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Fact Witness Compensation and Potential Pitfalls for Business Litigators

"The very heart of the judicial system lies in the integrity of the participants…Justice must not be bought or sold."

Although justice must not be bought or sold, a testifying witness — whose testimony may shape or control the outcome of a case — may be appropriately compensated for certain expenses related to giving testimony. Counsel, however, must be careful to sidestep potential pitfalls that may result from witness compensation. Consider the following scenario. Joe Litigator represents Big Corporation in a complex business litigation involving events that occurred approximately ten years ago. No current employee has first-hand knowledge of the facts of the case. However, a former managerial employee, Ima Witness, has extensive knowledge of the controversy. Witness is retired and cannot recall the events without a review of more than a dozen boxes of documents. Numerous meetings with Litigator will also be necessary to prepare Witness for her testimony. The trial presentation will be a disaster if Witness is not well prepared. Witness, however, is not interested in sacrificing her time at the golf course during the day or playing Gin Rummy in the evenings, without being compensated. Additionally, Witness has retired to Florida and is unwilling to travel to the forum state without being compensated for her travel expenses. Witness mentions that the value of her retirement plan has decreased dramatically in the past year given the decline in the

J. Warren Rissier

(Continued on page 2)

INSIDE

NanoTorts: A Brewing Storm of Commerce, Science, and Litigation Risk

"Nanotechnology" has become big business. Global sales of nanotechnology-containing products were estimated at roughly $50 billion for 2006 alone. (luxresearch-inc.com/press/2007-lux-research-nanotech-report-5.pdf). More than 600 consumer products contained nanomaterials as of February 2008, and approximately 3 to 4 new products hit the market each week. (nanotechproject.org/inventories/consumer/) These products originate in at least 20 different countries, including the United States, Canada, Mexico, China, Japan, Korea, Taiwan, Malaysia, Germany, France, Sweden, Italy, Israel and New Zealand. (*Id.*)

At the same time, clouds of concern about nanotechnology's potential risks to human health and the environment are gathering on the horizon. Advocacy groups have already labeled nanotechnology the "next asbestos," and Japanese scientists recently suggested that some nanomaterials may even share the same cancer-causing mechanisms as asbestos fibers. (Atsuya Takagi, *et al.*, "Induction of mesothelioma in p53+/- mouse by intraperitoneal application of multi-wall carbon nanotubule," *J. Toxicol. Sci.* 33:105 (2008).) Meanwhile, calls for greater regulatory efforts to protect workers, consumers, and the environment from the potential dangers of nanomaterials are arising with increasing frequency.

Orlyn "Skip" Lockard III

At this early stage, it is difficult to predict how the collision course between expanding commercial nanotechnology applications and rising fears about potential health and environmental risks will affect the regulatory, toxic tort, and environmental litigation landscapes. It is certain, however, that new rules and regulations engendered by burgeoning toxicology and environmental studies will give rise to a host of compliance issues. Likewise, ongoing scientific research is yielding data that could ultimately be used in claims against businesses that manufacture, use, or sell nanomaterials and nanomaterial-containing products. It is all too easy to envision an emerging world of "nanotorts" involving a range of personal injury, medical monitoring, product liability, and property damage claims.

"Nanotechnology" Defined

The term "nanotechnology" has become commonplace in the news media and popular culture, with a Google search for "nan-

(Continued on page 6)

Continued from page 1

stock market and states that she could be "a lot more helpful" if she is compensated for her time. Witness offers that she will not take payment unless Litigator prevails in the case. The testimony of Witness is relevant to cases pending in numerous jurisdictions across the country.

Witness compensation under such circumstances is fraught with potential pitfalls. Aside from its impact on witness credibility, improper witness compensation may expose counsel to sanctions, suspension, disbarment, and even criminal prosecution under bribery statutes. *See, e.g.*, 18 U.S.C. § 201(c)(2) (2008); *In re PMD Enterprise Inc.*, 215 F. Supp.2d 519, 519 (Dist. N.J. 2002); *People v. Belfor*, 197 P.2d 585 (Colo. 1979); *Florida Bar v. Wohl*, 842 So.2d 811, 816-17 (Sup. Ct. Fl. 2003); *In re Kien*, 372 N.E. 2d 376 (Ill. 1977); *In re Friedman*, 196 A.D. 280 (N.Y. App. 1994). Additionally, a court may exclude the testimony of a witness who has been improperly compensated. *See Golden Door Jewelry Creations, Inc. v. Lloyds Underwriters Non-Marine Ass'n*, 865 F. Supp. 1516, 1519 (S.D. Fla. 1994). Accordingly, it is critical for counsel to carefully analyze applicable law and be aware of the differing standards, depending upon the jurisdiction, for witness compensation.

Gwyn D. Quillen

Witness May Not Be Compensated Contingent Upon The Outcome Or Content Of Her Testimony

Joe Litigator should immediately reject Ima Witness's offer to collect payment only if Litigator prevails in the case. Witness compensation is governed in most states by a version of ABA Model Rules of Professional Conduct Rule 3.4(b) ("Rule 3.4(b)") or its predecessor, ABA Model Code of Professional Responsibility Rule DR 7-109(C) ("DR 7-109 (C)"). Under both Rule 3.4(b) and DR 7-109(C), attorneys may not compensate a witness contingent on the content of her testimony or the outcome of the litigation. California has enacted a version DR 7-109(C), California Rules of Professional Conduct Rule 5-310(B) (2008), which unambiguously provides that: "A [lawyer] shall not directly or indirectly pay, offer to pay, or acquiesce in the payment of compensation to a witness contingent upon the content of the witness's testimony or the outcome of the case." The policy behind this rule is to encourage witnesses to testify truthfully and not tempt them to do otherwise by financial incentives.

Similarly, the statement by Ima Witness — that she could be "a lot more helpful" if she is compensated for her time — should make Litigator nervous. Litigator should clarify Witness's statement to make sure that she referred solely to her ability and willingness to spend time on the matter. Witness must not change the substance of her testimony because she is being compensated. Furthermore, the written agreement with Witness regarding compensation should make clear that she is being compensated for her time and not based on the content of her testimony.

Witness May Be Compensated for Reasonable Out-Of-Pocket Expenses

Joe Litigator and his client, Big Corporation, may generally compensate Ima Witness for reasonable, out-of-pocket expenses she incurs while testifying, and in some jurisdictions while preparing to testify, including her travel expenses from Florida to the forum state. Although there is no explicit list detailing for which expenses Witness may be compensated, the following are expenses that state bar ethics committees and courts have approved when the expenses are incurred incident to testifying:

- Travel expenses
- Mileage expenses
- Parking fees
- Lodging when overnight stay is required
- Attorneys' fees the witness incurs defending a contempt action arising out of the litigation
- A witness's independent counsel fees to advise and protect her of any possible civil or criminal liability relating to her testimony
- Non-refundable vacation deposit forfeited by a witness in order to appear at trial

See, e.g., Hamilton v. General Motors Corp., 490 F.2d 223, 229 (7th Cir. 1973); Del. State Bar Ass'n Comm. on Prof'l Ethics, Op. no 2003-3 (2003) (hereinafter "Delaware Ethics Opinion"); New York County Lawyer's Ass'n of Prof'l Ethics, Formal Op. no 729, as Amended (2000); Philadelphia Bar Ass'n Comm. on Prof'l Guidance, Guidance Op. 94-27 (1997); ABA Comm. on Prof'l Ethics and Grievances, Formal Op. 402 (1996) (hereinafter "ABA Formal Opinion"); New Hamphire Bar Ass'n Ethics Comm., Op. 1992-93/10 (1993); Ill. State Bar Ass'n Comm. on Prof'l Ethics, Op. 87-5 (1988). This list is not intended to be all-inclusive, and counsel should always research the law of the applicable jurisdiction to determine whether these and any other reimbursements are required, permitted, or prohibited. Although the properly reimbursable expenses may vary by state, the ABA Committee on Professional Ethics and Grievances, Formal Opinion 402 (1996), provides that Rule 3.4(b) and DR 7-109(C) should be read broadly. So long as the expense is directly related to Witness's testimony, the expense may generally be reimbursed. However, the compensation must be reasonable and must not affect, even unintentionally, the content of Witness's testimony. Litigator should think carefully about whether he books Witness's hotel room in a luxury suite at the most expensive hotel in town or whether he chooses someplace more modest.

Shannon Ponek

Compensation to Witness for Loss of Time Requires Litigator to Carefully Side Step Pitfalls

Whether, to what extent, and in what amount Joe Litigator and his client, Big Corporation, may compensate Ima Witness for her loss of time requires Litigator to carefully consider the laws of each applicable forum.

The calculation of reasonable compensation is usually straightforward when a witness takes time off work in order to testify. Such a witness should be compensated at her normal rate of pay. However, the amount of reasonable compensation is less clear when a witness is unemployed, retired, or assisting after work or on the weekend. Further, not every forum agrees that a witness may be compensated for time spent *preparing* to testify, in addition to giving her testimony in deposition or at trial.

Whether Joe Litigator may, on behalf of his client, compensate Ima Witness — given her status as a retiree — depends upon the jurisdiction.

On the one hand, the Delaware State Bar Association Committee on Professional Ethics interpreted Rule 3.4(b) — which states only that "[a] lawyer shall not…offer an inducement to a witness that is prohibited by law"— to prohibit paying a retired or unemployed witness for loss of time. Delaware Ethics Opinion, *supra*. In the Delaware Committee's view, this prohibi-

(Continued on Page 3)

tion applies even if counsel merely seeks to compensate the witness at the same rate she was paid when she was last employed by the corporation for whom she is testifying. The Delaware Committee reasons that such payment would be unreasonable because a witness lacking current employment is not losing an economic opportunity by spending time preparing, attending trial, or testifying. Under the view of the Delaware Committee, Ima Witness should be compensated for her time only if it is shown that she has a "present source of income" and taking time as a witness will detract from that income.

On the other hand, the State Bar of California Standing Committee on Professional Responsibility and Conduct, Formal Opinion Number 1997-149 (hereinafter "Cal. Prof'l Resp. Op."), interpreted DR 7-109(C) — which states that "a lawyer may advance, guarantee, or acquiesce in the payment of…[r]easonable compensation to a witness for his loss of time in attending or testifying…" — to allow attorneys to compensate an unemployed witness. The California Committee further stated that, for an unemployed witness, reasonable compensation may be based on the amount the witness last earned. The California Committee reasoned that an unemployed or retired witness should be compensated because she is deprived of time she could otherwise devote to different activities. Thus, in California, Joe Litigator may reasonably compensate Ima Witness for her loss of time even though she is retired and spends her day perfecting her golf game rather than earning a wage. *See, e.g.*, Cal Prof'l Resp. Op., *supra*. Whether Ima Witness may be compensated for time preparing for her testimony, in addition to delivering her deposition or trial testimony, depends upon the jurisdiction.

Because both Rule 3.4(b) and DR 7-109(C) fail to explicitly address compensating a witness for her preparation time, states are left to individually interpret whether compensating a witness for preparation time violates the underlying principle that witness compensation must not be contingent upon the content of the testimony or the outcome of the case.

In Pennsylvania and New Jersey, for example, a witness should only be compensated for attending and testifying in deposition or trial, not preparing for her testimony, *e.g.* for reviewing documents or meeting with counsel. *See Alexander v. Watson*, 128 F.2d 627, 628-30 (4th Cir. 1942); *In re PMD Enterprises, Inc.*, 215 F. Supp. 2d at 529, 532 (D.N.J. 2002); Penn. State Bar Ass'n Comm. on Legal Ethics and Prof'l Resp., Op. No. 95-126A (1995). The Pennsylvania Ethics Committee analyzed the text of Rule 3.4(b) and Pennsylvania's witness compensation statute. The Committee noted that Rule 3.4(b) does not specifically provide for any witness compensation "beyond simply attending and/or testifying," and Pennsylvania's witness compensation statute only specifically provides that a fact witness may be compensated for travel and lodging expenses. Because neither Rule 3.4(b) nor Pennsylvania's witness compensation statute specifies that a fact witness may be compensated for preparation time, the Pennslyvania Ethics Committee concluded that such compensation is improper. Additionally, the Committee reasoned that the policy behind both the rule and the statute is that "a [fact witness] is expected to testify truthfully from recollection and not to render the 'service' of testifying in a prepared fashion." The Committee cautions that such payment, in effect, buys the witness' cooperation. Consequently, in the Pennsylvania Ethics Committee's view, payment for preparatory time undermines the administration of justice.

However, most states, including California, follow the modern trend to allow compensation to witnesses for preparatory time. *See* Cal Prof'l Resp. Op., *supra*; *see also* New York State Bar Ass'n Comm. on Prof'l Ethics, Op. No. 547 (1982). The ABA

(Continued on page 5)

A Quick Overview of Commercial-Damages Economics

Commercial damages occur in breach-of-contract and business-tort cases that result in claims of lost profits or diminished business goodwill or business value. Intellectual-property-infringement cases and antitrust cases also can involve such loss claims. The measurement of damages in these types of cases follows a basic methodology, with some variations in intellectual-property matters. Measurement of damages in securities-fraud cases uses a different approach.

Jules H. Kamin

In any of these cases, if defendant's actions caused a loss to plaintiff, the history of the plaintiff's business, or the price of the stock, after the onset of damages is different than it would have been without these actions. Of course, causation itself is an issue for trial, but any damage analysis must assume causation will be established, whether or not it eventually is. The principle of compensation for damages is to restore the plaintiff to the economic position it would have experienced but for the incident that caused the damages. If restoration is to the economic position the plaintiff reasonably could have expected, measurement of damages requires construction of an economic model that is a reasonable representation of the economic history of the business or the stock price had the defendant's damaging actions not occurred.

Lost Profits

An analysis of lost profits is demarcated by three critical dates: incident, valuation and full mitigation. The incident is the latest event that precipitated the loss. The date of full mitigation of damages is the latest date up to which a loss occurs. The date of full mitigation may precede or follow the valuation date.

Often lost profits results from a decline of sales, after the incident, relative to the trajectory that sales would have followed but for the incident. The plaintiff must exert reasonable efforts to offset the loss and mitigate the damages. Such efforts may result in an increasing trend of actual "with-incident" sales reversing the declining trend. At some subsequent point of time, actual sales may increase sufficiently that profits after that point equal or exceed the profits that would have occurred then and thereafter but for the incident. If so, full mitigation of damages would have been achieved.

An absolute drop of sales may not be necessary to cause lost-profit damages. The incident may have caused the growth trend of sales to decelerate. Another possible source of lost profits is increased costs with no sales decline. This can occur, for example, if a machine's efficiency is misrepresented or if it is defective.

Profits earned after the date of incident are offset against the profits that would have been earned, according to the economic model, but for the incident only if they are earned by resources liberated by the incident. Such profits that may be earned after the date of incident which are derived from other resources are not offset, because their generation is independent of the

(Continued on page 4)

Continued from page 3

incident.

It is possible that the incident damaged the business so severely that full mitigation at any time cannot be reasonably assumed. In that case the business experiences a permanent diminution of value. If the company goes out of business because of the incident, the loss is the full value of the business but for the incident. It may not be possible to determine if full mitigation could be achieved at some future time after the valuation date. In that case, another economic model "with incident" can be used to project a sales trajectory that intersects the but-for-incident trajectory within some reasonably minimum time. The damages so calculated can provided a minimum figure for comparison with damages calculated assuming that full mitigation is unachievable.

Estimation of the but-for-incident sales trajectory after the date of incident requires some economic data that were not affected by the incident but can reasonably be assumed to represent the trajectory that sales would have followed but for the incident. Various data sources may be suitable for this purpose, providing flexibility depending on availability of data. These include: the plaintiff's sales history before the incident; the plaintiff's sales history after full mitigation; the plaintiff's sales history after the incident at other locations; sales of comparable businesses after the incident; the defendant's sales history after the incident; an industry index; plaintiff's projections made before the incident.

Some efficiency in the calculation of lost profits is enabled by division of costs into fixed and variable categories. Fixed costs are insensitive to sales volume, and variable costs are proportional to sales. The quantity that is recoverable for damages is lost net profits. Net profits are sales less cost of goods sold and all expenses. In the calculation of lost net profits, however, fixed costs and expenses are the same but for and with the incident. Therefore lost net profits is equal to what we may call lost "variable" profits, which equals lost sales plus with-incident variable costs less but-for-incident variable costs. With-incident variable costs include extraordinary "out-of-pocket" costs incurred by the plaintiff because of the incident. This analysis enables fixed costs to be ignored in the calculation of lost profits with the same validity as if fixed costs were explicitly considered.

Past lost profits before the valuation date can just be accumulated to a total, but future lost profits must be discounted to present value as of the valuation date. The reason for discounting is that the plaintiff has the opportunity to invest the portion of the damage award corresponding to future losses and to earn a return on investment that would offset the damages. This benefits the defendant, but, if it were not considered, would enable to plaintiff to obtain a double recovery — both compensation for the future loss and the investment return. Since there is risk inherent in the generation of future profits, the discount rate should be consistent with investments of equivalent risk.

Patent Damages

Patent damages are lost profits, but, if they can't be reasonably quantified, at least a reasonable royalty. Special considerations are required for estimating lost revenue beyond the typical case described above. The analysis is guided by the landmark case *Panduit Corp. v. Stahlin Bros. Fibre Works, Inc.*, 575 F.2d 1152 (6th Cir. 1978). This requires demonstration of demand for the infringed product, plaintiff's production and marketing capacity, plaintiff's profit but for infringement, and the effect of substitute products on sales, if any.

The analysis considers whether plaintiff would have charged the same price as defendant on defendant's sales and how the defendant's sales may have caused erosion of plaintiff's price on sales it retained, due to additional competition from defendant. Conversely, plaintiff may not have lost *all* of defendant's sales, but for the infringement, because the higher but-for price may have limited but-for sales. Plaintiff may have also lost "convoyed" sales of unprotected products usually sold because of customers' demand for the patented product. In general there are no future lost profits in a patent case because plaintiff will be awarded an injunction against additional infringement. If the patent is close to expiration, however, defendant's entry before expiration may reduce plaintiff's post-expiration sales and cause future damages.

Panduit defines a reasonable royalty as an amount that would enable the licensee to earn a reasonable profit when viewed from the perspective of the beginning of the infringement. *Panduit* also refers to *Georgia-Pacific Corp. v. U.S Plywood-Champion Papers*, 446 F.2d 295 (2d Cir. 1971) for further guidance. *Georgia-Pacific* states fifteen criteria to consider in estimating a reasonable royalty rate. *Georgia-Pacific's* broadest criterion concerns conducting a hypothetical negotiation as if the parties would have been willing to negotiate a licensing agreement when the infringement first occurred. Apart from the hypothetical negotiation, actual royalties received on the patent in suit, if any, or paid by the infringer on similar products are to be considered. Other criteria concern the specific terms of the license, the patentee's licensing policy and the competitive or complementary business relationship of the parties. The effect of the patented item on convoyed sales is another criterion.

Securities Fraud

Rule 10(b)-5 pursuant to section 10(b) of the 1934 Securities Exchange Act prohibits fraudulent or misleading information in connection with securities transactions. In a buyer's suit, the measure of damages is the purchase price less the lower "true" value per share of the stock. In a seller's suit, the measure of damages is the "true" value less the lower sales price. The time period for calculation of damages is from the date the fraud occurred to the date of discovery. During the damage period, different investors may buy or sell the stock. The damage calculation is based on a "true-value line" that estimates the daily stock price but for the fraud. Daily damages are based on the difference between the estimated true value and the actual stock price.

During each day of the damage period, the estimated true value may be calculated from the estimated true "return" on the stock from the previous day, starting with the last trading day before the damage period. The return is the daily percentage change in the true value of the stock. The daily true returns during the damage period are estimated from a statistical financial model that relates returns on the stock prior to the damage period to returns on a market index (*i.e.*, an average price of a large basket of stocks) such as the S&P 500 and possibly also to returns on an industry index (*i.e.*, an average price of stocks in the same industry as the stock in suit).

Conducting the estimation based on data prior to the damage period excludes the effect of the fraud on the stock price and therefore is assumed to provide a model that can be extrapolated into the damage period to estimate the behavior of the stock price if the fraud had not occurred. The estimated parameters of the statistical model are applied to the actual daily returns on the market and industry indexes during the damage period to estimate the true daily returns on the stock absent the fraud.

The amount of damage each day in the damage period is the discrepancy between the true value and actual price, as estimated using the above methodology, multiplied by the number of shares disadvantageously traded on that day. It is likely, however, to be difficult or impossible to determine the trading behavior of each investor in the stock during the damage period. Therefore the number of shares disadvantageously traded is estimated from published data on aggregate trading volume.

Such a model postulates a different cohort of buyers in each

(Continued on Page 5)

Commercial-Damages Economics

Continued from page 4

day of the damage period. On a given trading day during the damage period, the model calculates the ratio of shares traded to the total number of shares outstanding that is available for trading, the "float." The model assumes that each prior cohort sells this percentage of its current holdings to the current day's cohort. This is called an "equal probability" trading model. By stepping the model through each day of the damage period, it is possible to generate the number of shares purchased and sold by each cohort each day.

For example, if the fraud has inflated the stock's price above its true value, there are damages to purchased shares only if the inflation on the purchase date exceeds that on the sale date or if the shares are held until disclosure of the fraud. For shares not held until disclosure, the damages of each cohort on each day is the inflation on the purchase date less the inflation on the sale date multiplied by the number of shares sold. For shares held until disclosure, the damages of each cohort is the inflation on the purchase date multiplied by the number of shares retained, since disclosure is assumed to reduce inflation to zero. That is, once the fraud is disclosed, it is assumed that market forces cause the share price to converge to its true value.

Several refinements can improve the accuracy of the trading model. It may be possible to determine that a percentage of outstanding shares have a very low probability of trading because they are held by long-term investors. The trading float can be adjusted downward for this percentage. The company may issue or buy shares back during the damage period, thereby affecting the number of outstanding shares. Such changes should be integrated into the trading model. Short sales distort the trading picture because they are borrowed from the cohorts and then sold, giving the appearance that trading among the cohorts is higher than actually by the amount of the short sales. Finally, trading by specialists causes double-counting of those trades, since they are buying and selling from the cohorts. Trading volume should be adjusted down for the percentage accounted for by specialists.

Antitrust

Economic analysis is used in antitrust cases to demonstrate the fact of damages as well as the amount of damages. Measurement of the amount of damages generally follows the lost-profits methodology above. Antitrust law is intended for the protection of consumers from abuses of the free-market system that result in loss of economic efficiency. The Sherman Act prohibits in Section 1 restraint of trade and in Section 2 monopoly in, or attempt to monopolize, a market.

Monopolization is the ability to control price or exclude competition. This is "market power." An economic model of a monopoly market has all of the price-quantity combinations on the downward-sloping demand curve available to the one seller. The monopolist prices where marginal revenue equals marginal cost. In a competitive market characterized by the same demand curve an equilibrium price would be established where the price on the demand curve equals the marginal cost of the least efficient competitor. The monopoly price is higher than the competitive price and the quantity sold is less in the monopoly market than in the competitive market. The higher price and lower quantity in the monopoly market represent an economic injury to the consumers in the market. Proof of the fact of damages requires identification of the relevant product and geographic markets and consideration of several of their economic attributes.

Restraint of trade can be manifested in collusion among competitors to fix prices, divide a market into exclusive sub-markets or establish a boycott. "Tying arrangements" require purchasers to buy a product having a high elasticity of demand together with one having a low elasticity of demand for which the seller has market power. Price discrimination violates the Clayton Act and the Robinson-Patman Act. Price discrimination involves the seller having access to at least two separate markets with market power in one of them. The seller charges a higher price in the low-demand-elasticity market.

Hopefully this brief overview of damages economics will provide a handy reference guide for where to initiate economic analysis in the case types discussed.

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Fact Witness Compensation

Continued from page 3

Committee on Professional Ethics and Grievances states that a lawyer may compensate a witness not only for time actually spent testifying or attending trial, but also for time spent preparing for testimony. ABA Formal Opinion, *supra*. Such preparation includes time spent reviewing and researching records and meeting with attorneys in connection with the case. *See In re Friedman*, 196 A.D. 280, 292 (NY App. 1994); State Bar of Arizona Committee on the Rules of Professional Conduct, Formal Op. 97-07 (1997) (hereinafter "Arizona Prof'l Conduct Op."). The Delaware Ethics Committee found that failure to allow compensation for preparation time undermines the realities of modern day litigation. Delaware Ethics Opinion, *supra*. Complicated cases often require a fact witness to devote a substantial amount of time preparing for testimony. The State Bar of California Standing Committee on Professional Responsibility and Conduct notes that "[i]n some cases, accurate testimony without substantial preparation may be impossible." Cal Prof'l Resp. Op., *supra*.

The Amount of Witness Compensation Must Be Carefully Determined

After Joe Litigator determines whether Ima Witness may be compensated for loss of her time, he must then carefully determine the appropriate amount of compensation, if any. The comments to ABA Model Rules of Professional Conduct Rule 3.4(b) state that the test for determining the proper amount of compensation is the reasonable value of the witness's time based on all the relevant circumstances. Model Rules of Prof'l Conduct, Rule 3.4(3) cmt. (1983). This nebulous test arguably results in a significant risk to counsel that a trier of fact might conclude that a witness was improperly compensated. *See In re Friedman*, 196 A.D. at 292; Arizona Prof'l Conduct Op., *supra*.

The California State Bar Standing Committee on Professional Responsibility and Conduct provides better guidance. Cal. Prof'l Resp. Op., *supra*. The California Committee suggests that it may be acceptable to compensate a witness in either the amount that the witness currently earns, the amount the witness most recently earned or in the amount paid to persons in the same occupation as the witness. This amount may then be adjusted to account for any special or unusual circumstances. When determining the "reasonable and necessary" amount to compensate a witness, counsel should use an objective standard because a subjective one may be ineffective to rebuff a claim that a witness was bribed or otherwise improperly influenced.

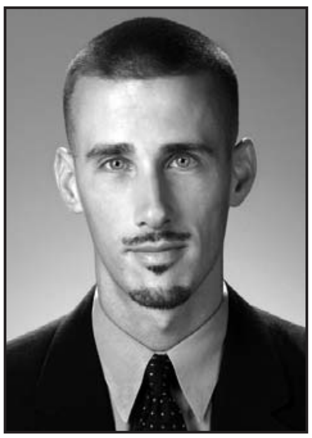
Accordingly, depending upon the rules of the applicable forum, counsel should consider whether a witness is employed, unemployed, retired, or assisting during non-working hours. If a witness is employed, whether the witness is paid hourly or by salary may affect the amount of appropriate compensation. When a witness employed on an hourly basis loses wages from missing work, she should be compensated in the amount of her normal working wage. *See* Alaska Bar Association Comm. on Ethics, Op. No. 93-2 (1993); Colorado Bar Ass'n Comm. on Ethics, Op. 103

(Continued on Page 10)

Continued from page 1

otechnology" currently yielding more than 13 million hits, yet no universally-recognized definition exists. At its heart, nanotechnology is about physical scale. A "nanometer" is a metric unit equal to one one-billionth (1/1,000,000,000) of a meter. A single sheet of paper is approximately 100,000 nanometers thick, and the common cold virus is approximately 25 nanometers thick. Put simply, a single nanometer is very, very small.

EPA has defined nanotechnology as (i) research and development of technology at the atomic, molecular or macromolecular level in the length scale of approximately 1 nanometer to 100 nanometers; (ii) the creation and use of structure, devices and systems with novel properties and functions because of their small size; and (iii) the ability to control or manipulate materials on the atomic scale. (*See* U.S. Envtl. Prot. Agency, EPA 100/B-07/001 Nanotechnology White Paper, (Feb. 2007) 5, [hereinafter EPA White Paper].) Fundamentally, "nanotechnology" is the pursuit of the technical ability to design, control, and use materials that are (or have components that are) in the nanometer size range.



Peter E. Masaitis

Why Nanotechnology Matters

Nanotechnology matters because "size matters." As materials become smaller, they necessarily have more surface area per unit of volume available to react with surrounding particles. Further, large-scale forces like gravity become less important, and other phenomena — such as quantum mechanics and surface tension — exert more powerful influences on particle behavior. As a result, nanomaterials have substantially different properties and structures than the same chemical substances at larger sizes. Nanoparticles are generally more reactive than larger particles. They also tend to be better catalysts, exhibit increased chemical reactivity and electrical conductivity, and possess improved hardness and strength.

These novel properties underlie the exploding scientific and commercial interest in nanotechnology. And even though the surface of nanotechnology's commercial potential has barely been scratched, the U.S, Patent and Trademark Office has already issued more than 4,800 nanotechnology-related patents. The wide range of commercial products incorporating nanomaterials currently includes industrial coatings, paints, computers, clothing, sunscreens, cosmetics, food packaging, disinfectants, sports equipment, and medical devices.

Potential Health and Environmental Risks

Unfortunately, the same characteristics that make nanomaterials increasingly common in commercial products are also generating substantial concern about nanotechnology's potential health and environmental hazards. Given their small size, unintentionally-released nanoparticles could remain air- and water-borne longer than other kinds of pollutants, thus creating exposure and property damage opportunities over large geographical areas. Once released, nanomaterials' small size may also make them more difficult to remove from the environment.

Small particle size also increases the likelihood that nanomaterials can enter the human body, as nanoparticles may be absorbed through the skin more easily than larger particles. There also may be cause for additional concern after the particles enter the body because it may be easier for nanomaterials to enter the blood stream after inhalation or dermal contact. Researchers have suggested that some nanomaterials can cross membranes and enter cells or tissues that larger particles cannot penetrate. (EPA White Paper, at 78.)

This increased *in vivo* mobility is troubling from a toxic tort perspective. Because nanoparticles may disperse throughout the body via the circulatory system, some researchers believe that nanoparticles' health effects may not be limited to specific areas in the body, but instead could manifest themselves at a systemic level. (*Id.* at 55). Some scientists have noted that nanoparticles may increase free radical production, thereby causing oxidative stress, inflammation and damage to proteins, membranes, and DNA. (particleandfibretoxicology.com/content/pdf/1743-8977-2-8.pdf.)

Although scientists continue to debate the potential health risks that nanoparticles may cause, researchers studying the relationship between particle size and toxicity have suggested that nanoparticles exhibit greater toxicity than larger particles of the same substance. (EPA White Paper, at 54.) This toxicity likely has multiple causes, including particle shape, charge, surface area, and reactivity. (*Id.*)

The National Nanotechnology Initiative and Expanding Health Effects Research

Nanotechnology research at the federal level is coordinated through the National Nanotechnology Initiative ("NNI"), a program established in 2001. Thirteen of the 25 federal agencies participating in the NNI have budgets specifically devoted to nanotechnology-related research and development in 2008, including EPA, NIOSH, the Department of Defense, the Department of Energy, NASA, the National Institutes of Health, and the National Science Foundation. (Nat'l Sci. & Tech. Council, National Nanotechnology Initiative Strategic Plan (Dec. 2007) [hereinafter NNI Strategic Plan], at 4.) The other 12 NNI member agencies, including the Consumer Safety Product Commission (CPSC), the Department of Labor, Food and Drug Administration, and the Nuclear Regulatory Commission, do not have nanotechnology-specific budgets but are nonetheless actively involved. (*Id.*)

The 21st Century Nanotechnology Research and Development Act, 15 U.S.C. § 7501 *et seq*., requires NNI to ensure that the environmental and other societal implications of nanotechnology are properly evaluated. Research on nanotechnology health implications is expanding quickly: the NNI's current $58 million budget for studies on nanotechnology health effects represents a dramatic 55 percent increase over 2006 levels. (nano.gov/pdf/NNI_FY08_budget_summary-highlights.pdf.)

EPA, NIOSH and the National Institutes of Health have already exercised substantial influence over research into nanotechnology's health and environmental risks. EPA, for example, contends that "[t]here is a significant gap in our knowledge of the environmental, health, and ecological implications associated with nanotechnology" and that EPA "has the obligation and mandate to protect human health and safeguard the environment by better understanding and addressing the risk from exposure to [nanomaterials.]" (NNI Strategic Plan, at 21.) Ongoing EPA research into the "environmental and biologic fate, transport, and transformation and bioavailability of engineered nanomaterials" could substantially impact the degree and scope of future nanotechnology litigation. (*Id.*)

Similarly, NIOSH's February 2008 draft strategic plan for investigating nanotechnology's health risks anticipates conducting multi-year research on (i) nanomaterial dispersion in the workplace; (ii) possible worker exposure routes; (iii) nanoparticle toxicities and particular health effects within the human body, including carcinogenicity assessments; (iv) development of toxicity models for use in human risk assessments; and (v) the feasibility of industry-wide epidemiologic studies of employees exposed to nanomaterials. (*Id.* at 26-30.) Results generated by NIOSH research activities in the next few years should be of major inter-

(Continued on Page 7)

Continued from page 6

est to toxic tort practitioners.

In yet another federal development of interest to litigators, the ATSDR is currently considering development of a full toxicological profile for "nanomaterials." (72 Fed. Reg. 60,673, 60,676 (2007).) Although the specific "nanomaterials" that ATSDR might include in a toxicological profile remains unclear, experts in toxic tort and environmental litigation will likely rely on the results for years to come.

NanoTorts and Other Challenges in a Changing World

The intensifying interest in nanotechnology's health implications raise many sticky issues for companies that manufacture, transport, or use nanomaterials. Future legal claims may be based on numerous scenarios, including (i) occupational exposures during the production, use or recycling of nanomaterials; (ii) general population exposures and property damage resulting from environmental releases during the manufacture and handling of nanomaterials; (iii) consumer exposures caused by the use of nanomaterial-containing commercial products. Speculation about the elevated toxicity of nanoparticles plainly raises the specter of toxic tort claims for alleged personal injuries, and the reported potential for nanomaterials to cause wide-ranging "systemic" health effects could significantly complicate causation-based defenses. The escalating calls for additional research and regulation of nanotechnology risks may portend personal injury, "failure to warn" and punitive damages claims in the near future.

In-house and private practitioners alike would be well-served to stay abreast of emerging information on nanotechnology's potential risks. Questions about potential nanotechnology health risks, for example, will only grow as nanotechnology's applications become increasingly ubiquitous. Stakeholders on all sides will be closely monitoring federal, state and local rulemaking developments, and assessing potential future liabilities for claims by consumers, workers, and/or residents near facilities that handle or use nanomaterials.

Some of the key issues developing around the current nanotechnology boom that will influence future "nanotorts" include:

• What are different agencies doing to regulate nanomaterials, what will the new regulations look like, and how can stakeholders participate in the process?

• What are the relevant rules and guidance documents for use in protecting workers from potential nanomaterial exposures?

• How can facilities that use nanomaterials anticipate and respond to health concerns by nearby residents?

• What consumer product warnings are, or should be, required for nanomaterials?

• How can agencies, businesses, the public, attorneys, and the courts evaluate the growing body of scientific literature and "get it right" on health and environmental issues?

In short, the confluence of explosive growth in commercial nanotechnology applications, rising public concern about health and environmental risks, and an expanding body of scientific literature offers numerous challenges for environmental and toxic tort practitioners. By anticipating these challenges and participating in the changing legal landscape, savvy counsel can place themselves — and their clients — ahead of the curve.

Published in the Environmental Litigator Newsletter of the Section of Litigation's Environmental Litigation Committee, Summer 2008.

— Orlyn "Skip" Lockard III and Peter E. Masaitis

ABTL's 35th Annual Seminar Got the Message Across

The 35th ABTL Annual Seminar was held this year on the island of Kauai, at the beautiful Grand Hyatt Kauai Resort & Spa in Poipu. In this lovely tropical setting, the seminar — entitled "Businesses in the Courtroom: Getting Your Message Across" — provided cutting-edge views on courtroom communications from top academics and trial lawyers, judges from federal and state courts across California, and respected consultants.

Featured speakers were a highlight of the program. Keynote speaker Joyce L. Kennard, Associate Justice of the California Supreme Court, delivered a moving address to a standing room only crowd. Professor Reid Hastie, who gave the opening reception address, is a leading scholar on the story-telling process, and its implications in a courtroom. And the tradition of obtaining the judicial perspective, in small breakout sessions with judges leading the discussion, continued with participation by all of the seminar's judicial guests.

Philip E. Cook

Panel presentations uniformly delivered the best on courtroom communications. Working with a program hypothetical about the sub-prime lending crisis, Thursday's panels covered *"Getting Your Message to the Jury"* — which included Harvey Levine's presentation on "Rethinking Jury Selection," a demonstration of *voir dire* techniques by Bill Claster and Carl Douglas, and views from jury consultants, trial lawyers and judges on how best to present the corporate defendant.

Friday's panels addressed *"Teaching Complexity to Communicate with the Fact Finder."* Topics began with a demonstration of opening statements from Bruce Broillett and Morgan Chu, for their panel addressing "An Effective Story — Is Your Theme Connecting?" Consultants worked with trial lawyers to show their expertise in a panel on courtroom graphics presentations, entitled "Seeing Is Believing — Using Graphics to Enhance Your Message." Finally, in the panel entitled "Experts as Educators – Making the Complex Understandable," both experts and experienced trial lawyers discussed ways to teach technical and financial details to a jury.

Finally, Saturday's panels, entitled *"Working With the Storytellers,"* focused on working with witnesses. The panel topics on this issue, which may be one of the most difficult parts of a trial lawyer's craft, included "Preparing the Corporate Witness to Testify," "Direct Examination — Telling a Compelling Story," and to quote Yogi Berra, "Cross-Examination — If You Don't Know Where You Are Going To Might Wind Up Somewhere Else."

The Grand Hyatt was an amazing venue, and provided a marvelous backdrop for the serious and the social — the educational and networking opportunities that are the hallmark of the ABTL Annual Seminar. Mark your calendars now for the 2009 annual seminar, to be held October 1-4, at the beautiful Broadmoor Resort, in Colorado Springs, Colorado. Hope to see you there!

— Philip E. Cook

Going belly up? Don't forget to WARN your employees

Not surprisingly in this economic downturn, the incidence of companies shutting down or closing less profitable facilities and laying off large numbers of employees is on the rise. Some of these companies will file for bankruptcy protection, while others will try to weather the storm through downsizing. However, *all* companies with at least 100 full-time employees that lay off 50 or more of them contemporaneously must comply with the federal Worker Adjustment Retraining and Notification (WARN) Act and applicable state WARN Acts. 29 U.S.C. § 2101(a). The California Relocations, Terminations and Mass Layoffs Act is substantially similar to the federal WARN Act except that it applies to California employers that employ at least 75 employees. Cal. Lab. Code § 1400(a) (2008). The federal and California WARN Acts require employers to provide employees and certain government agencies with 60 days notice of a large layoff or plant closing. 29 U.S.C. § 2102(a); Cal. Lab. Code § 1401(a). Absent 60 days notice, employers may be held liable to each terminated employee for wages and benefits for each day that notice was required but not given. 29 U.S.C. § 2104(a); Cal. Lab. Code § 1402. If, for example, an employer lays off 100 employees with only 20 days notice, then the employer may be liable to those employees for 40 days of wages and benefits.

Kimberly A. Posin

Because giving WARN notice signals that a company is in significant distress, efforts to save a struggling business thereafter may fail as employees, investors and creditors flee in search of less risky opportunities. Companies trying to resolve severe financial and operational difficulties often continue to pursue such efforts in earnest without notifying employees of a potential layoff until far fewer than 60 days before closing their doors, hoping and expecting to find a solution that will permit them to stay afloat and retain all or most of their employees. So, what happens when these efforts ultimately fail and a business must close a facility with less than 60 days notice? The federal and California WARN acts provide narrow exceptions to the notice requirement under certain circumstances. Where an exception applies, the court may completely excuse an employer from WARN liability or may determine that less than 60 days notice was required. If less notice was required, then employers still must have provided notice as soon as was practicable. In such instances, the employer's liability is limited to the number of days between the date notice should have been given and the date notice was actually given to affected employees. *See* 20 C.F.R. § 639.9 (permitting reduction in notice period where employers give notice as soon as practicable).

Unforeseen Business Circumstances Exception

In existing case law, the federal WARN Act exception most commonly invoked by employers is the "unforeseen business circumstances" exception. This defense does not exist under California law. Pursuant to the exception, employers are excused from full WARN notice if layoffs are forced by "business circumstances that were not reasonably foreseeable" at the time WARN notice would have been required. 29 U.S.C. § 2101(b)(2)(A). The circumstances must be caused by "some sudden, dramatic, and unexpected action or condition outside the employer's control." 20 C.F.R. § 639.9(b)(1). Examples of such actions include a principal client's sudden termination of a major contract with the employer, a strike at a major supplier, a dramatic economic downturn or a government-ordered closing of a worksite. *Id.*

Employers must satisfy two elements in order to invoke this defense. The first is causation — the unforeseen circumstance must actually cause the layoff. For example, in *Bradley v. Sequoyah Fuels Corp.*, 847 F. Supp. 863 (E.D. Okla. 1994), a toxic chemical leak at the defendant's plant caused the government to close the worksite indefinitely. As a result, the defendant was unable to generate revenue from the plant and had to lay off all of its employees. The court held that the leak caused the layoffs and that the first element of the defense was satisfied. *Id.* at 869-70.

The second element is foreseeability. *Id.* at 869. The test for whether the circumstance is foreseeable focuses on an employer's business judgment. The employer must exercise such commercially reasonable business judgment as would a similarly situated employer, but it need not accurately predict general economic conditions that may affect demand. 20 C.F.R. § 639.9(b)(2).

David B. Hazlehurst

Events held by courts to constitute unforeseeable business circumstances include the accidental release of airborne toxic chemicals at an employer's plant (*Bradley*, 847 F. Supp. at 869), the sudden loss of a non-profit employer's funding from a large charitable contributor (*Jurcev v. Cent. Cmty. Hosp.*, 7 F.3d 618 (7th Cir. 1993)), the sharp decline of the employer's market due to a credit squeeze (*Chestnut v. Stone Forest Indus., Inc.*, 817 F. Supp. 932 (N.D. Fla. 1993)), an employer's highly publicized federal indictment (*Roquet v. Arthur Andersen LLP*, 398 F.3d 585 (7th Cir. 2005)), an employee strike (*Teamsters Nat'l. Freight Indus. Negotiating Comm. v. Churchill Truck Lines, Inc.*, 935 F. Supp. 1021 (W.D. Mo. 1996)), a USDA-mandated closing of an employer's plant due to unsanitary conditions (*Pena v. Am. Meat Packing Corp.*, 362 F.3d 418 (7th Cir. 2004)), a regulatory commission's decision not to renew the employer's casino license (*Hotel Employees and Rest. Employees Int'l Union Local 54 v. Elsinore Shore Assocs.*, 173 F.3d 175 (3rd Cir. 1999)), and the loss of a major government defense contract (*Halkias v. Gen. Dynamics Corp.*, 137 F.3d 333 (5th Cir. 1998); *Loehrer v. McDonnel Douglas Corp.*, 98 F.3d 1056 (8th Cir. 1996)).

Several courts have adopted a rigid stance on the forseeability element of the exception. In *United Paperworkers*, 901 F. Supp. at 426, the court held that a bank-ordered closing did not qualify as an unforeseeable business circumstance. The defendant manufacturer had several significant loans from a bank, which it used to fund operations. Due to the manufacturer's poor financial performance, the bank called its loans and ordered operations to cease. *Id.* at 429-31. The court found that the closing was foreseeable. The defendant had been losing money for two years and, before closing down, had been forced to reorganize its business and restructure its bank loan because the business had been failing. Thus, the bank's

(Continued on page 9)

Continued from page 8

order to close was not "unforeseen or sudden," but rather was the "culmination of the continuing, and admittedly worsening, financial devastation" of the employer. *Id*. at 443.

Another court held that the failure of negotiations between two companies is not necessarily an unforeseeable business circumstance. In *Organogenesis, Inc*., the defendant engaged in negotiations with a competitor to sell the marketing and manufacturing rights to one of the defendant's products. These negotiations proceeded for four months and then failed. At that point, the defendant had to close down its operations. 316 B.R. at 579, 581-82. The court observed that the failure of the negotiations was foreseeable, noting that the defendant was aware of its financial instability four months before closing down when it began to seek capital from financial partners. In addition, the defendant's board of directors referred to one of its last votes as a "final attempt" to reach an agreement with the competitor, suggesting that the board understood that failure was a possibility. Finally, the defendant began to plan for bankruptcy during the negotiation period, indicating that it knew a closing might be imminent. *Id*. at 588.

Faltering Company Exception

Under federal law, full WARN notice is not required in the case of a plant closing (but not a mass layoff) if the following conditions are met: (1) the employer was actively seeking capital or business at the time notice would have been due, (2) the capital or business sought would have enabled the employer to postpone the shutdown, (3) the employer had a reasonable, good faith belief that giving notice would have precluded the employer from getting the capital or business it sought, and (4) there was a realistic opportunity to obtain the financing or business. 29 U.S.C. § 2102(b)(1) (2008); 20 C.F.R. § 639.9(a) (2008). California's exception is substantially similar except that it has no explicit requirement that the opportunity to obtain financing or business be realistic. Cal. Lab. Code § 1402.5 (2008). In addition, it appears that under the California statute, in the first instance, a government agency, not a court, is tasked with determining whether the defense applies. Section 1402.5(a) of the Labor Code limits the application of the faltering company defense to cases where "the department determines" that the above mentioned conditions exist. Section 19 of the Labor Code defines "department" as "Department of Industrial Relations."

There are no cases addressing the faltering company defense under California law. However, given the similarities between the California provision and the federal provision, federal decisions and regulations are instructive.

To be "actively seeking capital," an employer must seek financing or refinancing through loans, issue stock and/or bonds, or seek credit and/or business in other commercially reasonable ways. 20 C.F.R. § 639.9(a). In *Old Electralloy Corp*., 162 B.R. 121, during the year prior to closing its plant, the employer engaged in serious negotiations with potential investors, sought loans, contacted a law firm to help compile an investment prospectus and even offered to relinquish ownership of a majority of the company in exchange for a capital infusion. In light of these efforts, the court found the faltering company defense to apply. *Id*. at 125-26.

A key ingredient required to satisfy the first element of the defense is that the employer acts *affirmatively* to obtain capital. For example, the employer in *APA Transp. Corp. Consol. Litig*., 541 F.3d 233 (3rd Cir. 2008), met with a potential financier when it was in need of capital. However, the financier, not the employer, had requested the meeting. In addition, the financier, not the employer, opened discussions at the meeting about the employer's financial health. The court thus found that the employer was not "actively seeking capital." *Id*. at 249-50.

Also, merely attempting to sell a facility does not qualify as "actively seeking capital." In *Local 397 v. Midwest Fasteners, Inc*., 763 F. Supp. 78 (D.N.J. 1990), the defendant manufacturer ran out of capital and faced the possibility of closing operations. It searched for several months to find a buyer for the plant. Shortly after the last potential buyer announced that it was not interested in a sale, the employer closed the plant. The court held that searching for a buyer was not "actively seeking capital," and thus the defense did not apply. *Id*. at 83-84. Similarly, the defendant manufacturer in *Wallace v. Detroit Code Corp*., 818 F. Supp. 192 (E.D. Mich. 1993), attempted to sell its plant to avoid closure. The court found that this was "an option not covered under the [faltering company] exception." *Id*. at 197-98.

The second element of the defense is a question of causation. For example, in *Carpenters Dist. Council*, 15 F.3d at 1281, the defendant employer underwent a merger while it was seeking financing. The court found that the employer laid off its employees to trim expenses in order to facilitate the merger. The employer had not laid off employees because of capital problems. Therefore, obtaining capital would not have prevented any layoffs. *Id*. Thus, the defense did not apply.


Wayne S. Flick

The third and fourth elements of the defense are illustrated in *In re Organogenesis, Inc*., 316 B.R. 574 (D. Mass. 2004). There, the employer had been actively seeking capital during the notice period, but knew that to obtain financing, it would have to become fiscally attractive by acquiring marketing rights to a certain product. During negotiations, the owner of those rights told the defendant that the defendant needed to continue operations and "use its best efforts to preserve its business intact and to retain the services of its present employees." *Id*. at 586. In light of this, the court held that giving notice would have precluded the defendant from obtaining capital, and, therefore, the third element was satisfied. *Id*. Subsequently, negotiations broke down and the owner of the marketing rights informed the defendant by letter that it would be impossible for the defendant to acquire the rights. *Id*. The court found that the defendant should have given WARN notice after receiving the letter because, from that point forward, it knew obtaining financing was no longer realistic and thus the fourth element of the faltering business defense could not be satisfied. *Id*.

Good Faith Defense

Both the federal and California acts authorize courts to reduce an employer's WARN liability if the employer, when it violated the WARN notice requirements, acted in "good faith" and had "reasonable grounds for believing" that its conduct was not in violation of the applicable statute. 29 U.S.C. § 2104(a)(4); Cal. Lab. Code § 1405. Good faith requires "an honest intention to ascertain and follow the dictates" of the WARN statute and "reasonable grounds for believing that [the employer's] conduct complied" with the Act. *Childress v. Darby Lumber, Inc*., 357 F.3d 1000, 1007 (9th Cir. 2004). Relative to other defenses, the good faith defense appears rarely in WARN case law and, when invoked, is not often successful.

What does "good faith" mean? First, employers must have some knowledge of the WARN Act at the time it is violated. In *Childress*, 357 F.3d at 1000, the defendant mill operator closed one of its mills and laid off all employees at the facility with only

(Continued on page 10)

WARN

Continued from page 9

one day of notice. On the day of the shutdown, the mill operator had "little or no knowledge" of the WARN Act. Absent such knowledge, the court reasoned that it was impossible for the employer consciously to act in compliance with the law. Thus, the court held that the employer did not attempt to follow the statute in good faith. *Id.* at 1008. In contrast, the defendant steel manufacturer in *Old Electralloy*, 162 B.R. 121, knew of the WARN Act prior to its plant closure and was "cautious not to violate its requirements." Thus, even though the manufacturer gave no WARN notice, it was exempt from liability for its good faith attempt to comply with the Act. *Id.* at 126.

Second, the employer should seek the advice of counsel to verify its compliance with the Act. *See Old Electralloy*, 162 B.R. at 126. But legal advice may not be simply a token opinion of counsel. In *United Paperworkers Int'l Union v. Alden Corrugated Container Corp*, 901 F. Supp. 426 (D. Mass. 1995), the defendant manufacturer laid off a large number of employees without giving full WARN notice. Before doing so, the employer consulted outside labor counsel who opined that the WARN Act was not applicable. The court found that the legal advice was too "simplistic" given the complex nature and novelty of the WARN Act, which had taken effect just one year earlier. The court held that the defendant had not acted in good faith. *Id.* at 443-44.

In addition, employers (and legal advisors) must be objectively reasonable in determining whether compliance with the Act is required. The defendant retail store operator in *Carpenters Dist. Council of New Orleans v. Dillard Dept. Stores, Inc.*, 15 F.3d 1275 (5th Cir. 1994), failed to give 60 days notice to its employees before laying them off. When consulting with legal advisors about whether it would have to comply with the WARN Act, the defendant made favorable conclusions that were "aggressive" and "on tenuous grounds." Based on those conclusions, the employer determined that it need not comply with WARN notice provisions. Because its determination was not objectively reasonable, the court held that the defendant had not acted in good faith. *Id.* at 1288.

In the real world, 60 days WARN notice is often difficult to provide. But the cases in this article demonstrate that, even if employers cannot provide full notice, they may nevertheless be spared from all or at least some of the burden of WARN liability. The exceptions are narrow, however, and employers should simply not assume, merely because they were trying to avoid a mass layoff or plant closing, that a defense will be available. And even when a defense may exist under the particular facts and circumstances, employers must give at least some notice in order to avail themselves of a defense.

**— Kimberly A. Posin,
David B. Hazlehurst & Wayne S. Flick**

Fact Witness Compensation

Continued from page 5

(1998) (hereinafter "Colorado Ethics Op."). If a witness is salaried and is paid by her employer despite missing work, counsel should determine whether the employer or the witness should be compensated. Colorado Ethics Op., *supra*. If the witness is self-employed, she should generally be compensated in the amount she would normally earn per day. *Smith v. Allen*, 212 F. Supp. 713, 713 (East. Dist. Va. 1962). Determining the proper amount of compensation becomes more difficult when the witness is retired or unemployed; counsel must be even more careful not to cross the line between reasonable and unreasonable compensation.

Even If Litigator May Compensate Witness, Whether He Should Do So Is A Strategic Issue That Must Be Carefully Considered

Even if Joe Litigator may compensate Ima Witness for her preparation or testimony, whether Litigator and his client, Big Corporation, should do so is an entirely different question. The fact of a witness's compensation is discoverable and likely admissible at trial. *See* Colorado Ethics. Op., *supra*. Litigator must carefully weigh the benefits of having a well-prepared, but compensated, witness (and the degree to which the witness will be ill-prepared, absent compensation) against the harm to her credibility resulting from the compensation. Litigator should further consider the extent to which the trier of fact may change its perception of Big Corporation, or the opposing party, based on any witness compensation, and how witness compensation might change the dynamics of the case as a whole. Finally, Litigator should consider whether a skillful direct examination that reveals and addresses Witness's compensation will resolve any negative impacts that might otherwise result. The above analysis will vary depending upon the facts of each case, parties involved, nature of the compensation, and credibility of the witness.

Compensating a fact witness in an appropriate amount may, in certain circumstances, be critical to having a well-prepared witness who can deliver effective trial testimony. However, counsel must carefully analyze the governing law in all applicable jurisdictions and be wary of the differences among jurisdictions, so that he does not improperly compensate a witness. In general, a witness may be compensated for reasonable, out-of-pocket expenses incurred when testifying. A witness may also be appropriately compensated for loss of time depending upon the facts and the applicable jurisdiction. Counsel should unambiguously document that compensation is offered only as reimbursement for expenses and time, as appropriate, not based on the content of the witness's testimony. Finally, even when witness compensation is allowed, counsel must still carefully consider whether the benefits of witness compensation outweigh its negative effects.

**— J. Warren Rissier, Gwyn D. Quillen
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Bundled Product Discounts and the Sherman Act

The question of the Sherman Act's application to bundled product discounts has vexed courts for some time. In a recent decision, the Ninth Circuit has limited defendants' antitrust liability in this situation, but in doing so has also complicated the analysis.

Manufacturers of two or more products sometimes offer bundled discounts. Rivals — particularly rivals that offer only one of the competing products — may complain that the bundled discounts foreclose competition and violate Section 2 of the Sherman Act.

Courts have struggled with the question of whether such bundled discounting should be analyzed under an exclusive dealing analysis, a tying analysis, or a predatory pricing analysis. Under the exclusive dealing rubric, the question is whether the manufacturer essentially gives purchasers no choice but to buy its products. Under a tying analysis, the primary questions are whether the manufacturer conditions purchase of one product upon purchase of the other, and whether it has market power in the "tying" product market. Under a predatory pricing analysis, the main questions are whether the manufacturer is selling its product below some measure of incremental cost, and whether it has a dangerous probability of recouping its losses after its rival is driven from the market. Defendants generally prefer the predatory pricing analysis because its use of a cost/price screen is thought to be clear and to result in fewer "false positives."

In a heavily-criticized opinion, the Third Circuit in *LePage's Inc. v. 3M*, 324 F.3d 141 (3d Cir. 2003) (*en banc*), *cert. denied*, 542 U.S. 953 (2004), condemned bundled discounts even when they were above any measure of the defendant's cost. 3M had above a 90% market share in the transparent tape market and was a conceded monopolist. LePage's offered cheaper, "second brand" and private label transparent tape. LePage's challenged 3M's multi-tiered bundled rebate structure, which offered higher rebates when customers purchased products in a number of 3M's different product lines. LePage's asserted claims under Section 2. It did not, however, bring a predatory pricing claim. *See id.* at 151.

The *en banc* court, upholding the jury's Section 2 verdict against 3M, analogized the bundled discounts, not to predatory pricing, but to tying or exclusive dealing. "The principal anticompetitive effect of bundled rebates as offered by 3M is that when offered by a monopolist they may foreclose portions of the market to a potential competitor who does not manufacture an equally diverse group of products and who therefore cannot make a comparable offer." Id. at 155. The court did not require LePage's to prove that it or a hypothetical equally efficient competitor could not meet the discounts without pricing below cost. Rather, the court endorsed the trial court's jury instruction that conduct that "has made it very difficult or impossible for competitors to engage in fair competition" is actionable under Section 2. *Id.* at 168.

In *Cascade Health Solutions v. PeaceHealth*, 515 F.3d 883 (9th Cir. 2008), the Ninth Circuit declined to follow *LePage's*, and applied a cost-based test to bundled discounts. In that case, plaintiff and defendant each provided primary and secondary acute-care hospital services. Defendant also provided tertiary-care services, and had a high market share in that market (approaching 90% in some sub-specialties). Plaintiff did not compete in the tertiary-care market. The plaintiff brought a Section 2 claim against defendant, alleging that it offered bundled-service packages to some customers (such as insurance companies). The bundled discounts applied to all services if the insurance companies made defendant their sole preferred provider for primary, secondary, and tertiary care services. *See id.* at 892.

Howard M. Ullman

In the Ninth Circuit's view, the fundamental problem with *LePage's* is that it "concludes that all bundled discounts offered by a monopolist are anticompetitive with respect to its competitors who do not manufacture an equally diverse product line" and that it fails to consider whether such discounts may be pro-competitive. *See id.* at 899. The Ninth Circuit refused to adopt the *LePage's* approach, holding that bundled discounts may not be considered exclusionary conduct under Section 2 unless the discounts resemble predatory pricing behavior. *See id.* at 903.

The Ninth Circuit specifically adopted a discount attribution standard where, when the full amount of the defendant's discount on the bundled offering is allocated to the competitive product, and if the resulting price is above defendant's incremental cost to produce the competitive product, the arrangement is not exclusionary. *See id.* at 906-10. This refinement, although arguably less demanding than the amorphous Third Circuit test, still requires defendants to clear a higher hurdle than merely proving that all sales on average were above cost.

However, the Ninth Circuit also muddied the waters because it reversed a grant of summary judgment to the defendant on a Section 1 tying claim. The evidence presented genuine factual disputes about whether PeaceHealth forced customers (insurers) "either as an implied condition of dealing or as a matter of economic imperative through its bundling discounting" to take some of its services if the insurers wanted other services. *Id.* at 914. The Ninth Circuit did not resolve the question of whether a "no economic option" tying claim would require proof of below-cost pricing. (The Ninth Circuit also did not address bundled discounts involving contractual obligations not to buy from competitors.) As a result, blanket statements to the effect that the legality of price discounting always turns on a cost/price analysis should be considered with caution.

— Howard M. Ullman

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Young Lawyers Meet and Confer About Strategies for Winning Discovery

On October 29, the ABTL's YLD hosted another successful, well-attended event centered around teaching younger practitioners how to effectively and efficiently handle discovery disputes and motions in state and federal court. Two dozen attendees heard tips and ideas from both a practitioner's perspective, as well as views from the bench. Michael Bowse of Dreier Stein and Lisa Garner of Gordon & Rees discussed strategies and tactics from the lawyer's point of view and L.A. Superior Court Judge Peter Lichtman and U.S. Magistrate Judge Frederick Mumm offered their perspectives from the bench. The panel members offered practical tips on how to craft effective discovery, the value of good faith meet and confer discussions, when to bring a motion to compel, and most importantly, maintaining one's professionalism and credibility with the court and opposing counsel during discovery proceedings.

Some of the key tips offered by the panel:

Practitioners: understand the practical and legal goals of your case and craft your discovery to fit those goals; do not send out discovery for the sake of creating work for your adversary; conducting a professional, but thorough, meet and confer will help you to define the areas of real dispute, and focus your presentation of issues to the court; always maintain your credbility and be ready to concede points, even if it means your client will end up having to produce certain categories of discovery, because the judge's view of your word is more important than specific battles.

Judges: pick your battles wisely; judges are the ultimate arbiters of discovery, so do not expect to win every battle, just the important ones; be ready to concede, there is nothing more ineffective than a counsel who fights production as to every category of documents; discovery is an organic process and the judges rely on counsel to be fair and frank with them; a loss of credibility with the court is the number one failure of counsel in discovery; federal magistrate judges want to see effective meet and confer before a motion is brought; in CCW, judges are actively engaged in the meet and confer process and meetings with the court in chambers are the norm, rather than the exception.

Following the moderated discussion, the panel took questions from the attendees.

Judge Lichtman graciously offered the use of his courtroom for the event, and following the presentation, attendees and panel members gathered for an on-site reception to continue their networking and discussion.

— Felix Woo

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