

# Law Trends & News

Practice Area Newsletter



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Summer 2009  
Vol. 5, No. 4

## Chair's Note

Dear Division Member:

Below is the fourth issue of *Law Trends* for the 2008–09 bar year. As always, this is a very exciting issue, and I am very happy to present it to you. As with prior issues, this publication is designed to help simplify your practice by including articles, checklists, and other valuable practice information and practical tips.

In this issue, there are portions of newly published books, one about giving representation and counseling to nonprofit religious organizations, and the other about presenting a claim for a patent infringement. These books not only cover most issues attorneys will face in this kind of representation but also have many forms an attorney will need in that representation. Click through to take a look at the topics in these books; if you like what you see, you can immediately purchase them.

With this issue, *Law Trends* is now completing its fifth year and is certainly a member benefit. We hope you agree that with each edition, *Law Trends* continues to provide meaningful articles for you, and that this edition, like the others, helps you in your daily practice. I encourage you to take just a few moments to read the list of articles included below. Of course, it is yours to download and keep as a reference for the future. And, as in the past, you can either download specific articles, or you may download the entire newsletter by clicking the [PDF](#)  link.

There are many Division members integrally involved in putting this publication together. Their hard work and dedication are certainly present. I thank them for producing another fine year of *Law Trends* for the Division. Each of the assistant editors did a fine job. Without their superb efforts, none of this would be possible.

I hope each of you enjoys this issue of *Law Trends*. Next bar year, the publication will continue quarterly, and we hope you continue to find it a source of valuable information. If you are interested in either writing an article or participating in the production of the newsletter, please contact Jim Schwartz at [attyjls@aol.com](mailto:attyjls@aol.com). Jim has

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been the editor since its launch five years ago and will continue as editor next year. I thank him for his work as well.

I hope to see you at the ABA Annual Meeting in Chicago!  
Best regards,

A handwritten signature in black ink that reads "Robert A. Zupkus".

Robert A. Zupkus  
*Chair, General Practice, Solo & Small Firm Division*

**Letter from the Editor**

Dear Division Member:

I have been editor of *Law Trends* since its founding. We are now completing our fifth year as a publication. In that time, we have strived to bring you timely and helpful articles and checklists—all to help you in your daily practice. This year, we added two areas: Practice Management and a Young Lawyers Section. I am proud of the quality of articles and tips in both areas, and I hope you enjoyed them as well.

For a publication like *Law Trends* to excel, the people working on its behalf must be a dedicated group of volunteers. To be sure, I have had the extreme pleasure of benefiting from the efforts of such a group this year. And so, with this being our final edition of *Law Trends* for this bar year, I want to take this opportunity to thank the men and women from the Division who have volunteered their time and worked on *Law Trends* throughout the year. They are as follows:

Assistant Editors:

Kathleen Hopkins, Henry DeWoskin, John Carr, Jennifer Hilsabeck, Travis Cushman, Noah Davis, Linda Holder, Charles Lamb, Jay Ray, Randi Whitehead, and Arnettia Wright

Lastly, I also want to recognize Tom Campbell and Susan Wilson of the ABA staff. Without both of them, none of this would be possible. Their dedication and zeal can be seen in the product delivered to you, and I sincerely want to say thank you to both of them for a job very well done.

Without everyone's incredible help and assistance, none of this would have been possible. I again congratulate each and every one of them and look forward to their continued help next year.

Very truly yours,

Jim Schwartz  
*Editor*

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Featured Author

**Featured Author**

**John J. Paschetto** is a partner in the business and tax section of Young Conaway Stargatt & Taylor, LLP, in Wilmington, Delaware. His practice focuses on governance issues faced by Delaware corporations, limited liability companies, and limited partnerships. He also serves on the committee of the Delaware State Bar Association responsible for proposing amendments to the Delaware Revised Uniform Limited Partnership Act, the Delaware Revised Uniform Partnership Act, and the Delaware Limited Liability Company Act. John can be reached at [JPaschetto@ycst.com](mailto:JPaschetto@ycst.com) or 302-571-6608.



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### Featured Author

**Kyle Branum**

practices in real estate and business at Riddell Williams, P.S., in Seattle, Washington. He has extensive experience in real estate transactions. His real estate practice focuses on real estate purchase and sale transactions, commercial leasing, financing, construction and design, and condominium and mixed-use development. Kyle counsels clients in a broad range of business transactions, including business formations, mergers and acquisitions, private equity and debt financings, and professional practice acquisition.

In addition to practicing law, Kyle is active in the community and with local bar association. He has served as vice president (2005), president (2006), and trustee (2007) of the East King County Bar Association. He can be reached at [kbranum@riddellwilliams.com](mailto:kbranum@riddellwilliams.com) or 206-389-1671.





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## Family Law

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## Put Five Rainmaking Habits to Work for You

By Mark Powers and Shawn McNails

See if you recognize your own marketing approach in the following description: when business is good, you're scrambling to keep up with your caseload and not marketing at all. It is overwhelming enough to find yourself in a position that requires you to be a shoulder to cry on, a skilled mediator, a trial attorney, and fire fighter simultaneously. But when business starts to fall off, a sense of panic creeps in, and you desperately try to market yourself. Some of these marketing efforts pay off, the panic dies down, and the work begins to come in again.

So you stop marketing . . . until the next time. And the practice always seems as if it is in this cycle of stress and frustration . . . either too much production or never enough.

Does this sound familiar? For many family law attorneys, especially solo and small-firm practitioners, this frustrating feast-or-famine cycle repeats itself over and over again throughout the lifetime of their practices. If you recognize your own sporadic approach in this description, you probably never feel in full control

## • Past Issues

of where your practice is going, and a consistent, predictable stream of good clients remains elusive. Fortunately, there is a solution. A good client development plan, when properly implemented, can flatten the cyclical nature of your practice and make your marketing efforts much more successful. And it doesn't have to be difficult, expensive, or elaborate to be effective.

As practice advisors to attorneys throughout the United States, we are often called upon to help clients formulate marketing plans. Very elaborate plans are never used because they are too complex: we advocate a simpler approach. We begin by gaining agreement on two very important assumptions: first, we believe that the best family law clients come not from Yellow Pages, but from referral sources and that relationship-based marketing is the least expensive, most comfortable, and most ethical means of building a family law practice. Second, that one size does *not* fit all: a sustainable relationship marketing plan has to be customized to each individual personality, as well as values and interests.

Given this, we recommend the development of relationship-building habits. At Atticus, we call them the “Five Rainmaking Habits,” and they significantly leverage your marketing efforts because you do them week in and week out. After awhile they become second nature. Any marketing plan that is just a list of to-dos and doesn't include a persistent and habitual client development focus is likely to be ineffective and soon forgotten. That doesn't happen when you build in the right habits and commit to implementing them on a weekly basis.

### Make It a Habit

In a nutshell, the Five Rainmaking Habits are:

**1. The “have three marketing contacts” habit.** These contacts could involve lunch, might happen at the courthouse, or at a bar association event—so long as they involve at least 20 minutes of building rapport and relationships with existing or potential referral sources. Always take advantage of serendipitous meetings, but block time in your calendar to consistently market yourself three times a week. The results are worth the effort: 3 contacts x 50 weeks = *150 marketing contacts a year*. If 150 contacts don't make a difference to your business, nothing will. This is, by far, the most important of the Five Habits to implement.

**2. The “asking for referrals” habit.** At the conclusion of each case, say: “My practice has been built on (or relies on) referrals from people like you. If anyone you know needs my services, I'd appreciate your mentioning my name.” You don't have to use our words, but this is the general idea. Don't assume that clients automatically will think of referring others to you, as it may never occur to them. If you send any follow-up correspondence, repeat the suggestion there as well.

**3. The “sharpening the saw” habit.** Stephen Covey made the phrase “Sharpening the Saw” famous, and it means that we must seek constant

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improvement if we hope to achieve excellence. From Atticus's perspective, we believe that you must develop a marketer's mindset. Read a marketing book or articles on marketing once a month, supplemented by a marketing workshop whenever you have the chance. We teach marketing over the telephone to attorneys all over the country in a course called "Rainmakers," but you don't have to participate in one of our calls to learn about marketing. We believe that the extreme distaste many family law attorneys feel when it comes to marketing is due to lack of training. With relationship-based marketing, you already possess many of the skills you need to be successful but don't realize it. You have what it takes—but you must learn how to apply it strategically. Educate yourself about marketing at every opportunity.

**4. The "thanking referrals" habit.** Thanking referral sources every time they send a client, regardless of whether the client hires you, is imperative. Send a handwritten note, pick up the phone, or take the referrer to lunch every time they make an effort to send a client your way. Always reward this behavior as promptly as you can so that the referral source will think of you the next time he or she has business to send.

**5. The "adding names" habit.** Some referral sources are better than others and deserve the bulk of your attention. But they will move away, shift careers, retire, or otherwise stop sending you business. It pays to keep meeting new people to continually add new streams of referrals. For example, one family law attorney we know reads the "Welcome Section" of his bar news and calls each new attorney who comes to town and invites him or her to lunch. The new attorney feels welcomed, and a new person is added to the first attorney's network. Another attorney attends bar functions with the goal of always meeting three new attorneys who don't practice family law. She does this by always sitting at tables with no one she already knows.

If your client development plan consisted of nothing more than implementing these Five Rainmaking Habits, you'd have a much greater sense of control over your marketing, you'd see an improvement in the number of referrals sent—and you'd keep the panic at bay. But to help you be even more strategic as you build these marketing habits, here are a few more client development distinctions that all basic client development plans would address.

## Knowing Who to Talk to

If you don't know who to market to, your three marketing contacts a week will be misdirected and, given that you don't have time to waste being ineffective, it pays to know the answer to this question before you start. There are two groups of people on which to focus. These are *your clients* as well as *the people who send those clients to you*. Let's take a closer look at these two groups, starting with your clients.

**Identify your target market.** Generally speaking, this is the group of people that you serve: people seeking a divorce, help with custody issues, a prenuptial

agreement, or perhaps an adoption. These are all people you can help. But since the quality of your clients dictates the quality of your practice, you must define your potential clients not only by the problems they bring, but by the demographic and psychographic details most likely to predict their ability to pay, their level of cooperation, and likelihood of a successful outcome. Among the broad group you generally regard as potential clients are another group we'll call your *ideal* clients. The ideal client presents the kind of problems you are most interested in, and even passionate about, solving. Most importantly, ideal clients are those who can actually pay for your services. They are the first group to identify when putting together a marketing campaign because you need to know how to attract the group that is ideal for you and your practice. Your plan hinges on properly identifying this group. If you spend time marketing to referral sources that aren't tied to your preferred clients, they'll send you the wrong clients and you've wasted a lot of time. So let's examine their characteristics.

Your ideal clients will have unique socioeconomic, demographic, and psychographic attributes. Let's say, for example, you are a family law attorney interested in working with high-net-worth individuals. Your primary or ideal client (1) will probably be more highly educated than the average person, with at least some college, if not an advanced degree or two. (2) Your client will often be a professional (or the spouse of one), or may be an entrepreneur (or the spouse of one) who owns one or more businesses. (3) Your ideal client will have a high level of assets (*choose a level you are comfortable dealing with*), and the complex financial issues that accompany that level of assets. Generally, this means he or she will also have the ability to pay for your services. In addition, (4) your ideal client will range in age from mid-thirties to late fifties (though the upper age range is shifting as empty-nester divorces gain in popularity); and (5) tend to live in specific neighborhoods, hold memberships in specific clubs, participate in certain charitable efforts, and attend prominent churches.

**Identify your primary referral sources.** This is the group of people in the best position to influence your targeted group of clients to use your services. We'll discuss them by category, dividing them into the groups that are most likely to come into contact with your potential clients.

For family law attorneys, they are (1) your colleagues—other attorneys you know, including your competition (they can refer conflict business); (2) your partners, if you have them; (3) other professionals, such as CPAs (they rank as the number one most-trusted professional, and their referral potential is very strong); (4) psychologists, therapists, marriage counselors; (5) financial advisors; (6) business valuation specialists, and other experts; and (7) clergy.

Also, for most family law practitioners, your (8) past and present clients should be strongly counted as potential referrers. A key indicator of client satisfaction is that former clients send a significant number of referrals. If you aren't receiving at least 30 percent to 50 percent of your referrals from your existing client base, focus a part of your marketing campaign on improving the level of service you deliver.

To determine the categories of people you are already getting referrals from, list them and focus on developing relationships in categories of people who are not yet sending referrals. Write the eight categories (CPAs, psychologists, clergy, etc.) on a piece of paper underneath each category. Then list the names of the people who send you business. Put a star next to those you presently consider your best referral sources. This is a vitally important group that you should cultivate as part of your campaign. This step is critical: make a separate list of these individuals and keep it in an easy-to-access location so that you can review the names frequently and stay in communication with them. Your goal is to have 20 people on the list, even if you start out with far fewer. (Hint: have your bookkeeping software generate a report of all clients for the past year, ranked by fees from high to low. Go through the list and note who sent the high-fee cases—these are your most important referral sources).

## Knowing What to Say

Now that you have determined who your ideal client is, and you've assembled your most important list of referral sources, you know who to talk to. These are the people you'll focus on when you schedule three marketing activities a week. But what will you say when you get together with these people? Below are just a few of what we call "Strategic Conversations" central to a relationship-based marketing approach. Develop and use these conversations with your best and potential referral sources.

**The laser talk:** This should be a brief description of who you serve, the problems they have, how you help them with those problems, and what makes you uniquely qualified to do so. You will only use the more formal version of this talk when you are speaking or being introduced in a seminar setting, but you will use the informal version every time you are at a social gathering and someone asks, "What do you do?" One attorney we work with is a pioneer in the collaborative law movement. He introduces himself as a "recovering litigator who practices family law." In response to the questions this inspires, he'll go on to say he "has decided that the financial and emotional toll exacted by taking clients to trial isn't worth it. So he practices with a new approach called collaborative law." People are usually intrigued by what he says and ask him more questions, which lead to interesting conversations. This "brands" him in their minds and distinguishes him from other divorce attorneys. It is your job to distinguish or brand yourself in some fashion. Make this an objective of your marketing campaign.

**Ask questions:** Get to know your referral sources, as people—and better yet, potential friends. Spend time with them—especially your Top 20, but also with new potential referral sources, getting to know them and deepening your rapport with them. Relationships are built through conversation. When at a loss for words, ask the person questions about his or her life, work, family, background. Do 70 percent of the listening and 30 percent of the talking. The person will come away thinking you are a great conversationalist. Studies show that it can take

anywhere from one to seven conversations with potential influencers to earn their trust and get their business. Here's a tip: ask each new client who comes in to enter the names of his or her financial team on your intake form—CPA, tax attorney, stockbroker, financial planner, etc. These are all good potential referral sources. Use the opportunity to connect with them, to get to know them, and perhaps to build a referral relationship with them. Think of all of your other experts in the same way and add an element of marketing to everyday business conversations. Find out about the person behind the expertise.

## Knowing How and When

Next, let's look at the "How and When" part of your marketing campaign. These are the events, meetings, and activities that provide the backdrop for building your referral relationships. This is the setting for those three marketing contacts a week. Of all attorneys, family law practitioners are the most stressed due to the crisis-driven nature of their practices. You don't have a lot of extra time to spend with your own families and are too exhausted to take on much in the way of large marketing initiatives. Keeping this in mind, we suggest you design the "How and When" part of your marketing campaign around your passions, interests, and hobbies. You'll be more likely to follow through with the activities that you find fun, interesting, or otherwise compelling. Below are a few ideas.

**Food and marketing:** Breakfast, lunch, and dinner. Everyone has to eat, and if you have a favorite type of food or restaurant, by all means, use it in your marketing efforts. As mentioned before, lunch is the most popular marketing venue for most of our family law attorney clients because it doesn't intrude upon their evenings and weekends. If lunch is all you can manage, great. Many attorneys have marketed themselves very successfully with lunch as their favorite setting. If you do have extra time in the evenings and enjoy cooking and entertaining in your home, showcase your talents and invite referral sources to join you on a monthly basis. The idea is to incorporate food into your marketing efforts so that you'll look forward to the experience in a positive way.

**Sports and marketing:** If you love to golf, but never have the time, make it the theme of your marketing campaign. Block off several hours on a weekly or monthly basis to play a round of golf. Make it a point to invite current or potential referral sources to join you. One firm of golf fanatics we've worked with started a tournament entitled, "The Barrister's Cup." Another attorney plays tennis in spite of her busy schedule and has developed relationships with a wide variety of other women in town she'd otherwise never have met. So, if you play tennis, like to fish, sail, or ski, no matter what your sport—there is a way to use it in your marketing campaign. Invite referral sources to participate with you, or give them tickets or gift certificates to go on their own with a friend or relative. One attorney we know buys tickets for basketball games and gives them to referral sources saying something like, "John, here's two tickets to the basketball game. I know you and your daughter don't get to spend a lot of time together and you both love basketball. Have a good time on me." Giving tickets is a great way to score marketing points without actually having to take time to attend the

event.

**Community involvement and marketing:** There are lots of ways to combine your community involvement with marketing. Your participation in charities, community fundraisers, and historical societies allows you access to other professionals, executives, and their spouses who may one day need your services. If you serve on a board, make it a point to arrive early or stay a little later at your meetings and get to know your fellow board members. Invite fellow board members out to lunch as part of your marketing campaign. Sponsoring a table at the yearly fundraiser often provides a great opportunity to invite other referral sources for a night out. In fact, any fundraising you get involved in gives you a wonderful excuse to call people you ordinarily would not contact and is great for meeting new potential clients and referral sources.

**Speaking engagements and marketing:** If you are someone who excels at public speaking, make this the foundation of your marketing campaign. You can speak alone, which is the perfect way to demonstrate your expertise; team up with a CPA for a seminar (“Forensic Accounting and Divorce”); or partner with a marriage counselor (“The Impact of Divorce on Children”). Offer to make an appearance at a church function. If you love to speak in front of groups, this is a great way to build credibility and increase your visibility in your community.

## Knowledge and Commitment

Once you figure out who your ideal client is, determine who your best referral sources are and use strategic conversational approaches to build relationships with them, you’ll know who to talk to, what to say, and how and when to say it. If this knowledge is supported by a strong commitment to practice the Five Rainmaking Habits on a weekly basis, you’ll set yourself up for marketing success. Marketing is a numbers game and the more marketing activities you engage in, the more successful you will be. Like compound interest in a savings account, you’ll be surprised at how these small investments of time will add up to a substantial payoff in a steady stream of new clients, additional revenues, and keeping the panic at bay.

Mark Powers is president of Atticus. Shawn McNalis is an Atticus senior practice advisor. Mark and Shawn coauthored the book *The Making of a Rainmaker*, and Mark founded Atticus Rainmakers , which helps family law attorneys stay focused on marketing, generate new ideas, and create ongoing accountability with marketing. Find out more at [www.atticusonline.com](http://www.atticusonline.com).

### Note

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## Family Law

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## What a Move May Mean for the Child

By Samuel Roll and Candace Kern

*How to minimize the risk of loss*

In our highly mobile society, the geographical relocation of one parent following separation or divorce is increasingly prevalent. Unless the parents agree to a relocation plan, permission for one of the custodial parents to relocate and the terms and conditions of the subsequent parenting plan become a matter for the courts. Relocation creates a situation in which there is a potential for catastrophic trauma to the affected children from the loss of a parent. The best parenting plans recognize this problem and seek to reduce the risks of serious harm.

### Relocation Intensifies Loss

Freud understood that the source of anxiety for human beings, regardless of culture or century, is the anticipated threat of one or more losses. He described them as:

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1. the loss of the person one loves;
2. the loss of the love of that loved person;
3. the loss of physical or social integrity;
4. the loss of self-esteem.

Freud, S. *Inhibitions, Symptoms and Anxiety*. London: Hogarth Press (1926). Standard Ed. Vol. XX, 87–174.

Relocation of one parent subjects the child to all of these potential personal catastrophes or losses. The loss or apprehension of loss may or may not overwhelm the child's capacity to cope. In our experience as custody evaluators, the types of apprehensions of loss children confide to us are dramatic, especially for children across the developmental stages who already are experiencing anxious and depressive feelings. Children confide that they worry that the parent left behind will die or find someone else with whom to share his or her life; however, they also feel afraid of losing the secure base that has been established with the relocating parent.

For a child, divorce results in the loss of the family as the child understands it. That parents of friends have divorced or that home has often been an angry, uncomfortable place does not mitigate the loss of the family as a result of divorce.

The child realizes that the parents have lost their love for each other and fears the same loss for him or herself. When parents are hostile to each other, the child is both scared of the loss of love and the loss of the social or, worse, physical integrity of his or her parents and self.

A common challenge for children is the feeling that they must side with one parent—or that parent will not love them anymore. This is greatly complicated by the parents' catastrophes of lost love and loss of the love of the loved one. In especially hostile divorces, with vulnerable parents, the child can suffer loss of self-esteem as derived from one parent who distances him or herself as part of the divorce, while suffering the loss of secure feelings from the love of the parent who remains, as the child is now the caretaker to that parent. Although the actual and anticipated losses associated with relocation are always salient, negative emotional experiences, they are not always traumatic losses that lead to psychopathology. Psychological evaluation and input can help to reduce negative impact.

### **Minimizing the Risk**

The impact of the relocation of a parent may be exacerbated or mitigated by many factors. The most important factor is the level of attachment of the child to each parent and sibling. It is useful to determine whether the child has an attachment differential between parents and how that relates to the child's capacity for healthy functioning (cognitively, emotionally, and interpersonally). In addition, assessing attachment levels pinpoints ways to deal with the necessary loss of one parent through geographical distance.

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Other factors that mitigate or exacerbate the child's capacity to cope with relocation include the child's psychological and developmental needs and capacities and each parent's capacity to meet those needs. These factors are used as guidelines in the American Psychological Association (APA Guideline I.3. *American Psychologist*, July 1994) and in the American Academy of Child and Adolescent Psychiatry, *Practice Parameters for Child Custody Evaluation* (1997).

The role of the psychological evaluator in a relocation dispute is to ascertain what is in the best interests of the children. Using the framework embraced by the psychological profession and the ample literature on attachment and developmental needs of children, psychologists can assist with sensitive insights for mitigating losses.

An important—but still controversial—observation of attachment theory and research is that infants seem to have a predisposition to form a single primary attachment. When the infant is under stress, alarmed, ill, or tired, the primary attachment figure is required from the infant's point of view. This attachment relationship develops over time. Michael Lamb has reported that when infants live continuously with both parents, the child's preference for one parent over the other may wane (1977), but this research is incomplete. The fact that attachment figures are not interchangeable for children greatly complicates devising time schedules and relocation decisions. J. Soloman and C. George, eds. *Attachment Disorganization*. NY: The Guilford Press (1999).

There has been much controversy in psychology because of a public policy goal to keep both parents equally involved in raising the children. This goal sometimes substitutes a perceived best interest of the parent for that of the children. It usually is in the best interest of the child to maintain a secure base with the parent who is the primary attachment figure. See L. Gunsberg and P. Hymowitz, eds. *A Handbook of Divorce and Custody*. NJ: The Analytic Press (2005) (especially chapters 12 and 23).

## Psychological Evaluations

The inquiry begins by ruling out that either parent is dangerous or unfit, proceeds to the developmental and any special needs of the child, the psychological match between parent and child, and then to the attachment between the child and any siblings and each parent. Complicating factors include stepparents on each side, their psychological condition and relationship to the children, and, of course, the stepparents' children.

For example, each parent and other caretaker living in the home must be evaluated to rule out problems with impulse control, serious problems with reality testing, and serious distortions of thought. The children must be safe (no physical violence, no distortions concerning sexual roles of children and parents; no psychotic acting out by adults). Psychological testing is useful in ruling out these problems.

Psychological testing and clinical evaluation of adults and children also helps the psychologist understand the psychological match between parent and child. For example, if the child is autistic, the mother is hysterical, and the father is obsessive-compulsive, then the match between child and mother is better. When the autistic child stays in one place repeating behavior over and over, the hysterical mother will break into that psychological space and insist the child interact with her; whereas the obsessive father will intellectually but not emotionally engage the child. However, if the child has a colostomy bag that requires changing, a hysterical mother may be too squeamish to attend to the child's needs, but the obsessive father may be carefully attentive to the child.

Retaining meaningful language and traditional experience becomes an important component when considering the psychological match in families where there is a mixed cultural heritage. We see this frequently in our New Mexico practice where there are strong cultural traditions among Native American, Hispanic, and Anglo populations.

Once the needs of the child and the capacities of the parents are understood, the attachment between child and parent becomes the focus for parenting recommendations. Attachment and the developmental stage of the child typically go hand in hand. Below, we set out the principles of attachment with special emphasis on how the child handles necessary losses. Children with problems of anxiety or depression may need the secure base of their primary attachment figure at older ages than the children who have a normal capacity to cope.

A psychological evaluation provides a clearer picture of the psychological conditions of the children and parents and the respective level of attachment. This makes possible a more accurate estimate of the potential traumatic impact of relocation. It also allows for educational and prophylactic measures to be taken. A baseline is established that is useful in any subsequent evaluations, monitoring the child's increasing or decreasing capacity to cope and his or her reduced or increased emotional and intellectual capacity.

The skills parents bring to the task of helping a child cope with relocation vary widely. These skills can be improved and expanded, especially once the decision to relocate has been made and the parents embrace the task of working within a framework to enhance every family member's relationships.

Psychological evaluation pinpoints the psychopathology of either parent to contain its effect on the child. Reducing any incident of attempted suicide or other narcissistic self-involvement on the part of a parent relieves the child and strengthens his or her capacity to cope. Most children use their parents as an emotional barometer for their measure of safety or danger in the world.

The longitudinal research of Judith Wallerstein and Julia Lewis (21 *Psychoanalytic Psychology* 3 (2004), 353–70) on the effects of divorce on children establishes two crucial points. First, the level of hostility or amicability

in divorce is the factor that offers the worst harm or greatest benefit to the children. Second, the harm parents cause in a hostile divorce is to the child's capacity to develop and maintain intimate relationships throughout their lives. When the goal in creating a parenting plan is amicable partnering intended to preserve and enhance the child's feelings of intimacy with both parents, there is a likelihood of ameliorating an inherently damaging situation. Although equal time with each parent purports to address this issue, devising a plan that incorporates the measured level of attachment speaks to a more sanguine outcome.

Parents can be actively involved in minimizing the problems of relocation. Recognizing that the younger a child the more contact is needed, the relocating parent can enhance predictable, consistent contact between the child and the absent parent. Examples include establishing a pattern of saving the child(s) school work or other items that the child can send to the absent parent, including photographs of events the child experiences. With preschool children, it is useful to have a picture of the absent parent in the bedroom. It also is useful for the absent parent to tape-record stories for the child and to send hand-written notes and letters to the child on a regular basis. Both voice and handwriting reinforce the individual, intimate details between absent parent and child. With very young children, a transitional object of something the absent parent wore, which smells of the parent and is warm and cuddly, can alleviate some of the stress of loss.

## Developmental Factors

Along with helpful guidelines for attachment and developmental stages, a determination of physical custody of the child and time-sharing responsibilities must include consideration of the family's circumstances.

1. When a child is between six months and one year old, visitation that requires an overnight stay outside of the home of the primary parent is psychologically harmful because of the infant's need for that parent's physical presence to experience emotional security. In addition to emotional factors, there are cognitive factors, discussed in (3) below, that are not achieved until the child has further developed. Peter Fonagy describes in detail both the delicacy of the attachment process and the research supporting it. *Attachment Theory and Psychoanalysis*, Other Press (2001).

Because of legislative design or parental preference, there may be times when there is an insistence on overnights before age one. In such cases, the best interest of the child dictates that the parties be encouraged to permit the noncustodial parent more frequent or longer visitations during the day, rather than overnight visitations.

2. When the child is one to three years old, if there are coparenting conflicts or little communication between parents, disorganization occurs in the child's capacity to attach to the primary caretaker, which affects the child's sense of stability and coherence in development. Visitation with the absent parent must incorporate these considerations. We believe that the empirical research of

Judith Solomon, Ph.D. and Susan George, Ph.D. in *Disorganized Attachment*, cited above, is convincing.

3. When the child achieves object constancy—the ability to cognitively and emotionally internalize the primary caretaker—at about age three, the child now has an inner capacity to comfort self with the understanding that the primary caretaker is absent but has not abandoned the child. More flexibility is available for visitation at this point. However, for children between three and seven, other variables must be considered, including:

- the capacity of the child to integrate an understanding of time in order to cope with separation.
- the degree of the child's emotional liability; that is, whether the child is susceptible to momentary changes and has a harder time recovering from upheavals.
- the capacity of the child to reason and use logical thought. Until age seven, the child has a hard time using words to get a clear understanding of his environment.

4. After age seven, there are many more possibilities for creative visitation arrangements, depending on the level of anxiety and depression the child experiences.

5. Most children during adolescence re-experience separation issues in a more volatile way than between six and twelve years old.

Recent psychological literature has proposed that attachment concerns of younger children are different than those of adolescents. As a child grows and individuates, attachment needs to the primary attachment figure continue, but at a lesser urgency as the child better internalizes the parents and develops the capacity to cope more autonomously.

## Adolescent Separation

It is at this stage that we typically see a greater desire of the teenage child to maintain peer, school, and extracurricular activities. However, adolescent separation issues can be intensely experienced, depending on the child. A healthy teenager's desire and request not to relocate with the primary attachment figure because the child has successfully individuated, has a comfortable relationship with the parent not relocating, and has developed plans to maintain sufficient contact with the relocating parent is an acceptable parenting plan. However, we do not believe that a child attaches to place over person; rather, the child has sufficient psychological resources to flourish in the chosen environment with one parent and maintain a positive long-distance relationship with the other parent.

Dealing with the complexity of siblings at different developmental stages is challenging. It usually is better to keep siblings together because they provide

continuity in a family, even when parents are separate. The needs of the younger children usually are more urgent than those of older children. Balancing the internal needs of the younger children and the internal and external needs of the older children (including peer relations, educational aspirations, and other activities) must be considered.

To every extent possible, loved ones should continue to be a source of affection and emotional support for the child. In the end, the final test of our work with children in relocation disputes is the degree to which we have worked out arrangements that assure the children that their fears of loss are, if not unjustified, at least greatly exaggerated. The child should have a high level of self-esteem and feel that no important person has been lost, that no important person's love has been lost, and that parents have provided for the child a sense of social and physical integrity.

Standards for permitting relocation are not uniform throughout the country. Some courts consider reasons given for the move and its potential interference with the other parent's visitation before determining the best interests of the child. But in New Mexico, for example, the best interests of the child is directly linked to the determination of which parent is the primary attachment figure.

There can be psychological reasons to deny a relocation request. A child may be too vulnerable to suffer the additional stress of moving. For example, a child who has already developed phobias and nightmares and who is significantly distracted at school could be devastated by a major life change. In such a case, relocation should be reconsidered once the child reaches psychological equilibrium.

When a child, because of constitutional or environmental circumstances, has a tenuous capacity for attachment, the psychological consequences of relocation must be considered. For example, children with autism or Asperger's disorder attach to only a few people, and breaking any relationship makes a major difference for them. Relocation compounds this difficulty.

Another type of situation in which denial of relocation should be considered is when one parent has barely enough capacity to parent. Examples are a parent who suffers emotional storms, periods of serious depression, frequent hospitalizations, or frequent times when the parent cannot take care of the child because the parent is overwrought. This parent needs the other parent to share the burden of care. A review of how often the first parent asks the second parent for help is one way to begin to analyze the child's best interest in this kind of circumstance.

When the judge denies a relocation request, the parent petitioning to relocate must make a choice, a choice that significantly affects the family. The capacity of both parents to personally and interpersonally cope with the consequences of that choice greatly affects the child's experience of loss.

An order denying relocation usually does not anticipate what the petitioning

parent will do next. If judges and lawyers want to control the next step after denial, one practical way is for both parties to present parenting plans for either contingency. The judge then may order a new parenting plan as part of the denial. If the parent is going to relocate whether or not the children go with that parent, then the psychological and practical considerations and the recommendations of the evaluator may be presented to the court in a more timely manner.

Accordingly, the initial custody evaluation regarding relocation should be ordered to present alternatives that take into account the range of decisions available to the court. The goal is to help buffer the children against the disappointments of the petitioning (or responding) parent. The custody evaluation will have already sorted out each child's specific needs in terms of gender and age-related factors, in addition to the specific psychological makeup of the individual child.

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**Note**

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## The Top 12 Ways to Cut Costs and Survive the Downturn

By Lee S. Rosen

The economic downturn seems to be affecting nearly every industry, and family-law firms are no exception. MSN Money reported in January that couples might have to find a way to tolerate staying together in this economy because they simply cannot afford to get a divorce. Another issue is that law firms may no longer be able to rely on their bankers for lines of credit. Law Biz Blog ([www.lawbizblog.com](http://www.lawbizblog.com)) reports that banks are expected to be more cautious than usual and may begin to charge higher interest rates. So, where does all this bad news leave you? It means, of course, that you must cut costs like everyone else.

Let's look at the top 12 ways to reduce your operating budget now.

**1. Cut staff.** No one wants to think about laying anyone off, but the truth is that staff is a law firm's number one expense. *American Lawyer* reports that in an almost unprecedented turn, many of the largest New York firms have begun to

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lay off attorneys. Cadwalader, Wickersham & Taft laid off 96 lawyers last year; Clifford Chance let 80 go early this year; White & Case said goodbye to 70 associates; and the list goes on. It is time to ask yourself the hard questions: do you truly need all your staff? Do you have any employees whose performance is disappointing? Is everyone busy, or can a part-time position be eliminated and the tasks assigned to a full-time employee? If you have hourly employees, can you reduce their hours?

Some firms make the mistake of laying off employees, only to hire them back as soon as the firm has a couple of good months. Be careful. If the bottom drops out again, letting employees go a second time will have an extremely negative impact on remaining staff. It is best to let people move on and find stable employment elsewhere. Only bring back permanent employees when you feel confident you can afford to keep them long term.

**2. Renegotiate your lease.** Landlords are struggling in this economy too, which makes it a perfect time to get a great deal on your lease. If you agree to commit to a few more years, your landlord is likely to extend your lease at a lower rate. It is a win-win situation for both of you. Locking into a longer-term lease gives your landlord some leverage with lenders. Besides your lease term, are there other provisions that you would like to renegotiate? If so, now is the perfect time.

**3. Eliminate unnecessary equipment.** We tend to grow accustomed to the equipment we see every day without thinking about whether we actually need it. As staff shrinks, the need for office equipment shrinks as well. Save some real money by keeping only the equipment you use regularly. Do you really need all those phone lines? Is every leased copy and fax machine constantly busy? If not, get rid of the extraneous items.

**4. Require employee contributions for health coverage.** Although many firms throughout the country pay 100 percent of employee health insurance, a large number of firms do not, including large New York firms. At first, it may be a shock for employees to have some funds withheld from their paychecks for insurance coverage, but they will eventually get used to it. Paying 100 percent as an employer is not customary in many areas, and it certainly is not mandatory.

**5. Eliminate your 401(k) matching program.** According to *U.S. News & World Report*, numerous companies, including General Motors, have eliminated these programs. Contributions to 401(k) plans were largely eliminated during the last recession and reinstated when the economy improved. The bottom line is that employer 401(k) matching is not required or permanent.

**6. Outsource IT tasks.** In my firm, we have found that IT is one of the quickest ways to streamline staffing costs. Though it can be difficult to find one person to efficiently run a help desk and provide network support, an outsourced firm can provide both for less money. Sometimes an hourly employee will make better use of time, completing tasks quickly rather than stretching them out throughout the

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day. You might even discover that when you shift to an hourly consultant, the number of hours required to take care of your IT needs is a fraction of the time your full-timer spent on the job. Perhaps your full-timer has been assisting staffers with tasks that they can perform themselves. Although this work may be helpful, it may not be necessary. Even if you do require an on-site IT technician, you can use lower-paid staff for less complicated tasks, saving higher-paid personnel for the work that really matters.

**7. Outsource other projects.** If you require copywriting for marketing, print design, online design, or any number of other services, an enormous array of freelancers around the world will do the work for very reasonable prices. You can find these providers on websites, such as Elance.com, Guru.com, Crowdspring.com, and 99designs.com. We found a firm in India to do a web-coding project for \$500. It was quoted at \$10,000+ in the United States, and we have been using all sorts of services through these websites very successfully for years. Of course, you need to pay attention to the portfolios of the providers, as some freelancers are not as qualified as they profess. Choose carefully, and many talented and reliable professionals are available to work for your firm at prices substantially less than the cost of a large firm or full-time employee.

**8. Use a telephone/Internet broker.** My firm's broker cut our telephone bills in half. These brokers are similar to mortgage brokers. They become your agent for comparing and contrasting companies that provide dial tones in your area. Then they request bids for your telephone, Internet, and conferencing business. If a package deal with one company is not the most cost-effective for you, the broker can bundle your deal with several providers. In other words, you get the most economical services available to you, and the companies you choose pay the broker's commission.

**9. Use a media broker.** Similar to the telephone/ Internet broker, a media broker purchases advertising for you. If you spend any of your budget on ads, a broker definitely beats doing it yourself. Media brokers have relationships with the media and sometimes get discounts that can be passed on to you. They are experts on your demographic, and they know the territory—exactly when and where to reach your target audience. Most of them will put together a media plan for you for free and then purchase the advertising in several different outlets for you.

If you buy it yourself, you have to call each media outlet individually because they are only interested in selling you space or time in one place. With a broker, you need not deal with salespeople at all. Your broker is invested in buying time and space from a variety of outlets that best suit your needs. These brokers earn their commissions from the media outlets, and some of them are even willing to return a percentage of that commission to you. In the current economy, everything is negotiable.

**10. Extend the lifespan of your equipment.** Computers no longer become obsolete as quickly as they did a few years ago, so no need to replace equipment

as often. Keep your hardware as long as possible, and you will save considerably. Instead, spend money on maintaining your equipment to keep it functioning optimally.

**11. Buy used furniture, art, and equipment when businesses close.**

When my firm moved into our current location, a consulting firm was in the process of liquidating its office. We purchased all of that firm's paintings for a fraction of the original cost, furnishing our office with beautiful artwork, and no one was the wiser. If you need more furniture, artwork, or equipment, do not automatically buy brand new. Many used items are in like-new condition, and the savings to your firm can be substantial.

**12. Move employees from full-time to part-time status.** Some employers are requiring across-the-board reductions in employee hours. Some are moving full-time employees to part-time status to reduce benefits. Health-care costs are astronomical, and the numbers are expected to rise. Even if your employees contribute to their premiums, insurance costs are among your highest expenditures. As a last resort, consider putting some full-time employees on part-time status. This is certainly not for the faint of heart, but if it comes down to reducing your costs or closing your doors, eliminating the cost of benefits may be a viable recourse. Be careful to check your state laws as you explore this aggressive cost-cutting approach.

A few simple adjustments may save a substantial amount of money. You could discover, for example, that lowering your telephone, rent, and media costs alone is enough to allow you to keep all of your employees. Continue to look for hidden expenditures and areas in which you can slice and reduce. It is the best way through the perils of a difficult economy.

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## Potential Fraud Liability for Merger Agreement Representations and Warranties

By Michael Hutchings

A recent Ninth Circuit decision in *Glazer Capital Management, LP v. Magistri*, 2008 WL 5003306 (9th Cir. (Cal.) Nov. 26, 2008), found that investors may be able to rely on the representations and warranties contained in a merger agreement filed as an exhibit to a company's public filings as factual statements to investors to support a securities fraud claim. By so doing, the Ninth Circuit has called into question the customary practice by public companies of excluding merger agreement disclosure schedules from public filings.

In light of *Glazer*, and considering a 2005 SEC report in connection with the settlement of an enforcement action against the Titan Company, public

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companies should strongly consider including disclosure in the SEC report to which an acquisition agreement is filed as an exhibit disclosing material exceptions to representations or warranties that appear in the disclosure schedules.

### *Glazer Capital Management*

*Glazer* involved an appeal of a lower court's dismissal of *Glazer Capital Management's* class action securities fraud claims against *InVision Technologies, Inc.*, based on alleged public misstatements made by *InVision*. *InVision* was a publicly traded company providing explosive detection systems. On March 15, 2004, *InVision* announced that it had signed a merger agreement pursuant to which it would be acquired by *GE* in an all-cash transaction for \$50 per share. That same day, *InVision* filed its annual report on Form 10-K with the SEC and attached a copy of the merger agreement as an exhibit to the Form 10-K.

On July 30, 2004, *InVision* issued a press release stating that an internal investigation had revealed possible violations of the Foreign Corrupt Practices Act of 1997 (FCPA) in connection with certain foreign sales transactions. Following this announcement, the price of *InVision* stock dropped by more than \$6 per share. On December 6, 2004, *InVision* announced that it had entered into a nonprosecution agreement with the DOJ and had agreed to pay a fine of \$800,000. That same day, *InVision* and *GE* consummated the merger.

A few days after *InVision's* July 30 announcement, *Glazer* filed a class action complaint in the Northern District of California that alleged that *InVision*, along with its CEO and CFO, violated section 10(b) of the Securities Exchange Act and Rule 10b-5 there under by making three alleged statements to investors that were false or misleading. The three statements appeared in the representations and warranties section of the merger agreement between *InVision* and *GE*, and included *InVision's* representations that (1) it was in compliance in all material respects with all laws, (2) it was in compliance with the books and records provision of the Exchange Act, and (3) neither it nor, to its knowledge, any of its directors, officers, agents, employees, or other persons acting on its behalf had violated the antibribery provisions of the Exchange Act.

The merger agreement explicitly stated that the representations and warranties were qualified by a separate disclosure schedule delivered by *InVision* to *GE* simultaneously with the execution of the merger agreement. The disclosure schedule was not filed with the SEC nor otherwise publicly disclosed.

*InVision* argued that the mere context of the alleged misstatements—representations directed to *GE* in a private agreement between *InVision* and *GE*—rendered them legally incapable of supporting a securities fraud claim by public investors. *InVision* also pointed to a passage in the merger agreement that provided that the agreement was “not intended to . . . confer upon any [p]erson other than the parties hereto any rights or remedies hereunder.” In addition, *InVision* referred to language in the merger agreement that expressly qualified

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the representations and warranties by information contained in the disclosure schedule. InVision argued that, because the disclosure schedule was never released to the public, no reasonable investor would have relied on the representations and warranties contained in the merger agreement as statements of fact.

The Ninth Circuit court ultimately affirmed the dismissal of Glazer's claims because it ruled that Glazer did not plead facts raising a strong inference that the CEO knew that the representation was false. Nevertheless, the court rejected InVision's argument that the mere context of the statements in the representations and warranties section of the merger agreement was enough to render the statements incapable of supporting a securities fraud claim as a matter of law. It found that the fact that the merger agreement was a private document and included reference to a nonpublic disclosure schedule would not, as a matter of law, prevent a reasonable investor from relying on the representations and warranties as statements of fact when the merger agreement is filed with the SEC as an exhibit to a company's public filings.

Public companies can take heart in the court's ultimate affirmation of the dismissal of Glazer's securities fraud claims based on Glazer's failure to plead scienter on the part of InVision's CEO. However, the court's conclusion that *factual statements contained in the representations and warranties section of a merger agreement may support a securities fraud claim* becomes more important in light of the SEC's section 21(a) report in connection with the settlement of an enforcement action against the Titan Corporation, issued on March 1, 2005.

The Titan Report was issued in conjunction with the SEC's settlement of an enforcement action against the Titan Corporation, a defense contractor, for alleged violations of the FCPA. The SEC's stated purpose in issuing the Titan Report was to make clear its view that *representations and warranties included in agreements filed or summarized in documents filed with the SEC are statements subject to antifraud liability*. The SEC cautioned in the report that the failure to adequately qualify disclosure regarding material provisions of agreements described in public filings or filed as exhibits to or incorporated by reference into public filings may be actionable under sections 10(b) and 14(a) of the Exchange Act and Rules 10b-5 and 14a-9 thereunder.

## Best Practices for Disclosure

Public companies should reconsider their approach to public disclosure of material agreements in SEC filings, particularly with respect to whether information contained in disclosure schedules and disclosure letters is omitted from SEC filings. In the wake of Glazer and the Titan Report, companies should strongly consider the following two actions as part of the public filing of acquisition agreements.

First, companies should include a general disclaimer—both in the disclosure document (the proxy statement, Form 10-Q, Form 10-K, or Form 8-K) and in the agreement itself. The general disclaimer should explain when applicable that (1) the representations and warranties contained in the agreement were made for the purposes of allocating contractual risk between the parties and not as a means of establishing facts; (2) the agreement may have different standards of materiality than standards of materiality under applicable securities laws; (3) the representations are qualified by a confidential disclosure schedule that contains some nonpublic information that is not material under applicable securities laws; (4) facts may have changed since the date of the agreement; and (5) only parties to the agreement and specified third-party beneficiaries have a right to enforce the agreement. Note, however, that the SEC has advised that general disclaimers will not protect against a failure to disclose specific facts known to the issuer.

Second, companies should include disclosure of material information, including material exceptions to representations or warranties, contained in the disclosure schedules in their SEC reports to which an acquisition agreement is filed as an exhibit or in which an agreement is described. A company, at a minimum, should ensure that material information contained in the disclosure schedules is disclosed to investors in some way, such as by including separate disclosure in a Form 8-K of material facts appearing in the disclosure schedules that previously have not been disclosed.

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“Keeping Current: Securities: Potential Fraud Liability for Merger Agreement Representations and Warranties,” by Michael Hutchings, 2009, *Business Law Today*, 18:4. Copyright 2009 © by the American Bar Association. Reproduced with permission. All rights reserved. This information or any portion thereof may not be copied or disseminated in any form or by any means or stored in an electronic database or retrieval system without the express written consent of the American Bar Association.

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## Business Law

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## Standards of Review, Officer Fiduciary Duties, and Shareholder Ratification

By Julie Kaufer and Justin Radell

The Delaware Supreme Court recently clarified issues of Delaware law in its unanimous *en banc* opinion in *Gantler v. Stephens*, No. 132, 2008 (Del. Jan. 27, 2009). Specifically, the Delaware Supreme Court held that

a board's rejection of an acquisition offer, without more, is not a defensive action that triggers the Unocal enhanced scrutiny standard of review; officers owe the same fiduciary duties of loyalty and care as directors; and shareholder ratification is limited to circumstances where fully informed shareholders specifically approve director action that does not legally require shareholder

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approval to become effective.

In *Gantler*, the board of directors of First Niles Financial, Inc., a small bank holding company, decided to put First Niles up for sale and engaged financial and legal advisors to assist in the sale process. The board received three separate bid letters, all of which were in the suggested range, according to First Niles' financial advisor. With respect to the three bids:

one offer, in which the bidder stated it had no plans to retain the board, was not pursued at all by the board; another offer was withdrawn after defendants failed to comply in a timely manner with the bidder's due diligence requests; and a third offer was rejected by the board without any discussion or deliberation.

The board ultimately decided to go forward with a plan to privatize First Niles through a share reclassification rather than sell the company. The share reclassification became effective after a majority of the shareholders voted in favor of it.

In the complaint, plaintiffs challenge the board's decision to reject the third offer and to go forward instead with the share reclassification. Plaintiffs' allegations include that defendants breached their duties of loyalty and care as directors and officers of First Niles by abandoning the sale process, and defendants breached their duty of loyalty by effecting the reclassification. The chancery court granted a motion to dismiss each of plaintiff's claims. The supreme court reversed with respect to all claims and reinstated the suit.

### Standard of Review

The supreme court determined that the *Unocal* enhanced scrutiny standard did not apply to the board's decision to abandon the sale process because that decision was not a defensive action by the board as is required under *Unocal*. The supreme court also determined that the board's decision not to pursue the merger opportunity should not have received the benefit of the business judgment rule. For the business judgment rule to apply, directors must show that they reached their decision in the good faith pursuit of a legitimate corporate interest *and* must have done so advisedly. If plaintiffs assert facts that support director self-interest, the business judgment presumption can be rebutted, and the entire fairness review may be applied. Here, the supreme court held that the entire fairness standard should apply because the plaintiffs alleged sufficient facts to conclude that a majority of the board acted disloyally and did not reach its decision in good faith.

The plaintiffs' allegations included that the defendants rejected the bid to retain their positions and maintain corporate control, certain officers failed to respond timely to diligence requests or to inform the board of their failure to do so in an effort to sabotage the sale process, and there existed conflicts with certain

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directors who did business with the bank and would potentially lose a significant client if the bank were sold. The supreme court emphasized that facts related to a director's disloyalty must go beyond a mere assertion that the director desired to retain corporate control—as is the case here.

## Care and Loyalty Owed by Officers

The supreme court also found sufficient factual allegations of wrongdoing to support the plaintiffs' claim that officer defendants breached their duty of loyalty. Although the Delaware Supreme Court alluded to it in the past, the supreme court explicitly held for the first time that corporate officers owe the same fiduciary duties of care and loyalty as directors of Delaware corporations.

## Shareholder Ratification Doctrine

The chancery court held that claims that defendants breached their duty of loyalty were extinguished because a disinterested majority of shareholders ratified the share reclassification by voting in favor of it. The supreme court disagreed, concluding that the shareholder ratification doctrine is limited to circumstances approving director action that does not legally require shareholder approval to become effective. What's more, shareholder ratification is limited to those director actions or conduct that shareholders are specifically asked to approve and does not include all related actions taken by directors. Further, shareholder ratification does not extinguish claims relating to the director action that was ratified but merely subjects the director action to the business judgment rule.

## Observations From the *Gantler* Decision

***Evaluate Potential Director Conflicts.*** When considering transactions, boards must carefully evaluate any situations where a director could be considered to have a conflict of interest, including any business or other interests that arguably could differentiate the director's interests from the interests of other shareholders. If not properly addressed, those conflicts could subject the board's actions to the entire fairness standard of review.

***Inform Officers of Duties.*** Legal counsel typically advises directors of a corporation of their fiduciary duties at the commencement of any sales process. The corporation should ensure that its officers also are informed of and understand their fiduciary duties.

***Officers' Liability Exposure.*** While the court made clear that the fiduciary duties of officers are the same as those of directors, their respective liability exposure is different. Delaware law permits the inclusion of provisions in charter documents that eliminate directors' liability for damages arising from a breach of the duty of care; these provisions do not extend to corporate officers.

***Limits to Shareholder Ratification.*** This decision narrowed the application of the shareholder ratification doctrine and made it clear that shareholder ratification does not “cleanse” all aspects of a board’s decision, as many had thought, but rather subjects the challenged action to the business judgment rule.

Julie Kaufer is a partner at the Los Angeles office of Akin Gump Strauss Hauer & Feld, and is a member of the firm’s Corporate practice group. Justin Radell is an associate at the firm’s Los Angeles office and is a member of the Corporate practice group. Their respective emails are [jkaufer@akingump.com](mailto:jkaufer@akingump.com) and [jradell@akingump.com](mailto:jradell@akingump.com).

“Keeping Current: Corporate Governance: Standards of Review, Officer Fiduciary Duties, and Shareholder Ratification,” by Julie Kaufer and Justin Radell, 2009, *Business Law Today*, 18:5. Copyright 2009 © by the American Bar Association. Reproduced with permission. All rights reserved. This information or any portion thereof may not be copied or disseminated in any form or by any means or stored in an electronic database or retrieval system without the express written consent of the American Bar Association.

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## Business Law

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*By Michael Hutchings*

### • **Standards of Review, Officer Fiduciary Duties, and Shareholder Ratification »**

*By Julie Kaufer and Justin Radell*

### • **2008 Amendments to the Delaware Limited Liability Company Act and Limited Partnership Act**

*By John J. Paschetto*

Featured Author

## 2008 Amendments to the Delaware Limited Liability Company Act and Limited Partnership Act

By John J. Paschetto  
Featured Author

Effective August 1, 2008, the Delaware legislature made several significant amendments to the state's Limited Liability Company Act and Limited Partnership Act. Among other things, the amendments clarified provisions regarding the execution of documents

### *Featured Author*

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Delaware. His practice focuses on governance issues faced by Delaware corporations, limited liability companies, and limited partnerships. He also serves on the committee of the Delaware State Bar Association responsible for proposing amendments to the Delaware Revised Uniform Limited Partnership Act, the Delaware Revised Uniform Partnership Act, and the Delaware Limited Liability

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and effectively enlarged the subject-matter jurisdiction of the Court of Chancery. In addition, effective January 1, 2008, the legislature increased the state's annual franchise tax for limited liability companies (LLCs) and limited partnerships (LPs) from \$200 to \$250.

## Execution of Certificates When Entities Domesticated or Convert

The LLC Act and LP Act permit certain entities to domesticate in Delaware and to convert to Delaware LLCs or LPs. (6 *Del. C.* §§ 18-212 (LLC domestication), 18-214 (LLC conversion), 17-215 (LP domestication), 17-217 (LP conversion).) Domestication and conversion both involve, among other things, the filing of a certificate with the Secretary of State of Delaware.

Before the 2008 amendments, such certificates were to be signed by "1 or more authorized persons" (in the case of an LLC) or by "all general partners" (in the case of an LP; see 6 *Del. C.* § 17-204(a)(1)). The term "authorized persons" as used in the domestication and conversion provisions of the LLC Act had created some uncertainty. The term was frequently understood to mean persons authorized by a Delaware LLC. But in the case of a domestication in Delaware as an LLC or a conversion to a Delaware LLC, the Delaware LLC would not exist until *after* the execution and filing of the appropriate certificate. Similarly, the LP Act's reference to "all general partners" could be problematic because, for example, a corporation converting to an LP would not have general partners until *after* the certificate of conversion was signed and filed.

Those concerns do not arise under the amended LLC and LP Acts. As amended, the sections dealing generally with execution of documents now provide that certificates relating to conversion or domestication may be signed by "any person authorized" by the entity to be converted or domesticated. (6 *Del. C.* §§ 18-204, 17-204.) At the same time, the amendments did not cast doubt on the effectiveness of certificates executed pursuant to the prior texts of the LLC and LP Acts, since the amended provisions retain the option of having certificates executed by "all general partners" or "1 or more authorized persons[.]"

## Chancery Court Jurisdiction over Matters Involving LLC Management

The 2008 amendments effectively expanded the subject-matter jurisdiction of the Delaware Court of Chancery, by making the meaning of "manager" in sections of the LLC Act dealing with jurisdiction consistent with the section on managers' implied consent to service.

Formerly, "any member or manager" had standing to bring a claim in the Court of Chancery regarding the right of a person to be a manager. (6 *Del. C.* § 18-110.) The Court of Chancery also had jurisdiction over any action "to interpret, apply or enforce" the rights or duties of members or managers. (6 *Del. C.* § 18-111.)

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“Manager” was defined, in section 18-101(10), as a person named as a manager in the LLC agreement or pursuant to the LLC agreement.

Thus, persons that were essentially acting as managers but were not named as such could not bring an action in the Court of Chancery under section 18-110 (unless they were also members), and could not have their rights and duties adjudicated by the Court under section 18-111. Moreover, in this respect sections 18-110 and 18-111 differed from section 18-109, under which both managers and persons that materially participate in the management of an LLC are deemed to have consented to service in Delaware in actions relating to the LLC.

As amended, sections 18-110 and 18-111 are now consistent with section 18-109 in their definitions of “manager.” For purposes solely of those sections, the term covers not only a person named as a manager in or pursuant to the LLC agreement, but also any person that “participates materially in the management of” the LLC. The definitions also include a proviso, to the effect that the power to select a manager or participate in the selection of a manager “shall not, by itself, constitute participation in the management of” the LLC.

### **Increase in the Annual Franchise Tax; Other Changes**

The annual franchise tax payable by Delaware LLCs and LPs, and by foreign LLCs and LPs registered in Delaware, was increased from \$200 to \$250 by the 2008 amendments. (6 *Del. C.* §§ 18-1107, 17-1109.) This was the first increase in the annual franchise tax for LLCs and LPs since 2003. (See H.R. 268, 142d Gen. Assembly (Del. 2003).)

Clarification of certain definitions was also effected by the 2008 amendments. Before the amendments, the definition of “limited partnership” and “domestic limited partnership” included the phrase “a partnership formed by 2 or more persons under the laws of the State of Delaware[.]” (6 *Del. C.* § 17-101(9).) This phrase appeared to prohibit the *formation* of a limited partnership by one person (a sole general partner, pursuant to section 17-201), prior to the admission of one or more limited partners and any additional general partners. To exclude that interpretation, the definition was amended to read, in pertinent part, “a partnership formed under the laws of the State of Delaware consisting of two (2) or more persons[.]”

In addition, the definition of “person” was amended in both the LLC Act and the LP Act to make clear that “person” includes all forms of trusts. (6 *Del. C.* §§ 18-101 (12), 17-101(14).) In the definition, the following list of types of trusts was inserted after the word “trust”: “including a common law trust, business trust, statutory trust, voting trust or any other form of trust[.]”

Finally, a new subsection was inserted in section 17-303. That section provides that a limited partner may be liable to third parties for the obligations of the LP if “he or she participates in the control of the business[.]” and it then sets forth a

non-exclusive list of rights and capacities whose exercise or assumption will not, by itself, amount to such participation. Among the capacities in that list was independent contractor, contractor, agent, or employee of the LP or of a general partner, or a fiduciary of an entity that is a general partner. (6 *Del. C.* § 17-303(b)(1).) The 2008 amendments added to the list a subsection providing that the nomination, appointment, election, or removal of the foregoing persons likewise does not constitute participation in the control of the business. (6 *Del. C.* § 17-303(b)(8)n.)

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## Uniformity: The Land of Legal Enchantment

By Eric M. Fish

In a recent issue of *Law Trends*, I introduced you—many for the first time—to the Uniform Law Commission, the entity responsible for writing many of the laws learned during law school and bar review, quickly forgotten in the post bar-exam maelstrom of exhaustion and exuberance, and now relied upon, either directly or indirectly, in one’s daily practice.

This year, the commission convened in Santa Fe, New Mexico, for its 118th Annual Meeting. The meeting was held at the Santa Fe Convention Center from July 9th to July 16th. While the sun soaked the picturesque Sangre de Cristo Mountains, more than 200 commissioners, representing every state, the District of Columbia, the U.S. Virgin Islands, and Puerto Rico were indoors, worked tirelessly at crafting uniform acts that harmonize the wide variations in state law and improve upon current practice.

Central to the Commission’s recent activity are revisions to Article 9 of the Uniform Commercial Code. The Uniform Commercial Code is the Commission’s

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preeminent accomplishment and is under constant review by commissioners to ensure that commercial practices stay current with societal and legal developments. Article 9 was last revised in 1998, modifying the rights and duties of a third party and expanding the scope of the Article. The revisions that were presented in Santa Fe include modifications to the debtor name sufficiency provision, changes which will impact both registered organizations and individual debtor names.

The practice of business law will be impacted by the work of three standing committees. The Business Organizations Act committee drafted language to harmonize common provisions found throughout business organization codes. Their work makes definitions, the mechanics of filing, qualification of foreign entities, and the Model Entity Transactions Act provisions on mergers, interest exchanges, and domestications consistent for the various business organization models. Additionally, the Commission considered the Uniform Statutory Trust Entity Act. Statutory trusts have grown increasingly popular and widely used in the structured finance and the mutual fund industry. The Act modernizes the existing, but outdated, laws governing these entities. Also, amendments to the ABA Model Business Corporation Acts were proposed. The amendments contained within the Uniform Law Enforcement Access to Entity Information Act respond to the recommendations of the Financial Action Task Force that was instituted by the G-7 nations in 1989. The Commission believes that these amendments are consistent with the international imperative to fight money laundering and financing of terrorist activities.

The Uniform Collaborative Law Act was presented for final approval to the Committee of the Whole. Collaborative law is a form of alternative dispute resolution that became popular with family lawyers over twenty years ago and has since expanded to be used in many different practices, including the settlement of contract and insurance disputes. State law governing the practice varies greatly. States regulate collaborative law through a variety of statutes, court rules, and independent boards. The act standardizes the most important features of collaborative law participation, mindful of ethical concerns as well as questions of evidentiary privilege.

Significant modifications to probate, estate, and trust law were discussed. The Uniform Insurance Interests Relating to Trusts Act amends the Uniform Trust Code to address the *Chawla* problem and creates safe harbors for the trustee that are broad enough to apply to all commonly used estate planning mechanisms using life insurance in some way to fund a portion of the trust. The Uniform Partition of Inherited Property Act, presented for the first time to the Committee of the Whole, solves issues related to the pre-partition rights of parties. Additionally, this Act provides wealth and equity protection provisions in the partition sale context. Commissioners also reviewed the final draft of the Uniform Real Property Transfer on Death Act, an act that provides an asset specific mechanism for the nonprobate transfer of land.

Revisions to two previously drafted administrative law acts were debated during

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the week. The Uniform Law on Notarial Acts has been revised to address issues relating to new technologies. The revisions are of a limited scope and relate to notary responsibilities, electronic recording, interstate recognition, and remedies. Likewise, the Model State Administrative Procedures Act has been revised to account for developments in the nationwide system of administrative law judges and to account for 25 years of legislative modification of administrative rule making.

The Commission is recognized primarily for its work in commercial law, the law of business organizations, family law, and the law governing probate and estates. However, this year commissioners reviewed several acts in areas outside the familiar scope of the commission's work. Commissioners entertained uniform acts covering criminal and electoral law, as well as provide implementing statutes for several international conventions.

The Commission has addressed criminal law sporadically throughout its history, such as in the 1930s when it criminalized the tools of terror used by Dillinger, Capone, and Pretty Boy Floyd through the Uniform Handguns Act and the Uniform Machine Gun Act. The two acts that were considered this year do not criminalize behaviors, but standardize state procedures in order to ensure the equitable administration of justice. The Uniform Collateral Consequences of Conviction Act addresses the various penalties and disqualifications that individuals face incidental to criminal sentencing. Throughout the country these disqualifications exclude individuals from certain types of employment, bar the receipt of various public benefits, and place restrictions on voting. The Act does not address the prudence of the disqualifications, but is procedural, clarifying the policies and provisions that are already widely accepted by the states. For the first time, commissioners discussed the Uniform Electronic Recordation of Custodial Interrogations Act. This act addresses the use of audio and/or video electronic devices to during the questioning of individuals in police custody.

Growing interest in electoral reform has driven the Commission to entertain two acts dealing with the electoral process. The drafting committee for the Uniform Military Services and Overseas Civilian Absentee Voters Act has been actively working on an act that provides all eligible voters, no matter their location, the opportunity to exercise their right to vote. Careful study showed that overseas and military voters face a variety of unique challenges in participating in American elections. These challenges remain despite repeated Congressional efforts—most salient being the enactment of the Uniformed and Overseas Citizens Absentee Voting Act of 1986 (UOCAVA)—as well as various state efforts to facilitate these voters' ability to vote. The drafting committee has grappled with the relationship between state and federal election laws and the need to provide an act that maintains the uniqueness of each state's electoral system. The Committee intends for the act to be complete in time for enactment prior to the next presidential election.

Presidential elections are the central focus of another act considered in Santa Fe, the Uniform Faithful Presidential Electors Act. The act addresses the problem of

faithless electors; electors who vote for presidential or vice presidential candidates during the Electoral College that were not the preferred candidates of the party that nominated the elector. Further, the act provides procedures for electors to follow in the occurrence of the death of either a presidential or vice presidential candidate prior to the convening of the Electoral College. Fans of the show *West Wing* should be familiar with the issue, as it was a crucial part of series' conclusion. And although Aaron Sorkin is not on the drafting committee, the commissioners involved with the project would surely welcome the chance to collaborate with him on a solution.

Commissioners considered several acts with international flavor, an indication of the Commission's growing partnership with the U.S. Department of State in connection with the implementation and ratification of private international law treaties. Last year, the Commissioners successfully drafted amendments to the Uniform Interstate Family Support Act (UIFSA) that codified portions of the Hague Convention on the International Recovery of Child Support and Other Forms of Family Maintenance. This year, the Commission considered language that will implement three international agreements; the Hague Convention on Choice of Court Agreements, the UN E-Commerce Convention, and the UN Convention on Independent Guarantees and Stand-by Letters of Credit. The goal is to help the federal government fulfill the international obligations without disrupting the traditional primacy of state law in the affected subject matter areas.

Those interested in reviewing the acts and providing comments to any of their state commissioners can do so by visiting the Commission's website: [www.nccusl.org/Update/AnnualMeeting\\_General.asp](http://www.nccusl.org/Update/AnnualMeeting_General.asp). For a list of commissioners by state, please visit [www.nccusl.org/Update/DesktopDefault.aspx?tabindex=2&tabid=16](http://www.nccusl.org/Update/DesktopDefault.aspx?tabindex=2&tabid=16).

Eric M. Fish serves as a legislative counsel for the Uniform Law Commission based in Chicago. As legislative counsel, Mr. Fish is responsible for providing support to legislators considering uniform acts. He also advises committees drafting future uniform acts. Mr. Fish graduated from the University of Chicago and the Loyola University Chicago School of Law.

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## Preparing and Prosecuting the Patent Application

By Ronald Slusky

“Preparing and Prosecuting the Patent Application” addresses three topics: preparing the specification, responding to claim rejections during prosecution, and working with the inventor. These activities may seem unrelated, but each should be informed by the same notions that inform the analysis and claiming of the invention—the inventive concept, the problem, the solution, and the fallback features.

Chapter Sixteen begins the overall topic of preparing the specification by considering who its audience is and what their needs are. It then focuses on the first two sections of the specification—the Background of the Invention and the Summary of the Invention—and explains how the problem-solution statement can serve as the basis for an effective, storytelling Background and Summary that can engage that audience and, in the process, advance the interests of the patent owner.

## Writing the Background and Summary

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The writing of a patent specification should be guided by the same principles that guide invention analysis and claiming: problem, solution, and inventive concept. Another important consideration is the specification's intended readership.

This chapter begins with a discussion of "the audience" and then focuses in on the specification's Background and Summary. The chapter that follows discusses the Detailed Description.

### The Audience

A patent specification must be detailed enough to enable a person skilled in the art to practice the invention. This is the so-called enablement requirement of 35 U.S.C. 112:

The specification shall contain a written description of the invention . . . [sufficient] to enable any person skilled in the art . . . to make and use the same . . . Enablement is only a minimum legal requirement, however. An effective specification speaks to an audience extending far beyond the person skilled in the art. In fact, although we often say that the audience for the specification is the person skilled in the art, there is no such real-life reader. The person skilled in the art is only a legal construct defining a standard for the specification's required level of detail.

The specification's real-life audience is multifaceted, comprising the patent examiner, the Opposing Team, and possibly a judge and jury. When written with this wider audience in mind, the specification can further the interests of the patent owner in ways that a specification that is minimally enabling may not. Such a specification can facilitate allowance in the Patent Office, make the patent easier to license, and provide an effective platform from which a litigator can argue the merits of the invention to the judge and jury.

In one sense, everything ultimately does come down to the claims. The examiner, for example, is principally focused on ensuring that the claims do not read on the prior art. However, allowance of the claims is helped along when the examiner understands what the invention is and is convinced that there is inventive subject matter to *be* claimed. The specification is the place to convince him of that.

The Opposing Team is also focused on the claims. They want to know whether or not the claims read on their product. But even if the claims do read on the Opposing Team's product, they will resist taking a license unless convinced that their product takes advantage of something novel taught by the patentee. The patent owner's goal is for the Opposing Team to lay down their arms and take a license with as little fuss as possible. They will certainly not do so if they feel they are being asked to pay something for nothing. The specification is a place to convince the Opposing Team that they are *not* being asked to pay something for

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nothing. Judges and juries must decide if the claims are valid and infringed.

But before they hand over millions of dollars to the patent owner, judges and juries want to believe that justice is being done—that the essence of the invention has actually been appropriated by the accused infringer. They are therefore likely to look to the specification to be assured that justice *is* being done. Patent claims are a mystery to most non-patent professionals— a seemingly impenetrable morass of “saids” and “means for.”

The specification should be expressed in “regular” English to encourage judges and juries to try to read and understand it. Indeed, a patent application that is easy to read and understand is more likely to get the attention of a busy judge. A jury convinced that the inventive essence has been appropriated may return a finding of infringement even if the claims somewhat miss the mark.

A specification that achieves all of this is more than just a compendium of technical facts. It tells a story. It is a story of a problem, and of a solution made possible by the patentee’s recognition of something that others did *not* recognize. Ideally, that story is told twice—once in the Background and Summary, as discussed in this chapter, and again in the detailed Description, as discussed in the chapter that follows. Each of the two tellings is built upon and amplifies the problem-solution statement.

## **The Background**

The Background tells the story of a problem that others could not solve, or could solve only partially or only in a complex or expensive way. An effective Background brings the reader to a point of dramatic tension. By the end of the Background, the reader should be thinking two things: “Yes, I see that there is a problem,” and “I wonder how they solved it. Let me read on.”

It is not difficult to construct such a Background, but there are ways to enhance its story-telling effectiveness. These are illustrated both by examples in the discussion below and by a fictional patent for the invention of the chair presented in Appendix C.

## **Begin With the End in Mind**

Chapter Eight alluded to Stephen Covey’s exhortation, “Begin with the End in Mind.” There we were talking about drafting a claim by working backward from the inventive departure. The same idea applies to the Background. Its presentation of the prior art is driven by where the story is headed—the inventive solution. As discussed below, the style of Summary recommended by the author starts out with a one-sentence statement of the inventive solution. This is possible only if the necessary groundwork has been laid in the Background. Indeed, anything that is in the Background should be there because, one way or the other, the Summary relies on its being there.

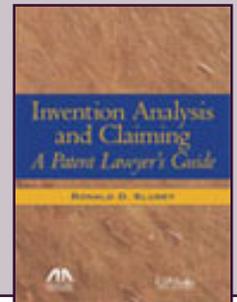
## Keep It Short and Conclusory

The problem is best described at a high level, without a lot of detail. This does not mean skimping on the story line. The Background should provide a full accounting of the problem and how the prior art falls short of solving it. But the technical details of the prior art should be kept to a minimum. The story moves along just fine if the prior art is described only in general terms. The Background best holds the reader's attention when it says as little as needed to make its point.

Ronald Slusky mentored dozens of attorneys in "old school" invention analysis and claiming principles over a 31-year career at Bell Laboratories. He is now in private practice in New York City. This article is adapted from his book *Invention Analysis and Claiming: A Patent Lawyer's Guide* (American Bar Association 2007). His monthly column, *Invention Analysis and Claiming*, appears in *Intellectual Property Today*. Slusky also teaches a two-day seminar based on this book ([www.sluskyseminars.com](http://www.sluskyseminars.com)). He can be reached at 212-246-4546 and [rdslusky@verizon.net](mailto:rdslusky@verizon.net).

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## Tort Liability of Religious Organizations

By Stephen J. Riccardulli, Michael D. Dillon, and Amy S. Beard

### I. Introduction

#### A. Torts and Common Law; Application to Religious Organizations

If someone, through an impermissible act, injures another, that person will be considered to have committed a “tort.” In legal terms, a tort is “a private or civil wrong or injury resulting from the breach of a legal duty that exists by virtue of society’s expectations regarding interpersonal conduct, rather than by contract or other private relationship.”<sup>1</sup> A system of tort law, which provides a civilized method of obtaining legal redress for such injury, has become part of our *common law*. Common law has been developed over time by the courts, as they decide the cases that come before them. Because court cases are only binding in the jurisdiction in which they are located, our common law often evidences jurisdictional or regional differences. In fact, a decision, and thus the law in one jurisdiction, may be completely contrary to a decision in another area. This fact should be kept in mind by any party faced with an issue of tort liability.

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As a general rule, churches and other religious institutions are not immune from tort liability in the modern world. For many years, the courts recognized a “charitable immunity” for certain religious and/or charitable institutions, but there is little left of such an immunity today. This follows the idea that injured parties be compensated for injuries caused by others, regardless of the intent of the actor.<sup>2</sup> For the most part, courts will address wrongs caused by religious organizations in much the same manner as they would any other public or private entity.

### **B. The Demise of Charitable Immunity**

Charitable immunity originated in England in 1846, and was adopted in the United States in 1876.<sup>3</sup> The theories advanced for charitable immunity were varied. A “trust fund” theory held, in essence, that the monies possessed by charities were actually monies held “in trust” by the charity for distribution to others; and, as such, were not available to tort plaintiffs because the donor’s intent would be frustrated, and the operation or existence of the charity compromised.<sup>4</sup> Some jurisdictions recognized an “implied waiver” theory, which held that the beneficiary of a charity impliedly waived his right to sue the same charity for the negligence of its personnel, and assumed the risks of accepting the “benefits” of the aid provided.<sup>5</sup>

Another reason advanced for charitable immunity was that the rule of respondeat superior, whereby a master is liable for the torts of his servants acting within the scope of their employment, did not apply to charities because they derived no gain or benefit of their own for services rendered.<sup>6</sup> Still another rationale was a vague “public policy” argument advocating immunity for charities, but typically adopting one of the other theories as validation for its application.

Charitable and religious organizations were granted immunity from tort liability by most jurisdictions in the United States until 1942, when it was abolished in the District of Columbia in the landmark case of *President and Dirs. of Georgetown College v. Hughes*, 130 F.2d 810 (D.C. Cir. 1942). A large number of states now follow that decision or have otherwise qualified the scope of their charitable immunity law.<sup>7</sup> The change in the law may be attributed to changes in society. By the middle of the 20th century, charity had become “big business” and an exception to the general rule that “liability follows responsibility” no longer made sense.<sup>8</sup> Nevertheless, as stated, some jurisdictions still acknowledge some degree of charitable immunity.<sup>9</sup> Those that still observe a level of charitable immunity may observe the immunity for religious organizations, but not for charitable hospitals; or may abolish the immunity to the extent that the charity is covered by liability insurance, or to the extent that the judgment can be satisfied by funds other than those held “in trust” by the charity. Because of the remaining vestiges of immunity in certain states, any analysis of a tort claim against a religious institution should begin with an examination of the existence of whether there is still any charitable immunity within the relevant jurisdiction.

### **Endnote**

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<sup>1</sup> Barron's Law Dictionary 516 (4th ed. 1996).

<sup>2</sup> See *Lambert v. Bessey*, T. Raym. 421, 83 Eng. Rep. 220 (K.B. 1681) (holding that "in all civil acts, the law doth not so much regard the intent of the actor, as the loss and damage of the party suffering").

<sup>3</sup> See Prosser, Wade & Schwartz, *Torts: Cases and Materials* 634 (10th ed. 2000).

<sup>4</sup> See Restatement (Second) of Torts § 895E, cmt. (c)(1) (1979).

<sup>5</sup> See N.J. Stat. Ann. § 2A: 53A7(a). However, those who are not beneficiaries are not precluded from recovery. See also 25 A.L.R.4th 517 (West 2005) for an outline of which jurisdictions observe a qualified charitable immunity and which do not.

<sup>6</sup> Restatement (Second), *supra* note 214, § 895E, cmt. (c)(2).

<sup>7</sup> See 25 A.L.R.4th 517 (West 2005) (collecting cases). See also Restatement (Second), *supra* note 214, § 895(E) (establishing that "one engaged in a charitable, religious, or benevolent enterprise or activity is not for that reason immune from tort liability").

<sup>8</sup> See, e.g., *Abernathy v. Sisters of Saint Mary's*, 446 S.W.2d 599 (Mo. 1969).

<sup>9</sup> For example, in New Jersey, the Charitable Immunity Act protects any "nonprofit corporation, society or association organized exclusively for religious, charitable or educational purposes" from tort liability arising from negligence. N. J. Stat. Ann. 2A:53A-7 (West 2006); see also *Schultz v. Roman Catholic Archdiocese*, 472 A.2d 531 (N.J. 1984) (dismissing negligent hiring claims based on charitable immunity). Although still law, the N.J. Legislature proposed legislation that would abolish the charitable immunity with respect to claims related to sexual assault or other crimes of a sexual nature. See S. 487, 212 Leg., 2006 Sess. (N.J. 2006).

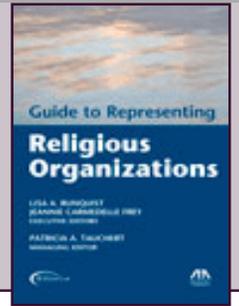
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#### **Note**

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*Guide to Representing Religious Organizations*

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## Real Estate

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## The Answer Really Is Blowing in the Wind

By Kyle Branum  
Featured Author

Historically, wind power was harnessed to operate traditional wind mills that were used for pumping water or grinding sand. Today however, the primary application of wind power throughout the world is the generation of electricity.

According to the World Wind Energy Association, wind currently produces approximately 1.5 percent of worldwide electricity. A recent Department of Energy report suggests that wind could

### Featured Author

#### Kyle Branum

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provide 20 percent of the electricity needs in the United States by 2030 as companies continue to build new transmission infrastructure and as the cost of wind technologies becomes more affordable. A key component to any successful wind farm development is owning or controlling the land required for wind turbines and insuring such real property against financial loss due to title defects, liens, or other encumbrances.

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On average, and given current technologies, most wind farms have an economic life of at least 25 to 30 years. Therefore, most developers do not acquire fee simple title to the property slated for development, but rather acquire long-term ground leases. Ground leases typically provide for a brief initial term (typically 3 to 7 years) with subsequent renewal terms, allowing for a total potential term of approximately 50 years. During the initial term, the developer studies the feasibility of the site including access rights, wind monitoring, permitting issues, and other necessary governmental approvals and consents, and typically pays a fixed rental amount. Once the developer installs wind turbines on the subject property, and such turbines deliver electricity on a commercial basis, the fixed rental amount may adjust to an amount based on their commercial output.

If title to the wind farm property were to fail following the commencement of commercial operations, a developer's losses and defense costs could be substantial and would likely place the entire development in financial jeopardy. Therefore, experienced developers will obtain a search and examination of the title to the wind farm property prior to entering into the ground lease and will purchase a policy of title insurance consistent with the amount of the developer's investment, which may well exceed hundreds of millions of dollars depending on the size of the particular wind farm. Therefore, selecting the appropriate title company is vitally important to the success of the project.

In selecting a title company, a developer should consider the following factors:

- The financial condition of the underwriter. The developer may obtain information from rating agencies and examine annual reports and the underwriter's own internal guides and limits on the size of a policy.
- The title company's resources and pricing in the area where the project will be located. Wind farm developments may span county lines and the ability of a local agent may be limited to providing a search and examination of local records only. The developer therefore should determine if one title company is capable of providing the necessary services for a multiple county project.
- The process for obtaining any necessary endorsements. In the event extended coverage will be obtained, confirm the title company's requirements for such coverage.

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- The flexibility of the title company to add subsequently-acquired properties to the developer's existing title policy. For example, if the developer acquires rights to properties following the issuance of the original title policy, is the title company able to add such properties to the developer's existing policies or will new policies need to be issued?
- The process for increasing the amount of title coverage over the life of the project. For example, will the title company allow the developer to increase the amount of coverage through the purchase of endorsements to the existing policies or will new policies need to be obtained?

One of the key components to the successful development of a wind farm project is selecting the correct title company. Making this determination during the initial stages of development will increase the odds of success for the overall project.

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## Final Rule on RESPA – Part III

By Linda Holder

The Department of Housing and Urban Development (HUD) issued its final rule regarding changes to the Real Estate Settlement Procedures Act (RESPA) in November of 2008. Part I of this article covered changes dealing mostly with the Good Faith Estimate (GFE), which covers estimates of closing costs and disclosures about loan terms. Part II covered tolerances in fee changes, unforeseeable circumstances that allow for changes in fees, enforcement and cure provisions, yield spread premiums, new definition of a mortgage broker, and limits on origination fees. Part III will cover changes to the settlement statement, the closing script, average cost pricing of settlement services, use of affiliates, and technical amendments.

For the HUD-1, the line item descriptions were changed to reflect the same terminology used on the GFE. Further, the HUD-1 now includes line number references that correspond to the appropriate sections of the GFE. All of this was done to make it easier for the consumer to compare the estimated costs with the

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actual charges. In addition, title insurance premiums must now be split out to show the agent's portion and the underwriter's portion of the premium charged. Lastly, a third page was added to the HUD-1 that includes a chart comparing charges from the GFE with the same costs on the HUD-1. This additional page also includes a summarization of loan terms. These changes resulted in the elimination of the proposed closing script. The loan originator is required to provide this information in such a way as to enable the closing agent to prepare the HUD-1 as well as the additional information needed for the new third page.

If a settlement service provider uses the services of a third party on behalf of a seller or borrower where the charge for the service is not based on the loan amount or property value, then the provider may use an "average charge" for that third-party service. This allows a settlement service provider to define a class of transactions based on a period of time, type of loan, and/or geographic area. If an average charge is used, it must be recalculated every six months, and all documents used to calculate the charge must be retained for at least three years after any closing that used the average charge. Further, when using an average charge for a third party service, all transactions within the provider's defined class must use the same average charge for that service. Finally, to ensure this method does not result in higher costs to consumers, the total amount paid to a third party servicer for a particular class of transactions may not exceed the total amount collected from borrowers in that same class.

In the rules that prohibit the required use of an affiliated service provider, HUD made some modifications to the definition of "required use" to better explain HUD's application of the definition. The rule allows service providers to offer discounts to consumers for a bundle of services so long as the bundle is optional and that the discount from the bundle is not made up elsewhere from other charges to the consumer.

A few technical amendments were made as well that involve the transfer of servicing disclosures, aggregate accounting for escrow accounts, and the use of electronic disclosures. The transfer of servicing disclosures will not be included on the new GFEs but the language on the disclosure form has been changed to provide a more comprehensive list of the servicer's functions. The previous regulations regarding aggregate accounting rules contained phase-in provisions that are no longer necessary and have been removed in the final rule. As to electronic methods of disclosure, the final rule makes clear that any disclosures included under RESPA regulations may be made electronically pursuant to the Electronic Signatures in Global and National Commerce Act (ESIGN) (15 U.S.C. 7001-7031).

Linda Holder practices in Granite City, Illinois where she handles real estate transactions, probate matters and business organizations. Ms. Holder is the current chair of the *ABA General Practice, Solo and Small Firm Division Real Estate Law Committee*.

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## The “Credit Crisis” in Commercial Lending and the Effect on Your Real Estate Practice

By Daniel C. Vaughn

The recent “credit crisis” affecting commercial lending might have a profound effect on real estate in the near future. The fallout from the subprime debacle and the sudden collapse of the Commercial Mortgage-Backed Securities (CMBS) market has dramatically changed the lending landscape. Long-term practitioners will recall that most real estate commercial loans were historically made by local and regional banks and life insurance companies: “relationship” lending was the only effective way for borrowers to find the debt capital necessary to buy or build commercial real estate. During the mid-90s, this practice changed. Banks and life insurance companies began to package commercial loans in large mortgage pools, and the interests in these pools were sold as bonds to foreign and domestic investors. This CMBS market, as it became known, maximized the liquidity available to finance commercial real estate. The available liquidity, in turn, led to an efficient or perhaps overly heated market for acquisition and disposition of real estate assets. Prices for commercial property increased significantly, in part

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as a result of available credit. Borrowers and lenders relied far less on relationship lending. Real estate loans became an easily available commodity. Lenders aggressively competed for borrowers. Real estate development and construction activity escalated as construction lenders lent funds in markets with sharply decreasing capitalization rates and a near certainty of “take-out” offered by the CMBS market. For those borrowers that were selling housing lots or condominiums, the “take-out” took the form of appreciating housing markets and ready buyers.

Sudden and recent changes in the housing and CMBS markets, however, have radically altered the core assumptions of the recent past. To provide some perspective, approximately \$200 billion of commercial real estate loans were processed through the CMBS market in 2007. In 2008, less than 10 percent of that figure will occur. The cutback in available liquidity is forcing developers and buyers to scramble as they search for secondary and tertiary lending sources. Portfolio lenders such as banks and life insurance companies do not have the available capital necessary to replace the liquidity shortfall. Such lenders are instead tightening lending standards, extracting higher interest rates, shortening loan terms, and demanding full recourse liability.

It might appear that the subprime and CMBS market problems are irrelevant to the real estate practitioner’s day-to-day practice in Washington State. Fortunately, our part of the country has been insulated from some of the economic contortions affecting other areas of the country. It might be a mistake, however, to assume that new market forces will not impact many of our clients, including the family who owns a highly appreciated piece of property, the homebuilder, the small company looking for construction financing to build a new plant or office, or the classic big-time developer of commercial and multifamily projects. This article will discuss the origins of the CMBS market, describe what is happening to CMBS and the overall real estate lending market, and attempt to offer some practical suggestions to the practitioner who wants to assist real estate borrowers, sellers, and buyers during these tumultuous times.

## The History of the CMBS Market

The CMBS market that developed in the mid-1990s reflected an innovative and sophisticated process to create a national lending market and securitize interests in commercial real estate loans as a liquid investment. Prior to the emergence of the CMBS market, commercial real estate loans were “portfolio” loans originated by a lender (typically a bank or insurance company) and held on the lender’s balance sheet until the loan was paid. The CMBS allowed for securitization of commercial real estate loans. In a CMBS transaction, individual commercial mortgage loans, with different loan amounts secured by different types of property in different locations, are pooled and contributed to a trust. The trust, in turn, issues bonds that typically vary by duration, yield amount and priority of payment. Bond purchasers choose bonds based on a credit risk rating with differing expectations for yield and bond term duration. Investors rely on national rating agencies to allocate credit ratings to the separate bond classes

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issued by the trust. Typically, the trust is created as a real estate mortgage investment conduit (REMIC) that allows pass-through tax treatment. The price for bonds issued in the REMIC generally reflects the understanding that a pool of loans is worth more than the aggregate value of all the loans contributed to the REMIC.

The REMIC structure attracted a wide number of corporate and foreign investors, which led to favorable pricing for borrowers. Many practitioners witnessed the evolution of commercial lending in the past 10 years as loans made for properties in Spokane, Vancouver, Puyallup, and Wenatchee were no longer held by local and regional banks but were immediately transferred to national “loan servicers” located far from Washington State.

Standard underwriting practices, pooling of performing and nonperforming loans across the country, and the securitization of commercial real estate loans to corporate and foreign investors, all characterized the CMBS market. The growth in CMBS was dramatic because of the inherent efficiencies of the loan pooling approach in contrast to historic portfolio lending. In 1995, total commercial real estate loans outstanding were approximately \$1.014 trillion. CMBS represented approximately 5.4 percent. By 2005, total commercial real estate loans outstanding were approximately \$2.618 trillion. CMBS represented 19.9 percent of this total and represented 37 percent of all commercial real estate loans issued in 2005 alone. In fact, from 2004 to 2006, CMBS originations outpaced commercial bank portfolio origination during 12 of 14 quarters. In 2007, there were approximately \$200 billion of newly issued CMBS loans, despite a dramatic drop-off in the last half of the year.

The CMBS market emerged in part as a result of the 1980s Savings and Loan meltdown and the ensuing formation of the Resolution Trust Corporation (RTC). The RTC acquired a significant number of loans and assets from defaulting savings and loan institutions. Wall Street recognized the need for a large amount of capital to liquidate billions of dollars in real estate assets and loans held by the RTC. However, without standard underwriting practices or an official rating system, it was not possible to attract the necessary capital from corporate and foreign investors. As a result, major bond rating agencies and uniform underwriting standards were formulated in the early to mid-1990s, which allowed for the subsequent pooling of mortgage loans and the securitization of the mortgage pools.

As mentioned earlier, most commercial real estate lending in the past was done on a portfolio basis by banks and insurance companies. Most banks, however, faced lending limits tied to the amount of deposits they held and loan allocation requirements imposed by regulators, which restricted the amount of commercial real estate loans a bank could have on its balance sheet. Regulators did not want to repeat the savings and loan fiasco and thus regulated the commercial real estate loan activity of banks. Moreover, because bank loan limits are tied to the amount of deposits held, which deposits are inherently short-term in nature, banks were further limited in the size and term of loans they could hold on their

balance sheets. Accordingly, most banks were able to provide short-term construction financing for real estate borrowers, but were limited in their ability to issue longer-term “permanent” loans. Life insurance companies often played the role of the long-term lender. A life insurance company is not bound by depositary restrictions and is generally in a better position to manage its long-term cash position to issue longer-term loans to borrowers. However, most life insurance companies limit their exposure for real estate loans to approximately 5 percent to 30 percent of total assets. Additional restrictions often include a limit on any individual loan (i.e., not to exceed 1% of aggregate assets).

The inherent restrictions facing banks and life insurance companies effectively limited the total amount of debt capital available to commercial real estate borrowers. Given the limited number of banks and life insurance companies, borrowers were forced to compete by promoting only the higher quality real estate assets, offering personal guaranties and personal balance sheets, and fostering longer-term working relationships with certain banks and life insurance companies. CMBS fundamentally changed the behavior of borrowers and lenders.

Securitized lending, available through the CMBS process, introduced a massive amount of new liquidity available for commercial real estate lending. Banks were in a new position to originate loans and then sell those loans without the restrictions of lending limits based on deposits or regulatory restrictions applicable to portfolio loans. The formation of REMICs essentially allowed nontraditional lenders (such as corporations and foreign investors) to become commercial real estate lenders by purchasing bonds in the new mortgage pools. Loan terms changed dramatically. Banks could make nonrecourse loans. Banks could offer long-term loans (i.e., 10-year loans rather than shorter-term loans) because the REMICs were structured as longer term investments. Banks became sales agents for the CMBS market. Because CMBS fostered a much more efficient process to raise debt capital, borrowers had greater access to available credit. Banks were forced to compete for customers on the basis of slight variations in interest rate spreads and commercial real estate loans became akin to commodities. Life insurance companies created CMBS departments to be competitive with banks selling loans to the CMBS market.

The freely available credit also had a direct impact on the overall real estate market. Buyers with easy access to credit competed with each other to acquire properties on a much more rapid basis. Cap rates plummeted in many parts of the country as the CMBS market matured into a highly efficient source of capital for real estate. Of course, CMBS was not the sole reason for property appreciation, but it was a significant contributor to the increase in value. The timing of real estate transactions changed dramatically as well. Long-term practitioners remember well that many property acquisitions were structured with much longer due diligence and financing periods. Recently, many acquisitions were structured with 30-day due diligence and 30-day closing periods. Financing of late was not much of an issue because the available credit from the CMBS market eliminated many of the inherent delays that were a necessary part of a real estate acquisition. Construction lenders also were more

willing to make construction loans because of the confidence lenders had in the “take-out” chances offered by CMBS. Moreover, the heated real estate market, created in part because of available credit, gave lenders confidence in project valuations as general property values across the country continued to escalate.

## What a Change a Year Can Make

The CMBS market took 10 years to develop and was becoming a predominant source of capital for real estate transactions. In late 2007, the bottom fell out. There are a number of possible explanations for the collapse of the CMBS market, including overly aggressive underwriting, loss of investor faith in the CMBS market’s assessment of project valuation and risk, and fears of repeating the “subprime” mess, but one effect of the collapse is clear: The projected CMBS issuances for 2008 will be less than 10 percent of what occurred in 2007.

During the past few years, the CMBS market began to offer aggressive loan products to feed its accelerated growth. For example, of the aggregate \$723 billion CMBS loans outstanding in 2007, at least 53 percent were interest only loans; 25.6 percent of these loans had a partial interest-only term, and 27.4 percent were interest-only for the full term of the loan. In addition, loan-to-value (LTV) ratios changed during the past few years, with loans often exceeding 80 percent LTV ratios for commercial real estate. Many loans were issued on a ten-year, nonrecourse basis. The loosening underwriting standards occurred as CMBS investors continued to have faith in the increasing property valuations across the country, and banks and life insurance companies competed with the CMBS market for deals. Investors and lenders assumed that property appreciation would resolve any underwriting concerns with project cash-flow, and would offer the most compelling exit strategy for borrowers and lenders. Given years of rapid escalation in property values, this investor and lender optimism was well founded. However, the house of cards could be shaken if commercial banks and CMBS investors lost faith in the core assumption that property valuation escalations were sustainable or even accurate in the first place.

The recent “subprime” mess and the precipitous drop in single-family home values across the country provided the first shock to the CMBS market. The subprime situation is beyond the scope of this article, but few practitioners are unaware of the daily news reports describing dramatic changes in homeowner lending, loss of home values, failing investment houses, etc. Many of the nation’s largest commercial banks were also heavily involved in the residential home loan business and have already suffered enormous losses because of home loan write-downs. Nearly 18 of the top 20 largest lenders currently have significant balance sheet problems because of home loan losses. The sharp downturn in the value of residential housing led in part to increased risk concerns for commercial banks in their underwriting of commercial loans. In fact, commercial bank portfolio lending dropped from \$37 billion in the second quarter of 2007 to \$9 billion in the third quarter of 2007. In addition, regulatory concerns escalated because of bank exposure to residential and commercial real estate.

The sudden loss of residential home values also led to another factor that affected the CMBS market. There is a perception that rating agency assessment of property valuations and risk was inaccurate. The credit rating agencies assessed risk for issuances of home loans packaged in similar pools known as mortgage backed securities or MBS. Part of the “subprime” mess is an overall recalculation of risk assessment for home loans and a general downgrading of MBS issuances. The downgrading that occurred created a general concern that the credit rating agencies were off track in assessing the risk of commercial real estate loans. The perception is that the risk of commercial property loan defaults will occur at a much greater rate than forecasted in the rating agency assessments. Because CMBS investors rely heavily on the credit rating agencies, it is not difficult to imagine a sudden loss of investor interest in CMBS issuances if the investors lose faith in the credit rating agencies and their ability to accurately assess risk.

The combination of bad news offered by the home loan crisis, a tightening of underwriting standards by commercial banks, and an overall unease in the perceived valuations of commercial real estate provided the ingredients for the CMBS collapse. The investors who purchased REMIC bonds issued from the CMBS market suddenly stopped buying.

The full extent of the CMBS and subprime loan problems is not known at this time. What is known is that there is not as much liquidity in the overall market for commercial real estate loans. Loans are harder to find and are far more expensive. For the near term, it is likely that several trends will affect commercial real estate loans. Interest rates have increased in the form of higher spreads charged by lenders. That is why loans are more expensive even though the U.S. Treasury rates have dropped in recent months. For example, it was common in 2007 to find loans with interest rates equal to 90–150 basis points above 10-Year Treasury rates. Today, spreads have jumped to 200–300 basis points and spreads can vary wildly in a day. The higher rates are required to attract investors back to the CMBS market. Banks, however, are unwilling to issue loans based on spread assumptions in an unstable market because they will suffer great losses if they issue a loan with a loan spread that is actually less than required by the CMBS market. Many borrowers will not accept the current spreads because the higher interest rates derail their acquisition pro formas. There is even a wide perception that the demand for CMBS will not occur again for some time. The CMBS collapse is based in large measure on investor loss of confidence in the market’s ability to accurately assess credit risk even though the actual foreclosure and loan loss rates for commercial properties have not increased significantly. The actual loan watch list for loans issued between 2005–2007 (when many “interest-only” loans occurred) has increased recently and there is fear that foreclosures and loan losses are just around the corner. If there is an increase in foreclosures beyond forecasts, the absence of CMBS investors could be long-term.

In addition to the loss of CMBS dollars, real estate borrowers also face loan limits affecting the portfolio lenders. As mentioned earlier, many of the large commercial banks have adverse balance sheet issues that curtail their ability to make additional loans. Commercial banks are also negatively impacted by

regulatory requirements. Many commercial banks must increase their capital reserves for anticipated loan losses, in part because of regulator evaluation of portfolio risk, which is changing quickly in light of the commonly accepted wisdom that property values are decreasing in many markets. A recent change to the Financial Accounting Standards Board (FASB) standards might limit commercial bank lending capacity. The new rule (157) requires that the property securing many commercial real estate loans be valued on a current market basis rather than original appraised value. The more stringent rule could impact capital reserve requirements, which further limits the ability of commercial banks to make loans.

The liquidity shortfall due to the CMBS collapse combined with fewer loan dollars available from commercial banks will mean tougher underwriting standards for any new commercial real estate loans. Interest rates are higher. Loan terms are shorter. Loan to value requirements have increased for many lenders. Full recourse lending is becoming common again as nonrecourse financing options are prohibitively expensive for most borrowers. Property values are flat or declining in many markets, partly because debt financing is far less available and much more expensive.

### **What Effect Does This Have on My Practice, and What Can I Do About It?**

The recommendations described below are my own and based solely on my experiences to date. It may be difficult to see how the macroeconomic forces affecting lending and commercial real estate can affect the day to day lives of practitioners and their clients in Washington State. We seem to be insulated from the severe problems occurring in other parts of the country. I believe, however, that our local market is more linked to the national credit and lending market than in prior years and that many of our clients will be caught off guard by the sudden change in the overall lending environment. We can be helpful by being proactive.

**1. *Dust off the loan documents.*** The practitioner should pull out copies of the loan documents affecting his or her clients and confirm the maturity dates for each loan. Borrowers do not have the luxury of assuming that debt financing is easily available to refinance loans that mature in the next few years. In fact, borrowers should assume that it may take 8–12 months to refinance a commercial loan. The practitioner can be helpful in advising the client well in advance of the impending maturity date and the market changes that may have a dramatic impact on available loan terms. Advising the client well in advance that he or she should expect tougher loan-to-value ratios and shorter loan terms will help the client prepare to raise the additional equity necessary to comply with new lending requirements. Perhaps the client needs to discuss the additional equity requirements with his or her partners. Perhaps the client needs to position the property for sale because the property cannot be refinanced and the client cannot raise additional equity. Perhaps the client needs to work on project performance to increase cash flow to support higher values for property to satisfy

tougher LTV ratio requirements. All of this requires time and the practitioner can really help a client by advising them to work on these approaches far in advance of an impending loan maturity date.

**2. Approach existing lenders early.** Sometimes, lenders are willing to extend loans if a borrower gives them enough notice to process the request in a reasonable manner through their credit committees. This approach does not work for borrowers who already have CMBS loans in an existing mortgage pool but can work for portfolio lenders and construction lenders. Many borrowers today are not able to easily refinance loans and have to seek extensions of their existing loans. Some lenders are using the last minute extension request to demand onerous conditions including increases in interest rate, loan remarking (pay down of a portion of the loan to improve the lender's LTV ratio), and personal recourse. Some lenders are simply refusing last-minute requests because of outside pressures described above that have nothing to do with the underlying property performance. Generally, however, it is wise to resurrect the "relationship" lending approach of several years ago and approach the existing lender early. Discuss the loan maturity date and the refinancing obstacles with the lender. Try to negotiate loan extensions. Many banks are willing to consider loan extensions for a fee or an increase in interest rate. For some clients, the cost is well worth it if they extend the loan to avoid a premature sale of the project or refinancing on terms that will not work well. Many people believe that the crisis affecting the overall lending environment will be worked out over time and that liquidity flow will increase. Many borrowers, however, will be hurt badly by premature sales or adverse refinancing of projects. In fact, if you are helping a client with a new construction loan, encourage the client to add as many loan extensions or "miniperm" options as possible because the client cannot assume that "take-out" financing will be available in the near future. In the recent past, borrowers based construction loan timing on their forecasts of project completion and income stabilization necessary to obtain a permanent loan. Today, borrowers have to also factor credit market uncertainty in that mix and give themselves more time.

**3. Broaden the net.** As commercial real estate lending became more widely available, borrowers had the luxury of viewing loan originators as commodity brokers. Today, borrowers have a much smaller pool of available and willing lenders. The practitioner can help clients by encouraging them to approach many lenders and qualified loan brokers to address their loan requirements. I cannot emphasize enough the level of change in the lending environment. Major lenders that were firmly affixed in the commercial real estate lending business only last year have completely shut down their real estate lending operations. There are some estimates that at least 500 banks across the country will go under in the next year or two. Borrowers can't rely on the lending sources they used in the past. Lenders that are still active in making construction and permanent loans are inundated with loan requests and can be very choosy. The practitioner can again really help the client by facilitating new lender contacts and encouraging the client to sit down with a number of lenders on a face-to-face basis to discuss their lending needs. This can include introductions to new mezzanine debt sources. The aggressive LTV ratio lending offered by commercial banks and

CMBS lenders in the past is gone. Borrowers can still find loans for quality projects with LTV ratios in the 50–60 percent; however, many clients do not have the equity necessary to satisfy the LTV requirements. A practitioner can help by introducing the borrower to new mezzanine debt sources which are developing to help borrowers with the extra equity necessary to obtain debt financing. Of course, mezzanine debt sources can be very expensive but it might be the only available option to borrowers to avoid foreclosure of a project.

**4. *Recourse is here to stay.*** Practitioners should advise clients that they should not assume that nonrecourse financing is easily available. Practitioners should advise clients to properly analyze the effects of recourse liability. For example, many recent permanent loans were nonrecourse and borrowers did not face personal liability for loan loss unless caused by “bad act” reasons such as fraud, misappropriation of insurance or condemnation proceeds, etc. Today, borrowers should consider ways to negotiate recourse liability with lenders. The practitioner can help clients by offering ideas such as partial recourse based on overall net worth or liquid net worth tests, lender requirements to foreclose on the property prior to seeking remedies against a guarantor, and recourse-sharing arrangements among co-owners or partners in the borrowing entity. Long term practitioners dealt with these issues prior to the emergence of the CMBS market and we must resurrect that analysis for recourse loans today.

**5. *Advising property owners and sellers.*** The credit crisis affecting commercial real estate will negatively affect property values. Cap rate reductions in the past few years reflected, in part, easily available credit. The higher cost and unavailability of debt make it much more difficult for buyers to purchase properties based on recent cap rates. Accordingly, cap rates will probably rise. It is unclear if property values will stay flat or decrease in value for an extended period. A practitioner can offer valuable advice to clients owning commercial real estate by recommending strategies to “ride out” the volatility in the credit markets. For example, property owners that have to sell property in the near future will likely not get the price they could if they sold at a time when the credit markets stabilize. Some property owners have to sell because their loans become due. Some property owners have to sell because a family is closing an estate or the partners do not want to pay for a capital improvement. The practitioner can suggest “bridge loan” strategies for these clients to allow them to retain the property for a short time, ride out the credit market volatility and then position the property for sale. There are nearly 700 investment funds for “distressed properties” that have been created recently precisely in anticipation that property owners will have to sell at inopportune times. The practitioner can provide enormous value to a client by assisting them with strategies that avoid sale at an inopportune time.

I am interested in creating a subcommittee for the Washington State Bar Association, Real Property, Probate and Trust Section, to assist bar members with timely market information and information-sharing about the commercial lending crisis. If you have any interest in joining a subcommittee, please let me know.

Daniel C. Vaughn is at the Seattle, Washington, law firm Cairncross & Hempelmann, P.S. Dan received his J.D. from University of Nebraska in 1986 and speaks to many industry and legal groups on matters related to real estate and business law. Dan can be reached at (206) 254-4484 or via email at [DVaughn@cairncross.com](mailto:DVaughn@cairncross.com).

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*By Greg Coffey and Maureen C. Kessler*

## Daily Meditations for Lawyers

By Greg Coffey and Maureen C. Kessler

The field of law is notorious for causing burnout and disillusionment, with many lawyers ultimately finding a loss of meaning and purpose in their lives. There are currently more than a million lawyers in the United States, and many attorneys express professional discontent and are seeking solutions. (Forty-four percent of attorneys surveyed by the ABA said they would not recommend the profession to a young person. *The New York Times*, 1/6/08).

This 376-page, meditation-a-day book is designed to help lawyers recover from spiritual bankruptcy. Each daily entry includes an introductory quotation, followed by a reflection related to that quotation. Each reflection deals with a commonly occurring issue in the lawyer's personal and/or professional life, offering guidance and perspective, as well as concrete action steps for dealing with troublesome matters. The book contains very practical and solid advice, drawn from trusted wisdom literature, enlightened teachers, and the authors' considerable personal and professional experience. Themes found in the book include overcoming fear, defining personal beliefs and values, maintaining integrity, personally defining success, dealing with difficult people, and common workplace challenges.

This is the only book of its kind written just for lawyers. Readers of this important book can reverse the burnout trend, and discover how easy it is to put energy and enthusiasm back into their career with this once-a-day meditation strategy. Lawyers might also appreciate the book as a gift as well. Special bulk

pricing is available from the ABA.

Psychologist Greg Coffey and attorney-minister Maureen C. Kessler have coauthored a book which is sure to be of help to the legal professional. *The Reflective Counselor: Daily Meditations for Lawyers*, published by the American Bar Association, can help pressured attorneys and attorneys-to-be to slow down, look around, and recall the noble impulses that brought them to the world of lawyering in the first place. The book also provides a readily accessible vehicle for the busy professional to find greater joy and meaning in the practice of law.

*The Reflective Counselor: Daily Meditations for Lawyers* will make your own lawyering more enjoyable, and can be a truly meaningful holiday or graduation gift for the lawyer or law student in your life. The book is available on Amazon and at the ABA website ([www.ababooks.org](http://www.ababooks.org): click “Best Sellers”).

Dr. Greg Coffey is a clinical psychologist who has been engaged in therapeutic practice for more than 25 years. Greg creatively utilizes proven cognitive behavioral techniques and short-term therapy to treat depression, anxiety, and all other manifestations of psychological distress and illness. Since 2001, he has been affiliated with Long Island Psychiatric, an organization which applies a team approach (psychiatrist, psychologist, social worker, nurse, art therapist and social skills group leader) in dealing with emotional and behavioral disturbances. Maureen C. Kessler began her legal career as a corporate associate with Kelley, Drye & Warren in New York. In 1980, Maureen joined the Legal Department of Goldman, Sachs & Co., eventually becoming a Vice President and Associate General Counsel. Maureen remained with Goldman Sachs through 2002. While employed as a practicing attorney, Maureen attended Union Theological Seminary on a part-time basis. After graduation in 2001, she was ordained as a minister. Maureen has served as an interim associate pastor, and as a chaplain to the inmates of the Nassau County Correctional Center and the Juvenile Detention Center.

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## Young Lawyers

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*By Bradley S. Shear*

## Civility in Discovery: The Good Faith Conundrum

By Candice A. Garcia-Rodrigo

In this fast-paced world, clients demand results, aggressive attorneys, and, above all, justice. To achieve justice we attorneys must find the essential facts, crucial legal elements, and, most important, evidence. Discovery rules were promulgated with the idea that full, complete disclosure is necessary for the expedient resolution of a case—tell that to the opposing counsel!

As a young lawyer, fresh out of law school where the perfect world existed and good prevailed, you think everyone will follow these rules—it is the law. Discovery is the most important and arguably the most difficult aspect of a civil litigation case. As a plaintiff you are presented with facts from your client, who tells you of supporting evidence that does not appear to be much of anything. Then, the defendant files an answer replete with affirmative defenses, which create new issues and facts requiring additional discovery.

Prior to deciding the path of your case, you decide to propound discovery to pick out the triable issues and facts, and lay to rest the irrelevant or agreed-upon facts. Much to your chagrin, the opposing counsel decides to provide responses containing objections to each and every request, demand, or interrogatory. After overcoming the initial shock of apparent abuse of discovery, you decide to meet and confer on the issues to attempt a resolution outside of court.

## • Past Issues

The California Code of Civil Procedure or Discovery Act requires a meet and confer attempt prior to filing a Motion to Compel Further Responses, but *not* a Motion to Compel Responses (where no responses have been served). Your state's Discovery Act may have comparable meet and confer requirements that you should review when conducting discovery. You also need to confirm whether any time limits exist in filing your motion. In California, if responses are served, then you must file a Motion to Compel Further Responses within 45 days of service. CCP § 2031.310. You need to keep these limits in mind when attempting to meet and confer.

With either motion, it is better that the attorney make at least the minimal effort of sending a letter to the opposing counsel to put them on notice that the responses are due or a motion will be filed. If you know the opposing counsel and have a good working relationship with him or her, then the most efficient method of conferring is by picking up the phone and asking for an ETA of the responses. Whichever route you choose, confirm *everything* in writing; after all, memories fade, people misunderstand, or there may be a miscommunication. It is better to explicitly state the issue in writing to avoid any misunderstandings or miscommunications and support your memory with a tangible confirmation. It may seem like a lot more work, but it saves a lot of misery in the future.

Now, you are faced with three potential results when meeting and conferring:

1. The opposing counsel participates in the meet and confer, and agrees to provide further responses, consisting of compliance or actual responses. Great! Wait for the new responses and hope they are sufficient. If you find deficiencies, then start the meet and confer again, until satisfied. Just make sure you act in good faith and not to harass, annoy, or oppress the opposing party.
2. The opposing counsel ignores your meet and confer attempts. Problem—a motion may be required.
3. The opposing counsel participates in the meet and confer, but tells you the responses will remain “as is.” Biggest problem—a motion to compel should be filed, depending on the legitimacy of the objections, which you should have considered before the meet and confer.

At this point you must make a decision whether to proceed with a Motion to Compel or attempt other means of discovery. In my experience, Motions to Compel Responses or Further Responses are granted 98 percent of the time, as long as the requests are reasonable and the moving party made a *good faith* effort to resolve the discovery disputes prior to filing the motion. However, proceeding with a Motion to Compel may not be in your client's best interests, because the motions increase litigation costs. Make the decision to file the motion *after* you attempt a meet and confer. Most of the time clients do not understand the need and importance of discovery. Take the time to explain it to the client before proceeding with a motion.

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If the meet and confer is not successful, carefully review your discovery requests to ensure they are narrowly tailored, and clearly stated, then draft your Motion to Compel with a declaration from you, as the attorney, explaining the efforts made to informally resolve the issue, in good faith. Regardless of whether or not responses were served to your discovery, a good faith declaration should be filed in every discovery motion. This will not only give you more credibility in the eyes of the court, but it also will strengthen your request for attorneys' fees for preparing the motion. In Southern California, the courts are reluctant to grant more than \$2,000 in attorneys' fees for a motion. Yet, as long as you have that good faith declaration and specify the time spent in preparing for the motion, the court is more than likely to grant your request.

The most important thing to remember in conducting discovery is *good faith*. Act in good faith when propounding discovery, responding to discovery, and participating in a meet and confer. That is the crux of the discovery rules, and a motto to live by in dealing with opposing counsel or parties. Above all, it makes you a more civil attorney.

Candice A. Garcia-Rodrigo is an associate attorney at Betty-Auton Beck, A Professional Law Corporation, in Redlands, California. Her practice focuses on civil litigation and probate.

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## Young Lawyers

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*By Candice A. Garcia-Rodrigo*

. **Planning Checklist for First-Time Entrepreneurs**

*By Bradley S. Shear*

## Planning Checklist for First-Time Entrepreneurs

By Bradley S. Shear

As an attorney who provides outside general counsel services to entrepreneurs and small- to medium-sized companies, I have found my work to be extremely rewarding and intellectually stimulating. I grew up in a family business, so I understand many of my clients' business and legal challenges because I have personally experienced many of them when I operated my family's small business.

During this current recession, I have encountered more first-time entrepreneurs requesting my services than ever before. Most of these clients have never previously started their own businesses and are accidental entrepreneurs. Some of these entrepreneurs have decided to start their own ventures because they are unable to obtain another job in their industry, while others have expressed that they want more control over their professional lives. Either way, many of them do not understand all of the responsibilities that starting a new business entails. When meeting with first time entrepreneurs, I discuss some of the following topics:

### Business Plan

• **Past Issues**

During my initial meeting, I request a copy of the client's business plan because it may offer some information that may not be discussed during our conversation. I advise my clients who do not have a formal business plan to create a concise, one-page memo that clearly identifies the reasons for starting the business, whether it be providing a much-needed service or selling a unique or popular widget and how their business will differentiate from their perceived competitors.

## **Choice of Entity**

Each state has distinct rules regarding the various forms of doing business. There are several different types of entities, and each one has its advantages and disadvantages. Some choices include a sole proprietorship, a partnership, a C corporation, an S corporation, a limited liability company, a limited partnership, and a professional service corporation. It is important to listen to your client's vision for the new venture so you can advise the proper entity type because changing legal entities at a later date may have tax and liability implications.

## **Business Name**

After a business name has been chosen, it should be researched with both your state's licensing department and the U.S. Patent and Trademark Office to see if the name is currently in use by another entity. Your client should also check to see if his desired domain name is available. I have several clients who have chosen their business name based on the availability of a domain name. Consistent branding is very important, so it is advisable to recommend your client obtain a Twitter account, a Facebook account, and any other web service account that pertains to his industry.

## **Employer Identification Number/Federal Tax Identification Number**

The Internal Revenue Service does not require an Employer Identification Number (EIN) for every entity, so it is important to understand the IRS rules to know which entities are required to have one. An EIN number may be obtained online through the IRS website. The type of goods and services your client provides may effect his tax obligations, so I advise my clients to utilize the services of a certified public accountant who can assist them with their accounting and taxes.

## **Permits and Regulatory Licensing**

Many businesses and service professionals need to have some type of permit or a professional license to legally operate. Some industries require federal permits, while others require state and/or local permits as well. Be aware of all pertinent regulatory requirements for your clients because compliance issues may have serious financial and legal consequences.

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## **Location**

Is the venture going to be a home-based business, an online business, a brick and mortar business, or a combination thereof? Local zoning laws may prohibit certain businesses in both residential zoned neighborhoods and in some commercial zoned areas, so it is imperative to know the relevant zoning laws. If your client has a brick and mortar location, you may want to review the lease to ensure that it is flexible enough to fit your client's needs. If your client has a website, you may want to discuss copyright and trademark issues, blogging and defamation issues, website linking, terms of service, and website security issues. Each location has its own set of legal issues that should be proactively addressed.

## **Employees**

Hiring employees creates another set of responsibilities that an entrepreneur must understand. There are numerous federal, state, and local laws that must be followed before, during, and after an employee's affiliation with an entity. Some of these laws pertain to minimum wage, employee benefits, working conditions, and discrimination. The size of the business may determine if certain laws apply.

## **Insurance**

Insurance needs may depend on the type of business and its location. For example, a home-based business may want to consider home-based business insurance because homeowners' insurance policies usually do not cover business-related activities. A brick and mortar entity may want to consider commercial property insurance, general liability insurance, and/or an umbrella policy. A professional services provider may want to consider obtaining errors and omissions/malpractice insurance. Federal or state law may mandate some forms of insurance such as worker's compensation insurance, unemployment insurance, and health insurance. I recommend my clients contact an insurance professional to learn more about which policies best suit their needs.

In the current economic climate, I have noticed that some businesses view reducing or eliminating their insurance coverage as an easy way to reduce their expenses. If my clients have already explored lowering their insurance premiums, I advise them against eliminating their insurance coverage entirely because one incident has the ability to destroy their financial position. Instead, I counsel my clients to look into reducing other office expenses or even their own salaries because these types of reductions usually have only a short-term impact, whereas an uninsured incident has the potential for long-term financial devastation.

## **Address the Important Issues**

Starting your own business can be both exciting and overwhelming at the same time. Addressing the above issues during the initial meeting may help your

clients determine if they have the “right stuff” to become an entrepreneur. Some clients may realize that entrepreneurship is not for them after discussing these issues. Others, however, might think that these new responsibilities sound easy compared to their prior or current situation. In my experience, a more informed client leads to a more successful attorney-client relationship

Bradley S. Shear provides outside general counsel and business consulting services to entrepreneurs and privately held entities. His practice is located in Bethesda, Maryland and he can be reached through his website at [www.shearlegal.com](http://www.shearlegal.com) or by email at [bshear@shearlegal.com](mailto:bshear@shearlegal.com).

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