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Inside

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Message from the Chair

To the Members of the Corporate Counsel Section:

It is my pleasure to serve as your Chair of the Corporate Counsel Section for calendar year 2003. I wish to recognize and thank my predecessor, Thomas A. Reed, for his efforts in chairing the Section in 2002. Many thanks to Tom for a job well done!

Turning to 2003, I'd like to report on what the Section has already accomplished as well as its plans for the future.

Annual Meeting/January 22, 2003

The Section co-sponsored two programs dealing with what can only be referred to as "the issue of the moment." The morning session which was co-sponsored with the Business Law Section, was entitled "**Sarbanes-Oxley: Corporate Governance and Lawyers Conduct**." This comprehensive program dealt with the key provisions of Sarbanes-Oxley and its probable effect on corporate directors, officers and their counsel. A very distinguished panel of regulators and corporate and outside counsel presented a detailed set of issues that lawyers need to consider when counseling corporate clients. In the afternoon, our Section, along with the Commercial and Federal Litigation Section and the Business Law Section, co-sponsored **The Presidential Summit on Corporate Responsibility and the Legal System**. The program was divided into three parts, the first of which was entitled "**A Matter of Corporate Responsibility: Where Are We Going From Here?**" This was followed by "**Examining the Roles of Lawyers, Corporate Officers and Directors, Accountants and Government: Where We've Been, Where We Are, Where We're Going**." This particular portion of the program, expertly moderated by Robert L. Haig, of Kelley, Drye & Warren, was a highly spirited debate among some of the true experts in the field including William T. Allen, Kenneth J. Bialkin, John H. Biggs, Stephanie B. Mudick, Attorney General Hon. Eliot Spitzer, Lawrence J. Fox and Professor Richard W. Painter. The third part of the program was entitled "**Attorney-Client Confidentiality and Related Ethics Issues.**" From a personal standpoint, I found the Presidential Summit to be one of the best programs I have ever attended and wish to offer my congratulations to then-President Lorraine Power Tharp and all other parties involved in putting the program together.

On May 22, 2003, the Section, along with the Women in the Law Committee, the Law Practice Management Committee and the Committee on Continuing

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Legal Education of the New York State Bar Association co-sponsored the reception at the first annual "Women on the Move" symposium. This program was designed to help pave the pathways to success for women attorneys within law firms and corporations in New York State. Topics included rainmaking strategies, ethics and leadership development skills.

There is little doubt that the subject of ethics has dominated our profession recently. Our Section has provided members with an opportunity to stay abreast of important developments through the annual "**Ethics for Corporate Counsel**" program which we began in 2000 and have offered each year since. We are pleased to announce that the program will once again be offered on October 27 in New York City, at the Association of the Bar of the City of New York. Look for the program mailer later this summer.

I am very pleased to announce that the Executive Committee is in the planning phase of developing a comprehensive symposium specifically for corporate counsel. Our initial discussions have focused on a program to be held in October 2004 that will offer a panel of experts on various topics of special interest to our members, presenting the latest developments in practice areas of great importance. The "**Corporate Counsel Institute,**" as it is currently being referred to, will be held in conjunction with the 2004 "**Ethics for Corporate Counsel**" program. This is an exciting development; more to come!

Included in this issue are articles entitled **"Removing Pending Litigation from the Deal: An Introduction for Deal Counsel"; "Constitutional Limitations on Punitive Damages: State Farm v. Campbell"; "Business Method Patents: Commerce in Digital Goods";** and '**Professionalism: What's In It for In-House Counsel?"** I hope that you enjoy this issue of *Inside*, and that the articles presented are helpful to your practice. If you or your outside counsel would like to contribute an article for future issues, contact the Editor, Bonni G. Davis, at bdavis@fnly.com.

Finally, I want our members to know that if they have any suggestions or comments, they should feel free to contact me at jmonitz@fds.com.

Jay L. Monitz

Removing Pending Litigation from the Deal: An Introduction for Deal Counsel

By Gary P. Blitz and Jill K. Kerxton

Have you ever had a client in the following predicament? Following an aborted sale, a company's stock plummets. Shareholders react with litigation, alleging hundreds of millions of dollars of damages for a multitude of violations of federal and state securities laws in conjunction with the botched sale. How in the world do you move forward and entertain new deals and prospects with this litigation blemishing its financials? The insurance industry has the solution—a product called Loss Mitigation Insurance or Litigation Buyout Insurance (LBI).

What Is LBI?

The concept of LBI is simple—the insurer assumes all, or part, of the risk of a lawsuit, thereby effectively removing the suit from, or definitively valuing it on, the books of the defendant. This has proven to be an extremely effective tool to provide comfort to deal counterparties and sources of capital.

Take the case of Samsonite Corporation,[1] which found itself in the dilemma described above in 1998. An attempt by its board to sell the company to strategic investors had failed. Following a releveraging, the share price dropped significantly. Shareholders class action and derivative action lawsuits were filed in various federal and state courts. Despite Samsonite's confidence that it had meritorious defenses to all of the complaints, the uncertainty of any lawsuit coupled with the huge time demand made necessary recapitalization efforts virtually impossible. An LBI policy permitted Samsonite to move forward. The insurer took over the litigation assuming all potential liability. With the litigation risk transferred, Samsonite refocused on its recapitalization—this time without the baggage. Within six months, Samsonite raised $55 million of equity capital. It retired debt and for 2000, EBITDA was $91 million, up from $50 million in 1998.

While LBI's genesis was in the area of securities litigation, the uses of LBI expand far beyond the securities law arena and the backdrop of a recapitalization. LBI has been utilized in the context of M&A transactions—removing the potential consequences of a pending litigation from the deal, particularly when the two sides cannot agree on the exposure from the litigation. A recent example of this was discussed in the December 2001 press release announcing the acquisition of Avant! Corporation by Synopsis, Inc. LBI also has been used in an ongoing business situation simply to manage litigation risk. Other subject matters where insurers have shown an appetite to provide LBI exist in the domestic and foreign arenas, including taxes, antitrust, construction, closely-held company shareholder disputes, interpleader actions, environmental cases and personal injury claims.

Types of LBI

LBI's uses have tended to fall within several categories: the Buyout, the Cap or the Hedge. The Buyout case is the most common. The insurer provides coverage for all liability resulting from a specific "Action" and assumes responsibility for defense, including costs. A first cousin of the Buyout is the Cap. As its name suggests, the Cap acts as a stop loss. Under such coverage, the insurer assumes liability above a pre-agreed amount, typically the amount the company expects to pay. A more unusual type, the Hedge, is essentially a put option on a case. It is likely to be pursued by a company that has won a case, which is being challenged on appeal. The Hedge locks in the benefit of the favorable ruling.

Buyout. The Samsonite coverage described above illustrates a Buyout. In a Buyout, in exchange for assuming the liability of a suit, the insurer looks to be paid a premium equal to what it sees as the expected settlement value, plus an additional amount for its trouble. In the Samsonite case, the insurer reportedly received a premium of $17 million. When all was said and done, both Samsonite and the insurer had won. From Samsonite's perspective, the coverage permitted Samsonite to proceed with its recapitalization, reaping the rewards highlighted above. When the case settled 15 months later, the insurer had achieved its desired result too—after payments under Samsonite's existing D&O policies, the insurer's contribution towards the settlement was well below the premium it had been paid.

Cap. An LBI Cap was used to address a litigated dispute between a general contractor and a hotel over construction of the hotel. By virtue of the coverage, a box was created around the case—allowing the downside to the defendant hotel to be quantified. The subject litigation was complex, involving overlapping claims of the general contractor and subcontractors, including numerous mechanics liens, in federal and state courts. Under the policy, the hotel remained liable for a specified amount of damages. The insurer assumed liability for the next layer of coverage. In addition, the insurer had responsibility for conducting the defense. Several benefits accrued to the insured in addition to removal of the financial liability for an unanticipated catastrophic result in the case. The company also could focus its management time on running the business, not the litigation, and proceed with its planned new financing and expansion of its business.

Hedge. An example of a Hedge can be found in a private antitrust action between an industry leader in the publishing industry and its primary competitor. The industry leader found itself the defendant in a case that alleged it acted in an illegal manner by attempting to monopolize. A jury had awarded the plaintiff over $25 million. The defendant, however, successfully argued in a post trial motion that the verdict was unsupported by the evidence, thereby winning a reversal. The trial judge's reversal was the subject of an appeal. While the appeal was pending, an investor purchased the company. The investor was reluctant to close the acquisition with this pending exposure on its target's books. As a means to address the prospective purchaser's reluctance, the company explored LBI. Had the case not been decided during negotiations, a policy insuring that the reversal would be upheld on appeal could have been purchased. The quoted premium was about $2 million. While expensive compared to traditional coverage, in the context of salvaging a $950 million acquisition, the cost made sense.

Structural Issues—What Is the Objective?

Regardless of the type of LBI sought, there are various structural issues facing an LBI purchaser: How much insurance is needed? Is the company willing to hand off control of the litigation? What sort of deductible is acceptable? In considering each of these questions, the insured must continually remind itself to ask, "what do I seek to accomplish by the insurance?" Is the goal simple risk management or is it more result oriented, such as satisfying the discomfort of an investor, a lender or a buyer?

Control of the Case: An insured also needs to become comfortable with the notion of ceding, or at a minimum sharing, control of the litigation with the insurer. An insurer will be quite concerned over major strategic decisions, choice of counsel, settlements, etc. For some insureds, the idea of sharing—let alone ceding—control over litigation does not come easy. Quite naturally, a defendant wants to maintain exclusive control over its own destiny. It also is quite reasonable for the insurer to want to have the ability to protect its position and utilize its expertise in handling litigation (which often is extensive) to minimize the exposure. The degree of control required by insurers may differ for Buyouts, Caps and Hedges to reflect the relative downside of the insured and insurer in the case.

Confidentiality: An interesting topic surrounding LBI coverage is confidentiality. In some cases, the ability to disclose the purchase of the coverage is absolutely critical. An announcement that an important liability has been removed from a company's balance sheet sends a major message to analysts following a company's shares. On the other hand, disclosure of the existence of coverage might be viewed as being harmful to the outcome.[2] Purchasers of LBI should recognize, however, that under Federal Rule of Civil Procedure 26(a) and similar state rules, at least the existence of the LBI policy may have to be disclosed to a plaintiff during discovery.

From this brief article, it is hoped that one takes away a general understanding of the availability of LBI as a means to prevent pending litigation from standing in the way of the business of a client. While obtaining LBI can be a complex process, the coverage itself can be extremely effective in closing the information gap or the comfort gap between buyer and seller or lender and borrower. LBI can make a lawyer a problem solver while others around the table are merely pointing out problems.

Endnotes

1. Information on the Samsonite case was derived from Samsonite's securities filings, discussions with its insurance broker and a November 1, 2000 article in *CFO Magazine* highlighting the coverage.
2. Another issue not discussed in this article due to space constraints relates to the implications on attorney-client privilege of purchasing LBI and opening up a defendant's and its counsel's files to an insurer to allow the insurer to underwrite the proposal. Various strategies have been employed by potential insureds to protect privileged information. The insurers tend to be cooperative with insureds on such matters. However, there is little ability on the part of counsel to identify a foolproof means to protect privilege.

Jill K. Kerxton and Gary P. Blitz are Partners in the Financial Risks Practice in the Washington, D.C. office of Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C. Ms. Kerxton and Mr. Blitz work with a number of insurance companies who underwrite M&A insurance and other transactional insurance products, including LBI. Ms. Kerxton and Mr. Blitz also are the principals of a Mintz Levin business affiliate, called ML Insurance Strategies, LLC, an insurance broker which assists clients in the context of LBI and other transactional coverages. Ms. Kerxton can be reached at (202) 585-3540. Mr. Blitz can be reached at (202) 585-3535.

Constitutional Limitations on Punitive Damages: *State Farm v. Campbell*

By Stuart M. Riback

Punitive damages often baffle corporate litigants. American juries have been known sometimes to return verdicts for punitive damages in numbers so large as to be outlandish. Overseas companies, in particular, read news accounts of multi-million dollar punitive damage awards and conclude that the American legal system is out of control. Though large punitive damages awards are often reduced by the trial judge or on appeal, the sheer size of some jury awards is sobering even when those verdicts do not stand.

In April of this year, the Supreme Court of the United States built on its earlier case law that placed limits on the size of punitive damage awards. *State Farm Mutual Automobile Insurance Company v. Campbell*[1] was a case against an insurance company for handling an insurance claim in bad faith. According to witnesses and State Farm's investigation, Mr. Campbell had caused a serious automobile accident that left one person dead and another disabled. But State Farm decided to contest liability rather than try to settle the claim within policy limits, and instead took the case to trial. The verdict at trial was over three times the amount of coverage, which potentially exposed the Campbells' personal assets. When State Farm declined to take an appeal, the Campbells themselves appealed, and lost. At that point State Farm paid the entire judgment.

But that didn't satisfy the Campbells. They sued State Farm for handling their claim in bad faith. After a trial, the jury awarded the Campbells $2.6 million of compensatory damages and $145 million of punitive damages. (Note that, because State Farm ultimately paid the entire judgment to the accident victims, the Campbells suffered no physical injury and no substantial economic injury, either; so the main item of compensatory damages was apparently compensation for emotional distress). The trial court reduced the verdict to $1 million of compensatory damages and $25 million in punitives, and on appeal, the Supreme Court of Utah upheld the $26 million judgment. State Farm then sought review by the United States Supreme Court, which was granted.

By a 6-3 vote, the Supreme Court reversed, in an opinion that demonstrates deep concern about the seemingly arbitrary nature of many punitive damage awards. The Court seemed to be especially concerned that businesses were being punished simply because they were large and asset-rich.

The Supreme Court's reasoning started from the baseline of its 1996 opinion in *BMW of North America v. Gore*.[2] In *Gore*, the Supreme Court decided that as a matter of a defendant's constitutional rights, an award of punitive damages had to bear some relationship to the misconduct and to the compensatory damages. But in *State Farm*, the Supreme Court of Utah upheld the punitive damages award even though the opinion in *Gore* had already warned against excessive punitive damages. Consequently, the Supreme Court in *State Farm* clarified the legal criteria for what makes a punitive damages award excessive. The overriding theme of the opinion is that punitive damages must bear a relationship to the conduct that caused the plaintiff's injury, and cannot simply be a way for juries to express disapproval of a defendant. The Court discussed the factors that must be applied to ensure that a punitive damages verdict passes constitutional muster.

"The overriding theme of the opinion is that punitive damages must bear a relationship to the conduct that caused the plaintiff's injury, and cannot simply be a way for juries to express disapproval of a defendant."

First, the defendant's conduct must be truly reprehensible, and the punitive damages award must be directed to the reprehensible conduct at issue in the case and not at some other ill. As the Supreme Court said, "A defendant should be punished for the conduct that harmed the plaintiff, not for being an unsavory individual or business." In *State Farm*, much of the bad behavior by State Farm that was placed before the jury was not of the same kind that the plaintiffs claimed to have suffered in this case and, in fact, much of the behavior complained of was legal in other parts of the country outside Utah. Allowing punitive damages for bad behavior, rather than limiting it to the acts at issue in the specific lawsuit, generally creates the possibility of numerous punitive damages awards for the same conduct. The upshot is that "[t]he reprehensibility guidepost does not permit courts to expand the scope of the case so that a defendant may be punished for any malfeasance." It also does not permit a state court jury to punish a defendant for actions outside that state.

Second, there cannot be an excessive ratio between the punitive damages award and the harm or potential harm that the plaintiffs suffer. Although the Court declined to fix a specific maximum ratio, it noted that "in practice, few awards exceeding a single-digit ratio between punitive and compensatory damage . . . will satisfy due process." The Court noted that traditionally, double or treble damages awards were prescribed by statute to achieve punitive purposes (for example, in anti-trust or racketeering cases). But there is no fixed rule fixing such a low ratio: when the conduct is very reprehensible but the compensatory damages are small, a higher ratio may be called for; conversely, when the compensatory damages are sizable, a smaller ratio may be appropriate. "In sum, courts must insure that the measure of punishment is both reasonable and proportionate to the amount of harm to the plaintiff and to the general damages recovered."

"[T]he Supreme Court in State Farm *may well have made the punitive damages inquiry something less of a crapshoot than it has been until now."*

The Supreme Court rejected several of the factors that the Utah Supreme Court had relied on when upholding the punitive damages award. Among these were: the fact that State Farm was statistically unlikely to be punished in very many cases; that State Farm's policies affected many Utah consumers; and that State Farm had "enormous wealth." But the Supreme Court's view was that these were not proper considerations in assessing the punitive damages award in this case. In the Supreme Court's words, "here the argument that State Farm will be punished in only the rare case, coupled with reference to its assets . . . had little to do with the actual harm sustained by the Campbells. The wealth of a defendant cannot justify an otherwise unconstitutional punitive damages award."

Third, and finally, the court must look to the disparity between the punitive damages award and the civil penalties that are authorized for comparable conduct. In the Supreme Court's view, great care must be taken to insure that a defendant is not, in essence, being punished criminally without being afforded the protections of the criminal law, including the requirement that guilt be proved beyond a reasonable doubt.

State Farm probably will be useful in restoring some sanity to litigation in which plaintiffs seek punitive damages. It provides a clarity that *Gore* did not. Importantly, *State Farm* may restrict the kinds of evidence that a plaintiff seeking punitive damages can submit to a jury. It specifically requires that punitive damages address only the particular reprehensible conduct at issue in the specific case. Because of that, the Supreme Court noted that such matters as (i) a defendant's conduct that is not related or similar to the conduct at issue in the specific case, or (ii) the defendant's wealth, cannot support a punitive damages award. Logically, that should mean that in the future, trial courts should keep out evidence of either general corporate bad behavior or corporate deep pockets—because they are both irrelevant and are likely to prejudice the jury unfairly. If that is what happens, the Supreme Court in *State Farm* may well have made the punitive damages inquiry something less of a crapshoot than it has been until now. Coupled with the relatively low multiples that the Supreme Court has now indicated are the ceiling of what is permissible, these factors should drive punitive damages awards downward, and also should mean that fewer outsized awards will be upheld.

Strictly speaking, the *State Farm* case's rules were guidelines for judges to use in evaluating whether a jury's punitive damages award is reasonable. As a practical matter, however, by setting forth clearly the legal standards that govern when an award is legitimate, the Supreme Court has provided standards for funneling a jury's discretion before the fact, and thus limiting it.

Endnote

1. __ U.S. __, No. 01-1289 (Apr. 7, 2003).
2. 517 U.S. 559 (1996).

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Business Method Patents: Commerce in Digital Goods

By Robert E. Krebs and Thierry K. Lo

In their broadest sense, "business method" patents are patents relating to the creation and distribution of "digital goods." Digital goods can comprise any product or service that can be turned into bits and bytes. Examples of digital goods are software, music, video materials, financial data, medical and pharmaceutical information, stock and bond information, airline tickets and home mortgages.

The digital goods involved in two decisions of the Court of Appeals for the Federal Circuit—the court that has jurisdiction over appeals in patent cases—were, respectively, mutual fund values and telecommunication charges.[1] In these two decisions, the Federal Circuit confirmed that computer-implemented "business methods" involving digital goods can be patented. Specifically, the Federal Circuit recognized that systems and methods involving digital goods—that is, systems and methods for collecting, manipulating, transforming and distributing electronic information for commercial purposes—are no less patentable than computer-implemented innovations that are not directly related to commercial activities.

Commerce in digital goods is the quintessence of commerce using the Internet. Although both physical and digital goods can use the Internet as a sales and marketing channel, only digital goods can use it for sale and delivery in a single customer transaction, thereby providing cost savings and customer convenience superior to physical distribution. In addition to benefiting consumers, e-commerce assists the sellers of digital goods and services by drastically reducing their distribution costs and decreasing transaction times.

In past years, business method patents have been relatively difficult to obtain and enforce. The situation changed, however, when earlier precedent was overruled in the 1998 decision of the Federal Circuit in the *State Street Bank & Trust Co.* case. In this opinion, which reversed a district court decision, the Federal Circuit held that an electronic system for assembling and distributing financial information was patentable subject matter. In particular, the system electronically distributed daily asset values to mutual fund companies that had pooled their assets in an investment portfolio organized as a partnership. In confirming the patentability of the system, the court said: "Since the 1952 Patent Act, business methods have been, and should have been, subject to the same legal requirements for patentability as applied to any other process or method."

Further, the court held that: "Whether the claims are directed to subject matter within [35 U.S.C.] § 101 should not turn on whether the claimed subject matter does 'business' instead of something else."

In 1999, the *State Street* case was buttressed by the Federal Circuit opinion in *AT&T Corp. v. Excel Communications Inc.* The *Excel* case involved a patent for a method that allows long-distance carriers to charge different billing rates depending upon whether the called party had the same or a different long-distance carrier as the caller. The method resulted in reduced charges to subscribers who placed long-distance calls to the carrier's other subscribers. Thus, as in the *State Street* case, the factual setting of *Excel* involved financial information that was electronically manipulated in digital form for business purposes. In finding that AT&T's method invention was patentable subject matter within the context of 35 U.S.C. § 101, the Federal Circuit drew no distinction relative to the system invention in *State Street.* Instead, the court deemed both inventions—each involving mathematical algorithms—to comprise patentable subject matter because ". . . the claimed invention as a whole is applied in a 'useful' manner . . ."

The decisions in *Excel* and *State Street* apply to innovations by a wide range of companies. These cases made clear that the standards for patenting business method innovations—namely, that patentable inventions must be new and unobvious in view of relevant prior art—are no more stringent than for other technologies.

One year after *State Street*, the United States Patent and Trademark Office (USPTO) saw the number of business method patent applications filed almost triple from 2,821 applications in 1999 to 7,800 applications in 2000. Many start-up companies saw business method patents as the shortcut to wealth during the "dot-com" era and were rushing to claim their stake in the land of untapped e-commerce wealth.

Amazon was one of the first e-commerce companies to capitalize on business method patents. In September 1999, the USPTO issued Amazon a business method patent on a "one-click" technology on their Web site. Immediately thereafter, Amazon sued its competitor, Barnesandnoble.com, for allegedly infringing on its recently issued patent. Amazon was awarded a preliminary injunction against Barnesandnoble.com. The controversial lawsuit and preliminary injunction sent a shockwave through the patent world, resulting in a fury of criticism against Amazon and the USPTO.

In March 2000, the USPTO reacted to the surge in business method patent applications and the public outcry by increasing scrutiny for patent applications falling within class 705, the business method class. For example, a secondary examiner would conduct a second independent review of a patent application falling within this class to determine whether the search by the primary examiner was conducted properly. In addition, the USPTO increased the number of examiners assigned to class 705.

In an effort to prevent a potential flood of litigation resulting from the increase of issued business method patents, Congress enacted the American Inventors Protection Act in late 1999. The American Inventors Protection Act provides a limited defense provision to insulate an accused party on charges of infringing a "method of doing or conducting business." The statute provides a defense to an accused party who "actually reduced the subject matter to practice at least one year before the effective filing date of such patent, and commercially used the subject matter before the effective filing date of such patent."[2] However, the enacted statute left out the definition of a "business method."

Concerned with the current state of business method patents, in October 2000, Representatives Howard Berman (D-California) and Rich Boucher (D-Virginia) introduced a bill (H.R. 5364, titled "Business Method Patent Improvement Act of 2000") into Congress to "repair the system before the PTO awards more monopoly power to people doing the patently obvious." Amongst the provisions, the bill provided a definition for "business method," a requirement that a patent application be determined whether it is for a business method within one year from the date of filing of an application, and a post-grant opposition procedure in which any third party can request an opposition to a patent on a business method invention within nine months after the granting of the patent. The bill was never enacted into law before Congress adjourned for the year.

On February 14, 2001, a federal appellate court vacated Amazon's preliminary injection against Barnesandnoble.com. The court found that the lower court failed to adequately interpret prior art cited by Barnesandnoble.com. This illustrated a problem the USPTO has in uncovering prior art involving digital goods because publications in technology fields that are very new, such as business methods, are not easily located. The USPTO's attempt to address the above problem involved additional training of examiners in the field of business method patents to better uncover prior art.

Based on the feedback received from the public after introducing the Business Method Patent Improvement Act of 2000, Rep. Berman reintroduced legislation attempting to address the problems of business method patents on April 3, 2001. On April 19, 2001, the bill was referred to the House Subcommittee on Courts, the Internet, and Intellectual Property. The bill (entitled "Business Method Patent Improvement Act of 2001") sought to amend title 35 of the United States Code "to provide for improvements in the quality of patents on certain inventions."

Rep. Berman still believed that Congress should enact specific legislation directed towards business method patents so that "the U.S. patent system produces high quality patents." Specifically, the Business Method Patent Improvement Act of 2001 would require the USPTO to publish all business method patent applications after 18 months. It also would establish an administration "Opposition" process where parties can challenge a granted business method patent. However, during the House Subcommittee hearing, many expressed the feeling that legislation should not be introduced, since the same existing laws of new and obviousness are also applicable to the business method patents. In particular, the new procedures adopted by the USPTO, along with the Federal Circuit Court vacating Amazon's preliminary injunction, have provided guidance on how to adjust and guide the U.S. patent system to continue issuing high quality patents.

To date, Congress has been preoccupied with other issues, and has not enacted or debated on any legislation addressing business method patents. Even so, we expect the availability and enforceability of business methods patents will increase.

Endnotes

1. *See State Street Bank & Trust Co. v. Signature Financial Group, Inc.*, 149 F.3d 1368, 47 USPQ2d 1596 (Fed. Cir. 1998); and *AT&T Corp. v. Excel Communications, Inc.*, 172 F.3d 1352, 50 USPQ2d 1447 (Fed. Cir. 1999).
2. 35 U.S.C. 273(b)(1).

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Professionalism: What's in It for In-House Counsel?

By Lisa A. Dolak

The prestige and prominence of the in-house attorney are on the rise. Today's in-house attorneys handle sophisticated legal matters, manage outside counsel, and actively participate in corporate administration. And according to a recent survey by the American Corporate Counsel Association, they enjoy management's esteem.[1] Ninety-six percent of the chief executive officers and other senior executives surveyed rated the performance of their legal departments as "excellent" or "very good."[2] Outside counsel were rated higher than in-house by only fifteen percent of the survey respondents.[3]

In-house practice, however, presents special professionalism[4] challenges. A number of attributes of the job potentially foster neglect, or even disregard, of professionalism obligations.[5] Part of the challenge is recognizing these potential obstacles.

Professionalism Challenges Are Built In

Every attorney owes his or her clients the sometimes-conflicting duties of loyalty and professional independence. The conflict is exacerbated in the in-house context, where exercising independent judgment and maintaining objectivity are more difficult, and even greater loyalty is demanded. The lawyer's economic well-being, at least temporarily, depends on continued good relations with a single employer. As a practical matter, there is little, if any, freedom to decline any particular representation. And in-house lawyers must regularly contend with the potential for conflicts between the interests of the corporation and the interests of its employees, who seek the lawyer's advice and, to some extent, direct his or her activities.

Maintaining High Professional Standards Can Conflict with Career Objectives

Attorneys looking to move into the general counsel position are advised to "stop thinking like a lawyer," "tolerate risk," and "schmooze with everyone."[6] Such advice makes good sense, but it also illustrates the conflict inherent in fulfilling the in-house counsel's dual (law and business) roles. The magnitude of the conflict depends on a variety of factors, including the corporate culture and the criteria used to evaluate the lawyer's performance. For example, if the lawyer's compensation and promotion opportunities are heavily tied to facilitating the corporation's pursuit of its business goals, the conflict may be greater. Furthermore, in the in-house setting, performance reviews are often conducted by non-lawyers, who may not recognize or understand the lawyer's ethical obligations.

The Risk of Sanction—Disciplinary Action or Malpractice Liability—Is Comparatively Low

Malpractice claims and complaints to disciplinary authorities against in-house lawyers are less common than those filed against outside counsel. Several factors probably contribute. For example, the in-house lawyer's ongoing exclusive representation of his or her client tends to engender greater loyalty. Also, corporations, in general, may be less willing to publicly air grievances against in-house counsel, and the potential for recovery against law firms is obviously greater. Furthermore, as their in-house attorneys' sole (or at least primary) income source, corporations are in a position to exert comparatively greater pressure on their in-house counsel, without resort to threats of malpractice liability or disciplinary sanction.

Given these "disincentives," why worry about professionalism? Consider the following:

Malpractice Claims Against In-House Lawyers Are on the Rise

Malpractice claims against in-house counsel may be relatively rare, but they are on the rise.[7] Recent examples include a counterclaim against a former general counsel who had sued to collect severance, based on the counsel's alleged negligent supervision of outside counsel, and a claim against a city attorney allegedly responsible for the entry of a default judgment against the city.[8] Claims by terminated corporate employees alleging conflicts of interest against in-house attorneys who participate in termination decisions are also reportedly a potential source of liability suits.[9] These examples illustrate that in-house lawyers are not immune from claims of malpractice.

Professionalism Serves the Lawyer's Own Interests

We admire highly skilled lawyers. Even more than skill, however, the quality that most often makes a lawyer attractive to desirable potential clients and employers is integrity. Furthermore, beyond the ability to earn a living, developing a reputation as a lawyer of integrity has other rewards. Many attorneys seek leadership opportunities with professional and charitable associations or advisory and policy-making bodies, and find such positions very fulfilling. A track record of demonstrated professional judgment and integrity is a generally a critical prerequisite to obtaining and retaining such positions.

Professionalism Makes Good Business Sense

Companies, like lawyers, are measured by their reputations. Corporate management is principally responsible for setting policy, but in-house counsel, intentionally or unintentionally, often make decisions or implement policies that have a profound impact on the company and its reputation. To fulfill the attorney's obligation to act in the best interest of the business,[10] the attorney must establish and maintain high standards of integrity, responsibility, and credibility. In the words of one commentator, lawyers have an obligation to act as "architects of the accountability processes which provide the corporate structure with the discipline necessary for effective decisionmaking and which legitimize the corporation's power and impact in society."[11] In their dealings with corporate management and employees, business partners and competitors, government and regulatory authorities, litigation adversaries, the courts, and the public, in-house counsel should strive to represent the corporation in a manner consistent with the highest professional ideals. The corporation's reputation—and hence its success—may well depend on it.

Endnotes

1. Margery Gordon, *Execs Like You Better*, Corp. Counsel, July 2001, at 24.
2. *Id.*
3. *Id.* Eighty percent or more of the executives surveyed reported that their in-house legal departments "[u]nderstand[ ] the company better," "[p]articipate[ ] in strategic business planning," and are the "[b]est to manage outside counsel." *See id.* A majority of respondents reported that, as compared with outside counsel, in-house counsel has a "[b]etter relationship with [the respondent]," and is "cheaper." *See id.*
4. There is no generally accepted definition of professionalism. *See, e.g.,* Peter A. Joy, *A Professionalism Creed for Judges: Leading By Example*, 52 S. Cal. L. Rev. 667, 669 (2001). It has been described as "like pornography, hard to define, but easy to recognize." *Id.* (quoting Editorial, *Professional Responsibility: Has the Rise of Megafirms Endangered Professionalism?*, 75 A.B.A. J., Dec. 1989, at 38). The Georgia Chief Justice's Commission on Professionalism offered the following definition: "An ongoing effort of lawyers to conform their conduct to the highest levels of professional integrity in their relationships with clients, other lawyers, dispute resolution forums, and the public, promoting a sense of the highest aspirations that the legal profession has, at its best moments, embodied." *See* J. Pat Sadler, *One Lawyer's Proposal for a Code of Professionalism in Securities Arbitration*, 1264 PLI/Corp 67, 74 (August 2001).
5. Commentators have distinguished professionalism from ethics on the ground that the latter entails avoiding violations of the applicable disciplinary minimums, while the former is aspirational. *See* Sadler, *supra* note 4, at 72–73. As discussed below, however, the in-house attorney should seek to advance the corporation's interests by establishing within his or her own sphere of influence an environment of personal and corporate responsibility. Furthermore, it is in the attorney's interest to maintain his or her own professional integrity and credibility. Viewed in this light, professionalism "ideals" are obligations.
6. Meyer Haberman, *Want to Be GC? An Action Plan for Getting to the Top*, Corp. Counsel, July 2001, at 47–48.
7. *See* Gerald J. Buchwald, *The Next Target: Corporate Counsel Face Their Own Cast of Malpractice Demons*, A.B.A. J., July 2001, at 54.
8. *See id.*
9. *See id.*
10. Under both the American Bar Association (ABA) Model Rules of Professional Conduct ("Model Rules") and the earlier ABA Model Code of Professional Responsibility, a lawyer retained or employed by an organization, such as a corporation, represents the organization. *See* Model Rules of Prof'l Conduct Rule 1.13; Model Code of Prof'l Responsibility EC 5-18. The Model Rules, for example, authorize a lawyer for an organization to "proceed as is reasonably necessary" to protect the organization from harm caused by its officers and employees. *See* Model Rules of Prof'l Conduct Rule 1.13.
11. Harold M. Williams, *Professionalism and the Corporate Bar*, 36 Bus. Law. 159, 165 (1980) (*quoted in* Grace M. Geisel, *The Ethics or Employment Dilemma of In-House Counsel*, 5 Geo. J. Legal Ethics 535, 556 n.93 (1992)).

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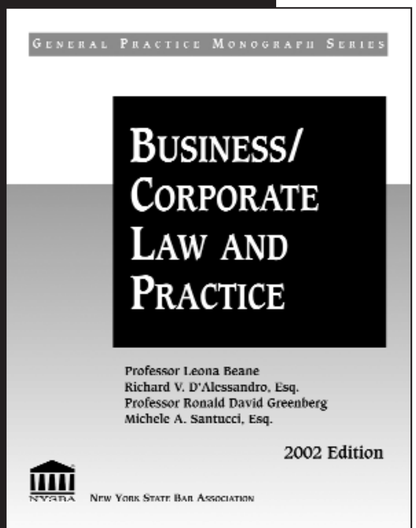

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