ReedSmith

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Sidebar

Non-Party Discovery in Arbitration (Part 1): Are Discovery Subpoenas to Non-Parties Enforceable?

The propriety and extent of discovery in complex commercial arbitration has been the subject of extensive debate. While the exchange of potential exhibits and identification of witnesses prior to the arbitration is required by the rules of most arbitral institutions, all other aspects of discovery, including the extent of document exchange, the use of expert reports, the permissibility of depositions or interrogatories, and the issuance of subpoenas compelling discovery from non-parties, are generally left to the discretion of the arbitrators.

Since arbitration is a creature of contract, the parties are free to craft the procedures that will govern their arbitration, including the nature and extent of discovery among the parties. However, third parties are generally not bound by the terms of an agreement to arbitrate to which they are not signatories. Consequently, while an arbitrator can issue a subpoena *duces tecum* to require a non-party to appear for deposition and/or to produce documents in advance of the arbitration, the arbitrators cannot enforce the subpoena if a non-party fails to comply. In the court proceeding to enforce the arbitrator's subpoena, the central question is whether the arbitrator had the legal authority to compel the non-party to produce the documents in advance of the hearing and/or appear for the discovery deposition. Unfortunately, the answer to that question depends upon the law governing the arbitration proceeding, as well as the location in which the arbitration is being conducted.

Part 1 of this article discusses the applicable arbitration law and the split of authority among the courts of appeals interpreting Section 7 of the Federal Arbitration Act ("FAA"). In the next issue, Part 2 will discuss the divergence among state arbitration acts regarding non-party discovery in arbitration, and will offer practical suggestions that create more certainty in the arbitration process.

What Law Governs the Arbitration?

Anne Devens, a partner in our Virginia Trial Group, recently authored an article entitled, "Federal versus State Arbitration Laws: Whose Law Applies and Why Does it Matter?" (*www.vba.org/comm/Fed%20v.%20State%20 Arbitration%20Final.pdf*). In her article, Ms. Devens concludes the FAA generally governs the conduct of the arbitration unless the parties specifically agree that the arbitration shall be governed by the arbitration law

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Reed Smith's Investment in Contingency Case Pays Off

In May 2001, Reed Smith partner Alan Cotler took on a contingency fee case. Although some large firms might scoff at taking on contingency representations, Cotler and Reed Smith believed in their cause—vindicating the interests of computer programming gurus James and Janet Baker, against a who's-who list of national and international defendants who induced the Bakers to sell their business to a financially troubled and now-defunct software company. Cotler never could have anticipated that within the next four years, he, together with partner Joan Yue and associates Stephen Voigt and Maraleen Shields, working seamlessly with co-counsel at Boies, Schiller & Flexner, LLP, would achieve multi-million dollar settlements against two of the largest defendants they sued on behalf of the Bakers.

"Reed Smith gave its resources and a great investment that other firms might not be able to give—Reed Smith's size made it possible."

The Bakers' Case

Husband and wife computer programming team James and Janet Baker created one of the world's leading voice recognition software firms in Dragon Systems, Inc. In early 2000, while looking to expand their firm's capabilities, the Bakers were approached by a well-known European speech recognition software corporation. Relying on audits, statements, and representations from high-level international accounting and investment firms, the Bakers and their fellow shareholders agreed to merge Dragon Systems into the purchasing software company ("the buyer") in exchange for the buyer's stock, a $600 million transaction. Just five months after the sale, however, the buyer fell apart. The Bakers were left with nothing.

Upon further scrutiny, it appeared that the buyer was not as financially sound as the investment and accounting firms had represented. The buyer's accountants had issued "clean" audit statements despite numerous potential "red flags" that appeared among business transactions—and in the face of an SEC inquiry regarding the practices that led to the buyer's collapse.

A top investment banking firm also touted the buyer's success to the Bakers and others, assuring that the buyer was doing well financially and was well-positioned for targeted growth-markets where it supposedly was already succeeding. Analysts continued to issue glowing reports on the buyers' financial outlook and bankers raised capital for and facilitated billion-dollar deals, despite alleged concerns internally that the buyer may have been heavily overburdened.

By the fall of 2000, the buyer had filed for bankruptcy under Chapter 11, its top directors had resigned, and the accounting firm withdrew its prior favorable audits. Dragon—the valuable and respected company the Bakers had conceived and worked years to develop—became a casualty of the buyer's demise, and Dragon's cutting-edge technology became an asset of the buyer's bankruptcy.

Reed Smith invests In Contingency

Shortly after joining Reed Smith in May 2001, Alan Cotler was approached by a friend and former co-counsel from Orlando, Florida to join in the representation of James and Janet Baker. The Bakers had already retained David Boies at the law firm of Boies, Schiller & Flexner ("Boies"), most recently well-known for representing Presidential Candidate Al Gore. But with David Boies' team in high demand and swamped with work, the Bakers wanted another top-notch trial attorney to spearhead the case and turned to Cotler.

The Reed Smith management team reviewed Cotler's detailed memorandum before approving the contingency case. Cotler recounted, "Reed Smith gave its resources and a great investment that other firms might not be able to give—Reed Smith's size made it possible." Cotler says that his new fellow partners, Michael T. Scott and Bob Nicholas in Philadelphia, were "instrumental in supporting the case." The firm and practice managers—Gregory Jordan, Tom McGough and Tom McGarrigle—gave Cotler what the team needed to support the Bakers and their claims.

Teaming up with Boies, Schiller & Flexner and the Bakers

Cotler says that the partnership with the Boies firm has been the "best relationship [he's] ever had with another firm." Together, the Reed Smith/Boies team launched a multilateral attack on behalf of the Bakers, bringing suit against the investment banking and accounting powerhouses involved in the deal, as well as banks involved in the buyer's transactions, the buyer's inside directors, the audit committee and others. Teamwork between the two firms was essential, Cotler explained, because they were up against "big New York firms with armies of attorneys who fought them every inch of the way." Cotler recalls the tremendous effort the Baker team undertook to "beat back extensive and well-written Motions to Dismiss" from the investment banking and accounting firms, and to overcome significant discovery obstacles to make the case against both firms.

In order to help the Bakers, Cotler drew on Reed Smith's vast talent across a variety of practice groups, including: Sean Halpin, Tracy Frisch, Liz Abrams and Melissa Laccabue, who assisted in the early briefing on the motions to dismiss and the extensive document reviews; George Stewart, Traci Rea and Jeff MacHarg, who analyzed the defendants' complicated insurance policies; Lori Lasher and Michael Pollack, who provided insight into the investment banking culture; John Smith, who introduced the team to a very skilled and litigation-savvy investment banking expert; and Joe Sedlack and Daheesh Patel, who counseled the Bakers on tax issues.

The Bakers, the computer geniuses at the forefront of speech recognition technology, were also an essential part of the team. Emotionally drained by the experience of having their life's work "trashed" by economic fraud, the attorneys had to support and prepare them for the Defendants' attacks and seven to eight days of videotaped depositions. Cotler described the Bakers as "an essential part of the team" as they learned the legal processes and prepared to withstand the New York onslaught.

The Settlements

The teamwork and persistence paid off. Nearly four years after taking the case, the Baker legal team successfully settled its claims against both the accountants and the investment firm. The accounting firm settlement came as the accountants and auditors were about to be deposed, and the investment firm settlement was reached the evening before oral argument on the parties' cross-motions for summary judgment. With the remaining claims still pending, the team has earned a seven-figure premium from the settlements.

The Baker settlements not only helped create a record year for Philadelphia's Business Trial group, but they also more than paid off Reed Smith's investment. In addition, an exemplary relationship with the Boies firm was forged, which provides an excellent model for developing similar multi-firm litigation partnerships in the future.

– By Sara Kornbluh & Christin Bassett

Diet Drug Cases Resolved in Favor of Client

Attorneys in the Philadelphia office have achieved several significant victories for Wyeth in the "diet drug" litigation pending in the Philadelphia Court of Common Pleas. The cases have been "reverse-bifurcated" for trial, meaning that Reed Smith convinced the courts that a jury should address damages before ever considering liability, which has both cost-saving and strategic benefits. Reed Smith attorneys have had great success in prevailing at the damages phases of these proceedings, thereby obviating the need for a jury to even hear evidence bearing on liability. Among the most recent victories using the "reverse-bifurcated" method were two unanimous defense verdicts returned by the jury in the case of two plaintiffs whose cases were tried together. These plaintiffs claimed to have developed heart valve damage as a result of using diet drugs. Barbara Binis, Bill McDonough, and Caroline Flotron represented Wyeth at trial and put together a compelling defense based on the absence of empirical proof that plaintiffs actually were injured because of diet drugs, and the presentation of strong expert witnesses who ultimately proved more credible than plaintiffs' experts.

Recent UK Decision Provides Guidance to Banks Regarding Suspected Money-Laundering Activities

> *The judge held that any of these courses of action should enable a bank to proceed consistently with the CHAPS rules whilst, at the same time, avoiding criminal liability under the money-laundering legislation.*

Introduction

The case of *Tayeb v HSBC Bank Plc* and another [2004] EWHC 1529 examined the relationship between banks and customers involved in money transfers in the United Kingdom by means of CHAPS (the Clearing House Automated Payment Scheme). CHAPS is an electronic system for the transfer of Sterling which provides an irrevocable, guaranteed, unconditional payment for settlement in real time. In practice, payments made by CHAPS clear immediately and, in the absence of error, are ordinarily irreversible and as good as cash.

The importance of this case can be demonstrated by the volume of CHAPS transfers that take place every day. The judgment records that in 2001 there was an average daily volume of 89,000 separate CHAPS payments in the UK, with an average transaction value of £2.31 million and an average daily total of £206 billion.

The Facts

Mr. Tayeb, a Tunisian national who was not permanently resident in the UK, had brokered a deal with the Libyan General Post and Telecommunications Company (GPTC) to sell a database for £944,114.27 (the Sterling equivalent of US$ 1.5 million). Mr. Tayeb opened an instant saver account at the HSBC branch in Derby and arranged for the money to be transferred into the account by CHAPS. The funds arrived automatically and Mr. Tayeb was notified that the money had been credited to his account.

On the strength of that, Mr. Tayeb completed the transaction by giving the database to GPTC. The assistant manager at the HSBC branch became suspicious of the nature and origin of such a large sum of money and was concerned that the bank may be implicated in a money-laundering transaction. He ordered a marker to be put on Mr. Tayeb's account which prevented withdrawals without his approval.

The next day, the assistant manager spoke to Mr. Tayeb (who spoke poor English) but remained suspicious as to the source of the funds. Accordingly, he arranged for the full sum to be re-transferred to the sending bank. Mr. Tayeb contended that HSBC was indebted to him for the sum of £944,114.27 because it had wrongfully transferred the money out of the account. HSBC contended that it had acted lawfully in returning the money and denied that it was liable to pay Mr. Tayeb the sum claimed. HSBC later conceded, however, that the transaction between Mr. Tayeb and GPTC was lawful.

The Judgment

The judge held that HSBC was liable to Mr. Tayeb for the full sum plus interest from the date the money was transferred into Mr. Tayeb's account. A CHAPS transference was held to be "ordinarily irreversible" because the rules under which CHAPS operated allowed for re-transference of funds in limited circumstances only. These limited circumstances did not include the circumstances in which HSBC returned this money.

HSBC should have used the money-laundering reporting procedures which provide protection against possible criminal sanctions under the money-laundering legislation. The judge found there was no "unavoidable inconsistency" between compliance with the requirements of the money-laundering legislation and the

finality of CHAPS transfers. The judge set out in the judgment how banks should deal with this problem in the future:

- If a bank has advance warning of a transfer about to be made by CHAPS as to which it already entertains suspicions:
    - it could report the matter to the relevant authority, the National Criminal Intelligence Service ("NCIS") in advance;
    - it could withhold authentication while it informs NCIS; or
    - it could, having credited the customer's account following authentication, report the matter to NCIS and wait for directions.
- If the bank fears that a transfer out of the customer's account is imminent, it could temporarily freeze the account and inform NCIS but with due regard to the dangers of tipping off the customer (an offence under the money-laundering legislation).
- If a bank has already received payments and credited them to its customer's account, but subsequently becomes aware of ongoing money-laundering investigations, the bank could apply to court for an interim declaration as to what actions to take and what information may be provided to the customer without tipping him off.

The judge held that any of these courses of action should enable a bank to proceed consistently with the CHAPS rules whilst, at the same time, avoiding criminal liability under the money-laundering legislation.

– Jonathan Stone and George Brown

Meeting the Pro Bono Challenge

On February 7, Reed Smith named Christopher K. Walters, a partner in the Philadelphia office, to the new position of Senior Pro Bono Counsel. Walters' long-standing relationship with Reed Smith began in 1978 when he founded the Philadelphia Litigation group—a group for which he served as the leader until 1988. Walters has extensive experience handling trials and appeals in complex commercial cases including construction, product liability, fraud, and intellectual property matters.

By naming Walters to the position of Senior Pro Bono Counsel, Reed Smith joins the ranks of a small number of firms that has committed a full-time attorney to the administration of pro bono matters, building a foundation for pro bono work for years to come. In this role, Walters will oversee the firm's pro bono efforts from coast-to-coast.

Reed Smith has been recognized widely for its recent pro bono accomplishments—including advocating for the Amish, winning cases that have shaped asylum law, and devoting nearly 80 attorneys from across the firm to the 2004 Election Protection Project. But Walters seeks to increase Reed Smith's pro bono profile even further. To this end, Reed Smith has recently accepted the ABA challenge that the firm's attorneys commit 3 percent of their time to pro bono matters. Walters also wants the firm's representation of indigent clients to account for one–third of its pro bono matters. Community service, even outside the realm of pro bono representations, is also on Walters' agenda.

Walters' approach is simple and direct—encourage individual attorneys to each take on pro bono responsibilities. He has familiarized himself with the matters in which Reed Smith attorneys are currently involved and is pursuing leads on more opportunities for all types of attorneys (not just litigators). Walters is also developing connections between Reed Smith and targeted pro bono organizations with which the firm will have ongoing institutional relationships.

Although his various pro bono matters may not have always resulted in positive outcomes, Walters says that working on these cases has always proved both memorable and valuable to him. With each pro bono matter came a new lesson about the law, strategy and writing. Pro bono cases provided Walters unparalleled opportunities as a young attorney to work directly with clients, develop case theory and gain coveted experience appearing in court. Simply put, from pro bono cases, Walters learned about how to be an attorney.

Based on his own experiences, Walters sees two different benefits to pro bono work. On the one hand, the cases provide indigent people with much-needed representation that they otherwise could not afford.

On the other hand, in this day and age of large-scale, multi-million dollar litigations where junior attorneys

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Proposed Tax on Dissemination of Drug Information Tramples First Amendment

AB 95 taxes all marketing in whatever form it may take. As such, it is a tax for exercising the rights protected by the First Amendment.

For decades, California has paved the health care path with incentives to prescription product companies to develop and distribute life-saving therapies. For example, almost 20 years ago the California Legislature enacted the California AIDS Victim Compensation Act to encourage research for therapies while fashioning a scheme to compensate those who might be harmed by a vaccine.

A more recent bill, however, attempts to place a tax on the disclosure of the public dissemination of information regarding treatments. On January 10, 2005, Assemblyman Paul Koretz introduced AB 95, which, as defined by the Legislative Counsel, would "establish a program that would require manufacturers of drugs for life-threatening chronic conditions that are on the list for Medi-Cal or the AIDS Drugs Assistance Program to pay the department a rebate equal to the costs of marketing that drug."

The only exception is for activities that are "associated with legitimate physician education and then only if the costs are reasonable and in pursuit of legitimate physician education."

The legislation is premised on a suspect finding—that while the costs of drugs continue to rise, these costs are most directly related to marketing costs. The legislation states that "some marketing expenses are used for inappropriate advertising that does a disservice to persons with life-threatening illnesses as well as persons who may be at risk of life-threatening illnesses."

The solution, as proposed by the legislation, is to require each company to identify the costs involved in marketing the drug to consumers and physicians except "to the extent that those costs are associated with the necessary and appropriate education of patients and physicians." "Marketing" includes the costs of direct-to-consumer information as well as costs involved in physician education.

If voluntarily disclosed, the manufacturer pays the state 90 percent of these costs. If the costs of marketing the therapy are not disclosed, the manufacturer must rebate 25 percent of the price of the drug to the public health service. If the rebates are not paid, the therapy can be removed from the Medi-Cal or AIDS Drug Assistance Program "unless the department determines that removal of the drug from the list would cause substantial medical hardship to beneficiaries."

"The state is limited," the legislation continues, "as to how much it can spend purchasing or subsidizing these critical drugs, especially as the state faces an immediate multibillion dollar deficit and the threat of deficits for at least the next few years."

Litigation Involving Similar Legislation

Recent years have seen numerous attempts to limit efforts to provide information about prescription products. When Congress attempted to prohibit pharmacists from providing information about their ability to compound therapies, it was struck down as a violation of the First Amendment. *Thompson v. Western States Medical Center*, 535 U.S. 357 (2002). ("If the Government could achieve its interests in a manner that does not restrict speech, or that restricts less speech, [it] must do so.")

In a group of lawsuits involving the Washington Legal Foundation, the

Food and Drug Administration's efforts to limit the distribution without limitation about information of unapproved uses of therapies were also rebuffed as a violation of free speech protections.

The foundation for evaluating the impact of any effort by government to limit or penalize providing information about therapies flows from *Central Hudson Gas & Electric Co. v. Public Service Commission*, 447 U.S. 557 (1980).

There, the Supreme Court held that four tests were to be applied in evaluating whether commercial speech can be limited or prohibited. According to Central Hudson, such speech may be prohibited if it is false or misleading. It may be banned if it advocates unlawful activity. If the speech does not meet these criteria, it may be limited based on findings that "the asserted governmental interest is substantial," that the restriction "directly advances the governmental interest asserted," and that the limitation is "[no] more extensive than is necessary to serve that interest."

Without question, providing truthful, scientifically valid information in whatever form is protected speech. And as emphasized by the Supreme Court in *Western States*, "[I]f the First Amendment means anything, it means that regulating speech must be a last—not first—resort."

AB 95's Fate

AB 95, by the breadth of its dragnet on marketing, has no less a chilling effect than the prohibitions struck by the Supreme Court in *Thompson* and, on its face, is an invitation to be struck if adopted. While it does acknowledge that "costs (that) are associated with the necessary and appropriate education of patients and physicians" are not subject to the tax, the bill provides no guidance as to what such costs or activities would be.

If companies were to sponsor seminars or offer financial support for providing information about therapies, they would have to disclose their interests and the fact that the therapy was not approved for a specific condition.

AB 95 taxes all marketing in whatever form it may take. As such, it is a tax for exercising the rights protected by the First Amendment.

Indeed, most serious studies that have looked at the issue, including many conducted by the FDA, conclude that there are demonstrable benefits of direct-to-consumer information. As consumers learn about illnesses and diseases through the mass media, they become informed patients and will seek the care of a physician sooner than they might have otherwise done so, if at all.

Last year, the state Legislature enacted Drug Marketing Practices, a law that mandates manufacturers adopt "comprehensive compliance programs" governing marketing practices. The mandated compliance programs must conform to the pharmaceutical research code—as noted, a set of voluntary industry guidelines—and the inspector general's compliance program guidance.

A broadside at marketing by a tax on constitutional speech is not only unwarranted, it violates state and federal constitutions as well.

California is in an economic crisis, but surely there are solutions other than to impose a tax on the proper dissemination of information about life-saving therapies. The Legislature should continue on the path that it, and the citizens of California, have taken to encourage, not penalize, the development and distribution of life-saving therapies.

– James M. Wood

James Wood, author of "Recalls of Prescription Products: A Proactive Primer," is a partner with Reed Smith in the firm's Product Liability Group in Oakland.

Highlights of Recent Case Victories Around the Firm

The NAD directed the competitor to discontinue all of its blade life claims, as well as various other claims that we had challenged as false, including that the competitor's blades are "unbreakable" and result in "40% less cost." The competitor agreed to comply by discontinuing the campaign, and our client achieved its victory quickly without resorting to a lawsuit.

Victory in the NAD Enables Client to Avoid Litigation

Jeffrey M. Tamarin, a partner in the New York office who concentrates in litigating advertising issues, recently scored a major victory for a client at the National Advertising Division of the Council of Better Business Bureaus, Inc. ("NAD"), an advertising industry self-regulatory organization that investigates and adjudicates competitive challenges among advertisers. Our client, a worldwide manufacturer and marketer of tools for consumer, industrial and professional use, had been targeted by a competitor's advertising campaign. Hoping to grab market share for its new line of utility knife blades at the expense of our client's dominant brand, the competitor's campaign claimed, among other things, its new blades "last up to three times longer," perform "3 times the work" and "outlast 3 standard blades." In addition, the competitor's ads stated or implied that the longer blade life claims were true when using the blades in cutting a broad range of materials, including drywall and insulation. However, we established that the competitor had tested the life of its blade using only a single material—a heavy duty paper used by contractors. The NAD agreed with us that such testing on a single material did not substantiate any kind of advertising claims regarding use in cutting drywall, insulation, or any kind of material other than the particular paper tested. We also showed flaws in how the competitor had analyzed and presented its data, rendering even the paper-cutting test invalid. Moreover, our client's own blade life testing, conducted on drywall and subjected to appropriate mathematical and statistical analysis, completely refuted the competitor's false claims.

The NAD directed the competitor to discontinue all of its blade life claims, as well as various other claims that we had challenged as false, including that the competitor's blades are "unbreakable" and result in "40% less cost." The competitor agreed to comply by discontinuing the campaign, and our client achieved its victory quickly without resorting to a lawsuit.

Jeffrey M. Tamarin

Aftermath of September 11, 2001

In the aftermath of the tragedy of September 11, 2001 in New York City at the World Trade Center, disputes arose between surviving members of the families involving the property of the deceased. Reed Smith was retained by two of the daughters of a businessman who was at a weekly meeting at the Windows of the World on Tuesday morning, September 11, 2001. This individual had been married for a period of 26 months prior to September 11, 2001. This was his second marriage. His first marriage was to a woman to whom he was married for 26 years and who gave him two daughters—our clients. The property in the Estate of the deceased was more than $10 million. Reed Smith was substituted for a law firm in New Jersey that had been representing the two daughters for two-and-a-half years and had made little progress in resolving the various disputes with the deceased's wife at the time of his death. The property involved a lavish condo in Key Largo, Florida; a home in Mt. Claire, New Jersey; the Victim's Compensation Fund Award of $6 million; an insurance policy involving $700,000; a seat on the American Stock Exchange; several businesses in New York City; and other assets. With a team headed by

Allan Samuels of the New York office, along with Lance Gotthoffer and Lawrence J. Reina of the New York office, James A. Kosch of the Newark office and Lawrence F. Gilberti and John D. Martini of the Phildelphia office, the matter was settled most beneficially to our clients.

Newark and Princeton Offices Work in Tandem to Assure Victory

On March 16, 2005, Judge William J. Martini of the United States District Court for the District of New Jersey (Newark), ruled in favor of our client, a national mortgage lender, by denying class certification that had been sought on behalf of several thousand New Jersey borrowers. It had been contended under a variety of federal and state law theories, including the New Jersey Consumer Fraud Act, that our client and a New Jersey-based mortgage broker had a pattern and practice of failing to disclose certain fees and points in the initial good faith estimate, or had wrongfully increased such charges at such a late stage of the mortgage transactions that a meaningful choice was effectively denied to the borrowers. Plaintiffs amended their complaint several times, reviewed loan files, presented two expert witnesses (one on mortgage industry practices and one on statistical sampling) and were given many opportunities to brief and re-brief the class certification issues presented. After considering our opposition briefing and the transcripts of the depositions of plaintiffs' experts, Judge Martini issued a 17-page opinion largely tracking our briefing and finding that there were insufficient common questions of law or fact to bind together a class, that the named plaintiffs were not typical of the group they hoped to represent and that, therefore, no common issues predominated over the all-too-obvious individualized issues presented. Plaintiffs' counsel has been pursuing this case since 2001. It remains to be seen whether they will appeal this ruling to the U.S. Court of Appeals for the Third Circuit.

Northern California Section 17200 Litigation

In *Leonhardt v. American Telephone & Telegraph Co., et al.*, Case No. A103610 (Ca. Ct. App. Jan. 21, 2005), a consumer brought suit against a cable service provider alleging unfair business practices, false or misleading advertising, and violation of the Consumer Legal Remedies Act. The cable company had distributed a notice to customers amending the company's terms and conditions to require that disputes be resolved by binding arbitration and not by class actions. After the case was filed, an appellate decision in a case involving credit cards held a similar clause to be unconscionable under California law. Soon thereafter, the cable company

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Litigation Victory Enables Clients To Avoid Restrictive Covenant and Join New Cosmetics Display Company

New York partners Gil Feder and Herbert F. Kozlov recently prevailed in a litigation they filed in Supreme Court, New York County, on behalf of three officers who sought to leave a cosmetics display manufacturing company to join a competitor. The three officers had annual billings of several million dollars and had been with the company for several decades. The employer threatened to enforce a non-competition agreement if the officers left. Rather than wait for the employer to file suit, Gil and Herb filed a suit on behalf of the officers seeking a declaration that the restrictive covenant was overbroad as a matter of law. The restrictive covenant prevented the officers from working for any competitor whether as an employee or consultant for a period of two years anywhere in the world.

After the suit was commenced, the employer counterclaimed and immediately sought injunctive relief from the court seeking to temporarily restrain the three individuals from joining the competitor.

In a lengthy opinion, the Supreme Court, New York County, denied the employer's motion for injunctive relief. Specifically, the court held that the employer failed to show a legitimate protectable interest such as a trade secret or confidential information.

Gil and Herb then moved to dismiss the employer's counterclaim and the officers settled the case on very favorable terms.

rescinded the relevant provisions of its notice. The court of appeal upheld the trial court's order granting summary judgment in favor of defendants as to all of plaintiff's claims. In the course of its discussion, the court of appeal found plaintiff's injunctive relief claims were moot, and restitution and damages were unavailable because the subject provisions were rescinded in California and never enforced against California consumers. The court also found that since defendant changed its conduct on account of a recent court decision, the trial court could properly find that plaintiff was not the prevailing party for purposes of an award of costs. The case contains important analysis of what constitutes actual injury under Section 17200 and the CLRA. For a copy of this opinion, please contact Robert D. "Bo" Phillips, Jr. at 510.466.6722.

The case contains important analysis of what constitutes actual injury under Section 17200 and the CLRA.

Eight-Year Litigation Ends Favorably

Steve Blitch, Marshall Wallace and Ted Ting recently finished a trial for First American Title Insurance Company in Alameda County Superior Court before the Honorable Stephen Dombrink. After the plaintiff finished its case-in-chief, seeking $3 million to $4 million in damages plus punitives, the court granted the motion for judgment (equivalent to a nonsuit). First American then tried its counterclaim for breach of the title insurance policy. The court took it under submission, and if successful, First American will wind up recovering damages.

This case began in 1997, when Plaintiff Bar-K loaned $4.1 million to Circle Rainbow, a Hawaii borrower, secured by a mortgage on Circle Rainbow's improved leasehold at the Honolulu Airport. Co-defendant Security Title Corp. served as the escrow agent, while First American issued a title insurance policy. After Circle Rainbow defaulted and challenged Bar-K's rights to the property, Bar-K made a claim on the policy, demanding that First American defeat the challenges so that Bar-K could foreclose on its leasehold collateral. First American followed through on its obligations, first paying Hawaii attorneys to defend Bar-K, then paying an additional $1 million to settle those issues and actually obtain title to the leasehold for Bar-K.

In general terms, this was more than Bar-K had even bargained for, since Bar-K's rights under its mortgage was only a lien—not title. Yet, Bar-K wasn't satisfied with having title to a leasehold that it had valued at $8 million to $9 million. It sued First American and Security Title, claiming they breached the escrow instructions, which led to Circle Rainbow's default. It also sued for bad faith, claiming First American did not honor the title insurance policy.

Since First American never agreed to act as an escrow agent and had more than met its duties under the title insurance policy, and since Bar-K was not damaged, Bar-K's case was meritless from the start. It appeared that Bar-K had manufactured a claim and was looking to "shake down" First American and Security Title. Numerous settlement attempts went nowhere, even after First American prevailed on a motion for summary adjudication on the bad faith cause of action, and the parties headed to trial on November 29, 2004.

Several people played critical roles in contributing to the team's success, including Bernie Brass, Marsha Kirschbaum, Elaine Lew, Sharon Pinter, E.J. Rankin, and Kathy Samo.

Dateline: Philadelphia

Reed Smith litigators defeated plaintiffs' efforts to certify in a medical monitoring class of women across Pennsylvania who used Prempro, a form of postmenopausal hormone therapy manufactured by Wyeth which remains on the market. In an action in the Philadelphia Court of Common Pleas, plaintiffs sought breast cancer surveillance on behalf of allegedly more than 700,000 users who had not developed breast cancer but claimed that use of Prempro increased their risk for developing the disease in the future. After a three-day hearing, where Wyeth was represented by Michael Scott, Kerry Kearney and Christin Bassett, the court concluded that class certification was inappropriate in large part because of critical admissions that Scott secured from plaintiffs' own experts. The decision will assist Wyeth in challenging putative medical-monitoring class actions regarding Prempro pending in other jurisdictions.

Gary Tucci and Jon Nadler recently received a very favorable award in a UPS national labor arbitration. The grievant alleged that UPS violated an article in the national collective bargaining agreement between UPS and the International Brotherhood of Teamsters—and the Americans With Disabilities Act ("ADA")—by refusing to place him in another job after he sustained an on-the-job injury. The arbitrator denied the grievance in full, ruling that UPS did not violate any provision of the ADA. The award will assist Reed Smith in defending UPS in a federal court putative class action raising ADA claims where the grievant is a principal plaintiff. Because the collective bargaining agreement provision in question covers UPS Teamster employees across the country, the arbitration award procured by Reed Smith also has nationwide application.

On behalf of GE Capital Corporation, the Wilmington office obtained a very rare ex parte Temporary Restraining Order in the Court of Chancery in February of this year, which ultimately paved the way for achieving a highly favorable settlement for the client. Specifically, the litigation involved GE's replevy rights to a certain multi-million dollar Lear Jet, whose owner had defaulted on his financing obligations and was continually moving the jet such that GE could not readily ascertain its whereabouts. Reed Smith managed to obtain a Temporary Restraining Order from Vice Chancellor Strine, enjoining the defendant/debtor from in any way using or encumbering the aircraft, GE's collateral.

Reed Smith's Philadelphia office recently obtained a decision from the Commonwealth Court that provided client Corning Asahi Video Products Company with $900,000 in tax relief. The case involved an appeal of a Board of Finance and Revenue decision, which raised novel issues concerning the Taxpayers' Bill of Rights and application of collateral estoppel to Board of Finance and Revenue decisions. Andrew Soven successfully briefed and argued the matter.

Steel City Highlights

For several years, Stephanie Wilson, Paul Rooney, and John Unkovic have represented Dreyfus in a four-plaintiff case being pursued by the EEOC in the Eastern District of New York. Discovery was long and costly, and involved Dreyfus operations that were in flux. We have finally received a decision granting our motion for summary judgment—a decision which has very much pleased the Mellon folks in Pittsburgh. Great thanks to Stephanie and Paul for their strong support of our effort and hard work for our client.

In two rulings entered the same day in two different courts, Chris Soller was successful in securing summary judgment in favor of our client, Assurant Solutions. Both cases involved the determination of whether a certificate of insurance was void ab initio due to misrepresentations made in the application for the insurance. Additionally, both cases included claims of bad faith insurance practices and violations of Pennsylvania's consumer protection statute. The decisions entered in Assurant's favor dismissing the two cases were issued by Judge John E. Jones III of the United States District Court for the Middle District of Pennsylvania and Judge Daniel J. Ackerman, President Judge of the Court of Common Pleas of Westmoreland County, Pennsylvania.

Recent Appellate Victories in Maryland and California Reaffirm the Enforceability of Arbitration Provisions

In a thoughtful 40-page opinion, the Maryland Court of Appeals rejected the "unquestionably minority view" expressed in the California, West Virginia, and Pennsylvania decisions, and enforced the arbitration provision as drafted.

Despite all the case law endorsing arbitration, many trial courts remain hostile to this alternative dispute resolution process and refuse to enforce arbitration provisions. In the last two months, our appellate lawyers have obtained reversals of orders denying arbitration in three California cases. Kathy Banke handled a combined writ proceeding and appeal for a large investment advisor in the Second District Court of Appeal, located in Los Angeles. In that case, brought by an investor claiming poor investment advice was the cause of his losses in the recent bear market, the trial court not only refused to enforce standard NASD arbitration provisions, but also purported to compel arbitration before an entirely different arbitral forum. The Court of Appeal reversed in full and directed the trial court to grant the defendants' petition to compel arbitration. Ray Cardozo handled two appeals for a telecommunications company in the First District Court of Appeal, located in San Francisco. In these class action lawsuits, the plaintiffs claim certain customer charges were deceptively presented. The trial court denied our client's petitions to compel arbitration under the arbitration clause in its standard terms and conditions of service. The Court of Appeal reversed and remanded with directions to grant the petitions and order the cases to arbitration.

Similarly, on April 19, 2005, the Maryland Court of Appeals affirmed the decision of the trial court and an intermediate appellate court enforcing our client's agreement to arbitrate over objections to the validity of the agreement raised by the plaintiffs. The plaintiffs in the case raised claims under the Maryland Second Mortgage Loan Law and sought to certify a class of all Maryland borrowers whose second mortgage loans were sold to our client. We moved to compel arbitration or, in the alternative, to dismiss. In response, the plaintiffs argued that the arbitration agreement was unconscionable and therefore unenforceable because it allowed the lender the option to seek foreclosure and prohibited class-wide relief.

Both the trial court and the intermediate court of appeals rejected the plaintiffs' arguments and found the arbitration provision to be enforceable. On August 25, 2004, the Maryland Court of Appeals granted *certiorari* to consider the issue. In their brief, the plaintiffs argued that the trend in states such as California, West Virginia, and Pennsylvania was to find arbitration provisions reserving the right to foreclose, and prohibiting class-wide relief to be unconscionable.

In a thoughtful 40-page opinion, the Maryland Court of Appeals rejected the "unquestionably minority view" expressed in the California, West Virginia, and Pennsylvania decisions, and enforced the arbitration provision as drafted. The victory was a joint effort of the trial team of Tom Allen, Roy Arnold, Jim Bentz and John McIntyre working in conjunction with Jim Martin of our Appellate Group. *Walther v. Sovereign Bank*, 2005 WL 900551.

– Kathy M. Banke and John M. McIntyre

"Non-Party Discovery in Arbitration" – *continued from page 1*

of a particular state. For example, language such as the following demonstrates an objective intent that the agreement to arbitrate be subject to a state arbitration law rather than the FAA: "This arbitration, and any subsequent proceeding to enforce, modify, vacate or confirm the arbitration award, shall be governed by the Pennsylvania Arbitration Act of 1927." An unequivocal expression of contractual intent to be bound by a state arbitration act will not be preempted by the FAA unless the state arbitration law conflicts with the purposes of the FAA. However, the majority of cases hold that a general choice of law provision determines the substantive law applicable to the underlying transaction, but is not sufficient to invoke the arbitration law of that state. Consequently, in the absence of a specific agreement as to the law governing the arbitration, the FAA will apply as long as the arbitration agreement involves interstate or international commerce.

Third-Party Discovery Under the FAA

Section 7 of the FAA expressly grants arbitrators the authority to summon "any person to attend before them or any of them as a witness and in the proper case to bring with him or them any book, record, document or paper which may be deemed material as the evidence indicates." Consequently, the FAA expressly permits an arbitrator to compel a non-party to attend the arbitration and/or to produce documents to the arbitrators at the arbitration. However, federal courts are split over whether Section 7 permits an arbitrator to order a non-party to produce documents or appear for a discovery deposition.

In a recent case in which Reed Smith was involved, the U.S. Court of Appeals for the Third Circuit held that an arbitrator's subpoena power under the FAA is limited to ordering a non-party to appear before the arbitrator to testify or produce documents. *Hay Group, Inc. v. E.B.S. Acquisition Corp.*, 360 F.3d 404, 407 (3rd Cir. 2004). The Fourth Circuit has taken a more tempered approach, holding that the FAA does not grant an arbitrator the authority to demand that a non-party produce documents for pre-hearing discovery, but suggesting *in dicta* that an arbitrator may order discovery upon a non-party "under special circumstances" and "upon a showing of special need or hardship." *COMSAT Corp. v. Nat'l Science Foundation*, 190 F.3d 269, 276 (4th Cir. 1999). At the opposite end of the spectrum from *Hay*, the Eighth Circuit has held that the power to compel non-parties to produce documents prior to the arbitration hearing is "implicit" in the authority granted to arbitrators in Section 7 of the FAA, and that the "efficient resolution of disputes through arbitration" is furthered by permitting limited third-party discovery. Arbitration between Security Life Insurance Company and Duncanson & Holt, Inc., 228 F.3d 865, 870–71 (8th Cir. 2000). The Sixth Circuit, in a case arising under Section 301 of the Labor Management Act of 1947 and decided prior to Duncanson, also commented that the FAA "has been held to implicitly include the authority to compel the production of documents for inspection by a party prior to the hearing." *Am. Fed'n of Television & Radio Artists v. WJBK-TV*, 164 F.3d 1004, 1009 (6th Cir. 1999). While several district courts have also addressed this issue, the remaining federal circuit courts have not ruled upon the availability of third-party discovery in arbitration proceedings.

While the federal law on these issues is not settled, two general points can be gleaned from these cases. First, the location of the arbitration may determine the extent to which third-party discovery requests are enforceable under Section 7 of the FAA. Under current law, permissible discovery upon non-parties under the FAA is far broader in an arbitration conducted in St. Louis than in one conducted in Philadelphia. The extent of permissible third-party discovery in arbitrations conducted under the FAA in venues such as New York, Chicago, California, Florida, or Texas remains an open issue. Second, while the availability of document discovery from non-parties in advance of an arbitration hearing is an open issue in many federal circuits, relatively few federal courts have interpreted Section 7 of the FAA to authorize a discovery deposition of a non-party. In a practical sense, the logic seems to be the more intrusive the third party discovery sought, the less likely a court will find that the arbitrator had the authority under Section 7 of the FAA to order that discovery.

While the rules invoked in *Hay* and *COMSAT* may appear impractical in today's world of complex commercial arbitration, stay tuned for Part 2 of this article in the next issue. Part 2 will address the divergence among state arbitration laws regarding non-party discovery in arbitration, and will offer practical suggestions to create more certainty in the arbitration process and to allow for third-party discovery in appropriate circumstances.

– Albert Bates, Jr.

"Meeting the Pro Challenge" – *continued from page 5*

may have limited involvement in their client-billable matters, taking on pro bono cases allows associates the chance to run their own cases. Hoping to grow and cultivate a commitment to pro bono work among junior associates, Walters emphasizes the experiential learning element of the work, holding out his own experiences as proof that pro bono cases can provide even junior attorneys with plentiful opportunities to develop their skills. And the skills—and confidence—they gather from running their own cases contribute greatly to their overall professional development.

Walters is also well aware of the pressures attorneys face to maintain their caseload apart from pro bono obligations. He hopes to create more incentives to encourage attorneys to do pro bono work. For instance, Reed Smith automatically gives up to 60 hours of credit for pro bono work towards the firm's billable hour requirement. In special circumstances, additional billable credit may also be given.

So, what will the future of pro bono look like at Reed Smith? Walters can't say for sure. But by placing him at the helm of the pro bono effort, Reed Smith has taken a substantial step toward fostering its commitment to pro bono work across the country.

– Maraleen Shields and Christin Bassett

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