June 10, 1997

Seth Aronson of O'Melveny & Myers is Dinner Chair. You are invited to suggest program ideas and speakers to him. Help us make our

programs relevant to your needs.

Lunch Programs. Last year, we started a series of lunch programs, designed for substantive topics which would appeal to a subsection of our membership. Our first two programs, on the new securities litigation law and on unfair business practices, were very successful. The lunch programs are open only to ABTL members. Miles Ruthberg of Latham and Watkins and Richard Mainland of Fulbright & Jaworski co-chair the committee. Contact either one with program and speaker ideas.

(Continued on page 12)

INSIDE

Doctor's Assocs., Inc. v. Casarotto: The Federalization of Arbitration	by Peter S. Selwin Glen A. Rothstein.....	p. 3
Issues in Trying the Amount of Punitive Damages	by Robert Olson	p. 5
Cases of Note	by Denise M. Parga and Vivian R. Bloomberg	p. 7
The Surprising Power of the Unclean Hands Defense	by Michael L. Cypers	p. 9

Tips on a Successful Appeal: An Interview
With Justice John J. Zebrowski

In this interview, Justice Zebrowski provides a helpful insider's view of appellate practice, providing tips on a variety of issues including how to effectively prepare the record for appeal, whether there are obscure local-local rules that must be followed (there aren't), what practice guides are respected and how cases are assigned.

Justice Zebrowski served on the Los Angeles Superior Court bench for more than a dozen years before his appointment to the Second District Court of Appeal about one year ago. While on the Superior Court bench, he served in areas of importance to business litigation, such as law and motion and requests for provisional relief. He has also generously contributed his time and help to the ABTL, including service as a member of the ABTL Board. The interview was conducted for ABTL by Laurence Jackson.



Hon. John J. Zebrowski

Preparing the Record on Appeal

ABTL: Are there particular issues that either the appellants or respondents ought to bear in mind in preparing the record or that you would like to see more often?

Justice Zebrowski: One thing I find is that when you look at the table of contents in the record, the descriptions that are given to the documents are often really not useful at all; for example: "Stipulation filed on such and such date." Well, you can't tell from looking at the table of contents whether that's the stipulation where the key document is to be found. It doesn't let the court know where to find those documents if you want somebody to look at the key documents. Unfortunately, sometimes lawyers reference the documents so poorly it makes you think maybe they don't want anybody to look at the documents. While a clerk's transcript is not within counsel's control, the table of contents in an attorneys' appendix filed in lieu of the reporter's transcript is subject to the attorney's control. It should be prepared so it provides useful information to the court.

Researching the Brief

ABTL: In trial court practice, attorneys have gotten used to looking for local rules, local-local rules, and rules for individ-

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Tips on a Successful Appeal:

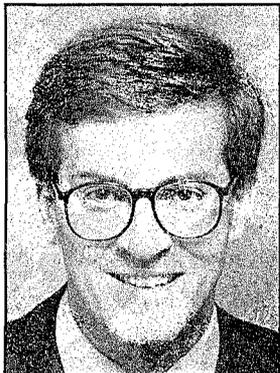
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ual courtrooms. Is this a concern before the Court of Appeal?

Justice Zebrowski: No. Our Division has no local rules or other rules different from the statewide Rules of Court for the Courts of Appeal. I was on the Superior Court for 13 years so I really got to know the local rules of all types, but our Division has only the statewide Rules of Court.

ABTL: Many trial lawyers look to something like Jefferson's Evidence Benchbook as particularly persuasive because many judges refer to it. Is there a treatise or guide like that which is commonly used by the judges on the Court of Appeal?

Justice Zebrowski: We do use several books here. We look at, and oftentimes rely on, Witkin's procedural series and the Rutter Group's book on appellate practice.



Laurence Jackson

Preparation of the Briefs

ABTL: As an overview of the briefing process, have you seen areas that attorneys should watch out for or could improve on generally, particularly in appeals of business litigation?

Justice Zebrowski: It is important to begin at the beginning and to make sure you don't start on step five of the theory. You can't assume that the judge already knows the subject matter of your

appeal. In many cases it will be true that the judge already knows steps one, two, three and four because we have a lot of experienced people here and they have seen a lot of things, but that may not be true for a particular issue in your specific appeal. If you brief an issue without covering steps one, two, three and four it just may get somebody off on the wrong track and perspective. This may delay the case or impede our understanding of your position.

In the Second District Court of Appeal, incoming cases are generally divided into civil and criminal, and an even amount of each type of case is randomly assigned to each division. In turn, in most divisions of our Court, your appeal will be assigned to an individual justice randomly to achieve what I might say is a proportional distribution of work. Within some divisions, the presiding justice then assigns primary responsibility for the case to an individual justice. In my own division, and I think in a lot of others, that assignment of a specific justice to the case is also done on a rotational basis so that the work will be assigned proportionally. As a result, in preparing your brief, you should not assume that the justice primarily responsible for your appeal already knows about the subject matter of your appeal.

ABTL: Are there particular issues involved in preparing briefs in business cases?

Justice Zebrowski: Business cases tend to be document-intensive. In these types of appeals, it is very important to make clear references to the record and to prepare a record so that it makes reference to the pertinent documents. For example, attention needs to be paid to the process of preparing the record. This is generally a photocopying process. With a big long document, for example, all the exhibits to the document will end up being photocopied without any tabs because no one bothers to go through and write them onto the copy of the exhibit or put in a

tab on the copy. And so, it becomes very difficult sometimes for us to find the document in question. In order to avoid that, since the record will be numbered sequentially, it is very important when you are discussing a particular passage of a contract or page to cite the precise, individual page number rather than the entire document or a range of page numbers.

You can set up anything particularly striking by placing a quote of the key language right in your brief. If there is a particular quote in a brief, we'll normally assume that it is correct unless the opposing brief contests it, even though we will, at some point, check in the record to confirm the accuracy of the quoted language. With the quote, we have it right there as we are reading. We have it right in front of us rather than having to go and look for it.

ABTL: Have you seen any briefing styles or techniques that were different from the traditional flow of argument and that you have found to be more persuasive or useful than the typical arrangement of questions presented, facts, argument, etc.

Justice Zebrowski: I haven't seen much in the way of different styles; it is really just a matter of trying to stay clear about what you are trying to say.

ABTL: How much reliance should an attorney place on oral argument as a way to present an argument as compared to the written brief?

Justice Zebrowski: As a general statement, the written briefing is more important than the oral argument, but that will also depend to some extent on the subject matter. Our procedure works on a monthly cycle with oral argument at the end of that cycle, which in our division happens to be at the end of the calendar month, although that varies from division to division. Before we hold oral argument, the law clerks and the justices will have read and considered the briefs and the record; we will have either a detailed bench memo or even a draft opinion, and the justices will have held a conference to discuss the case. As a result of these procedures, in our division, we have a fairly good idea in most cases of how a case will be decided before oral argument.

Amicus Curiae Briefs

ABTL: Have you found that amicus briefs are helpful or persuasive?

Justice Zebrowski: I have seen them be helpful, helpful and maybe more focused perhaps, because normally someone who is motivated to file an amicus brief is someone quite knowledgeable in the area. The court has to keep in mind that the amicus brief presents a perspective different from that of the parties, who are trying to win a particular appeal. But, with that thought in mind, normally I find it quite helpful to have an amicus brief from someone interested in the subject of the controversy.

Settlement Program

ABTL: Is the court's voluntary settlement program widely used or a comparative rarity and is it having any impact on the court?

Justice Zebrowski: I and several other justices have acted as settlement officers as a part of that program. I am not really familiar with the statistics with regard to the overall flow to state the precise numbers. It appears that in a substantial portion of the appeals the parties participate in the voluntary program, but participation is not universal and does not appear to have had enough of an impact for the justices to see the effect.

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Assignment of Cases

ABTL: Are there any rules or procedures that are effectively exceptions to the general rule of random assignment of cases that you referred to previously? For example, does the Court of Appeal have any equivalent to the District Court's "low-number" rule for related appeals or successive appeals in the same case?

Justice Zebrowski: As I understand it, within the past year or so, the Second District has instituted a procedure to assign appeals to the same division that may have handled prior writ proceedings or preliminary appeals in the same case. This was simply a matter of judicial economy since you already had one division familiar with the facts of the case. However, there is no procedure to require the same three judge panel on any subsequent appeal in the same case. So while the same division should be assigned, the three judges out of the four from that panel that actually hear the subsequent appeal may not be the same three judges who determined the first appellate proceeding in that case.

Oral Argument

ABTL: What do you see as the goals to be accomplished in oral argument?

Justice Zebrowski: I have always regarded oral argument even on the trial court level, and now on the appellate court level, as an opportunity to: number one, correct any errors or misapprehensions that the Court may have based on the briefs; number two, make sure that the panel appears conversant with the major points on the appeal; and, number three, respond to any new matters, such as matters in the last brief to have been filed or decisions that have arisen since the briefing ended. Probably the most important aspects of oral argument are the things the attorneys want to be sure the panel understands. In a day of oral argument, many cases may be argued without any questions from the panel and only brief oral presentations. Then an oral argument may lead to thirty questions from the panel. Oral argument can be exciting and interesting and in some cases the panel's view may be one of "let's wait and see what happens at oral argument" in terms of how the case will be decided. Even in the more typical case, where we have a pretty good idea of the outcome before the argument, oral argument has been valuable in structuring the opinion even when it doesn't change the panel's preliminary view formed from the briefs.

ABTL: How do you see attorneys addressing the second goal of ensuring the panel's familiarity?

Justice Zebrowski: Well it's a difficult thing. Different people react in different ways, and I know some justices would feel insulted by an oral argument that recited the briefs and thereby implied that they weren't already familiar with the briefs. On the other hand if you don't say anything then you are running a greater risk of a misapprehension of your position by the panel. One approach I have seen is to state briefly the main points, especially any that you can't afford to have misunderstood, and then ask the panel if there are any questions.

ABTL: How should attorneys estimate oral argument time in response to the Court's inquiry about oral argument?

Justice Zebrowski: I suggest that attorneys should be sure they allow enough time to communicate their prepared remarks and allow time for whatever questions they anticipate from the panel.

—Hon. John J. Zebrowski and Laurence Jackson

Doctor's Assocs., Inc. v. Casarotto: The Federalization of Arbitration

The U.S. Supreme Court has issued an important decision concerning the viability of state statutes which govern the availability of arbitration in civil disputes. In *Doctor's Assocs., Inc. v. Casarotto*, 64 U.S.L.W. 4370 (1996), the U.S. Supreme Court invalidated a Montana statute which required that notice that a contract is subject to arbitration be typed in underlined capital letters on the first page of the contract. The *Doctor's Assocs.* case is significant because it implies that any state statute which imposes special requirements for the enforceability of arbitration provisions may be struck down on the ground that such requirements are inconsistent with Section 2 of the Federal Arbitration Act ("the FAA"). The Court's decision also underscores the trend toward the federalization of virtually all civil disputes which are subject to arbitration.

In *Doctor's Assocs., Inc. v. Casarotto*, a franchisee of a Subway sandwich shop in Montana, brought suit against DAI, its franchisor, based on various state law contract and tort claims. The underlying franchise agreement contained an arbitration provision which provided that any dispute between the parties would be settled by arbitration.

DAI moved the trial court to have Casarotto's suit stayed pending arbitration. Casarotto opposed that motion on the ground that the arbitration provision in the franchise agreement was unenforceable because the contract did not comply with the applicable Montana statute requiring that notice that a contract is subject to arbitration be typed in underlined capital letters on the first page of the agreement.

The trial court granted DAI's motion and stayed Casarotto's lawsuit pending arbitration. The trial court apparently determined that because the franchise transaction involved interstate commerce the FAA was thereby implicated. The trial court also apparently found that the "first page" Montana statute was in direct conflict with Section 2 of the FAA, which provides that contractual arbitration provisions are enforceable, except "upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2 (West 1996). Ruling that the federal statute preempted Montana statute, the trial court ordered the matter to arbitration.

Casarotto appealed to the Montana Supreme Court, which reversed the trial court's order. *Casarotto v. Lombardi*, 268 Mont. 369, 886 P.2d 931 (1994). DAI petitioned for certiorari from the U.S. Supreme Court, which was granted. *Doctor's Assocs., Inc. v. Casarotto*, 515 U.S. ___, 115 S. Ct. 2552, 132 L. Ed. 2d 807 (1995). The Supreme Court remanded the case back to the Montana Supreme Court for further consideration in light of *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. ___, 115 S. Ct. 834, 130 L. Ed. 2d 753 (1995). Following remand, the Montana Supreme Court adhered to its original ruling. *Casarotto v. Lombardi*, ___ Mont. ___, 901 P.2d 596 (1995). DAI again petitioned for certiorari, which the U.S. Supreme Court again granted. *Doctor's Assocs., Inc. v. Casarotto*, 516 U.S. ___, 116 S. Ct.



Peter S. Selvin

(Continued on page 4)

690, 133 L. Ed. 2d 594 (1996). Finally addressing the merits of the dispute, the U.S. Supreme Court reversed.

The heart of the Court's opinion is its discussion of the scope of the preemptive effect of section 2 of the FAA. In *Perry v. Thomas*, the Court reiterated that state law principles such as fraud, duress or unconscionability may be applied to invalidate contracts containing arbitration provisions "if that law arose to govern issues concerning the validity, revocability and enforceability of contracts generally." 482 U.S. 483, 492 n.9, 107 S. Ct. 2520, 2527 n.9, 96 L. Ed. 2d 426, 437 n.9 (1987). But state courts "may not, however, invalidate arbitration agreements under state laws applicable only to arbitration provisions." *Doctor's Assocs.*, 64 U.S.L.W. at 4372. Put differently, Congress



Glen A. Rothstein

has precluded the States "from singling out arbitration provisions for suspect status, requiring instead that such provisions be placed 'upon the same footing as other contracts.'" *Id.*

The case has wide implications, not only concerning the arbitration of civil disputes, but also as to the whole notion of federalism and whether, in the wake of this decision, individual states have any remaining ability to impose limitations on the availability of arbitration in commercial agreements.

Consider the following syllogism:

1. *All civil disputes, no matter how seemingly local in nature, involve interstate commerce.* The Court applied the FAA based on its implicit conclusion that the subject franchise purchase transaction involved interstate commerce. *Doctor's Assocs.*, 64 U.S.L.W. at 4371-72. The Court reached this conclusion even though the subject transaction involved the purchase of a single franchise located in a single state.

Nevertheless, the Court's characterization of the transaction in *Doctor's Assocs.* is hardly surprising. In *Allied-Bruce*, which the Court decided last year, it found sufficient "interstate commerce" in a dispute brought by a single home buyer *under state tort and contract law* against a termite company to invoke the FAA. If the Court could find "interstate commerce" in the context of the dispute in *Allied-Bruce*, it will undoubtedly find "interstate commerce" in virtually any and all civil disputes — especially where there happens to be agreement with an arbitration agreement.

2. *Because all civil disputes involve interstate commerce, the FAA preempts state regulation of arbitration agreements in every case.* The Court's decision in *Doctor's Assocs.* could not be clearer: where interstate commerce is involved, section 2 of the FAA prohibits states from subjecting arbitration provisions to "special treatment." Put differently, preemption will be applied in every case where interstate commerce is involved. As Justice Marshall stated: "Section 2...embodies a clear federal policy requiring arbitration unless the agreement to arbitrate is not part of a contract evidencing interstate commerce." *Perry*, 482 U.S. at 489 (emphasis added).

3. *Because preemption occurs in every case, no state statute limiting or controlling the enforceability of arbitration provisions will be held to be valid.* The plain implication of *Doctor's Assocs.* is that any state statute which is specifically directed to the enforceability of arbitration provision will be invalidated. Put differently, state public policy concerns about

enforcement of arbitration provisions — and the corresponding denial of a potential litigant's access to the civil courts — must give way to a uniform, federal structure.

An example of the potentially broad reach of the holding in *Doctor's Assocs.* can be found in the area of real estate sales. In that context, and as a matter of state statute, arbitration provisions are required to be specially identified, highlighted and presented "either in at least 10-point bold type or in contrasting red print in at least 8-point bold type." Cal. Code Civ. Proc. § 1298(c). The purpose of these special requirements — which are also contained in other state statutes dealing specifically with arbitration agreements — is to put consumers on notice of the potential loss of their access to the civil courts for the resolution of any dispute arising out of their agreement. See, e.g., *Grubb & Ellis Co. v. Bello*, 19 Cal. App. 4th 231, 240-41 (1993) (holding that the various legislative documents dealing with section 1298 evidence the Legislature's overriding concern with consumer protection and efforts to assure that arbitration will be voluntary and knowing).

Section 1298(c), like the "first-page" statute in Montana, was based on the belief that because arbitration carries with it the loss of recourse to the civil courts, and the concomitant loss of a party's constitutional right to a jury trial, particular attention ought to be drawn to such a provision in a contract. See *Cal. Legislature, Senate Comm. on the Judiciary, Selected Bill Analyses*, vol. 1, ch. 881, A.B. 1240 (1988) (commenting that the uniform notice requirement of section 1298(c) is necessary "to ensure that individual[s] who sign...arbitration provisions are clearly advised that they are waiving their rights to court or jury trial"). Other statutes, both in California and across the nation, reflect a similar public policy concern. See, e.g., Cal. Bus. & Prof. Code § 7191(a) (requiring that notice of arbitration provision in printed contract for work on residential property with four or fewer units be set out in roman boldface type or contrasting red print); S.C. Code Ann. § 15-48-10(a) (Supp. 1993) (requiring that notice of arbitration provision be prominently placed on first page of contract).

But the state policies underlying such statutes are apparently insufficient to overcome the federal imperative to further the efficiency of our economic life through a federalization of the arbitration remedy, where arbitration agreements will be uniformly enforced on a nationwide basis, without regard to the vagaries of local law. *Perry*, 482 U.S. at 489 ("Section 2 is a Congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary."). In this respect, the Court's decision is squarely at odds with a number of state court decisions which have reaffirmed the primacy of state regulation over local transactions and the right of local citizens who have suffered damages in commercial transactions to seek their remedies in the civil courts. See, e.g., *Columbus Anesthesia Group v. Kutzner*, 218 Ga. App. 51; 459 S.E.2d 422 (1995) (court declined to enforce arbitration provision in agreement to join medical practice group because services provided did not constitute interstate commerce, invoking the FAA, and contract did not conform to state's procedural requirements for arbitration of employment contracts); *Barter Exch., Inc. of Chicago v. Barter Exch., Inc.*, 238 Ill. App. 3d 187, 606 N.E.2d 186 (1992) (court declined to enforce arbitration provision in franchise agreement due to franchisor's failure to comply with state franchise regulations).

The timeliness of the *Doctor's Assocs.* decision is underscored by the fact that the California Supreme Court has recently granted review in two cases which also explore the interplay between the FAA and state policies relating to the enforceability of arbitration agreements. See *Engalla v.*

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Permanente Medical Group, Inc., 41 Cal. App. 4th 1698 (1995), review granted, 46 Cal. Rptr. 2d 747 (Nov. 2, 1995); Clark v. Prudential Securities, Inc., 40 Cal. App. 4th 766 (1995), review granted, 50 Cal. Rptr. 2d 74 (Feb. 22, 1996). The Court of Appeal decisions in both Engalla and Clark address such important issues as whose law — state or federal — applies to adjudication of disputes governed by arbitration and the proper standard to be applied in determining whether contracting parties can avoid arbitration on the ground of fraud, duress or other similar defenses.

Significantly, although both decisions acknowledge the preemptive impact of the FAA, neither decision expressly applied the federal statute or federal case authority arising under the FAA. In light of the U.S. Supreme Court's holding in Doctor's Assocs., and with both of these California appellate cases currently under review, it remains to be seen how our state Supreme Court will untangle the legal knot created by competing state and Federal policies in this important area.

A determination that a particular arbitration proceeding is governed by the FAA has implications beyond simply the invalidation of state statutes which "single out" arbitration provisions. The Federal Arbitration Act is not an independent source of federal question subject matter jurisdiction. See Robert Lawrence Co. v. Devonshire Fabrics, Inc., 271 F.2d 402, 408 (2d Cir. 1959), cert. dismissed per stipulation, 364 U.S. 801 (1960). As such, if the scope of "interstate commerce" is limitless, in the absence of an independent basis for federal jurisdiction, state courts will be forced to apply federal arbitration law at an increased rate. Put another way, the Court has succeeded in federalizing virtually all civil disputes which are subject to arbitration provisions, leaving the problems of increased court congestion and the application of inconsistent federal arbitration law for the state courts to handle themselves.

Preemption may also have significant consequences in particular cases because there are important differences between the applicable state law rules and the FAA when it comes to procedural matters. For example, under state law, separate arbitration proceedings can be consolidated if those separate proceedings involve a series of related transactions and involve common issues of law and fact. C.C.P. Section 1281.3. By contrast, recent Ninth Circuit authority suggests that consolidation is not available under the FAA. See Weyerhaeuser Co. v. Western Seas Shipping Co., 743 F.2d 635 (1984), cert. denied, 469 U.S. 1061, 105 S. Ct. 544, 83 L. Ed. 2d 431 (1984); see also Paine Webber, Inc. v. Fowler, 791 F.Supp. 821 (D. Kan. 1992).

The reality that the FAA may displace state procedural matters regarding arbitration begs the following questions: if the scope of "interstate commerce" per Allied-Bruce allows preemption in every case, and presumably every commercial dispute involving arbitration is subject to the FAA, what is the remaining relevance of procedural statutes such as section 1281, et seq.? For that matter, what is the remaining vitality of any state's procedural scheme relating to arbitration?

These questions are more than a matter of academic discourse. The limitless scope of "interstate commerce" espoused in Allied-Bruce and Doctor's Assocs. will greatly affect the impact of cases currently pending before the California Supreme Court. For example, in Engalla, the Court of Appeal held that California arbitration law will be preempted only insofar as it is inconsistent with the FAA. Engalla, 41 Cal. App. 4th at 1722. While such a holding may on its face evidence an attempt to retain some state

(Continued on page 11)

Issues in Trying the Amount of Punitive Damages

In most California punitive damages cases trial is bifurcated between liability and compensatory damages, on the one hand and the amount of punitive damages on the other. See Cal. Civ. Code § 3295(d). All too often after the parties may have spent days, weeks, or even months trying the liability and compensatory damages issues, the punitive damages phase consists of no more than one or two pieces of noncontroversial evidence (typically the defendant's financial statement), counsels' argument rehashing the underlying facts, and the court reading, without objection, a standard instruction or two. Understandably, a defense disheartened by setback, a plaintiff elated by success, and a court worn out by prolonged proceedings simply may not focus on the real and different issues presented in the punitive damages phase.

Although the proceedings often are abbreviated, the stakes are not. Hundreds of thousands or even millions of dollars, and potentially the defendant's continued financial health or even existence, can be at issue. With such stakes, the unique evidentiary and instructional issues posed by the trial's punitive damages phase deserve special attention at trial, both to influence the jury and to make an adequate record for any potential appeal. Like other issues on appeal, the appellate argument inevitably is much stronger when a firm evidentiary foundation has been laid at trial. When issues are not confronted, an inadequate record may handicap a party wishing to attack, or to support, the punitive award on new trial motion or on appeal. The result then may be effectively to leave the punitive award's size entirely up to the trial and appellate judges' own personal sense of what might or might not be "too much."

The degree to which a party may be left to the vagaries of individual judicial temperament, however, can be mitigated. This article suggests some evidentiary and instructional issues parties should address in trying the amount of punitive damages.

As a preliminary matter, counsel should remember that the law in this area continues to evolve. In particular, constitutional challenges to the size of punitive awards once thought dead, see TXO Prod. Corp. v. Alliance Resources Corp., 509 U.S. 443 (1993), appear now to be alive and well, see BMW of North America, Inc. v. Gore, 116 S.Ct. 1589 (1996). If constitutional challenges are not raised at the earliest opportunity, however, they may be waived and the benefit of the law's evolution lost. See People v. Bransford, 8 Cal.4th 885, 893 n.10 (1994) (constitutional issues must be raised at earliest opportunity or may be waived).

Assuming that some amount of punitive damages will pass constitutional muster, appellate courts have identified various facts as relevant to whether a punitive award is excessive, including:

1. Reprehensibility of the defendant's conduct, BMW of North America, Inc. v. Gore, 116 S.Ct. at 1599 ("Perhaps the most important indicium of the reasonableness of a punitive damages award is the degree of reprehensibility of the defendant's con-



Robert Olson

(Continued on page 6)

Punitive Damages

Continued from page 5

duct"); *Neal v. Farmers Ins. Exch.*, 21 Cal.3d 910, 928 (1978);

2. Relationship between punitive award and compensatory damages, *BMW of North America, Inc. v. Gore*, 116 S.Ct. at 1602 ("a comparison between the compensatory award and the punitive award is significant"); *Neal*, 21 Cal.3d at 928;

3. The defendant's financial condition, *Adams v. Murakami*, 54 Cal.3d 105, 110 (1991); *Neal*, 21 Cal.3d at 928;

4. The statutory sanctions available for comparable misconduct, *BMW of North America, Inc. v. Gore*, 116 S.Ct. at 1603;

5. The absolute size of the award and the amount by which it exceeds compensatory damages, *Grimshaw v. Ford Motor Co.*, 119 Cal.App.3d 757, 822 (1981) ("the magnitude of the punitive award, including the amount by which it exceeded the compensatory [award is also a] proper consideration[] for determining whether the award was excessive as a matter of law"); and,

6. How closely the award comports with punitive damages' purpose to punish and deter, but not to destroy, *Adams v. Murakami*, 54 Cal.3d at 112.

These same facts should be equally relevant to the jury's initial determination of the amount of punitive damages. Indeed, in most instances the evidence to support these facts, and any claims that the jury should consider them, must be developed at trial, not for the first time on appeal. Thus, they provide a useful framework for considering what evidentiary and instructional arguments trial counsel may wish to advance.

1. *Reprehensibility*. This may well be the most important fact in determining a punitive award's size; it is also one of the most misunderstood. Reprehensibility has become a straw man. Plaintiffs simply reargue the facts that led the jury to find malice, fraud, or oppression, and then argue "of course this conduct is reprehensible." As far as they go, plaintiffs are correct. If the defendant's conduct was not reprehensible (e.g., "despicable"), the jury has no business awarding any punitive damages and there should not be a punitive damage phase at all. On the other hand, one of the biggest mistakes the defense makes is to argue that the defendant's conduct was not reprehensible at all. If there is a punitive damage phase, the defense has already lost that argument; the jury found malice, oppression, or fraud because it thought the defendant's conduct reprehensible in some way. Thus, such a defense argument is likely doomed to fail.

The problem is that plaintiff and defense alike mistake (just as jurors and courts may) what "reprehensibility" means in this context. The reprehensibility that appellate courts reference is *relative* reprehensibility, that is, how reprehensible is this defendant's conduct "in light of the types of misconduct that will support punitive damages." *Adams v. Murakami*, 54 Cal.3d at 110-112 & n.2. The question is not how bad is the defendant's conduct on a scale of one to ten with one being saintly conduct, it is how bad is the defendant's conduct on a scale of one to ten, with one being despicable conduct deserving punitive damages and ten being evil incarnate.

A wrongful economic act (even if "despicable") harming one victim is not as reprehensible as, say, double murder or a product defect causing multiple deaths and severe injury. More generally, acts causing economic harm are not as reprehensible as acts causing physical injury; intentionally inflicted injuries are worse than those resulting from despicable disregard for others rights; harm to many is worse than harm to few. See *BMW of North America, Inc. v. Gore*, 116 S.Ct. at 1599 (purely economic harm is less reprehensible conduct and, absent intentional, affir-

mative acts of misconduct or a target that is particularly financially vulnerable, economic harm torts "are [not] sufficiently reprehensible to justify a significant sanction in addition to compensatory damages"); *Vossler v. Richards Mfg. Co.*, 143 Cal.App.3d 952, 966 (1983) (continued sale of surgical implant knowing it would cause excruciating pain to hundreds of mostly elderly arthritic patients still less reprehensible than marketing defective vehicle which top management knew would result in fiery deaths), *disapproved on other grounds*, *Adams v. Murakami*, 54 Cal.3d at 115-116. Likewise an act directed by top management is worse than one approved at a lower echelon, see *TXO Prod. Corp. v. Alliance Resources Corp.* 509 U.S. at 468-469, 113 S.Ct. at 2726, 125 L.Ed.2d 366 (Kennedy, J., concurring), and a first offense is less reprehensible than an act that is just the latest in a pattern and practice of misbehavior. (The federal criminal sentencing guidelines may provide some useful relative reprehensibility guidelines.) Further, the fact of life is that certain defendants (e.g., large employers, brokerages, insurers) sooner or later inevitably are going to suffer a punitive damage award. That only a handful of successful punitive damages claims result from multiple tens of thousands of transactions which could generate punitive damages claims, likewise, suggests lower reprehensibility.

For the defense to argue such *relative* reprehensibility to the jury, e.g., in business disputes between large entities where the harm is purely economic, it is important to have the jury properly instructed on the relevant standard. Sadly, the standard BAJI instruction, 14.71 or 14.72.2 (depending on whether trial is bifurcated), does not contain the critical definition that reprehensibility means reprehensibility *relative to other conduct warranting punitive damages*. The defense should insist that the court modify the BAJI instruction to define reprehensibility as being relative to other conduct deserving punitive damages. If the trial court refuses to modify the BAJI instruction, the defense may have an instructional error it can appeal. Failing to request the modification, however, might waive any instructional error on appeal. See *Agarwal v. Johnson*, 25 Cal.3d 932, 948-949 (1979).

By contrast, plaintiffs will want to emphasize to the jury more than just the conduct for which the jury found malice, oppression, or fraud. If possible, plaintiffs will want to explore (and present evidence of) a pattern or practice of malfeasance and to establish direct, high-level responsibility. See *TXO Prod. Corp. v. Alliance Resources Corp.*, 509 U.S. at 468-469, 113 S.Ct. at 2726, 125 L.Ed.2d 366 (Kennedy, J., concurring). Evidence of the defendant's other misconduct that may not have been admissible in the liability phase may now come in.

2. *A Reasonable Relationship To Compensatory Harm*. The jury will determine, in the first instance, the reasonable relationship between punitive damages and compensatory harm. As a general proposition, however, the larger the compensatory award, the smaller the punitive to compensatory damages ratio it will support. Likewise, a high ratio is hard to justify where the punitive award may significantly reduce the defendant's net worth. Thus, the only California cases approving high punitive to compensatory damages ratios involve either small compensatory awards or minuscule proportions of the defendant's net worth or both. E.g., *Finney v. Lockhart*, 35 Cal.2d 161, 163 (1950) (2000:1 ratio, but only \$1 in compensatory damages); *Wetherbee v. United Ins. Co. of America*, 18 Cal.App.3d 266 (1971) (200:1 ratio, \$1,050 in compensatory damages, 0.33% of net worth); *Moore v. American United Life Ins. Co.*, 150 Cal.App.3d 610 (1984) (83:1 ratio, \$30,000 in compensatory damages, 3.2% of net worth).

On the other hand, a small compensatory award often justifies a higher than normal ratio. The plaintiff may also be entitled to present evidence of other harm suffered or that plaintiff poten-

(Continued on page 8)

Cases of Note

Civil Procedure — Statute of Limitations

In *Tomko Woll Group of Architects, Inc. v. Superior Court*, 96 Daily Journal D.A.R. 8038 (Court of Appeal June 27, 1996), the Second Appellate District held that substantial completion of a real property improvement triggers the commencement of the statute of limitations set forth in Code of Civil Procedure § 337.1 relating to patent defects in real property even if the patent defect arose after substantial completion of the property.

Attorney Work Product

In *Nacht & Lewis Architects, Inc.*, 96 Daily Journal D.A.R. 8209 (Court of Appeal July 2, 1996), the Third Appellate District held that the identities of witnesses interviewed by opposing counsel were protected by the work product privilege because the identities would reflect counsel's evaluation of the case by revealing which witnesses who claimed knowledge of the incident were deemed important enough to be interviewed by counsel.

Summary Judgment

In *DeCastro West Chodorow & Burns, Inc. v. Superior Court*, 96 Daily Journal D.A.R. 8511 (Court of Appeal July 16, 1996), the Second Appellate District confirmed that Code of Civil Procedure § 437c does not permit summary adjudication of a single item of compensatory damages which does not dispose of an entire cause of action.

Civil Procedure

In *Elise Stoner Castro v. Sacramento County Fire Protection District*, 96 Daily Journal D.A.R. 8849 (Court of Appeal July 23, 1996), the Third Appellate District held that the mandatory relief for dismissed plaintiffs provision in Code of Civil Procedure § 473 does not include relief for dismissal as a result of counsel's error in filing the complaint beyond the statute of limitations.

In *Crib Retaining Walls, Inc. v. NBS/Lowry, Inc.*, 96 Daily Journal D.A.R. 8793 (Court of Appeal July 22, 1996), the Fourth Appellate District held that a cross-defendant who obtains dismissal of an equitable indemnity cross-complaint under a § 877.6 order approving a good faith settlement is entitled to recover costs as a prevailing party against the cross-complainant.

Insurance

In *General Star Indemnity Company v. Superior Court*, 96 Daily Journal D.A.R. 9263 (Court of Appeal July 31, 1996), the Second Appellate District held that a self-insured retention endorsement to a comprehensive general liability insurance policy effectively transforms the policy from a primary policy into an excess policy covering only amounts in excess of the self-insured retention.

Attorneys Fees

The Court of Appeal ruled that attorneys should have been awarded nearly \$140,000 in fees where their client prevailed in a case against the City of San Rafael although that client netted only \$17,500. *Morales v. City of San Rafael*, 96 Daily Journal D.A.R. 10941 (9th Cir. Sept. 6, 1996). A dissenting opinion called the lawyer's fee "obscene." The trial court had awarded only \$20,000 in reliance on *Farrar v. Hobby*, 506 U.S. 103 (1992) (holding that low attorneys' fees should be awarded to plaintiffs who recover only nominal damages). The Ninth Circuit held that the plaintiff's recovery of \$17,500 was not nominal and, therefore, the trial court should have applied the lodestar approach in

which fees are awarded by multiplying the number of hours the prevailing party reasonably should have spent on the litigation by a reasonable hourly rate.

Securities Fraud

New life has been injected into the "bespeaks caution doctrine" with two recent cases holding that the doctrine protected defendants from liability for securities fraud where they disclosed risks that were the subject of later lawsuits. *In re STAC Electronics Securities Litigation*, 82 F.3d 1480 (9th Cir. 1996); *Rosenbaum v. Syntex*, 96 Daily Journal D.A.R. 11226 (9th Cir. Sept. 16, 1996). The doctrine "provides a mechanism by which a court can rule as a matter of law that defendants' forward-looking representations contained enough cautionary language or risk disclosure to protect the defendant against claims of securities fraud." *Fecht v. The Price Co.*, 70 F.3d 1078, 1081 (9th Cir. 1995). The continued vitality of the doctrine as a device for obtaining dismissal of a securities fraud complaint had been in question following the Ninth Circuit's decision in *Fecht*. There, the court opined that, "A motion to dismiss for failure to state a claim will succeed only when the documents containing defendants' challenged statements include enough cautionary language or risk disclosure that reasonable minds could not disagree that the challenged statements were not misleading." 70 F.3d at 1082 (citations and quotations omitted).

Stac Electronics held that investors failed to state a claim for securities fraud against a computer software maker where they alleged that the company failed to disclose in its prospectus its knowledge of a competitor's plans to introduce a competing product. The lawsuit arose from the collapse of the stock price of Stac Electronics, which manufactured Stacker, a data compression product. The market for Stacker evaporated when Microsoft released a new version of its DOS operating system containing similar data compression technology. Investors alleged that Stac Electronics went public without disclosing Microsoft's plans. The court ruled that, even if Microsoft had told Stac that it planned to introduce data compression technology, Stac could not have truly known that it would do so because a competitor's plans can never be known to a certainty. The court further held that adequate cautionary information regarding competition and other risks was contained in Stac's prospectus and distributed to the market through "road shows," analyst reports and press statements. Such risk disclosure invoked the "bespeaks caution doctrine."

In *Rosenbaum v. Syntex*, the court held that investors failed to state a claim for securities fraud against a drug manufacturer where they alleged that the manufacturer falsely predicted that no material adverse effects would result from a consent decree with the FDA and made false statements regarding the anticipated success of its products. The court ruled that the company's statements were inactionable forecasts and they included cautionary language that "bespoke caution." Additionally, the market was aware of certain negative information. The court also held that the company was not liable for analysts' statements that were the culmination of a one-way flow of information from company representatives to analysts, and then to customers, without the company's express or implied imprimatur.



Denise M. Parga

—Denise Parga and Vivian R. Bloomberg

tially might have suffered and for which the plaintiff is not compensated by ordinary damages. *TXO Production Corp. v. Alliance Resources Corp.*, 509 U.S. at 459-461 (a more than 500:1 ratio between punitive and compensatory damages justified because the potential harm that plaintiff might have suffered, but did not, would have resulted in a 10:1 ratio).

3. *Defendant's Financial Condition.* This is one of the areas of greatest current evidentiary dispute. It is now resolved in California that a plaintiff must establish the defendant's "financial condition." *Adams v. Murakami*, 54 Cal.3d at 110-111. How to measure financial condition, though, is another question. The most common measures are the defendant's net worth and net income. *Kenly v. Ukegawa*, 16 Cal.App.4th 49, 57 (1993) ("We are convinced that in most cases there must be evidence of the defendant's net worth in order to support the punitive damage award"); *Devlin v. Kearny Mesa AMC/Jeep/Renault, Inc.*, 155 Cal.App.3d at 391 ("Net worth generally is considered the best measure of a defendant's 'wealth' for purposes of assessing punitive damages"); *Pistorius v. Prudential Ins. Co.*, 123 Cal.App.3d at 554-555 (net worth and net income are relevant standards). Gross assets (or gross income) is not relevant. *Little v. Stuyvesant Life Ins. Co.*, 67 Cal.App.3d 451, 469 n.5 (1977). The defense may wish to object to (and even to move *in limine* to restrict) any reference to gross assets (or gross income).

Several appellate courts have suggested ten percent of net worth as a presumptive maximum for punitive damages. *Michelson v. Hamada*, 29 Cal.App.4th 1566, 1596 (1994); *Storage Servs. v. Oosterbaan (formerly People ex rel. Dept. of Transp. v. Grocers' Wholesale Co.)*, 214 Cal.App.3d 498, 514-516 (1989); see *Little v. Stuyvesant Life Ins. Co.*, 67 Cal.App.3d at 469 (15% of net worth excessive); *Burnett v. National Enquirer, Inc.*, 144 Cal.App.3d 991, 1012 (1983) (29% of net worth excessive; award reduced to 6% of net worth); *Zhadan v. Downtown L. A. Motors*, 66 Cal.App.3d 481, 500 (1976) (33% of net worth excessive); *Merlo v. Standard Life & Accident Ins. Co.*, 59 Cal.App.3d 5, 18 (1976) (30% of net worth excessive). But see *Vallbona v. Springer*, 43 Cal.App.4th 1525 (1996) (approving punitive awards representing 23% of individual defendants' net worth and almost 33 percent of their corporation's assets); *Devlin v. Kearny Mesa AMC/Jeep/Renault, Inc.*, 155 Cal.App.3d at 391 (approving punitive award constituting 17.5% of defendant's net worth on default). Equally, appellate courts are reluctant to approve more than a small percentage of a defendant's annual net income. *Egan v. Mutual of Omaha Ins. Co.*, 24 Cal.3d 809, 824 (1979) (seven months of defendant insurer's net income was excessive); *Burnett v. National Enquirer, Inc.*, 144 Cal.App.3d at 1012 (punitive damages constituting 50% of annual net income excessive as a matter of law).

What the defendant's net worth is may be subject to proof. For example, in *Vallbona v. Springer*, 43 Cal.App.4th 1525, defendants claimed little or no equity in various properties they owned, testifying that the properties were encumbered with various debts. But they produced documentary evidence supporting only two such encumbrances. The appellate court held that, on appeal, the jury could be assumed to have disregarded the defendants' uncontradicted testimony regarding encumbrances for which documentation had not been produced. The court also held that the jury could be assumed to have disregarded the defendants' testimony that equipment their corporation had purchased for \$77,000 was now worth \$17,000, again because there was no documentary support. *Vallbona* strongly suggests that if the defendant's net worth is disputed, documentary evidence and perhaps expert testimony are in order.

Plaintiffs have also attempted at times to question various accounting entries included in a defendant's financial statement, e.g., claiming that depreciation expenses and other accounting "book entries" should not be deducted from gross income or assets. This approach appears dubious, at least where generally accepted accounting principles have been followed. See *Rudolph v. Johnson*, 127 Cal.App. 451, 462 (1932) (deducting depreciation to obtain net lost profits); *Lee v. Durango Music*, 144 Colo. 270, 279, 355 P.2d 1083, 1088 (1960) ("The expenses of the business, including depreciation of capital, deducted from its income...produces the customary net profits of the business,"). A creative plaintiff might, however, present expert evidence that particular entries were improper or that the defendant's lifestyle reflected greater assets or income than reported in financial statements. As the issue is the defendant's available net worth to respond to a punitive award, the defendant's future monetary needs, including any amounts necessary to respond to this or other compensatory judgments, properly could be taken into consideration. To the extent the defendant's net worth is a disputed fact, a defendant may wish to request a special verdict to determine on just what "net worth" the jury bases its punitive award.

Another looming question as to a defendant's net worth is whether a parent corporation's net worth can be considered, at least absent an alter ego showing. To date, the answer appears to be "no." E.g., *Tomaselli v. Transamerica Ins. Co.*, 25 Cal.App.4th 1269, 1284-1286 (1994) (due process forbids use of parent company's financial status to prove net worth absent showing that parent controlled litigation); *Institute of Veterinary Pathology, Inc. v. California Health Lab, Inc.*, 116 Cal.App.3d 111, 120 (1981); *HCA Health Servs. of Midwest, Inc. v. National Bank of Commerce*, 294 Ark. 525, 531-532, 745 S.W.2d 120, 124 (1988); *Walker v. Dominick's Finer Foods, Inc.*, 92 Ill.App.3d 645, 649, 415 N.E.2d 1213, 1216-1217, 47 Ill.Dec. 900, 903-904 (Ill. App. Ct. 1980); see also *Liberatore v. Thompson*, 157 Ariz. 612, 621, 760 P.2d 612, 621 (Ariz. Ct. App. 1988) (where punitive damages are insurable, carrier's net worth is irrelevant; "It is a defendant's own wealth, not his insurer's wealth, that bears on the proper level of punitive damages"). But the issue is pending in the California Supreme Court. *West American Ins. Co. v. Freeman*, No. S049306 (Cal. filed Jan. 8, 1996). And, a plaintiff is free to establish an alter ego relationship between corporations, between an individual and another entity he or she controls, or based on the fact that the defendant controls assets nominally in another's name.

Alternate financial condition measures have been suggested. All such alternates are controversial. One is the profit the defendant made from the wrongful activity. Compare *Wyatt v. Union Mortgage Co.*, 24 Cal.3d at 790-791 and *Cummings Medical Corp. v. Occupational Medical Corp.*, 10 Cal.App.4th 1291, 1298-1301 (1992) with *Kenly v. Ukegawa*, 16 Cal.App.4th 57 (disagreeing with *Cummings Medical*). Cf. *Adams v. Murakami*, 54 Cal.3d at 116 n.7 (leaving open whether profit from the misconduct is a proper measure). Some have argued that the defendant's true financial condition is best reflected by a publicly traded defendant company's stock market value. The argument is that the market's valuation more accurately reflects a company's true worth, both in net assets and earnings potential, than a net worth based on historical asset purchase prices. On the other hand, such a market value arguably measures only investor expectation and not true value and can be notoriously subject to inexplicable market fluctuations. An investment banker or similar expert's valuation opinion may be more relevant. If expected future earnings are relevant, then an individual defendant's financial condition might include his or her discounted expected lifetime income, as reflected, e.g., in how much life

(Continued next page)

Punitive Damages

Continued from page 8

insurance or disability insurance he or she might have.

Appellate courts have not ruled definitively on these alternative financial condition theories. Until they do, both sides will want to object as appropriate and to provide expert testimony as to why their theory is better. Any party proposing such an alternate financial condition theory must be prepared to show why traditional net worth and net income measures are inadequate, e.g., if the defendant is a non-profit organization.

The defense, on the other hand, may wish to focus upon financial factors that do not address a corporate defendant as a whole, but rather just its parts. If the misconduct is limited to a particular division, department, branch, or office, the defense may wish to present evidence of that division's, department's, branch's, or office's budget or profits or size compared to the corporate entity as a whole. Arguably, if the problem is a rogue office, the punishment should be limited to that office.

Another problem arises where both federal and state claims are tried together. The burden of proving financial condition is a substantive legal rule and governed by the applicable substantive law. Contrary to California law, federal law imposes the burden of proving financial condition on the defendant. Thus, if federal and state claims are tried together, the plaintiff has the burden of proving financial condition on the state claims while the defendant has the burden of proving financial condition as to the federal claims. *Chavez v. Keat*, 34 Cal.App.4th 1406 (1995). This can lead to a procedural morass. It may require that state and federal claims be tried separately. It may also provide an incentive for the plaintiff to continue to pursue both state and federal claims in the same action, even though ultimately the plaintiff may have to choose between the federal and the state remedies. Differing state and federal rules and attitudes toward bifurcating trials may also suggest which forum a party might prefer.

4. *Comparable Statutory Sanctions. BMW of North America, Inc. v. Gore*, 116 S.Ct. at 1603, relied on statutory civil and criminal sanctions for comparable misconduct as one of three factors in concluding that a punitive damage award was constitutionally excessive. Previous California decisions hardly mentioned this factor. Now, however, the parties should scrutinize statutory provisions for comparable penalties. One common statutory civil penalty is treble damages. This is the equivalent to a two-to-one ratio between punitive and compensatory damages. But the parties should not overlook criminal and administrative penalties. Loss or suspension of a state license could be much more devastating than any fine.

(Continued on page 11)

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The Surprising Power of the Unclean Hands Defense

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We all learned about the affirmative defense of "unclean hands" in law school. And in preparing an answer to a complaint, many lawyers routinely include this defense among a list of affirmative defenses without giving the matter much thought.

Many lawyers fail to appreciate the power of the "unclean hands" defense. In the right circumstances, it can be the key to winning the case on a motion or at trial. It may be applied regardless of whether the plaintiff's claim is considered to be "in law" or "in equity."

A surprising number of decisions from the California courts in recent years have applied the unclean hands defense to bar the plaintiff's lawsuit in its entirety. Many of these decisions arise from dispositive motions. And even where the defendant cannot prevail on summary judgment because of disputed issues of fact, a party can obtain a bifurcated trial based on the affirmative defense of unclean hands. This may result in a victory for the defendant without trial by jury of the remaining issues in the case. This defense has been applied to bar plaintiffs' claims in various types of cases such as professional liability, employment and intellectual property cases.



Michael L. Cypers

The Essence of "Unclean Hands"

The United States Supreme Court has stated that the unclean hands doctrine is "far more than a banality. It is a self-imposed ordinance that closes the doors of a court of equity to one tainted with inequity or bad faith relative to the matter in which he seeks relief, however improper may have been the behavior of the defendant." *Precision Instrument Mfg. Co. v. Automotive Maintenance Machinery Co.*, 324 U.S. 806, 65 S.Ct. 993, 997 (1945).

The unclean hands doctrine rests upon the long-recognized maxim that "he who comes into equity must come with clean hands." *Ellenburg v. Brockway, Inc.*, 763 F.2d 1091, 1097 (9th Cir. 1985). Under California law, the unclean hands doctrine may apply to bar "legal" claims as well as "equitable" claims, *Pond v. Insurance Company of North America*, 151 Cal.App.3d 280, 290 (1984); *Fibreboard Paper Products Corp. v. East Bay Union of Machinists*, 227 Cal.App.2d 675, 728-729 (1964), and it may be applied to both tort and contract remedies. *Burton v. Sosinsky*, 203 Cal.App.3d 562, 573 (1988); *Blain v. Doctor's Co.*, 222 Cal.App.3d 1048 (1990).

In *Camp v. Jeffer, Mangels, Butler & Marmaro*, 35 Cal.App.4th 620, 638-639 (1995), the California Court of Appeal distinguished the type of improper conduct by plaintiff which will bar the plaintiff's claim from that which will not:

"Of course, ...it is not every wrongful act nor even every fraud which prevents a suitor in equity from obtaining relief. The misconduct which brings the unclean hands doctrine into operation must relate directly to the transaction concerning which the complaint is

(Continued on page 10)

The Unclean Hands Defense

Continued from page 9

made, *i.e.*, it must pertain to the very subject matter involved and affect the equitable relations between the litigants. Accordingly, relief is not denied because the plaintiff may have acted improperly in the past or because such prior misconduct may indirectly affect the problem before the court." Citing *Fibreboard Paper Products, supra* at 728-729.

The unclean hands doctrine may be applied at the pleading stage [*Blain v. Doctors Co.*, 222 Cal.App.3d 1048 (1990)], on summary judgment [*Camp v. Jeffer, Mangels, Butler, & Marmaro*, 35 Cal.App.4th 620 (1995); *DeRosa v. Transamerica Title Ins. Co.*, 213 Cal.App.3d 1390 (1989)] or at trial [*Dills v. Delira Corp.*, 145 Cal.App.2d 124 (1956)].

The Pleading Stage

In *Blain v. Doctors Co.*, 222 Cal.App.3d 1048 (1990), the Court of Appeal applied the unclean hands doctrine at the pleading stage to bar a legal malpractice claim. The plaintiff was a physician and defendant in an underlying medical malpractice action. In the underlying action, the physician's attorney advised him to lie at a deposition, and he followed the advice. *Blain*, 222 Cal.App.3d at 1052. The underlying action eventually settled and thereafter plaintiff brought a legal malpractice claim against the attorney who advised him to lie. Plaintiff alleged that defendant attorney's improper legal advice precluded plaintiff's further work as a physician, in part because the size of the settlement made it difficult for him to obtain malpractice insurance, and caused him emotional distress. *Id.*

The trial court held that plaintiff's legal malpractice claim was barred by the doctrine of unclean hands and sustained defendant's demurrer to plaintiff's complaint. *Blain*, 222 Cal.App.3d at 1057. The Court of Appeal affirmed. *Id.*

The Court of Appeal stated the unclean hands defense — "He who comes into Equity must come with clean hands" — applied to plaintiff's claim against the attorney who allegedly counselled him to lie. *Blain*, 222 Cal.App.3d at 1059. After a review of the history of the unclean hands doctrine, the Court of Appeal found plaintiff's own unclean hands of lying barred his relief. Plaintiff could not demonstrate that he suffered either emotional distress or a loss of ability to practice medicine independent of his lie. *Id.* at 1063-1064. The Court of Appeal observed: "Even the most naive must know that lying under oath is illegal" and plaintiff's emotional distress (from being exposed to greater liability because the lie was discovered) resulted from his own misconduct. *Id.* at 1063.

Summary Judgment

The California courts have applied the unclean hands doctrine in a number of cases to grant summary judgment in favor of the defendant. See, *e.g.*, *Camp v. Jeffer, Mangels, Butler, & Marmaro*, 35 Cal.App.4th 620 (1995); *DeRosa v. Transamerica Title Ins. Co.*, 213 Cal.App.3d 1390 (1989); *Pond v. Insurance Co. of North America*, 151 Cal.App.3d 280 (1984).

In *Camp v. Jeffer, Mangels, Butler, & Marmaro, supra*, the court applied the analytical underpinnings of the unclean hands doctrine in a wrongful discharge case to award summary judgment in favor of the employer. The plaintiffs were employed by a law firm, which terminated their employment. They filed an action for wrongful discharge and related torts. During discovery, the law firm learned that the plaintiffs lied in their job applications, in which they certified under penalty of perjury that they had not been convicted of a felony, which assertion the law firm required its employees to make because it was a condition of the

firm's representation of one of its clients, the Resolution Trust Corporation. In fact, both plaintiffs had previously been convicted of conspiracy to use false information to defraud a federally insured bank, which convictions they omitted in their job applications.

The Court of Appeal concluded that this "after acquired evidence" by the law firm during discovery in the wrongful discharge case barred the plaintiffs' claims. The court looked to the doctrine of unclean hands for guidance. The court concluded as follows:

"In this case, we are satisfied that the Camps' misrepresentations about their felony convictions relate directly to their wrongful termination claims. Since the Camps were not lawfully qualified for their jobs, they cannot be heard to complain that they improperly lost them. Given the nature of the misrepresentations, the potential damage to Jeffer, Mangels, and the fact that the Camps were disqualified from employment by means of government requirements, the public policies of the state are adequately served by barring Camps' claims and allowing them, if they so desire, to report Jeffer, Mangels's alleged wrongdoing to the appropriate authorities."

35 Cal.App.4th 620, 639.

In *DeRosa v. Transamerica Title Ins. Co.*, 213 Cal.App.3d 1390 (1989), the court held that the unclean hands doctrine barred plaintiff from bringing a malicious prosecution claim and granted a summary judgment motion in favor of defendant. In that case, plaintiff and defendant were involved in a quiet title action in an underlying action. *Id.* at 1394. During the course of the underlying action, defendant received certain information that plaintiff was involved in a conspiracy against it; defendant thus asserted a fraud claim against plaintiff. *Id.* Defendant's fraud claim was based on plaintiff's misrepresentation of his true ownership interest in the property that was the subject of the quiet title action. Specifically, plaintiff took title to the property solely to assist another in avoiding creditors. *Id.* Plaintiff prevailed on the fraud claim and then turned around and brought the malicious prosecution claim against defendant. The Court of Appeal affirmed the trial court's granting of summary judgment.

The Court of Appeal held that plaintiff's failure to reveal to defendant his true interest in the property when he demanded title be quieted in him constituted unconscientious conduct. *DeRosa*, 213 Cal.App.3d at 1396. And the court held this conduct was directly related to his malicious prosecution action because defendant would not have become involved in and subsequently proceeded against plaintiff for fraud if plaintiff had not concealed the true facts about his ownership interest. *Id.* at 1397. Under these circumstances, the Court of Appeal concluded the unclean hands doctrine barred plaintiff's action. *Id.*

In *Pond v. Insurance Co. of North America*, 151 Cal.App.3d 280 (1984), the plaintiff sued for malicious prosecution after prevailing in a prior action. However, it appeared that he withheld evidence in the prior action, which may have had a material effect on the outcome of the case.

The trial court ruled that plaintiff's knowing failure to disclose evidence in the prior action constituted "unclean hands," and granted summary judgment dismissing the malicious prosecution case. The Court of Appeal affirmed, holding that the trial court properly applied the unclean hands doctrine on summary judgment because plaintiff's conduct "directly 'infected' the actual cause of action before the court." *Id.*, at 290.

Trial Considerations

Even where the unclean hands doctrine does not bar the plaintiff's case at the pleading stage or on summary judgment, it can

(Continued on next page)

The Unclean Hands Defense

Continued from page 10

be presented at trial. And because the affirmative defense, if asserted successfully, would bar the plaintiff's entire case, the defendant may be able to obtain a bifurcated trial based on the defense. The rationale for such a bifurcation motion is that it could reduce the time and cost required for a full trial. In addition, because the unclean hands defense is classically considered an "equitable defense" which is tried to the court, this procedural strategy appeals to some defendants who would like to avoid a jury trial.

Precedent exists for this approach under both California and federal law. In California, the trial court enjoys broad discretion to order bifurcation of any cause of action or any special issue. Code of Civil Procedure Section 1048. This procedure was followed in *Dills v. Delira Corp.*, 145 Cal.App.2d 124, 129-130 (1956). The court bifurcated the equitable issues, and tried them in a court trial, which made a jury trial on the legal issues moot. The Court of Appeal affirmed the procedure, and the result. See also, *Raedeke v. Gibraltar Savings & Loan Co.*, 10 Cal.3d 665, 671 (1974).

A similar procedure may be used in federal court. See, Rule 42(b) of the Federal Rules of Civil Procedure; *Gardco Manufacturing, Inc. v. Hearst Lighting Co.*, 820 F.2d 1209, 1213 (Fed. Cir. 1987) (district court bifurcates trial on affirmative defense of plaintiff's alleged inequitable conduct in obtaining patent, and rules against plaintiff in court trial, making jury trial on plaintiff's claims moot; Court of Appeals affirms.); *In Re Yarn Processing Patent Validity Litigation*, 472 F.Supp. 170, 174 (S.D. Fla. 1979) (similar procedure followed in intellectual property dispute by trying defendant's "unclean hands" defense first to court before plaintiff's claims to a jury).

Conclusion

The unclean hands defense can be a very powerful weapon in the hands of the defendant. The defendant's counsel should consider the defense at the outset of the case and throughout its pendency to determine whether the defense applies and, if so, when and how it should be asserted. The unclean hands defense affords plenty of opportunities for creativity in the hands of defense counsel. If it is asserted properly, it has the potential to yield a satisfying outcome and a satisfied client.

— Michael L. Cyfers

Doctor's Assocs., Inc. v. Casarotto

Continued from page 5

authority over arbitration proceedings, the effect of such a holding remains to be seen.

The *Engalla* holding may provide more "bark" than "bite." For example, in dealing with statutes like Code Civ. Proc. § 1281.3, an expansive view of "interstate commerce" and corresponding application of the FAA which contradicts state law would nullify such a procedural statute. As such, all state procedural statutes at odds with the FAA could suffer the same fate. Thus, the potential for eviscerating state arbitration schemes under the guise of "interstate commerce" is as limitless as the scope of "interstate commerce" itself.

— Peter S. Selvin and Glen A. Rothstein

Punitive Damages

Continued from page 9

The standard BAJI jury instructions do not direct the jury even to consider comparable statutory penalties. Again, if a party wants to rely on such comparable statutory sanctions, it should request appropriate instructions and modifications to the current BAJI instructions.

5. *The Size of the Punitive Award.* Punitive damages are a windfall. E.g., *Las Palmas Assocs. v. Las Palmas Ctr. Assocs.*, 235 Cal.App.3d 1220, 1258 (1991). For a plaintiff, obtaining a punitive award is a little like winning the lottery. A balance needs to be struck between an award large enough to make a difference to the defendant and one that simply is too great a windfall. But the present standard jury instructions do not even mention the absolute size of the award as a consideration for the jury. Proffering an appropriate jury instruction and objecting to the standard instructions as deficient may at least preserve the issue for appeal.

6. *To Punish And To Deter, But Not To Destroy.* This in many ways is the ultimate test for any punitive damage award. A civil trial's punitive damage phase has much in common with a criminal sentencing hearing. The defense, if possible, may wish to emphasize why such misconduct will not happen again: e.g., the defendant has gone out of the particular business, the responsible individuals have left, the responsible individuals have been disciplined. Plaintiffs on the other hand may wish to argue that the defendant remains recalcitrant and unrepentant.

For plaintiffs, this argument is made easier if the defense continues to deny that the defendant did anything wrong. The defense, therefore, must walk a fine line between a *mea culpa* (which might come back to haunt the defense on appeal from the liability verdict) and a denial of any wrongdoing. One approach may be for the defense to argue that the defendant recognizes that the jury has found that it acted wrongfully. If the facts are as the jury found them, the defendant recognizes that such conduct is impermissible. And the defendant has taken a number of steps to ensure that similar conduct does not happen in the future (regardless of whether it happened here).

Plaintiffs typically argue even in circumstances where the defendant may have gone out of the particular business, that punitive damages are necessary to deter others. Either the plaintiff or the defense, however, may wish to present evidence of whether the misconduct at issue is a problem with others still engaged in the former line of business.

If the defendant is still in the particular business, another issue is when the punitive award will be large enough to be felt. If the award is premised upon senior management conduct, the relevant standard may be that of materiality for the purposes of accounting reports and financial disclosures to owners and stockholders. If the conduct at issue took place at a lower echelon, the standard may more appropriately be based on the particular department's or office's budget or what amount would have an effect on the individual actor's career.

Conclusion

This article has not attempted comprehensively to survey all the possible evidence relevant to determining the amount of punitive damages. Rather, the point is that the trial's punitive damages phase should be more than just regurgitating the evidence during the trial's liability and compensatory damages phase. Given the potential stakes, thorough attention to evidentiary and instructional issues and a complete record are in order, both for the jury's initial decision and to allow for thorough review on a motion for new trial and on appeal.

— Robert Olson

Letter from the President

Continued from page 1

1996 Annual Seminar. The 1996 Annual Seminar is set for October 25-29, 1996 at the Four Seasons Hotel in Maui on trying punitive damages cases. If you want to attend, you should quickly contact Windsor Travel at 310-477-6783. An illustrious group of lawyers, judges and consultants are preparing the program and an equally terrific group is attending.

1997 Annual Seminar. The 1997 seminar is set for October 24-26, 1997 at the Westin Mission Hills Resort in Rancho Mirage, CA. Contact John Pennington at Sheppard Mullin if you are interested in planning the seminar.

Trial Practice Project. We are working with Public Counsel to develop a project to provide hands-on trial experience to ABTL members. We hope to create concrete trial opportunities for our members which will enhance our skills and self-confidence, while meeting a community need. Pat Benson of Mitchell Silberberg and Margaret Levy of Manatt, Phelps & Phillips are chairing the committee.

Federal Courts Committee. Last year the committee evaluated proposed rule changes and put on a dinner program. This year the group will be chaired by Michael Grace at Greenberg, Glusker. Last year's chair, Alan Friedman of Tuttle & Taylor, is now on our board.

ABTL Report. Vivian Bloomberg of Peterson & Ross continues to put out our first-rate newsletter. Send her material or volunteer to work on our publication.

Technology Law Committee. This new committee put on a dinner program last year and meets regularly, sometimes with outside speakers. Michael Sherman of Alschuler, Grossman & Pines chairs the committee.

Newer Lawyers Committee. We have formed a new committee to focus on what newer lawyers need. Eric Waxman of Skadden Arps chairs the committee.

Membership Committee. Our membership committee is chaired by William Wegner of Gibson Dunn & Crutcher and Alan Friedman of Tuttle & Taylor.

ABTL Expansion. Two other ABTL chapters, in San Francisco and San Diego, have been formed in the last several years based on our model. Those chapters have been successful in attracting the highest quality lawyers and judges. Both groups have been equal partners with Los Angeles in putting on our annual seminars. We are now working with interested lawyers and judges in the Central Valley and Orange County to replicate ABTL there. Bob Fairbank of Fairbank & Vincent and Harvey Saferstein of Chadbourne & Parke are leading the support team from Los Angeles, along with Art Shartsis of San Francisco and Mark Mazzarella of San Diego. Expansion is exciting for our chapter because it broadens our network of highly competent lawyers and judges.

We want to be a diverse and inclusive organization. If you want to participate, feel free to contact the committee chairs above or any of our board members or officers. Your ideas and involvement are welcome. ABTL seeks to enhance the work of the community of lawyers, judges and clients who are involved in business litigation. Give us the benefit of your ideas. You can reach me at Alschuler, Grossman & Pines by phone or email me at kkaplowitz@agplaw.com. Along with fellow officers David Stern, Richard Burdige and Jeff Briggs, I look forward to ABTL members' enjoying a year of professional enrichment and growth.

— Karen Kaplowitz

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