

# Barth REPORT

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## *Effective Practice Management and Performance Evaluation*

In the past three years, law firms of all sizes have enjoyed record revenues and profits. Yet, there is a startling contradiction at work in the legal market place. In spite of the longest period of American economic expansion on record, in 1999 we have seen a sharp increase in the number of law firm dissolutions. More firms are vulnerable. Why? There is a sea change occurring in the legal industry and it affects firms of all sizes in all markets including the Bay Area.

Changes in the legal market place are partially the result of dramatic changes in the American and global economy. Staid and slowly changing business climates have given way to constant change and volatility. According to experts, this volatility has become a fact of business life. Dramatic fluctuations in the stock market or an economic crisis in one country can have profound and swift ramifications in many countries. These situations require businesses

to be proactive and make adjustments to strategic plans in a reasoned, but timely, manner. These changes have significant impact on the prosperity of law firms.



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## *Ruminations Upon Retirement: Reflections of a Trial Judge*

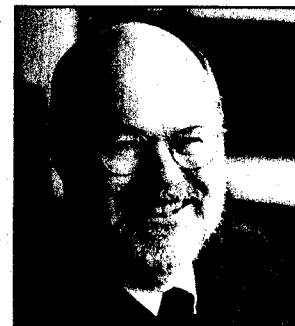
Presiding over a jury trial affords the judge a very different perspective from that of the lawyers engaged in the trial. Lawyers often become so preoccupied with their own view of the evidence and the law that they develop tunnel vision, lose perspective, and suffer lapses in common sense. The judge's perspective from the bench provides a broader view. Having had this view for 20 years, I have reached some conclusions about the conduct of a jury trial which might be of interest to aspiring trial lawyers.

This loss of perspective and common sense among modern litigators may be because they are not "trial lawyers" in the historic sense. Trial lawyers tried jury cases, many of them, back to back, over careers spanning many years. This constant and repeated exposure to juries gave these lawyers insight into the attitudes and reactions of the ordinary citizens who serve on juries — a real sense of the human condition — that helped them maintain perspective and common sense; to see the "forest," as it were.

To a large extent, these trial lawyers have been replaced by a generation of lawyers who describe themselves as "litigators." While this may be the result of many factors, from the proliferation of lawyers to the increased complexity of litigation, these folks are different from the trial lawyers of my youth.

My impression is that this new generation of litigators consists of lawyers who file demurrers, send and answer interrogatories, make document production requests, review document production responses, take numerous depositions, file motions for summary judgment, occasionally settle cases, but rarely, if ever, try a case to a jury. The

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Hon. Michael E. Ballachey (ret.)

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## *Ruminations Upon Retirement*

problem, of course, is that sometimes a case will actually go to trial. And therein lies the rub.

I have been told by one lawyer that many lawyers trying jury trials today enter the courtroom "hoping only to look the part and with little or no perspective on how to influence the outcome." This person believes, and I agree, that every decision made in the course of a lawsuit, to do or not to do something, influences the outcome of the trial. Every move made while on the "stage" — whether to object and when, whether to call or cross-examine a witness, and how to conduct oneself in that process — must be considered in the context of the outcome. To litigate without this perspective, to fail to see the forest for the trees, is to litigate with no view to the consequences other than the record on appeal. If one maintains this view of the forest and uses available tools of advocacy and common sense, the trees will take care of themselves.

A colleague of mine, Judge Richard Hodge, has formulated a basic principle regarding jury trials: "This is not a deposition. This is a trial." Left to his own in designing a courtroom, Hodge would have this principle emblazoned on the bench in neon lights. His purpose would be to focus on the "drama" of the trial. While not as architecturally inspired, I agree that a jury trial should be viewed as a chance to capture the juror's imagination and touch them emotionally. The essence of a trial, after all, is to persuade. It bears emphasizing that a trial is fundamentally different from, and frequently at odds with, most other pretrial procedures. Regrettably, this message is frequently lost on all but real trial lawyers, who do not need the advice.

Pretrial procedures are designed to shape and form the issues to be resolved at trial, while a trial is a dynamic, dramatic process. A trial should not be an endless repetition of favorable facts; rather, it should be an effective presentation of only those facts necessary for success.

To maximize this chance of success, and to guide the conduct of the trial toward that goal, the first task of any lawyer preparing for a jury trial should be to organize the jury instructions and draft the closing argument. For reasons that have never been clear to me, most lawyers defer these tasks to the end of the trial, presumably because instruction and argument come at the end of the trial. Addressing these jobs early on, however, will go a long way toward ensuring that the proof includes only those facts necessary to achieve the result asked for in the argument. Once the argument and instructions have been prepared, it becomes much clearer that no question need be asked, on either direct or cross-examination, which is not necessary for that precise purpose.

Too often pretrial machinations result in total confusion about the actual issues to be resolved at trial. On more than one occasion it has become obvious to me that neither side knew which of the many amended complaints was operative, or which of the numerous affirmative defenses would be asserted at trial. By way of an

extreme example, I recall one case in which, at the time of assignment for trial, counsel and I discovered an unresolved cross-complaint that everyone had forgotten about. Its existence led to a settlement when the defense attorney on the cross-complaint discovered, much to his surprise and chagrin, that he, and more important, his client, were in trial.

Another manifestation of the development of this generation of lawyers who describe themselves as litigators is a frequent and palpable "disconnect" between pretrial proceedings and the conduct of the jury trial. This disconnect can have disastrous consequences. For instance, some litigators, with no apparent tactical forethought, will furiously assert some kind of privilege as to certain witnesses or documents during early discovery proceedings. The price of this lack of forethought, made worse if the attempt is successful, becomes obvious when the litigator, apparently for the first time at trial, discovers that the protected witness or document has become crucial to the case. To the surprise of no one but the litigator who successfully asserted the privilege, and precisely because of the assertion of that privilege, the evidence is disallowed in the trial. The moral: Avoid, if possible, being hoist by your own petard.

Similarly, litigators, usually representing out-of-state defendants, frequently refuse to produce out-of-state witnesses for deposition or trial in California, forcing the plaintiff to travel to the residence of the witness for a videotaped deposition. The questionable wisdom of refusing to produce witnesses "live" can best be summed up in two words: Bill Gates. Two additional words: Bill Clinton.

Witnesses who appear at trial on videotape, especially high-level corporate officials, frequently do not show themselves at their best. The practice also gives the other side an argument it would not otherwise have: that the witness is unwilling, or "too important," to face the jury.

In addition, witnesses appearing on videotape are presented to the jury, either on a television monitor or large screen, as a disembodied head, usually filmed in isolation, facing the camera, with little or no attention to artistic sensibility. Nervous gestures or tics, such as blinking, side-long glances at counsel (who are usually off camera), or fiddling with pens or papers, are all exaggerated by the filmed presentation. Additionally, given the informal atmosphere of most depositions, as contrasted with the formality of the courtroom, filmed witnesses tend to be non-responsive, flippant, combative, argumentative, defensive, and otherwise less effective than when questioned in the presence of a jury.

The impact of watching hours of videotaped depositions must also be measured against the amount of television watched by the average juror. Videotaped depositions must be reminiscent of television news coverage of Oliver North appearing before the Senate and consulting with his lawyer before answering each question. This behavior became a cultural joke, exploited in clever television advertising, and must resonate with many jurors.

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Another problem with the use of videotaped depositions is that the very purpose of a deposition, namely to obtain information, is at odds with the type of examination a trial lawyer should conduct before a jury. At trial, the lawyer should be organized, coherent, and controlled in presenting the witness. Coherence and control are usually impossible at a deposition, especially with a hostile witness. Frequently, deposition examination is disorganized, incoherent, and uncontrolled, not to mention painfully slow: hardly an effective way to present any witness at trial.

Although there may be some tactical advantage to a defendant in forcing the plaintiff to subject the jury to the mind-numbing experience of watching hours of video film of deposition testimony, this tactic puts the defense in a completely passive posture for much of the plaintiff's case. The reluctance of defense counsel to present any portion of the defense case during the plaintiff's case by calling any of these witnesses out of order (a request routinely granted by many trial judges to accommodate a witness's travel problems and expenses) only adds to this appearance of passivity.

It has been said that one measure of intelligence is a person's ability to entertain opposing viewpoints simultaneously. Properly selected jurors can hold opposing viewpoints simultaneously, to the extent that calling witnesses out of order constitutes such an experience. Failure to trust the jury to handle this experience not only results in total passivity on the defense side during much of the plaintiff's case, it also allows the juror's first impressions of the case to harden, even though the court repeatedly instructs them not to decide the case until the completion of all of the evidence. Common sense tells us that this is a difficult task even in brief trials. One should be mindful of research that suggests that few jurors change their view of the case after the opening statements. Imagine the impact of presenting the plaintiff's case, day after day, with zero input from the defense.

Of course, these observations do not apply to use of videotaped depositions to impeach live witnesses in the courtroom. For that purpose, videotaped depositions, and other forms of modern technology, such as CD-ROM, can be very effective. Whether done by videotape or more traditional transcripts, however, the execution of the impeachment is the central consideration.

Impeachment, like cross-examination, is rarely done effectively. Too often, poorly prepared lawyers will spend what seems to be an interminable amount of time fumbling through the deposition transcript, trying to locate the impeaching material. The lawyer will incur even more delay giving the court, counsel, and the witness the page and line designations. The entire effort is often in pursuit of a trivial point of inconsistency. By the time the impeaching question is asked, the jury may have completely lost the point of the entire exercise. To paraphrase Winston Churchill: Never have so many wasted so much time proving so little.

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## Clearing Conflicts: The Basics

Most lawyers today are sensitive to conflicts of interest. But any lawyer who serves as general counsel to his or her firm or who sits on the firm's conflicts or ethics committee knows that the most frequently asked questions from the firm's attorneys center on exactly how to clear the conflict and allow the representation to proceed.

A host of conflicts and potential conflicts are identified in the California Rules of Professional Conduct ("RPC"). The majority of these are described at Rules 3-300, 3-310, and 3-320. This article provides some direction in how to deal with these important issues.

### Addressing the Conflict

There are two different methods for clearing conflicts — disclosure and consent. Both, according to RPC 3-310(A)(3), must be in writing.

A disclosure is a writing putting the client on notice of the relevant circumstances and of the actual and reasonably foreseeable adverse consequences of those circumstances (RPC 3-310(A)(1)). The client does not need to sign a written disclosure.

The first aspect of a proper disclosure to a client is to set forth as clearly as possible the nature of the conflict. If it is an actual conflict, it should be explicitly described. If the conflict is potential rather than actual, the lawyer should attempt to describe any circumstances that might arise which could result in an actual conflict. This is not the time for "lawyer-ese" or obfuscation. The risk of losing the engagement by a full and frank disclosure should be offset in a practitioner's analysis by the prospect of the unhappy consequences of securing the engagement and later losing it through a disqualification motion, facing potential disciplinary action or, more likely, a claim of malpractice or breach of fiduciary duty for failing to adequately disclose.

The second element of a disclosure is a discussion of the "actual and reasonably foreseeable adverse consequences to the client or former client." In other words, now that the client or former client has been informed of the conflict, why should he or she care? This aspect of the disclosure is intended to give the client sufficient information to not only understand the conflict but to intelligently evaluate the effects of that information. Although a lawyer is not obligated to explain every conceivable consequence of a conflict (*Zador Corp. NV v. Kwan*, 31 Cal. App. 4th 1285, 1301 (1995)), it is in his or her best interests to do so to avoid problems as the representation pro-



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ceeds. The more comprehensive the disclosure and the description of the conflict and its significance, the better — for both the lawyer and the client or clients.

A waiver is the client's "informed written consent" (RPC 3-310(A)(2)). As one would surmise, the client must acknowledge the disclosure of the conflict and consent by his or her signature to the representation in light of that disclosure.

#### Types of Conflicts

In general, conflicts arise from three situations: (1) concurrent representation of two or more clients; (2) successive representation of clients; and (3) a lawyer's own personal or financial relationship.

"Informed written consent" is required in the following situations:

- Representation of more than one client in a single matter in which the clients have a potential conflict (RPC 3-310(C)(1)). For example, the owner of a business and his sales manager are sued for misrepresentation. They wish to have the same lawyer represent them. They tell the lawyer that are in complete agreement as to how they wish the litigation to be handled. Representation of more than one client in a single matter will usually create at least a potential conflict. The disclosure of the potential conflict in this example of concurrent representation should address, at a minimum, what would happen if a dispute arises between the two clients during the representation; if the attorney is given conflicting instructions; if the two clients have different positions as to settlement; if one of the defendants may have a claim against the other; or if, at the conclusion of the engagement, they both demand return of the file.

- Concurrent representation of two or more clients in a single matter in which the interests of the clients actually conflict (RPC 3-310(C)(2)). Suppose that the attorney representing the two defendants in the example above realizes during the initial consultation that the sales manager is an employee who claims indemnity from the owner of the business or that the owner claims that the sales manager exceeded the scope of his employment. The attorney would need to explain in writing not only the nature of the actual conflict but the reasonably foreseeable adverse consequences of having a single lawyer representing both clients whose interests conflict. The written consent of both clients would permit the representation to proceed.

- Representation of client A in one matter in which B is an adverse party and then taking on B as a client in an unrelated matter (RPC 3-310(C)(3)). Imagine a situation in which an attorney is defending a corporate developer in a construction defect case and has filed a cross-complaint against a roofing subcontractor. The attorney could not then agree to represent the roofing subcontractor in a mechanics lien claim unrelated to the construction defect case without the informed written consent of the developer and of the subcontractor.

- Representation of more than one client and entering

into an aggregate settlement of the clients' claims or settlement of aggregate claims against the clients (RPC 3-310(D)). A somewhat common example is presented by the case of an attorney who represents a group of homeowners with claims against a developer. Each homeowner claims specific defects. If the attorney settles the entire case for a single unallocated lump sum, he or she would need each of the clients' informed written consent.

- Representing client A against B in one matter and formerly or currently representing B in a separate matter in a case where, as a result of the representation of B, the lawyer has obtained confidential information from B which is material to the employment of the lawyer by A (RPC 3-310(E)). Here, the determination of the existence of a conflict usually focuses on whether or not confidential information has been communicated. California courts interpret this rule to mean that, lacking informed written consent, an attorney may not take on a matter adverse to a former client that is "substantially related" to work done for the former client. *HF Ahmanson & Co. v. Salomon Bros.*, 229 Cal.App. 3d 1445 (1991).

- Entering into a business transaction with a client or taking a pecuniary or security interest adverse to the client (RPC 3-300. Please note that this scenario requires not only a waiver, but also written notice that the client may seek independent counsel.) In *Hawk v. State Bar*, 45 Cal. 3d 589, 599 (1988), an attorney took a promissory note from his clients secured by a deed of trust to insure payment of his fees. When the clients could not pay, he assigned the note to a third party who foreclosed. This example was clearly a violation of ethical restrictions on counsel, which led to the suspension of the attorney's license and a finding that he had committed acts of moral turpitude.

Disclosures, without written consent, are required in the following instances:

- When the attorney has a "legal, business, financial, professional, or personal relationship" with either a party or a witness to the matter in which he or she is being retained (RPC 3-310(B)(1)). An example would be where a plaintiff retains a law firm to sue a corporation for breach of lease. One of the firm's members sits on a bank's board of directors and the bank owns and controls 100% of the defendant corporation's stock. Assuming that the lawyer representing the plaintiff knows of his firm's connection to the corporation through the bank, if no disclosure is made to the plaintiff, there is a violation of RPC 3-310(B)(1).

- When the attorney knows or should know that he or she had a prior legal, business, financial, professional, or personal relationship with a party or witness and that prior relationship would affect the attorney's representation in the matter in which he or she is being retained (RPC 3-310(B)(2)). Suppose an attorney representing a party to litigation learns that the opposing side's designated expert is someone the attorney has previously retained on several earlier unrelated cases to serve as an expert or consultant. If undisclosed, a disgruntled client who is later informed of this past relationship could sus-

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pect that any real or imagined lack of vigorous cross-examination or a perceived reduction in zealous advocacy by his lawyer might have been instigated by that prior business and professional relationship.

- If the attorney has either a past or present relationship with someone or something that would be "affected substantially" by the outcome of the matter (RPC 3-310(B)(3)). An attorney "agreed to form a new law firm with her opposing counsel, while they continued simultaneously to represent adverse parties in a highly contentious dissolution action." *Stanley v. Richmond*, 35 Cal. App. 4th 1070, 1089 (1995). This scenario resulted in legal problems for the attorney as a result of her lack of disclosure.

- When the attorney has a past or present "legal, business, financial or professional interest in the subject matter" of the engagement (RPC 3-310(B)(4)). Imagine that a lawyer agrees to defend a client in commercial litigation brought against the client by a bank which claims that the client committed fraud in a loan application. Should the lawyer neglect to disclose to the client that he owns substantial stock in the bank, the lawyer would have an undisclosed and unresolved conflict of interest.

- Where the attorney is related to or in "an intimate personal relationship" with another attorney involved in the same matter. The relatives described in the Rule at issue include spouses, parents, children, or siblings of the lawyer, but only of the lawyer who is counsel of record, and not relatives of other members of the same law firm. (RPC 3-320). This is a narrowly drafted rule which is rarely triggered.

### Conclusion

Recognizing the conflict of interest to be cleared is the major hurdle. Clearing it requires careful consideration and diligent application of the guidelines set forth in the Rules of Professional Conduct.

*Michele K. Trausch counsels lawyers and law firms and defends them in legal malpractice actions. She practices with Rogers, Joseph, O'Donnell & Quinn in San Francisco and can be reached at MTrausch@rjoq.com.*



### *COMING EVENTS*

December 7, 1999

MCLE Dinner

#### *Using Videotaped Evidence at Trial: A Practical Approach*

Moderator: John J. Bartko

#### Panel Members:

Hon. Charles A. Legge, Cristina C. Arguedas, James Brosnahan,  
Thomas J. Hannan, Jon B. Streeter

Sheraton Palace Hotel, San Francisco  
Cocktails at 6:00 p.m. • Dinner at 7:00 p.m.

For further information, please call  
(415) 773-4227

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### *Effective Practice Management*

**A**nother critical reason for the increase in the number of law firm failures, and the likelihood for more, is complacency. Firms are internally focused rather than being market driven and client focused.

### Economics

Global mergers, acquisitions and consolidations are commonplace in almost all industries and have been for several years. This trend has resulted in less legal work for most firms. The real estate industry is just one example of this consolidation trend. Large national or international real estate developers move into markets that for generations have been dominated by local developers. International conglomerates headquartered in Frankfurt or London may own the acquiring companies. When this occurs, local law firms frequently lose work that they were doing for developers based in their communities. They may not lose all the work, but what work is left may be commodity work that most probably will not result in additional work from a client headquartered out of state. Commodity work will result in lower fees and in some cases less profit.

Insurance and banking are two more industries that have experienced consolidation. The larger consolidated companies have demanded, and received, enormous changes in the delivery and pricing, of legal services. Demands for volume pricing fixed fees and other alternative billing practices have resulted in lower profits per partner, unhappy attorneys and instability in firms that historically generated impressive profits from these practices.

Other examples of consolidating industries include telecommunications and energy. ATT competes with US West to provide local telephone service. Quest, a long distance carrier that seems to reinvent itself every two years, has acquired US West. What does this mean for firms that have telecommunications practices specializing in regulatory, merger & acquisitions and litigation work? It probably means less work. Energy has been deregulated and firms are battling for the merger and acquisitions and regulatory work that is the result of the deregulation. In the near future this means more work at higher rates. As the industry matures, it means pricing pressure and less work.

**U**ltimately, these massive consolidations in specific industries will result in more legal work but for fewer law firms. In many industries, in-house legal departments have increased in size but, according to Corporate Times, the budgets for in-house legal departments, as a whole, are shrinking. Because of the increased debt from these acquisitions, the general counsels and other corporate officers of these corporations are pressured to reduce legal costs. They will rely on fewer law firms that understand the goals and objectives of general counsel and help the company contain costs. These companies will also look to other providers of legal services, such as consulting and accounting firms.

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### *Effective Practice Management*

Firms, just like their clients, are getting bigger. In addition to rapid growth fueled by large recruiting classes, some firms are growing via mergers. Most firms are looking at merger and acquisition opportunities because there is real concern that larger clients will demand larger firms that provide "one stop shopping" and offer it in national and global locations.

This rush to get bigger and bigger for firms and clients alike will alter the market for legal services at all sizes of firms. It means that more and more mid-size and large law firms will compete for the same clients and business. As a tier of mega firms with offices in London, Asia, Europe and the United States emerge, some large national and regional firms will reshape their marketing plans as they are shut out of higher profile corporate work. Their plans will focus on smaller corporations or regional companies rather than Fortune 500 ones.

In addition to competition from other law firms, accounting and consulting firms are successfully competing with law firms. Too many lawyers erroneously assume that this threat is remote and far off. It isn't. Accounting firms with prominent consulting arms are the largest employers of non-tax attorneys in Europe. These firms are better capitalized and more externally focused than law firms. They are developing and implementing strategic plans that will make significant in-roads into the legal market in the United States. In the past year, accounting firms have lured away senior tax partners from prominent law firms, but their strategic plans are not limited to tax practices. Their goals are to offer "one stop shopping" or solutions to most business issues including corporate finance, intellectual property and technology, tax, labor and employment, environmental, alternative dispute resolution, regulatory and all the legal issues that are common to corporate clients.

#### Strategic Planning and Change

Too many leaders of law firms are complacent and internally focused. Just like the late 80s and early 90s, profitability has covered a multitude of sins. In recent years, many firms have had the luxury of ignoring problems that require tough decisions or addressing valid complaints from partners. Firms fail because they are unwilling to make tough decisions and hold people accountable. For instance, rather than making tough decisions regarding admission to the partnership, many firms admit lawyers that should not be partners. These decisions frequently haunt firms in later years. Failures happen over a period of years, not overnight. Isolated events such as a defection of one or several key partners are normally the result of years of inaction by a firm's leadership.

The very nature of the ownership structure in law firms — partners being equals in most matters (except compensation) and committee based participation in firm governance leads to preoccupation with internal matters. This preoccupation blocks effective leadership.

Firms traditionally have given most partners strong

voices in internal matters that can, and often do, divert attention from the more important and vital issues. Partners must trust and delegate the business side of running the firm to a small group of partners that have the vision and leadership necessary to take the firm into the next decade.

Firms must focus on strategic planning and the delivery of legal services. In order to accomplish this, the firm must have a vision, a strategic plan and a culture that puts the firm first. There are at least two criteria that are essential to building this culture: 1) true or effective practice management; and 2) performance management systems for partners and associates. Partners must be held accountable by implementing performance management systems. Performance management systems are evaluation systems that identify the criteria necessary for success at the partner level. If partners fail to meet these criteria (after being given a reasonable time to achieve them), there must be consequences, including decreases in compensation or dismissal from the partnership. It is no longer possible for law firms to carry owners who do not contribute. Performance management systems must be designed so that everyone is provided the opportunity and resources to succeed. If success is not forthcoming, then changes must be made.

Firms that have implemented true practice management have a tremendous advantage over their competitors. The genius of practice management is that all partners must contribute. It creates accountability to clients, peers and the firm.

What are the building blocks of effective practice management?

- Professional development plans
- Practice group marketing plans
- Key client relationship plans
- Client satisfaction surveys or interviews
- Associate mentoring and development programs
- Research and development of new services and products
- Profitability analysis by client and matter
- Integration into the firm's strategic plan
- Cross selling of firm's other practice groups

The processes of practice management address issues crucial to business planning: quality assurance, client follow-up, market analysis and research, ownership transition planning, retention of key employees (associates), marketing, financial planning and analysis, planning the next line of services or products and publishing expectations that everyone must take significant contributions year in and year out. Effective performance evaluation or management systems are measuring tools for the partnership as they gauge how the firm's partners are progressing towards key goals such as quality assurance, client follow-up and retention of key associates.

The list is long and requires strong commitment from the firm. Implementing the program will require several years and should be planned and carried out carefully.

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CHARLES R. RICE

## On SECURITIES

The Ninth Circuit's decision in *Silicon Graphics* may have finally put some teeth in the Private Securities Litigation Reform Act (the "Reform Act"). Although other Circuits have articulated somewhat different versions of the new pleading standard, the emerging consensus should change what and how securities fraud cases are brought.

### The Reform Act

The Reform Act requires a securities fraud complaint to "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." Unfortunately, neither the statute nor its legislative history are clear about exactly what this means. Part of the new standard came from Second Circuit cases that required plaintiffs to establish a "strong inference of fraudulent intent" by alleging either (1) "facts constituting circumstantial evidence of either reckless or conscious behavior" or (2) "facts establishing a motive to commit fraud and an opportunity to do so." See *In re Time Warner Inc. Securities Litigation*, 9 F.3d 259, 268-69 (2nd Cir. 1993). The Conference Report, however, stated that Congress did "not intend to codify the Second Circuit's case law" and "chose not to include in the pleading standard language relating to motive, opportunity or recklessness."

The Reform Act's reference to the "required state of mind" also invites judicial interpretation. 10(b)-5 liability has always required scienter — the "intent to deceive, manipulate or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 (1976). But the Supreme Court has left open "whether, in some circumstances, reckless behavior is sufficient." *Id.* at 194 n. 12. Lower federal courts have imposed liability for "recklessness" that constitutes "an extreme departure from the standards of ordinary care" and "presents a danger of misleading buyers or sellers that is either known...or so obvious that the actor must have been aware of it." See, e.g., *Hollinger v. Titan Capital Corp.*, 914 F.2d 1564, 1569 (9th Cir. 1990).

### The Ninth Circuit Court Decision

Judge Fern Smith had dismissed the complaint for failing to meet the new pleading standards. *In re Silicon Graphics, Inc.*, 970 F.Supp. 746 (N.D. Cal. 1997). The Ninth Circuit has now affirmed, in a 2-1 decision written by Judge Sneed, holding that plaintiffs must "plead, in great detail, facts that constitute strong circumstantial evidence of deliberately reckless or conscious misconduct." *Id.*, 183 F.3d 970 (9th Cir. 1999).

Relying on *Hochfelder* and *Hollinger*, the Ninth Circuit concluded that "recklessness" constitutes scienter only "to the extent that it reflects some degree of intentional or conscious misconduct." *Id.* at 977. Relying primarily on the Conference Report, the Court also concluded that plaintiffs cannot allege intent "in general terms of mere 'motive and opportunity.'" *Id.* at 979.

Plaintiffs' allegations of negative internal reports that contradicted the defendants' public statements did not raise the required "strong inference," because they lacked "adequate corroborating details." The Reform Act requirement that plaintiffs "state with particularity all facts" supporting such allegations was interpreted to mean that plaintiffs must allege the author, recipients and sources of such reports. *Id.* at 985.

The Ninth Circuit also found that the alleged insider trading (\$13.8 million in proceeds over fifteen weeks) was not sufficiently "unusual" or "suspicious." Viewed in the context of the defendants' total holdings, including vested options, and their prior trading practices, these stock sales were not "suspicious enough to create a strong inference of the required deliberate recklessness." *Id.* at 987.

The Ninth Circuit's decision is the strongest formulation yet of the new pleading requirements. The Second and Third Circuits have recently chosen to apply the Second Circuit test of "motive and opportunity" or "recklessness." See *Stevelman v. Alias Research, Inc.*, 174 F.3d 79 (2nd Cir. 1999); *In re Advanta Corp.*, 180 F.3d 525 (3rd Cir. 1999). The Sixth and Eleventh Circuits have tried to split the difference, concluding that allegations giving rise to "a strong inference of recklessness" are sufficient, but merely pleading "motive and opportunity" is not. *In re Comshare, Inc.*, 1999 WL 460917 (6th Cir. 1999); *Bryant v. Avado Brands, Inc.*, 1999 WL 688050 (11th Cir. 1999) (requiring "severe" recklessness).

Although the formulations differ, the results appear to be converging. Both the Sixth and Third Circuits affirmed dismissals of complaints for failing to meet the Reform Act standard, however articulated. In particular, these courts, like the Ninth Circuit, made realistic evaluations of alleged "insider trading" based on all the facts, including vested options and prior trading patterns.

Other appellate courts should also adopt the Ninth Circuit's holding that plaintiffs have to allege "corroborating details" about "negative internal reports." Forcing plaintiffs' counsel to do their investigative work before filing their complaints was one of the main goals of the Reform Act.

Charles R. Rice is a partner with Shartsis, Friese & Ginsburg and the editor of the ABTL Report for Northern California.



Charles R. Rice





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## *Effective Practice Management*

Lawyers, by their training and education, are risk averse. This process can be very threatening to partners that pride themselves on their independence. Accordingly, it is critical that the firm have a coalition of leaders that are committed to change, set the examples and see the process through.

### Resource Allocation

Law firms distribute almost all of their net income on an annual basis. In fact, some firms use borrowing capacity to make partners draws. It would be unusual to discover other industries that do the same. Most companies in other industries retain earnings to protect and expand the companies' position in the market place. Because law firms distribute earnings yearly, this puts more pressure on firms to consistently beat the previous year's profits per partner. This practice, combined with alarming increases in expenses for associate and staff compensation, occupancy, technology and marketing expenses, exacerbates the situation, making it difficult to repeatedly exceed the previous year's profits per partner. Increased mobility of partners lured by more money at bigger firms adds to the pressure. Because of this increased pressure on firms to be as profitable as possible, firms are more vulnerable. It has been said that many firms are only 3 to 5 key partner defections away from dissolution.

**I**n terms of resource allocation, implementing an effective performance management system will help the compensation committee allocate compensation to partners on a fair basis that must apply equally to all partners. Partners must submit individual professional development plans that are supportive of the practice groups that they belong to. These practice group plans must then support the firm's strategic plan.

The requirements for a successful firm are varied and the personal professional development plans should take advantage of the different strengths that individual partners have. Some partners will be good mentors and developers of associates. Some partners may have better business skills and provide the sophisticated analysis necessary to maintain profitable clients and matters. Hopefully, practice groups will include partners that spend time developing new services or, in a traditional sense, perform research and development so that the firm can move swiftly and take advantage of new niches that will benefit clients.

These professional development plans should be required of associates as well. Development, mentoring and retention of associates should be top priority in practice groups and at all firms. The costs of losing young lawyers are well documented in the legal press. It varies according to firm and region, but when a mid-sized or large firm in Northern California loses a fourth year attorney, the cost, according to the Association of Law Firm Placement, is high — perhaps as much as \$200,000.

These are challenging times for law firms. Challenges

come from within the industry as well as externally. Many are new and reflect the changing nature of the new global economy and shift in the American economy from a manufacturing base to a service economy. Also, the increasing importance that technology and intellectual property play mean that the client bases of many firms are changing.

**M**any of the challenges are inherent to the professional services industry and more specifically to law firms. The successful business model of democratically run firms with full partner participation that was so successful for many years will not succeed in the future. Partners must be willing to give up their autonomy and dedicate themselves to their firms. By implementing strong practice management and effective performance evaluation systems, law firms are taking their best asset — the intellectual capital of their members — and employing it where it is most wisely used, at the client level. Not only where it is most effective, but where the partners at the firm are most satisfied — practicing law and working with clients, rather than dwelling on internal business matters.

*Gerry Holt is a consultant with Hildebrandt International in San Francisco.*



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## *Ruminations Upon Retirement*

Properly done, of course, especially with videotape of the actual impeaching material, impeachment can be devastating. Again, the focus should be on preparation, execution, and judgment. Deciding when to impeach and when not to impeach is a difficult judgment. In my experience, the decision to attempt impeachment is made too often rather than too seldom.

**A** particular pet peeve of mine is the failure of lawyers to use the grammatical form of the question during trials. The law contemplates that the examination of witnesses will be conducted in a question and answer format. We know that there are leading questions, compound questions, vague questions, argumentative questions, and questions which assume facts not in evidence, among others. The common theme is that they are all questions. A current vogue of communication in our culture at large is to ask "non-questions," a form of verbal exchange sometimes referred to as "Valley Speak," in which a statement of fact is asserted with the apparent expectation of a response: "You went to L.A." This is different from asking the witness: "Did you go to L.A.?" This style of verbal interaction has permeated the courtroom and is simply not proper legal form. Using voice inflection to create a question from a simple declarative sentence does not meet the requirements of the law. Lawyers

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RACHEL KREVANS

## On PATENTS

A group of telephone company marketing executives are sitting in a conference room talking about this year's Christmas advertising campaign. One of them suggests that they offer a special deal to long-distance customers on any call made to a person who subscribes to the same service. It's better than the old "Friends and Family" program, because the caller won't have to put the call recipient on a list to get the discount. The rest of them love the idea, and they call the head of billing operations. "Can we track this and bill accordingly?" Five minutes later he calls them back. "No problem. The engineers say we already have the capability, and so does everyone else, so it won't matter whose lines the call goes over. We just haven't ever bothered to do it."

A new ad campaign is born. But that's not the only thing created at the meeting: according to the Federal Circuit Court of Appeals, those marketing executives may have just invented a patentable method for "providing differential billing treatment for subscribers, depending upon whether a subscriber calls someone with the same or a different long-distance carrier." *AT&T Corp. v. Excel Communications, Inc.*, 172 F.2d 1352 (Fed. Cir. 1999). The *AT&T* decision, which issued in April, was the logical extension of the Federal Circuit's 1998 decision in *State Street Bank & Trust Co. v. Signature Financial Group*, 149 F.3d 1368 (Fed. Cir. 1998). Both decisions hold that a method of doing business is patentable under 35 U.S.C. § 101 so long as it meets other statutory requirements for patentability. In *State Street*, it was the combination of several mutual funds into one pool for investment and administrative purposes while separately accounting for each fund.

These two decisions pose interesting challenges to intellectual property practitioners, because they attempt to define the dividing line between abstract ideas (unpatentable under section 101) and a patentable idea which is a "new and useful process, machine, manufacture, or composition of matter." Before *State Street*, a series of sometimes confusing precedents from the Supreme Court and the Federal Circuit had left many with the impression that a "business method" like the discount idea described in *AT&T* was unpatentable subject matter because it was "abstract" or a "disembodied concept." Now the Federal Circuit has indicated twice and in no uncertain terms that that is not the case.

Businesses must start thinking in very different ways about how to identify and protect their "business methods." Perhaps a company has no intention of suing other companies who use its for running its business. It may still

need to patent its idea so that a competitor cannot do so and exclude the originator. Moreover, the scope of potentially patentable "business methods" goes far beyond industries that normally think of themselves as owning or developing intellectual property. Companies which do not perceive themselves as being in the "intellectual property" business will not have in-house or outside patent counsel. They will not be familiar with the framework of intellectual property law, let alone the concept of identifying novel ideas and taking steps to protect them.

Even companies that regard intellectual property as part of their business are not accustomed to thinking of marketing or administrative ideas as patentable, and generally do not have mechanisms in place to identify those ideas promptly and to select those worthy of patent protection. Most companies engaged in technical research and development have a system requiring R & D personnel to report potentially useful ideas. But I doubt if many such companies also systematically collect potentially patentable ideas from the marketing group, or financial managers, or executives in charge of warehousing and distribution.

For patent prosecutors and litigators, "business method" patents pose new problems as well. The Federal Circuit was quite careful to emphasize, in both *State Street* and *AT&T*, that these decisions hold only that a claim was not unpatentable subject matter simply because it was directed to a method of doing business. Such claims must still be tested to determine whether the ideas are truly new, and whether the scope of the claims is adequately supported by the description of the invention provided in the application.

Resolving these questions will require patent prosecutors and litigators to think about intellectual property in new ways. The databases typically used to identify "prior art" in a field will not tell us whether a marketing idea is new. Where does one go to research such a proposition? What evidence will courts find compelling on such points? These topics may never have been discussed in any journal, let alone the sort of scholarly journal on which courts, counsel, and the patent office are accustomed to rely. Moreover, it will be years before we know how the Federal Circuit will define the "field" of such inventions. Would a marketing plan tied to discounts in one industry render an analogous marketing plan in another completely unrelated industry obvious? Business methods patents are a new frontier for intellectual property practitioners, and creativity will be a requirement for success.

Ms. Krevans is a partner in the firm of Morrison & Foerster.



Rachel Krevans



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### *Ruminations Upbn Retirement*

should ask questions in court. And on cross-examination, of course, a lawyer should never ask a question without knowing the answer, unless the lawyer, for well-considered strategic reasons, is unconcerned about the answer.

**H**aving observed hundreds, if not thousands, of cross-examinations, I never cease to be amazed at how few lawyers take advantage of the most powerful tool in their repertoire: the leading question. An inexplicable dichotomy occurs repeatedly during the examination of witnesses in which the lawyer, apparently unable to ask anything but leading questions on direct examination, fails to ask any leading questions on cross-examination. And all too often, the non-leading questions used on cross-examination are designed, unwisely, to simply regurgitate the direct examination, as if to make sure that the jury did not miss anything the first time around. The failure to use leading questions on cross-examination, when coupled with reiterating the direct examination, demonstrates a lack of planning, strategic thinking, and common sense.

Another common mistake is the practice of many litigators to cross-examine expert witnesses on the substance of the witness's expertise. While there are obvious exceptions, it is rarely productive to make a frontal challenge to an experienced professional expert witness. I have never seen an expert witness collapse on cross-examination and I have heard of an expert witness changing his or her opinion only anecdotally. It seems far wiser to limit expert witness cross-examination to issues of bias, compensation, and the lack of recent actual work experience in the expert's field. It is frequently the case that expert witnesses are just that: full time witnesses. And they are vulnerable on that score.

In a typical case, the litigator is at a significant information disadvantage because there is simply no way for the lawyer to learn as much medicine, engineering, or other technical information as the expert witness. In spite of this, far too many lawyers attempt to cross-examine expert witnesses on the substance of the witness's expertise, sometimes for no apparent reason other than to impress the jury. It almost never works. The result of protracted cross-examination of an expert witness, usually, is to give the witness a second (or third) opportunity to restate damaging opinions already given on direct examination.

**T**he most obvious exception to limiting cross-examination of opposing experts occurs, ironically, in precisely the type of litigation to which many modern litigators will most likely be exposed: highly complex and technical commercial litigation such as antitrust litigation, various forms of unlawful competition claims, and intellectual property litigation. In these cases, although cross-examination of opposition experts may be necessary, control and caution should be the order of the day. Preparation is obviously critical to this endeavor. It is mandatory that the lawyer master as much knowledge as the expert and use it judiciously. Cross-examination in this type of litigation

should be viewed as a "commando raid — in and out," using leading questions to maximize control of the witness. The focus should be on eliciting agreement with one's own expert witnesses and exposing the opposition expert's failure to explore or consider information that one's own expert will testify is crucial to proper analysis.

Another strategy that often backfires is the failure to retain and call an expert to oppose the other side's expert witnesses, thereby relying solely on the cross-examination strategy. The result, if the cross-examination is predictably unsuccessful, is to leave the jury with no contravening evidence to consider. The clearest analogy is to an alibi defense in a criminal case. If the alibi is rejected, a guilty verdict is assured. The jury has no choice.

Another practice that is of concern is the habit of many lawyers, after covering the qualifications of an expert witness on direct examination, to ask the court to "accept" or "certify" the witness as an expert. While judges differ on this issue, it seems to me that the test of the law is whether the court should allow the witness to express opinions, not to place its imprimatur on the witness. The proper procedure is to ask whether opposing counsel has any *voir dire* on the witness's qualifications before proceeding to the substance of the testimony. Moreover, the modern practice is to address questions about expert qualifications with a pretrial motion in limine.

**A**s basic as it may seem, it is prudent to carefully examine all exhibits to make sure that all extraneous or prejudicial information has been removed. I have heard of a products liability case in which a fan blade in an automobile had allegedly failed as the result of metallurgical stress, severely injuring the plaintiff. Copies of engineering drawings were presented at trial by the defendant and were offered into evidence. The plaintiff's counsel had the original drawings and they were received in evidence without careful inspection by the defense. The originals contained a notation, not present on the defendant's copy: "Caution: At certain vibration frequencies, metallurgical stress can occur." Because metallurgical stress was claimed to be the cause of the injuries, one can see the problem caused by this inattention to detail. Since no witness was asked any questions about the notation, the first discussion of it occurred in final argument with no possibility of evidentiary rebuttal.

To conclude, we need to consider some basics of common sense. Jurors do not approve of rude conduct between lawyers. Nor do judges, I might add. Perhaps because of the permeation of our culture by television and the constant drum beat of anti-lawyer and anti-judge propaganda from politicians, jurors come to court with definite, and frequently very negative, views about lawyers and judges and a high level of cynicism about the process. Sharp practices, cheap shots, and other "tricks of the trade" only serve to remind jurors of those biases. A sure fire way to get a jury to sympathize with an opposing lawyer is to engage in *ad hominem* attacks. Rude conduct toward the judge is even more counterproductive. Remember, the jury looks to the judge, notwithstanding

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**BARRY P. GOODE**

## On ENVIRONMENTAL LAW

*Plus ça change, plus c'est la même chose.*

Were there environmental lawyers in California in the nineteenth century? Sure. What did they do? A lot.

Environmental issues attended California's birth. At Statehood the foothills were filled with miners diverting water and working claims. So there were disputes. But there was not much law.

### Mining Claims and Water Rights

Although divided by their native tongues, the miners managed to establish rules by which mining claims and water rights could be secured. The cardinal principle was "first in time, first in right."

The new legislature chose to tread lightly. The 1851 California Practice Act simply gave legal effect to the "customs, usages, or regulations established and in force at the bar or diggings." So it fell to lawyers and judges to express, organize and systematize the miners' customs and rules.

The firm of Rowe and Dunn had the distinction of arguing (and losing) the first environmental case heard by the California Supreme Court. (Opposing counsel are listed only as "\_\_\_\_"; a loss to history.) *Eddy v. Simpson*, 3 Cal. 249 (1853) held water rights to be usufructuary only, and noted "the foundation of the plaintiff's right (to the use of water in his mining ditch) was his 'first possession.'"

Only two years later, Mr. Dunn appeared again, in the second environmental law case to come before the Supreme Court: *Irwin v. Phillips*, 5 Cal. 140 (1855). (Again, he lost.) Saying "[c]ourts are bound to take notice of the political and social condition of the country which they judicially rule," the Court recognized the miners' practices and affirmed the appropriative rights doctrine.

With few statutes to guide them, the early lawyers and judges reasoned from miners' rules, first principles and the developing common law. Ever since, our California Reports have been filled with water law cases determined by common law principles; although in recent decades by the Constitution and Water Code too.

As the State's population and industry grew, more serious land use conflicts arose. With limited statutory law, our forebears often turned to two sources: One, the common law of nuisance; the other, the maxim that "one must so use his own rights as not to infringe upon the rights of another." (These were later codified in the 1872 Civil Code as sections 3479 *et seq.* and 3514, respectively.)

### The Hydraulic Mining Cases

These principles were decisive in one of California's first great environmental cases: *Woodruff v. North Bloomfield Gravel Mining Co.*, 18 F.753 (9th Cir. 1884). By the 1880s, the miners were employing hydraulic "moni-

tors" to blast huge quantities of earth from the foothills. Detritus filled the lowland river channels, increased flooding, impaired navigation, covered farmland, and generally wreaked havoc. (The bed of the Yuba River at Marysville was raised nine feet.) Those living downstream formed the "anti-debris association" and sought redress.

A modern environmental lawyer would recognize their litigation techniques. Having lost earlier test cases, the anti-debris association funded a plaintiff (Woodruff) who had standing to sue for both public and private nuisance. He plausibly claimed a variety of commercial, agricultural, navigational and personal injuries.

Woodruff's lawyers emphasized the great public injury as well. Indeed the Court acknowledged that it was appropriate for "the private party [to] sue...rather as a public prosecutor than on his own account" (provided he also shows "special damages," still the rule in public nuisance cases).

At the heart of the proof was an expert opinion bolstered by percipient evidence. The judges "took a view" of both the mining operations ("a night scene...at the mine, is in the highest degree weird and startling, and it cannot fail to strike strangers with wonder and admiration") and the affected lowlands ("the amount of debris discharged into the rivers...can only be duly appreciated by actual observation").

Defense counsel presented their own experts and raised innumerable legal theories, all of which the Court rejected. Instead, Judge Lorenzo Sawyer applied both the maxim and principles of public and private nuisance to enjoin the mining operations.

### Mountain Copper

Twenty years later, the United States filed perhaps the next great environmental case: a suit to enjoin Mountain Copper's multi-million dollar smelting operations in Shasta County. Suing as a landowner, the government alleged the smelter's air pollution was killing trees on vast expanses of public land. *Mountain Copper Co. v. United States*, 142 F.625 (9th Cir. 1906).

Again, a modern lawyer would recognize the litigation tactics: experts on both sides, testimony about how and where the smelter's gases blew, much discussion of the state of the art and possible improved technologies, and evidence of how much money the mine pumped into the local economy. In the end, the Court of Appeals applied the law of nuisance and refused (after balancing the equities) to enjoin the operation. The mine continued to operate and pollute. Incidentally, it created employment, decades later, for Superfund lawyers.

So, next time you handle a nuisance or water law case, consider yourself only the latest in a very long line of lawyers who have applied fundamental, common law principles to an environmental problem. You are Mr. Dunn's worthy successor.

Mr. Goode is a partner in the firm of McCutchen, Doyle, Brown & Enersen.



**Barry P. Goode**



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## *Ruminations Upon Retirement*

political attacks on the judiciary in general, as a neutral authority figure. For this reason, it is a very bad practice to argue with the judge in front of the jury, especially after the judge has ruled on a point. It is worse yet to interrupt the judge. (Judicial interruption, on the other hand, is merely "participatory listening.")

Several corollaries follow from these concepts. For instance, many litigators vigorously argue every point with no apparent differentiation as to their relative importance. Sometimes called "playing every flyspeck in the music," this practice tends to undermine the litigator's credibility on crucial points. No one wins every argument, so choose your fights carefully. Similarly, objections that do not advance the client's interest should not be made. Testimony about photographs, documents, or other physical evidence is useless if the jury does not see the evidence. All too often the lawyer and a witness will animatedly discuss a photograph or document, usually in a whispered conversation off the record, and never show the photo or document to the jury. It bears repeating: The trial is not for the record; it is for the audience of twelve.

Arguments over the authenticity of clearly admissible documents will serve only to confirm most juror's preconceived and generally unflattering ideas about lawyers. Similarly, it is not necessary to prove each point in contention through each witness. If everyone in the courtroom knows the answer to the question, it is probably not a good question. One should distinguish the forest from the trees, if possible.

The attention span of humans should also be a serious concern of lawyers trying jury trials. There seems to be intuitive wisdom in the "one hour" schedule, which is so deeply ingrained in our culture in many areas such as class length, television shows, psychiatric sessions, etc. Arguments and opening statements that exceed this length frequently become counterproductive. Boring the jury is almost as sure a way to lose as insulting the jury.

The essential decency of jurors and the conscientious manner in which they approach their task never cease to amaze me. Most individual jurors have a surprising amount of common sense, and certainly all juries do. I have seen jury after jury reject overreaching claims by both plaintiffs and defendants. Parties who present dishonest or exaggerating witnesses frequently feel the lash of the jury. If a witness's testimony seems implausible to you, when viewed objectively, you can bet that it will seem implausible to the jury.

Careful and thoughtful planning for trial, restrained examination of witnesses designed to produce only evidence needed for closing argument, respect for the jurors' intelligence, and the use of plain English are all behaviors I have seen rewarded by juries.

In the end, of course, the case makes the case. Lawyers, if they do their job correctly, can usually hope for little more than to "do no harm." However, being aware, at the

beginning of every case, that at its end looms the potential of a decision by twelve ordinary citizens, should guide all of the decisions made along the path to that end. Foresight, and the sensible use of intervening alternative dispute resolution processes, can avoid many of the litigation disasters that are all too obvious in hindsight. If this sounds like an appeal to use common sense, it is.

*Judge Michael E. Ballachey has recently retired after 20 years on the Alameda County Superior Court to join the American Arbitration Association Center for Mediation in San Francisco. His e-mail address is [mballachey@msn.com](mailto:mballachey@msn.com).*

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