Fortuity is a fundamental principle underlying liability insurance. “...fortuity is an inherent requirement of all risk insurance policies... 'The concept of insurance is that the parties, in effect, wager against the occurrence or non-occurrence of a specified event; the carrier insures against a risk, not a certainty.' [citations omitted].” Two Pesos v. Gulf Ins. Co., 901 S.W.2d 495, 501 (1995). For this reason, intentional acts, as well as liabilities arising from an insured’s contractual commitments, are generally excluded from coverage.

At the same time, copyright infringement is one of the covered “offenses” which is enumerated in the “advertising injury” portion of a typical Commercial General Liability (“CGL”) policy. In many cases, a claim for copyright infringement arises when a licensee is alleged to have breached the terms of the license agreement under which the licensee was given the right (often limited by duration, type of media and other limitations) to exploit the underlying work. In such circumstances, the copyright licensee will seek to obtain coverage from its insurer.

It should be emphasized that in order to be covered under the “advertising injury” portion of a CGL policy, the infringement must occur either “in” the policyholder’s advertising or must have been committed “during the course of advertising.” As discussed below, the current trend is that “in the course of advertising” language is used by carriers to limit the scope of coverage to those circumstances where the alleged infringement occurs during a wide-scale advertising campaign, as opposed to more limited forms of advertising. See, e.g., Hameid v. National Fire Ins. of Hartford, 31 Cal. 4th 16 (2003).

The cases involving coverage disputes illustrate an important intersection between copyright and insurance law. This article analyzes the pertinent cases in this area, provides an analytical framework for evaluating coverage problems and suggests tools that policyholders can use to obtain coverage in difficult cases.

Basic Grant of Liability Insurance Coverage for Copyright Infringement

Among the covered “offenses” typically included within Coverage B is the “infringement” of another’s copyright, trade dress or slogan in your “advertisement.” Thus, on its face, the licensee’s CGL policy will typically provide coverage for copyright infringement.

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Prior to the advent of the 1998 and 2001 ISO forms, a key dispute that arose in this area was whether the insured could show the required nexus between the infringement and its advertising. See, e.g., Sentry Ins. v. R.J. Weber Co., 2 F.3d 554 (5th Cir. 1993) (publishing, distributing, and selling opponent’s copyrighted works does not bear sufficient causal connection to sustain coverage for advertising injury); Robert Bouden, Inc. v. Aetna Cas. & Sur. Co., 977 F.Supp. 1475 (N.D. Ga. 1997) (no nexus found when insured claimed it was induced to copy software in order to create its advertising campaign). See also Hameid v. National Fire Ins. of Hartford, 31 Cal.4th 16 (2003) (construing "in the course of advertising" language under the earlier ISO forms to mean widespread dissemination of advertising, as opposed to one-on-one solicitation). Under the new ISO forms, copyright infringement must now occur "in" the policyholder’s "advertisement." At the same time such policies also typically exclude coverage for certain personal and advertising injuries arising out of breach of contract. A current version of this exclusion reads as follows:

"[This insurance does not apply to] [p]ersonal and advertising injury arising out of a breach of contract, except an implied contract to use another's advertising idea in your 'advertisement.'"

This exclusion takes on particular importance in those copyright disputes that arise in the context of an alleged breach of a license agreement. In these disputes, a licensee is alleged to have breached the underlying license by, for example, using the copyrighted material beyond the time period provided for in the license or in a manner not authorized by the license. As more fully discussed below, the first step in analyzing coverage for these kinds of disputes is to classify the nature of the dispute.

**Classification of the Claim is Key to Determining Coverage**

In cases involving the breach of a copyright license, a carrier may claim that the underlying dispute does not assert a claim for copyright infringement, as opposed to a claim for breach of contract. Thus, for example, where the gravamen of the underlying suit is that the defendant-insured exceeded the scope of the copyright license, the carrier may seek to avoid coverage by characterizing the underlying claim as one sounding in breach of contract, as opposed to copyright infringement.

Whether a particular claim is deemed to constitute the "offense" of copyright infringement for purposes of coverage under a CGL Policy will likely depend on whether the claim "arises under the Copyright Act" for purposes of establishing federal subject matter jurisdiction. In this regard, practitioners seeking to obtain insurance coverage in respect to copyright infringement claims will need to address the federal jurisprudence concerning whether a claim under the Copyright Act has been asserted. In this regard, the most commonly cited test for whether federal jurisdiction exists for a particular claim (under the Copyright Act) is in *T.B. Harms Co. v. Eliscu*, 339 F.2d 823, 828 (2d Cir. 1964), cert. denied, 381 U.S. 915 (1965):

"Mindful of the hazards of formulation in this treacherous area, we think that an action "arises under" the Copyright Act if and only if the complaint is for a remedy expressly granted by the Act, e.g., a suit for infringement or for the statutory royalties for record reproduction, 17 U.S.C. § 101 (citation omi-

Put simply, "[w]hen a complaint alleges a claim or seeks a remedy provided by the Copyright Act, federal jurisdiction is properly invoked." *Basset v. Mashantucket Pequot Tribe*, 204 F.3d 343, 355 (2d Cir. 2000).

Importantly, there is ample case law which supports the principle that a claim against a copyright licensee for breach of the copyright license may "arise under the Copyright Act" for purposes of establishing subject matter jurisdiction in federal court. See *Kamakazi Music Corp. v. Robbins Music Corp.*, 684 F.3d 228, 230 (2d Cir. 1982) ("Kamakazi’s suit is, was, and always has been based on the Copyright Act. Kamakazi sued Robbins for publishing Manilow works after the contract between the two had expired. Once the contract had expired, Robbins was liable for infringement of Kamakazi’s copyrights"); *Gerg vs. Krause Pubs., Inc.*, 58 F.Supp.2d 1261, 1268 (D. Kan. 1999).

These cases have implications for insurance coverage: to the extent that a claim for breach of a copyright license agreement states a claim "arising under the Copyright Act," the insured-licensee will more likely be able to establish the underlying copyright infringement “offense” for purposes of obtaining coverage.

In *Kamakazi*, Kamakazi Music ("Kamakazi") licensed defendant Robbins Music ("Robbins") until the end of 1979 to print and sell the sheet music of pop star Barry Manilow. After the end of 1979, however, Robbins continued to sell the sheet music, contending it could do so based on its interpretation of a provision in the license agreement relating to Robbins’ right after 1979 to sell "mixed folios" of the sheet music.

Kamakazi filed suit under the Copyright Act. Following the District Court’s confirmation of an arbitration award in favor of Kamakazi, Robbins appealed, claiming, among other things, that the District Court had lacked subject matter jurisdiction. Robbins claimed that because its liability turned on a question of contract interpretation, no claim was asserted under the Copyright Act. The Second Circuit rejected Robbins’ contention that no Copyright Act claim was presented:

"We agree with Judge Sweet that the district court had jurisdiction. Kamakazi’s suit is, was, and always has been based on the Copyright Act. Kamakazi sued Robbins for publishing Manilow works after the contract between the two had expired. Once the contract had expired, Robbins was liable for infringement of Kamakazi’s copyrights. Given the explicit language of Kamakazi’s complaint, and the acts complained of, it is frivolous for Robbins to contend that its contractual defense makes Kamakazi’s suit one for breach of contract. The district court had jurisdiction because the claim was for copyright infringement. The claim sent to the arbitrator was for copyright infringement. The damages calculated by the arbitrator at Robbins’ urging were for copyright infringement." 684 F.2d at 230.

The Court reached a similar conclusion in *Gerg v. Krause Publications, Inc.*, 58 F.Supp.2d 1261 (D. Kan. 1999). In that case defendant magazine hired plaintiff photographer to take photographs for its magazine. Defendant later republished some of the photographs in a book which plaintiff claimed was a breach of contract and copyright infringement. Defendant moved to dismiss the complaint for lack of subject matter jurisdiction on the ground that there was no claim asserted under the Copyright Act. The District Court denied the motion on the ground that the contract claim arose under the Copyright Act because it alleged that the defendant had used the photographs beyond the scope of its license:

"Once an assignment or license has expired, "the copyright (Continued on Page 3)
Liability Insurance Coverage

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The Court finds that Gerig’s copyright claim “arises under” the Copyright Act... [The Court is not presented with the question of whether or not the acts of Krause were sufficient to constitute a termination of the agreement. Rather, this case is one in which Krause is alleged to have published the images beyond the scope contemplated in the agreement. Further use of the images beyond their publication in the magazine required Gerig’s consent. Therefore, because the alleged contract had expired, the court finds Gerig has a potential claim for copyright infringement, which rightfully belongs to this court.” 58 F.Supp. 2d at 1208.

Not every action predicated on rights derived from the Copyright Act, however, is necessarily one “arising under” the Copyright Act. See Yount v. Acuff-Rose-Opryland, 103 F.3d 830, 834 (9th Cir. 1996) (construction of an assignment of royalties under copyright implicates strictly a question of state law); Dolch v. United Cal. Bank, 702 F.2d 178 (9th Cir. 1983) (claim that assignment of copyright was invalid for lack of consideration is strictly a question of state law); Dosey v. Money Mack Music, Inc., 304 F. Supp. 2d 858, 867 (E.D. La. 2003) (in action for rescission of a contract involving copyrights, the state courts have jurisdiction); Wolfe v. United Artists Corp., 583 F.Supp. 52, 56 (E.D. Pa. 1983) (No federal jurisdiction when defendants continued to collect royalties on plaintiff's work after expiration of contractual right to do so, and failed to repay these royalties to plaintiffs).

The importance, for purposes of assessing coverage, of determining whether a copyright claim “arises under” the Copyright Act is illustrated by plaintiffs). The importance, for purposes of assessing coverage, of determining whether a copyright claim “arises under” the Copyright Act is illustrated by plaintiffs).

The Early Neutral Evaluation Program — A Personal Perspective

In 2005, the Los Angeles Superior Court received a grant from the California Judicial Council to develop an Early Neutral Evaluation (“ENE”) program patterned after a process developed and adopted by the United States District Court for the Northern District of California in the 1980s as part of an effort to identify means for reducing the staggering expense of traditional litigation. Early assessments of the Northern District ENE experience were promising, strongly suggesting that a preponderance of its participants found the process valuable. (See, D.I. Levine, Early Neutral Evaluation: The Second Phase, Journal of Dispute Resolution (1989) 1; and, Joshua D. Rosenberg, H. J. Folberg, Alternative Dispute Resolution: An Empirical Assessment, 46 Stanford Law Review (Fall 1994).

In May of 2006, a group of seasoned attorneys, handpicked to participate in a pilot program by the Los Angeles Superior Court to experiment with the ENE process, gathered for a daylong training designed to introduce them to the process, the objective of which is to make available to civil litigants in Los Angeles courts a panel of experienced litigators, with expertise not only in ADR, but also in commercial, employment, medical or legal malpractice, real estate, trade secret, or unfair competition litigation, who would provide parties and counsel — on a fully voluntary and totally confidential basis, and at an early stage in litigation — with a neutral, informed evaluation of their respective positions, to help organize the cases going forward and, ultimately, to encourage settlement.

Commencing in the summer of 2006, parties and counsel with cases pending in the participating Los Angeles venues who chose to participate in the program began selecting members of the pilot program panel to evaluate their cases. Through December 2006, lawyers in some 88 cases in the Los Angeles Superior Court chose to submit their cases to the ENE pilot program.

The following are personal reflections based on my experience as a pilot panel member in the dozen or so cases in which I have been involved to date, some of which have been concluded, a number of which have settled, and several of which are ongoing. Clearly, my comments are based on anecdotal evidence—not scientific research — and should consequently be viewed with some degree of skepticism.

First, many counsel seem to find value in the process because it can be useful to them in conveying to their clients the highly unpredictable nature of traditional litigation, the costs of going forward, and the risk of losing cases in which clients may have a deep, but unrealistic, emotional investment, without making the lawyer seem disloyal or unsupportive. In many cases both counsel and parties respond to the ENE experience as a “wake-up call,” giving them their first opportunity to view their cases through the lens of an experienced neutral rather than through the frequently distorting lens of partisan self-interest. Counsel on occasion request written evaluations expressly for the purpose of pointing out to clients the possibility of loss, the expense of going forward, and other factors counsel may be reluctant to express for fear of

— Peter S. Selvin and Jed I. Lowenthal

Robert Wrede
incurred client dissatisfaction for a perceived lack of fighting spirit. Indeed, clients and counsel alike seem to take some comfort in evaluations rendered by knowledgeable neutrals, who seem generally to be viewed by clients and counsel alike as experienced, well intentioned, unbiased and reliable.

Second, many counsel and parties appear to view the ENE process as an opportunity to commence settlement negotiations without suffering the perceived (but in my view, totally unjustified) stigma many lawyers and litigants seem to associate with willingness to discuss settlement early in the litigation process. As an overwhelming number of civil cases settle at some stage before the commencement of trial, commencing early settlement negotiations without stigma benefits all parties. (The best currently available information suggests that only 0.8% of the civil cases filed in our California courts, and less than 2.8% of the civil cases filed in our federal system, actually commence trial, let alone reach final, unappealable verdict. See, M. Galanter, The Vanishing Trial: An Examination of Trials and Related Matters in Federal and State Courts, 1 Journal of Empirical Legal Studies, No. 3 (November 2004); also found at http://www.abanet.org/litigation/vanishingtrials. See also, R. Wrede, Honolulu: Geneva of the Pacific?, Mealey’s International Arbitration Report, November 2006.)

Third, the ENE process clearly encourages early investigation, analysis and preparation — the end result of which is highly useful in both evaluating and even resolving cases soon after filing — thus facilitating settlement discussions, and even settlement, well before significant litigation costs have been incurred and barriers to settlement have consequently escalated.

Fourth, as with other ADR methodologies, the ENE process allows considerable flexibility to the evaluator and counsel in structuring the proceeding, ranging from the extensive use of teleconferences and the transformation of the process from pure evaluation to settlement discussions, on the one hand, to a full-blown hearing to test and train witnesses in a quasi-litigation environment, as well as to provide a written evaluation should the participants so desire, on the other.

Fifth, many counsel seem largely unaware of the rationale behind ENE or the various options it makes available to help them clarify factual and legal issues, identify and resolve case management problems, provide a neutral, informed perspective on the dispute, as well as to emphasize the desirability to clients of negotiated resolution. More detailed communication by the court with litigation counsel, generally, and those who opt for ENE, in particular, to familiarize them with the process at or about the time an eligible case is filed would seem desirable.

Sixth, ENE offers participants the better attributes of both mediation and arbitration. The ENE process provides the judgmental aspects of arbitration without the negative implications of a binding, public judgment or verdict, since the ENE evaluation is both confidential, non-binding and “risk free.” If the parties so desire, ENE can also offer the facilitated negotiation aspects of mediation at a stage in the litigation when settlement should be easier to reach because significant litigation expenses have not yet been incurred and positions are less likely to have become intractably polarized. Unlike mediation, in which a mediator may develop an evaluation of the case based upon confidential information or with the intent to move the parties towards settlement, the ENE evaluation is rendered by the neutral directly to the parties and counsel without ex parte contact, providing the participants the assurance that they are hearing an experienced neutral’s true evaluation of the case, based upon information presented in the joint session.

Seventh, far from being limited to cases in their early stages, ENE is being utilized by some counsel relatively late in the litigation process as a cost-free, neutral indicator of the possible outcome of summary judgment motions, apparently to assist them in deciding whether to fight or settle or to bolster their settlement posture.

In a nutshell, from my perspective as an advocate with forty years of experience and as a strong believer in ADR, the LASC pilot ENE program holds great promise as an expedient and affordable means of moving complex commercial cases toward resolution, and for reducing the cost of litigation that so many litigants find too expensive to bear.

There is, however, one aspect of the program that I believe needs to be carefully addressed and remedied. It strikes me as unrealistic to expect highly qualified professionals to donate large chunks of their time, gratis, to provide expert advice regarding challenging cases to counsel who are being well compensated for their efforts and parties who should receive tangible benefits from the free advice, as well. There is, in short, an absence of fair pro quo, with all participants — including the neutrals — receiving something of value in exchange for their efforts.

The ENE pilot program design provides that:

Evaluators shall provide convening time, preparation time (including preparation of the evaluation), and the first (3) hours of hearing time on a pro bono basis. Thereafter, the parties may be charged for additional hearing time on an hourly basis at rates established by the evaluator if the parties so consent in writing.

The dozen or so cases in which I am or have been involved as neutral evaluator have been both legally and factually complex, with some resulting in the submission of opening and reply briefs that have required hours of analysis to adequately prepare for the ENE session; hearings that also require hours to conduct; with yet more time required to draft an advisory opinion. One such case I recently handled involved briefs and replies some 4 1/2 inches thick. Far more than three hours must be spent to competently organize, consider and opine in such cases.

Quite candidly, imposing on qualified neutrals, however eleemosynary their inclinations, the obligation to expend the significant time and effort necessary to do a thorough, competent and credible job in evaluating factually and legally complex cases without some form of compensation for their services is unrealistic and, quite candidly, unfairly shifts to these neutrals a cost that properly should be borne by the government, not charitable individuals.

I firmly believe that the proponents of this program in the judiciary, as well as the political arms of our government, should remedy this inherent inequity in order to render the ENE program not only viable, but robust and popular. Traditional litigation is in steep decline, yet civil disputes (not surprisingly) are increasing commensurate with the increase in population, and the growth of commercial activity and its complexity. What’s wrong with this picture? The fact is that our social institutions must change with the times, to keep pace with changing needs and expectations. ENE is just such a change, but — in my opinion — it needs refinement and polish.

One step in the right direction might be to credit all organizational and preparation time expended by neutrals against the three pro bono hours. Another approach — perhaps in addition to charging ALL neutral time expended to the three hours — could be to impose some type of “administrative fee,” to be borne either by the participant or the court, or both, to help defray the out-of-pocket cost of communicating, filing and filing forms, and so forth, all of which costs are now borne by the neutrals.

Winston Churchill once observed that “Democracy is the worst form of government except all those other forms that have been tried from time to time.” That same observation could be applied to traditional American litigation. In his 1984 State of the Judiciary Address, Chief Justice Warren Berger, a vigorous ADR

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advocate, observed,

"The entire legal profession: lawyers, judges, law teachers has become so mesmerized with the stimulation of the courtroom contest that we tend to forget that we ought to be healers of conflicts. For many claims, trials by adversarial contest must in time go the way of the ancient trials by battle and blood... Our system is too costly, too painful, too destructive, too inefficient for a truly civilized people." (Emphasis added.)

To me, it seems beyond rational dispute that if our legal profession and judicial system are to truly offer litigants a cost-effective, reliable, and — above all — affordable means for dealing with civil conflict, they must do so by providing mechanisms that are less costly, less painful, less destructive, more predictable and more efficient than traditional litigation. The relatively recent addition of ADR, generally, and ENE, specifically, to the conflict management and resolution toolbox are certainly important and imaginative steps in the right direction, but much yet needs to be done to refine these processes, to attract participation by competent neutrals, and to encourage their utilization by litigants and their counsel.

It seems clear to me that ENE holds great promise for becoming a valuable tool in the pursuit of the challenging and elusive goal of providing cost-effective justice to our citizenry. ENE participants who have been polled have strongly indicated support for the process. Some 90% of the lawyers polled in the Levine study cited above felt that ENE should be expanded; 77% viewed evaluators as having made a useful contribution to the parties' understanding of the case; and 68% believed that the process improved case development, and contributed to eventual disposition. Moreover, some 20% to 30% of the cases in the study actually settled at the ENE session, which is consistent with my experience. It is not unreasonable to expect that the likelihood of subsequent settlement well short of trial is also significantly enhanced by the process.

Hopefully, the ENE process will continue to be refined and improved, and its objective of providing a less costly, less painful and destructive, more efficient and civilized means of dealing with civil conflict than the trial by ordeal and combat process that currently characterizes American litigation will eventually be realized - for the benefit of all concerned: taxpaying public, litigants, and the legal profession, alike.

In the final analysis, no matter how effective the program, the Court demands too much of its panelists when it asks them to donate large chunks of otherwise billable time to providing their expert assessments, or their abilities at brokering settlement, especially since counsel are being well compensated for their participation and the parties receive tangible benefits as well. In short, the program as currently designed simply does not provide all participants with compensation commensurate with the value of their respective efforts.

I am hopeful that our state government will eventually choose to appropriately compensate ENE panelists, much like the Court's party pay mediation panel. Alternatively, the Court might (at the very least) consider charging the organizational and preparation time necessarily expended by the neutral against the three pro bono hours. Another approach — hopefully in addition to full credit for time actually expended — would be to charge some type of "filing" or "administrative" fee to at least help defray the costs of filling out, filling and serving forms, and so forth, all of which costs are now borne by the neutrals.

My premise is simple: If ENE is to fulfill its significant promise its cost must be borne by society as a whole — not imposed on individuals, no matter how generous they may be.

— Robert Wrede

Bankruptcy Bulletin: Lawsuit to Recoup Preference Fails

A n individual makes a final payment to a company in settlement of an embezzlement claim, receives a release, and then files a chapter 7 bankruptcy petition within 90 days of the final payment. The chapter 7 trustee sues the company to avoid the final payment as an avoidable preference. The company settles the preference claim and pays the settlement amount. The company wants to recoup the preference.

If the company only has an allowed general unsecured claim against the bankruptcy estate for the repaid preference, it will have to share any distributions from the estate pro rata with other creditors holding allowed general unsecured claims. Typically, creditors holding such claims receive a small fraction of the allowed amount of the claim in distributions. The company, however, filed suit against the debtor in bankruptcy court seeking a determination that the debt was excepted from discharge on the theory that the repaid preference reinstated its embezzlement claim against the debtor that existed immediately prior to the debtor's final payment. If this determination were made, the debtor would have personal liability for the debt.

In Busseto Foods, Inc. v. Laizure (In re Laizure), 349 B.R. 604 (B.A.P. 9th Cir. 2006), the Ninth Circuit Bankruptcy Appellate Panel ("BAP") affirmed the bankruptcy court's decision that the company only had a claim against the bankruptcy estate to recoup the preference and dismissed the company's suit. This article discusses this recent case and offers some practical considerations for creditors confronted with the prospect of settling an alleged fraud claim and the risk that a settlement payment may be the subject of preference litigation in a subsequent bankruptcy.

The Laizure Decision

In Laizure, supra, the BAP concluded that Bankruptcy Code section 502 authorizes only a claim against the bankruptcy estate upon surrender of a preference and does not reinstate a claim against the debtor. Busseto Foods, Inc. ("BFI") employed Charles Laizure ("Laizure") as its controller and chief financial officer for several years. BFI terminated Laizure in 2004. BFI later discovered that he had allegedly embezzled funds from BFI during his employment. Laizure agreed to repay the money and made the final payment of $38,833.70 in June 2005, pursuant to an agreement. He received a comprehensive release in exchange for payment of the funds. Less than 90 days later, Laizure and his wife filed a chapter 7 petition, and a chapter 7 trustee was appointed.

The chapter 7 trustee demanded repayment of the final $38,833.70 payment to BFI as a preferential transfer. The trustee or debtor in possession is permitted to avoid certain pre-petition transfers as preferences under Bankruptcy Code section 547(b). An avoidable preference is: (a) any transfer of an interest of the debtor in property; (b) to or for the benefit of a creditor; (c) for or on account of an antecedent debt; (d) made while the debtor

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was insolvent; (e) within ninety days before the date of the bankruptcy petition (or within one year before the petition in an “insider” situation); and (f) the effect of which was to give the creditor more than he would have otherwise received in a chapter 7 distribution. Preference litigation is commenced by filing an adversary proceeding in the bankruptcy court and requires the filing and service of a summons and complaint.

BFI settled the preference claim for $34,000, paid that amount to the chapter 7 trustee, and filed a general unsecured claim against the bankruptcy estate for the amount paid. While in settlement negotiations, BFI filed a complaint seeking a determination that its claim against Laizure was excepted from discharge under Bankruptcy Code section 523(a)(4).

An individual debtor receives a discharge in chapter 7 unless one or more bases for denying a discharge set forth in Bankruptcy Code section 727(a) is proven to exist. Under Bankruptcy Code 726(b), the discharge in a chapter 7 case discharges the debtor from all pre-petition debts, except as provided in Bankruptcy Code section 523. Section 523 sets forth categories of debts that Congress has deemed should be nondischargeable. The categories of debt include, among others, any debt for embezzlement, larceny or fraud or defalcation while acting in a fiduciary capacity under Bankruptcy Code section 523(a)(4).

Laizure moved to strike the complaint, which BFI opposed. The bankruptcy court dismissed the complaint for failure to state a claim on which relief could be granted, reasoning that there was no debt owing to BFI on the petition date, and that, upon surrender of a preference, Bankruptcy Code section 502(h), which allows a creditor’s claim for property turned over pursuant to Bankruptcy Code section 550, gives rise only to a claim against the bankruptcy estate, and does not reinstate a personal claim against a debtor.

Bankruptcy Code section 502(h) states: “A claim arising from recovery of property under section 522, 550, or 553 of this title shall be determined, and shall be allowed under subsection (a), (b), or (c) of this section, or disallowed under subsection (d) or (e) of this section, the same as if such claim had arisen before the date of the filing of the petition.”

BFI appealed. The BAP affirmed the bankruptcy court’s decision, holding that section 502(h) does not reinstate a debtor’s liability, and that BFI did not articulate any other basis for reinstatement. In affirming, the BAP concluded that section 502(h) authorizes only a claim against the bankruptcy estate upon surrender of a preference, thereby rejecting BFI’s contention that section 502(h) reinstated its allegedly non-dischargeable claim against Laizure once it paid the settlement of the preference claim.

Practical Considerations

A creditor may not want to adjudicate its fraud claim for various reasons, including potential costs involved and the risk of losing. A creditor deciding to settle its fraud claim, however, runs the risk that settlement payments received may be avoidable preferences in a subsequent bankruptcy. As a practical matter, the risk may be worth taking. The creditor receives a cash payout for its fraud claim and avoids expending funds on litigation. The debtor may not file a bankruptcy petition at all, or it may not file a petition within the preference period. Even if the debtor were to file a petition with the preference period, avoiding an alleged preferential transfer would require filing an adversary proceeding and satisfying each element of an avoidable preference. In addition, settlement of an adversary proceeding for less than the value of the alleged preferential transfer may be possible considering, among other things, the cost and uncertainty of litigation. These considerations suggest that a creditor may be well-advised to settle its fraud claim and accept payments in settlement from the debtor notwithstanding the risk of potential preference litigation later.

In an effort to avoid the outcome of Laizure, a creditor might consider agreeing to forebear from pursuing its fraud claim against the debtor until ninety-one days after the last settlement payment is made. If the debtor makes the required settlement payments and the time period expires without the debtor filing bankruptcy, the debtor would receive a release. If the debtor makes the required settlement payments but files bankruptcy before the time period expired, the debtor would not have received the release. As a result, under this approach, if preference litigation ensues, the creditor might be in a better position to argue that it has an allegedly nondischargeable debt owed by the debtor after repayment of any preference. The creditor would want to file a complaint seeking a determination that the debt is excepted from discharge in the bankruptcy court within the prescribed time absent a timely extension.

Federal Rule of Bankruptcy Procedure 4007(c) sets a deadline for filing a complaint objecting to the discharge of certain debts, including those identified in Bankruptcy Code section 523(a)(4), which is 60 days after the first date set for the meeting of creditors under Bankruptcy Code section 341(a). Rule 4007(c) permits the bankruptcy court to extend the deadline for cause upon motion filed within the period and after a hearing on notice. This may be accomplished by the parties stipulating to an extension and seeking an order from the bankruptcy court within the prescribed period.

Whether this approach would permit the creditor to avoid the outcome in Laizure in its own case may be possible but remains to be seen.

— James P. Menton, Jr.

Multidistrict Litigation

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- District where a settlement of one of the related actions is pending. In re Medco Health Solutions, Inc. Pharmacy Benefits Lit., 254 F.Supp. 2d 1364, 1365 (J.P.M.L. 2003).
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**Airline Crash Cases**

In airline crash cases, the Panel has adopted the general rule that the MDL cases will be transferred to the district in which the crash occurred. **In re Helicopter Crash Near Meadowview, Arizona on August 10, 2001, 330 F.Supp. 2d 1365, 1366 (J.P.M.L. 2004); In re Air Crash Near Edgartown, Mass, on October 6, 2000, 269 F.Supp. 2d 1370, 1371 (J.P.M.L. 2003).**

Like many general rules, however, the “situs of the crash” test is not inflexible. **In re Air Crash Disaster at Covington, Kentucky, 579 F.Supp. 1057, 1058 (J.P.M.L. 1984),** the Panel transferred the MDL cases to the district where the aircraft was assembled, inspected and certified by the Federal Aviation Administration. The “situs of the crash” test does not, of course, apply when the crash occurred outside the United States. **In re Air Crash Near Castellon, Spain, 296 F.Supp. 2d 1372, 1373 (J.P.M.L. 2003) (cases transferred to district with majority of pending actions and favorable caseload of judge); In re Korean Airlines Lines Disaster of September 1, 1983, 575 F.Supp. 342, 343 (J.P.M.L. 1984) (District of Columbia selected by reason of proximity of governmental agencies and implication of sensitive areas of national policy, international relations and military intelligence).**

**Tag Along Actions**

Rule 1.1 of the Panel defines a “tag along” action to be “a civil action pending in a district court and involving common questions of fact with actions previously transferred under Section 1407.” A tag along action is transferred to the transferee district by way of a conditional transfer order entered by the Panel pursuant to Rule 7.4(a). A party who opposes the transfer may file a notice of opposition within 15 days after service of the conditional transfer order. **R.J.P.M.L. 7.4(c).** This automatically stays the conditional transfer order. **Knutson v. Allis-Chalmers Corporation, 358 F.Supp. 2d 983, 987 (D. Nev. 2005).** The party opposing transfer must, within the next fifteen days, file a motion to vacate the conditional transfer order and a brief in support thereof. **R.J.M.L. 7.4(d).**

When a conditional transfer order is opposed, there is a 3 to 4 month delay from the time the order is issued, to a subsequent order by the Panel. **In re Prudential Ins. Co. Of America Sales Practices Lit., 170 F.Supp. 2d 1346, 1347 (J.P.M.L. 2001).** During this time, the jurisdiction of the transferee court is unaffected. **State of Wisconsin v. Abbott Laboratories, et al., 390 F.Supp. 2d 815, 819 (W.D. Wis. 2005), citing Illinois Municipal Retirement Fund v. Citigroup, Inc., et al. 391 F. 3d 844, 850-852 (7th Cir. 2005).**

A tag along action may also be transferred by a motion filed with the Panel. In that instance, the moving party has the burden of proof that (1) the potential tag along action has questions of fact common to the actions transferred previously; (2) its transfer would best serve the convenience of the parties and witnesses; and (3) promote the just and efficient conduct of the litigation. **In re Tobacco/Governmental Health Care Costs Lit., 76 F.Supp. 2d 45, 7 (J.P.M.L. 1999).**

**Powers of the Transferee Judge**

**Pretrial Motions**

The MDL statute does not define the term “pretrial proceedings,” but the House Report on the bill which enacted §1407 stated that “by the term ‘pretrial proceedings,’ the committee (House Committee on the Judiciary) has reference to the practice and procedure which precede the trial of an action. These are governed by the Federal Rules of Civil Procedure.” H.R. Rep. No. 1130, 90th Cong.2d Sess., reprinted in 1968 U.S. Code Cong & Adm. News 1898, 1900. This led to a general rule that the transferee judge may exercise any power that the transferor judge could have exercised in the absence of the transfer. **In re U.S. Office Products Co. Securities Lit., 251 F.Supp. 2d 58, 64-65 (D.D.C. 2003).** This includes the power to do the following:

Order the filing of a consolidated complaint. **Katz v. Realty Equities Corp. Of N.Y., 521 F. 2d 1354, 1358-1359 (2d Cir. 1978); Murphy “Unified and Consolidated Complaints in Multidistrict Litigation,” 132 F.R.D. 597 (1991). This is, however only a procedural device to accomplish pretrial procedures. **In re Bridgestone/Firestone, Inc. Tires Products Liability Lit., 256 F.Supp. 2d 884, 888-890 (S.D. Ind. 2003) (filing of consolidated complaint does not make an entity a party to any action in which it has not been named or served). In the Propulsed Products Liability Litigation, 208 F.R.D. 133, 141-142 (E.D. La. 2002), the court held that the filing of a consolidated complaint in the transferee court did not make that court the court of origin for the transferred cases.

Order an amendment of the pleadings. **Senter v. Amtrak, 540 F.Supp. 557, 558 (D.N.J. 1982).**


Grant Motions for summary judgment. **In re TMJ Implants Products Liability Lit., 113 F. 3d 1484, 1488 (8th Cir. 1997).**

Exercise supplemental jurisdiction over state law claims after dismissal of federal claims. **Crispino v. New England Mutual Life Ins. Co., 358 F.3d 16, 19 (1st Cir. 2004).**

Grant a motion for relief under F.R.C.P. 60(b) from a judgment entered by a transferor court. **In re New England Mutual Life Ins. Co. Sales Practices Lit., 204 F.R.D. 6, 12 (D. Nev. 2001).**


The only limitation on the power of the transferee judge to rule on pretrial motions is that the judge cannot grant a motion for a change of venue. This issue has had a long and tortuous path.

A motion for a change of venue pursuant to § 1404(a) is, of course, a classic example of a pretrial motion routinely considered by district judges, but the statute collides with § 1407(a) which states, in pertinent part, that “...Each action so transferred shall be remanded by the Panel at or before the conclusion of such pretrial proceedings to the district from which it was transferred unless it shall have been previously terminated...”

**In Pfizer v. Lord, 447 F.2d 122, 124 (2d Cir. 1974),** the transferee judge, who was from Minnesota, transferred 31 MDL cases from the Southern District of New York to the District of Minnesota pursuant to § 1404(a) at the conclusion of pretrial proceedings so he could try the cases. The Second Circuit denied a petition for a writ of mandamus and held that § 1407(a) only (Continued on page 8)
restricts the power of the Panel to remand cases at the conclusion of pretrial proceedings but does not restrict the transferee judge from granting a motion for a change of venue prior to remand by the Panel. In an opinion written by former Supreme Court Justice Tom Clark, the Second Circuit reasoned that since a transferor court lacks jurisdiction to rule on a § 1404(a) motion after transfer a holding that the transferee court also lacked such authority would require suspension of all § 1404(a) proceedings until the cases could be remanded to the various transferee courts. "The inevitable result would be further extensive delay in litigation which already is among the most time consuming on the federal dockets. We see no reason to sanction such a result." 447 F.2d at 125. Justice Clark’s opinion was followed for the next 27 years. During this time, it became routine for the transferee court to transfer the MDL cases to itself for all purposes, if the requirements of § 1404(a) were satisfied. Instances of remand were infrequent.

In Lexecon, Inc. v. Milberg Weiss Bershad Hynes & Lerach, 525 U.S. 26, 36-37, 118 S. Ct. 956 (1998), however, a unanimous Supreme Court overruled the Pfizer case and held that § 1407(a) does, in effect, require the suspension of all § 1404(a) proceedings while the MDL cases are in the transferee court and precludes the transferee judge from ruling on such motions. See 74 Notre Dame L. Rev. 1337 (1999). The Lexecon holding applies equally to transfers under any venue statute, Shah v. Pan American World Services, 148 F.3d 84, 90-91 (2d Cir. 1998), but does not restrict the transferee judge from ruling on other pretrial motions even though they may dispose of the litigation on the merits. In re African-American Slave Descendants Litigation, 471 F.3d 754, 756-757 (7th Cir. 2006) (motion to dismiss).

It is, however, still possible to obtain a trial in the transferee district with the consent of all parties. In re Carbon Dioxide Industry Antitrust Lit., 229 F.3d 1321, 1327 (11th Cir. 2000) (trial in transferee district upheld on basis of stipulation that venue in transferee district was proper); In re Farmers Insurance Exchange Claims Representative’s Overtime Pay Lit., 336 F.Supp. 2d 1077, 1082 (D. Oregon 2004), rev’d in part on other grounds, 466 F.3d 853 (2006) (trial in transferee district by express stipulation); In re Brand Name Prescription Drugs Antitrust Lit., 264 F.Supp. 2d 1372, 1377 (n. 4) (J.P.M.L. 2003) (Trial in transferee district by waiver of remand) and the transferee judge may “follow” the remanded cases back to their transferor districts pursuant to 28 U.S.C. §202(d) for trial. In re CBS Color Tube Patent Lit., 329 F.Supp. 540, 541 (n. 3) (J.P.M.L. 1971).

Discovery Powers

Stated broadly, the responsibility of the transferee judge is to fashion a pretrial program to prevent duplication of discovery and unnecessary inconvenience to the parties and witnesses. In re U.S. Financial Lit., 64 F.R.D. 76, 78 (S.D. Cal. 1974). The transferee judge may therefore establish a separate discovery schedule for any unique issues concurrently with the conduct of common pretrial matters, In re National Century Financial Enterprises, Inc., 293 F.Supp. 2d 1375, 1377 (J.P.M.L. 2003). In that event, the parties only are required to participate in that discovery related to their actions. Southern Railways v. Templar, 463 F.2d 968, 971 (10th Cir. 1972). Alternatively, the transferee judge may leave discovery on unique issues to the supervision of the transferee judge on remand. In re Train Derailment at Frankewing, Tennessee, 431 F.Supp. 916, 918 (J.P.M.L. 1977).

The transferee judge may enjoin subpoenas issued by other courts. In re Automotive Refinishing Paint Antitrust Lit., 229 F.R.D. 482, 486 (E.D. Pa. 2005); In re Welding Rod Products Liability Lit., 406 F.Supp. 2d 1064, 1066-1067 (N.D. Cal. 2005) (documents only subpoena); and the judge may also hear motions for protective orders by non-parties who reside outside of the transferee district. In re Orthopedic Bone Screw Products Liability Lit., 79 F.3d 46, 48 (7th Cir. 1996).

There is no requirement that all discovery be taken in the transferee district. F.R.C.P. 45(d)(2) permits depositions to be taken where the witness resides and pursuant to §1407(b), the transferee judge may preside over depositions in other districts. In re IBM Peripheral E.D.P. Devices Antitrust Lit., 411 F.Supp. 791, 792 (J.P.M.L. 1976). The physical presence of the judge outside of the transferee district is, however, unnecessary. U.S. ex rel Pogue v. Diabetes Treatment Centers of America, 444 F.3d 462, 468-469 (6th Cir. 2006). In the Corrugated Container Antitrust Lit., 644 F.2d 70, 73-74 (n.6) (2d Cir. 1980) (Appeal of Fleischacker), the transferee judge in Texas conducted a telephonic hearing to hold in contempt a nonparty witness who resided in New York. For that hearing, the transferee judge sat as a judge of the Southern District of New York.

Recently, the Ninth Circuit considered the extent to which those factors relevant to imposition of the sanction of dismissal apply in a multidistrict context. In re Phenylpropanolamine (PPA) Products Liability Lit., 460 F.3d 1217, 1222, 1229, 1252 (9th Cir. 2006). The case involved the appeal of eighteen plaintiffs whose cases were dismissed for failure to comply with case management orders. The case has an interesting procedural twist in that the appeals were argued before two separate panels of the Ninth Circuit but the two panels issued a joint decision. In the beginning of its opinion, the court said:

“...while the rules are the same as for ordinary litigation on an ordinary docket...multidistrict litigation is different because of the large number of cases that must be coordinated, its greater complexity, and the court's statutory charge to promote the just and efficient conduct of the actions. 28 U.S.C. §1407. As a result, the considerations that inform the exercise of discretion in multidistrict litigation may be somewhat different, and may tip the balance somewhat differently, from ordinary litigation on an ordinary docket.”

460 F.3d at 1222.

The court then made an exhaustive review of the procedural history of the litigation and the history of MDL proceedings under §1407. The court ultimately affirmed sixteen of the eighteen dismissals and reversed in the other two. The court concluded:

“...while the factors which guide a court's discretion in ordinary cases on an ordinary docket also inform an MDL court's decision to invoke dismissal as a sanction for failure to comply with its orders, the court's discretion is necessarily informed, and broadened, by the number of actions, their complexity, and its charge in the multidistrict context to promote the just and efficient conduct of the actions that are coordinated or consolidated for pretrial purposes.”

460 F.3d at 1252.

Settlement Powers

The powers of the transferee judge to make rulings in connection with settlements are coextensive with those powers of the transferor judge. The following cases thus have upheld the authority of the transferee judge to do the following:


(Continued on page 9)
Choice of Law

The leading case which discusses the choice of law issues in a multidistrict context is In re Korean Air Lines Disaster of September 1, 1983, 829 F.2d 1171, 1175-1176, 1180 (D.C. Cir. 1987), aff’d on other grounds, 490 U.S. 122 (1989). In an opinion written by Justice Ginsburg (then a circuit judge), the court held that in diversity cases, the law of the transferor court will apply but, in federal question cases, although entitled to “close consideration,” the law of the transferor court is not binding on the transferee court. In that instance, the transferee court is bound only by the Supreme Court and the Court of Appeals for the transferee circuit. The district and circuit courts have generally followed the Korean Airlines case. Desiano v. Warner-Lambert & Co., 467 F.3d 85, 91 (2d Cir. 2007) (in federal question cases, transferee court is bound to apply law of transferee circuit); Toll Bros., Inc. v. Dryvit Systems, Inc., 432 F.3d 564, 568 (n.4) (4th Cir. 2005) (law in diversity cases after transfer is law of transferor court); In re General American Life Ins. Co. Sales Practice Lit., 391 F.3d 907, 911 (8th Cir. 2004) (same); In re Air Disaster at Ramstein Air Base, Germany, 81 F.3d 570, 576 (5th Cir. 1996) (same); Murphy v. Federal Deposit Insurance Corp., 208 F.3d 959, 956-966 (11th Cir. 2000), citing Compos v. Ticketmaster Corp., 140 F.3d 1166, 1171 (8th Cir. 1998) (law in federal question cases after transfer is law of transferee court).

Two exceptions to the foregoing rule exist: (1) on matters of federal contract law, where federal law borrows state statutes of limitations, the law of the transferor court will apply; In re United Mine Workers of America Employee Benefit Plans Lit., 854 F. Supp. 2d 914, 918-919 (D.D.C. 1994) (n.7) citing Eckstein v. Balcor Film Investors, 8 F.3d 1121, 1126-1127 (7th Cir. 1993); (2) in federal question cases, the law of the transferor court also will apply where precedent in the transferee circuit is unique and arguably divergent from the predominant interpretation of federal law. In re Cardizem CD Antitrust Lit., 332 F.3d 896, 912 (n.2) (6th Cir. 2003) (dictum).

Appeals from Orders of the Transferee Judge

Appeals from orders of the transferee judge go to the circuit with jurisdiction over the transferee court, In re Exterior Siding and Aluminum Coil Lit., 538 F.Supp. 45, 48 (D. Minn. 1982), unless the dispute involves a nonparty witness who resides outside of the transferee district. U.S. ex rel Pogue v. Diabetes Treatment Centers of America, 444 F.3d 462, 469 (6th Cir. 2006). In In the Corrugated Container Antitrust Lit., 644 F.3d 70, 73-74 (n.6) (2d Cir. 1980) (Appeal of Fleischacker), the Court of Appeals for the Second Circuit held that it and not the Fifth circuit had jurisdiction to review an order of the District Court for the Southern District of Texas holding in contempt a non-party witness who resided in New York.

In multidistrict cases, some courts are more favorably inclined to certify interlocutory rulings for immediate appeal under 28 U.S.C. §1292(b). In re Food Lion, Inc., 73 F.3d 528, 533 (4th Cir. 1996); In re Microsoft Corp. Antitrust Lit., 741, 743 (D. Md. 2003); In re Air Crash Off Long Island, N.Y. on July 17, 1996, 27 F.Supp. 2d 431, 434 (S.D.N.Y. 1998).
Saying Goodbye to Becky and Hello to Adrienne

The New Year brought change to the LA Chapter of the ABTL, with our long-time Executive Director Rebecca Cien announcing that she would be leaving her position to join her husband Ben along with their two young children, Olivia, 7 and Margret, 5, in their relocation to the suburbs around Dallas, Texas. Becky’s story is a familiar one to so many of us, no doubt — Ben got a job offer “of a lifetime,” and the Cien family would be Texas-bound!

Becky — we will miss you. You headed our administrative functioning as our Executive Director for eleven years — a time period that saw ABTL significantly change, and grow to its state-wide prominence as the premier business trial lawyers bar association. You tried hard and you succeeded. You helped personalize our organization and provided continuity. On behalf of the Executive Board and Board of Governors, I thank you for your hard work, dedication, and your smile. We are so very pleased that you will be assisting us this year in providing event planning services for the 2007 annual seminar.

We are very excited, now, to be introducing you to our new Executive Director, Adrienne King. Adrienne is a native of the San Francisco Bay Area, who graduated from USC in 2000, and then proceeded to make Los Angeles her home. She has worked in corporate sales and marketing for the past seven years and has demonstrated excellence in building and maintaining strong relationships, event planning, and logistics management, first with a major pharmaceutical company and then with an educational/testing company. She is married to Pasadena-based attorney Stephen King, a founder of Rios & King, which presumptively makes her an expert in working with attorneys! She is excited about her new role and eager to contribute to the continued growth and success of the ABTL. Please join us in welcoming Adrienne, who can be reached at abtl@abtl.org.

“I am thrilled about joining the ABTL as Executive Director,” Adrienne told ABTL Report. “I am impressed and amazed at the dedication and thoughtfulness of everyone I have met thus far and look forward to contributing to the continued growth and success of the organization. Thank you for having me and I hope to see you all soon.”

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Michael A. Sherman

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Randall A. Spencer

### Multidistrict Litigation

Continued from page 9

issued to vacate discovery order of transferee court, despite conditional remand order from the Panel.

After remand, the transferee judge loses all jurisdiction to modify or vacate any orders that were entered previously. In re Asbestos Litigation, 963 F.Supp. 247, 251 (S.D.N.Y. 1997); In re Upjohn Co. Antibiotic “Cleocin” Products, 508 F.Supp. 1020, 1021 (E.D. Mich. 1981). Thereafter, the Court of Appeal for the transferee district has jurisdiction over unreviewed rulings of the transferee and transferee court. In re Briscoe, 448 F.2d 201, 213 (3rd Cir. 2006).

In Winkler v. Eli Lilly & Co., 101 F.3d 1196, 1202-1203 (7th Cir. 1996), however, the Court of Appeals for the Seventh Circuit held that after remand, the transferee court had the authority pursuant to the All Writs Act, 28 U.S.C. §1651, to enjoin parties to the previously remanded MDL actions from obtaining discovery which the transferee judge had denied.

“...the mere fact of that remand did not deprive [the transferee judge] of jurisdiction to issue the injunction. It would vitiate much of the purpose of consolidated litigation if, after remand, parties could simply re-visit the transferee court’s pre-trial rulings, and force the common defendant to deal piecemeal with once-collective matters. Accordingly,...we believe that a transferee court’s statutory power to control multidistrict litigation necessarily includes the equitable power, after remand, to interpret the scope and protect the integrity of orders issued while in charge of the consolidated lawsuits.”

101 F.3d at 1202 (n 5).

The impact of the foregoing passage was, however, lessened when the court vacated the injunction after finding that the district court committed an abuse of discretion. 101 F.3d at 1205-06. The foregoing passage from the Winkler case was, however, given an expansive interpretation in the Lineboard Antitrust Litigation, 292 F.Supp. 2d 644, 665 (E.D. Pa. 2003), where the transferee judge, in awarding fees to class counsel, ordered that a portion of any recovery in the transferred cases brought by plaintiffs who elected to opt out of the class action be sequestered on remand, and paid to class counsel for work done for the common benefit. “Thus, the sequestration order will be applied to settlement and judgments in the tag-along actions after remand.” 292 F.Supp. 2d at 665.

Whether a transferor court is bound to comply with an order of the transferee court applicable to remanded cases, or an injunction of the transferee court after remand, depends on whether the transferor court may modify or vacate orders of the transferee court. The authorities on this issue are scarce and not in harmony. Compare In re Food Lion, Inc. Fair Labor Standards Act “Effective Scheduling Lit.”, 73 F.3d 528, 531 (4th Cir. 1996), citing Weigel “The Judicial Panel on Multidistrict Litigation, Transferor Courts and Transferee Courts,” 78 F.R.D. 575, 577 (1977) (rulings of transferee judge cannot be vacated even if the failure to do so might result in reversal of the final judgment in the transferor court”) with Winkler v. Eli Lilly & Co., 101 F.3d at 1202 (n 5).

In re Korean Air Lines Disaster of September 1, 1983, supra, 289 F.2d at 1176, 1180 (interlocutory ruling of transferee court affirmed on appeal should be treated by transferor courts on remand as law of the case).
A Message from the President

This past New Years Day, Chief Justice Roberts ignited a fierce debate, via his annual report on the federal judiciary, over how judicial pay has lagged. The Chief Justice observed how pay for federal judges has seriously lagged behind average workers’ wages, and has been completely eclipsed by the hyper-acceleration of wages for lawyers in private law firms and even law school faculty. He characterized this growing issue as presenting constitutional implications for the maintenance of a robust, independent judiciary.

The fact that federal judges are openly stimulating this debate is itself somewhat curious, and sad. The idea of Chief Justice Roberts having to stir up a veritable media/blogger’s hornet’s nest on the subject of judicial pay, or of Justice Kennedy having to appear “hat in hand” at a recent Senate Judiciary Committee hearing on the subject, is itself reason for all of us to sit up and take notice: Something is wrong in the third branch of government when they are reduced to fighting for a raise.

Justice Roberts’ comments ought to have special relevance to those of us in private law practice, because we are the proverbial “Exhibit ‘A’” to both sides of the debate.

Exhibit “A”

First year associate pay in 1969:
- Schwartz & Alschuler (nka Alschuler Grossman) – $9,500
- Gibson Dunn & Crutcher – $13,500
- Sonnenschein Nath & Rosenthal (Chicago) – $9,500
- LA County DA, Public Def. and County Counsel – $12,000

Pay of Federal Judges in 1969:
- District Court – $40,000
- Court of Appeals – $42,500
- Supreme Court – $60,000 – $62,500

First year associate pay in 2007:
- Many national and regional law firms have announced salaries in the range between $145,000 - $160,000, with the opportunity at some law firms for bonuses on top of those salaries.

Pay of Federal Judges in 2007:
- District Court – $162,200
- Court of Appeals – $175,100
- Supreme Court – $203,000 - $212,100

* * * *

The numbers do tell the whole story, with first year associate salaries now almost equaling the pay of a federal judge. Having now moved Exhibit “A” into evidence, as we are wont to say, I rest my case.

But look at the opposition’s use of their own Exhibit “A,” another argument that focuses on those of us in the private practice of law:

“Yes, many top lawyers earn much more. But judges work less, enjoy many perks, are appointed for life and have much more generous benefits, including full pay for those who retire after age 65 with 15 years of experience on the bench.”


OK, “top lawyers,” which of you is clamoring to become a federal judge? The answer is not too many of us are nowadays. From what I have seen, though, judges are not working less than many of us in the private sector — certainly not appreciably less. And those “benefits” don’t take into account the occasional member of Congress screaming for someone’s impeachment, or of the prospect of the creation of a new judicial “inspector general” that critics claim is ideologically motivated, or of the frightening increase in violence targeted at judges.

The ever-widening pay disparity between the public and private sector diminishes the value of a lifetime appointment. By now, many of us anecdotally know of federal judges who are resigning for lucrative compensation packages either in private ADR, or occasionally at law firms, or in academia. More than anecdotable or personal experience, an increasing number of federal judges are resigning these lifetime positions in large part because of ever widening pay gaps. In Chief Justice Roberts’ 2006 year-end report, he noted that within the last six years, 38 judges left the federal bench, including 17 in the last two years alone. And the ink on that report was barely dry when David Levi, the Chief Judge of the Eastern District of California, announced in early January that he would be resigning the bench to serve as Dean of the Duke University Law School for an undisclosed but publicly rumored salary of between $200,000 to $300,000. In a Wall Street Journal Law Blog posting on the date his resignation was announced, the following was reported, attributed to Judge Levi: “One of the reasons I could afford to do this is that judges are paid poorly compared to law school deans and law professors,”…”Because I am so poorly paid by comparison to comparable groups, I made the judgment that I could afford to do this even though I was losing whatever prospect of a pension there was.”

We “top lawyers” ought to stake out a position in this debate. First and foremost, we ought to take a position because generating interest (much less sympathy) for the plight of someone who takes home $165,200 a year is not easy among minimum wage workers, or two-wage earner households in California earning the median income of approximately $89,000. Clearly those of our colleagues who choose careers in public service generally, and specifically in the judiciary, cannot expect to earn in the public sector nearly what we would earn in the private sector, and do receive some non-salary benefits and rewards that we in the private sector do not typically receive. Just as obviously, do we live in a market-based society where if the pay disparities become too significant — as they now are — then “something’s gotta give.” And in our market-based society, how realistic is it to expect a member of the judiciary to not care that judges are woefully underpaid in comparison to those in private practice or academia? Stated differently, do we want a judiciary made up of individuals who either arrive on the bench independently wealthy, or who lead the type of lifestyle or have the type of values where they do not care that they make many multiples less than what they would make in private practice?

Fewer and fewer lawyers in private practice now choose careers in the judiciary. Those of us who have been practicing law in Los Angeles for twenty years or more have certainly seen this phenomenon among our mentors and now our peers. Indeed, Chief Justice Roberts notes that in the Eisenhower administration, two-thirds of the federal judiciary were drawn from the pri-
private sector, whereas today the private sector only accounts for one-third, and concludes: “Our judiciary will not properly serve its constitutional role if it is restricted to (1) persons so wealthy that they can afford to be indifferent to the level of judicial compensation, or (2) people for whom the judicial salary represents a pay increase.” As a society, is this what we want as the predominant talent pool?

As those of us in private practice know, attracting and retaining key, qualified employees is important in our business, and important to any business. These business principles are not suspended because the paycheck comes from the US Treasury. Our broken system of paying judges a fair salary will not be fixed if we sit on the sidelines. Fortunately, California’s senior Senator, Dianne Feinstein, has taken an active role in supporting legislation for increases in judicial pay. I urge you to contact either her or Speaker Nancy Pelosi, and ask that they provide leadership in this area.

— Michael A. Sherman

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