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ARTICLES

The Trial of the Hidden Agenda: Part I

By T. Ray Guy

The plaintiff was a hedge fund that, along with affiliates controlled by a single investment manager, collectively held one of the largest blocks of stock of the defendant corporation. The complaint filed by the plaintiff in the Court of Chancery of Delaware ostensibly sought an order from the court, pursuant to section 220 of the Delaware Corporation Code, requiring the corporation to turn over books and records for inspection by the hedge fund. A few weeks earlier, the hedge fund and its affiliates had initiated a proxy contest for control of the corporation, and the hedge fund then sent a written demand that the company produce records on a wide variety of subjects. When the corporation refused the demand, the hedge fund filed its suit under section 220.

The statute required the plaintiff to prove that its purpose was a proper one and that the documents sought by its statutory demand were reasonably related to that purpose. Both the hedge fund's written demand for inspection and the subsequently filed complaint recited several purposes that, if true, would have been considered proper. In pretrial discovery, responding to the defendant's request for production, the plaintiff (not surprisingly) did not produce any documentary evidence that would directly contravene its claimed purpose.

The company's primary defense was that the hedge fund did *not* have a proper purpose for the request—that its stated purpose was a ruse and that its actual purpose was to generate publicity for the proxy contest. The company also contended that the request was overbroad, encompassing among other things information already in the possession of the hedge fund or available from other sources.

At trial, the hedge fund shareholder presented one witness, a corporate representative employed by its manager, who predictably testified that the fund's purposes in sending the demand and filing suit were noble: to investigate possible mismanagement at the company, to evaluate potential corrective measures, and to obtain information with which to communicate with stockholders in the proxy contest. He further testified that the books and records for which inspection was requested were related to those purposes. The company obviously could offer no witness as to the state of mind of the hedge fund's decision makers, who had managed to avoid admitting any improper purpose in sending the inspection demand and filing and pursuing the lawsuit.

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So what was the outcome? We'll get back to that. For now, let's look at the concept of ascertaining, and proving, your opposing party's unstated motives—its "hidden agenda."

The Opponent's Motivation as a Trial Theme

Most of us have received, acted upon, or even given the advice that a good trial plan should be built around simple themes. Effective persuasion includes (among other things) reducing the complex to the simple and providing memory devices for the retention of disparate arguments and multiple pieces of evidence. The bits and pieces of your case are more readily remembered by the trier of fact at decision time if they support or relate to a common theme or central idea. On the other hand, powerful demonstrative aids and vivid word pictures can be lost on jurors if we don't enhance their comprehension and retention of facts by relating them to a simple story line or, at most, a few such story lines.

The hardest part of putting such advice into practice is determining the most compelling theme or themes. And your opponent's motivation for the acts that (you claim) provoked the dispute can provide such a theme, a strong framework on which to build your presentation.

The Criminal Trial-Practice Analogue: Motive

Our friends who practice criminal law are no doubt more attuned to this notion than those of us who try civil cases. For them—and for the rest of us who enjoy watching reruns of *Law & Order* or *The Practice* on television—the familiar concept is that of "motive." Distinguished from "intent," motive is rarely an actual element of a crime, but it nonetheless typically occupies a significant amount of the parties' and court's attention in a criminal trial. The obvious reason is that proof that the accused had a strong motive to commit the crime is a powerful persuasive tool in convincing the trier of fact the accused *did* commit the crime; conversely, the absence of such a motive renders the defendant's guilt less likely.

There are several similarities between the concept of "motive" in criminal law and the subject matter of this article—the "hidden agenda" in civil litigation. We'll discuss them in the following paragraphs.

The Search for the Hidden Agenda

Not every trial or arbitration involves a concealed motive. There are, of course, cases in which the dispute involves a genuine disagreement; conflicting but genuinely held memories of the events leading to the dispute; or good-faith belief on the part of each party that its position is correct. Two automobiles collide in an intersection; each driver believes that he or she had the right of way, because, after all, everyone considers himself or herself a careful driver who simply wouldn't have ignored a traffic signal. A once-promising venture fails; each party believes that it has done its best to make it succeed and, therefore, that the failure must necessarily be the fault of the other party. One company manufactures and ships parts that the purchaser contends were

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not suited for the intended use; the manufacturer knows all the steps that were taken on the factory floor to ensure compliance, while the purchaser is equally certain that the goods when received would not fit into the assemblies it planned to ship to its customers, and the case proceeds to trial with each side convinced that its position is right.

And there are other cases in which the defendant's conduct that provoked the lawsuit, litigation, and its subsequent litigating posture were *not* in good faith but did not involve a hidden motive—nothing other than to win, whether at trial or by attrition. To borrow an example from literature, in John Grisham's novel *The Rainmaker*, the defendant Great Benefit Life Insurance Company repeatedly denied claims, but in doing so was not pursuing some concealed aim other than to avoid paying claims. In the automobile-collision case, one motorist may realize that he or she is at fault but persist (through trial and thereafter) in insisting that the light was green with no hidden motive other than to be absolved of deserved liability. The parts supplier may realize that the parts were not satisfactory but contend otherwise just to avoid a ruinous judgment.

However, in three decades of trial practice I've seen many cases in which the dispute leading to the lawsuit resulted from one party's hidden agenda (always my opponent's, naturally). Human conduct is seldom truly random. People generally act or fail to act for cognizable reasons. Choices have consequences, and those choices—including the ones that lead to conflict and ultimately to litigation—often stem from unexpressed, underlying desires or motives. One party is pursuing an unstated goal, a "hidden agenda," that generates the dispute necessitating resolution through litigation or arbitration. Your ability to prevail at trial or in arbitration is significantly enhanced if you can convince the jury or judge or arbitration panel that your opponent's hidden agenda is the *real* reason they're being called on to decide and rule on the issues that divide the parties.

This hidden agenda—an unacknowledged reason why the opposing party acted as it did—is something more than "to make more money" or "to breach the contract." Ferreting it out requires conscious thought, putting yourself in the opposing party's shoes; understanding the forces at work in its world; temporarily assuming, as nearly as possible, the opponent's mindset; and discerning the strategy or goal that caused the opponent, not just to do something adverse to your client, but to do so in precisely the way he or she did.

And *proving* the hidden agenda to the satisfaction of the trier of fact requires marshaling circumstantial proof, typically objective in nature, to demonstrate what your opponent will never admit and what your client isn't competent to testify to: the opponent's intent or state of mind.

Proving the Hidden Agenda: The Section 220 Case Example

In the case described in the opening paragraphs—the stockholder demand for inspection of books and records—the defendant corporation relied on a substantial amount of objective,

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circumstantial evidence that the shareholder had an unstated improper purpose, entirely different from the proffered one, in sending the statutory demand and thereafter in prosecuting its suit. For one thing, the hedge fund's control person had for years served on the defendant company's board of directors, during the entire period when the alleged mismanagement was supposedly occurring. For that matter, in his capacity as a director he had voted to approve most of the transactions that his hedge fund now supposedly wanted to investigate. Many of the categories of documents that the plaintiff purportedly sought to review involved information that had been, or on his request would have been, made available to the plaintiff's control person by virtue of his position as a director.

Further, the plaintiff's letter demanding review of books and records was far lengthier than necessary, with the statement of the alleged purpose and the listing of requested documents occupying only a few of the letter's 24 single-spaced pages. The rest of the demand letter consisted of lurid recitations of supposed wrongdoing on the part of company management, directors, and related parties. A legitimate request for information could have been made in a much shorter letter, shorn of the accusations and allegations. And immediately after sending the statutory demand—and without waiting for a response, which was due five business days later—the plaintiff made its allegations public with a press release and by including the demand as an attachment to filings with the Securities and Exchange Commission (SEC), where they could easily and immediately be accessed online and read by other voting stockholders. Those allegations of corporate misconduct that were superfluous to a legitimate request for information were undeniably germane to an indirect communication to shareholders who would soon vote in the proxy contest. Shortly thereafter, when the hedge fund filed its complaint initiating the lawsuit, it likewise immediately (weeks before an answer was due) attached a copy of the complaint to a press release and concurrently filed it as an attachment to SEC filings on Forms 13D and 14A.

Finally, the hedge fund and its affiliates had for months, both before and after announcing its proxy contest, carried on a publicity campaign through a drumbeat of SEC filings concerning the company, with similar accusations of mismanagement and self-dealing—more than a dozen Forms 13D and 14A during the eight months preceding the sending of the statutory demand. Most of the superfluous accusations in the section 220 demand letter had already been made known to company management and its board of directors through the earlier SEC filings and accompanying press releases, adding to the impression that the demand for inspection was intended primarily for an audience other than its ostensible addressees.

Ultimately, the court of chancery agreed that the hedge fund's actual purpose—its hidden agenda—was not its stated one, and denied any relief. The court ruled that the stated purpose “verge[d] on being a ruse” and that the hedge fund appeared to have pursued its books-and-records demand largely for its utility as a rhetorical platform.

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A section 220 case differs from most trials in that the statute in question places the plaintiff's motive—its intent in sending its demand and filing suit—directly in issue. If the hedge fund's real purpose was its desire to use the court of chancery as a tool in the proxy-fight public-relations campaign, then the hedge fund necessarily did not have a proper purpose for the demand, as required by the statute. In contrast, in most business litigation, the motivation of your opponent in filing suit or provoking the dispute is *not* directly in issue, but the circumstantial proof of an unstated purpose either inferentially rebuts other elements of the opponent's claim or defense, or at least undermines the opponent's credibility.

Proving a Hidden Agenda with Circumstantial Evidence: Proprietary Seed

The above section 220 case illustrates another parallel with proof of motive in criminal cases: the nature of the proof of the opponent's hidden agenda. The opposing party will always control the direct evidence of its intent—testimony from the opponent's mouth or testimony from its corporate representatives—and your opponent cannot be expected to oblige you by admitting its real intentions. You rely on objective but circumstantial evidence pointing to the hidden agenda and on your ability to persuasively argue the inferences that you want the jury or judge or arbitrators to draw from that evidence.

I'll illustrate with another example, one in which the opponent's real intention was *not* an explicit element of its cause of action or of our defense. Several years ago we represented a United States-based producer of proprietary cotton seed in arbitration involving the termination of our client's relationship with its local distributor in another country. During the course of our initial client interviews and subsequent investigation we learned some interesting things about the agricultural-seed industry. Among other things, we learned that there is a difference between "generic" seed and "proprietary" seed. Generic seed is generally available for production and sale by any entity (including governmental agricultural authorities) and is not marketed for any specific benefits or characteristics. Proprietary seed, on the other hand, is marketed under the label of a particular seed company and reflects the company's seed "technology"—its experience in generating and testing new strains of seed—as well as its reputation for seed quality and beneficial characteristics.

Our client, Stoneville Pedigreed Seed Co., had been in existence for more than seven decades and had developed a strong following among cotton planters in the United States. (John Grisham's novel *A Painted House*, set in rural Arkansas in 1951, includes a scene in which the narrator's grandfather is negotiating with migrant laborers for their services harvesting cotton. "'What kinda cotton?' Mr. Spruill asked. 'Stoneville,' my grandfather said. 'The bolls are ready. It'll be easy to pick.'") In the early 1990s, seeking to expand into overseas markets, Stoneville entered into a distributorship agreement with a seed distributor in a European Union country, shortly after the local agricultural authorities removed restrictions on imported cotton seed. As it

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turned out, there was substantial demand among the country's farmers for proprietary seed, and Stoneville's imported seed quickly gained impressive market shares, to the mutual profit of Stoneville and its local distributor. However, the relationship between producer and distributor deteriorated during the later years of their multi-year distributorship agreement. Stoneville became frustrated with (among other things) the distributor's continued failure to send reports of its activities with respect to Stoneville seed, as required by the distributorship agreement, as well as by the distributor's incessant demands for compensation for lost sales and other damages supposedly caused by Stoneville's seed.

A final problem arose when local authorities, at the urging of environmental groups, imposed a temporary ban on imports of seed containing even trace amounts of genetically modified organisms (GMOs). Genetically modified seed is popular here in the United States, where Stoneville produced most of its seed for export and sale. Seed is genetically engineered for a number of purposes, such as making it resistant to a particular pesticide so that the crop will survive when that pesticide is applied to kill weeds. However, overseas markets have been slower to adopt GMO seeds. And because seed grown without deliberate genetic modification is often grown in close proximity to genetically enhanced seed, it is difficult to prevent non-GMO seed from exhibiting minute amounts of GMO characteristics because of natural (wind or animal) transmittal of organisms from nearby fields containing genetically modified seed. The local government's ban was illogical, and it affected imported seed produced by competitors as well as our client—but the local distributor blamed Stoneville for the problem and made clear that it wanted compensation for lost sales.

When Stoneville announced that the distributorship agreement would not be renewed at the end of its primary term, the distributor responded by suing in a local court for more than 100 million Euros—an amount approximating the distributor's total sales of Stoneville seed during the term of its agreement. The complaint sought damages for wrongful termination under local law, as well as compensation for sales lost as the result of the government's anti-GMO fiat.

Fortunately for our client, the distributorship agreement contained an arbitration clause, and thus we were able, by filing and expeditiously prosecuting the arbitration, to accelerate the resolution of the dispute in a neutral forum. As we began working with Stoneville's officers and employees to prepare the case for arbitration, we—client and law firm—expected the dispute to break down into simple, us-versus-them elements: Either Stoneville was entitled to rely on the distributorship agreement's fixed term, or the pro-distributor, anti-termination statutes in the distributor's home country would control and create extra-contractual liability; either our client caused lost sales by failing to prevent adventitious GMO contamination, or neither party was at fault when government officials arbitrarily imposed a new and oppressive interpretation of the governing seed-quality regulations.

However, as we met with our client and reviewed the documents evidencing its contentious relationship with the local distributor—and began to understand some simple facts about the seed industry—another subtext began to emerge, one that involved something unique about the seed industry. Like other plants, when cotton plants grow, they do not just produce cotton fiber; they also produce more cotton seed. The company that gins the cotton can, if it chooses (and is permitted) to do so, separate the seeds from the ginned cotton and resell them. During the term of the distributorship agreement, the local distributor built facilities for ginning cotton and concurrent seed production; the distributorship agreement permitted the distributor to produce limited amounts of second-generation seed—processed from cotton grown from imported Stoneville first-generation seed—as a hedge against Stoneville’s potential weather-related inability to supply the country’s demand for seed. The agreement obligated the distributor to report its sales of locally produced seed and to pay royalties on such sales. Stoneville was aware that the distributor had built and equipped a seed-processing plant, and Stoneville had actually sent employees overseas to assist the distributor in readying its plant for production. But over the years, as Stoneville repeatedly asked for reports of the distributor’s local production of seed, the distributor consistently denied that any such sales had occurred, proffering a variety of excuses: Weather destroyed the entire crop, for example, or the plant malfunctioned and ruined an entire run of seed.

What we noticed as we reviewed sales records was that the distributor’s purchases of seed exported by Stoneville—which increased dramatically during the early years of the agreement—had declined during the later years. We further found that when the GMO controversy arose, blocking import of most of Stoneville’s seed, the distributor nevertheless seemed able to meet farmers’ demand for Stoneville seed. Finally, as the term of the agreement came to an end, the distributor seemed to have on hand an inventory of Stoneville’s seed that did not match its purchases of imported seed—and the distributor began brazenly advertising locally produced Stoneville seed for sale, even touting it to farmers and local dealers as being superior to imported seed (including Stoneville imported seed) because of the absence of any inadvertent GMO contamination!

In short, we determined that our opponent, which claimed to have been devastated and grievously harmed when our client announced that it would not renew the distributorship relationship, had for years been pursuing a hidden agenda: producing and stockpiling inventories of second-generation Stoneville seed. The distributor, while asserting consistent crop or production failures and failing to report to Stoneville its production and sales of locally produced seed, had in fact been successfully producing seed, meeting a portion of its dealers’ demand with locally grown seed and concurrently multiplying its stockpiles. It appeared that the distributor had planned and prepared for the fully anticipated end of the distributorship agreement, when it would be able to meet market demand for product bearing our client’s proprietary-seed technology without having to pay for it.

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The hidden agenda became our theme for the arbitration. While we still had to defend against the distributor's various claims of Stoneville's supposed nonperformance, our overriding theme was that the distributorship relationship did not end when Stoneville announced that the agreement would not be extended beyond the primary term. Rather, it came to an end gradually, over a period of years, as our opponent cheated and lied to our client while preparing in stealth for a post-termination future.

As discussed above—and as is typical in “hidden agenda” cases—our proof was circumstantial; the distributor's witnesses vehemently denied any wrongdoing, and we had no admissions or other direct evidence that the distributor had been appropriating Stoneville's seed technology while planning for termination. The circumstantial evidence was objective, primarily numerical, in nature. Stoneville had of course kept records of the foreign distributor's annual purchases of imported Stoneville seed. The stagnation and decline in such purchases was suspect, given proof from other sources that the demand among the country's farmers for imported proprietary seed continued strong throughout the term of the agreement. Further, however, on our motion the arbitral tribunal ordered the distributor to produce its records of sales of Stoneville seed within its territory. Such sales *increased* steadily even as the distributor's imports of Stoneville seed *declined*. The gap between imports and sales could only have been filled by seed produced in the distributor's local facilities, collected during ginning of cotton plants grown from imported seed—even while the distributor claimed to have produced little or no seed, paid little or no royalties, and took steps to undermine Stoneville's reputation in the country in anticipation of the expected end of the term of the distributorship agreement.

After an evidentiary hearing, the arbitral tribunal ruled that the distributor had breached the distributorship agreement and that Stoneville had not done so—and scheduled a further hearing, several months later, to determine the damage suffered by Stoneville from the distributor's breach. The case settled in the interim. I am convinced that Stoneville was in the right and deserved to win. I am also of the firm belief, however, that the victory resulted in part from the mutual decision of client and lawyers to focus our case on the faithless distributor's hidden agenda—its intention to appropriate Stoneville's proprietary seed and market it as its own following termination—instead of simply reacting and responding to the distributor's unfounded claims.

To Be Continued

The next issue of this newsletter will feature Part II of this article, containing an additional case example involving a hidden agenda and setting out four lessons to remember in presenting and proving your opponent's hidden agenda:

1. Don't lose sight of the explicit elements of your claims or defenses.

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2. Don't assume an unnecessary burden of proof.
3. Marshal your circumstantial proof.
4. Determine the best time to raise the hidden agenda and the best way to do so.

Keywords: in-house counsel, criminal litigation, motive, proprietary seed

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Tuning In with Bob Donohoo, RadioShack's General Counsel

By Zachary Newman

Associate Editor Zachary Newman sat down with Bob Donohoo, general counsel of RadioShack. Bob's responsibilities include legal oversight over the nearly 7,200 retail locations internationally that offer electronic products, accessories, and services.

Bob graduated from Texas Tech University in 1984 with a BBA in accounting, and received a master's of science in accounting, specializing in taxation in 1985. After a stint with Arthur Andersen, Bob attended St. Mary's University School of Law and graduated in 1991.

Bob took time out during the busy holiday season to discuss all things in-house.

How long have you been with RadioShack?

I have been with RadioShack a little over four years. Before joining RadioShack, I worked with i2 Technologies and EF Johnson. Before making the move in-house, I was associated with Shannon Gracey Ratliff & Miller, which had at the time about 100 lawyers. I practiced corporate law, negotiated contracts, and even had the chance to do some litigation.

A corporate lawyer with litigation experience?

Yes, it actually helped provide me with a valuable perspective of how issues evolve in the courtroom, a perspective difficult to possess without being involved firsthand. I even tried four cases as an associate. While the amounts in dispute were not large, I did get to pick juries and try the cases. I even remember the one where an 18-year old pro se litigant beat me hands down in a collection case. It's a long story. . . .

How is your legal department structured?

We have nine lawyers here in our Fort Worth headquarters and five additional lawyers stationed in Mexico supporting operations there. We also have about 10 support personnel in the form of administrative personnel or paralegals.

Our legal department is divided generally in four groups: Intellectual Property, Commercial (meaning contracts and related items), Litigation, and Mexico Operations. As the company's corporate secretary, I also supervise the assistant corporate secretary to fulfill my corporate governance and SEC reporting responsibilities.

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Lawyers do not always exhibit or employ exemplary management abilities. If you were giving a seminar to lawyers on your management style, what would it look like?

As general counsel, it is my responsibility is to enable our lawyers and support staff to perform efficiently and effectively. To this end, I promote the team concept and I have an open-door policy. I also welcome, and encourage, free-flowing communication to permit the exchange of innovative ideas and solutions. We obviously have rules and procedures, but I try to avoid imposing a rigid corporate environment.

Let's get to the important stuff—are you a Tony Romo fan?

At times I am. He can be extremely frustrating to watch, but he is brilliant at times. You brought it up; I didn't.

If a newly minted lawyer interested in an in-house position asks you whether he or she should work in a firm first, how would you respond?

I would say definitely. I believe the intensity and workload of a private law firm as well as the diversity of work available provide invaluable training grounds. The law firms do a very good job of teaching young lawyers how to service clients, which are invaluable lessons as in-house counsel are inextricably intertwined with their clients. We support our clients each and every day, and we are committed to ensuring that business operations are not impeded with unresolved legal issues.

True or False: Litigators are better lawyers than corporate lawyers.

False. It is a good question because each group thinks they are better lawyers than the other. But, truthfully, each practice area complements each other.

What is your general view of litigators?

I have had very positive experience with litigators throughout the country. The only caution I would give to the litigators is to remember that there is a forest beyond the trees. I have noticed that sometimes the litigators become so embroiled in the fight that they lose focus on achieving the client's goals.

How do you stay organized?

I actually manage my own calendar and I maintain a to-do list in a notebook. Of course, what I think I am going to do during the day and what I actually do is very different. It will be a difficult day in my position if I am not exceedingly flexible in my schedule.

I would have figured you had all the latest in electronic data management, using one of many tablets on the market now for example?

I do have an iPad and an iPhone. But I actually get more mileage out of maintaining a written to-do list.

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Time to take the gloves off: What state has the best lawyers—it is New York, right?

Truthfully, it depends on the type of work involved. For example, while New York has exceptional securities and corporate lawyers, I have found top-class lawyers throughout the country. And, with respect to litigation, I strive to forge relationships with local litigators. In fact, each town and smaller city has proven to have top-notch litigation counsel.

What can outside counsel do that will sour the relationship with you?

The one thing that causes in-house counsel to scratch their heads is when firms raise their rates without consulting us first. I must be reading a different newspaper than what those firms are reading. I strongly suggest the law firms contact their clients and discuss the need or intention to raise rates before doing so in the invoice. There is one other pet peeve I have. I find it particularly frustrating when you end up litigating right up to trial only to have your trial counsel express for the first time that a settlement might be more appropriate. This goes back to the forest-from-the-trees comment earlier and my recommendation to outside firms to keep the client's goals and objectives firmly in mind at all stages of the litigation.

Many law firms move associates up each year in the billing rate structure—does the yearly step-up bother you?

No, that does not offend me. I fully understand the need to elevate associates up the ranks, and appreciate the law firm's model of leveraging associates. The raise in the rates I mentioned was more of an unexplained or unexpected bump-up in rates.

What is the best way to communicate the pitfalls of electronic communications to the business employees?

Constant training and discussions about the appropriate use of email and the fact that emails oftentimes become key business records. Because business communications are so dependent these days on email, you need to constantly remind the business folks to be mindful of what they write in email and to express what they mean unambiguously with non-inflammatory language.

Suppose you have a very senior manager, as opposed to a mid-level or junior manager, who is communicating inappropriately by email. How do you best handle this situation to respect the chain of command and to deal with the issue?

You have to address the situation regardless of the seniority of the individual. Involve your human resource professionals and deal with the issue directly and without delay. Also consider consulting with any outside directors that may sit on the board if additional support or consultation is required.

What advice would you give to small, regional firms that are looking to introduce themselves to companies like RadioShack?

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I am very open to retaining smaller firms and always interested in determining whether regional firms are more efficient or capable than larger, national firms. Smaller or regional firms also have shown to be wealthy in “local” knowledge especially in the litigation context. That said, larger, national firms also have many positives so it really just boils down to which firm is better positioned for the particular matter to deliver capability, knowledge, and efficiency.

I constantly evaluate the availability of alternative billing arrangements, which, for me, seems to be more successful in corporate matters. I still am struggling to find a solution for litigation and other matters.

Be honest—what is the last thing you purchased from RadioShack?

I purchased a case for my iPhone.

Keywords: in-house counsel, litigation, management, electronic communications, Tony Romo

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Using Experts to Expedite Document Review

By Amy Romo-Loomis and Holly Dixon

With electronic discovery and document review playing a significant role in litigation, the search for a more efficient and cost-effective approach to controlling cost and managing cases is paramount. Advances in technology and the use of electronic-discovery experts can reduce the number of documents requiring review on a case-by-case basis. Using both technology and experts in the initial stages of the litigation process results in a more concise and cost-effective review, specifically, the use of experts with both subject-matter expertise and review experience.

E-discovery entails many players with expertise in multiple disciplines including identification, preservation, collection, processing, review, and electronically stored information (ESI) production. With the advance of technology and the changing rules of civil procedure such as the broad and varied interpretations of Federal Rule of Evidence 502 (FRE 502), no one is immune from sanctions and malpractice. The case of *J-M Manufacturing Co. Inc. v. McDermott Will & Emery*, filed on June 2, 2011, in Los Angeles Superior Court (Case BC462832) is a good example. The central complaint of this suit is the allegation that McDermott failed to properly supervise its staff attorneys and the electronic-discovery efforts of its client J-M Manufacturing, which resulted in the inadvertent disclosure of privileged information. Additionally, the suit was amended to include that the contract attorneys negligently performed their document-review duties. McDermott produced 250,000 documents, which included almost 4,000 privileged documents. This lawsuit serves as a good illustration of what can happen when counsel fails to be realistic about what is required to oversee a defensible e-discovery process.

If you've ever played the telephone game, you know it doesn't take more than one exchange to lose the meaning of the original message. Dealing with a variety of service providers presents the opportunity for confusion and disorder. Because the production process evolves as the documents are analyzed, there is often a need to adjust and make changes to the original plan. Change to even one step in the discovery process will affect every other step along the way. Failing to communicate consistently with every vendor involved can be catastrophic to the production. An example of this might be a case in which midway through a review it is discovered that there is a key piece of confidential information that now requires a privileged marking. This change will require that any document previously reviewed be flagged for new key terms and placed back into the review. All vendors will need to be made aware of this new protocol in a manner that is consistent with counsel's new instruction. Furthermore, the production team will need to be put on notice as to how this change will impact Bates stamps, confidential/privileged stamps, and any other production requirements. This is just an example of

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one change; the average e-discovery process will have multiple changes through the life of the project. The notification process must be repeated with the same level of consistency for every change made during the course of the discovery process to ensure accurate results. Investing in a single vendor provides one source of information and accountability from planning through production, a consistent communication protocol, and faster turnaround time.

Because document review is the most time-intensive and costly phase of the process, using current technology to reduce the size of the document collection is a good place to start. There are currently many tools on the market to manage, search, and cull ESI. Some of the most commonly used tools provide options such as predictive coding, de-duplication, near-duplication, concept searching, and email threading. Unfortunately, having experience in litigation does not give rise to expertise with these tools and their proper application. A specific type of technology may not be suited to a particular case, thus experts who are experienced with these tools and the best practices for using them on a case-by-case basis will reduce exposure to sanctions and significantly cut costs. Proper use of current technology can lessen the size of a document collection by targeting specific documents required for production, thereby minimizing the scope of the review. This concise collection of documents can now be reviewed by a small group of professionals.

Document review provides value beyond the mere categorization of documents as relevant or not relevant and the application of issue coding. The quality of document review is directly proportional to the experience of the team leading and performing it. A review team made up of specialists with both subject-matter expertise and review experience will not only lessen the amount of time and cost spent on review but also increase the consistency and accuracy of the results. The use of expert reviewers provides many advantages:

- **Professionalism.** Expert reviewers provide a level of professionalism acquired from experience in the field. Unseasoned reviewers do not have a sense of their value and indispensability to the project. They are more likely to quit before the project is complete, thus creating the need to hire and train another reviewer when the timeline is often at its most crucial.
- **Confidence.** An expert is confident in his or her review ability and does not require as much validation in the decision-making process. He or she can be relied upon to process instructions with ease and provide a desired output with consistency.
- **Attention to Detail.** A veteran reviewer will quickly recognize issues and bring them to the attention of those leading the review, allowing them to make adjustments that can save time and money. Some issues that may be found include problems with the review platform, identification of fundamental players, and variations in key terms unforeseen at the start of the review.

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- **Adaptability.** Seasoned reviewers are able to make timely changes to their review method during the review based on new information provided by counsel. A major change to instructions or logic does not require a reevaluation of their entire routine; they can absorb the process and apply new information with ease. They will adjust quickly, discarding old information no longer applicable.

- **Perspective.** Experts in review or subject matter can hit the ground running and become familiar with the document collection faster because they won't have to overcome a learning curve. They are able to determine quickly whether documents require a detailed or cursory assessment, increasing the speed of the review. Subject-matter professionals can easily navigate the issues, because they have training in the subject field, its vernacular, and specific nuances. Through analysis these reviewers identify crucial documents that can challenge or validate earlier expectations.

In addition to the above benefits, the efficiency and speed gained will provide counsel with a manageable group of documents to work with and evaluate. Another factor to consider is the consistency of determinations made during review. Every time a document is reviewed by a different individual, the risk of inconsistent markings increases proportionally. Experts can provide a higher level of consistency, and they allow counsel to concentrate on other aspects of litigation and trial preparation.

The advancement of technology in the legal field, particularly as to how and what is gathered, culled, and reviewed, has given discovery a much larger role and effect in litigation. The use of technology to meet discovery obligations has created the opportunity to delve deeper into the facts of a case and create a more complete view of the issues. But with the increased amount of data now available, the likelihood of a privileged document being produced has increased exponentially. With that in mind, FRE 502 was enacted to address this problem. Although Rule 502 has addressed some of the issues, its broad interpretation, particularly in relation to what is deemed "reasonable," has left counsel without any bright-line guidance as to how it will be applied to their client's issues. The use of technology has given counsel the ability to handle discovery in a multitude of ways: keyword searching, sampling, culling, native-document review, etc. These advances help to increase the amount of data one is able to collect, cut the cost of human review, and shorten the amount of time spent on this phase of litigation, but they also bring about many new risks. With recent rulings by the courts regarding inadvertent disclosure under FRE 502, it is not clear how much effort is enough when it comes to document review for privilege. What is clear is that there must be some effort put forth by counsel to manage their electronic-discovery productions and some effort is given deference over no effort in the eyes of the court. Not only should counsel have an understanding of the steps their client's documents are going through to determine privilege but they must be able to explain the progression to the court. With this in mind, the use of technology is not the problem and we should let technology

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move us forward, but to meet privilege preservation standards under FRE 502 it is paramount that quality controls are put in place to mitigate the increased risk of disclosure that it can create. The following is just a sample of some decisions addressing the preservation of privilege and waiver under Rule 502.

In *Relion, Inc. v. Hydra Fuel Cell Corp.*, 2008 U.S. Dist. LEXIS 98400 (D. Or. Dec. 4, 2008), 40 feet of files were collected by the plaintiff's counsel in paper format. These documents were reviewed by the plaintiff's counsel to remove any privileged materials. Subsequent to this review, the defendant's counsel was allowed to select the documents it wanted the plaintiff to produce. The plaintiff's counsel was provided with electronic, text-searchable copies of the documents that counsel for the defendant had selected. Four months after they had produced the documents, the plaintiff asserted that it had inadvertently disclosed documents to the defendant. The court, in making its decision regarding waiver of the documents, provided the following interpretation of Rule 502(b): "[T]he court will find the privilege preserved if the privilege holder has made efforts 'reasonably designed' to protect and preserve the privilege; conversely, the court deems the privilege waived if the privilege holder fails to pursue all reasonable means of preserving the confidentiality of the privileged matter." The court held that the plaintiff had waived the privilege, noting that the plaintiff had many opportunities to review the documents including two additional opportunities when the defendant provided the plaintiff's counsel with the hard copies and electronic, text-searchable copies they had selected, and concluding that the plaintiff did not use "all reasonable means" to preserve privilege.

In *Eden Isle Marina, Inc. v. United States*, 89 Fed. Cl. 480, 508 (2009), a case regarding the inadvertent disclosure of privileged documents under the Freedom of Information Act (FOIA), the court found that the defendant's adequacy of review procedures could not be assessed because the defendant did not adequately describe the privilege-review procedures. The court noted the following: "Here, defendant has provided scant information concerning the screening procedures it employed in connection with plaintiff's FOIA request." The court went on to note that the defendant did not provide any information regarding the scope of the review and whether the documents in question were ever identified as privileged. Additionally, the court pointed out that "all that the court can glean" from the affidavit provided by the defendant is that the documents had been reviewed twice, that the second review took "several weeks," that a specific number of boxes of material had been reviewed, and that a list of withheld documents had been created. The court believed that there was not enough detail provided about the review procedures taken to ensure that privileged documents were not released. The court went on to say that "[w]ithout such information, defendant has not met its burden to demonstrate the adequacy of its efforts to prevent the disclosure of privileged and protected material." Thus, the privileges were waived.

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In *Thorncreek Apartments III, LLC v. Village of Park Forest*, Nos. 08-C-1225, 08-C-0869, 08-C-4303, 2011 U.S. Dist. LEXIS 88281 (N.D. Ill. Aug. 9, 2011), 159 documents were inadvertently disclosed to the plaintiff by the defendant. The defendant, with the use of an outside vendor, reviewed documents loaded into an online database for responsiveness, non-responsiveness, and privilege. After the review was completed, the defendant allowed the plaintiff to review all responsive and non-responsive documents presumably excluding any documents marked privileged. The inadvertent disclosures were discovered when the plaintiff attempted to use two of the privileged documents during a deposition. The parties resolved their dispute over all but six of the documents. The court stated that it “[had] little confidence in the reasonableness” of the defendant’s safeguards when the only information they could provide to the court was that they thought marking a document as privileged would have prevented the vendor from placing it in the production database for the plaintiff to view. The court also noted the defendant’s failure to run any basic checks on the database before it was made available to the plaintiff, that every document the defendant claimed was privileged was produced to the plaintiff’s side, and that it took nine months for the defendants to realize that documents had been inadvertently disclosed. The court held the privileges were waived.

Experts are valuable because they are able to anticipate pitfalls in advance that would likely become larger issues for the e-discovery novice. Having a perspective to see the smallest nuances can prevent costly rework, missed deadlines, and the inadvertent release of privileged information.

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Enterprise Risk Management: Making It Count

By Carolyn Rosenberg and Carl Krasik

Enterprise risk management (ERM) sounds great in theory, but what does it really mean in practice?

As organizations embark on this process, consider the following questions.

What Do We Mean by Enterprise Risk Management?

To some, ERM means protection against a computer crash or terrorist attack. To others, it may mean addressing reputational issues or fallout from losing key product lines to a competitor. Executives' perspectives may vary from what an IT specialist observes.

An overseas subsidiary may perceive risk much differently from domestic-based headquarters.

Note that the term is risk "management," meaning that some risk is inevitable and the key is to manage it. But what may have seemed like a risk at the time—remember Y2K?—may not be a risk today. And our children no doubt have a much better handle on the risks of the future than we do.

How Do We Figure Out What the Risks Are?

Organizations have implemented various approaches; there is no one answer. An ERM program may be part of an internal risk-management group or under the auspices of the legal department, or be the purview of an audit committee or a special committee of the board.

What is helpful is to have an interdisciplinary team identify or vet potential risks—and an appropriate program to combat them. For example, representatives from IT, internal audit, risk and compliance, insurance, operations, and legal, potentially aided by outside consultants or advisers, may be best able to initially identify risks. A process may be as simple as brainstorming and listing them on an easel in a small group meeting. What emerges as a risk may be amazing to the organization. For example, the risk to an organization of key producers leaving or lack of a solid integration plan upon a merger may be just as large as an inadvertent disclosure of customer data. Thinking broadly and deeply about what truly are risks can be eye-opening.

Balancing risks is also difficult. Should the organization focus on risks that are likely to occur but that may have a modest impact, or laser in on the event that, although unlikely, would be devastating if it occurs?

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Healthy debate typically leads to prioritizing risks. Perhaps focus on the top 10 or 15 risks rather than a laundry list of issues that, although worth noting, are not likely to impact the organization in a material way.

Once the smaller group or committee has identified the risks, it's important to verify whether others in the organization agree, or not. Getting input from select or representative constituencies can be helpful when later seeking a "buy-in" to the plan to mitigate risks.

What Do We Do Once We Identify the Risks?

Once the top risks are identified, they should be written down in ways everyone can understand. The goal is then to do something about them. This involves looking at each risk and realistically assessing steps that may reduce risk, and noting who will be responsible for monitoring and implementing these measures. That may involve a group of people in the company or in partnership with legal or other outside advisers. The plan itself should identify the basic steps, even if they involve exploring more about the issue or watching the risk over time.

As an example, one virtually universal concern is the safeguarding of confidential or private information, whether generated internally or brought into the company's possession. The steps taken to mitigate that risk might involve (1) identifying the categories and sources of the information; (2) reviewing legal requirements for protecting the information; (3) identifying client or customer requirements for protecting information; (4) studying practices of those in similar industries or positions; (5) developing an information-management policy; (6) determining any indemnification or insurance issues or protection that may be available; and (7) implementing a preset game plan on how to react if a loss of information actually occurs. Each of those steps may be on a different timeline and may involve tapping a variety of resources. Someone needs to supervise and make sure the pieces are put in play in a manageable time frame.

Some risks may be more urgent than others. Some may have more gradual solutions. For example, if large-scale mergers of foreign operations may create risk, and cultural integration is key, then one response may be to identify integration teams or mentors or secondments to assist on the ground in the epicenters of those transactions.

Companies can also routinely take some measures to potentially mitigate risk. Review of vendor agreements as a whole to minimize inconsistencies or include additional protections (as well as save costs) may be of value. An annual "audit" or review of insurance programs—from directors-and-officers liability to commercial-general-liability insurance to newer data-privacy and cyber-liability policies, and negotiation of coverage enhancements—may cushion exposure.



Analysis of indemnity agreements may provide a better handle on obligations and exposure, as well as reveal gaps between what may be indemnifiable or insurable.

Now Can We Rest?

No. Two additional items are essential: First, the plan needs to be communicated in an appropriate way to those within the organization. The goal is not to use scare tactics. Rather, if done well, the discussion of risk and the steps to implement a plan should instill confidence, not fear, and empower people in the organization to do more. The messaging can be communicated by top management with the help of key leaders in all aspects of the company. Familiarity with and approval of the plan by the board or audit or other committees is extremely useful.

Second, the plan can't sit on the shelf. Reassessment of risks should be done on a regular basis, perhaps every six months. Moreover, communicating changes in risks and progress in implementing risk management need to be reported back to the committee and kept on the front burner of the organization.

Thus, while many in the marketplace may be talking about ERM, organizations that confront the challenges will have a good story to tell, both internally and externally.

Keywords: in-house counsel, ERM, enterprise risk management

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Avoiding Lawsuits over False Advertising on the Internet

By Gary L. Beaver

As the economy continues to stagger, businesses are becoming more aggressive in seeking customers through advertising, which often includes an Internet component. Businesses have become more sophisticated in scrutinizing competitors' Internet advertising and seem less reticent to challenge such advertising. Attorneys specializing in consumer-protection class actions are filing creative pleadings attacking companies for ads that, even if false in insignificant ways, may, in the context of a class action, cost the company posting the ad millions of dollars. Likewise, the Federal Trade Commission (FTC) appears to be taking a more aggressive stance in examining and challenging Internet advertising as it updates its 11-year-old Rules of the Road for Internet advertising.

Recent cases in which either private plaintiffs or the FTC made false-advertising claims in which at least part of the challenged advertising was published on the Internet provide some clues about what not to do. Please note that some of the examples of infringement are of unproven claims; they are provided to show what led to the filing of the lawsuits or what has to be shown to defend the lawsuits.

Don't Just Make Things Up

Boldness is no substitute for good judgment. For example, on April 19, 2011, the FTC announced efforts in federal court to stop 10 operators from using fake news websites to market acai berry weight-loss products. The FTC alleges that the websites are set up to look like legitimate news organizations, make false statements about investigations and weight loss examples, include phony consumer testimonials, and fail to disclose the financial relationship between the site operators and the acai product sellers. Apparently, some even claim the reports on the website come from named, well-known, legitimate news organizations when they were not. It is not hard to guess how this turns out.

Don't Make Claims Without Adequate Substantiation Evidence

This is where most of the friction occurs. Competitors are going to review ads for accuracy. It does not matter if advertisers are deluded true believers or people who have evidence that does not quite make the grade. They must substantiate the claimed wonders of their products and services. How good is the evidence backing up the claims? Is the advertiser puffing or making actionable fact statements? Are there medical or scientific studies or customer surveys that properly support the claim? Are the studies objective? Not surprisingly, many studies provide

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results favorable to the companies/industries that pay for them. Your adversary will attack their credibility. Here are some recent lawsuits in this area:

- Class actions have been filed against athletic shoe companies New Balance and Reebok for claims that just wearing and walking around in their shoes tones leg muscles.
- In March 2011, Power Balance, LLC, agreed to pay more than \$57 million to settle a class-action claim that it falsely advertised on websites that its products improve customers' balance, strength, and flexibility through holograms embedded in bracelets and other products that react to the body's natural energy field.
- General Mills and Yoplait USA, Inc., were denied summary judgment in a consumer class action alleging false advertising about the health benefits of probiotic bacteria in YoPlus yogurt. The case may have been triggered when competitor Dannon filed a complaint with the Better Business Bureau, which then chastised General Mills for the claims. A similar lawsuit is pending against Procter & Gamble regarding its probiotic supplement Align.

The substantiation problem causes special concern with respect to health claims, as those will draw the close scrutiny of competitors, the Food and Drug Administration (FDA), the FTC, and the consumer class-action bar. For example, in December 2010, consumers filed a class action against a Kansas winery for claiming its elderberry juice was a medicinal product with curative properties. The FDA sent a warning letter to the winery four years earlier that its website claims meant the juice was a drug, was misbranded, and could not be sold without FDA approval. The winery apparently ignored the FDA.

Be Cautious and Conservative in Comparative Advertising

Competitors will sue if an ad attacks their products or services, so advertisers need to be able to substantiate the comparison. They may be sued even if they have the substantiation, so they need to budget for legal costs. Lawsuits in this area include the following:

- In January 2011, Jackson Hewitt, Inc., sued H&R Block, Inc., for claiming in a nationwide advertising campaign, including statements on H&R Block websites, that it found errors on two out of three tax returns done by other preparers.
- Even advertising comparing two of a company's own products can lead to a lawsuit. P&G's Gillette was sued for advertising that its Fusion Power razors were superior to its cheaper Fusion manual razor cartridges. However, the lawsuit was dismissed with leave to amend on May 17, 2011.

Don't Throw Mud

In May 2011, a PR firm hired by Facebook tried to plant negative stories about Google with

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newspapers. When one reporter published the effort and the email evidence, the black eye was worn by Facebook, not Google.

Comply with the FTC Endorsements Guidelines

The FTC's guidelines governing endorsements and testimonials in advertisements are not binding law, but they are administrative interpretations that hold great weight in enforcing the FTC Act against deceptive advertising. The guidelines were modified on December 1, 2009. The most significant change is the removal of the 29-year-old safe harbor that allowed a testimonial to describe unusual results from the use of a product or service so long as the testimonial included a disclaimer such as "results not typical." Now, advertisers must have proof that the experience or results described advertising is "representative of what consumers will generally achieve," or the ad must "disclose the generally expected performance in the depicted circumstances."

The guidelines now make it explicit that the FTC can prosecute both advertiser and endorser for making false statements or for failing to disclose material connections between the advertiser and the endorser. Advertisers need to be careful not to publish endorsements from friends, families, or compensated endorsers without full disclosure. An endorser must be a "bona fide" user of the product endorsed and must continue to be a bona fide user of the product for as long as the ad runs. If the celebrity stops using the product, the advertiser must stop using the endorsement.

The FTC is not the only one acting against false endorsements. In 2002, Sony entered into a settlement with the State of Connecticut for using fake "person on the street" interviews in which Sony employees pretended to be moviegoers praising Sony movies that they claimed to have just viewed.

An expert endorsement must be supported by an actual exercise of the expert's expertise in evaluating the product and must include an examination or test of the product at least as extensive as someone with the same level of expertise would normally need to conduct to support the conclusion in the endorsement. The FTC has not added a requirement for peer-reviewed evidence or studies to support a conclusion, but an example the FTC recently added to the guidelines certainly pushes the standard for acceptable expert advertising in that direction.

Advertisers should not manufacture phony endorsements. Posting phony endorsements in online bulletin boards or elsewhere online shows the poster is willing to deliberately mislead the public to enhance sales and, therefore, is not credible with respect to any aspect of its challenged business practices. This is great evidence for a plaintiff.

Don't Trade on a Competitor's Good Will

Trademark and copyright infringements are often a form of false advertising as a company tries

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to use the good will and reputation earned by a competitor's product to either draw consumer attention to its own product or to confuse consumers into thinking its product is somehow associated with the product that is already well regarded. On the Internet, trademarks are used to falsely advertise in many ways, including use of another's trademarks or of slightly misspelled trademarks in domain names or using another's trademarks in keywords or metatags where there is no appropriate use of the trademark in website text. (It is often a fair use to use another's trademark in a comparative ad.) Similarly, copying another's famous products and advertising them as your own can lead to a copyright infringement. Some cases involve both types of infringement; in April 2011, Disney and Hanna-Barbera sued Costume World, Inc., for both types of infringement for selling through Internet websites allegedly infringing costumes based on cartoon characters.

A company should carefully consider how best to protect its products and services through the use of registered trademarks and then regularly search the Internet for any infringing uses of those trademarks. Even if a company's common-law trademarks are not yet registered, it should monitor the Internet for possible infringements. Use cease-and-desist notices to try to stop such abuses. If necessary, escalate to proceedings in federal or state courts or proceedings before the National Advertising Division (NAD), National Arbitration Forum, or World Intellectual Property Organization.

Other Internet Advertising Issues

Survey Evidence

Proving customer confusion if you are challenging a competitor's actions or proving substantiation of consumer preferences stated in your client's advertising are often done by survey. Internet surveys are usually cheaper and faster than other forms of surveys, but there are many inherent weaknesses in their accuracy. You should not compound those weaknesses with skewed questions designed to get the result you want. At some point, you may have to prove in court that it was reasonable to rely on your survey.

Personal Jurisdiction

Not every ad on the Internet can be the basis of a lawsuit in every jurisdiction in which the Internet reaches—that is, all of them. You should understand in which jurisdictions your client can be dragged to court and why. Generally, if a company targets someone or some group in a particular state with advertising or if it does a substantial amount of business of any kind in that state, then it may be subject to jurisdiction in that state.

Use of False-Advertising Claims as Means of Competition

MGA Entertainment, Inc., filed suit in a California federal court against electronic toy competitor Innovation First, Inc., alleging Innovation made false and misleading statements to the public and to retailers that its competitors, including MGA, had stolen design components

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related to a popular toy made by Innovation. MGA’s lawsuit was dismissed for lack of personal jurisdiction. Innovation already has a lawsuit pending in Texas state court against MGA for patent infringement. We should expect to see more allegations like these from companies represented by creative attorneys making close examinations of statements made by their clients’ business competitors on the Internet or elsewhere.

To avoid a lawsuit over false advertising, a company would be well advised to do the following:

- Use a system to review in advance all public statements, including Internet advertising, to identify claims needing substantiation and gather sufficiently reliable substantiation;
- Where appropriate, work with scientists, engineers, and other technical personnel to ensure that they understand the legal standards for substantiation and that marketing personnel understand whether the technical information meets those standards;
- Develop proper survey evidence if it is to be used in advertising; and
- Obtain a legal review of any advertising that makes claims requiring substantiation or that directly criticizes or compares to competitors’ products.

Even if a company does everything right, it may be sued by a competitor who simply does not believe that the company can substantiate its claims or is using litigation as a means of hurting the company’s pocketbook or reputation. All a company can do is try its best to be accurate and be prepared to fight back swiftly and effectively.

Keywords: litigation, commercial, business, false advertising, Internet, substantiation

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NEWS & DEVELOPMENTS

Post-*Nicastro*, Opposite Jurisdiction Outcomes for Foreign Defendant

In summer 2011, the U.S. Supreme Court decided *J. McIntyre Machinery Ltd. v. Nicastro*, 131 S. Ct. 2780 (2011). *Nicastro* dismissed New Jersey state tort claims against J. McIntyre, a British company, finding that J. McIntyre's contacts with New Jersey—which were limited to the sale of the one machine at issue—were insufficient to establish specific jurisdiction. However, *Nicastro* failed to produce a majority opinion and left unresolved whether Justice Brennan's stream-of-commerce theory, first articulated in *Asahi Metal Indus. Co. v. Super. Ct. of Cal., Solano Cnty.*, 480 U.S. 102 (1987), would become obsolete. Indeed, although six justices agreed the claims against J. McIntyre must be dismissed, only four justices outright rejected Justice Brennan's approach and applied Justice O'Connor's *Asahi* opinion, which requires purposeful availment of the forum state and more than mere placement of a product into the stream of commerce. The decision was hailed as a victory for foreign manufacturers but the unresolved spilt between the applicable jurisdiction tests outlined by Justice Brennan and Justice O'Connor has limited its impact.

Most recently, two federal district courts came to differing conclusions with regard to jurisdiction over the same foreign defendant. In *Ainsworth v. Cargotec USA Inc.*, No. 2:10-cv-00236, 2011 WL 4443626 (S.D. Miss. Sept. 23, 2011), a federal district court in Mississippi considered *Nicastro* in a case involving state-tort claims against an Irish forklift manufacturer. The *Ainsworth* court found *Nicastro* to be "rather limited in its applicability" because the Supreme Court majority had "declined to choose between the [Justice Brennan and Justice O'Connor] *Asahi* plurality opinions." Left without clear guidance, *Ainsworth* followed Fifth Circuit precedent and applied Justice Brennan's stream-of-commerce theory to determine that jurisdiction over the foreign defendant was proper.

Conversely—and just one week later—a Kentucky federal district court decided *Lindsey v. Cargotec USA Inc.*, No. 4:09-cv-00071, 2011 WL 4587583 (W.D. Ky. Sept. 29, 2011). *Lindsey* determined that, in light of *Nicastro*, it could not exercise jurisdiction for state-tort claims over the same Irish forklift manufacturer. The *Lindsey* court followed *Nicastro* and prior Sixth Circuit precedent adopting Justice O'Connor's jurisdiction theory from *Asahi*. It also noted many similarities between the foreign defendants in *Nicastro* and *Lindsey*: no physical presence in the forum state, no ownership or use of property in the forum state, no direct shipments to or sales in the forum state. In both *Nicastro* and *Lindsey*, the foreign defendant's contact with the forum state was limited to an independent distributor.

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Cases like these that produce inconsistent results for the same foreign defendant having the same contacts with the forum state highlight the need for the Supreme Court to finally adopt one of the *Asahi* tests. Certainty and predictability in this realm is preferable for both foreign corporations and the domestic ones that deal with them. While it remains to be seen when such a decision will come down, *Nicastro* seems to indicate that the Court is not likely to take another 20-year hiatus from personal jurisdiction. The two tie-breaking justices indicated that they were open to hitting the reset button on this issue if the Court were presented with a case that provides “a better understanding of the relevant contemporary commercial circumstances.”

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Sixth Circuit Strikes Out Class Allegations at Pleadings Stage

Defense attorneys, whether they are in-house litigators or outside counsel, are always looking for creative ways to make early attacks on facially unsustainable class allegations. The Sixth Circuit recently made a strong statement on this front by affirming a district court’s order granting a motion to strike class allegations on the grounds that individual questions raised by the 50 states’ consumer-protection laws predominated over any factual questions common to the proposed class. See *Pilgrim v. Universal Health Card, LLC*, 660 F.3d 943 (6th Cir. 2011).

In *Pilgrim*, the plaintiffs pled a nationwide class against the defendants, alleging that they had deceptively marketed a plan for obtaining discounted health services in violation of the Ohio Consumer Sales Practices Act (the law of one of the defendants’ residences). Rather than await a motion for class certification, one of the defendants moved to strike the class allegations at the responsive pleadings stage. The defendant argued that the law of each individual class member’s state of residence governed his or her claims, such that the laws of all 50 states must be applied and individual issues would predominate over common ones. The district court agreed, struck the class allegations, and dismissed for lack of subject-matter jurisdiction.

The Sixth Circuit affirmed. It agreed that the law where the injury occurred governed each class member’s claim, and that the individual legal questions raised by the 50 states’ laws predominated over any common factual questions. Individual fact issues also plagued the allegations, including regional variations in availability of discounts, a substantial number of apparently satisfied customers in the class, and differences in the defendants’ advertising due to the varying requirements of state consumer-protection laws.

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The Sixth Circuit’s ruling provides an instructive precedent for those who seek to attack class certification on the pleadings, before class discovery in certain instances. While the *Pilgrim* plaintiffs maintained that the court addressed the class issues prematurely and that they should be entitled to class discovery, the Sixth Circuit noted that Federal Rule of Civil Procedure 23(c)(1)(A) contemplates resolution of certification “at an early practicable time,” not necessarily only once class discovery has occurred. Those facing class allegations that require application of all 50 states’ laws or allegations that on their face defy even the possibility of compliance with Rule 23’s predominance and superiority requirements should keep the *Pilgrim* case in mind.

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