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CONTENTS:

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CONTENTS & OPINIONS

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- ARTICLES -

A MODEL FOR MANAGING PRIVATE COMPANY LEGAL RISKS AND HARNESSING LEGAL OPPORTUNITIES

By

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The face of legal practice has dramatically changed in recent years.[1] Financial pressures have led to a call for reduced legal fees and for law graduates who are better-trained and well-versed in the practical skills needed to practice law. [2] Strengthened legal regulations are demanding increased compliance on the part of all businesses at the very time that financial constraints are calling for

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[1] Larry E. Ribstein, *The Changing Role and Nature of In-House and General Counsel: Delawyering the Corporation,* 2012 WIS. L. REV. 305, 307(2011) (observing that technology and the demand for efficiency will gradually lead to less one-on-one individualized counseling, and a greater use of systems to ensure regulatory compliance.

[2] Mitchell D. Hiatt, *Changes in Legal Education and Ethics: Note: Why the American Bar Association Should Require Law Schools to Increase and Improve Law Students' Practical Skills Training,* 45CREIGHTON L. REV. 869, 882 (2012)(indicating that many law school graduates are not ready to practice law and that legal employers complain that law school graduates do not understand clients' needs or their businesses) .

them to reduce overhead. [3] As one noted scholar observed, the future of legal practice lies in the development of systems that can be used by non-lawyers to ensure that legal objectives and legal compliance are achieved.[4] Private companies surely receive legal advice, but all too frequently, the advice stops short of including suggestions as to how the legal risks can be effectively monitored by overworked owners with limited staff. The end result is that the business valuation and buy-out agreement fails to be executed and/or updated, [5] agency authority is not properly limited, [6] or the sexual harassment policy never gets properly promulgated, as advised.[7] This article discusses a framework that can help the private company to systematically monitor legal risks and thereby keep pace with best practices in business management.[8] The Integrated Frameworks for Internal Controls (IC) [9] and Enterprise

[3] David Hess, *Enhancing the Effectiveness of the Foreign Corrupt Practices Act Through Corporate Social Responsibility,* 73 OHIO STATE L. J. 1121(2012)(discussing the high price of poor legal controls which if discovered could lead to the calling off of an acquisition in the midst of due diligence).

[4] *See* Larry E. Ribstein, *The Changing Role and Nature of In-House and General Counsel: Delawyering the Corporation,* 2012 WIS. L. REV. 305, 307(2012).

[5] See Chapman v. Regional Associates, PLLC, No. 2010-CA-000131-MR, 2011 WL 1085999, at * 1 (Mar. 25, 2011)(involving a suit to recover a buy-out payment upon withdrawal from a private radiology practice where the LLC lacked a written operating agreement).

[6] Nature's Sunshine Products v. Sunrider Corps., No. 11-4214, 2013 WL 563309(10th Cir. 2013)(refusing to set aside a settlement agreement entered into by someone who had apparent authority to settle the case).

[7] Joanna L. Grossman, T*he Culture of Compliance: The Final Triumph of Form Over Substance in Sexual Harassment,* 26 26 HARV. WOMEN'S L.J. 3 (2003)(discussing the central role that sexual harassment policies are designed to play in deterring sexual harassment).

[8] Thomas C. Pearson & Gideon Mark, *Investigations, Inspections, and Audits in the Post-SOX Environment*, 86 NEB. L.REV. 43, 64-65(2007).

[9] See COMMITTEE OF SPONSORING ORGANIZATIONS OF THE TREADWAY COMMISSION, INTERNAL CONTROL - INTEGRATED FRAMEWORK (1992), *available at*

Risk Management, an Integrated Framework (ERM) [10] are practical models published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).[11] Both frameworks are widely employed by large public companies that must report on internal controls and comply with the Sarbanes-Oxley Act.[12] However, the ERM framework in particular has enormous, untapped potential for helping the smaller, private company control legal risks. This is precisely the type of *practical* legal assistance that small clients are demanding today. [13]

Part I of the paper highlights several recent legal developments which make legal risk management an urgent priority particularly for the closely-held business. Part II discusses the ERM framework and Part III then provides two examples of its applications. The first example illustrates how the model can be used to address an internal legal risk – that associated with conflicts among owners. The second example shows how the model can be used to address an external legal risk – that associated with piercing the corporate veil of limited liability.

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http://www.cpa2biz.com/AST/Main/CPA2BIZ_Primary/InternalControls/COSO/PRDOVR~PC-990009/PC-990009.jsp.

[10] See COMMITTEE OF SPONSORING ORGANIZATIONS OF THE TREADWAY COMMISSION, ENTERPRISE RISK MANAGEMENT – AN INTEGRATED FRAMEWORK (2004), available at < http://www.coso.org/guidance.htm>

[11] See COMMITTEE OF SPONSORING ORGANIZATIONS OF THE TREADWAY COMMISSION, available at http://www.coso.org/aboutus.htm

[12] Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, § 404, 116 Stat. 745, 789 (codified at 15 U.S.C. § 7262(2006)[hereinafter Sarbanes-Oxley Act].

[13] Susan Swaim Daicoff, Synthesizing Leadership, Professionalism, Emotional Intelligence, Conflict Resolution, and Comprehensive Law, 52 SANTA CLARA L. REV. 795, 799(2012)(indicating that clients want more from legal services and are also demanding lower fees).

I. THE URGENCY OF LEGAL CONTROLS FOR THE PRIVATE COMPANY

The importance of utilizing law as a valuable managerial capability has been recognized by Bagley[14] and other legal scholars.[15] Management scholars such as Kaplan and Norton have observed that legal and regulatory expertise and competence are essential for a successful competitive strategy. [16] From an internal governance standpoint, uncertainty in the law governing the internal relations of LLC members,[17] as well as in the law governing business valuation make it critically important for the private business owner to put into place an effective buy-out agreement containing a valuation provision.[18] From an external or operational standpoint, escalating demands stemming from the Sarbanes-Oxley Act, [19] Dodd-Frank Act,[20] and from the Federal Sentencing

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[14] Constance E. Bagley, *What's Law Got to Do With It?: Integrating Law and Strategy* 47 AM. BUS. L. J. 587, 629-630(2010).

[15] *See* Robert C. Bird, *Special Issue: Law as a Source of Strategic Advantage: The Many Futures of Legal Strategy,* 47 AM. BUS. L. J. 575, 577 (2010)(explaining the sophisticated, competitive contemporary business environment and the value of the ability of top management to communicate with counsel and solve complex problems).

[16] *See id.* at 602-603. *See generally* ROBERT KAPLAN & DAVID NORTON, STRATEGY MAPS 165 (2004).

[17] *See* Thomas M. Madden, *Do Fiduciary Duties of Managers and Members of Limited Liability Companies Exist as With Majority Shareholders of Closely-held Corporations?* 12 DUQ. BUS. L.J. 211, 215(2010)(exposing the uncertainties regarding minority LLC member protections under selected LLC statutes).

[18] Sandra K. Miller, *Discounts and Buyout in Minority LLC Valuation Disputes Involving Oppression or Divorce,* 13 U. OF PA. J. BUS. LAW 607, 612-651 (2011)(providing an analysis of business valuation policy issues and calling for uniform business entity legislation to address valuation issues in private enterprises).

[19] Sarbanes-Oxley act of 2002(SOX), Pub. L. 107-204, 116 Stat. 745(2002).

[20] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376(2010)(codified in scattered sections of 12 U.S.C.).

Guidelines[21] make it important for even small privately-owned companies to adopt systems for managing legal compliance and utilizing legal opportunities.

A. Internal Governance: Need for Buy-out Agreements Including Valuation Mechanisms

Scholars and practitioners have long noted that a well-considered up-to-date shareholder or limited liability company (LLC) agreement containing a valuation mechanism is vitally important for the privately-held company.[22] Particularly if conflicts arise between majority and minority members or among equal owners, a current shareholder or limited liability company agreement can be invaluable in resolving the dispute without the expense of a protracted lawsuit.[23]

It has been widely noted that investors in privately-owned businesses are largely locked into illiquid investments. [24] This illiquidity problem is now typical of both closely-held corporations and LLCs, which are rapidly replacing the corporation as the entity

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[21] Fair Sentencing Act of 2010, Pub. L. No. 111-220, 24 Stat. 2372 (codified as amended in scattered sections of 21 U.S.C.

[22] *See generally* F. HODGE O'NEAL & ROBERT THOMPSON, F. HODGE O'NEAL & THOMPSON'S OPPRESSION OF MINORITY SHAREHOLDERS AND LLC MEMBERS (2d ed. 2012)(offering an overview of issues that plague minority owners of private business entities). *See* JAMES D. COX & THOMAS LEE HAZEN, COX & HAZEN ON PRIVATE CORPORATIONS(2d ed. 2003 to date)(addressing legal issues concerning private and public companies). See DOUGLAS K. MOLL & ROBERT RAGAZZO, CLOSELY-HELD BUSINESS ORGANIZATIONS : CASES & MATERIALS & PROBLEMS (West 2006)(highlighting the particular vulnerability of minority owners who are locked into private companies without a liquid market).

[23] *See* Mathew C. Lucas, *Revoking the Irrevocable Buy-out: Aligning Equity With Diligence*, 75 ALB. L. REV. 15. 17(2011/2012(discussing the prevalence of disputes in closely-held enterprises).

[24] SANDRA K. MILLER, LIMITED LIABILITY COMPANIES: A COMMON CORE MODEL OF FIDUCIARY DUTIES 7.3 (2012).

of choice for private businesses. [25] Under Revised Uniform Partnership Act (RUPA) Section 701,[26] an express buy-out right is given to a dissociating partner.[27] Thus, a general partner can obtain a buy-out upon dissociating from the general partnership.[28] In contrast, such default buy-out rights have been largely eliminated in LLC statutes.[29] The removal of default buy-out rights has enabled LLC members to divest themselves of majority control and thereafter qualify for minority and lack of marketability discounts under the federal estate and gift tax regime.[30] While the removal of buy-out rights has helped many families achieve estate planning goals, simultaneously it has created huge problems for LLC members who do not have an

[25] *See id.*

[26] UNIFORM PARTNERSHIP ACT (1997) [RUPA] 7.01, available at http://www.uniformlaws.org/shared/docs/partnership/upa_final_97.pdf ; see also http://www.uniformlaws.org/LegislativeFactSheet.aspx?title=Partnership Act (enacted in Alabama, Alaska, Arizona, Arkansas, California, Colorado, Connecticut, Delaware, District of Columbia, Florida, Hawaii, Idaho, Illinois, Iowa, Kansas, Kentucky, Maine, Maryland, Minnesota, Mississippi, Montana, Nebraska, Nevada, New Jersey, New Mexico, North Dakota, Ohio, Oklahoma, Oregon, South Dakota, Tennessee, Texas, U.S. Virgin Islands, Utah, Vermont, Virginia, Washington, West Virginia, Wyoming)

[27] *Id.* 701(a) and 701(c).

[28] *Id.* 701(c).

[29] CARTER G. BISHOP & DANIEL S. KLEINBERGER, LIMITED LIABILITY COMPANIES 8.03 (2007)(discussing the evolution of member exit rights).

[30] Under IRC 2704(b) restrictions that arise from private operating agreements are disregarded for purposes of supporting estate tax discounts but restrictions stemming from the underlying state law are respected and thus, the LLC owner who has divested himself of a majority interest in an LLC under a state law that denies buy-out rights can readily argue for a minority discount for estate tax purposes). *See* Sandra K. Miller, *What Buy-Out Rights, Fiduciary Duties, and Dissolution Remedies Should Apply in the Case of the Minority Owner of a Limited Liability Company?* 38 HARV. J. LEGIS. 413, 432(2001)(discussing the elimination of exit rights following the revision in Treasury tax classification rules).

updated operating agreement containing a buy-out provision with a valuation mechanism.[31]

One of the thorniest questions concerns valuation of a privately-held interest in a corporation or LLC – that is, whether a minority discount should be applied to reflect the fact that a minority interest lacks voting control and/or whether a marketability discount should be applied to reflect the difficulty of bringing a private company to market.[32] Thus, disputes can arise regarding whether the buy-out should be accomplished with reference to the "fair market value" or the "fair value" of the business entity.[33] The "fair market value" reflects the owner's proportionate share of the business, adjusted for any premiums or discounts that would arise were the business interest sold in the marketplace.[34] In contrast, "fair value" ignores adjustments entirely. The "fair market value"

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[31] *See* Chapman v. Regional Radiology Associates, PLLC, No. 2011-SC-000233-D, 2011 Ky. Lexis 364(Dec. 15, 2011).

[32] *See* SHANNON P. PRATT, ROBERT F. REILLY, ROBERT P. SCHWEIHS, VALUING A BUSINESS 298-365(5th ed. 2008)(discussing minority interest discounts, control premiums, and discussing other discounts including the lack of marketability discount). *See also* Bernier v. Bernier, 873 N.E. 2d 216, 222-224(Mass. 2007)(considering discrepancies in value due to discounts and distinguishing fair value from fair market value). *See also* Marsh v. Billington Farms, LLC., C.A. No. PB 04-3123, 2007 R.I. Super.LEXIS 105, at * 12-*13(R.I. Super. Ct. 2007)(concluding without discussing that the pro rata valuation approach should be taken to a buy-out of an LLC
interest as the result of oppressive conduct). *See also D*ouglas Moll, *Shareholder Oppression and "Fair Value": Of Discounts, Dates, and Dastardly Deeds in the Close Corporation,* 54 DUKE L. REV. 293, 297 (2004)(discussing the valuation issues in the context of disputes between shareholders of closely-held companies).

[33] *See* SHANNON P. PRATT, ROBERT F. REILLY & ROBERT P. SCHWEIHS, VALUING A BUSINESS : THE ANALYSIS AND APPRAISAL OF CLOSELY HELD COMPANIES 345-355 (5th ed. 2008).

[34] *See* Douglas Moll, Shareholder Oppression and "Fair Value": of Discounts, Dates, and Dastardly Deeds in the Close Corporation, DUKE L. REV. 293, 297(2004)(providing an overview of discounts and addressing the policy issues presented by competing approaches to business valuation).

of a business interest reflects what a willing buyer would pay a willing seller, neither being under a compulsion to sell, and both having a reasonable knowledge of relevant facts. [35] The "fair value" of the business simply reflects the owner's proportionate share of the business as a going business.[36] Discounts may include a "key man discount" to reflect the negative impact of the departure of key personnel,[37] or the "minority discount" that adjusts for a minority owner's lack of voting control.[38] Another common discount is the "marketability discount" that reflects the fact that it may take longer and may be more problematic to sell a private company than a public one.[39] Alternatively, buy-outs can be structured at "fair value" which ignores the above adjustments.[40]

While uncertainties exist in the valuation of all private business interests, irrespective of form, there is a particular lack of guidance in the case of the valuation of LLCs. Typically, in the absence of a buy-out agreement, the plaintiff seeking a buy-out will have to resort to a petition to dissolve the LLC, which will frequently result in a court-ordered buy-out in lieu of dissolution. However, as shown in Table I, most LLC statutes do not provide specific valuation guidance.[41]

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[35] *See* Rev. Rul. 59-60, 1959-1 C.B. 237(providing the landmark guide to business valuation used by the IRS in valuing business interests).
[36] *See id.*
[37] *See id.* (including a discount where the loss of an important person in the business has left the entity, thus having a downward effect on the value of a business).
[38] Sandra K. Miller, Discounts and Buyout in Minority LLC Valuation Disputes Involving Oppression or Divorce, 13 U. OF PA. J. BUS. LAW 607, 612-651 (2011)(providing an analysis of business valuation policy issues and calling for uniform business entity legislation to address valuation issues in private enterprises).
[39] *See id.* at 614.
[40] *See id.*
[41] *See* id. *See also* Table I.

Where valuation terms are not contained in the LLC statute, one can look to corporate and partnership prototypes. Unfortunately, there are subtle yet important differences among the corporate and partnership valuation guideposts. Both the corporate and partnership models eschew the minority discount, but have different views regarding the marketability discount. Section 701 of the Revised Uniform Partnership Act provides that a disassociated partner has the right the obtain a "buyout" of his interest at the greater of the liquidation value or the amount distributable to the dissociating partner if the entire business had been sold as a going concern without the dissociating partner.[42] The Comments to RUPA explain that the buyout price is formulated to reject the minority discount but *may* encompass the application of a marketability discount or other relevant discounts.[43] Interestingly, the Comments indicate that other

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[42] *See* the REVISED UNIFORM PARTNERSHIP ACT 701 *available at* http://www.law.upenn.edu/bll/archives/ulc/uparta/1997act_final.htm.

> (a) If a partner is dissociated from a partnership without resulting in a dissolution and winding up of the partnership business under Section 801, the partnership shall cause the dissociated partner's interest in the partnership to be purchased for a buyout price determined pursuant to subsection (b).
>
> (b) The buyout price of a dissociated partner's interest is the amount that would have been distributable to the dissociating partner under Section 807(b) if, on the date of dissociation, the assets of the partnership were sold at a price equal to the greater of the liquidation value or the value based on a sale of the entire business as a going concern without the dissociated partner and the partnership were wound up as of that date. Interest must be paid from the date of dissociation to the date of payment.

[43] Comment 3 provides:

discounts may be fair and appropriate to reflect the private nature of the firm or to factor in a discount for the loss of a key partner.[44] Like RUPA, The Principles of Corporate Governance reject the minority discount. However, the possibility of exceptions for the marketability discount is made only in extraordinary circumstances.[45] In contrast, the Model Business Corporation Act

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> The terms "fair market value" or "fair value" were not used because they are often considered terms of art having a special meaning depending on the context, such as in tax or corporate law. "Buyout price" is a new term. It is intended that the term be developed as an independent concept appropriate to the partnership buyout situation, while drawing on valuation principles developed elsewhere.
>
> Under subsection (b), the buyout price is the amount that would have been distributable to the dissociating partner under Section 807(b) if, on the date of dissociation, the assets of the partnership were sold at a price equal to the greater of liquidation value or going concern value without the departing partner. Liquidation value is not intended to mean distress sale value. Under general principles of valuation, the hypothetical selling price in either case should be the price that a willing and informed buyer would pay a willing and informed seller, with neither being under any compulsion to deal. *The notion of a minority discount in determining the buyout price is negated by valuing the business as a going concern. Other discounts, such as for a lack of marketability or the loss of a key partner, may be appropriate, however (emphasis added).*

[44] *See generally* Donald J. Weidner and John W. Larson, *The Revised Uniform Partnership Act,* 49 BUS. LAW. 1 (1993)(indicating that the buy-out to the dissociating partner should be based on the higher of the liquidation value or the going concern value, and that the dissociating partner should not be paid for his human capital that goes with him). *See* Warnick v. Warnick, 133 P. 3d 997, 1004(2006) (failing to discuss the marketability discount but holding that pursuant to Wyoming's partnership statute that included "willing buyer/willing seller language" there should be no reduction for hypothetical costs of selling the business where the business is continued after the buyout of the dissociating partner).

[45] *See* AMERICAN LAW INSTITUTE, PRINCIPLES OF CORPORATE GOVERNANCE ALI § 7.22 (2010).

contains a broad prohibition of both the "minority discount" and the "marketability discount" in its definition of "fair value" governing the purchase in lieu of a judicial dissolution.[46] Thus, the valuation guidelines in the partnership and corporate arenas are not uniform.

Clearly, there are compelling policy reasons to eschew the minority discount which have been widely noted in the literature on minority conflicts.[47] Arguably, the minority discount facilitates rather than deters oppressive minority conduct and interjects substantial uncertainties in the business valuation process.[48] Also there are persuasive arguments against the marketability discount, which is widely criticized for double-counting or duplicating reductions that are already made by the valuation expert in valuing the underlying business.[49] The marketability discount arguably has no place in a small business that was never intended for sale,[50] and has been roundly criticized for contributing to the overall undervaluation of an active minority owner who has been squeezed

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[46] *See* 3 MODEL BUS. CORP. ACT § 14.34. (authorizing a buy-out in lieu of a judicial dissolution) and § 13.01(4) at 13-3 (1998) (providing guidelines for determining fair value defined as "…the value of the corporation's shares …using customary and current valuation concepts…without discounting for lack of marketability or minority status"). *See also* App. D and see Brown v. Arp. & Hammond Hardware Co., 141 P.3d 673, 684-685(Wy. 2006)(offering a superb history of the valuation guidelines contained in the Model Business Corporation Act).

[47] *See* Cavalier Oil Corp. v. Harnett, 564 A. 2d 1137, 1145(Del. 1989)(eschewing the minority discount). See also Douglas Moll, Shareholder *Oppression and "Fair Value": of Discounts, Dates, and Dastardly Deeds in the Close Corporation,* DUKE L. REV. 293, 297(2004); *See also* Sandra K. Miller, Discounts and Buyout in Minority LLC Valuation Disputes Involving Oppression or Divorce, 13 U. OF PA. J. BUS. LAW 607, 612-651 (2011)

[48] See Elder v. Elder, No. 2006AP2937, 2007 Wis. App. LEXIS 1130(Wis. App. Dec. 27, 2007).

[49] See Brown v. Brown, 792 A. 2d 463, 475(N.J. Super. Ct. App. Div. 2002).

[50] Harry Haynesworth, Valuation of Business Interests, 33 MERCER L. REV. 457, 459(1982).

out of an LLC which is already undervalued since the value normally does not include the value of the minority owner's expectation interest in future employment.[51] Nevertheless, some states such as Florida[52] and New York[53] have rejected the minority discount but permit the discount for the lack of marketability.

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[51] Douglas Moll, Shareholder *Oppression and "Fair Value": of Discounts, Dates, and Dastardly Deeds in the Close Corporation,* DUKE L. REV. 293, 349(2004);

[52] In Munshower v. Kolbenheyer, 732 So. 2d 385(Fla. 3d DCA 1999)(upholding the marketability discount but providing little analysis, and not containing a discussion of the minority discount). It should be noted that this decision was reached prior to Florida's statutory changes prohibiting the minority and marketability discounts in corporations with ten or fewer shareholders. *See* FLA. STAT. ANN. §607.1430(2010)(expressly disregarding minority and marketability discounts for corporations with ten or fewer shareholders but remaining silent with regard to larger corporations). *See also* FLA. STAT. ANN. § 608.4351 (5) (expressly disregarding minority or marketability discounts for LLCs with ten or fewer members.).

[53] *See* In Re Murphy, 903 NYS 2d 434, 437-438(N.Y. Sup. Ct. 2010)(applying a 15% marketability discount in a corporate purchase in lieu of a dissolution); *see also* In e Murphy, No. 002640/2006, 2008 N.Y. Misc. LEXISS 990 at *23-28 (N.Y. Sup. Ct. May 19, 2008)(observing precedents that have considered a marketability discount). *See* In Re Jamaica Acquisition, Inc., 901 N.Y.S.2d 907, at *17-*18(N.Y. Sup. Ct. 2009)(applying a marketability discount). *See also See* Mohlas Realty, LLC v. Koutelos, 2009 N.Y. Misc. LEXIS 4780(N.Y. Sup. Ct. April 7, 2009)(regarding a 30% lack of marketability discount) *See* Farrell Fitz, P.C., N.Y. Business Divorce, June 7, 2010, *available at* http://www.nybusinessdivorce.com/2010/06/articles/valuation-discounts/ruling-on-valuation-discounts-for-marketability-builtin-gains-tax-ends-rift-among-new-york-appellate-courts/. (discussing Matter of Murphy and noting that the Nassau County Commercial Division opinion had applied a 15% marketability discount to the value of the enterprise as a whole thereby rejecting precedents that had previously applied the marketability discount only to the goodwill of the company). *See* Blake v. Blake Agency, 486 N.Y.S. 2d 341, 349(N.Y. App. Div. 1985)(allowing a discount for lack of marketability where the marketability discount was applied to the goodwill of the company). In Hall v. King, 177 Misc. 2d 126, 133-134(N.Y. Sup. Ct. 1998)(observing the best approach is to apply the marketability discount to the company as a whole, thus disagreeing with prior applications of the discount to goodwill only in Whalen v. Whalen's Moving & Storage Co., 612 N.Y.S.2d 165, 166 (N.Y. Sup. Ct. 1996) and in

Many small entrepreneurs are overwhelmed with operational business matters, and have difficulty follow through on advice to maintain updated LLC operating agreements and buy-out provisions. As more fully described in Part II, COSO's Framework for Enterprise Risk Management (ERM) can help the

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Matter of Cinque v. Largo Enterprises, 212 AD2d 608, 610(N.Y. Sup. Ct. 1995). *See* In re Jamaica Acquisition Inc., 901 N.Y.S. 2d 907, at *16-*18 (N.Y. Sup. 2009), (observing that "upon a fair ready of Whalen and Cinique, the court is left without a reason for the rulings vis-à-vis goodwill v. other assets of an enterprise" and upholding the application of the marketability discount to the entire enterprise). *See* Raskin v. Karl, 129 A.D.2d 642, 644-645(N.Y. App. 1987)(applying the marketability discount in the context of a corporation dissolution case).Matter of Blake v. Blake Agency, 107 A.D.2d 139, 149(N.Y. App. Div. 1985)(applying a marketability discount). Note that some cases have rejected the marketability discount in the case of real estate holding companies. *See* Chiu v. Chui, 2013 NY Slip Op 30033(U)(2013) (accepting valuation testimony applying a zero marketability discount for an LLC holding real estate); *But see* Giamo v. Vitale, 2012 N.Y. Slip Op. 08778(1st Dept. Dec. 20, 2012)(applying a discount for lack of marketability in the valuation of a real estate holding company, and reversing the lower court opinion in Giamo v. Vitale, Supreme Court, New York County (Aug. 26, 2011) that the discount for lack of marketability was inappropriate because the real estate portfolio had unique attributes rendering shares very marketable). . Some New Jersey decisions have rejected both the minority and marketability discount. *See* Wheaton v. Smith, 734 A. 2d 738, 750-751(N.J. 1999)(observing that in appraisal actions the marketability discount should generally not apply and finding no extraordinary circumstances that would justify the discount where the dissenting shareholders had exercised their appraisal rights because they lacked confidence in new management). *Compare* Balsamides v. Protameen Chems. Inc., 734 A. 2d 721 (N.J. 1999)(decided the same day as Wheaton but recognizing the lack of marketability discount in extraordinary circumstances where there was a feud between two owners of a corporation and considerations of equity justified the marketability discount under unusual facts where the court ordered one fifty percent owner to buy out the other owner who had engaged in oppressive conduct). Subsequently, in Brown v. Brown, 792 A. 2d 463, 477-478 a N.J. appellate court refused to find extraordinary circumstances justifying a marketability discount in connection with a divorce in the valuation of the husband's minority ownership of a family florist where there was no evidence of a possible sale of the business, presumably making market considerations relevant.

private company set an agenda for implementing legal advice and for monitoring progress toward stated legal compliance goals. Part III and Table V explains how the ERM Framework can be used to promote communication among private business owners and to provide a systematic process for updating shareholders or LLC operating agreements.

B. The Continuing Problem of Veil-Piercing

Respecting the corporation or LLC as an entity separate from the beneficial owners is nearly as important to the privately-owned business as an up-to-date buy-out and valuation agreement.[54] Veil-piercing, the legal doctrine that allows a court to impose personal liability on the controlling corporate or LLC owner where there has been inequitable conduct or an abuse of the corporate form, certainly is nothing new. [55] As early as 1658 courts have set aside or "pierced" this liability protection in individual cases.[56] However, two factors indicate that closely-held business owners should pay increased attention to veil-piercing risks at this time. First, a recent empirical study suggests that veil-piercing rates may be even greater than previously estimated .[57] Second, there is a growing body of law that extends veil-piercing doctrines to the LLC.

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[54] *See* Peter B. Oh, *Veil-Piercing Unbound,* 93 BOSTON U. L. REV. 89, 90(2013)(providing an excellent overview of the troubling status of veil-piercing jurisprudence).D. G. Smith, *Piercing the Corporate Veil in Regulated Industries*, 4 BRIGHAM YOUNG U. L. REV. 1165, 1167 (2008). *See Irrigation Mart Inc. v. Gray,* 965 So. 2d. 988 (2d Cir. 2007)(involving business cards that did not properly disclose the name of the LLC); *see also* Orx Resourses Inc. v. MBW Exploration, LLC 32 So. 3d 931 (La. App. 2010)(involving a company that lacked a separate bank account).

[55] *See* Franklin A. Gevurtz, *Why Delaware LLCs?* 91 OR L. REV. 57, 77-78(2012)(discussing veil-piercing in connection with empirical studies of attorney preferences for state LLC formation).

[56] Peter B. Oh, *Veil-Piercing,* 89 TEXAS L. REV. 81, 85(2010).

[57] *Id.*

A landmark study of veil-piercing cases which was conducted by Prof. Robert Thompson over twenty years ago showed that courts pierced the corporate veil in approximately 40.18% of the cases surveyed.[58] The findings of a more recent study are even more dramatic. Prof. Peter Oh recently studied a data set of 2,908 cases dating from 1658 to 2006 and showed that courts proceeded to pierce the corporate veil in approximately 48.5% of the cases – an even higher rate than that contained in Prof. Thompson's earlier study. [59] In 100% of the cases, the veil-piercing took place with regard to privately-owned rather than publicly-owned corporations. [60] Different types of claims revealed different veil-piercing rates. Veil-piercing rates were highest for activities involving criminal violations (66.67%), [61] cases involving fraud (61.0%), [62]cases involving statutory violations (49.50%)[63] and cases involving torts (47.75%).[64] Veil-piercing rates were somewhat lower with regard to contract cases (46.4%).[65] Agency-related veil-piercing occurred in 52.63% of the cases.[66]

Further, courts are well along the way toward extending veil-piercing doctrines to the LLC.[67] Courts are piercing the veil of

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[58] Robert B. Thompson, *Piercing the Corporate Veil: An Empirical Study,* 76 CORNELL L. REV. 1036, 1038 (1991).
[59] Peter B. Oh, *Veil-Piercing,* 89 TEXAS L. REV. 81, 85(2010).
[60] *Id.*
[61] *Id.*
[62] *Id.*
[63] *Id.*
[64] *Id.*
[65] *Id.*
[66] *Id*. §301
[67] Regarding veil-piercing generally, *see In re Kandel,* No. 11-6297 and No. 12-6003, 2013 WL 310302(Bkrtcy N.D. Ohio2013)(setting forth veil-piercing factors under Ohio law to show that an entity is being used as an alter ego including (1) grossly inadequate capitalization, (2) failure to observe corporate formalities, (3) insolvency of the debtor corporation at the time the debt is incurred, (4) shareholders holding themselves out as personally liable for certain corporate obligations,(5) diversion of funds or other property of the company

property for personal use, (6) absence of corporate records, and (7) the fact that the corporation was a mere facade for the operations of the dominant shareholder(s)). For the adaptation of veil-piercing principles to the LLC, *see* Martin v. Freeman, No. 11CA0145, 2012 WL 311660 (Colo. App. Feb. 2, 2012); *See* Howell Contractors, Inc. v. Berling, No. 2010-CA-001755-MR, 2012 WL 5371838(Ky. Ct. App. Nov. 2, 2012)(citing the Restatement (Second) of Conflict of Laws indicating that the law of the state's incorporation applies to determine the shareholder's liability to creditors and applying Ohio veil-piercing law to an Ohio LLC but refusing to pierce since there was no evidence of fraud or an illegal acts). *See* Sun Nurseries, Inc. v. Lake Erma, LLC, 730 S.E. 2d 556, 564 (Ga. Ct. App. 2012) (refusing to find grounds for veil-piercing where an LLC transferred 93 real estate lots to two of its members who used them for collateral for loans and then transferred them back to the LLC, indicating that the transfers did not amount to an abuse of the corporate form). *See* Inter-tel Technologies, Inc. v. Linn Station Properties, 360 S.W. 3d 152, 164-165 (Ky 2012)(involving a landlord seeking to pierce the corporate veil of a parent and grandparent company where the corporation in question was arguably stripped of assets making continued recognition of the corporation an injustice, and indicating that actual fraud is not necessary to pierce the corporate veil); Haugen v. Dept. of Revenue, No. TC-MD 100052C, 2011 Ore. Tax LEXIS 187 (Or. T.C. April 26, 2011) (concluding that an LLC member who was a member of a manager-managed LLC, occasionally signed checks, and was listed as being in charge of hiring and firing employees, was not liable for unpaid Oregon withholding taxes since he lacked actual authority and control to pay or direct payment of the tax withholdings). Soroof Trading Development Co. Ltd. V. GE Fuel Cell Systems LLC, No. 10 Civ. 1391(LTS)(JCF), 2012 WL 209110(S. D. N.Y. Jan. 24, 2012)(piercing the veil of a Delaware LLC where the LLC was found to be the alter ego of its two members and where the LLC was unable to meet its contractual obligations and dissolve without any provision for unpaid claims). Bakke v. D & A Landscaping, LLC, No. 20110308, 2012 WL 3516859 (N.D. Aug. 16, 2012)(defendant LLC owner acted individually when giving his business card to the plaintiffs without designating the LLC and making the plaintiff aware of the LLC ant the court imposed liability directly upon the defendant without resort to veil-piercing). S*ee In re Steffner,* 2012 WL3563978(Bkrtcy E.D. Tenn. 2012)(involving a Tennessee LLC that was used in conducting polysomnography or sleep studies and indicating that veil-piercing may be justified when the entity has been used to work a fraud or injustice or where factors are present such as failure to collect paid in capital; gross undercapitalization, non-issuance of stock; sole ownership by one individual; use of the same office or business location; employment of same employees the use of the corporation as an instrumentality or business conduit

LLCs, notwithstanding LLC statutory attempts to limit veil-piercing where the LLC fails to observe formalities.[68] Veil-piercing continues to be a troubling legal quagmire, with one court listing as many as twenty potential triggers for lifting the veil of limited liability. [69] As one scholar recently observed, veil-piercing has "enabled judges to unleash their inner poet," [70] leaving

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diversion of assets or the manipulation of assets and liabilities; use of the corporation as a subterfuge in illegal transactions; transferring existing liability and non-arms length relationships); *See also* LLC v. McCullar, 765 F. Supp. 2d 1036, 1049-1050 (W.D. Tenn. 2011)(acknowledging that the veil-piercing doctrine applies to Tennessee LLCs). See Dave Rgani, *Tailoring the Corporate Veil-Piercing Doctrine to Limited Liability Companies in North Carolina,* 47 WAKE FOREST L. REV. 899, 919 (2012)(providing an overview of veil-piercing and suggesting that North Carolina place special emphasis on whether there was a fraud, a violation of a statutory duty, or unjust conduct); *See* Jeffrey K. Vandervoortl, *Piercing the Veil of Limited Liability Companies: The Need for a Better Standard,* 3 DEPAUL BUS. & COM. L.J. 51, 65-73(2004)(recommending that veil-piercing on grounds of lack of formalities or use of the LLC as an alter ego are inappropriate give the management flexibility of the LLC, but that veil-piercing on the basis of undercapitalization or fraud makes should be equally applicable to corporations and LLCs). *see also* Franklin A. Gevurtz, Piercing Piercing: *An Attempt to Lift the Veil of Confusion Surrounding the Doctrine of Piercing the Corporate Veil,* 76 OR. L. REV.853, 903-904 (1997)(arguing that the justifications for applying the law of the entity's state of formation via the internal affairs doctrine include shareholder choice and practicality but these rationales don't hold true in veil-piercing contexts, observing that tort victims don't have choice and that it is reasonable for states to seek to apply their own laws to business transactions occurring within the state).

[68] *See* Martin v. Freeman, No. 11CA0145, 2012 WL 311660(Colo. App. Feb. 2, 2012)(where a single-member LLC had entered into a contact to have plaintiff construct an airplane hangar, veil was pierced after the LLC had sold its only asset and distributed the proceeds to the LLCs single member owner, notwithstanding that the Colorado LLC statute provided that the failure to observe formalities is not itself a ground for imposing personal liability on the members for liabilities of the LLC).

[69] *See* Peter B. Oh, *Veil-Piercing Unbound,* 93 BOSTON U. L. REV. 89, 90(2013)(providing an excellent overview of the troubling status of veil-piercing jurisprudence). *See* Associated Vendors, Inc., v. Oakland Meat Coo., 26 Cal. Rptr. 806, 813-15(Dist. Ct. App. 1962)(indicating that veil-piercing included

[70] *See id.*

practitioners to fight over whether the corporation or LLC was used as an "alter-ego," an "instrumentality," or whether the entity was dominated by the owner to perpetrate a fraud, wrong, or injustice.[71]

Veil-piercing jurisprudence is unlikely to become predictable in the short term.[72] First and foremost, it is an equitable doctrine that is applied on a case-by-case basis. [73] However, sound internal controls may go a long way toward diminishing the presence of veil-piercing factors. Comingling of funds, unauthorized diversion of assets, treatment by an individual of the assets of a corporation as his own, unauthorized agency authority, or the holding out by an individual that she is personally liable for the debts of the corporation or LLC are all symptomatic of weak controls over financial reporting and over the business generally.[74] The likelihood of veil-piercing can be diminished greatly where the entity is properly formed, capitalized, and respected, where separate books are maintained, where all transactions are properly authorized, and where appropriate public representations of the business are made indicating the entity is a corporation or an LLC.[75]

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[71] *See id.*

[72] See Jeffrey K. Vandervoort, *Piercing the Veil of Limited Liability Companies: The Need for a Better Standard,* 2004 DEPAUL BUS. & COMMERCIAL L. J. 51, 92(2004)(recommending a broader definition of fraud).

[73] *See id.*

[74] *See* Associated Vendors, Inc. v. Oakland Meat Co., 26 Cal. Rptr. 806, 813-815(1962). *See also* Peter B. Oh, *Veil-Piercing,* 89 TEXAS L. REV. 81, 85(2010) (showing that agency law-related veil-piercing, something that can be potentially controlled by putting into authorization procedures, occurred at a rate of 52.63%

[75] *See* Breen v. Judge, 4 A. 3d 326, 332-333(Conn. App. 2010)(refusing to pierce the corporate veil where the company was properly formed, the LLC observed formalities, kept separate books, filed separate tax returns, and filed appropriate dissolution documents).

As more fully described in Part II and Part III, legal counsel, in collaboration with the company's outside accountants, should emphasize the importance of sound internal controls and an effective system legal monitoring system. [76] Table VI illustrates how COSO's Internal Control, and Enterprise Risk Management paradigm can be applied to help preserve the corporate veil of limited liability even in the case of the small private LLC or corporation. Unfortunately, these frameworks are woefully underutilized precisely where they are needed most.

C. External Obligations: The Overlooked Impact of Sarbanes Oxley upon the Small Private Entrepreneur

Although many of the regulations imposed by SOX apply to public rather than private companies, a number of the rules have indirectly impacted private enterprises.[77] Further, as more fully discussed below, some SOX provisions apply across-the-board to public as well as private concerns.

The internal control reporting and attestation requirements have been eased and now apply to all public companies except those who are non-accelerated filers (having a float less than $74 million).[78] However, the SOX compliance rules raise the reference

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[76] *See* Tables II to VI.

[77] Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, § 404, 116 Stat. 745, 789 (codified at 15 U.S.C. § 7262(2006)[hereinafter Sarbanes-Oxley Act].

[78] *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 989G(a), 124 Stat. 1376, 1948 (2010)(codified at 15 U.S. C. §7262(c). *See also* Donald C. Langevoort & Robert B. Thompson, *"Publicness" in Contemporary Securities Regulation Under the Jobs Act,* 101 GEO. L.J. 337, 351(2013)(providing an overview of the securities registration rules). The requirements for filing with the SEC were recently relaxed by the Jumpstart of Business Startups Act, Pub. L. No. 112-106, § 501, 126 Stat. 306 (2012)(relaxing the prior rule
requiring a company to file with the SEC if it had more than $10 million in total assets and a class of equity securities "held of record" by 500 or more persons at

point for best practices for all businesses. SOX's requirement of a Code of Conduct and ethics, although not required of private companies, sets a higher example for all organizations.[79] Similarly, requirements for a majority of independent directors put pressure on all businesses with public aspirations to add independent outsiders to management.[80] Further, lenders extending credit to private firms may look to selected SOX

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the end of its fiscal year and amending 12(g)(1)(A) of the Securities Exchange Act of 1934 (15 U.S.C. 78l(g)(1)(A)to require filing when the company reaches either 2,000 holders of record or 500 holders of record that are not accredited investors, whichever occurs sooner). *See* Sarbanes-Oxley Act §302 and §906 for the required rules concerning certifications of CFO and CEO. *See also* §404a for the rules applicable to non-accelerated filers regarding self-certifications regarding the adequacy of internal controls).
See John C. Coffee, *The Political Economy of Dodd-Frank: Why Financial Reform Tends to be Frustrated and Systemic Risk Perpetuated,* 97 CORNELL L. REV. 1019, 1037-1041(2012)(tracing the implementation of the internal control requirements under SOX).

[79] Sarbanes-Oxley § 406.

[80] Thomas C. Pearson & Gideon Mark, I*nvestigations, Inspections, and Audits in the Post-SOX Environment,* 86 NEB. L. REV. 43, 64-65(2007)(discussing the ripple effects of SOX). For the NY Stock Exchange listing requirement that a majority of board members be independent, see NY Stock Exchange Listing Requirement 303A.01, available at < http://nysemanual.nyse.com/LCMTools/PlatformViewer.asp?searched=1&selectednode=chp%5F1%5F4%5F3%5F1&CiRestriction=%22independence+requirements%22&manual=%2Flcm%2Fsections%2Flcm%2Dsections%2F> and see Nasdaq Rule 5605(b)(1) for its listing rule requiring a majority of independent directors, available at < http://nasdaq.cchwallstreet.com/NASDAQTools/PlatformViewer.asp?searched=1&selectednode=chp%5F1%5F1%5F4%5F3%5F8%5F3&CiRestriction=%22independence%22&manual=%2Fnasdaq%2Fmain%2Fnasdaq%2Dequityrules%2F>

assurances.[81] Venture capitalists may well expect private firms with public aspirations to move toward SOX compliance.[82] Nevertheless, SOX sets a higher reference point for all businesses, and in today's competitive financial marketplace, lenders are apt to give preference to tightly-managed firms. Thus, internal controls over accounting and financial matters as well as over legal responsibilities are increasingly important.

Aside from the indirect impact of SOX discussed above, several of SOX's provisions directly apply to public as well as and private firms. For example, the document shredding rules under U.S.C. § 1512 apply across the board to public as well as private enterprises and impose a fine or imprisonment for as much as 20 years. [83] Also, the document alteration or falsification provisions under U.S.C. § 1519 apply to private as well as public companies and similarly impose a maximum of fines or imprisonment of not more than 20 years, or both. [84] Section 1519 expands the obstruction of

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[81] *See* Board of Governors of the Federal Reserve Board, Senior Loan Officer Opinion Survey on Bank Lending Practices (January 2013), *available at http://www.federalreserve.gov/ and at* http://www.federalreserve.gov/boarddocs/snloansurvey/201302/fullreport.pdf

[82] *See* Gabor Garai, Beth J. Felder, & David W. Kantaros, *Sarbanes-Oxley for Private Companies, A Compliance Guide Tailored Towards the Growth of Your Company,* available at < http://www.foley.com/files/tbl_s31Publications/FileUpload137/3253/Sarbanes_Oxley_Article.pdf>

[83] *See* 18 U.S.C.§ 1512(c). Sec. 1512(c) provides:

> whoever corruptly - 1) alters, destroys, mutilates, or conceals a record, document, or other object, or attempts to do so, with the intent to impair the object's integrity or availability for use in an official proceeding; or 2) otherwise obstructs, influences, or impedes any official proceeding, or attempts to do so, shall be fined under this title or imprisoned not more than 20 years, or both.

See also Albert Spaulding, Jr. and Mary Ashby Morrison, *Criminal Liability for Document Shredding After Arthur Anderson LLP,* 43 AM. BUS. L. J. 647, 650-651(2006). It should be noted that prosecutors have applied Section 1512(c) beyond securities fraud cases including

[84] 18 U.S.C.1519 provides:

justice provisions to cover the creation of new false documents, and extends their application beyond court proceedings such as to investigations or other administrative proceedings. [85] In light of the severity of these penalties and the fact that the penalties are being asserted outside of the specific context of SEC violations, extreme care must be taken by all companies, both private and public, with regard to the accuracy and completeness of information provided in connection with all federal investigations.[86]

Whoever knowingly alters, destroys, mutilates, conceals, covers up, falsifies, or makes a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence the investigation or proper administration of any matter within the jurisdiction of any department or agency of the United States or any case filed under title 11, or in relation to or contemplation of any such matter or case, shall be fined under this title, imprisoned not more than 20 years, or both.

[85] *See* Gary G. Grindler & Jason A. Jones, *Please Step Away From the Shredder and the "Delete" Key: §§ 802 and §1102 of the Sarbanes Oxley Ac*t, 41 AM. CRIM. L. REV. 67, 79(2004).

[86] *See* Sarah O'Rourke Schrup, *Obstruction of Justice: Unwarranted Expansion of 18 U.S.C. 1512(c)(1)*, 102 J. CRIM. L. & CRIMINOLOGY 25, 30 and 47-48 at note 144(2012)(criticizing prosecutors' broad application of 1512(c)(1) to garden variety drug possession cases and police misconduct cases and indicating that Congress intended 1512(c) to apply in connection with corporate fraud cases, fraud cases generally, or cases in which there is a judicial proceeding underway or imminent). It should be stressed that 1512(c)(1) has been applied outside of the narrow context of securities violations. *See* U.S. v. Castellar, 242 F. App. 773 (2d Cir. 2007)(involving an IRS investigation), U.S. v. Stevens, 771 F. Supp. 2d 556(D. Md. 2011(involving an FDA investigation), and U.S. v. Coren, No. 07-CR-265 (ENV) 2009 WL 2579260(E.D. N.Y. Aug. 20, 2009)(involving alternation of payroll records during a grand jury investigation). Similarly, Section 1519 has been applied outside of the context of securities violations. *See* U.S. v. Yielding, 657 F. 3d 688, 710-711(8th Cir. 2011)(involving the violation of a Medicare anti-kickback statute and aiding and abetting the falsification of a document based on the falsification of a promissory note with the intent to disguise checks paid as loans rather than kickbacks). S*ee also* SOX Changes Everything: Sarbanes-Oxlety Creates Personal Liability for Public and Private Companies and Their Executives for Violations Related to Environmental Issues,

As discussed below in part III, COSO's system for Enterprise Risk Management can provide a much-needed framework for the private firm's adoption of a Code of Ethics and a systematic way of managing legal risks – both of which are important given the demanding post-SOX legal and business environments.

D. The Expansion of Whistle-blower Protections Increases the Stakes of Private Company Legal Compliance

Federal and state provisions rewarding individuals for reporting a wide array of violations have been enacted in recent years. Whistle-blower statutes can implicate private as well as public firms. A variety of rewards and employee protections now exist that facilitate the reporting of legal violations to the state or federal authorities charged with monitoring legal compliance.[87]

Whistle-blower protection for the reporting of securities law violations is provided under Section 922 of Dodd-Frank.[88] The whistle-blower regime applies to any individual and not just to employees of public companies.[89] Section 922 of Dodd-Frank

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<http://www.wallerlaw.com/articles/2003/06/26/sox-changes-everythingsarbanes-oxley-creates-personal-liability-for-public-and-private-companies-and-their-executives-for-violations-related-to-environmental-issues.5752>

[87] *See* Rachel Goodson, *The Adequacy of Whistleblower Protection: Is the Cost to the Individual Whistleblower too High?* 12 HOUS. BUS. & TAX L.J. 161, 174 (2012)(indicating that all fifty states have whistleblower statutes of some kind).

[88] ***See* Dodd-Frank Wall Street Reform and Consumer Protection Act of 20 [§922, Pub. L. No. 111-203, 124 Stat. 1376, 1841-43, codified at 15 U.S. C.§ 78u-6(b)(1). Sec. 922 added Sec. 21F to the Securities and Exchange Act of 1934 and is codified at 15 U.S.C. § 78u-6.**

[89] *See* Securities Exchange Act of 1934 § 21F(b)(1)[15 U.S.C. §78 u-6(b) providing:

> In any covered judicial or administrative action, or related action, the Commission….shall pay an award …to…whistleblowers who voluntarily provided original information to the Commission that led to the successful enforcement of the covered judicial or administrative

provides for bounty payments of between 10 to 30 percent to whistleblowers who voluntarily provide original information to the SEC Commission regarding securities law violations. [90] Thus, for example, since the anti-fraud provisions of the Securities Exchange Act Section 10b and 10b-5 apply to everyone, it is quite conceivable that an individual whistleblower could disclose information about securities violations involving a private company. Moreover, Dodd-Frank expands the reach of whistleblower provisions under Sarbanes-Oxley by clarifying that whistleblower protection provisions that protect employees of public companies extend to employees of subsidiaries or affiliates that are private companies of publicly-traded companies whose financial information is included in the consolidated financial statements of a publicly–traded company.[91]

In addition to whistle-blowing incentives in connection with securities violations, the False Claims Act provides bounty awards for a range of violations of federal statutes. [92] These federal violations can involve anything from Medicaid to military fraud. In addition, special statutory whistleblower provisions offer between 15% to 30% of the collected proceeds from tax fraud disclosures.[93] Overall, the IRS has developed an aggressive

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action, or related action, in the aggregate amount equal to [10 to 30%of any monetary sanctions…).

[90] *See* 21F(b)(1)[15 U.S.C. §78 u-6(b)Awards]

[91] *See* Chinyere Ajanwachuku, *An In House Decision to Whistleblow,* 25 GEO. J. LEGAL ETHICS 379, 383(2012).

[92] *See* 31 U.S.C. 3729-33(2006). A summary of federal provisions can be found on the U.S. Dept. of Labor website at: http://www.dol.gov/dol/compliance/comp-whistleblower.htm .

[93] *See* 26 U.S.C. 7623 (2011). *See* Karie Davis-Nozemack & Sarah Webber, *Paying the IRS Whistleblower: A Critical Analysis of Collected Proceeds*, 32 VA. TAX. REV. 77, 86-87(2012)(discussing 2006 revisions to tax whistleblower payments under IRC 7623(a). *See* Geoffrey Christopher Rapp, *Mutiny by the Bounties? The Attempt to Reform Wall Street by the New Whistleblower Provisions of the Dodd-Frank Act,* 2012 B.Y.U.L. REV. 73, 79(2012)(arguing that empirical studies show that monetary incentives are effective in motivating

whistleblower protection office to encourage tax fraud disclosures, however payments will be reduced by 8.7% due to the sequestration reduction, effective March 1, 2013.[94] Further, the U.S. Department of Labor's Occupational Safety and Health Administration (OSHA) enforces whistleblower provisions of 21 statutes that protect employees who report legal violations involving workplace safety.[95] Such safety issues arise in a vast array of industries. [96]

Finally, the Equal Employment Opportunity Commission (EEOC) provides whistleblower protection to those reporting various discriminatory actions under Title VII of the Civil Rights Act of 1964. [97] The whistle-blower protections cover retaliation taken against not just the employee but also against the employee's family members and/or other close.[98] Punitive as well as

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reporting of frauds and that whistleblowing is rarely frivolous, misleading or unreliable).

[94] See IRS Announcement, *available at* http://www.irs.gov/pub/whistleblower/2013SequesterNotice_WhistleblowerOffice_Final%202282013342pm_2.pdf (discussing the reductions that are required under the Balanced Budget & Emergency Deficit Control Act of 1985).

[95] *See* OSHA News Release 11-1136-NAT, Aug. 1, 2011, available at http://osha.gov

[96] *See* The Whistleblower Protection Program (providing OSHA protections in environmental and nuclear safety industries, transportation industries, and in the Consumer and Investor area), *available at t*http://www.whistleblowers.gov/index.html .

[97] *See* Title VII of the Civil Rights Act of 1964 (Pub. L. 88-352), 42 U.S.C.2000e. *See also* < http://www.eeoc.gov/laws/statutes/titlevii.cfm>.

[98] *See* Thompson v. North American Stainless, LP, 131 S.Ct. 863, 870-871(2011)(holding that an employee's fiancé who was fired allegedly after the employee reported a sexual harassment violation had standing to sue and was within the zone of those sought to be protected by Title VII of the Civil Rights Act). *See* Brandon Underwood, *Third Party Retaliation Claims After Thompson v. North American Stainless,* 38 IOWA J. CORP. L. 463, 482(2013)(recommending that employers modify their human resources procedures to ensure that they document the facts surrounding employer knowledge of relationship and discipline procedures, indicating that plaintiffs will have to establish a close

compensatory damages are authorized. Moreover, with regard to harassment, whether because of race, sex, color, or religion, employers are responsible for the acts of its supervisors unless the employer puts into place sound preventive or corrective opportunities.[99]

In addition to federal whistleblower rewards and protections, there are many state whistleblower provisions.[100] Under a complex network of statutes, such state whistleblower provisions may affect public and/or private companies. Some of these state whistleblower protections are quite broad. For example the Connecticut whistleblower statute makes it unlawful for a public or private employer to discriminate against an employee for the reporting of a violation or a suspected violation of any state, federal or local law.[101] The emergence of federal and state whistle-blower provisions clearly raises the likelihood that violations will be discovered, thus makes legal compliance measures increasingly important for all firms - public and private alike.

E. Federal Sentencing Guidelines Demand Effective Legal Compliance Programs for All Firms, Public or Private

Federal Sentencing guidelines continue to place a premium upon legal compliance.[102] Again, such guidelines are not just of concern

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enough relationship between the complaining employee and third party target, that the employer had knowledge that the relationship existed, and that their was a retaliatory intent).

[99] *See* Equal Employment Opportunity Commission*, Enforcement Guidance on Vicarious Employer Liability for Unlawful Harassment by Supervisors,* available at < http://www.eeoc.gov/policy/docs/harassment.html>.

[100] *See* http://www.ncsl.org/issues-research/labor/state-whistleblower-laws.aspx.

[101] *See* CONN. GEN. STAT. §4-61dd (2013). *See also* description of Connecticut Whistleblower program, *available at* Office of the Attorney Genera http://www.ct.gov/ag/cwp/view.asp?A=2095&Q=296820

[102] Fair Sentencing Act of 2010, Pub. L. No. 111-220, 24 Stat. 2372 (codified as amended in scattered sections of 21 U.S.C.

to public companies but have broad application to individuals and to all types of organizations.[103] The guidelines provide a formula for determining the amount a corporation should be fined factors, one of which is the effectiveness of the company's compliance program. [104] A key ingredient of an effective compliance program is the extent to which the organization offers reasonable steps for the corporation to take when it detects criminal conduct through its compliance program. [105]

A program that outlines what to do upon discovery of a legal violation is critically important on a number of levels. Whether involving a violation of the corporation, an individual employee, or both, the outlining of procedures once the violation is detected can be critically important to the organization. Unreported violations of federal or state criminal laws can have devastating results for an organization, as recently illustrated by a failure to properly report sexual crimes of a former employee.[106]

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[103] *See* Thomas F. O'Neil III & T. Brendan Kennedy, *Answering to a Higher Authority: Sovereign-Mandated Oversight in the Board Room and the C-Suite,* 17 FORDHAM J. CORP. & FIN. L. 299,312(2012)(discussing Federal Sentencing Guidelines generally and the DOJ's use of corporate settlement agreements to institute legal compliance programs to institute new processes, training, and monitoring to detect and prevent unlawful conduct).

[104] *Id*. Diana E. Murphy, *The Federal Sentencing Guidelines for Corporations: A Decade of Promoting Compliance and Ethics,* 87 IOWA L. REV. 697, 710-711(2002)(discussing the way in which the Federal Sentencing Guidelines promote incentives for legal compliance).

[105] *Id.*

[106] *See* Mark Viera, *Former Coach at Penn State is Charged with Abuse,* N.Y. Times, available at http://www.nytimes.com/2011/11/06/sports/ncaafootball/former-coach-at-penn-state-is-charged-with-abuse.html?pagewanted=all> (involving the failure to report the acts of sexual abuse of eight boys over a fifteen year period by the former defensive coach of Pennsylvania State University, and resulting in the indictment of certain university employee/ administrators).

In short, managing legal compliance is even more important given today's legal environment than ever before. Uncertainties in the law regarding valuation of LLCs and other private firms makes it even more important than previously to develop a strategy for fostering positive relations among private business owners and for maintaining current buy-out agreements with valuation mechanisms. The age-old problem of veil-piercing now appears to be more prevalent than previously thought, thus making it even more important to develop systems for maintaining the integrity of the corporation or LLC, for controlling the authority of agents, and for ensuring that all representations to the public are appropriately made. SOX, expanding whistleblower laws, and federal sentencing laws all directly and indirectly affect private firms making legal compliance critical for survival. The enterprise risk management system discussed below is not just for large public companies but offers an extremely helpful tool to systematically manage the legal risks of even the private firm with limited legal resources.

II. A MODEL FOR MANAGING PRIVATE COMPANY LEGAL RISKS AND HARNESSING OPPORTUNITIES

Given the legal environment described above, it is critical that private as well as public companies take a proactive stance with respect to managing both external and internal legal risks and utilizing legal opportunities. The two basic business models that companies are now using to maintain a reliable financial reporting system and to control a variety of business risks generally, can be tailored for use in monitoring the legal risks opportunities in the case of a private company – even one without in-house counsel or an internal legal department. [107] Preliminarily, it is helpful to

[107] COMMITTEE OF SPONSORING ORGANIZATIONS OF THE TREADWAY COMMISSION [hereinafter COSO], INTERNAL CONTROLS: INTEGRATED FRAMEWORK (IC)(1992) 2), *available at* < http://www.coso.org/documents/coso_framework_body_v6.pdf> (providing a

understand the basic features of an internal control system, the legal history as to why internal controls are important, and what the two leading models have to offer in the way of guidance for controlling legal risks and harnessing legal opportunities.

A. The Emergence of Internal Controls

Internal controls are usually thought of as the processes that management puts into place to ensure that the organization is reliably reporting financial results, properly complying with laws and regulations, and is achieving its operational objectives in an efficient manner.[108] Typical control activities might include: 1) segregation of duties (i.e. the person authorizing a transaction is separate from the person recording it, who is separate from the person having physical custody of assets); 2) use of authorizing procedures; 3) adequate documentation; 4) physical controls to safeguard assets; 5) reconciliation of main or control accounts and subsidiary accounts; and 6) having capable, trustworthy employees.[109]

Internal controls first received attention in 1972 in the wake of the Watergate scandal in which several large corporations had funded the break-in of the Democratic headquarters. [110] Thereafter, amidst

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model for ensuring a sound financial reporting system) and COMMITTEE OF SPONSORING ORGANIZATIONS OF THE TREADWAY COMMISSION [hereinafter COSO] ENTERPRISE RISK MANAGEMENT – INTEGRATED FRAMEWORK, (Sept. 2004) *available at* < http://www.coso.org/documents/coso_erm_executivesummary.pdf>. (providing a model for controlling a wide range of business risks beyond financial reporting, having to do with risks concerning virtually every aspect of the business).

[108] LARRY E. RITTENBERG, KARLA M. JOHNSTONE, & AUDREY A. GRAMLING, AUDITING: A BUSINESS RISK APPROACH 192 (7th ed. 2010).

[109] Id. at 205.

[110] Donald C. Langevoort, *Internal Controls After Sarbanes-Oxley: Revisiting Corporate Law's* 31 J. CORP. L. 949, 951-952 (2006).

concerns over questionable campaign financing and foreign bribery allegations, Congress introduced the Foreign Corrupt Practices Act in 1977 which added to the Securities Exchange Act the requirement that public companies maintain accurate books and records and a reasonable system of internal controls.[111]

Concerns about fraud triggered another round of study, in the mid-1980's when the Treadway Commission on Fraudulent Financial Reporting was formed and began an intensive study of internal controls.[112] As a result of the Commission's initial report in 1987, the Committee of Sponsoring Organizations (COSO) was formed, which was composed of representatives from five professional accounting and finance organizations. Also in 1987, Congress adopted the Federal Sentencing Guidelines [113] under which defendants can obtain penalty reductions where systems had been adopted to encourage legal compliance. Finally, in 1992, COSO published its report, *Internal Controls: An Integrated Framework (*IC) [114] and in 1994 published *Enterprise Risk Management – Integrated Framework* (ERM) to provide guidelines for developing internal controls and business strategies to manage

[111] *Id. See also* Joseph W. Yockey, *Choosing Governance in the FCPA Reform Debate,* 38 J. CORP. L/ 325. 329(2013)(discussing the increase in enforcement activities).

[112] *See generally* Joseph A. Grundfest & Max Berueffy, The Treadway Commission Report: Two Years Later, Jan. 26, 1989 available at http://www.sec.gov/news/speech/1989/012689grundfest.pdf.

[113] Kate Smith & Joseph A. Cabranes, *Judging Under the Federal Sentencing Guidelines*, 91 NORTHWESTERN U. L. REV. 1247(1997), *available at* http://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?article=2272&context=fss_papers

[114] COMMITTEE OF SPONSORING ORGANIZATIONS OF THE TREADWAY COMMISSION [hereinafter COSO], INTERNAL CONTROLS: INTEGRATED FRAMEWORK (IC)(1992) 2), *available at* < http://www.coso.org/documents/coso_framework_body_v6.pdf>

financial, operational, and legal risks facing contemporary organizations.[115]

Internal controls, ethics, and corporate governance again took center stage following the Enron debacle leading to the adoption of the Sarbanes-Oxley Act of 2002 (SOX). [116] Shortly thereafter, following the 2007-2008 financial crisis, concerns regarding internal controls and corporate governance re-surfaced, culminating in the enactment of and the Dodd-Frank Wall Street Reform and Consumer Protection Act.[117] Dodd-Frank ushered in increased regulatory oversight of public companies, new consumer financial protections, and increased whistleblower protections in connection with the sale of securities.

In the wake of SOX and Dodd-Frank legislation, COSO's two integrated frameworks – the first dealing with internal controls (IC), and the second, expanded paradigm that includes enterprise risk management (ERM) - the management of business risks beyond those strictly associated with financial reporting, are leading tools in the post-SOX environment.

B. The Internal Control (IC) Framework and the Enterprise Risk Management (ERM) Frameworks

COSO's frameworks for IC and ERM have much in common. The *Internal Control – Integrated Framework (IC)* is an essential part of Enterprise Risk Management. [118] Both models provide

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[115] COSO, ENTERPRISE RISK MANAGEMENT – INTEGRATED FRAMEWORK, (Sept. 2004) *available at* < http://www.coso.org/documents/coso_erm_executivesummary.pdf>.

[116] Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, § 404, 116 Stat. 745, 789 (codified at 15 U.S.C. § 7262(2006)

[117] *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376(2010)(codified in scattered sections of 12 U.S.C.).

[118] COSO, INTERNAL CONTROL INTEGRATED FRAMEWORK (Dec. 2011).< http://www.coso.org/documents/coso_framework_body_v6.pdf> . COSO is in

processes for providing reasonable assurance regarding the achievement of the entity's objectives. However, ERM expands the IC model and provides a guide for addressing a wide range of risks as well as opportunities. Events that might be monitored under ERM could include anything from economic events (i.e. a new competitor enters the market), social changes (i.e. increase in empty nesters), political changes (increase in taxation), and technological or other important developments. [119] The focus of ERM goes far beyond controls for assuring that there is a reliable financial reporting system in place.

As depicted in Table II, The ERM model asks that the organization establish four categories of objectives including strategic, operations, reporting, and compliance objectives.[120] Strategic objectives are the organization's highest level goals – those goals most closely aligned with the organization's mission.[121] As one might expect, operations objectives concern effectiveness and efficiency of operations. Reporting pertains to objectives associated with having a reliable reporting system. Finally, compliance concerns the company's compliance with laws and regulations.[122]

The ERM model consists of eight major components including:

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the process of updated the IC framework and just issued a draft revision which has yet to be finalized. A comment period has now ended. The draft does not fundamentally change the key features of the IC framework.

[119] COSO, ENTERPRISE RISK MANAGEMENT – INTEGRATED FRAMEWORK, EXECUTIVE SUMMARY FRAMEWORK (Sept. 2004) *available at* < http://www.coso.org/documents/coso_erm_executivesummary.pdf>.

[120] *Id.* at 21.

[121] *Id.*

[122] *Id.* The IC paradigm recognizes the objectives concerning operations, reporting, and compliance but does not speak to strategic objectives. See COSO, INTERNAL CONTROL INTEGRATED FRAMEWORK(1992), available at < http://www.coso.org/guidance.htm>

1) *The Internal Environment*: The internal environment focuses on the tone of the organization, its philosophy, integrity, ethical values, etc.

2) *Objective Setting*: Objective setting involves the setting of objectives that flow from the organization's mission regarding overall strategy, operations, reporting and compliance.

3) *Event Identification:* Event identification refers to events that are relevant to the objectives and which will get management's attention.

4) *Event Assessment:* Risk assessment concerns an evaluation of the risks presented. 5) *Risk Response:* Risk response entails either avoiding the risk if possible, accepting it, reducing it, etc. depending upon the organization's risk appetite.

6) *Control Activities:* Control activities are those policies and procedures that make sure that the organization is in fact responding to the risk according to plan.

7) *Information and Communication:* Information and communication concerns the effective communication of relevant information throughout the organization.

8) *Monitoring:* [123] Monitoring involves evaluating the process and determining whether any modifications should be made.[124]

These eight interrelated components comprise the framework companies use to design their internal control systems to meet the strategic, operating, reporting and compliance objectives. Part III

[123] *Id.* at 5. The IC model contains five components including the control environment, risk assessment, control activities, information and communication, and monitoring.
[124] *Id.* at 6.

provides examples of how these components can be used to address internal and external legal risks.

III. PRIVATE COMPANY STRATEGIC LEGAL AND COMPLIANCE PLANNING USING COSO's ERM FRAMEWORK

The ERM paradigm calls for the establishment of objectives with regard to strategy, operations, reporting, and compliance. The two major focal points of the ERM paradigm that are particularly relevant to legal matters concern the objectives pertaining to : 1) Strategic Planning; and 2) Compliance. Successful strategic planning and effective compliance go hand-in-hand and should flow from the company's overall mission and related business plans. Now more than ever it may be beneficial to coordinate legal and accounting services for the private firm. If the company has no in-house counsel, it may be helpful for the outside counsel to collaborate with the firm's certified public accountants in establishing the company's strategic legal plans and legal compliance objectives. *See Table IV*

A. Strategic Legal Planning and Compliance Planning Within ERM Framework

Introducing the ERM framework to clients who with growing private businesses inspires management to engage in the development of a mission, map out a short-term and long-term business plan, and articulate a Code of Ethics.[125] COSO's ERM framework begins with an articulation of the company's mission or vision. Thereafter, management establishes four major categories of objectives: 1) strategic objectives; 2) operational objectives; 3)

[125] *See* George J. Siedel & Helena Haapio, *Using Proactive Law as a Competitive Advantage,* 47 AM. BUS. L. J. 641, 644-645(2010).

reporting objectives; and 4) compliance objectives.[126] Operational objectives deal with the operations of the company and reporting objectives focus on financial and related reporting – neither of which deal squarely with legal planning. However, legal planning is clearly implicated when it comes to the firm's overall strategic planning and compliance planning. See Tables II and III.

1. A Code of Conduct – Not Just for the Public Firm:

Legal planning must be done within the context of the private firm's short and long-range goals. Regardless of whether the firm plans on going public, a code of conduct provides a critical starting point in paving the way toward future growth. Clearly, a code of ethics is required of public companies, firms desiring government contracts, and those seeking state funding. But beyond that, the code of conduct can help foster an internal culture that fosters legal compliance. Moreover, it can help achieve managerial objectives. As noted by Lynn Sharp Paine, Managers' reasons for turning to values often reflect their company's stage of development. Executives of large, well-established companies typically talk about protecting their company's reputation or its brand, whereas entrepreneurs are understandably more likely to talk about building a reputation or establishing a brand.. For skeptics who wonder whether a struggling start-up can afford to worry about values, Scott Cook, the founder of software maker Intuit, has a compelling answer. In his view, seeding the company's culture with the right values is "the most powerful thing you can do." "Ultimately, says Cook, "[the culture] will become more important to the success or

[126] *See* COMMITTEE OF SPONSORING ORGANIZATIONS OF THE TREADWAY COMMISSION [hereinafter COSO] ENTERPRISE RISK MANAGEMENT – INTEGRATED FRAMEWORK, 9 (Sept. 2004) *available at* < http://www.coso.org/documents/coso_erm_executivesummary.pdf>.

failure of your company than you are. The culture you establish will guide and teach all your people in all their decisions." [127]

The ERM Code of Conduct provides a model code of conduct that expressly captures legal compliance issues,[128] as do guidelines established under Federal Sentencing Guidelines.[129] It may be helpful for the private organization to consult both of these sources. The code of conduct can help to establish a culture of integrity and ethics – so indispensable given the current regulatory environment.[130]

2. Choice of Entity, Internal Ownership, Internal Governance Structure, and Other Strategic Legal Planning:

The ERM Framework defines strategy as the achievement of the entity's high-level goals that are consistent with its overall mission.[131] The firm's short and long-term objectives have profound legal implications in the four areas discussed below including the selection of the optimal legal entities, the development of the appropriate ownership relationships, the development of the appropriate internal governance structure; and other legal planning to harness legal opportunities to achieve a competitive advantage. See Table III.

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[127] LYNNE SHARP PAINE, VALUE SHIFT 7 (2003).

[128] *See* COSO, ENTERPRISE RISK MANAGEMENT –INTEGRATED FRAMEWORK, APPLICATION TECHNIQUES 9-10(Sept. 2004).

[129] *See* U.S. Sentencing Guidelines 8B2.1 Effective Compliance and Ethics Program < http://www.ucdmc.ucdavis.edu/compliance/pdf/ussg.pdf> . See Shanti Atkins and Scott Schneider, C*ode of Conduct Training and the Federal Sentencing Guidelines,* 54 HR MAGAZINE (2009), available at <http://www.shrm.org/Publications/hrmagazine/EditorialContent/Pages/0409legal1.aspx >.

[130] *See* COSO, ENTERPRISE RISK MANAGEMENT –INTEGRATED FRAMEWORK, APPLICATION TECHNIQUES 5.

[131] *See id.*

Legal entity planning is critical to control legal liability and to ensuring that the company is structured in a manner that will enable it to achieve its short and long-term goals. The private firm that has no plans of going public will undoubtedly benefit from an entity structure providing flow-thru taxation using one or more limited liability companies or S Corporations.[132] However, if the company plans to become public, C Corporation status is typically recommended, particularly because it positions the company to utilize the advantages of non-taxable reorganizations.[133]

Additionally, the internal governance structure of the firm is extremely important. Ownership in a private firm presents an illiquid investment. This leaves the minority investor in a particularly vulnerable position. As noted in Part I, disputes regarding valuation are extremely problematic given the uncertainty in the law regarding valuation.. Now, more than ever, it is important for the private company to contractually address buy-out and valuation issues. [134]

A plan to appropriately coordinate buy-out agreements with estate planning and to periodically update agreements is essential. Of course, for the private company with plans of going public, or with

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[132] *See* I.R.C §1362.

[133] *See* I.R.C §368.

[134] The problem of "investor lock in" is even more complicated if the business is formed as an LLC. A growing number of states have statutory judicial dissolution provisions similar to those provided for corporations. But LLCs are thought to be highly contractual business entities and if the private parties have not previously entered into their own LLC operating agreements and/or buy-out agreements, courts may be reluctant to order a judicial dissolution or a court-ordered buy-out. *See* Chapman v. Regional Radiology, No. 2011-SC-000233-D, 2011 Ky. LEXIS 364, at *20-*21(Dec. 15, 2011)(holding that by he withdrawing 40% owner of an LLC was not entitled to a return of his capital because the Kentucky LLC statute does not require the LLC to make a distribution upon a member's withdrawal and failing to order a dissolution, thus locking in the capital of the withdrawing LLC member).

plans of participating in a private equity and/or merger or acquisition in the future, the company will need to create of a Board of Directors comprised of a majority of independent directors.[135]

Other strategic efforts should focus on proactive planning to ensure that the company is using legal and tax opportunities to obtain a competitive edge. For example, securing patents or licenses can give the firm an advantage. Providing timely input into the legislative or administrative rule-making process can also benefit a business. As noted by Prof Constance Bagley, the PepsiCo Frito Lay division secured an advantage when they asked the Food and Drug Administration whether they could label selected products " 0 Trans Fat."[136] Thus, the ERM paradigm can help the private business develop "legal astuteness" – a valuable managerial capability of both achieving legal compliance objectives and securing legal advantages through proactive legal planning and participation in influencing legislative or administrative rule-making that affects the firm.[137]

3. Legal Compliance Planning: Coordinating With CPA and Implementing Legal Advice:

[135] *See* Corporate Governance Listing Standards, Sec. 303A, 312.03, and 313 of The Listed Company Manual, available at < http://usequities.nyx.com/regulation/listed-companies-compliance/corporate-governance> (providing a guide to relevant New York Stock Exchange listing standards); See also H. Rodgin Cohen and Glen T. Schleyer, Shareholder *v. Director Control Over Social Policy Matters: Conflicting Trends in Corporate Governance,* 26 N.D. J. IF LAW, ETHICS, & PUBLIC POLICY 81, 96-99(2012)(providing an excellent history of New York and Nasdeq listing requirements Sarbanes-Oxley Act provisions regarding governance, and post-Sox regulatory developments).

[136] Constance E. Bagley, *What's Law Got to Do With It?: Integrating Law and Strategy* 47 AM. BUS. L. J. 587, 598(2010).

[137] *See id.* at 629-630.

As indicated in Part I above, legal compliance planning for the private company is increasingly important given uncertainties in the law regarding valuation of LLCs and the potential for disputes among owners, the continuing problem of veil-piercing, and expanding whistleblower laws, and federal sentencing guidelines. It is no longer enough for lawyers to offer sound theoretical advice. The superior attorney – the one with a competitive advantage in the legal marketplace – will be the one who offers legal advice with tangible suggestions as to how the advice can be implemented and monitored.[138]

The benefit of using the ERM framework to monitor the attainment of legal planning and compliance objectives is that it is an integral part of the framework that is being used to audit internal controls in conformity with SOX.[139] Thus, the ERM framework is a helpful tool for the private company with aspirations of becoming publicly-held in the future.[140] The post-SOX business environment is one marked by increased vigilance.[141] As one commentator recently noted, "SOX has had substantial ripple effects on corporate activity, government oversight, private companies, and non-profit organizations."[142] Private companies,

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[138] *See* Peggy Kubicz Hall, *Legal Costs in Minnesota: I've Looked at Fees From Both Sides Now: A Perspective on Market-Valued Pricing for Legal Services,* 39 WM. MITCHELL L. REV. 154, 161-162(2012).

[139] COSO, ENTERPRISE RISK MANAGEMENT – INTEGRATED FRAMEWORK, EXECUTIVE SUMMARY FRAMEWORK 8 (Sept. 2004) (observing "internal control is an integral part of enterprise risk management…this enterprise risk framework encompasses internal control, forming a more robust conceptualization and tool for management…While only portions of the text of Internal Control-Integrated Framework are reproduced in this framework, the entirety of the framework is incorporated by reference into this one.")

[140] 15 U.S.C. § 404 (2006).

[141] Thomas C. Pearson & Gideon Mark, *Investigations, Inspections, and Audits in the Post-SOX Environment,* 86 NEB. L. REV. 43, 65-70(2007).

[142] *See id.* at 65-70(2007).

and in particular, larger private businesses, are voluntarily upgrading their accounting practices.[143]

For smaller businesses without inside legal counsel, it may be useful for the outside attorney to contact the company's CPA firm to determine what internal control and/or ERM strategies have already been recommended to the client. Particularly with regard to federal and state tax compliance, there may be processes that the CPA already has in mind that could dove-tail with the processes needed for other legal compliance matters. See Table IV.
The examples that follow demonstrate how the ERM framework can be used to address both internal governance matters, and external legal compliance matters. Table V Example 1 illustrates the use of ERM to achieve internal governance goals by systematically coordinating efforts to prepare and update shareholder and/or LLC agreements and to foster effective communication among business owners. Table VI Example II applies the ERM framework to systematically ensure that the corporate veil of limited liability will be preserved.

4. Additional Challenges Faced by Private Companies:

The segregation of duties and an independent board of directors lie at the heart of an effective ERM system, so essential to controlling accounting, legal and business risks.[144] Yet, owners of many private companies may argue that they can't afford sufficient staff to achieve a segregation of duties, and that outside management is expensive and cumbersome.[145] Nevertheless, overcoming these

[143] *See id.*
[144] LARRY E. RITTENBERG, KARLA M. JOHNSTONE, & AUDREY A. GRAMLING, AUDITING: A BUSINESS RISK APPROACH 13 (7th ed. 2010).
[145] Sensiba San Filipppo, *The Internal Controls in a Closely-Held Business, available at*
http://www.ssfllp.com/pdf/knowledge/IdeaCast1_CloselyHeldBusiness.pdf (recommending

obstacles may prove critical to success through the expansion of capital, growth through acquisition, or a plan to go public.
As one family business expert explained:

"Outsiders provide a system of checks and balances that can help make top managers accountable, offering credibility for management's actions…even board of directors or advisors without formal power should act as a further check… because of the influence their opinion will have on owner-manager behavior; all else equal, individuals tend to want the approval of their actions from friends and peers." Outside board members can effectively steer the dynamics of board discussion to be more objective and constructive…in this context, the outside directors' involvement helps underscore that business decisions are adequately arrived at, taking into account all interests. [146]

Sharing or rotating certain functions and/or the creation of a board of directors may deter or expose sexual harassment, environmental violations, or any number of frauds and/or irregularities.[147] Family business experts stress that corporate governance can be significantly improved even without outside board members so long as the board has strategic competencies, a diversity of skills, a forum of open communication, and a culture of open dissent. [148] Ultimately in the long run, however, audited financial statements,

[146] Sundaramurthy, Chamu, *Sustaining Trust Within Family Businesses*, 21.1 FAMILY BUS. REV. 89, 92(Mar. 2008).
[147] *Id.*
[148] *See* Suzanne Lane, Joseph Astrachan, Andrew Keyt, & Kristi McMillan, *Guidelines for Family Business Boards of Directors,* 19, 2 FAMILY BUS. REVIEW 147, 149-152(2006)(comparing the market model of corporate governance relying on independent board members typical of public companies in the U.S. and U.K., and the Control Model typical of Asia, Latin America, and continental Europe wherein the company is governed by one or more family shareholders, and indicating that family businesses following the control model where conflicts of interest are endemic can nevertheless be structured to foster accountability).

sound internal controls, and a competent board of directors or board of managers with some or most outside directors will prove invaluable to the successful long-term growth of any private organization.

IV. CONCLUSION

Legal monitoring for private companies is increasingly important. Uncertainty in the law concerning business valuation makes it critically important for private business owners to have up-to-date buy-out agreements including comprehensive valuation provisions. The legal quagmire presented by veil-piercing jurisprudence and its extension to the LLC have increased the importance of internal controls over financial reporting and business practices generally. SOX has raised the standard for best business practices, and the risks associated with non-compliance have increased due to state and federal whistle-blowing provisions, and Federal Sentencing Guidelines. The Committee of Sponsoring Organizations of the Treadway Commission (COSO)'s *Enterprise Risk Management – Integrated Framework* (ERM) offers an effective tool for managing the legal risks facing the private company. However, until now, the Framework has been largely overlooked as a strategic legal planning and compliance tool for the private company. As illustrated above, ERM's eight-point Framework can be readily applied to manage a host of legal risks facing private companies today - including two of the most notorious ones – the internal risk of owner conflict and the external risk of veil-piercing.

Table I

Judicial Dissolution Provisions of LLCs
Judicial Dissolution Provisions Silent on Buy-Out/Valuation

Alabama	ALA. CODE ANN. §10-12-38
Alaska	ALASKA CODE §10.50.405
Arizona	ARIZ. REV. STAT ANN. §29-785 A.1-A.4
Arkansas	ARK. CODE ANN.§ 4-32-902
Colorado	COLO. REV. STAT. ANN. § 7-80-810
Connecticut	CONN. GEN. STAT. ANN. §34-207
Delaware	DEL. CODE ANN. TIT. 6 §18-802
District of Columbia	D.C. CODE ANN. §29-807.01
Florida	FLA. STAT. ANN. §608.449(2)(a)-(b) *
Georgia	GA. CODE ANN.§14-11-603(A)**
Hawaii	HAW. REV. STAT. tit. 23A, §428-801
Idaho	ID CODE ANN. 53-643
Indiana	IND. CODE ANN. §23-18-2
Iowa	IOWA CODE ANN. §490A.1302
Kansas	KAN. STAT. ANN. 17-76, 117
Kentucky	KY. REV. STAT. ANN. §275.290
Louisiana	LA. REV. STAT. ANN. §12:1335
Maine	ME. REV. STAT. TIT. 31, §1595
Maryland	MD. CODE ANN. §4A-903
Massachusetts	MASS. ANN. LAWS CH. 156C, §44
Michigan	MICH. COMP. LAWS ANN. §450.4802

Mississippi	MISS. CODE ANN. §79-29-803
Missouri	MO. ANN. STAT. §347.143
Montana	MONT. CODE ANN. §35-8-902
Nebraska	NEB. REV. STAT. ANN. §21-147
Nevada	NEV. REV. STAT. ANN. §86.495
New Hampshire	N.H. REV. STAT. ANN. §304-C:134 ***
New Jersey	N.J. REV. STAT. ANN. §42:48
New Mexico	N.M. STAT. ANN. §53-19-40
New York	N.Y. LT. LIAB. CO. LAW §702****
North Carolina	N.C. GEN. STAT. §57C-6-02
Ohio	OHIO REV. CODE ANN. §1705.47 *****
Oklahoma	OKLA. STAT. TIT. 18, §2038
Oregon	OR. REV. STAT. ANN.§63.661
Rhode Island	R.I. GEN. LAWS §7-16-40
South Carolina	S. C. CODE ANN. §33-44-801.. Revised Uniform Limited Liability Company Act was introduced on Feb. 12, 2013, and its dissolution provision is silent regarding buy-out and valuation at §M33-43-701, *available at* http://www.scstatehouse.gov/sess120_2013-2014/bills/377.htm
South Dakota	S.D. CODIFIED LAWS §47-34A-801(A)(4)(IV)
Vermont	VT STAT. ANN. tit. 11 u §47-30101
Virginia	VA. CODE ANN. §13.1-1047

Washington	WASH. REV. CODE §25.15.275 ******
West Virginia	W. VA. CODE §31B-1-801(b)(5)
Wisconsin	WIS. STAT. ANN. §83.0902
Wyoming	WYO. STAT. ANN. §17-29701

* Compare FLA. STAT. ANN. §608.4351 providing appraisal rights at "fair value" with fair value to be determined without discounting for minority or marketability discounts for LLCs with ten or fewer members.
** Compare GA. CODE ANN.§14-11-1108 providing Dissenters' Rights at "fair value."
***Compare N.H. REV. STAT. ANN. §304-C:166 providing Dissenters' Rights at "fair value"
**** Compare N.Y. BUS. CORP. §623 providing Dissenters' Rights at "fair value"
*****Compare OHIO REV. CODE ANN. §1705.41 providing Dissenters' Rights at fair cash value
******Compare WASH. REV. CODE §25.15.430 providing Dissenters' Rights at "fair value"

Judicial Dissolution Provisions Containing Express Language Referring to Buy-out at "Fair Market Value"

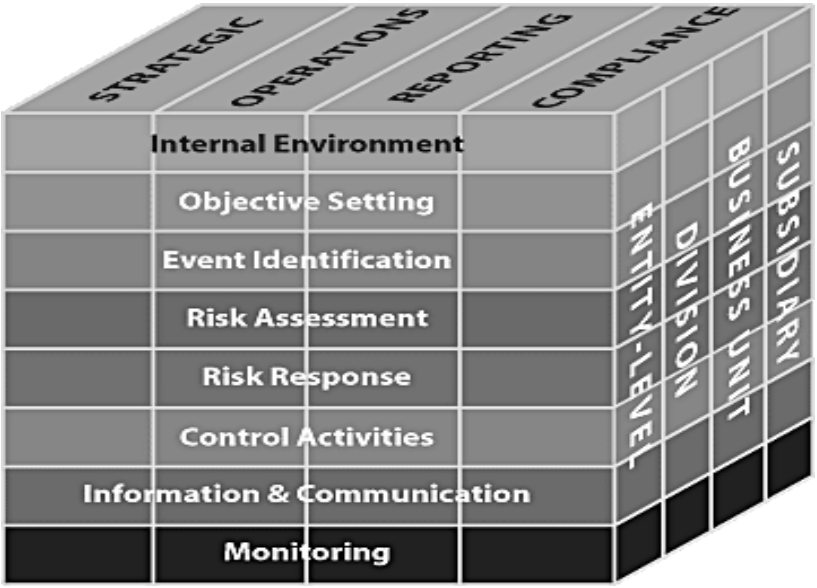
California LLC	CAL. CORP. CODE ANN. §17707.03(1) effective Jan. 1, 2014; see §17351 & §17604 which will be repealed effective Jan. 1, 2014.
Utah LLC	UTAH CODE ANN. §48-3-702 providing for a purchase in lieu of dissolution at "fair market value"

Judicial Dissolution Provisions Containing Express Language Specifying Distribution/Buyout at "Fair Value"

Minnesota	MINN. STAT. ANN. §322B.833
North Dakota	N.D. CENT. CODE §10-32-119
Pennsylvania	PA. CONS. STAT. ANN. §8933 providing for distribution of fair value upon dissociation; §8972 authorizes dissolution .
Tennessee	TENN. CODE ANN. §48-249-617 authorizing judicial dissolution; 48-249-503 and 48-249-506 providing for purchase at fair value determined with reference to going concern value, agreements fixing price, appraiser recommendations, and legal or financial constraints.
Texas	TEX. BUS. ORGS. CODE ANN. §§ 101.205

Table II

COSO's Enterprise Risk Management – Integrated Framework (2004)



COSO Released Control - Integrated Framework for Public Comment available at <December 19, 2011 http://www.coso.org/> Applying COCO's Enterprise Risk Management-Integrated Framework, Power Point prepared by the Institute of Internal Auditors, http://www.theiia.org/guidance/additional-resources/coso-related-resources/

Table III

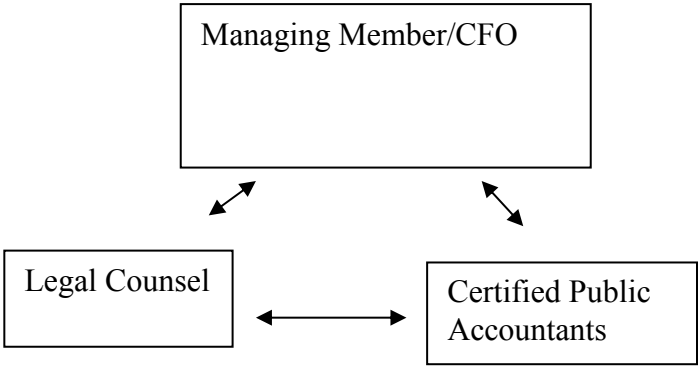
Private Legal Monitoring

Strategic Legal Planning	*Legal Compliance*
Code of Conduct	Federal/State/Local Law Compliance
Choice of Entity	Contractual Obligations
Internal Governance	Loan Obligations
Management Structure	Tort Laws
LLC /Shareholder Agreements	Environmental Laws
Buy-out Agreements	Employment Laws
Succession or Exit Plan	Privacy Laws
Proactive Legal Planning	Tax Laws
Licenses	Licensing Laws
Patents	Intellectual Property
Trademarks	Criminal
Lobbying	Other

COSO Released Control - Integrated Framework for Public Comment

Table IV

SETTING THE AGENDA IN THE PRIVATE COMPANY WITH LEGAL COUNSEL & CPA



Code of Ethics

Strategic Legal Planning

Planning for Legal Compliance

Table V

Example I: Applying ERM to Foster Sound Internal Governance Practices for the Private Company

Phase I Setting the Tone at the Top for Improved Owner Communication and Updated Legal Documents

The CEO and/or owners must set the tone at the top for integrity and ethics. Although many small firms conduct business quite informally, it may be beneficial for even small firms to adopt a Code of Ethics. The organization should consider articulating the value of fair and respectful treatment with respect to all stakeholders in the company including co-owners, employees, customers, and suppliers. One or two owners should assume responsibility for taking the lead on the firm's conflict prevention agenda for the year.

Phase II: Setting Objectives to Address Owner Legal Issues

Measurable targets should be established regarding management of the owners' relationship. For example, one goal may be to update the company's LLC operating agreement and buy-out agreements. Another goal may be to develop a business valuation formula for use in owner buy-outs. A third objective may be to create a system for fostering owner communication through designated meetings, reports, and other communications.

Phase III: Identifying Events that Could Impact the Owner's Legal Relationship

The owner or owners assigned to managing the internal legal relationship of owners should work with legal counsel to identify possible events that could impact the owners' legal relationship (e.g., a new owner joins the firm, a member retires, an acquisition is pending, or a new compensation agreement is reached). Many

events may create the need to revisit the firm's LLC operating agreement, shareholder agreements, and other legal contracts.

Phase IV: Assessing Risks Surrounding the Owners' Legal Relationship

The risks associated with potential conflicts among owners should be considered. The primary risks from owner disputes typically include owner lock-in of capital, inadequate compensation, inability of the firm to make on-going business decisions, and the like. The absence of viable and updated buy-out agreement including a dispute resolution procedure and a proper business valuation mechanism can present costly consequences of failure to develop the appropriate internal legal agreements among owners.

Phase V: Risk Response: Strategies for Deterring or Resolving Owner Conflicts

A variety of possible strategies for managing the legal relationship among owners should be considered. Strategies should focus on the owners' personal as well as legal relationships. Initiatives to foster sound owner communication, and initiatives to enter into appropriate legal agreements may prove helpful as described below under control activities.

Phase VI: Control Activities to Deter and Resolve Owner Conflicts

Control activities may include: 1) mechanisms designed to foster owner communication such as monthly meetings; 2) the establishment of deadlines for the updating of important contractual agreements among owners; 3) the assignment of one or more owners to review existing insurance policies or to find new insurance policies that may be needed to fund buy-out agreements

in the event of a member's death or disability; and 4) the assignment of one or more owners to focus on issues that are apt to be quite sensitive in a privately owned business such as compensation arrangements, reimbursement policies for business entertainment, and/or assignment of duties and responsibilities among owners.

Phase VII: Information and Communication

Care should be taken to circulate all appropriate written and oral information to the owners on a timely basis. Dates for special owner meetings should be communicated. If legal documents such as a buy-out agreement are being drafted, care should be taken to make sure that all owners have an opportunity to review and provide input into the process.

Phase VIII: Monitoring

A review of the management of the owners' legal relationship should be undertaken on an annual basis, or more frequently if needed, to evaluate the firm's success in following through on control activities that have been established. Monitoring includes follow-up questions such as: Were owner meetings actually conducted? Was the firm successful in resolving sensitive matters during the time period? Were LLC operating agreements and buy-out agreements successfully updated and signed? The agenda for the following period should include an evaluation of the firm's effectiveness in managing owner conflict and a report on progress achieved in updating key legal documents. Outside legal counsel may need to be consulted for appropriate updates in light of business and legal developments that may impact the owners' relationship.

Table VI

Example II: Applying ERM to Control Agency Authority and Prevent Veil-Piercing

Phase I: Setting the Tone at the Top for Preventing Veil-Piercing and Unauthorized Conduct of Agents

The CEO and/or top responsible owner or manager should review the tone at the top regarding the formalities of doing business. Does the CEO and/or top owners or managers set an example for a disciplined company that is not sloppy on paperwork? Does the tone at the top reflect a respect for the integrity of the corporation or LLC? Does top management set a good example for separating business from personal assets and transactions? Is the CEO conscientious about finalizing paperwork using the correctly identified name of the firm on customer contracts, business cards, and other public representations of the business?

Phase II: Setting Objectives for Preserving the Corporate Veil

The CEO and/or top responsible owner or manager should consult with outside counsel and establish two or more goals for the year. One such goal for the year may focus on stricter observance of the divide between business and personal travel & entertainment expenses. Another goal might be to achieve stricter compliance with recordkeeping surrounding customer contracts.

Phases III and IV: Event Identification and Risk Assessment

CEO and/or top responsible owner or manager should consult with outside legal counsel to identify risks associated with the failure to respect the business entity. Major recent transactions should be reviewed to determine if there are any events that present increased

risks of common veil-piercing factors such as comingling of funds or an increase in the personal use of business assets.

Phase V Risk Response:

The CEO and/or top responsible owner or manager in consultation with outside legal counsel should take practical steps to minimize risks of personal liability. For example, to avoid veil-piercing, the company policy regarding the personal use of business assets may have to be changed. A procedure for spot-checking business recordkeeping may have to be implemented to ensure proper public representation of the firm to third parties. Systems may be needed to ensure that the website and company forms and contracts accurately use the appropriate LLC or Inc. designation.

Phase VI Control Activities:

The CEO and/or top responsible owner or manager should consult with the firm's CPA to identify and coordinate control activities that will be instrumental in reducing the risks of veil-piercing. These will include control procedures to ensure proper authorization of transactions, appropriate public representations of the firm, thorough completion of order forms and contracts, and compliance with procedures that will prevent comingling of funds.

Phase VII Information and Communication:

Procedures and information will have to be effectively communicated and shared among the appropriate employees in order to successfully implement the control activities.

Phase VIII Monitoring:

Systems and procedures designed to preserve limited liability must be evaluated in light of goals that have been established. Changes should be made as needed.

MEDICAL TORT REFORM: POLICY CONSIDERATIONS AND PROPOSALS

By

A. David Austill*

I. INTRODUCTION

The health care sector of the U.S. economy has grown to an enormous size over the decades.[1] Many regard it as out of control and in need of regulation while others argue for a hands-off approach; let the market decide how efficient health care ought to be. Regarding tort reform in the health care industry, the political left and right seem to have their basic political philosophies mixed up. The left prefers to have more government regulation over the industry and little to no tort reform, and the right prefers to have less regulation over the industry but is willing to accept congressional reform of medical tort law, even if it means erosion of the federalism principle and states' rights. Thus is the debate over medical tort reform.

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[1] Available at http://www.supplementalhealthcare.com/blog/2012/us-healthcare-industry-employs-one-eight-americans (last visited Mar. 13, 2013). The health care industry is quickly making a name for itself as the most dominate sector of the American economy. Health care employs one out of every eight American workers, includes 16 million jobs, and generates approximately $2.7 trillion each year. Those are pretty big numbers for a growing industry.

This paper discusses the reform of medical tort law as it applies to medical malpractice lawsuits, the underlying substantive law on injuries resulting from negligent medical providers, and the remedies available for liability thereon. This paper does not generally argue for change in what constitutes medical malpractice, except as proposed in the discussion on substantive and procedural law proposals for the use of the avoidability standard. Medical tort standards of customary medical practice and accepted medical practice still apply in medical malpractice cases.[2]

A. Why Is Medical Tort Reform Necessary?

If Americans were not informed about the rising costs of health care and the ruinous effects continued rising costs will have on the national debt, employers, and the insured, national politics in the past few years have changed that. A number of factors contribute to rising medical costs above general inflation rates. The

[2] Probably the most common test to determine if the physician meets the good medical practice professional standard is the customary medical practice standard. With this test for a physician's negligent practice, the trier of fact determines whether or not the physician followed a practice that is customarily and usually done by physicians under the circumstances. *See, e.g.*, *Rosenweig v. State*, 171 N.Y.S.2d 912 (App.Div. 1958); aff'd, 158 N.E.2d 229 (N.Y. 1959). The recent trend is to apply the accepted practice standard. Under this test the question is did the physician deviate from an accepted medical standard of practice? Here, the trier of fact looks to see what physicians collectively recognize as that which "should be done" not what is "customary". The medical profession recognizes that in some areas physicians reasonably disagree on the best practice to be used. Therefore, a physician will not be held negligent when he or she in good faith follows a course of treatment advocated by a considerable number of physicians of good standing. A physician, however, will be negligent if an injury results from his or her deviation from those accepted standards of medical practice in treating patients. *See, e.g., Classen v. Izquierdo*, 520 N.Y.S.2d 999, 1002 (Sup.Ct. 1987).

following is a general discussion of some of these contributing factors all relevant to the medical tort resolution system.[3]

First, it is argued that there are too many medical malpractice lawsuits filed and that the tort resolution system for medical malpractice is broken and inefficient. In 2007, Towers Perrin, a medical consulting firm, estimated that medical tort litigation costs about $30 billion a year.[4] A substantial portion of these lawsuits should not have been filed. Frivolous lawsuits are substantial in creating inefficiency in health care in time, legal costs, and insurance premiums. In 2006, the Harvard School of Public Health estimated that 40 percent of medical malpractice lawsuits are without merit.[5] Restructuring how medical disputes are resolved could substantially resolve this problem. Resolution may be through use of medical review panels or may take the form of enhanced pleading requirements requiring the plaintiff to state the

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[3] *See generally*, Lynna Goch, *Medical-malpractice tort reform trouble spots*, BEST'S REVIEW, reprinted in THE FREE LIBRARY, Dec. 1, 2002, *available at* http://www.thefreelibrary.com/Medical-malpractice+tort+reform+trouble+spots.+(Property%2FCasualty)-a095198721 (last visited Mar. 13, 2013).

[4] Anne Underwood, *Would Tort Reform Lower Costs?* NEW YORK TIMES, Aug. 31, 2009, at 3, *available at* http://prescriptions.blogs.nytimes.com/2009/08/31/would-tort-reform-lower-health-care-costs/ (last visited Mar. 13, 2013).

[5] Lex Taylor, *Medical tort reform is key*, NORTHSIDE SUN, Sept. 10, 2009, available at http://www.northsidesun.com/printer_friendly/3557310 (last visited Mar. 22, 2010). These findings have been questioned as to accuracy given that the purpose of filing many lawsuits is to obtain information that was withheld from the plaintiff so that a better decision on resolution, if at all, could be had or lawsuits were about the amount of compensation due clients. See, e.g., David M. Studdert & Michelle M. Mello, *When Tort Resolutions Are "Wrong": Predictors of Discordant Outcomes in Medical Malpractice Litigation*, 36 J. LEGAL STUDIES S47 (2007); CENTER FOR JUSTICE & DEMOCRACY, *Statement of Joanne Doroshow, Executive Director, Center for Justice & Democracy, Before the House Committee on the Judiciary*, January 20, 2011, available at http://judiciary.house.gov/hearings/pdf/Doroshow01202011.pdf (last visited Mar. 13, 2013).

particulars of the tortious act similar to pleading requirements under the Private Securities Litigation Reform Act of 1995.[6]

Second, it is generally argued that damage awards for noneconomic damages for pain and suffering are excessive. In plaintiffs' tort litigation, pain and suffering damages commonly provide that portion of the plaintiff's verdict that renders money for the contingent attorney's fee. To the skeptic, under contingent fee arrangements, this form of damages provides the incentive to medical malpractice lawyers to seek out more plaintiffs rather than simply to right a wrong. If this incentive was reduced, then fewer lawyers would practice medical malpractice law.[7] Fewer medical malpractice lawyers result in fewer medical malpractice lawsuits. This was shown to be the case in California following the

[6] *See generally* Pub.L. 104-67, 109 Stat. 737, 15 U.S.C. §78u *et seq*. It should be noted, however, that such pleading particularity should not mean abolishing the doctrine of *res ipsa loquitur* in medical malpractice cases.

[7] The American Bar Association has taken a strong position against capping noneconomic damages, *contra* to the position of the American Medical Association, or federalization of medical tort law. The following is the ABA's position as of March 9, 2010:

> The ABA urges the legal and medical professions to cooperate in seeking a solution to medical liability problems and maintains that federal involvement in the area is inappropriate. In particular, the ABA opposes caps on pain and suffering awards, supports retaining current tort rules on malicious prosecution, collateral sources and contingent fees, and believes that the use of structured settlements should be encouraged. It also supports certain changes at the state level in the areas of punitive damages, jury verdicts and joint and several liability. The ABA believes that notices of intent to sue, screening panels and affidavits of non-involvement are unnecessary in medical malpractice actions. It also supports the enactment of apology legislation at the state and territorial level. ABA Government Affairs Office, *Health Care Law: Medical Liability Law*, American Bar Association, Mar. 9, 2010, *available at* http://www.abanet.org/poladv/priorities/mpl/ (last visited Mar. 17, 2010).

enactment of a cap on noneconomic damages in medical malpractice cases.[8]

Third, excessive and unwarranted litigation has resulted in excessively high medical malpractice insurance premiums paid by health care providers.[9] To the extent the market will allow, health care providers pass along these rising liability insurance premiums on the consumers, which drive medical costs higher for consumers. If health care providers cannot recover those malpractice insurance premiums from consumers, these costs reduce profits or income, for example, obstetricians, and they either leave the geographic area altogether or they practice another type of medicine. Also, medical malpractice insurance companies may refuse to suffer the risk if the number of medical malpractice lawsuits or jury verdicts becomes excessive. Sometimes, malpractice insurance premiums rise because malpractice insurance companies simply quit doing business in the state causing a tighter insurance market in which the premiums increase under a less-competitive insurance market.

Evidence exists for the states of Mississippi and Florida that obstetricians, a higher-risk specialty, gave up their practice causing shortages in this extremely important medical specialty. Following Mississippi's cap on noneconomic damages to $250,000 in 2004[10], medical malpractice claims dropped 91 percent and medical malpractice insurance rates dropped by 42 percent. Texas also capped noneconomic damages at $250,000 and resulted in more medical malpractice insurance providers entering the state (going

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[8] *See* Rachel Zimmerman & Joseph T. Hallinan, *As Malpractice Caps Spread, Lawyers Turn Away Some* Cases, WALL ST. J., Oct. 8, 2004, at A1.

[9] *See* Michelle M. Mello, *Understanding medical malpractice insurance: A primer*, ROBERT WOOD JOHNSON FOUNDATION, RESEARCH SYNTHESIS REPORT NO. 8, Jan. 2006, *available at* http://www.rwjf.org/pr/synthesis/reports_and_briefs/pdf/no10_primer.pdf (last visited Mar. 22, 2010).

[10] Mississippi's tort reform also included limiting joint and several liability and placing limits on forum shopping.

from four to 30), an increase in the number of practicing physicians, and a reduction in malpractice insurance costs. In Texas for the period 2003-2008, physicians' liability insurance premiums dropped by 25 percent and the state's largest medical malpractice insurer saw a 50 percent reduction in the number of lawsuits filed.[11] From 2003, the year Texas made its tort law reforms, to 2009, Texas saw 16,500 more physicians practicing medicine in Texas, many of these new physicians to underserved and rural communities. Furthermore, Texas jumped six spots on the American Medical Association's ranking of doctors per capita.[12]

Fourth, unlike the direct results of excessive or unfair medical tort litigation discussed above, an indirect result is the physician practice of defensive medicine where doctors order needless tests as an inefficient means of warding off potential medical malpractice lawsuits. The American Medical Association (AMA) has estimated that 93 percent of physicians admit to practicing defensive medicine. A 2008 survey by the Massachusetts Medical Society found that about 25 percent of medical procedures are defensive in nature.[13] This inefficiency, which to a point may even be fraudulent, is estimated to be about $191 billion annually.

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[11] American Medical News, *5 years of tort reform: Lone Star success story*, AMEDNEWS.COM, Sept. 15, 2008, available at http://www.ama-assn.org/amednews/2008/09/15/edsa0915.htm (last visited Mar. 22, 2010). For a discussion of Texas' legislation and Texas Proposition 12, s*ee*, Alan J. Ortbals, *Dramatic changes follow Texas medical malpractice tort reform*, ILLINOIS BUSINESS JOURNAL, May 9, 2005, *available at* http://www.ibjonline.com/print_medical_malpractice_tort_reform.html (last visited Mar. 22, 2010). Results have not been as favorable for Florida where noneconomic damages were capped at $500,000 in 2003. It has been argued that the cap was too high and medical malpractice insurance premiums have not fallen.

[12] Lawrence J. McQuillan, *CBO Underestimates Benefits of Malpractice Reform*, THE WALL STREET JOURNAL, Oct. 23, 2009, *available at* http://online.wsj.com/article/SB10001424052748703573604574491690229571588.html (last visited Mar. 14, 2013).

[13] Id.

Furthermore, it has been estimated that an indirect consequence of rising medical costs directly due to defensive medical practices adds at least 3.4 million Americans to the rolls of the uninsured and reduced productivity and output by more than $41 million in 2008.[14] These estimates may be old given the constraints that managed care organizations and health insurance companies have placed on the insured and health care providers through utilization review policies. A question that should be considered in assessing the savings of defensive medicine is to what extent will physicians forego tests and medical consultations even with medical tort reform? To the extent that certain tests have become "accepted medical practice", substantial savings may not follow. Perhaps what makes this nation's health care so great, at least for those who can afford it, is the availability of medical technology and the willingness of physicians to use it freely. Regardless of the reason behind excessive testing—ready availability, customary practice, fear of litigation, etc., it is apparent that too many tests are being ordered by physicians.[15]

Fifth, the medical tort dispute resolution system in very inefficient and burdensome on the victims while remaining very profitable to lawyers. One may make a general argument that the lawyer's incentive to profit in filing medical tort cases is what drives litigation in the medical area. Once attorney fees and other administrative costs are taken out of judgments, plaintiffs are left, on average, with only 46 percent of the award.[16] This reflects

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[14] *Id*.

[15] *See* Linsey Tanner, *Some reports suggest excessive screening*, THE ORANGE COUNTY REGISTER, Mar. 13, 2010 available at http://www.ocregister.com/news/cancer-65687-ocprint-screening-tests.html (*citing The New England Journal of Medicine* and the National Institutes of Health that physicians are requiring needless tests and procedures, like Caesarian sections and angiograms. *See also* Linsey Tanner, *Experts say U.S. doctors over test*, COMMERCIAL APPEAL, Mar. 13, 2010, at A1.

[16] *Also*, the President's Council for Economic Advisors have estimated that "58 percent of tort costs go to pay for administration, claimants' attorney fees, and defense costs", The Foundry, *An Overlooked Health Care Cost Cutter: State*

inefficiency in the medical tort dispute resolution system and requires a new approach to resolving medical disputes that is more efficient and beneficial to victims.

Last, the above-described medical practices and medical tort dispute resolution system directly and negatively affect consumers, health insurers, employers, and federal and state governments that have to bear the economic burden of rising health care costs. These costs have risen much faster than general inflation, and health care consumes a greater portion of this nation's gross domestic product each year. It is obvious that inflation in the health care sector is not entirely due to litigation. Unhealthy lifestyles, diet, medical fraud, risk-taking activities, the high quality of best medical practices and tests, an older population, the profit motive, high start-up costs for physicians resulting from huge education indebtedness, governmental regulation, *inter alia*, account for most of the excess in medical costs. Medical tort reform may, however, be the easiest, at least procedurally and legislatively, to accomplish by the government.

What *could be* the overall cost savings should Congress enact effective medical tort reform? In 2009, the Congressional Budget Office (CBO) estimated that medical tort reform, which included capping noneconomic damages and punitive damages, modifying the collateral source rule, reducing the statute of limitations, and adopting several liability, could save government health care programs about $41 billion over 10 years in expenditures plus another $13 billion over 10 years in federal tax savings directly resulting from lower private health care expenditures by persons and employers.[17] This does not take into account the savings,

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Medical Liability Reform, THE HERITAGE FOUNDATION, Aug. 10, 2009, *available at* http://blog.heritage.org/2009/08/10/an-overlooked-health-care-cost-cutter-state-medical-liability-reform/ (last visited Mar. 14, 2013.)

[17] *See* Douglas W. Elmendorf, *Letter to Senator John D. Rockefeller IV*, CONGRESSIONAL BUDGET OFFICE, Dec. 10, 2009, *available at*

directly and indirectly, to those covered by private insurance or uninsured paying out-of-pocket.

Opponents of medical tort reform argue that medical tort reform is not necessary. For instance, in 2008, only 11,037 in medical malpractice claims were paid out in U.S.[18], the lowest number since 1990. Adjusted for inflation, medical malpractice claims were was only $3.6 billion, the lowest for the 18-year period according to the National Practitioner Data Bank.[19] A CBO estimate of medical malpractice claims revealed these malpractice payouts to have resulted in only 0.6 percent to 2 percent of health care expenditures in the U.S. As a result of this estimate, the CBO concluded substantial savings would not be achieved with medical tort reform. On its face, these are good evidentiary facts. However, the CBO failed to take into account cost savings to self-insured health care institutions, costs to defend lawsuits, and the savings that could result from avoidance of defensive medicine practices, which may be large amounts.

A significant argument about justice, in particular, access to justice, is raised when plaintiffs' incentive to litigate, or that of their legal counsel, is reduced through substantive or procedural rules. The counterargument is that fewer medical malpractice lawsuits mean more victims of medical malpractice are going without compensation for their injuries—an injustice. Only a relatively small number of medical errors resulting in injury

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http://www.cbo.gov/ftpdocs/108xx/doc10802/12-10-Medical_Malpractice.pdf (last visited Mar. 14, 2013).

[18] *See* Geoff Pallay, *Why Tort Reform Needs to Be Part of Health Care Reform*, SOUTH CAROLINA POLICY COUNCIL, Sept. 16, 2009, available at http://www.scpolicycouncil.com/research-and-publications-/health-care/779-why-tort-reform-needs-to-be-part-of-health-care-reform (last visited Mar. 22, 2010), noting that 25 percent of physicians are sued each year but only 10-20 percent of those lawsuits ever reach trial. For 2008, the 11,037 paid claims represented 1.1 percent of all physicians.

[19] Tom Charlier, *Medical lawsuits radically declining*, THE COMMERCIAL APPEAL, Nov. 1, 2009, at A1.

actually are compensated. Some argue that without the fear of liability medical practitioners and facilities will result in lower standards for health care, quality would suffer, and more patients would die. Evidence has shown the contrary. For example, the CBO studied states that have capped noneconomic damages to see if the reform reduced the quality of care. The CBO found that health outcomes in these states were not negatively affected in any substantial way the CBO was able to measure. Rubin and Shepherd of Emory University studied non-automobile accident death rates from 1981-2000. Considering death rates before and after enacting tort reform measures, and taking other variables into account, they found that most individual reforms lead to statistically significant reductions in death rates. This was the case for caps on noneconomic damages and punitive damages. This could be explained, in part, because some tort reforms reduced costs of services and products, which lead to greater availability and use and actually saved lives in the long run.[20]

B. Criteria for Medical Tort Reform

In considering what should be done in reforming medical tort law, if anything at all, state and federal governments should consider certain criteria, or goals, for the policy. These criteria for sound medical tort reform are borrowed, in large part, from those criteria for sound tax policy.[21] The criteria that should be given due

[20] Paul H. Rubin & Joanna M. Shepherd, *Tort Reform and Accidental Deaths*, 50 J. Law & Econ. 221 (2007), *available electronically at* SSRN: http://ssrn.com/abstract=781424 (last visited Mar. 14, 2014).

[21] *See generally*, Joseph T. Sneed, *The Criteria of Federal Income Tax Policy*, 17 STAN. L. REVIEW 567 (1965), applying the following criteria to a good income tax system: (1) administrability of the tax regime, (2) equity in terms of supporting progressivity rather than regressivity (i.e., vertical equity), (3) equity in terms of who is exempted from taxation or tax preferences given (i.e., horizontal equity), (4) promotion of free market principles and competition (horizontal equity), (5) adequacy of tax revenues, and (6) political feasibility ; S. P. Horn, *Taxation of E-Commerce*, 2 J. AM. ACAD. BUS. 329 (2003), applying the following goals for a good sales and use tax system: (1) neutrality, (2)

consideration by the legislative and executive branches of government include (1) adequacy of the tort reform legislation's contribution in controlling health care costs, (2) equity, fairness and justice in the remedy and dispute resolution process, (3) neutrality in the health care industry marketplace, (4) efficiency in resolving disputes, (5) administrability of the dispute resolution system, and (6) political feasibility.

First, any new attempt at medical tort reform must be predicated on controlling health care costs, this being the impetus for federal attempts to regulate health care. If a form of medical tort reform does not reduce health care costs through increased efficiency or some other result, then that attempt should be abandoned so as not to encroach upon federalism. Health care costs in the aggregate may be reduced through more efficient and fair dispute resolution, reduced litigation, fairer remedies, etc., all of which, presumably, would reduce medical liability insurance premiums and reduce wasteful defensive medicine practices.

Second, any changes in the health care dispute resolution process or substantive law pertaining to medical malpractice or defective medical products must be fair and equitable resulting in both procedural and social justice for those injured and for health care providers, manufacturers, and sellers of medical products or equipment. Medical tort law, as it has developed, has resulted in a medical industry cautious in the development of pharmaceuticals and medical equipment or devices. Part of this is due, at least in part, to regulation by the Food and Drug Administration (FDA), which requires proper testing of new drugs and medical equipment/devices. The fear of malpractice lawsuits is a deterrent for giving hospital privileges to bad physicians, accepting them as partners in medical practices, or selling medical malpractice

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efficiency, (3) certainty and simplicity, (4) effectiveness and fairness, and (5) flexibility; A.D. Austill and T. Proctor, *Death of Death Taxes: Not Likely*, TAX NOTES, April 27, 2009, at 1, adapting Joseph Sneed's criteria to estate taxation.

insurance to them. Whereas this fear may be negative reinforcement, it is still a deterrent. These benefits of the current medical tort system place some form of constraint on radicalizing the medical tort dispute resolution process. There is a fear that drastically changing the system to favor physicians, providers, and manufacturers would reduce patient safety and well-being. A reasonable argument may be made that the medical tort system, as it has developed, presently favors plaintiffs. It is a logical proposition, however, that any significant reduction in deterrence of bad medical practice or defective medical products through reduced legal costs (e.g., capped non-economic damages) must be offset by greater government and professional licensure regulation.

Third, reform must remain neutral within the health care industry marketplace. Reforming the medical tort system should not reduce competitiveness within the industry nor interfere with innovation in the development of new medical drugs, devices, services, and techniques, which has been the hallmark of American medicine for decades. It is hard to accept an argument that the present medical tort system has stymied American medicine at all.

Fourth, the legal process for resolving disputes between the parties in medical tort cases should be efficient in terms of cost and time consumed to bring about final resolution. Presently, the process is expensive and time consuming. If a physician is responding to a malpractice lawsuit, then the physician is wasting time that he or she could be providing medical services. It may be that the dispute resolution process must be bifurcated between medical professionals and health care institutions on the one hand and medical product liability cases on the other. Legal disputes involving the manufacture of defective medical devices, equipment, drugs, or supplies simply require more attention because of the complicated nature of product design and testing than do lawsuits for personal services. An expanded version of arbitration, for example, greater discovery rights and procedural safeguards, may be necessary for medical product liability cases.

Arbitration may be preferable to litigation because of the technical aspect of product design and testing. Efficiency is of lesser concern given the nature of product liability cases. Efficient means of resolving medical malpractice disputes may be through traditional alternative dispute resolution methods, like mediation, arbitration, or med-arb. An important factor in measuring efficiency is attorneys' fees for both parties. Mediation and arbitration generally require less attorney's fees because of the time spent in the dispute resolution process.

Fifth, any reforms and any new processes or dispute resolution systems must be administrable without excessive burden, cost, and delay. If Congress enacts sweeping medical tort reform legislation that requires alternative dispute resolution or medical review panels or boards, then a determination must be made as to whether to create a new federal agency, create new state agencies under the control of the governors, or to federalize medical dispute resolution wherein the federal courts would be given jurisdiction over all of these cases. Federal exclusive jurisdiction would require new policies and procedural rules for resolving medical disputes. This may increase the cost of litigation or arbitration. However, adopting mandatory arbitration for medical disputes could create specialists in medical malpractice and medical product liability to hear the cases, and efficiency may be enhanced like it is for labor disputes under the National Labor Relations Act. Federalization of the medical dispute resolution process could create uniformity of results, definition of best medical practices, and consistency in verdicts. It may be more difficult and less efficient to allow state courts and state legislatures to establish their own tribunals and medical review panels or boards.

Finally, medical tort reform will be successful only if it is politically feasible and is acceptable on a bi-partisan basis in legislatures. Generally, medical tort reform is favored, *inter alia*, among the political right, health care providers, pharmaceutical and medical supplier industries, and the National Chamber of

Commerce. On the other hand, the political left, public interest advocacy groups, trial lawyer associations, and similar groups repel at the notion of medical tort reform. Whereas a number of state legislatures have enacted some medical tort reform legislation, the 111th Congress rejected reform when the Patient Protection and Affordable Care Act[22] (Affordable Care Act) was enacted.

II. FORM OF MEDICAL TORT REFORM

There is a plethora of reforms that government has at its option that could provide benefits and cost savings in the health care sector. Whereas a particular victim of medical malpractice or a provider may be worse off as a result of any one or all of the reforms, good reforms would necessarily meet the criteria discussed above. There is a utilitarian rationale, even a social compact rationale, with the adoption of reform measures. The following represent some of the options available to state and federal governments. In some instances states have adopted these reforms for medical malpractice, and in some instances states have adopted these reforms regardless of the nature of the civil litigation to reign in perceived abusive tort litigation. The discussion will first focus on changing the substantive law itself followed by a change in dispute resolution procedure.

A. Substantive Law Reform Measures

Probably the most significant reform has been the limitation on noneconomic damages, usually pain and suffering. State legislatures through statutory enactment have been reluctant to

[22] Pub. L. No. 111-148, 124 Stat. 119 (2010), 42 U.S.C. §18001 et seq. The Senate bill (H.R. 3590) was passed through the procedural rule of reconciliation and the House of Representatives passed the Senate's version without the need for two bills going to conference. The Patient Protection and Affordable Care Act is a huge and complicated piece of legislation that includes 12 pages in its Table of Contents and 906 pages (PDF version).

place a cap below $250,000. Usually the cap is either $250,000 or $500,000. Obviously, a $250,000 cap is more effective in reducing law suits and medical malpractice insurance premiums than are caps substantially higher; the risk-reward changes significantly with a lower cap. Furthermore, a cap has an additional benefit of reducing health care services as there is less need for defensive medicine practices.[23] The issue of whether to cap non-economic damages can be seen as an issue of fairness and justice. Some injuries have a long and deep psychological effect but do not result in high economic damages, for example, medical out-of-pocket expenses or lost wages over time. If, say, a young physician, who is a proponent of a low cap on non-economic damages, considered this legal policy from a Kantian perspective, then that young physician would answer in the affirmative the question: Would you be willing to give up your prostate for $250,000?[24] Clearly, the effect of a cap on non-economic damages will cause injustice to some persons quite possibly more so than any other recommended form of tort reform.

The general policy on joint and several liability in tort cases is grounded in protection of the victim even if injustice may result to a tortfeasor. The policy, which accepts the deep pocket theory, rests, at least in part, on the theory that a tortfeasor can and should protect himself through the purchase of liability insurance. Further, as between the joint tortfeasors, there is a right of contribution under tort law. By moving away from joint and several liability to several liability, each tortfeasor would be liable

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[23] *See* Elmendorf, *supra* note 17; Douglas W. Elmendorf*, Letter to Senator Orrin G. Hatch*, CONGRESSIONAL BUDGET OFFICE, Oct. 9, 2009, *available at* http://www.cbo.gov/ftpdocs/106xx/doc10641/10-09-Tort_Reform.pdf (last visited Mar. 14, 2013).

[24] This example was taken from a question posed to lawyers at a small CLE seminar which the author attended. One young lawyer commented that he would. He changed his mind once he discovered the significance of the prostate. From an ethical or moral perspective based on deontological or religious theory, a low cap on non-economic damages would appear to be hard to support; yet, it can be supported under utilitarian theory.

only for his individual share of the damages as determined by the court. Many states have moved toward several liability with the adoption of comparative fault as the notion of comparative fault focuses on allocation of fault. Tennessee, for example, in *McIntyre v. Ballentine*[25] abolished joint and several liability when it adopted modified comparative fault. An argument for adopting several liability in medical tort cases is similar to the argument for adopting the comparative fault doctrine, which creates fairness to both the plaintiff and defendant in the sharing of responsibility and replaces the potential harshness of the contributory negligence doctrine.[26] Some states have retained joint and several liability, even in comparative fault states, when a joint tortfeasor is more than 50 percent at fault or when the act is intentional, willful or reckless.[27]

It should be noted that the doctrine of *respondeat superior* giving rise to vicarious liability of an employer would not be affected. To allow the doctrine of several liability to override the doctrine of respondeat superior would create fissures in the relationships between hospitals and clinics and their employed staff, such as physicians, nurses, and physical therapists. These medical professionals would then have to purchase extremely high malpractice insurance policies and create tension between them as employers, employees, and co-workers.

An argument against abolishing joint and several liability and adopting several liability is the burden it will place on plaintiffs to sue all parties, who may have been negligent in causing the plaintiff's injury, and to seek enforcement of the judgment against each one. Furthermore, a joint tortfeasor may be under-insured or

[25] 833 S.W.2d 52 (Tenn. 1992); thus, Tennessee has not been counted in Table No. 1 as having legislatively adopted reform of its joint and several liability law.
[26] *See generally* P. Beider & C. Elliott, *The Economics of U. S. Tort Liability: A Primer*, CONGRESSIONAL BUDGET OFFICE, C. Spoor, ed. (Oct. 1, 2003).
[27] *See generally* R.S. Peck, *The Development of the Law of Joint and Several Liability*, 55 FDCC Q. 465 (2005).

insolvent placing the burden squarely on the plaintiff. There could be an exception in the event the plaintiff can show that one of the joint tortfeasors has fled, has become insolvent, or service of process cannot be had. In such case, the other joint tortfeasor(s) should bear the cost of the other joint tortfeasor on a pro rata basis.[28] There is also question about whether any benefit would be derived from adoption of several liability. A CBO study found that, after switching to several liability, Medicare spending increased for hospitals and physicians. The CBO attributed this increase to additional defensive medicine practices to reduce liability risk.[29]

Limitations on attorney fees in medical malpractice cases would have a deterrent effect on malpractice lawsuits. Whereas medical malpractice lawsuits are typically filed on a contingent fee arrangement, with a malpractice lawyer retaining all of the downside but limited on the upside, there would be greater reluctance for lawyers to accept medical malpractice cases that have a lower probability of success or lower fees. California, for example, has placed limits on attorney fees in settlement and judgment situations: 40 percent on the first $50,000, $33 percent on the next $50,000, 25 percent on the next $500,000, and 15 percent of any amount exceeding $600,000.[30] Before final enactment of the Affordable Care Act, an attempt was made by Republications to amend the Senate's version of the bill (H. R. 3510) by capping attorney fees in a medical malpractice case. It failed by a 2:1 margin.[31]

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[28] This would be similar to a provision in Tennessee's Product Liability Act (T.C.A. §29-28-106) that provides strict liability solely to the manufacturer of a sealed and packaged product unless the plaintiff cannot obtain service of process on the manufacturer, then the retailer could be strictly liable. See

[29] *See* Elmendorf Letter to Sen. Hatch, *supra* note 23.

[30] *See* Rachel Zimmerman & Joseph T. Hallinan, *As Malpractice Caps Spread, Lawyers Turn Away Some Cases*, WALL STREET JOURNAl, Oct. 8, 2004, at A1.

[31] Calvin Woodward, *Health Care Issues: Medical Malpractice Lawsuits*, Associated Press, THE SEATTLE TIMES, Dec. 8, 2009, *available at*

To create a system of efficiency and fairness to the victims of medical malpractice, limitations on attorney fees should not just be considered on medical malpractice cases filed in court. Rather, there should be some review mechanism for all medical malpractice attorney fees when an attorney is used to make a legal claim on behalf of an individual regardless of whether a lawsuit or arbitration petition is filed. An efficient medical malpractice tort system should address attorney fees when the claim is settled or judgment is rendered. Such a mechanism would require the plaintiff's lawyer to submit a time and expense report reviewable in a manner similar to probate or chancery court actions in guardianships and estates. The time and expense reports should be reviewed by a judge or magistrate, when an action has been filed in a court, or by an arbitrator or some administrative law judge (ALJ) with proper jurisdiction, when the dispute is resolved through administrative process or arbitration. These review procedures should be expedited for lowest cost and greatest efficiency. The attorney's fee should be limited by the attorney's contract with the complainant, but the fee and expenses allowed by the court, arbitrator or ALJ should be based on work done on the engagement and reasonable expenses incurred in performing the work. When medical disputes are resolved through negotiation or mediation without resorting to formal dispute resolution processes, similar fee arrangements should be required with adequate notice given by the complainant's attorney to the complainant of the limitation on fees and expenses and the attorney's obligation to provide a detailed accounting of time and expenses. If a client is dissatisfied with his or her attorney's fees and expenses, the client could seek resolution through administrative means.

Abolition of the collateral source rule would reduce amounts paid by defendants. The policy behind the collateral source rule is that a defendant tortfeasor should not benefit from the fact that the

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http://seattletimes.nwsource.com/html/politics/2010452973_apushealth carebriefing.html (last visited Mar. 14, 2013).

plaintiff has received money from other independent sources, such as health or life insurance, resulting from the defendant's tort. It seems that the policy behind the rule is sound enough such that it should remain unchanged. To abolish the collateral source rule would violate the equity criterion and favor the health care provider over the victim, who was prudent to purchase the insurance in the first place. It would seem that an alternate argument would be to give an insurer, for example and insurer of life or health having a policy providing a benefit to a victim, a limited right of subrogation to recover from the medical provider. This could be done in a manner similar to a worker's compensation lien when an injured employee sues a third party for his injury on the job.

Statutes of limitations could be shortened in medical malpractice and medical product liability cases. One proposal has been to set the basic limitation of one year from the date of discovery, but no later than three years from the date of the tortious act or age eight for a child. This is a marked change from existing statutes of limitations. The statute of repose on medical product liability could be shortened from a typical ten-year period from date of manufacture to a shorter period for both adult and child plaintiffs.

Structured settlements may be required when damages are over a certain threshold, say $100,000. This measurement would be beneficial in several ways. First, because of the time value of money, the total payout by the defendant would be reduced. Second, the structured nature of the payout would give greater assurance that the damage award or settlement would not be squandered.[32] The old adage "a fool and his money are soon

[32] There appears to be growth in the number of factoring firms purchasing structured settlements for cash payouts. Although plaintiffs have the liberty to assign their economic rights to these structured settlements for cash, this type of transaction would defeat the purpose of the statute as it is intended to protect the plaintiff from his own folly or for any "look-back" by the defendant. Perhaps

parted" is still true today. If there is proof later that a fraud has been committed by the plaintiff, the defendant would still have some ability to recover, or withhold, the remaining unpaid balance or the balance of the damages safely invested. This would almost provide the wherewithal for a "look-back" rule common in taxation and the executive compensation clawback provision contained in Section 304 of the Sarbanes-Oxley Act of 2002.[33]

Punitive damages in medical tort cases could be revised in several ways. First, there could be a cap on punitive damages similar to a cap on noneconomic damages. Second, a legislature could enact constraints on courts giving the courts less leeway for awarding punitive damages in medical tort cases than the three guideposts of *Gore v. BMW of North America*[34], as modified by *State Farm Mutual Automobile Insurance Company v. Campbell*[35] provides. It has been proposed to standardize these guidelines.[36] Third, punitive damages could not be awarded against a manufacturer or

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the transaction would need to be legislatively prohibited unless the plaintiff obtained permission from the court upon showing extraordinary need.

[33] Pub. L. No. 107-204, 116 Stat 745, 15 U.S.C. §7243(a).

[34] 517 U.S. 559, 574-85 (1996).

[35] 538 U.S. 408, 424-25 (2003).

[36] An example of why these punitive damages guidelines may be needed is the case of *Quicken Loans, Inc. v. Lourie Brown*, Case No. 11-0910, on appeal to the West Virginia Supreme Court of Appeals filed September 6, 2011. In this case plaintiff-homeowner refinanced her house through the defendant-mortgagee after an excessively high appraisal was performed on her home. The trial judge found the mortgage contract ($144,800) to have been unconscionable as it converted $25,000 of unsecured debt into secured debt thereby increasing the risk of losing her house. He found clear and convincing evidence of fraud even though the plaintiff's overall interest rate on her indebtedness was lowered, her monthly debt payments were reduced by $300, and she received cash of $40,768.78 to purchase a new car and pay off some credit card debt. She soon thereafter defaulted. The appraiser settled before trial. The trial court (1) awarded the plaintiff restitution of $17,476.72, (2) cancelled the plaintiff's mortgage debt ($144,800), (3) awarded her attorneys $495,956.25 in fees, and awarded her $2,168,868.75 in punitive damages by considering the cancellation of debt and attorney's fees as compensatory damages.

distributor of a medical product approved by the FDA. Prudence and equity here would necessitate allowing punitive damages where the manufacturer acted with scienter in obtaining approval by the FDA.

It has been argued that the U. S. should follow an approach used by several Scandinavian countries to determine compensation for medical mistakes using the "best medical practice" inquiry. The argument is that compensation decisions would not be based on negligence, but rather a determination is made as to whether the injury would have been avoided by properly using the best medical practice in the situation. More injured patients would receive compensation, but there would be fewer legal disputes and a less litigious and combative environment. The weakness of this approach is that it does not meet the goal of cost reduction.[37] A theory of adopting an "avoidability" standard is discussed *infra* in the medical courts section.

One unique approach could be to adopt New Zealand's no-fault insurance for compensating for accidents. New Zealand has an Accident Compensation Corporation which is a government run entity responsible for administering accident compensation. Flat-rate taxes on individuals provide the funding for this entity. If a patient is injured as a result of a negligent physician, rather than sue the physician, the patient would file a claim against an entity similar to New Zealand's Accident Compensation Corporation to recover medical expenses, lost wages, and modifications to accommodate disabled persons at home or in their vehicle.[38]

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[37] *See* Paul J. Barringer, III, *A New Prescription for America's Medical Liability System*, 38 THE ADVOCATE, Fall 2008, at 7, *available at* http:// http://www.flatls.org/index.php?option=com_rubberdoc&view=category&id=38&Itemid=60/tl-0908.pdf (last visited Mar. 13, 2013).

[38] *See generally* Michelle M. Mello, Allen Kachalia & David M. Studdert, *Administrative Compensation for Medical Injuries: Lessons from Three Foreign Systems*, THE COMMONWEALTH FUND, July 2011, *available at* http://www.commonwealthfund.org/~/media/Files/Publications/Issue%20Brief/2

Under a national health insurance regime, New Zealand's approach might be workable in the U.S.; however, this approach would be so radical that it probably would not be politically achievable. Quality of health care services could suffer if negligent doctors and other health care professionals go unpunished too often under lax licensure and self-regulation in the medical professions. Financing a no-fault system would be problematic. New broad-based taxes in the U.S. are never easy to pass in Congress, so an alternate and narrower financing vehicle would be necessary. Workers' compensation is no-fault and has been successful for many decades. About thirty years ago, however, some consideration was given in the U.S. to adopt no-fault automobile insurance. It met too much resistance and no state ever adopted it. This approach might work, however, if health care providers paid into a government pool for medical malpractice victims. This would take private medical malpractice insurance companies out of the marketplace and provide for a much more streamlined approach to medical dispute resolution.

Finally, consideration may be given specifically to a high risk area for medical malpractice because medical errors during child birth emanates passion and lawsuits naturally flow when injuries or death occur during pregnancy or delivery. Birth funds that compensate families for childbirth injuries and are financed by physician surcharges provide an approach to reduce these lawsuits, start the victims' healing process, and hold down medical malpractice insurance premiums to obstetricians.[39]

011/Jul/1517_Mello_admin_compensation_med_injuries.pdf (last visited Mar. 13, 2013); Accident Compensation Corporation of New Zealand, *available at* http://www.acc.co.nz/about-acc/index.htm (last visited Mar. 17, 2010); Paul J. Barringer, David M. Studdert, Allen B. Kachalia & Michelle M. Mello, Administrative Compensation of Medical Injuries: A Hardy Perennial Blooms Again, 33 J. HEALTH, POL. & L. 725, 725-60 (2008).

[39] *See* kaiserhealthnews.org, *States Have Initiated Tort Reform Experiments*, reprinted by MEDICALNEWSTODAY.COM, Oct. 14, 2009, *available at* http://www.medicalnewstoday.com/articles/167294.php (last visited Mar. 14, 2013).

B. Procedural Reforms

Procedural reforms in health care may take several forms, but, thus far, no states have taken drastic steps to reform health care litigation. The following discussion covers some of the alternatives, which may be separate or combined with others. Furthermore, some are more preferable than others and some are questionable from a constitutional perspective as they may violate the right to a trial by a jury.

1. Medical Screening Boards.

Probably the best starting point for reform in medical malpractice litigation is with screening malpractice complaints either before the plaintiff's complaint is filed or to determine if the plaintiff's case can continue. About a dozen states have established medical review boards (sometimes called medical litigation screening panels or medical screening boards) to end abusive and inefficient medical malpractice litigation practices. The purpose of medical review boards is to assure that the plaintiff's claim has merit before the case can continue in litigation. The review board is established and funded by the state. Funding may be from state assessments on health care providers.

To illustrate how an effective screening panel might be set up, Montana's Medical Legal Panel[40] will be considered. The medical legal panel includes six members—three health care members and three attorneys. The health care members on the panel must be from the profession or type of facility being sued; thus, they provide relevant technical expertise in the medical area. The attorneys on the panel can assess the legal issues that may be

[40] MONT. CODE ANN. §§ 27-6-101 et seq. (2009); *see* Gazette Staff, *Montana sets example on medical tort reform*, BILLINGS GAZETTE, Oct. 11, 2009, *available at* http://billingsgazette.com/news/opinion/editorial/gazette-opinion/article_e9bfa996-b62a-11de-b11e-001cc4c03286.html (last visited Mar. 14, 2013).

pertinent and the likelihood of success given the input of the medical members on the board. As a jurisdictional requirement for filing a medical malpractice complaint, the plaintiff must submit the complaint for review by the Montana Medical Legal Panel, which has 120 days to review the plaintiff's claim.

Montana has used the screening panel since 1977. Since its inception to 2009, the screening panel has handled over 6,145 claims and has done a remarkable job in screening bad legal cases, and, presumably, encouraging settlement of those cases having merit. During the past decade, for instance, 82 to 86 percent of the claims have been closed at the panel level with the health care provider prevailing. Even when cases continued to litigation, health care providers prevailed in 63 percent of those cases. The data for 2008 revealed 194 claims were filed with the panel and of these 27 were abandoned or settled without a hearing, 107 ended with a hearing, eight were abandoned or settled after the hearing without a lawsuit, and 22 complaints resulted in lawsuits. The most remarkable statistic reflecting efficiency of Montana's screening process is that in the 10-year period only 24 medical malpractice lawsuits went to jury trial in Montana courts with only five resulting in a verdict for the plaintiff.[41]

2. Medical Courts.

Special medical (or health) courts could achieve some of the benefits of medical screening panels in an efficient manner. As has been proposed by the Harvard School of Public Health, the special medical courts would give exclusive jurisdiction to the federal courts and would require litigation without juries.[42] Juries

[41] Gazette Staff, *id*.

[42] *See generally* Philip G. Peters, Jr., *Health Courts?* 88 B. U. L. REV. 227 (2007), in which Peters concludes that health courts may have an inherent risk of bias and overreaching and would not make an improvement over the existing tort system. Furthermore, because hospital enterprise liability would be weakened, the goal of patient safety would not be achieved.

would be replaced with neutral medical experts, the courts would have the authority to establish precedent on what constitutes malpractice through establishing a proper legal standard for medical care, and the medical court could provide a more efficient and equitable remedy for victims.[43] Legislation was proposed in the 110th Congresses to fund pilot programs to establish medical courts.[44] Some states have established special medical courts or are studying doing so.[45]

Medical courts could take either of two forms. First, states may simply incorporate a specialized court as a division of a general trial court for the jurisdiction. Second, the model proposed by Common Good and the Harvard School of Public Health would establish an administrative tribunal similar to that for workers' compensation without the no-fault element of workers' compensation.[46] Formal litigation would not be required and the matter could be handled pro se by the victim. The process could be initiated, for example, by filing a claim with the hospital or the insurer for the hospital where the malpractice was alleged to have occurred. The hospital would convene a review panel of medical experts to evaluate the claim. Injuries resulting from the failure to use best medical practices would be compensable. In essence, the medical standard would change from common medical practice or

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[43] *See* Jeanne Lenzer, *Medical courts could ease US malpractice crisis group says*, BMJ PUBLISHING COMPANY, Feb. 19, 2005, *available at* http://www.bmj.com/cgi/content/full/330/7488/382-a (last visited Mar. 23, 2010). Medical courts have been recommended by former U.S. Senators Bill Frist and Bill Bradley, the Harvard School of Public Health and the charity Common Good.

[44] *See* Fair and Reliable Medical Justice Act, S. 1481, 110th Cong. § 1 (2007); H. R. 2497 § 1 (2007, which would have established funding for pilot programs for health courts.

[45] *See* Peters, *supra* note 42, at 232-233 (citing that Maryland, New York, Oregon, Pennsylvania, and Virginia had initiated pilot programs and Wyoming, Colorado, Michigan, and Massachusetts had been reported as starting initiatives to begin medical courts.

[46] *See generally* Barringer *et al*., *supra* note 38.

accepted medical practice to an "avoidability" standard. With the avoidability standard, patients could recover when their injuries could have been avoided using state of the art medicine, but this was not used or was used improperly.[47] Either party could appeal the tribunal's decision or the value of the judgment awarded. One unique feature of the medical court would be the right of the tribunal to solicit testimony from an independent and unbiased expert not hired by either party in the dispute. This feature in the litigation is comparable to courts in civil law countries where the judges act as inquisitors.

There are potential significant benefits from using specialized medical tribunals. First, the process is streamlined so it would be much more efficient in resolving medical disputes. Second, average payouts would be reduced because of changes in substantive law reducing potential verdicts. These substantive law changes might include capping non-economic damages for pain and suffering, no longer applying the collateral source rule to medical malpractice claims, and encouraging structured settlements allowing for periodic payments. Third, the cost of dispute resolution would be reduced since the process would be administrative and would not necessarily require the use of an attorney by the patient. Fourth, verdicts and settlements would be more rational because the triers of fact would have specialized knowledge of health care and experts would be neutral. Fifth, the goal of the medical courts would be to provide fair and equitable compensation to victims of medical malpractice using a fair avoidability legal standard. Finally, proponents argue that taking the notion of "fault" out of medical dispute resolution would ultimately result in more patient safety through using better clinical practices and creating a centralized database for victim claims.[48]

[47] *See* Peters, *supra* note 42, at 230.
[48] *Id*. at 230-231.

3. Mediation and Arbitration.

Alternative dispute resolution (ADR) methods using mediation, arbitration, or med-arb could be an attractive process in resolving medical disputes. Whereas these methods are usually consensual, except in certain statutorily required legal areas, like labor disputes under the National Labor Relations Act, for medical dispute resolution, ADR would have to be mandatory before it would contribute to improving efficiency in the medical dispute resolution process. Though mediation alone offers benefits as an ADR method, it retains its biggest disadvantage as a non-conclusive means to resolving a dispute. If the parties are not serious about resolving a legal dispute, mediation is fruitless. A third-party neutral with relevant experience and training in the health care issue in dispute would be a requirement for any mediation system for medical disputes.

Med-arb may be used to facilitate resolution of the dispute. The third-party neutral could be the same person in both the mediation phase, and if necessary, the binding arbitration phase. The med-arb process might be an option when there is a statutory requirement of binding arbitration. This process would appear to be much more effective given the heightened emotions commonly existing in medical malpractice cases.

Arbitration could take either the form of a nonbinding or binding process with consequences for each one. Non-binding arbitration might be required before any medical malpractice case could proceed to trial in court. To keep non-binding arbitration from creating greater inefficiency, an incentive must exist to encourage resolution. The author suggests that either party dissatisfied with the judgment of the arbitrator has the right to try the case in court *de novo*. However, the English rule on attorney fees would apply at trial. Thus, if a plaintiff was awarded $500,000 by an arbitrator in non-binding arbitration, and the plaintiff elected to litigate in court, the award would have to exceed $500,000 or the plaintiff

would be required to pay the defendant's attorney's fee. Surety would have to be given by the appealing party for court costs and the opposing party's attorney's fee. A study by the Manhattan Institute reveals that a loser pays approach to litigation (the English rule) would reduce litigation and most likely increase the likelihood of negotiated settlement.[49]

Use of binding arbitration would seem to be the better of the two forms of arbitration because of a greater degree of finality. As binding arbitration of medical disputes would signify a dramatic departure for usual dispute resolution practice and may conflict with constitutional guarantees of a right to trial by jury, certain safeguards would be essential. First, by necessity there would have to be greater discovery rights to create fairness to the victim. Second, there would need to be more rights to appeal arbitrator decisions in medical malpractice cases. Generally, there is a limited right to appeal arbitrated disputes. To be overturned findings of fact by the arbitrator would still need to be unreasonable, arbitrary or capricious. Certainly, instances where the arbitrator is biased or unreasonable would be appealable. Perhaps arbitrators in medical malpractice cases should have less leeway to interpret and apply the law. Presently, a decision of an arbitrator can be overturned on due process grounds if the arbitrator ignores the manifest weight of the law. One may argue, however, that medical malpractice law, in itself, is not that complicated as the determination of the facts brings about the complexity. That being the case, there would be no need for applying a different standard for appeal of the arbitrator's decision.

[49] *See* Marie Gryphon, *Greater Justice, Lower Cost: How a "Loser Pays" Rule Would Improve the American Legal System*, MANHATTAN INSTITUTE FOR POLICY RESEARCH, CIVIL JUSTICE REPORT NO. 11, Dec. 2008, *available at* http://www.manhattan-institute.org/html/cjr_11.htm (last visited Mar. 14, 2013). The report cites Alaska's experience with the loser pays rule as a contributing factor that tort lawsuits in Alaska constitute only five percent of all the state's civil litigation cases, half the national average. (at 9-10)

One of the biggest advantages of mandatory binding arbitration would be the use of medical and legal experts to serve as arbitrators. Rather than a single arbitrator, a panel of three to five arbitrators, depending on the size of the case, might be used to guard against bias and to get a broader view of the case from both medical and legal perspectives. In this regard, a complicated and high damages case could be treated like a high-dollar construction dispute in arbitration where a panel is selected under the rules of the American Arbitration Association. In order to solve the problem of plaintiff's attorneys taking an excessive portion of the victim's award, the arbitrator should determine the attorney's fees to be paid to the victim's attorney. Because alternative dispute resolution is usually a much more efficient means of resolving disputes than litigation under the rules of civil procedure, attorney's fees should usually be substantially less than they are in litigation today.

4. Other Procedural Reforms.

Other procedural reforms are not as significant as those discussed above, yet they may offer greater fairness in the process and impetus to resolve medical disputes. Measures should be put in place to resolve the dispute early and for culpable parties to make amends for medical errors. Some programs in hospitals have been designed to review case files to determine if medical errors did in fact occur and to rectify those errors early through medical fixes or compensation negotiation. "Apology" statutes encourage health care providers to make amends to victims while prohibiting any admission or apology to be used against them in court. Apology statutes facilitate dispute resolution by disclosure of the medical error, offering an apology where it is due, and negotiating a payment to the patient. Such a process would increase the speed of problem resolution, create greater transparency, provide less incentive to cover up practitioner errors, and provide the victim of the medical error with closure sooner. The inability to admit an error because of legal consequences at trial would be diminished.

Finally, limits could be placed on attorney's fees as about ten states have done, including California. An alternative to this is to have the trial judge, arbitrator, ALJ, or medical court set the victim's attorney's fee to be paid by the health care provider, as discussed *supra*.

The American Bar Association (ABA) has taken a strenuous position against the adoption of specialized medical courts, as proposed by Common Good and the Harvard School of Public Health, and capping non-economic damages. The ABA argues for retaining medical malpractice law in state courts and trials by juries to protect the interest of the injured patients.[50] It argues that capping non-economic damages has not been proven to significantly reduce medical malpractice insurance premiums, a position that has been disproven in several, but not all, states which have capped noneconomic damages.[51] In an argument similar to Peters' hospital enterprise liability rationale[52], the ABA considers it vital to hold health care providers accountable. Given its opinion that too many people die in hospitals each year, estimated at 44,000 to 98,000, as a result of preventable medical errors, the adoption of medical courts would be an injustice to victims. The ABA's argument against medical courts does not mean that the trial bar is completely against any reforms in medical dispute resolution. To the contrary, the ABA supports (1) establishing programs that enable and encourage medical personnel to report "near misses" or hospital events that, if repeated, would threaten patient safety; (2) apology legislation that would not be admissible

[50] *See* Carolyn B. Lamm, *Health Courts: Adding Injustice to Injury*, AMERICAN BAR ASSOCIATION, Mar. 2010*, available at* http://www.abanow.org/2010/03/health-courts-adding-injustice-to-injury-3/ (last visited Mar. 14, 2013).

[51] *See* Michael S. Greco, *Don't Add Insult to Injury*, AMERICAN BAR ASSOCIATION, May 2, 2006, *available at* http://www.abanow.org/2006/05/dont-add-insult-to-injury-by-michael-s-greco-president-american-bar-association/ (last visited Mar. 14, 2013).

[52] *See* Peters, *supra* note 42.

in court; (3) closer court scrutiny and set aside of awards of noneconomic damages that are disproportionate to community expectations; (4) stricter enforcement of procedural rules and evidentiary standards for filing medical malpractice lawsuits; (5) stricter enforcement of disciplinary rules for prosecuting meritless lawsuits.[53]

III. STATE AND FEDERAL REFORMS

A. State Medical Tort Reform Measures

The Heritage Foundation reported that in 2005, over 400 medical malpractice reform measures were introduced in 48 state legislatures with 27 of those legislatures enacting some kind of malpractice reform. Some of these states enacted sweeping reforms[54] of various types; for example, from 1986 and to 2005, 38 states reformed joint and several liability law; 23 states enacted statutes limiting noneconomic damages; and 34 states restricted punitive damages.[55] Table No. 1 summarizes the efforts at tort reform through 2011 for the 50 states and the District of Columbia as surveyed by the American Tort Reform Association (ATRA), an advocacy group for tort reform.[56] It should be noted, however, that ATRA included the state as having taken legislative measures in an area of tort reform even if the measure was insignificant, relative to most other jurisdictions. Expressed differently, if a state was listed

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[53] Lamm, *supra* note 50.

[54] Conn Carroll, *An Overlooked Health Care Cost Cutter: State Medical Liability Reform*, THE FOUNDRY, Aug. 10, 2009, *available at* http://blog.heritage.org/2009/08/10/an-overlooked-health-care-cost-cutter-state-medical-liability-reform/ (last visited Mar. 14, 2013).

[55] *See* Kathy Gill, *Tort Reform – State Recap*, ABOUT.COM, Feb. 10, 2005, *available at* http://uspolitics.about.com/od/health care/a/01_tort_reform.htm (last visited Mar. 14, 2013).

[56] ATRA, *Tort Reform Record*, December 22, 2011, *available at* http://www.atra.org/sites/default/files/documents/record_12-22-11.pdf (last visited Mar. 13, 2013).

in a category of tort reform, the state had at least done something related to that form of tort reform.

Table No. 1—States Enacting of Some Measure of Tort Reform Through 2011

Type of Tort Reform	*No. of States*
Punitive damages	32
Joint and several liability	39
Prejudgment interest	19
Collateral source rule	24
Non-economic damages	23
Product liability	20
Class action reform	11
Attorney retention sunshine	12
Appeal bond reform	39
Jury service reform	14

Source: Compiled from ATRA's Tort Reform Record At-A-Glance[57]

Using ATRA's compilation of state legislation of two major areas of tort reform, specifically, caps on non-economic damages and caps on punitive damages, the following summarized information shows the degree to which the states have moved forward in the last 20 years or so on tort reform, most particularly aimed at medical tort reform. Table No. 2 shows the states that have legislatively capped non-economic damages through July 2012 and those that have done so since 2009. Table No. 3 shows the states that have legislatively capped punitive damages through July 2012 and those that have done so since 2009.

[57] *See id*. for summaries of actions taken by each state and for those states whose legislative attempts at reform were judicially struck down as unconstitutional.

As Table No. 2 shows, seven states have had their legislative efforts to cap non-economic damages thwarted by the state's courts. On July 31, 2012, the Missouri Supreme Court in *Watts v. Lester E. Cox Medical Center*[58] struck down Missouri's cap on non-economic damages in holding that Missourians had a common law right to seek damages for medical malpractice claims in court. Under the Missouri Constitution there was a right of a trial by jury which was inviolate. Since there was no right of the legislature in 1982, when Missouri's Constitution was enacted, to limit non-economic damages, any limitation on damages that restricted the jury's fact-finding role violated the plaintiff's constitutional right to trial by jury.

Table No. 2—Caps on Non-Economic Damages Through July 2012

22 States capping non-economic damages:

- 18 states capping non-economic damages for medical malpractice: AR, CA, CO, FL, MI, MS, MT, NV, NC, ND, OH, OK, SC, TN, TX, UT, WV, WI
- 4 states capping under a general limitation also covering medical: HA, ID, KS, MD

7 States whose caps on non-economic damages were declared unconstitutional:

- 4 states where medical liability limits declared unconstitutional: AL, GA, IL, MO
- 3 states where general limitation declared unconstitutional: NH, OR, WA

[58] Case No. SC91867, slip op. (Mo. July 31, 2012), *available at* http://www.courts.mo.gov/file.jsp?id=55761 (last visited Mar. 13, 2013).

5 States (included above) recently enacting new legislation capping non-economic damages:

- Caps medical malpractice: UT (2010); NC, TN (2011)
- Caps under a general limitation: OK (2011)

Source: Compiled from ATRA Tort Reform Record, December 22, 2011[59] *and Internet.*

The data from Table No. 2 reflects that those 22 states capping non-economic damages represent 52.6 percent of the U.S. population. Further, the majority of the people supporting medical tort reform widens to 67.2 percent when taking into account those states legislatively capping non-economic damages only to have their courts declare those caps unconstitutional.[60]

Data from Table No. 3 on caps on punitive damages reflects that those 21 states capping punitive damages represent 43 percent of the U.S. population, and, when considering those other four states that had punitive damages caps declared unconstitutional, proponents represent a majority of the country (59.2 percent).[61]

Since these two tort reform measures are generally regarded as the lynch pin in controlling medical costs through tort reform, one must wonder why they have not been effective thus far. Perhaps, medical product and service pricing is at the national level which defeats a policy of the state to try to control runaway medical costs through tort reform. It is possible that medical costs cannot be controlled, at least in part, through tort reform unless medical tort law and dispute resolution is federalized.

[59] AATRA, *supra* note 56.
[60] Calculated using July 1, 2011, state populations from *Wikipedia*.
[61] *Id*.

Table No. 3—Caps on Punitive Damages Through July 2012

21 states limiting dollar amount of punitive damages: AL, AK, CO, FL, ID, IN, KS, MS, MT, NH, NV, NJ, NC, ND, OH, OK, SC, TN, TX, VA, WI

4 states whose caps on punitive damages were declared unconstitutional: AR, GA, IL, MO
7 states requiring a portion of punitive damages to be paid to a state fund: FL, IN, IA, MO, NY, OR, UT

2 states requiring portion of punitive damages to state fund declared unconstitutional: CO, GA

3 states recently enacting legislation to cap punitive damages: SC, TN, WI (2011)

Source: Compiled from ATRA Tort Reform Record, December 22, 2011.[62]

B. Federal Attempts at Medical Tort Reform

Federal medical tort reform legislation has been introduced in the past without much success. In addition to the Fair and Reliable Medical Justice Act (discussed *supra* note 44), Representative Michael Burgess introduced the Medical Justice Act of 2007 in the 110th Congress. The bill aimed to establish medical tort reform at the national level by capping non-economic damages at $250,000 against health care practitioners, at $500,000 against health care institutions, and setting a total damages maximum cap at $1,400,000 (all adjusted annually by the consumer price index).[63] In the 111th Congress, Representative John Gingrey introduced the Help Efficient, Accessible, Low Cost, Timely Health Care

[62] ATRA, *supra* note 56.
[63] H. R. 3509, 110th Cong., 1st Sess. (2007).

(HEALTH) Act of 2009.[64] The bill went to committee but did not get out. Gingrey's bill would have capped noneconomic damages at $250,000; replaced joint and several liability with several liability of health care defendants making each defendant liable only for his proportional share of fault; allowed the court to restrict contingent attorney's fees and limited the amount of attorney's fees based on the size of the judgment; and set a statute of limitations of three years from the date of manifestation of the injury but not longer than one year of discovery.

In winding down the legislative process leading to health care reform, in 2009 H. R. 3962 passed in the House of Representatives before H. R. 3590 passed in the Senate. H. R. 3962 contained a short provision on medical tort reform. Section 2531 of the bill contained funding for pilot programs to alternative medical liability law that would encourage prevention of and the fair resolution of disputes, encourage disclosure of errors, make the medical liability system more reliable, and make access to medical liability insurance more affordable. The requirement was placed on the states that the reforms could not (1) limit attorney's fees or (2) impose caps on damages. In late 2009, the Senate took up H.R. 3590, the Senate's version of health care. Though medical tort reform proposals were made, for example, Senator John Ensign's amendment to cap noneconomic damages at $250,000 from a health care provider and up to two health care institutions each for a total of $750,000, no medical malpractice reform measures were passed, save one provision, namely, Section 6801—Sense of the Senate regarding medical malpractice, which states the following:

> It is the sense of the Senate that—
>
> > (1) Health care reform presents an opportunity to address issues related to

[64] H. R. 1086, 111th Cong., 1st Sess. (2009).

> medical malpractice and medical liability insurance;
> (2) States should be encouraged to develop and test alternatives to the existing civil litigation system as a way of improving patient safety, reducing medical errors, encouraging the efficient resolution of disputes, increasing the availability of prompt and fair resolution of disputes, and improving access to liability insurance, while preserving an individual's right to seek redress in court; and
> (3) Congress should consider establishing a State demonstration program to evaluate alternatives to the existing civil litigation system with respect to the resolution of medical malpractice claims.

The Sense of the Senate language became the only provision related to medical malpractice reform in the Affordable Care Act[65]. The U.S. Supreme Court found the legislation to be constitutional[66] under the Taxing Clause. Congressional repeal and a do-over would require, at least, Republications to control all three branches of government. Repeal is very unlikely to occur given the results of the November 2012 election of President Obama and retention of the voting majority by Democrats in the Senate. The likelihood of any new federal medical tort reform measures in the near future appears to be very small. State legislatures and governors, on the other hand, are moving ahead with passing tort reform measures without waiting on the Congress. Thus, it appears that federalism in the medical tort area will be retained.

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[65] Affordable Care Act, *supra* note 22.
[66] *National Federation of Independent Business v. Sebelius*, No., 11-393, slip op. (S. Ct., June 28, 2012), 567 U.S. ____ (2012); 132 S. Ct. 2566.

What might states consider in developing pilot programs? Probably the best chance is for states to establish medical screening boards. If a medical screening board operates like Montana's screening panel, the goals for medical tort reform as described in the Sense of the Senate in the Affordable Care Act could be achieved. It is hard to imagine, however, that states would give up their options to cap non-economic damages. Without substantial tort reform measures proposed by the Harvard School of Public Health, including caps on economic damages and limits or controls on plaintiff's attorney's fees, it is hard to image how medical courts could be effective in reducing costs.

IV. CONCLUSION

In the end, it is hard to predict any improvement the federal government could make in medical tort reform unless the Congress and the President become more politically conservative. It appears that the current Congress and presidential administration will not make sweeping changes for political reasons. One could make a very good argument that Congress should abandon regulation of medical disputes and leave dispute resolution and medical tort law to the states. Weak federal regulation could inhibit state regulation from providing for more substantive reforms. Furthermore, the notion of federalism is still relevant. Is medical tort reform by federal legislation necessary? No, it isn't. Whereas, federal regulation of medical tort disputes would create uniformity in the dispute resolution process, national standards for medical malpractice, available defenses for medical defendants, and afford greater consistency in verdicts, the goals of medical tort reform can be achieved by progressive states leading the way. States have already adopted some substantive reform measures, and, over time, unless the federal government limits further progress, states will continue to try new reform measures, like California, Texas, Montana, Mississippi, and Tennessee.

THE BROADENING SCOPE OF THE FMLA COMPLIANCE PERIOD: EMPLOYERS, YIELD AND PROCEED WITH CAUTION!

By

Keith William Diener*

I. INTRODUCTION

The Family and Medical Leave Act of 1993 (FMLA) was created in response to socio-economic changes to twentieth century families. In its twenty years as federal law, the FMLA has enabled innumerous families to survive qualifying life events without fear of retaliation or interference by employers. Since February 6, 1995, when the original Department of Labor (DOL) regulations came into effect to implement the FMLA, the mandatory fifteen day compliance period of 29 CFR 825.305(b) has ensured the effective administration of certifications of serious health conditions under the FMLA. From 1995 through 2009, the compliance period was strictly construed to recurrently hold employers liable for taking adverse actions against employees during the compliance period. The 2008 Amendments to the DOL regulations came into effect in 2009, and expanded the compliance period to apply to all requests for FMLA leave, but, in doing so, weakened the language pertaining to the mandatory fifteen day compliance period. Regardless of the changed wording, United States' courts should continue to strictly construe the compliance period in accordance with the intent of the DOL to ensure efficiency in administration

and litigation, to fulfill the purposes of the FMLA, and to promote fairness.

Section II examines the scope and application of the FMLA. Section III analyzes the statutory provisions and regulations pertinent to serious health conditions. Section IV discusses compliance period cases. Section V argues that courts should continue to strictly construe and enforce the compliance period. Section VI concludes.

II. FMLA: SCOPE AND APPLICATION

In 2013, the FMLA celebrated its twentieth anniversary. The FMLA was enacted on February 5, 1993, and came into effect on August 5, 1993.[1] The enactment of the FMLA signified the first federal legislative regime for the governance of family-work issues.[2] When President Bill Clinton signed the FMLA into law, he declared that United States' employees "will no longer need to choose between the job they need and the family they love."[3] The passage of the FMLA was an early victory for the Clinton administration; a victory in accord with the administration's aim of returning the government to the people.[4] The passage of the FMLA

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[1] Luis A. Cabassa, *Columns: Labor and Employment Law: The Family Medical Leave Act – Ten Years Later*, *77 Fla. Bar J. 69, 69 n.1 (October 2003).*

[2] Pauline Kim, *The Family and Medical Leave Act of 1993: Ten Years of Experience, 15 WASH. U. J.L. &POL'Y 1, 1* (2004).

[3] Paul Richter and Gebe Martinez, Clinton Signs Family Leave Bill Into Law, Las Angeles Times (February 6, 1993). *See also* Amanda Scott Vaccaro, *Ninth Annual Review of Gender and Sexuality Law: Family Law Chapter: The Family and Medical Leave Act*, *9 GEO. J. GENDER & L. 1001, 1004 (*2008); *and* Pauline Kim, *The Family and Medical Leave Act of 1993: Ten Years of Experience, 15 WASH. U. J.L. &POL'Y 1, 1* (2004).

[4] Pauline Kim, *The Family and Medical Leave Act of 1993: Ten Years of Experience, 15 WASH. U. J.L. &POL'Y 1, 1-2* (2004).

followed George H.W. Bush's vetoes of two family-work bills during the preceding administration.[5] Over the past twenty years, the FMLA enabled countless families to survive qualifying life events, without fear of retaliation or interference by their employers.

Congress identified the purposes of the FMLA within the text of the statute.[6] Prior to the enactment of the FMLA, less than half of the states maintained family-work protections, and many of those that did, were non-binding for private employers.[7] The socioeconomic climate of United States' families changed in the twentieth century to include more families with both spouses working, and more single-parent households.[8] The FMLA was created to balance the changing needs and demands of families and the workplace, to provide mandated leave for qualifying life events, and to promote equal opportunity for both men and women.[9] The FMLA aspired to attain these purposes by accommodating the legitimate interests of employers, taking into account the need to provide economic security to the family unit.[10]

The purposes of the FMLA are curtailed by its limited scope of application. The FMLA only applies to "eligible employees" who work for "covered employers." Generally, an "eligible employee" is an employee who works for a covered employer for at least

[5] *Id. See also* The Family and Medical Leave Act of 1990 (101st Congress), Library of Congress Online Thomas Database; *and* The Family and Medical Leave Act of 1991 (102nd Congress), Library of Congress Online Thomas Database, *available at http://thomas.loc.gov* (last visited July 10, 2013).
[6] 29 USCS § 2601.
[7] Charles L. Baum, *The Family and Medical Leave Act of 1993: Ten Years of Experience: Has Family Leave Legislation Increased Leave-Taking?*, 15 WASH. U. J.L. & POL'Y 93, 98 n. 30 (2004).
[8] Pauline Kim, *The Family and Medical Leave Act of 1993: Ten Years of Experience, 15 WASH. U. J.L. &POL'Y 1, 2* (2004); *and* 29 USCS § 2601.
[9] 29 USCS § 2601.
[10] *Id.*

twelve months prior to requesting leave, has worked at least 1,250 hours with that covered employer during the previous 12 month period, and whose employer has 50 or more employees within 75 miles of the worksite where the employee works [11] Generally, a "covered employer" is one who is engaged in commerce who "employs 50 or more employees for each working day during each of 20 or more calendar workweeks in the current or preceding calendar year," or is a public employer.[12] It is estimated that these prerequisites for application of the FMLA result in approximately 40% of the workforce remaining without the benefits of FMLA leave.[13]

Eligible employees who work for covered employers may request up to 12 weeks of FMLA designated leave in a 12 month period, for a variety of qualifying life events.[14] Qualifying life events include: (a) the birth of the employee's son or daughter; (b) the adoption of a son or daughter by the employee; (c) the need to care for a son, daughter, spouse, or parent with a serious health condition;[15] (d) the occurrence of a serious health condition by the employee that prevents the employee from performing the functions of the employee's job; and, after the 2008 and 2009 Amendments[16] to the FMLA, (e) because of a qualifying exigency

[11] 29 USCS § 2611(2); 29 CFR 825.110; *and* 29 CFR 825.111.
[12] 29 USCS § 2611(4); *and* 29 CFR 825.104.
[13] Michael Selmi, *Family Leave and the Gender Wage Gap*, 78 N.C. L. Rev. 707, 760-61 (2000) ("Despite these restrictions, it is estimated that the Act covers approximately 60% of the nation's private-sector workforce, even though only about 11% of the nation's employers are covered. Public employers are also bound by the statutory provisions, bringing the total number of covered employees to roughly 66% of the workforce, with approximately 55% of employees statutorily eligible to take leave").
[14] 29 USCS § 2612.
[15] 29 CFR 825.122 (for the DOL's broad construal of the definitions of these family members).
[16] As Amended by Section 585 of the National Defense Authorization Act for FY 2008, Public Law [110-181] (January 28, 2008); and Section 585 of the National Defense Authorization Act for FY 2010, Public Law [111-84] (October

"arising out of the fact that the spouse, or a son, daughter, or parent of the employee is on covered active duty (or has been notified of an impending call or order to covered active duty) in the Armed Forces."[17] Subject to minor exceptions,[18] if any of these life events occur, an eligible employee may take up to 12 weeks of FMLA leave in a 12 month period (from a covered employer), and is guaranteed reinstatement to an equivalent position upon completion of leave.[19] After the 2008 and 2009 Amendments, for certain servicemember leave requests, eligible employees who work for covered employers may take up to 26 weeks of leave during a 12 month period to care for a son, daughter, parent, spouse, or next of kin who is a servicemember.[20] This servicemember leave "shall only be available during a single 12-month period."[21] Although FMLA leave is generally unpaid leave,[22] employers must maintain employees' benefits, including health benefits, throughout FMLA leave and reinstatement.[23]

In its twenty years as federal law, the FMLA continues to impact families and employers alike. A complex system of Department of Labor (DOL) regulations implements and interprets the FMLA. These regulations govern, among other things, the certification process for serious health conditions. The FMLA statutory provisions and DOL regulations pertinent to serious health conditions are considered in the next section.

28, 2009). *See also* 29 CFR 825.112-825.125 (for definitions and interpretations relating to these qualifying life events).

[17] 29 USCS § 2612(a).

[18] 29 USCS § 2614(b) provides an "Exemption concerning certain highly compensated employees," otherwise known as the "key employee" exemption (29 CFR 825.217-825.219). *See also* 29 CFR 825.216 (for other exemptions).

[19] 29 USCS § 2614(a). *See also* 29 C.F.R. 825.214-825.216 (for rules relating to reinstatement).

[20] 29 USCS § 2612(a)(3-4).

[21] 29 USCS § 2612(a)(3).

[22] 29 CFR 825.207 (describing certain circumstances when FMLA leave may be paid leave).

[23] See 29 U.S.C. 2614(a)(2), 2614(c)(1); *and* 29 C.F.R. 825.209.

III. SERIOUS HEALTH CONDITIONS

FMLA leave requests resulting from serious health conditions give rise to unique issues of interpretation and application of the FMLA and its implementing regulations. Although the definition seems clear on its face, in light of the myriad of regulatory requirements pertaining to serious health conditions, there is considerable room for both employers and employees to procedurally misstep before, during, or after a request for FMLA leave. The FMLA defines a serious health condition as "an illness, injury, impairment, or physical or mental condition that involves-- (A) inpatient care in a hospital, hospice, or residential medical care facility; or (B) continuing treatment by a health care provider."[24] The DOL regulations deconstruct the language of this statutory provision to further define what constitutes a "serious health condition,"[25] "inpatient care,"[26] and "continuing treatment,"[27] in the context of the FMLA. The DOL regulations specifically exclude "cosmetic treatments…such as most treatments for acne or plastic surgery…unless inpatient hospital care is required or unless complications develop," and further exclude "the common cold, the flu, ear aches, upset stomach, minor ulcers, headaches other than migraine, routine dental or orthodontia problems, and periodontal disease" from the definition of serious health conditions, unless complications arise.[28] On the other hand, the DOL regulations also provide that "[r]estorative dental or plastic surgery after an injury or removal of cancerous growths are serious health conditions provided all the other conditions of this regulation are met. Mental illness or allergies may be serious

[24] 29 USCS § 2611(11).
[25] 29 CFR 825.113.
[26] 29 CFR 825.114 provides that "Inpatient care means an overnight stay in a hospital, hospice, or residential medical care facility, including any period of incapacity as defined in § 825.113(b), or any subsequent treatment in connection with such inpatient care."
[27] 29 CFR 825.115.
[28] 29 CFR 825.113(d).

health conditions, but only if all the conditions of this section are met."[29] Determining if an employee has a serious health condition, as defined by the FMLA and the DOL regulations, can be a complex task.

Due to the complexity of determining if an employee has a serious health condition, the FMLA permits an employer to request a medical certification from the employee's health care provider to certify that the employee does have a serious health condition.[30] If an eligible employee requests leave to care for a son, daughter, spouse, or parent with a serious health condition, then an employer may similarly request that the pertinent person's health care provider complete the medical certification.[31] A sufficient medical certification is explicitly defined in the FMLA, and includes the following: the date the serious health condition began, the likely duration of the serious health condition, a statement by the health care provider of medical facts about the serious health condition, and, depending on which type of leave is taken, either a statement that the employee needs leave to care for the pertinent family member (and the estimated time of leave), or a statement that the employee cannot perform the functions of the employee's position.[32] There are also additional requirements for a sufficient certification when intermittent leave or a reduced leave schedule, are recommended.[33] In the event the employer has reason to doubt that a submitted certification, even if sufficient, is valid, then it may (at its own expense) request a second opinion from another health care provider (who is not employed by the employer on a regular basis).[34] If there are conflicting opinions resulting from the two evaluations, then the employer may (at its own expense),

[29] *Id.*
[30] 29 USCS § 2613(a).
[31] *Id.*
[32] 29 USCS § 2613(b). *See also* 29 CFR 825.306.
[33] *Id.*
[34] 29 USCS § 2613(c). *See also* 29 CFR 825.306.

request the employee seek the opinion of a third health care provider (approved jointly by the employer and employee).[35] The decision of the third health care provider is binding on both the employer and employee.[36] These basic requirements of medical certifications under the FMLA are further refined by the DOL regulations.

The DOL regulations include the general rule for medical certifications in 29 CFR 825.305. This general rule is elaborated in subsequent regulations that address the content of medical certifications,[37] the authentication of medical certifications,[38] re-certifications of serious health conditions,[39] and a variety of other types of certifications that may arise in FMLA situations.[40] The interim DOL regulations were promulgated on June 4, 1993, and came into effect with the FMLA on August 5, 1993.[41] The first, non-interim version of 29 CFR 825.305 was promulgated on January 6, 1995 (and took effect on February 6, 1995).[42] It was

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[35] 29 USCS § 2613(d). *See also* 29 CFR 825.306.
[36] 29 USCS § 2613(d). *See also* 29 CFR 825.306.
[37] 29 CFR 825.306.
[38] 29 CFR 825.307.
[39] 29 CFR 825.308.
[40] *See* 29 CFR 825.309 ("Certification for leave taken because of a qualifying exigency"); 29 CFR 825.310 ("Certification for leave taken to care for a covered servicemember"); 29 CFR 825.312 ("Fitness-for-duty certification"), *and* 29 CFR 825.313 ("Failure to provide certification").
[41] 58 FR 31794, 31807 (June 4, 1993) (interim rule §825.305 went into effect with the FMLA on August 5, 1993; this rule provides: "Employers may require a medical certification from a health care provider to support FMLA leave requests either to care for an employee's seriously-ill family member, or for leave due to a serious health condition that makes the employee unable to perform the functions of the employee's job. Employees must provide such certification "in a timely manner." The regulations define "timely manner" as within 15 calendar days, unless it is not practicable to do so under the circumstances. Employers must advise the employee if medical certification will be required when the employee requests leave so the employee can obtain it during visits to the health care provider").
[42] 60 FR 2180, 2258 (Jan. 6, 1995).

substantially revised on November 17, 2008 (these revisions took effect on January 16, 2009).[43] The DOL regulations were again revised on February 6, 2013 (these revisions took effect on March 8, 2013), but the most recent revisions did not substantively impact 29 CFR 825.305.[44] As originally promulgated, the 1995 version of 29 CFR 825.305 provided a requirement that employers must request the medical certification from employees within two business days of the employees' notice to the employer of the need for leave.[45] It also required that:

> (b) When the leave is foreseeable and at least 30 days' notice has been provided, the employee should provide the medical certification before the leave begins. When this is not possible, the employee must provide the requested certification to the employer within the time frame requested by the employer (*which must allow at least 15 calendar days after the employer's request*), unless it is not practicable under the particular circumstances to do so despite the employee's diligent, good faith efforts (emphasis added).[46]

The 2008 revisions to 29 CFR 825.305 extended the two business day requirement to five business days, allowing employers more time to request the medical certification from employees.[47] The revisions also changed the wording of 29 CFR 825.305(b) significantly, so as to make the same fifteen day time frame apply to all cases of FMLA requests for certification (in order to promote consistency with the requirements of related FMLA provisions).[48]

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[43] 73 FR 67934, 68100-68101 (Nov. 17, 2008).
[44] 78 FR 8834, 8902 (Feb. 6, 2013).
[45] 60 FR 2180, 2258 (Jan. 6, 1995).
[46] *Id.*
[47] 73 FR 67934, 68010-68013 (November 17, 2008).
[48] *Id.*

When this change was proposed to the rule, commenters supported it because the change established "a clear deadline that would facilitate FMLA administration."[49] The DOL decided to implement the proposed change because it believed "that applying the 15-day time period as the outer limit of the time period by which the employee must respond to all requests for certification will facilitate the prompt determination of whether leave qualifies as FMLA protection."[50] The final rule, as adopted in 2008, and still in effect today, reads:

> (b) Timing. In most cases, the employer should request that an employee furnish certification at the time the employee gives notice of the need for leave or within five business days thereafter, or, in the case of unforeseen leave, within five business days after the leave commences. The employer may request certification at some later date if the employer later has reason to question the appropriateness of the leave or its duration. *The employee must provide the requested certification to the employer within 15 calendar days after the employer's request*, unless it is not practicable under the particular circumstances to do so despite the employee's diligent, good faith efforts or the employer provides more than 15 calendar days to return the requested certification (emphasis added).[51]

The revised 29 CFR 825.305(b), mandates that employers must give employees at least fifteen calendar days to return the medical

[49] *Id*.
[50] *Id*.
[51] 73 FR 67934, 68010-68013 (November 17, 2008).

certification.[52] The fifteen day compliance period currently applies to foreseeable leave, unforeseeable leave, and recertification.[53] If, however, an employee does not provide the medical certification within the requested time period (which must be at least fifteen days), then the employer may deny the employee's FMLA leave.[54] During the compliance period, the employer must yield and proceed with caution before terminating or taking any adverse action against the requesting employee. The next section examines cases from federal courts across the United Sates involving the fifteen day compliance period. After examining these cases, this essay then explains why strict enforcement of the fifteen day compliance period should continue.

IV. COMPLIANCE PERIOD CASES

Many federal courts hold that terminating an employee within the fifteen day compliance period required by 29 CFR 825.305(b) is a violation of an employee's FMLA rights. Although federal courts vary in their interpretations of viable causes of action under the FMLA, it is generally accepted that there are two causes of action an injured employee may bring against an employer under the FMLA: interference (entitlement theory) and retaliation (discrimination theory).[55] If an employer terminates an employee within the compliance period, the employer is at risk of both interference and retaliation claims.

The DOL regulations provide examples of activities that constitute interference with FMLA rights. According to the DOL regulations,

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[52] The compliance period is fifteen *calendar* days (not business days), but the five day time period for the employer to request a certification after notice of the need for leave is five *business* days (not calendar days).
[53] 29 CFR 825.313.
[54] 29 CFR 825.305(c); *and* 29 CFR 825.313.
[55] 29 USCS § 2615. *See also* 29 CFR 825.220; *and Washington Convention Ctr. Auth. v. Johnson*, 953 A.2d 1064, 1075-76 (D.C. 2008) ("the retaliation or discrimination theory and the entitlement or interference theory").

interference includes "not only refusing to authorize FMLA leave, but discouraging an employee from using such leave. It would also include manipulation by a covered employer to avoid responsibilities under FMLA, for example: (1) Transferring employees from one worksite to another for the purpose of reducing worksites, or to keep worksites, below the 50-employee threshold for employee eligibility under the Act; (2) Changing the essential functions of the job in order to preclude the taking of leave; [and] (3) Reducing hours available to work in order to avoid employee eligibility."[56] The regulations also provide that the "prohibition against interference prohibits an employer from discriminating or retaliating against an employee or prospective employee for having exercised or attempted to exercise FMLA rights."[57] The FMLA's prohibitions against interference are broadly construed to include a variety of activities.

Many courts indicate that terminating an employee within the compliance period constitutes a violation of the FMLA. The Courts of Appeals for the Fourth Circuit, Fifth Circuit, Sixth Circuit, Seventh Circuit, and Eleventh Circuit all indicate that terminating an employee within the compliance period may be a violation of the FMLA.[58] These courts generally determine that

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[56] 29 CFR 825.220(b).

[57] 29 CFR 825.220(c).

[58] *Rhoads v. FDIC*, 257 F.3d 373, 383 (4th Cir. 2001) (stating that "the employer must allow the employee at least fifteen calendar days to submit" the medical certification); *Saenz v. Harlingen Medical Center, L.P.,* 613 F.3d 576, 581-582 n. 7 (5th Cir. 2010) (reversing district court's granting of summary judgment as to FMLA interference claim, in part, because employee was terminated during 15 day period granted to complete medical certification); *Lubke v. City of Arlington*, 455 F.3d 489, 496-97 (5th Cir. 2006) (mentioning that it is required under DOL regulations (29 C.F.R. §825.305(b)) that an employer permit an employee 15 days to complete medical certification); *Killian v. Yorozu Auto. Tenn., Inc*., 454 F.3d 549, 554-555 (6th Cir. 2006) (holding it "clearly a violation of the FMLA" to terminate an employee 6 days into the 15 days permitted to complete medical certification); *Muhammad v. Ind. Bell Tel. Co.*, 182 Fed.Appx. 551, 553 (7th Cir. 2006) (mentioning the 15 day period to complete medical

termination within the compliance period may constitute interference with an employee's FMLA rights.[59] These cases, however, were decided by application of the pre-2008 amendments to 29 CFR 825.305(b) which provides that the employer "must allow [the employee] at least 15 calendar days after the employer's request…" to return the medical certification.[60] After the 2008 Amendments to the FMLA, the language of 29 CFR 825.305(b) was changed to say instead that the "employee must provide the requested certification to the employer within 15 calendar days after the employer's request…"[61] Although the language is not as explicit in its assertion of the 15 day requirement post-2008, it is apparent from the notice of final rulemaking that the DOL intended to maintain the compliance period, and aspired to extend the scope of its application, as opposed to limit the scope of its application.[62]

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certification); *and Cooper v. Fulton County,* 458 F.3d 1282, 1286 (11th Cir. 2006) (stating that the employer must give the employee fifteen days to complete the certification).

[58] *Id.* (The current regulation 29 CFR 825.313 (formerly 29 CFR 825.311) includes the fifteen day compliance period, and at least one court has based a compliance period violation upon this regulation) (*see Killian v. Yorozu Auto. Tenn., Inc*., 454 F.3d 549, 553 (6th Cir. 2006)). *See also* 73 FR 67934, 68068 (November 17, 2008) ("Current § 825.311, renumbered as § 825.313 in the final rule, provides that if an employee fails to provide medical certification in a timely manner, the employer may "delay" the taking of FMLA leave until it has been provided.")

[59] *Id.* (The current regulation 29 CFR 825.313 (formerly 29 CFR 825.311) includes the fifteen day compliance period, and at least one court has based a compliance period violation upon this regulation) (*see Killian v. Yorozu Auto. Tenn., Inc*., 454 F.3d 549, 553 (6th Cir. Tenn. 2006)). *See also* 73 FR 67934, 68068 (November 17, 2008) ("Current § 825.311, renumbered as § 825.313 in the final rule, provides that if an employee fails to provide medical certification in a timely manner, the employer may "delay" the taking of FMLA leave until it has been provided.")

[60] 60 FR 2180, 2258 (Jan. 6, 1995).

[61] 73 FR 67934, 68010-68013 (November 17, 2008).

[62] *Id.*

In a 2009 decision, *Deluca v. Simmons Mfg. Corp.,* the United States District Court for the Middle District of Pennsylvania granted plaintiff's motion for summary judgment as to her interference claim because she was terminated two days into the fifteen day compliance period.[63] Although the facts of *Deluca* arose prior to the 2008 Amendments to the DOL regulations (Deluca was terminated on July 19, 2007), the court applied the post-2008 version of 29 CFR 825.305(b) when reaching its decision in 2009.[64] When determining that termination within the fifteen day compliance period was interference, the court quoted the post-2008 language of the regulation. The court held that: DeLuca was required to

> provide the requested certification to [Simmons] within 15 calendar days after [Simmons'] request, unless it [was] not practicable under the particular circumstances to do so despite [DeLuca's] diligent, good faith efforts…In this case, however, Simmons terminated Ms. DeLuca's employment on July 19, 2007, just two (2) days after Ms. Rushton sent the July 17, 2007 letter requesting information for FMLA purposes. Accordingly, the Court finds that Simmons' termination of DeLuca's employment interfered with, restrained, and denied DeLuca's efforts to seek FMLA leave in July 2007, and will grant her Motion for Summary Judgment with respect to her FMLA interference claim.[65]

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[63] *DeLuca v. Simmons Mfg. Corp*., Civil Action No. 3:07-cv-2143, 2009 U.S. Dist. LEXIS 36164, 14 Wage & Hour Cas. 2d (BNA) 1479 (M.D. Pa. Apr. 29, 2009).

[64] *Id*. at 19.

[65] *Id.(* internal citations and quotations omitted).

Deluca indicates that federal courts will continue to apply a strict reading of 29 CFR 825.305(b) in interference actions, despite the changed language of the regulation.

Although employers generally must yield for fifteen days after requesting a medical certification from an employee before taking adverse action against that employee, courts differ as to whether termination of the employee is a permissible recourse after the expiration of the fifteen day compliance period. Many courts hold that the failure to provide a medical certification within the appropriate time frame "is fatal to a claim of FMLA interference."[66] The DOL regulations also provide that the employer may deny FMLA leave if an employee does not return the medical certification by the end of the compliance period, subject to diligent, good faith efforts.[67] The Sixth Circuit holds that the appropriate option for an employer to take in the event that an employee does not submit a medical certification by the end of the compliance period is to delay leave, and not to terminate the employee.[68] Other courts hold that it is permissible to terminate an employee who does not submit a medical certification within the fifteen day compliance period.[69] The Fifth Circuit determined that if an employee submits a completed medical certification before

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[66] *Tippens v. Airnet Sys.,* No. 2:05-CV-421, 2007 U.S. Dist. LEXIS 23808, 15 (S.D. Ohio Mar. 30, 2007) (*quoting Carpenter v. Kaiser Permanente,* No. 1:04-CV-1689, 2006 U.S. Dist. LEXIS 69564, 2006 WL 2794787 at *13 (N.D. Ohio Sept. 27, 2006) (*citing Gulan v. Fed. Reserve Bank of Cleveland,* 2003 WL 22047802 (N.D.Ohio Aug. 27, 2003); *and Harrington v. Boysville of Michigan, Inc*., 145 F.3d 1331 (6th Cir.1998))).

[67] 29 CFR 825.313.

[68] *Stroud v. Connor Concepts, Inc*., 2009 U.S. Dist. LEXIS 112072, 15, 22 Am. Disabilities Cas. (BNA) 1220 (M.D. Tenn. Dec. 2, 2009) (*quoting Killian v. Yorozu Auto. Tenn., Inc*., 454 F.3d 549, 555 (6th Cir. 2006) ("even if Killian had failed to provide the certification in a timely fashion, [the employer's] remedy under the regulations was [] delayed leave, not termination").

[69] *Young v. Russell Corp*., 2008 U.S. Dist. LEXIS 104817, 6-7 (M.D. Ala. Dec. 29, 2008) (*citing Baldwin-Love v. Electronic Data Systems, Inc*., 307 F. Supp. 2d 1222 (M.D. Ala. 2004)).

the fifteen days expires, that "29 C.F.R. 825.305(b) is no longer implicated and the employer is not required to wait fifteen days before taking action on the employee's request for medical leave."[70] For interference actions, the employee's failure to submit a medical certification by the close of the compliance period, could lead to an award of summary judgment to the employer in subsequent litigation (subject to the employee's diligent, good faith efforts to timely submit the certification).

The DOL explained that they key to an employee's diligent, good faith efforts is communication with the employer regarding efforts to attain the completed medical certification.[71] The DOL suggested a "totality of the circumstances" test to determine if an employee made diligent, good faith efforts to return a medical certification.[72] The circumstances an employer should consider include the "employee's efforts to schedule appointments and follow-up with the health care provider's office, or other appropriate offices in the case of qualifying exigency leave or military caregiver leave, to ensure that the certification is completed; employers should be mindful that employees must rely on the cooperation of their health care providers and other third parties in submitting the certification and that employees should not be penalized for delays over which they have no control."[73] In other words, employees should communicate their efforts to employers, and employers should be sympathetic to the individualized circumstances of employees. If adverse action is taken against an employee who properly communicates diligently and in good faith to the employer, then it may lead to employer liability (even if the employee does not return the medical certification within the fifteen day compliance period).

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[70] *Boyd v. State Farm Ins*., 158 F.3d 326, 332 (5th Cir. Tex. 1998).
[71] 73 FR 67934, 68010-68013 (November 17, 2008).
[72] *Id.*
[73] *Id.*

Termination within the fifteen day compliance period could also create a *prima facie* case of retaliation under the FMLA. Retaliation claims are governed by the burden-shifting framework described by the United States Supreme Court in *McDonnell Douglas Corp. v Green*, and its progeny.[74] The United States District Court for the District of Columbia held that termination five days into the fifteen day compliance period constituted a *prima facie* case of retaliation under the FMLA.[75] The District Court described the burden-shifting framework as follows:

> [a]n employee may establish a prima facie case creating a presumption of retaliation by showing (1) that he exercised rights afforded by the [FMLA], (2) that he suffered an adverse employment action, and (3) that there was a causal connection between the exercise of his rights and the adverse employment action If a prima facie case is established, the burden then shifts to the defendant to overcome this presumption by proffering a legitimate basis for this adverse action, and then the burden shifts back to a plaintiff to show that the proffered reason is pretextual.[76]

The District Court held that Plaintiff's request for FMLA leave constituted protected activity (Plaintiff was sent the medical

[74] *McDonnell Douglas Corp. v. Green,* 411 U.S. 792 (1973). *See also Burlington Northern & Santa Fe Ry. v. White*, 548 U.S. 53 (2006).
[75] *Hopkins v. Grant Thornton Int'l,* 851 F. Supp. 2d 146, 152-153 (D.D.C. 2012) (internal citations and quotations omitted). *See also Hopkins v. Grant Thornton LLP*, No. 12-7037, 2013 U.S. App. LEXIS 9171, 3 (D.C. Cir. May 3, 2013) (in affirming the district court's decision, the circuit court, on first impression, determined that "The fifteen-day window does not bar termination for a valid business reason such as low hours or being part of a project that comes to an end").
[76] *Id.*

certification the same day as his request).[77] The fact that he was terminated constituted an adverse action.[78] The fact that he was terminated five business days after his request for FMLA leave constituted causality (holding that close temporal proximity can constitute causality).[79] In this case, the District Court determined that terminating an employee five days into the fifteen day compliance period constituted a *prima facie* case of retaliation.

Employers that do not yield prior to taking adverse action against their employees after requesting a medical certification embrace significant risks of employee lawsuits arising under both interference and retaliation theories.[80] The next section argues that the compliance period should continue to be strictly construed and enforced by courts despite the changed wording of 29 CFR 825.305(b).

V. THE NECESSARY ENFORCEMENT OF THE COMPLIANCE PERIOD

Regardless of the modified language of 29 CFR 825.305(b) resulting from the 2008 Amendments, courts should continue to strictly enforce the fifteen day compliance period in accordance with the intent of the DOL. The compliance period increases efficiency, promotes the underpinning purposes of the FMLA, and is fair to employers and employees, particularly considering the significant limits to damages under the FMLA.

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[77] *Id.*
[78] *Id.*
[79] *Id.*
[80] *See also* 29 CFR 825.220(e) ("Individuals, and not merely employees, are protected from retaliation for opposing (e.g., filing a complaint about) any practice which is unlawful under the Act. They are similarly protected if they oppose any practice which they reasonably believe to be a violation of the Act or regulations").

Upon the 2008 notice of the final rulemaking of the revised 29 CFR 825.305(b), the DOL explained that its intent, when changing the language of the regulation, was to expand the scope of the compliance period and ensure consistency with other regulations. According to the DOL, the proposed regulation which was adopted as the final regulation "applied the 15-day time frame, subject to the employee's diligent, good faith efforts, to all cases of FMLA leave in order to make it consistent with the timing requirements set forth in §825.311 [currently §825.313] of the regulations."[81] According to the DOL, the 1995 version of the rule provided "that where the need for leave is foreseeable and notice is provided 30 days in advance, the employee must provide any requested medical certification prior to the commencement of the leave; in all other cases, the employee must provide medical certification within 15 days after the leave is requested 'unless it is not practicable under the particular circumstances to do so despite the employee's diligent, good faith efforts.'"[82] The DOL changed the wording of the regulation believing that the fifteen day limit would facilitate determinations as to whether requested leave qualified for the protections of the FMLA.[83] In fact, in the 2013 notice of final rulemaking, the DOL reiterates that the "employer must provide the employee at least 15 calendar days to provide the initial certification, and any subsequent recertification, unless the employee is not able to do so despite his or her diligent good faith efforts."[84] By changing the language of 29 CFR 825.305(b), the DOL intended to expand the scope of the compliance period to apply to all requests for FMLA leave requiring certifications of serious medical conditions (and not diminish its effectiveness).

The compliance period promotes both the efficiency of the FMLA leave process and efficiency in FMLA litigation. When an injured

[81] 73 FR 67934, 68010-68013 (November 17, 2008).
[82] *Id.*
[83] *Id.*
[84] 78 FR 8834, 8872 (2013).

employee is terminated prior to the expiration of the fifteen day compliance period, it becomes increasingly difficult for the employee to prove (in a court of law) a serious health condition under the FMLA. Perhaps, in a court of law, the employee's (or family member's) health care provider's notes and charts could evidence a serious health condition. Other requirements of a sufficient certification, such as the duration of requested leave, would not necessarily be in the health care provider's notes.[85] The pertinent health care provider could be a witness at trial, but memories fade, and, even worse, the health care provider could relocate, retire, or otherwise become unavailable in the time between the FMLA violation and trial. Further, any attempts to subsequently gather information pertaining to the serious health condition, after the termination, could lead to employer allusions of impropriety in such actions (which could unduly influence a court or jury). By requiring abidance to the fifteen day compliance period, it will ensure that the medical certification is completed, or, if the medical certification is not completed within the compliance period, the employer is then entitled to deny leave or otherwise take adverse action against the employee. The fifteen day compliance period promotes the prompt and efficient facilitation of FMLA leave, and preserves the evidence necessary for prompt and efficient litigation of FMLA litigation.

The compliance period promotes the underlying purposes of the FMLA. The purposes of the FMLA include the desire to "balance the demands of the workplace with the needs of the families," and to "promote the stability and economic security of families, and…family integrity."[86] The purposes of the FMLA also include the entitlement to reasonable leave for, among other things, medical reasons taking into account the need to accommodate the legitimate interests of employers.[87] Strict enforcement of the

[85] 29 USCS § 2613(b). *See also* 29 CFR 825.306.
[86] 29 USCS §2601(b).
[87] *Id.*

compliance period promotes the purposes of the FMLA by ensuring that employees are given the opportunity to medically certify their need for leave, and in a way that is fair to the legitimate interests of employers (i.e., when the fifteen days expires, employers can deny FMLA leave or otherwise take adverse action if the medical certification is not provided).[88] The compliance period ensures that employees have adequate time and opportunity to certify a serious health condition that requires time away from work. By ensuring adequate time to complete the certification, the compliance period enhances economic security of families and safeguards reasonable leave for serious health conditions.

Finally, the FMLA includes severe limitations to damages. Given these significant restrictions to damage recovery by injured employees, it is fair to require strict adherence to the fifteen day compliance period – to both protect employees and deter employers from violating the FMLA. As the Supreme Court of the United States explained, under the FMLA, "[t]he damages recoverable are strictly defined and measured by actual monetary losses…and the accrual period for backpay is limited by the Act's 2-year statute of limitations …extended to three years only for willful violations…"[89] These limits to damages, including the preclusion of punitive damages, provide another reason to ensure strict abidance to the fifteen day compliance period.[90] Otherwise,

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[88] 29 CFR 825.313.

[89] *Nev. Dep't of Human Res. v. Hibbs*, 538 U.S. 721, 739-740 (U.S. 2003).

[90] Under 29 CFR 825.400(c), other damages for FMLA violations include "wages, employment benefits, or other compensation denied or lost to such employee by reason of the violation; or, where no such tangible loss has occurred, such as when FMLA leave was unlawfully denied, any actual monetary loss sustained by the employee as a direct result of the violation, such as the cost of providing care, up to a sum equal to 26 weeks of wages for the employee in a case involving leave to care for a covered servicemember or 12 weeks of wages for the employee in a case involving leave for any other FMLA qualifying reason. In addition, the employee may be entitled to interest on such

injured employees may be deterred from asserting their rights under the FMLA, and employers may be encouraged to ignore the requirements of the FMLA (knowing full well that any violation of the compliance period will result in relatively minor payouts to employees). Strict adherence to the compliance period is fair to both employees and employers, particularly in light of these severe limits as to damages.

The fifteen day compliance period is fair to both employers and employees, promotes the underpinning purposes of the FMLA, and ensures efficient processing of FMLA requests and efficiency in FMLA litigation. Despite the changes in wording resulting from the 2008 Amendments to 29 CFR 825.305(b), the compliance period should continue to be strictly enforced by United States' courts in accordance with the intent of the Department of Labor.

VI: CONCLUSION

The Family and Medical Leave Act of 1993 requires covered employers to provide eligible employees with up to twelve weeks of unpaid leave (twenty-six weeks for servicemember leave) for, among other reasons, serious health conditions. The Department of Labor regulations include complex procedural requirements that govern the process by which employees with serious health conditions may request leave and certify their health conditions to employers. The complex array of Department of Labor regulations

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sum, calculated at the prevailing rate. An amount equaling the preceding sums may also be awarded as liquidated damages unless such amount is reduced by the court because the violation was in good faith and the employer had reasonable grounds for believing the employer had not violated the Act. When appropriate, the employee may also obtain appropriate equitable relief, such as employment, reinstatement and promotion. When the employer is found in violation, the employee may recover a reasonable attorney's fee, reasonable expert witness fees, and other costs of the action from the employer in addition to any judgment awarded by the court."

includes a mandatory fifteen day compliance period for medical certifications of serious health conditions.

From 1995 through 2009, the mandatory fifteen day compliance period of 29 CFR 825.305(b) was strictly construed and enforced to impose liability on employers that took adverse action against employees prior to the expiration of the compliance period. The 2008 Amendments to 29 CFR 825.305(b) came into effect in 2009, and intended to broaden the scope of the compliance period but, in broadening the scope, weakened the language pertaining to the fifteen day compliance period. Regardless of the changed wording, United States' courts should continue to strictly construe the compliance period in accordance with the intent of the DOL to ensure efficiency in administration and litigation, to fulfill the purposes of the FMLA, and to promote fairness.

I DON'T DO WRITING: A MODEL FOR OVERCOMING FACULTY RESISTANCE TO USING WRITING ASSIGNMENTS IN THE CLASSROOM

By

Michael R. Koval*
R. Michael Garner**

I. INTRODUCTION

It is generally accepted that there is significant educational value in using writing assignments to help students learn, understand and apply complex topics, and that business programs have incorporated writing into the curriculum.[1] There is evidence, however, that many business school instructors feel insecure when it comes to creating, explaining, and especially assessing writing assignments,[2] and this insecurity in turn limits the use and effectiveness of such assignments.[3] The authors believe the

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[1] Susan Plutsky & Barbara A. Wilson, *Writing Across the Curriculum in a College of Business and Economics,* 64 BUSINESS COMMUNICATION QUARTERLY 26, 27 (2001).

[2] *Id.* at 28.

[3] The authors, and probably many readers, have experienced that 'pang of guilt' upon receiving the start-of-semester email from the good people at the University Writing Center cheerily offering their services to help our students

resulting faculty resistance to "teaching writing" can be lessened by deconstructing the often ethereal and little-understood objectives of Writing Across the Curriculum (WAC), and repackaging them into a more useful model based on specific pedagogical criteria related to the various business disciplines. The resulting model can be used to show reluctant faculty that the educational rewards of writing can be had for very little additional teaching effort, and this effort is not about teaching the mechanics of writing, but rather the how and why of creating a discipline-specific document.

Following this introduction, Part II provides a brief history of the WAC movement, a practical way for faculty to think about WAC in terms of knowledge domains, and a discussion of one of the most commonly experienced obstacles to its adoption in business school classrooms, faculty resistance. Part III describes how, by viewing WAC through the lens of the well-established Bloom's taxonomy, faculty can more easily recognize the value of writing as a valuable pedagogical tool. In Part IV, a new model which combines the components of WAC with the knowledge and cognitive dimensions of Bloom's taxonomy is provided, which encourages faculty to focus on the knowledge components of writing for their specific disciplines, rather than the mechanics of writing. This model is then used to create and categorize specific writing assignments for a Legal Environment course to assess specific knowledge and cognitive components in Part V. Finally, Part VI provides a conclusion that summarizes how adoption of the model can allow faculty to embrace writing assignments in the classroom without becoming "writing teachers."

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complete their assignments, and realizing such services will not be necessary this semester.

II. WRITING ACROSS THE CURRICULUM

The practice of using writing assignments as a pedagogical learning tool in higher education dates from the early 1970's in England and the United States.[4] A principal reason for utilizing writing as a tool was the understanding that as academic disciplines became more diversified, writing instruction had to expand to meet the more specialized needs across the curriculum.[5] The resulting movement, about which much has been written,[6] became known as Writing Across the Curriculum ("WAC"), which, by 1988 had been adopted and solidly established at 38% of all U.S. colleges and universities.[7] Today, approximately 50% of U.S. schools have WAC programs in place, and another 11% have plans to establish the same.[8] Clearly WAC has become an accepted and important educational offering used to enrich the academic life of our students.

While WAC has been embraced in higher education, the term itself is somewhat imprecise. It generally refers to a university-wide initiative to assist faculty in incorporating writing assignments as an instructional tool in the classroom.[9] From a faculty perspective, when asked to develop and use writing assignments in the classroom, it is useful to deconstruct the broad concept of WAC into three distinct components, or pillars, based on the

[4] DAVID R. RUSSELL, WRITING IN THE ACADEMIC DISCIPLINES: A CURRICULAR HISTORY, 271 (2d ed. 2002).
[5] Chris Thaiss & Tara Porter, *The State of WAC/WID in 2010: Methods and Results of the U.S. Survey of International WAC/WID Mapping Project,* 61 College Composition and Communications 534, 535 (2010).
[6] *See generally* Russell, *supra* note 4; CHARLES BAZERMAN ET AL., REFERENCE GUIDE TO WRITING ACROSS THE CURRICULUM (2005); SUSAN H. MCLEOD, STRENGTHENING PROGRAMS FOR WRITING ACROSS THE CURRICULUM (1988).
[7] McLeod, *supra* note 6 at 103.
[8] Thaiss & Porter, *supra* note 5 at 540-541.
[9] *Id.* at 538.

learning goals to be achieved: Writing to Learn, Writing Process Pedagogy, and Writing in the Disciplines.[10]

The first pillar, Writing-to-Learn ("WTL") answers the instructor's question "what specific concepts do I want the student to master with this assignment." WTL is a foundational principle of WAC based on the belief that the physical and intellectual activity of writing something in one's own words is a superior pedagogical technique to rote memorization because it requires the student to internalize, evaluate, and critique material through the perspective placement of the student's personal frame of reference and understanding.[11] The second question a faculty member must ask before using a writing assignment is "What level of general writing proficiency will I require of the students?" This brings in the second pillar of WAC, Writing Process Pedagogy (WPP).[12] WPP represents modern composition theory and practices as taught by English Departments and Writing Centers, and from a faculty perspective is often thought of as "writing mechanics." In essence, WTL is directed at knowledge about course content, while WPP focuses on knowledge about the writing process.

The third pillar of WAC, and the one that is probably most helpful for faculty to consider when contemplating writing assignments, is Writing in the Disciplines ("WID"), which generally refers to understanding the types of writing that actually occur in different disciplinary areas, and accepting that what may be good writing in one discipline may not necessarily met expectations in another.[13] WID broadly encompasses the various efforts in individual disciplines toward improving writing skills, and usually implies that writing assignments that relate to discipline-specific material

[10] Anne Beaufort, *Freshman Writing, WAC, and Beyond: Is It Time for a Paradigm Shift?* Presentation made at Ninth Annual International Conference on WAC, University of Texas at Austin, Austin Texas, May 28, 2008.
[11] *See* Bazerman et al., *supra* note 6 at 57.
[12] Beaufort, *supra* note 10.
[13] *See* Bazerman, *supra* note 6 at 9-10.

and forms of communications are occurring in the classroom in some form.[14] While WTL focuses on content knowledge and WPP on process knowledge, WID contains both content and process components which faculty must take into consideration.

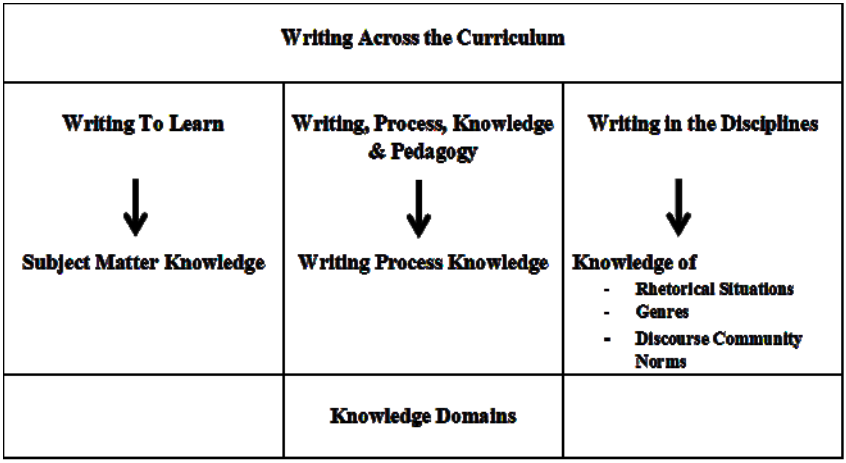
From a practical standpoint, these three pillars of WAC have been usefully mapped into discreet knowledge domains, all of which are necessary for proficient student writing.[15] The first, WTL, becomes *subject matter knowledge*. The second, WPP, becomes *writing process knowledge*. The third, WID, breaks into three subcategories: *knowledge of rhetorical situations, knowledge of genres, and knowledge of discourse community norms*.[16] The authors believe this mapping of WAC into knowledge domains, illustrated in Figure 1, infra, is the first step in encouraging business school faculty to fully embrace writing in the classroom.

[14] Thaiss & Porter, *supra* note 5, at 538.

[15] Beaufort, *supra* note 10. *See also* ANNE BEAUFORT, COLLEGE WRITING AND BEYOND: A NEW FRAMEWORK FOR UNIVERSITY WRITING INSTRUCTION, 18-19 (2007).

[16] Id. at 18-20. Beautfort describes knowledge of rhetorical situations as the consideration of the specific audience for and purpose of a particular writing, and the subsequent choice of appropriate rhetorical devices. Genres are those stylized forms of writing in a particular discipline, which could be anything from essays to journal articles to grant proposals. Knowledge of discourse community norms, according to Beaufort, is important because writing expertise is ultimately judged on its ability to engage a particular community of writers, who share a set of goals and values regarding appropriate roles and tasks of the writers, which are specific, if not unique, to the community.

Figure 1. Mapping WAC into Knowledge Domains



While the importance and effectiveness of an institutionalized WAC philosophy as a pedagogical tool has not diminished nor come into question, WAC programs themselves tend to be structured and utilized as isolated, self-contained resource centers to help students with the *mechanics* of their required writing, regardless of discipline, and separate and apart from actual classroom pedagogy.[17] There is little evidence of successful systematic implementations of WAC into the disciplines.[18] This lack of integration, arguably, stems from a lack of faculty enthusiasm, who equate WAC with teaching and assessing the very same writing mechanics, for which they feel either unqualified, uninspired, or both. One of the recognized weaknesses of

[17] Beaufort, *supra* note 15 at 17. *See also* Thaiss & Porter, *supra* note 5, at 547. The authors' university has had a WAC program in place since 1985, the elements of which have changed little in last 25 years. The establishment of a writing center for students and the appointment of director are the primary advancements, with little emphasis on WID. This experience reflects the trends at institutions throughout the United States.

[18] *Id.* at 15.

traditional WAC programs is the third pillar, WID, primarily because faculty in the disciplines are not, by specialty, writing teachers.[19] They are focused on imparting the factual, conceptual, and procedural knowledge of their disciplines, but seldom have the class time, expertise or motivation to teach the subconscious skill accumulated over years of practice of "how" to demonstrate this knowledge to peers in their discipline-specific discourse community.[20] In addition, the assessment process is burdensome,[21] and so, from a faculty perspective, the benefits of writing assignments often do not outweigh the burdens.

Mapping WAC into Beaufort's discrete knowledge domains is the first step in increasing faculty appreciation of the value of using writing assignments as a pedagogical tool. Next, by combining the knowledge domains with the widely known and utilized Bloom's Taxonomy,[22] a usable discipline-specific model can be developed to demonstrate to that bringing WAC principles into the classroom is a valuable pedagogical practice that does not focus on, nor even require, the teaching of writing mechanics.[23]

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[19] *See id*.

[20] *See id*. The authors are reminded of Justice Potter Stewart's definition of obscenity in *Jacobellis v. Ohio*, 378 U.S. 174 (1964): I shall not today attempt further to define the kinds of material I understand to be embraced within that shorthand description ["hard-core pornography"]; and perhaps I could never succeed in intelligibly doing so. But *I know it when I see it . . . [Emphasis added.]* The same could be said of good writing.

[21] Plutsky & Wilson, *supra* note 1 at 28.

[22] *See* Beaufort, *supra* note 15 at 25 (acknowledging that Bloom's hierarchy can be a useful tool for developing writing assignments, but noting the difficulty in assigning unique cognitive tasks to such assignments).

[23] It is important to emphasize that using writing as a pedagogical tool does not require faculty to teach writing mechanics, as this is a major impediment to the practice. *See, e.g.,* Plutsky & Wilson, *supra* note 1 at 33. (describing statements from faculty which include "I don't have time to teach writing. I don't know what to do," and "If I were a student, I'd be worried having me teach writing.")

III. VIEWING WAC THROUGH A BLOOM'S TAXONOMY LENS

When discussing WAC in terms of knowledge domains, it is helpful to examine it in conjunction with a firmly entrenched and generally accepted pedagogical concept: Bloom's Taxonomy of Educational Objectives.[24] This framework was intended to facilitate evaluation and assessment of student learning by categorizing necessary learning skills into discreet learning objectives. These objectives of the taxonomy are generally referred to as *Knowledge, Comprehension, Application, Analysis, Synthesis,* and *Evaluation*. The entire structure, including sub-categories, is shown in Figure 2, infra.

Figure 2. Structure of Bloom's Original Taxonomy[25]

1.0 Knowledge
- 1.10 Knowledge of specifics
  - 1.11 Knowledge of terminology
  - 1.12 Knowledge of specific facts
- 1.20 Knowledge of ways and means of dealing with specifics
  - 1.21 Knowledge of conventions
  - 1.22 Knowledge of trends and sequences
  - 1.23 Knowledge of classifications and categories
  - 1.24 Knowledge of criteria
  - 1.25 Knowledge of methodology
- 1.30 Knowledge of universals and abstractions in a field
  - 1.31 Knowledge of principles and generalizations

2.0 Comprehension

[24] BENJAMIN S. BLOOM ET AL., TAXONOMY OF EDUCATIONAL OBJECTIVES: THE CLASSIFICATION OF EDUCATIONAL GOALS (1956).

[25] David R. Krathwohl, *A Revision of Bloom's Taxonomy: an Overview*, 41 THEORY INTO PRACTICE 212, 213 (2002). Reprinted by permission of Taylor and Francis, publishers.

2.1 Translation
2.2 Interpretation
2.3 Extrapolation
3.0 Application
4.0 Analysis
4.1 Analysis of elements
4.2 Analysis of relationships
4.3 Analysis of organizational principles
5.0 Synthesis
5.1 Production of a unique communication
5.2 Production of a plan, or proposed set of operations
5.3 Derivation of a set of abstract relations
6.0 Evaluation
6.1 Evaluation in terms of internal evidence
6.2 Judgments in terms of external criteria

Subsequently, Bloom's original taxonomy has been expanded into a more sophisticated two dimensional model,[26] recognizing that useful learning outcomes require both the identification of subject matter content (knowledge) and a description of what to do with that content (cognition). The expanded model (Revised Taxonomy) refines Bloom's original learning objectives, which had indiscriminately combined the distinct knowledge and cognition components, into a more useful matrix that differentiates between the two. The Revised Taxonomy is shown in Figure 3, infra. The basic category headings are expanded to more fully capture the entire pedagogical spectrum. In addition, the revision is careful to employ nouns for identification of knowledge components and verbs to describe the associated cognitive processes, allowing for easier application by instructors. The full descriptions of each category are listed in Figures 4 and 5, infra.

[26] *Id.* at 214. *See generally* LORIN W. ANDERSON ET AL., A TAXONOMY FOR LEARNING, TEACHING AND ASSESSING: A REVISION OF BLOOM'S TAXONOMY OF EDUCATIONAL OBJECTIVES (2001).

Figure 3. The Revised Taxonomy[27]

	The Cognitive Process Dimension					
The Knowledge Dimension	1. Remember	2. Understand	3. Apply	4. Analyze	5 Evaluate	6. Create
A. Factual Knowledge						
B. Conceptual Knowledge						
C. Procedural Knowledge						
D. Metacognitive Knowledge						

Figure 4. Structure of the Knowledge Dimension of the Revised Taxonomy[28]

A. Factual Knowledge – The basic elements that students must know to be acquainted with a discipline or solve problems in it.
   Aa. Knowledge of terminology
   Ab. Knowledge of specific details and elements

B. Conceptual Knowledge – The interrelationships among the basic elements within a larger structure that enable them to function together.
   Ba. Knowledge of classifications and categories
   Bb. Knowledge of principles and generalizations
   Bc. Knowledge of theories, models, and structures

C. Procedural Knowledge – How to do something; methods of inquiry, and criteria for using skills, algorithms, techniques, and methods.
   Ca. Knowledge of subject – specific skills and algorithms

[27] *Id*. at 216.
[28] *Id*. at 214.

Cb. Knowledge of subject – specific techniques and methods
Cc. Knowledge of criteria for determining when to use appropriate procedures

D. Metacognitive Knowledge – Knowledge of cognition in general as well as awareness and knowledge of one's own cognition.
Da. Strategic knowledge
Db. Knowledge about cognitive tasks, including appropriate contextual and conditional knowledge
Dc. Self-Knowledge

Figure 5. Structure of the Cognitive Process[29]

1.0 Remember – Retrieving relevant knowledge from long-term memory.
- 1.1 Recognizing
- 1.2 Recalling

2.0 Understand – Determining the meaning of instructional messages, including oral, written, and graphic communication.
- 2.1 Interpreting
- 2.2 Exemplifying
- 2.3 Classifying
- 2.4 Summarizing
- 2.5 Inferring
- 2.6 Comparing
- 2.7 Explaining

3.0 Apply – Carrying out or using a procedure in a given situation.
- 3.1 Executing
- 3.2 Implementing

[29] *Id*. at 215.

4.0 Analyze – Breaking material into its constituent parts and detecting how the parts relate to one another and to an overall structure or purpose.
    4.1 Differentiating
    4.2 Organizing
    4.3 Attributing
5.0 Evaluating – Making judgments based on criteria and standards.
    5.1 Checking
    5.2 Critiquing
6.0 Create – Putting elements together to form a novel, coherent whole or make an original product.
    6.1 Generating
    6.2 Planning
    6.3 Producing

By adapting the Revised Taxonomy to specifically apply to writing assignments, a model can be developed that can be used to encourage faculty to embrace writing in the classroom. By demonstrating that various knowledge and cognitive dimensions regarding discipline-specific course content can be assessed using writing assignments, with very little time spent "teaching writing," more faculty may utilize them more often.

IV. EXTENDING THE TAXONOMY TO ENCOURAGE WRITING IN THE DISCIPLINES

By combining Beaufort's writing knowledge domains[30] and the Revised Taxonomy,[31] a refined pedagogical framework can be created that can be used to specifically develop and evaluate the educational effectiveness of a writing assignment for a particular discipline with respect to its knowledge and cognitive dimensions.

[30] Figure 1, *supra*.
[31] Figure 3, *supra*.

Such a model would provide pedagogical value to both students and faculty by demonstrating that mastery of discipline-specific writing is intertwined with mastery of content. Such a model, and the theory behind its construction, is proposed infra.

Krathwohl, in extending Bloom's taxonomy from one dimension to two, introduces the sixth component of the cognitive process as "*Create*," which is defined as 'putting elements together to form a novel coherent whole or make an original product.'[32] This causes some difficulty when applying the model to writing assignments. When writing, the cognitive process of *creating* is a given, and is used to demonstrate the mastery of one or more of the other five cognitive dimensions. Moreover, in order to demonstrate this mastery, the student must have a specific *knowledge* of how to demonstrate this mastery. Krathwohl's revised taxonomy fails to take into account the additional knowledge dimension needed by a student that is specifically related to the sixth cognitive dimension, "*Create*," when the task is to create a writing. This is where Beaufort's knowledge domains can be of use.

The Revised Taxonomy as it stands can be readily used to design and evaluate writing assignments by incorporating Beaufort's first two writing knowledge domains:[33] subject matter knowledge is mapped perfectly into the knowledge dimensions of Figure 4, supra; and writing process knowledge neatly overlays the first five cognitive dimensions listed in Figure 5, supra.[34] Beaufort's knowledge domains about writing in the disciplines, which comprise the third pillar of WAC (the trio of Rhetorical Situations, Genres, and Discourse Community Norms),[35] underpin the sixth

[32] Krathwohl, *supra* note 25 at 215.
[33] Figure 1, *supra*.
[34] There is a slight change in use with this overlay, as now the cognitive dimensions relate to the utilization of the knowledge of the mechanics of writing, as well as the discipline-related knowledge.
[35] *See* Beaufort, *supra* note 15.

cognitive dimension of the Revised Taxonomy, *Create*, and emphasize that the importance of these three areas of writing knowledge is critical to persuading faculty to embrace WAC in the classroom. Reluctant faculty need to be shown that using WID in the classroom is not the same as teaching the mechanics of writing. Including WID can be a rich and rewarding pedagogical tool because the knowledge of WID is tightly wound with the knowledge dimensions of the discipline itself. By extending the Revised Taxonomy in a way so as to incorporate WID knowledge components for writing assignments, the value of WAC in the classroom becomes more evident.

Knowledge about discipline-specific rhetorical situations, genres, and discourse community norms must be understood by students if they are to be able to create writings that their professors, and by extension members of the discipline community, would view as successful. As stated above, WAC programs often fall short with regard to the third pillar, writing-in-the-disciplines, because most business school faculty are not, and do not want to be writing teachers.[36] They are focused on imparting the knowledge of their disciplines, but seldom have the class time, expertise or desire to teach students how to demonstrate this knowledge in a manner appropriate to their discipline.[37] However, by filling in this small knowledge gap about discipline-related writing norms, which is often intimately entwined with the course content anyway, faculty can easily increase the number of students who can successfully demonstrate their mastery of content through writing assignments.[38]

[36] Plutsky & Wilson, *supra* note 1 at 28.
[37] *Id.*
[38] Writing mechanics may still present a problem for some students, but traditional writing centers can be leveraged for improvements in this area, and faculty do not need to spend class time on this knowledge domain.

Figure 6, infra, is an attempt to combine Beaufort's writing knowledge domains and the Revised Taxonomy, or rather, fold our third WAC pillar, WID knowledge, into the Revised Taxonomy's 6th cognitive dimension, "*Create*," and thereby create a model specifically for writing in a Legal Environment course.[39] Notice under this dimension the separate knowledge component based on Beaufort's WID knowledge domains.

Figure 6. An Extended Taxonomy for Writing in Legal Environment

	← WAC Pillar #2: Cognitive Process Knowledge →						
WAC Pillar #1: Subject Matter Knowledge	1. Remember	2. Understand	3. Apply	4. Analyze	5. Evaluate	6. Create: Legal Writing Applications	WAC Pillar #3 (WID) Requires Knowledge of: E. Rhetorical Situations F. Genres G. Discourse Community Norms
A. Factual Knowledge						Case Briefs Pleadings	
B. Conceptual Knowledge						Appellate Briefs Legal Argument	
C. Procedural Knowledge						Judicial Opinions	
D. Meta-cognitive Knowledge						Law Review Articles Critical Analysis	

[39] This model could easily be adapted to other business-related disciplines by identifying the WID rhetorical situations, genres, and discourse community norms associated with each. *See* note 47, *infra*.

Because of the technical specificity of the legal field, knowledge about how lawyers write within their discipline is of paramount importance in a Legal Environment course if the instructor is to use writing assignments as measures of academic achievement. Lawyers and judges create different types of writings, or genres, such as case briefs, pleadings, appellate briefs, and opinions, and each genre employs its own analytical structure and rhetorical techniques. Therefore, in order for a writing assignment to be a successful pedagogical tool in a Legal Environment course, the student must recognize these legal genres, and understand how they are structured and how they are used.

Notice that when applied to writing assignments, Krathwohl's 6th dimension, *Create*, becomes a de facto part of the assignment; one cannot complete a writing assignment without creating a writing. Figure 6 shows that knowledge components tied specifically to the discipline, E through G, should be taught in addition to the knowledge dimension components A through D. By teaching the students the parameters of how to structure their papers for a particular discipline, they will be more successful at translating their knowledge of the course content into a creative work that will demonstrate their level of mastery.

Specific types of legal writing that lawyers and legal scholars commonly use in their practice are shown in the last column of Figure 6. Each of these have expected structures, styles, and flow which, if deviated from, cause a jarring response in the lawyer-reader, and therefore would be viewed in the community as mediocre or poor examples. The student writer, then, must identify the parameters of the each genre, understand the purpose, and utilize the required structure and style in order to create a successful writing that will be graded positively by the instructor.[40]

[40] Business faculty are often are uncomfortable assessing student writing assignments because what is submitted is not what is expected. *See* Plutsky &

Finally, the reality of students with poor writing skills cannot be denied. Students still must learn and apply the mechanics involved in good writing, regardless of the discipline being studied. This knowledge about the general writing process, however, is where most WAC programs target their resources,[41] and students can generally access these resources outside of the classroom if properly motivated.

V. USING THE MODEL TO CREATE WRITING ASSIGNMENTS IN LEGAL ENVIRONMENT

To illustrate the utility of the extended taxonomy provided in Figure 6, supra (the "Model") a series of writing assignments for Legal Environment will be presented and categorized, based on their 1) subject-matter knowledge dimension; 2) cognitive process dimension (both in terms of the students' thought process and the expression of the thought process in writing); and 3) knowledge requirements of discipline-specific writing techniques. One topic of the course which lends itself to this exercise is the Dormant Commerce Clause. These writing assignments, in fitting with the goals of a Legal Environment course,[42] are relatively short assignments that could be used in various ways, from in-class assignments to minor "research" papers.

Wilson, *supra* note 1 at 36. This deviation from expected norms causes a poor first impression, followed by faculty doubt as to whether the work should nevertheless be judged harshly. By explaining the expected norms initially, this doubt can be removed in the assessment.

[41] Thaiss & Porter, *supra* note 5 at 552 (stating that 70% of WAC programs include participation of a writing center).

[42] *See* Carole J. Miller & Susan J. Crain*, Legal Environment v. Business Law Courses: A Distinction Without a Difference?*, 28 J. LEGAL STUD. EDUC. 149, 150 (2011) (stating the goal of a legal environment of business course is "help businesspersons recognize legal issues, prevent and resolve legal disputes, and function within the parameters of government regulations . . .").

The Commerce Clause of the United States Constitution states that Congress shall have the power "to regulate Commerce . . . among the several states."[43] This clause has been interpreted by the courts many times over the years, and for purposes of Legal Environment students, means that Congress has the authority to pass laws that are "substantially related to interstate commerce."[44] In a Legal Environment course, after understanding the limitations of Commerce Clause on the federal government, the next question typically asked is "What about the states?" Does the Commerce Clause place any limitations on states that want to pass laws that affect interstate commerce? The answer is yes, and the complex legal logic surrounding this issue, known as the Dormant Commerce Clause, is a good place to illustrate examples of writing assignments ("WA") that fit quite nicely into the Model.

WA #1:

Prepare a Case Brief for Granholm v. Heald, 544 U.S. 460 (2005).

This case is a Supreme Court opinion in which the Court decides whether laws passed by the states of Michigan and New York restricting the direct sale of wine by out-of-state wineries to in-state residents is a violation of the Dormant Commerce Clause. In order to successfully complete the assignment, on the knowledge dimension, the student must read the case to determine what happened (i.e., the factual knowledge). On the cognitive dimension, the student must put the facts together to *understand* the outcome of the case, placing the assignment in Box 2A of the Model.[45] In addition, the student must *create* a case brief, which means having knowledge of what a case brief is, what it is used for, and the structure it must take in order to be useful to lawyers. This is a separate knowledge component used specifically for the

[43] U.S. Const. art. III, § 8, cl. 3.
[44] *See U.S. v. Lopez*, 514 U.S. 549, 559 (1995).
[45] See Figure 7, infra.

creation of the writing, and is found in Column 6 of the Model. The simple acts of 1) identifying that students need to be taught the purpose and proper structure of a case brief, and 2) spending a few minutes disseminating this information, will enable many students to complete the assignment to the instructor's satisfaction. Otherwise, even if students understood the subject matter and could orally demonstrate the cognitive requirement, their creation of the writing could well be frustrating to the instructor's trained eye.

WA #2:

Write a short essay describing the legal reasoning used by the Supreme Court to strike down the restrictive wine delivery laws passed by Michigan and New York.

To complete this assignment, the student must again cognitively *understand* the facts presented in the opinion, but unlike WA #1, she must also understand the interrelationships among the facts, and parse the opinion to discover the logical progression used by the Court to reach its conclusion. The student is moving beyond factual knowledge into the realm of conceptual knowledge. This assignment, then, lands in Box 2B of the Model. However, for most students, the additional WID knowledge of the structure of judicial opinions, and how legal reasoning is employed by lawyers and judges, is necessary for creating an essay that demonstrates to the instructor an adequate understanding of the legal reasoning used. The Model attempts to convey to the instructor the importance of this additional WID knowledge component.

WA #3:

After the Court handed down its decision in Granholm v. Heald, assume that the state of Colorado, proud of its status as the "healthiest state in the country," passed a law prohibiting restaurants from "preparing, cooking, serving or selling any food

or beverage that contains any amount of trans-fat, unless the food was produced within the state of Colorado." The law was quickly challenged as unconstitutional under the Commerce Clause. As the judge in the case, using Granholm v. Heald as your guide, write an opinion explaining whether or not this law is constitutional.

The student in this instance must be able to *apply* the legal reasoning employed in one case to a second, hypothetical case. In addition, the student must use the process of legal argument in order to successfully construct her own parallel argument. This assignment therefore increases the level of complexity of the needed cognitive process to the "*apply*" dimension, and the level of knowledge to the "*procedural*" dimension, placing it in Box 3C of the Model. Once again, the Model indicates that a separate type of creative knowledge regarding the purpose, structure, and style of legal argument and judicial opinions will also be employed for most students to successfully complete this assignment, and an instructor who takes some time to impart this knowledge about writing in the legal field will receive a higher quality product from students.

WA #4:

The state of Alabama recently passed a law regulating out-of-state waste. The law imposed a special fee on any hazardous waste, such as chemicals and heavy metals, brought into the state to be put into a landfill. The legislature cited the danger to the citizens of the state of increasing the amount of hazardous waste in Alabama's landfills. No additional fee, however, was imposed on the disposal of hazardous waste generated within the state. Explain whether or not this law is constitutional.

This assignment[46] is similar to WA #3, except that the Dormant Commerce Clause is not mentioned. Therefore, to successfully complete this assignment, the student must *analyze* the situation and choose the appropriate legal precedent that has been discussed in class, which in this case would be Granholm v. Heald. The student must then use her *procedural knowledge* of legal analysis, similar to the preceding assignment, to create the appropriate written response. Because of the necessity to use the higher-order cognitive process, *analyze*, in order to identify that this is a Dormant Commerce Clause issue, this assignment is placed in box 4C in the Model.

WA #5:

Critique the Supreme Court's decision in Granholm v. Heald. Given the facts of the case, do you believe the Court properly applied the Dormant Commerce Clause test that it has established in previous cases? What facts in this case would you change in order to reach a different conclusion?

Here the student is being asked to evaluate the Supreme Court's process of reaching a legal conclusion. Basically, the student must critically analyze and *evaluate* the opinion and decide whether the legal reasoning used is fair and honest. Because the case was decided 5-4, this is a good place to require the students to read the dissenting opinion, which, by definition, reaches the opposite conclusion as to the constitutionality of the restrictive wine delivery laws. This allows the student to see both sides of the argument, and understand how the process of accentuating certain facts and ignoring others can lead to different legal conclusions in the same situation. This assignment falls in Box 5C of the Model, requiring the student to *evaluate* the arguments on both sides using her *procedural knowledge* of legal argument. It also requires the

[46] This assignment is based on the facts from *Chemical Waste Management, Inc. v. Hunt*, 504 U.S. 334 (1992).

student once again to use her knowledge regarding the purpose, structure, and style of legal argument and judicial opinions to create her paper.

WA #6:

The judicial interpretation of the Dormant Commerce Clause attempts to balance states' rights in promoting the general welfare of its citizens with the authority granted to Congress under the Commerce Clause to regulate interstate commerce. Does the legal test utilized by the Supreme Court in Granholm v. Heald strike the proper balance? How would you change the test, if given the opportunity? What would be the impact on our society?

This assignment is more like a traditional persuasive essay, where the student can rely on her writing process knowledge. From a legal discipline perspective, we are asking the student to draw on her own experience and beliefs to come to a conclusion, and then persuade the reader to agree with that conclusion. This is the type of writing often found in law review articles, where the author is attempting to improve the state of the law with his or her own ideas, and our student author would benefit from understanding that connection. This assignment falls into Box 5D of the Model, where the student is *evaluating* a legal argument using her own *metacognitive knowledge*. This is the most complex assignment we have described, and the student would probably need more time in this instance to read, reflect and write than in the previous examples. Figure 7, infra, illustrates how the six writing assignments described above fit into the Model.

Figure 7. Using the Extended Taxonomy to Categorize Writing Assignments

	← WAC Pillar #2: Cognitive Process Knowledge →						
WAC Pillar #1: Subject Matter Knowledge	1. Remember	2. Understand	3. Apply	4. Analyze	5. Evaluate	6. Create: Legal Writing Applications	WAC Pillar #3 (WID) Requires Knowledge of: E. Rhetorical Situations F. Genres G. Discourse Community Norms
A. Factual Knowledge		**WA #1**				Case Briefs Pleadings	
B. Conceptual Knowledge		**WA #2**				Appellate Briefs Legal Argument	
C. Procedural Knowledge			**WA #3**	**WA #4**	**WA #5**	Judicial Opinions	
D. Meta-cognitive Knowledge					**WA #6**	Law Review Articles Critical Analysis	

While the Model has been applied to a Legal Environment course, we believe it could successfully be applied to other disciplines within business schools.[47] The keys are to identify the appropriate genres of a given discipline, and to recognize that specific knowledge about each discipline-specific writing application must be imparted to our students in order for them to be successful in

[47] *E.g.*, in accounting, discipline-specific writings include operational audit analyses and reports, capital expenditure analyses and reports, and other more specialized project-related reports.

their writing assignments. While this sounds obvious, the authors believe it is an often overlooked detail.

VI. CONCLUSION

Using the WAC philosophy of bringing writing assignments into business courses can offer significant educational value, but its application is often minimized due to faculty resistance. This resistance often flows from the belief that instructors have neither the time nor expertise to teach writing mechanics, and are also insecure about assessing student's written work. This insecurity can be overcome if faculty can be explicitly shown that WAC can be translated into discipline-specific knowledge and cognitive domains, and that writing assignments based on these domains, related to specific business disciplines, can be pedagogically effective with little additional time spent in the classroom. The model presented above does this, and emphasizes that if faculty impart to students knowledge about why and how discipline-specific writings are structured and used, students can excel at creating writings that demonstrate their mastery of the various knowledge and cognitive dimensions which are being taught. Applying the model to create a variety of writing assignments applicable to the same topic from a legal environment course demonstrates its usefulness, and the flexibility of the model allows it to be adapted to other business school disciplines.

CHE AND KORDA: A CONVOLUTED AND CONTENTIOUS CUBAN COPYRIGHT CASE

by

Michael E. Jones *

Before the 1958 Cuban revolution led by Fidel Castro, the Cuban born photographer Alberto Korda, born Alberto Diaz Gutierrez, was a well-known commercial artist.[1] Korda lived a modern, western lifestyle in the most exclusive neighborhood of Havana.[2] He loved exotic cars and photographing beautiful women.[3] His personal photographs were likened to those of the acclaimed American photographer Richard Avedon.[4] Korda was the fashion photographer for the *Havana Weekly*.[5] In 1959, shortly after the armed forces of Fidel and Raul Castro, Camilo Cienfuegos, and Ernesto "Che" Guevara successfully forced President Fulgenico Batista into political exile, Korda rejected his old lifestyle, joined the revolution and became a documentary journalist.[6]

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[1] Jon Thurber, Alberto Korda: Took Famous "Che" Picture, L.A. TIMES, May 26, 2001 *available at* http://www.articles.L.A. Times.com/2001/May26.

[2] *Id.*

[3] *Id.*

[4] *Id.*

[5] *Id.*

[6] CHRISTOPHER LOVING & JAMIE SARUSKY, CUBA BY KORDA (2006).

Immediately after the revolution began, the new government of Cuba started a newspaper, the *Revolución.* Korda joined the paper as a freelance photographer.[7] In April of 1959, he was sent to document Fidel Castro's visit to Washington, D.C.[8] One of his portrait photographs for the paper was an image of Fidel Castro standing by the Lincoln Memorial.[9] He and Castro became friends, and for 10 years he served as Castro's personal photographer.[10] Among his signature portraitures is a picture of Ernest Hemingway beside the Cuban leader on a golf course.[11]

On March 4, 1960, Korda was working on assignment for the *Revolución* covering the memorial service for 136 who were killed after a French freighter carrying munitions exploded in Havana Harbor.[12] Fidel Castro was the principal speaker for the service.[13] Unexpectedly, Che Guevara suddenly appeared near the front of the stage.[14] Something about Che's expression caught Korda's eye, according to an interview he gave.[15] Using his Leica camera, Korda captured Che's likeness in two frames.[16] He did not like one of the images he had taken because someone had stepped into the frame.[17]

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[7] BRANDI LEIGH, ALBERTO KORDA: THE ART HISTORY OF ARCHIVE-PHOTOGRAPHY *available at* www.arthistory/photograph/albertokorda.
[8] *Id.*
[9] *Id.*
[10] *Id.*
[11] *Id.*
[12] *Id.*
[13] *Id.*
[14] *Id.*
[15] Korda, Alberto, audio interview by Maria Carrin for Democracy Now!, May 29, 2001, *available at* for listening at http://www.democracynow.org/2001/5/29/an_interview_with_the_late_great.
[16] *Id.*
[17] *Id.*

Korda followed his established practice of developing his own negatives and then presenting the images to the editor of the paper.[18] Neither image of Che was selected for publication.[19] Instead, a photograph of Fidel Castro was chosen for the front-page article illustrating the event that ran the following day.[20]

The newspaper kept the picture of Che on file.[21] Korda also kept the negative and hung the image he liked in his home.[22] On April 16, 1961 the *Revolución* used the photo as part of an announcement that "Dr. Ernesto 'Che' Guevara" would be speaking at an upcoming conference.[23] This was the first publication of the Che image.[24] Ironically, the conference was postponed until April 28, 1961 because of the ill-fated Bay of Pigs invasion.[25] The photo was republished on that date.[26]

By 1963 Che began to have serious disagreements with Fidel Castro over political and economic matters.[27] Guevara had been appointed Minister for Industries and President of the Central Bank; yet, two years later Che left Cuba for the Congo and later

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[18] *See supra* note 7.
[19] *Id.*
[20] *Id.*
[21] *See supra* note 15.
[22] *Id.*
[23] *See supra* note 7.
[24] *Id.*
[25] *Id.*
[26] *Id.*
[27] Batista, Castro and Che Guevara *available at* http://www.fsmitha.com/h2/ch24x.html. This may be a minority view, however. Che's farewell letter to Fidel Castro: "I am also proud of having followed you without hesitation, of having identified with your way of thinking and of seeing and appraising dangers and principles" is frequently cited as an indication Che left Cuba on good terms, as reported in a television interview with Fidel Castro by Gianni Mina, Italian journalist, June 1987, and later published in book form as: GIANNI MINA, AN ENCOUNTER WITH FIDEL (1996).

Bolivia.[28] In 1967, at the age of 39, the Argentinian born Guevara was captured by CIA-trained Bolivian forces and executed as he was attempting to foment revolution throughout South and Central America.[29]

By then, Korda's historic photograph of Che with his long, dark hair flowing freely beneath his star affixed beret, eyes pensively transfixed into the distance had become "the most famous photograph in the world." [30] The author of *The Fall of Che Guevara* refers to it as "one of the greatest images of all time." [31]

I. WHO CAN CLAIM COPYRIGHT OVER THE CHE PHOTOGRAPH?

Under Cuban copyright law the author of a work including a photograph is "the person who has created a work."[32] Barring

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[28] *See supra* note 7.

[29] William Stodden, Chronology of The Economic Ministry of Comrade Guevara after the Revolution in Cuba, *at* Marxists.or/archive/Guevara/biography/econ-ministry.htm. *See also:* PACO IGNACIA TAIBO II, ALSO KNOWN AS CHE (1997) translated by Martin Roberts.

[30] Michael Casey, The Brand That Sprang from a Frozen Revolutionary Moment, THE AUSTRALIAN, Jan. 01, 2009, *available at* http://theaustralian.com.au/arts/the-brand-that-sprand…It is nearly impossible to verify whether Korda's picture of Che is in fact the most famous image in the world. This statement is repeated as fact. There is little dispute the image speaks to many people and has come to mean many different things both inside and outside Cuba. The image conjures up issues of redistribution of wealth, poverty ownership, freedom to protest, culture, and labor practices. For those who have an interest in the cultural aspects of this artistic image *see* Ariana Hernandez-Reguant, Copyright Che: Art and Authorship under Cuban Late Socialism, PUBLIC CULTURE, Vol. 16, No. 1, Issue 42, Winter 2004.

[31] HENRY BUTTERFIELD RYAN, THE FALL OF CHE GUEVARA: A STORY OF SOLDIERS, SPIES AND DIPLOMATS (1999).

[32] Copyright Law, Graceta Official de la Republica de Cuba, No. 49, art. 11, 30 de diciembre de 1977 (Cuba) translated in Copyright Laws & Treaties of the World (U.N. Educ., Scientific & Cultural Org.et al eds (2000).

evidence to the contrary, "the person whose name or pseudonym the work has been publicly made known shall be considered the author." [33] Furthermore, Cuba has a condition for claiming ownership, whereby the copyright of a photograph is only recognized so long it follows established government regulations.[34]

In 1967, an Italian publisher by the name of Giangiacomo Feltrinelli traveled to Cuba seeking a picture of Che.[35] Feltrinelli came from a wealthy family and gained notoriety for publishing the first western translation of *Dr. Zhivago* after he had smuggled it out of Russia.[36] In Cuba – and Havana to be specific – he located Korda and the photo of Che he was looking for.[37] Korda gave him two copies of the same image that had been published by the *Revolución*.[38] Korda later explained in an interview because Feltrinelli was a friend of the revolutionary movement he could have it for free.[39]

Before arriving in Cuba, Feltrinelli was in Bolivia where he acquired the rights to publish Che's *Bolivian Diary.*[40] Korda's image of Che was to become the cover image for the soon to be published diary of Che's experiences in Bolivia.[41]

Upon returning to Italy, Feltrinelli decided to create a poster using the image to create public awareness of Che's precarious situation

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[33] *Id*.
[34] *Id.*
[35] MICHAEL CASEY, CHE'S AFTERLIFE: THE LEGACY OF AN IMAGE 114 (2009).
[36] *Id.*
[37] *Id.*
[38] *Id*.
[39] *Id.*
[40] *Id*.
[41] *Id.*

in Bolivia.[42] He printed 1000 copies and they all sold quickly.[43] Feltrinelli made a few stylistic changes and enlarged the image, but otherwise it was all Korda's likeness of Che on the poster.[44] Feltrinelli never sought permission or authorization from Korda and, in fact, he added his own name to the poster as author and copyright owner![45]

Around the same time, late summer of 1967, the French magazine, *Paris Match*, featured Korda's image of Che under the name *Guerrillero Heroico* or *Heroic Guerilla*, as part of an article about the revolutionary leader.[46] The magazine did not identify the author of the photograph, although it did refer to it as "the official photograph of Che Guevara."[47]

Che was dead before the year was over.[48] During the summer of 1968 students were rioting around the world including on the streets of Paris and college campus of Berkeley. By now Korda's image of Che had been transformed into an international, idealistic and ideological symbol for left-leaning revolutionary movements everywhere.

Feltrinelli continued to print his posters.[49] He sold more than 1 million copies, and, he used the same Che image he received from Korda for the cover of the book, *Bolivian Diary*.[50]

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[42] Trisha Ziff, *Introduction/Korda's Che Moves Out Into The World*, FROM REVOLUTION AND COMMERCE: THE LEGACY OF KORDA'S PORTRAIT OF CHE, Jan. 2005 at http://www.cmp.ucr.edu/exhibitions/che/essay_002.htm.
[43] *Id.*
[44] *Id.*
[45] *Id.*
[46] *Id.*
[47] *Id.*
[48] *Id.*
[49] *See supra* note 7.
[50] *Id.*

In 1967, the Irish artist Jim Fitzpatrick began producing his own sting of red-on-black posters using, once again, Korda's photo of Che.[51] Various theories abound about Fitzpatrick discovered the picture; however, it was not from Feltrinellli. The best evidence is he somehow acquired it from the French philosopher Jean-Paul Sartre, who was present when Korda took Che's photograph at the funeral service. Sartre had also visited Korda around that same time and maybe Korda gave him a copy, too.[52]

Fitzpatrick did not know the author of the image.[53] His interest in creating his poster was to share his personal admiration for the revolutionary change espoused by Castro's comrade in arms.[54] The poster Fitzpatrick created is the very recognizable and classic image of the longhaired Che wearing a beret that is most well known by the public even today. Fitzpatrick slightly tweaked the image by raising Che's eyes and adding a reversed "F" to his shoulder, but not enough of a change or transformation to fall within any classic definition of "fair use."[55]

Referring back to 1960 when Korda took the photograph and 1961 when it was first published, he was "working" for two entities: personal photographer for Fidel Castro and documentary photographer for the *Revolución.*[56] The intriguing initial legal copyright question is whether the photograph was made as part of a "work for hire" or a "special order or commission" or at the personal request of Fidel Castro? He was sent to cover the memorial service by the newspaper, not Castro, even though the photojournalism assignment was Castro. Thus, the issue lies between the newspaper and Korda regarding who owns the

[51] *Id.*
[52] *Id.*
[53] *Id.*
[54] *Id.*
[55] *See supra* note 35.
[56] *See supra* note 6.

copyright. Cuba's law of "work for hire" or "commissioned" work was not clear at the time Korda took the photo. There was not a written agreement reserving or assigning the copyright to one party or the other.[57]

A copyright can be recognized in an author even though the work may have been created when the photographer was working for a government agency.[58] Works of art created in the course of employment by any state organization, institution, entity or undertaking, social or people's organization are subject to regulations regarding the exercise of these rights, issued by the Council of Ministers.[59]

While Cuba's "work for hire" law at the time is not clear, what would happen were the same issue to arise under U.S. federal copyright law? Title 17 states that in the case of a "work made for hire, the employer or other person for whom the work was prepared is considered the author for purposes of this title, and, unless, the parties have expressly agreed otherwise in a written instrument signed by them, owns all of the rights compromised by the copyright." A recent law review article regarding Korda surmises he would have retained the copyright over the Che image under the work for hire factors articulated under *Community for Creative Non-Violence v. Reid,* 490 U.S 730, 750-51 (1989).[60] The argument is the newspaper he was free lancing for did not directly order the photo of Che not control the theme, subject matter, composition or any aspect of the final work.[61] However, and this is huge however, even were this all true, Korda's copyright interest

[57] *Id.*
[58] Sarah Levy*, Comment and Casenote, A Copyright Revolution: Protecting The Famous Photography of Che Guevara,* 13 LAW & BUS. REV. AM. 687, 692 (2007).
[59] *Id.* Cuban Law, Law No. 49, art. 19.
[60] *Id.*
[61] Id.

would have expired in 1971, or ten years after the initial publication in the newspaper under Cuban law.[62]

In the early 1960s Fidel Castro began nationalizing privately owned businesses.[63] All Cubans were expected to work collectively for the benefit of the revolution.[64] Jobs were defined and classified and it was illegal to work outside the centrally planned listing of job categories.[65] In a way, Korda could not lawfully work as a private photographer so everything he photographed and published belonged to the government.

In 1967, all intellectual property laws were repudiated as capitalist tools contrary to the tenets of socialism.[66] For years Cuban artists were denied opportunities to recognize and realize the value in their works until years later when Castro acknowledged the commercial benefits to intellectual property. This change was prompted by two simultaneous events.[67] The first was the global success of the revived Buena Vista Social Club music in the mid to late 1990s and the second was the "branding" of Che Guevara's image.[68] His likeness was now found on pop art posters, condoms, baseball caps, T-shirts and coffee mugs. The mythical image of Che espousing sacrifice, collectivism, and armed revolt against the capitalism and western ideology had now been converted into a trendy marketing global symbol. Castro began to embrace the same international intellectual property system years earlier he had

[62] Garcia, Caste Clanos, Susel, personal interview by Michael E. Jones with Director of ADAVIS, an artists' rights society located in Havana, Cuba, about the history of Cuba and the rights of artists. Interview took place on Jan. 4, 2013.
[63] WAYNE S. SMITH, PORTRAIT OF CUBA 91 (1991).
[64] *See supra* note 62.
[65] *Id.*
[66] *See supra* note 35.
[67] *Id.* at 309.
[68] *Id.* at 308.

assailed, and started to allow the recognition and exercise of copyrights previously barred.

II. COPYRIGHT DURATION UNDER CUBAN LAW: THEN AND NOW

As previously mentioned, the term for copyright of photographs in 1961 was ten years from the first publication date. Adding the statutory 10-year period to when the *Revolución* printed the Che image, by 1972 the copyright to Korda's photo would have fallen into the public domain. Once the term expired then the image became available for anyone to use, and would not be subject to infringement claims.

Examining U.S. copyright rules and standards for works published between 1923 and 1963, under the assumption that any copyright originally created was not renewed in the 28th year of its first publication, the copyright would have expired no later than 1988.[69] During this time period neither Korda nor the newspaper nor any license known to this author ever sought U.S. statutory copyright protection recognition and protection. Therefore, having fallen into the public domain the Che image could be used in the U.S. without obtaining permission from the heirs of Korda or agents of the Cuban newspaper.

Another wrinkle to consider is that the Uruguay Round Agreement Act (URAA) restored copyrights in the U.S. for certain foreign works that as of 1966 had fallen into the public domain for failing

[69] TAD CRAWFORD, LEGAL GUIDE FOR THE VISUAL ARTIST 6-7 (2010) and *see further* Copyright Term and the Public Domain in the United States, http://copyright.cornell.edu/resources/publicdomain.cfm, last visited 2/14/13 based on a chart first published in Peter B. Hirtle, "Recent Changes to the Copyright Law: Copyright Law: Copyright Term Extension, "*Archival Outlook*, Jan/Feb 1999, updated as of Jan. 1, 2012.

to comply with the formalities of copyright registration.[70] This restoration only applied to those works including photographs that were still in copyright in the place of first publication, Cuba, and the country in question was a member of the Berne Convention as of January 1, 1966.[71] The URAA is of no assistance to Korda in the U.S. in the event there was an attempt to claim copyright protection in the U.S. over the original photograph. Cuba was no longer a member of the Berne Convention on the effective date of the URAA. However, had the photograph been published before 1978 in Cuba, published in compliance with all U.S. formalities required, e.g. notice and renewal, and Cuba had been a member of Berne, then the copyright period in the U.S. would have been 95 years after its first publication date of 1961.[72]

In 1994, Cuba issued Decree Law No. 156.[73] It extended the term for copyright protection for works to 25 years from date of first publication.[74] Adding 25 years to the time the newspaper first published the Che image, assuming it had a retroactive component reinstating the copyright to an image already in the public domain as of 1971, and then copyright protection would extend to 1986.

Under Article 48 of the Cuban Copyright Act, the Council of Ministers in Cuba is granted the extraordinary authority to declare any copyrighted work the property of the government once the original copyright period has expired.[75] This policy is an extension of Article 3 of the Act that holds "the protection of copyright established by this Law is subordinated to the superior interest

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[70] John Tehranian, *The Emperor Has No Copyright: Registration, Cultural Hierarch and the Myth of American Copyright Militancy,* 24 Berkely Tech. L. J. 1399 at 1433 (2009). Copyright Extension Act of 1909 section 304.
[71] *Id.*
[72] *See supra* note 69.
[73] *See supra* note 58 at fn 26 and *supra* note 70.
[74] *Id.* at fn 108.
[75] *See supra* note 58 at fn 45.

imposed by the social necessity for the most ample diffusion of science, technology, education and culture in general.[76] The exercise of the rights recognized by this Law must not affect these social and cultural interests." [77]Socialist law is the supreme law so unless the Cuban government stated otherwise by the end of 1971 any private right Korda might have had over the Che image had expired and now belonged to the state.

III. CUBA JOINS THE BERNE CONVENTION

On February 20, 1997 the Republic of Cuba officially rejoined the International Union for the Protection of Literary and Artistic Works ("Berne Convention" or "Convention").[78] Cuba's accession meant that authors and artists would have legal protection independent to the inherent copyrights granted by the Cuban government.[79] The requirement of a visible copyright notice – the standard name of the author, copyright symbol and date – was eliminated.[80] Korda had signed and dated some of his early photographs.[81] The Convention provided a minimum copyright duration of the life of the author plus 50 years, except the term for photographs was limited to 25 years from first use, although states are free to provide longer terms.[82] Cuba also approved the World Trade Organization's rules governing intellectual property.[83]

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[76] *Id*. at 695.
[77] *Id.*
[78] Berne Notification No. 17, Berne Convention for the Protection of Literary and Artistic Works Accession by the Republic of Cuba, http://www.wipo.int/treaties/en/notifications/berne/treaty-berne-17…
[79] *See supra* note 35 at 695.
[80] MARY LAFRANCE, COPYRIGHT LAW IN A NUTSHELL 96 (2008).
[81] Korda, Dante email correspondence by Michael E. Jones, Feb. 14, 2013.
[82] *See supra* note 58 at fn 26.
[83] *See* on April 20, 1995: World Trade Organization membership list: http://www.wto.org/english.thewto-e/whatis-e/tif-e/org6-.htm.

The United States, United Kingdom and other European Union members now grant photographs a copyright term for 70 years from when the author dies.[84] Cuba still maintains the 25 years from first publication term for photographs.[85]

The Convention gives authors *national treatment*, meaning signatory countries automatically issue the same copyright protection as is extended to its own citizens.[86] The right to proclaim or even disclaim authorship and the right to protect the reputation of the photograph by objecting to distortions was now available for Cuban artists throughout the world.[87] Collectively, these rights are the *moral rights* of attribution, integrity, disclosure, and right to resale royalties, and are independent of the economic monopoly rights associated with copyrights.[88] (Note that the U.S. did not fully embrace the parameters of moral right found in many other countries when it acceded to the Berne Convention in 1988. Under the Visual Artists Rights Act or VARA of 1990, moral rights are extended to some works of art, but generally do not protect photographs created prior to June 1, 1991.) Cuban artists now were permitted to claim ownership and collect royalties from foreign use of works of art.

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[84] Information of the UK copyright period for photographs is available at http://copyrightservice.co.uk/copyright/p01_uk_coyright_law; and information on the US copyright period for photographs is available at http://www.cpyright.cornell.edu/resources/publicdomain.cfm; information on the Berne Convention copyright period for photographs is available at http://www.wipo.int/treaties/en/ip/berne/trtdocs_wo01.html. *See also supra* note 80 at 115-35 for a general discussion of Term of Protection under Berne and US copyright laws.

[85] *See supra* note 65.

[86] THE RT. HON SIR ROBIN JACOB, DANIEL ALEXANDER AND LINDSAY LANE, A GUIDEBOOK TO INTELLECTUAL PROPERTY 212-20 (2004).

[87] *Id.*

[88] DAN HUNTER, INTELLECTUAL PROPERTY 54 (2012).

Forty years after Korda's historic photograph, he utilized a foreign court to exercise these newly acquired global rights. The London based Cuba Solidarity Campaign acting on his behalf, sued two companies involved in making an advertisement for Smirnoff Vodka that incorporated the Che image in the company's marketing campaign. Korda told the press he was upset on the use of the image because it was a "slur on his (Che) name and memory."[89] Some commentators have reported that the London High Court affirmed Korda's copyright interest in the photo.[90] This may be an overly generous assessment because the court merely affirmed the parties out of court settlement of $75,000.

In what may be another revelation to those who have applauded Korda's successful legal objection to what he viewed as a prejudicial use of the photo, moral rights do not apply to photographs made for newspaper reporting.[91] Photographs made in the course of one's employment also do not qualify for moral rights.[92] The monetary settlement may have had less to do with the application of any legal principals, and more with Smirnoff's desire to protect its own business image and reputation. In 2001, a few months after the case was resolved, Korda died in Paris extinguishing any moral rights he might have had in the photograph.[93]

IV. KORDA'S CHILDREN AND COPYRIGHT

Korda died leaving five children from three separate relationships.[94] The children in some manner have all disputed copyright ownership or use in his photographs.[95]

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[89] *See supra* note 35 at 313.
[90] *Id.*
[91] *See supra* note 86.
[92] *Id.*
[93] *See supra* note 35 at 313.
[94] *See supra* note 81.

Inheritance laws in Cuba dictate that any heir who leaves Cuba and establishes residency in another country may lose all property ownerships rights.[96] The Constitution expressly states the right to inherit personal property, including intellectual property, is lost once a child or heir vacates Cuba.[97] In those circumstances when a property interest is inherited and the beneficiary then leaves the country, the Council of Ministers may declare the artwork and copyright as *patrimonial* property of the Republic of Cuba.[98] According to the director of the leading artists' rights group in Cuba, ADAVIS, patrimonial art is visual fine art that best embodies the spirit and history of the state created by her leading master artists.[99] The oil paintings of the esteemed Wilfedo Lam, Amelia Pelaez and Rene Portocarrero qualify as patrimonial art; therefore, cannot be sold or transferred outside of Cuba without government permission.[100] Korda's photographs would qualify as patrimonial art.

At Korda's death only two of his children lived on the island, Dante Korda and Diana Diaz, his oldest daughter.[101] Those two were the only two heirs who qualified to inherit his personal property: negatives, contact sheets, physical photographs already printed and any copyrights thereto. Korda written will named Diana as his "sole and universal heir."[102] Some of the children and

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[95] *Id.* and *supra* note 35 at 320.
[96] DEBORAH EVENSON, REVOLUTION IN BALANCE: LAW AND SOCIETY IN CONTEMPORARY CUBA 22 (1994).
[97] *Id.*
[98] *Id.*
[99] *See supra* 62.
[100] *Id.*
[101] *See supra* note 81.
[102] See supra note 35 at 314-19. In addition, Dante Korda supplied Michael E. Jones a copy of what is purported to be Alberto Korda's last will designating Diana Diaz as lawful heir. He contests the circumstances regarding the signing of the will.

even a non-family member, an alleged mistress, have fiercely disputed the validity of the will.[103]

Korda's son, Dante, challenged the government's recognition of Diana as the sole heir that granted her the copyright interests in his photographs including the original picture of Che.[104] Diana and the Cuban government upset Dante because of their joint global mass marketing blitz of the Che image.[105] Together they geographically license the Che image abroad and frequently sue those who have exploited the image without permission or license.[106]

For example, they successfully sued Reporters Without Borders (Reporters Sans Fronteires) to stop them from displaying the Che photo on posters.[107] This Paris based human rights activist organization was seeking to bring attention to Cuba's imprisonment of scores of dissident reporters accused of spying. Che's face was superimposed over a baton-waiving policeman with the words "Welcome to Cuba, the world's largest jail for journalists."[108] This 2003 lawsuit would have failed had Cuba not resurrected its own copyright laws and rejoined the Berne Convention. Diana and her government now sell Che themed merchandise even in the U.S. through a license issued to Fashion Victim, and on its website, "The CheStore.com."[109]

According to Dante, his father never sought to copyright the image.[110] His father always thought of the photograph as belonging to the public.[111] What was once the symbol of a communist

[103] *Id.*
[104] *Id* and *see supra* note 81.
[105] *Id.*
[106] *Id.*
[107] *See supra* note 35 at 320.
[108] *Id.*
[109] *Id.* at 323-24.
[110] *Id.*
[111] *Id.*

revolutionary movement has been morphed into a commercial brand based on a photograph frozen in time. Dante eventually vacated Cuba and made south Florida his new home, where he sells his own personal collection of photographs taken by his father, including the Che picture on eBay.[112] Dante's move solidified Diana's legal interest in Korda's personal and intellectual property under Cuban law. Diana was also granted exclusive access to Korda's negatives the Cuban government "confiscated" in 1968.[113]

In 1999 Korda granted global freedom to exploit a collection of signed and unsigned prints and negatives to his youngest daughter, Norka.[114] In addition, a former business associate, Patrick Magaud, succeeded in registering a trademark over the Che photo image in the European Union that granted Magaud rights to collect royalties.[115] Korda had given him a 10-year license that expired in 2005.[116]

Even the Che Guevara family itself has joined the controversy. His widow, Aleida March, and a daughter established the Che Guevara Studies Center in Cuba, in part to prevent his image from further unapproved commercial use.[117] The Center's website does not reveal any ongoing activities or litigation.

More than forty years after the Irish artist Jim Fitzpatrick first published his original Che poster he succeeded in gaining copyright protection for a republished version of the original poster

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[112] *Id.*
[113] *See supra* note 35 at 327.
[114] *Id.* at 318.
[115] *Id.* at 319.
[116] *Id.* at 312.
[117] Che's family plans to fight use of famed photo, Aug. 29, 2005, at http://www.newsgroups.derkeiler.com/archive/soc/soc.culture.cuba2005.

in Europe.[118] In 2008, Fitzpatrick then assigned his interest in the copyright to the William Soler Pediatric Cardiology Hospital in Havana.[119] The original print he physically gave to Aleida March, Che's widow.[120] The Che poster generally available at poster websites in the U.S. typically sell Fitzpatrick's republished image of Che.

V. SUMMARY

The legacy of the copyright over the original photograph of Che Guevara by Alberto Korda remains convoluted, contentious and complicated even to this day. Undoubtedly, any copyright interest Korda, a freelancing photographer for a government controlled and owned newspaper, may have had in the image expired years ago.

However, the Cuban government restored the copyright in Korda. After rejoining the Berne Convention in 1997, Korda was encouraged to pursue economic rights in an English court, and he did so successfully. Shortly thereafter, he died, and tensions arose among his children over who is the rightful guardian over Korda's photographs and copyrights. Diana Diaz, the child most loyal to the Cuban regime and the purported sole personal property beneficiary named in Korda's will, was granted exclusive rights in the Che photograph. She and the Cuban government jointly have embarked on a global marketing campaign to capitalize on Korda's photograph.

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[118] *Che Guevvara, Jim Fitzpatrick and the making of an icon,* HISTORY IRELAND, Jul/Aug 2008, Vol 16-Issue 4, at http://www.historyireland.xon/volumes/volumes16/issue-4/features.

[119] *Id.*
[120] *Id.*

- END ARTICLES -

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