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The Massachusetts Bar Association
20 West St., Boston, MA 02111
(617) 338-0500

e-mail: communications@massbar.org
online: www.MassBar.org
LEGAL PROTECTIONS FOR TRANSGENDER PEOPLE

By Laura K. Langley and Jennifer Levi

Andrew was hired recently by a local town police force. He was a decorated officer who had moved to the local community to be closer to family after having served on the state force in another state for 20 years. He retired there and had not intended to get back into the police service again. But the local community he lived in was under-staffed, and after striking up a conversation with the chief of police one day at a local pub, decided to start working part time. The chief was enthusiastic as it had been hard to recruit highly qualified officers. Andrew required little training and started on the force within two weeks of the initial interview. He was highly regarded and fit in well.

However, less than six months after he was hired, Andrew noticed that things started to change. He was issued defective equipment. The dispatcher often gave him inaccurate directions or the radio signal inexplicably faded during calls. Other officers stopped talking when Andrew entered the room and stopped inviting him to social events. Andrew feared he had lost his abilities as an officer. To be sure, he was older than when he had earlier served, but he could not understand how so much could have changed in just six months. The pattern of disregard for him at work intensified, as did his reaction to it. He developed insomnia, had a resurgence of panic attacks (that had begun as a result of a shooting incident during his former service), and began to develop severe physical abdominal pains for which he sought treatment. His home life suffered. His temper shortened and he was quick to snap at his wife and daughter.

About three weeks after the chief who hired him left to take a position in another community, Andrew received a call from him. His former boss called to tell him that there was a reason for the treatment he had begun to receive. The former chief explained that someone had done a computer search and learned that Andrew is transsexual. While born genetically female, Andrew has always had a male gender identity. In order to conform his outward appearance to that of his sense of who he has always been, Andrew went through a course of medical treatment to transition from female to male. His co-workers had such stereotypes about how people should look and act, and such raw prejudice against transgender people, that they had gotten together and decided to work collectively to run Andrew off the force. Their plan worked. The treatment Andrew faced was so severe that he simply could not do his job, and he left the force.

After receiving the information from the former police chief, Andrew decided to pursue legal recourse.

Sadly, Andrew’s experience is far from unique. For many people who do not fit their co-workers’ or society’s views of what a “real man” or “real woman” should look or act like, this kind of discrimination is all too real and pervasive. Many transgender people – including those, like Andrew, who transition, and those who do not but continue for a variety of reasons to defy expectations of “appropriate” gender roles – face rampant discrimination in employment, public accommodations, housing, credit and education.
Amongst other damaging repercussions, this discrimination results in chronic unemployment and underemployment amongst transgender people. 

Though data collection on the subject is scarce, the available statistics confirm the troubling reality suggested by Andrew’s story. In one survey of transgender people in San Francisco, almost half of the respondents reported experiencing discrimination by their employer or co-workers, 64 percent reported earning under $25,000 per year, and 79 percent reported earning under $50,000 per year. Further, this discrimination transcends the employment arena. Over one third of the transgender people responding to the San Francisco survey reported being discriminated against at a place of public accommodation, and according to one national survey, nearly 75 percent of transgender students feel unsafe at school because of their gender expression. Additionally, for many transgender people, different treatment extends beyond discrimination into acts of violence perpetrated against them. One of the most widely known incidents of anti-transgender violence stems from the case of Brandon Teena, a transgender person who was assaulted, raped and ultimately murdered by friends associated with his social circle when they learned of his transgender identity. 

In response to this widespread discrimination and violence, many states and localities have begun to enact statutes clarifying the scope of legal protections for transgender people. Nine states—California, Connecticut, Hawaii, Maryland, Minnesota, Missouri, New Mexico, Pennsylvania and Vermont—and the District of Columbia, have amended their hate crimes laws to make clear that crimes motivated by bias against the victim’s gender identity or expression constitute hate crimes. Additionally, nine states—California, Hawaii, Illinois, Maine, Minnesota, New Jersey, New Mexico, Rhode Island and Washington—and the District of Columbia, have more than 80 cities and counties from geographically diverse regions of the country, have amended their nondiscrimination statutes to be explicitly inclusive of transgender people. 

Of these statewide nondiscrimination laws, five were enacted in the last two years. Indeed, a growing number of employers and professional associations have recognized the importance of codifying explicit legal protections for transgender people. Last summer, the American Bar Association issued a recommendation calling on federal, state, local and territorial governments to pass laws prohibiting discrimination on the basis of gender identity or expression in employment, housing and public accommodations. 

In Massachusetts, although the cities of Boston, Cambridge and Northampton have enacted transgender-inclusive nondiscrimination ordinances, no explicit statewide protections exist for transgender people. This does not mean that transgender individuals in the commonwealth have no legal protections against discrimination. The Massachusetts Commission Against Discrimination and the Massachusetts Superior Court have ruled that transgender people are protected by existing prohibitions against sex and disability discrimination. Although not without exception, most courts across the country that have recently considered whether transgender people are covered by existing law have said that they are. 

Nonetheless, even in jurisdictions like Massachusetts with positive case law, explicit statutory protection is crucial for transgender people. Adding “gender identity or expression” to nondiscrimination and hate crimes laws puts stakeholders, such as employers, landlords, educators and transgender people themselves, on notice of their rights and responsibilities. Doing so reduces liability for employers by clarifying their obligations and simultaneously ensures that transgender people know their rights. Additionally, a clear law makes a strong public policy statement that discrimination against transgender people is wrong and is not tolerated in the commonwealth. 

Recognizing the importance of explicit inclusion for transgender people within the General Laws, state Representatives Carl Sciotto and Byron Rushing introduced House Bill 1722, An Act Relative to Gender-Based Discrimination and Hate Crimes, this legislative session. In addition to its two lead sponsors, the bill currently has 21 co-sponsors in the House and Senate. HB 1722 amends G.L. c. 151B and G.L. c. 272, §§92A, to explicitly prohibit discrimination based on gender identity or expression in employment, housing, credit and public accommodations. The bill also amends those statutes prohibiting discrimination in public education, and G.L. c. 22C, §32 and G.L. c. 265, §39, the state’s hate crimes laws. Following the ABA’s recommendation, the MBA House of Delegates voted unanimously at its meeting on March 1, 2007, to endorse HB 1722. 

In Connecticut and Vermont, bills that would provide explicit protection against discrimination for transgender people are well on their way to becoming law. At the federal level, the Local Law Enforcement Hate Crimes Prevention Act of 2007, which permits the Justice Department to investigate and prosecute crimes motivated by “inter alia, the victim’s gender identity, was recently introduced in the House and Senate. And the Employment Non-Discrimination Act of 2007, which prohibits discrimination in employment on the basis of sexual orientation and gender identity, was introduced in the House on April 24. 

As Andrew’s experience demonstrates, the pervasive discrimination faced by transgender people in many areas of their lives is emotionally, financially, and often physically, devastating. The introduction of HB 1722 in Massachusetts is an important step toward ending the discrimination and hate-based violence experienced by transgender individuals in the commonwealth. Its adoption will provide key legal protections for transgender people and make a strong public statement.

End notes

1. This example, while fictional, is based upon a real incident.
2. “Transgender” is an umbrella term that encompasses all people whose gender identities and expressions challenge traditional notions of how men and women should appear and behave. Transgender people include, for example, transgender and genderqueer individuals and all who are gender nonconforming.


7. CAL. GOV’T CODE § 12940 (West 2005); CAL. PENAL CODE § 422.56 (West 2005); CAL. WELF. & INST. CODE §§ 16003, 16013 (West 2005); HAW. REV. STAT. §§ 489-2-489-3, 515-2-515-7 (2006); ILL. COMPT. STAT. 5/1-101 (2005); ME. REV. STAT. ANN. tit. 5, § 4551 (2005); MINN. STAT. § 363A.01 (2005); N.J. STAT. ANN. §§ 10:2-1, 10:5-1 (2006); N.M. STAT. § 28-1-1 (2005); R.I. GEN. LAWS §§ 11-24-2, 28-5-2, 34-37–1 (2004); WASH. REV. CODE § 49.60.010 (2006). In Iowa and Oregon, similar statutes have passed both houses and are awaiting the governor’s signature. See SF 427 (Iowa 2007); SB 2 (Or. 2007).


9. These localities include, for example, major cities such as Cincinnati, Dallas, Denver, Los Angeles, New Orleans, New York and Seattle, and smaller cities and towns such as Bend, Oregon, York, Pennsylvania, Louisville, Kentucky, and Rochester, New York. For a list of all the cities and counties with transgender-inclusive nondiscrimination laws, see Transgender Law & Policy Institute, U.S. Jurisdictions with laws prohibiting discrimination on the basis of gender identity or expression, http://www.transgenderlaw.org/nldlaws/index.htm (last edited Dec. 17, 2006).


A recent decision from the Business Litigation Session of the Massachusetts Superior Court serves as a powerful reminder to corporations of all sizes of the vital importance of commissioning timely, thorough, and independent investigations of shareholder derivative suit allegations—or for that matter, serious internal allegations of any kind, whether brought by shareholders, policyholders, or employees. In Boylan v. Boston Sand & Gravel Co., Judge Ralph Gants—who at the time of this writing was slated for promotion to the chief administrative judge of the BLS upon Judge Allan van Gestel’s retirement in January 2008—allowed a shareholder derivative suit to survive summary judgment because the board of directors failed to conduct an adequate investigation of the shareholders’ claims. Significantly, Gants closely scrutinized the corporation’s decision to refuse the shareholder demand even though the vote to do so was made by a group of disinterested directors acting as a de facto special litigation committee.

The law in most states requires a careful, comprehensive evaluation of shareholder claims even for a majority-disinterested board enjoying the protection of the highly deferential business judgment rule. Indeed, the duty to investigate any claim relating to the business of the corporation is a bedrock principle underlying a director’s fiduciary duty. In Massachusetts, the Supreme Judicial Court has held that a “lack of investigation into the demand” neutralizes the protection of the business judgment rule. Moreover, under the law of several states—including Massachusetts, and even more dramatically in Delaware—courts employ a heightened standard requiring corporations to employ even greater investigative diligence when the board of directors is not comprised of a majority of disinterested directors. Where corporations cannot demonstrate such diligence...
to a court, the derivative suit survives and is able to proceed to trial, causing, at best, distraction, uncertainty, legal expense and a weakened settlement position, and, at worst, an eventual verdict against the corporation for significant money damages, court-ordered dismantling of corporate transactions and an overall erosion of marketplace confidence in the company. Corporations can forestall this range of unpleasant possibilities by undertaking a thorough and independent investigation of the shareholder demand as soon as it is made. This is most effectively done through an unbiased special litigation committee (“SLC”) that is aided in its investigation by outside counsel.

**Alli guidance for an effective investigation of derivative actions**

The American Law Institute has outlined the steps corporations should take to conduct an effective investigation of a derivative action. The Massachusetts Supreme Judicial Court, while not formally adopting the entire Alli provision on this subject, has embraced its spirit as well as several of its specific recommendations. Specifically, the Alli guidance states that corporate boards of directors should do the following when faced with a derivative demand:

1. appoint an SLC comprised of at least two members, each of whom should be disinterested and objective;

2. employ counsel and other such necessary professionals to assist the SLC;

3. ensure that the SLC has made determinations that are supported by a careful review and evaluation of the facts and relevant law; and

4. if the SLC determines that refusal or dismissal of the demand or action is the appropriate course of action, prepare a detailed report to be filed in court justifying its determination.

**Background of the Boylan decision**

The consequences of a poor internal investigation are brought to life in the recent Boylan decision. There, a long-running schism in a family business led to the estate of one shareholder (Dan Boylan, the deceased older son of the company founder) bringing suit against the corporation, the ready-mix concrete supplier Boston Sand & Gravel, which was under the majority ownership of the company founder’s other son, Dean Boylan Sr., and his two children, Dean Boylan Jr. and Jeanne-Marie Boylan. Dean Sr., Dean Jr. and Jean-Marie also served as directors of BS&G, along with four other individuals who were not members of the Boylan family. The suit alleged that Dean Jr. and Jean-Marie breached their fiduciary duty by entering into an agreement whereby a separate company owned by them leased a parcel of land in New Hampshire—for well below market value, the Dan Boylan Estate contended—from a wholly owned BS&G subsidiary. The agreement included a three-year option to purchase. The lawsuit sought rescission of the agreement as well as damages for Dean Jr. and Jeanne-Marie’s alleged misappropriation of a BS&G corporate opportunity.

After the Dan Boylan Estate filed suit, the BS&G board of directors voted unanimously to ratify the lease/option agreement. Voting in favor of ratification were Dean Sr., Dean Jr. and Jeanne-Marie, admittedly interested directors; a third director, longtime counsel for BS&G who Gants found also was interested based on the circumstances; and three directors who Gants determined were disinterested. The ratification of the agreement by the three disinterested directors was the functional equivalent, Gants found, of a disinterested SLC voting not to prosecute the estate’s ongoing derivative suit.

**“Demand excused” cases are a dying breed in Massachusetts but the heightened standard of judicial scrutiny that governs them still lives**

Because the Estate had not presented a formal demand prior to filing suit, the Boylan case presented a “demand excused” type of case. Such cases occur where the shareholder alleges that a majority of directors is interested and therefore making a demand on the board prior to filing suit would be futile. In these cases, as in Boylan, the corporate board may still vote whether or not to join the suit after it is filed. The other type of shareholder derivative action is referred to as “demand refused,” that is, a case which proceeds in court following the shareholder’s pre-complaint presentation of his demand to the board and the board’s refusal to litigate the demand on behalf of the corporation. By statute, after June 30, 2004 all shareholder derivative lawsuits filed in Massachusetts courts must have been first presented to the board for action. This made Massachusetts one of at least 23 “universal demand” states, and has made every viable shareholder derivative suit filed in the state after June 30, 2004 a “demand refused” case.

So the Boylan case, commenced in 2002, may be one of the last “demand excused” decisions to come out of the Massachusetts courts. However, the standard under Massachusetts law governing the judicial evaluation of corporate decisions not to join (and instead to seek to dismiss) “demand excused” cases, set forth in the Supreme Judicial Court decision *Houle v. Lou*, is equally applicable to “demand refused” cases in which there is not a majority of disinterested directors on the board. In such cases, even where the board delegates the litigation decision to a disinterested SLC, “a good deal of judicial oversight is necessary,” to temper the “structural bias” that may permeate a board when most of its members are interested and those who are not may be inclined to protect their fellow directors from liability.

**Houle’s heightened standard of judicial scrutiny of Massachusetts SLCs**

The *Houle* standard, employed by Gants in Boylan, calls for a searching review that asks, in essence, whether the decision of the SLC—or, if no SLC, that of the voting disinterested directors—was “reasonable and principled.” To answer that question, *Houle* sets forth a three-tiered test, well described by Gants in *Boylan* as follows:

1. whether the SLC (or other directors making the decision) was “independent, unbiased, and [acted] in good faith,” and, if so,

2. whether the SLC/independent direc-
tors conducted “a thorough and careful analysis,” and, if so,

(3) whether the decision was “contrary to the great weight of the evidence.”

Applying the facts of Boylan to this heightened standard, Gants found that BS&G’s de facto SLC had fallen short on the first two tiers of the test, which made an in-depth analysis on the final tier, whether the merits of the corporate decision were “contrary to the great weight of evidence,” unnecessary. On the first inquiry regarding the de facto SLC’s independence and lack of bias, Gants pointed out that these concepts are not the same as mere disinterest: A director may not meet the definition of being interested under the particular factual circumstances, yet may be susceptible to “pressures … to recommend dismissal of the [shareholder] action” that may raise questions of bias and lack of independence and therefore, “call for scrutiny of … members of a litigation committee.”

On the second inquiry, whether the de facto SLC conducted a “thorough and careful analysis,” Gants answered flatly, “no,” because the evidence BS&G could muster supporting a diligent investigation was virtually non-existent.

Harhen’s more deferential standard of judicial oversight of Massachusetts SLCs appointed by disinterested boards: diligent investigation is still required

In the widely-known Harhen decision of the Supreme Judicial Court, a case involving a group of policyholders’ derivative action against certain directors of the John Hancock Mutual Life Insurance Company, the court set forth the standard of judicial oversight applicable to a refusal of a shareholder demand when the SLC is comprised of disinterested members and is appointed by a board on which there is a majority of disinterested directors. As discussed above, in such cases, Massachusetts law treats the SLC decision to refuse the demand as a business decision that is protected by the business judgment rule. Therefore, unlike in cases governed by the heightened Houlé standard, Massachusetts courts will not delve into all the particulars of the SLC’s investigation, nor question whether the merits of the SLC’s decision was supported by sufficient evidence. However, as Gants pointed out in his Boylan decision, Harhen does require that a disinterested SLC appointed by a disinterested board still conduct a good faith investigation of some kind, lest the SLC and the board be deprived of the protections of the business judgment rule and face far more intense judicial scrutiny into their demand refusal decision.

Consequently, even a board in the comfortable position of facing a shareholder derivative demand that brings with it no hint of potential director interest or the taint of “structural bias” should not allow overconfidence, nonchalance or undue delay to pervade its internal investigation of the allegations. A timely, thorough and independent inquiry, conducted or aided by outside counsel and other such necessary professionals (e.g., independent accountants, appraisers, computer forensics experts), will buttress an already strong position enjoyed by the disinterested board and create a nearly impenetrable business judgment.

Delaware standard of judicial scrutiny of SLCs

Given the vast number of corporations maintaining a principal place of business in one state but incorporating in Delaware, it is worth summarizing the standard under Delaware law governing the adequacy of SLC investigations. As enunciated in the seminal case Zapata Corp. v. Maldonado, Delaware has adopted a more intense standard of judicial oversight than even the heightened Houlé standard in Massachusetts.

Specifically, an SLC must conduct an “objective and thorough investigation” into the claims of the derivative suit, and if the SLC determines that the action is not in the corporation’s best interests, it may file a motion to dismiss. The reviewing court then:

(1) inquires into the independence and good faith of the committee and the bases supporting its conclusions. The corporation holds the burden of showing independence, good faith and a reasonable investigation; then, additionally, and at the court’s discretion,

(2) applies its own independent business judgment to determine whether the motion to dismiss should be granted.

In short, for Delaware corporations facing derivative suits, the importance of commissioning a diligent and independent investigation aided by outside counsel is even more acute than for corporations chartered in Massachusetts.

Benefits of a timely, thorough, Independent internal investigation

Besides the direct benefit in the shareholder derivative context of winning a court’s assent to the board’s business judgment, a timely, thorough and independent internal investigation brings several other benefits in situations where allegations are lodged against (usually from within) a company. When planned and executed properly, an internal investigation can accomplish the following results:

(1) head off civil liability exposure to directors who might otherwise be alleged to have shirked their fiduciary duties;

(2) eliminate or reduce the scope of potential fiduciary breach or other wrongdoing. Such internal investigations are best discharged by outside counsel.

(3) minimize potential criminal liability for certain offenses by self-reporting violations (a factor considered under the Federal Sentencing Guidelines); and

(4) win the external public relations battle by highlighting to the media the company’s proactive approach.

Conclusion

As most recently highlighted by the Massachusetts Superior Court Business Litigation Session in the Boylan decision, there is no substitute for a timely, comprehensive and independent investigation when a corporation is faced with a shareholder derivative claim, or any internal allegation of fiduciary breach or other wrongdoing. Such internal investigations are best discharged with the prompt creation of a wholly independent SLC aided by outside counsel.
Following this course of action will not only help the company fully understand the validity of allegations lodged against it, but also will bring immeasurable value in protecting against a later attack on the adequacy of its internal investigation.

**Endnotes**

2. *Id.* at *13.
3. *Id.* at *10-*11.

4. Massachusetts, adopting the relevant provisions of American Legal Institute’s Principles of Corporate Governance, defines, in short, an “interested” director as one who (a) is a party to the transaction or conduct at issue; (b) has a financial or familial relationship with such party that would reasonably be expected to affect the director’s judgment in a manner adverse to the corporation; (c) has associates who have a financial interest in the transaction at issue that would reasonably be expected to affect the director’s judgment; or (d) is subject to a “controlling influence” on the board that could reasonably be expected to affect the director’s judgment in a manner adverse to the corporation. *See* Harhen v. Brown, 431 Mass. 838, 844 (2000). At an earlier stage of the case, the defendants’ unsuccessful motion to dismiss, the Superior Court excused the Dan Boylan Estate’s lack of pre-filing demand based on its having properly alleged self-interest by the directors. Boylan v. Boston Sand & Gravel Co., No. 02-2296-BLS2, 2007 WL 836753, *11 (Mass. Super. Mar. 16, 2007).

5. *Id.* at 847.

9. *Id.* at *1.
10. *Id.* at *1.
11. *Id.* at *1.
12. *Id.* at *6.
13. One of those disinterested BS&G directors was former Red Sox great Dom DiMaggio, a lifelong friend of Dean Boylan, Sr. *Id.* at *5. In his decision, Gants could not resist the aside that “my father-in-law still believes that Dominic was a better defensive outfielder than his more famous brother, Joe.” *Id.* at *5 n.6.
14. *Id.* at *11.


17. Other “universal demand” states ( i.e., where “demand excused” cases are no longer permitted) include each of the New England states except Vermont, as well as Arizona, Florida, Georgia, Hawaii, Idaho, Iowa, Michigan, Mississippi, Montana, Nebraska, North Carolina, Pennsylvania, South Dakota, Texas, Utah, Virginia, Wisconsin, and Wyoming. *See* Boland v. Engle, 113 F.3d 706, 712 (7th Cir. 1997); In re Guidant Shareholders Derivative Litigation, 841 N.E.2d 571, 574 (Ind. 2006).
21. Though not dispositive on the question of whether a majority of a board of directors is interested, close corporations ( i.e., closely-held (often family-held), non-public corporations) are likely to be hindered by a judicial assumption that they are ruled by an interested board. “The factors which contribute to making a corporation a close corporation may … bear on the independence and good faith of an [SLC] in such a corporation. To that end, a reviewing court should consider those factors in its inquiry.” *Id.* at 824, 825 n.11.
22. *Id.* at 824.
24. *Id.* at *12.
25. *Id.* at *13.
26. *Id.* at *13 (quoting *Houle*, 407 Mass. at 823).
27. *Id.* at *13.
31. *Id.* at 787-89.
Introduction

The traditional forum selection doctrine, hostile to choice of law provisions, has disappeared. In its place, a new doctrine, clothing such provisions with a presumption of validity, has taken its place. For some litigants, the costs of defending or prosecuting a case in a distant forum may be an effective bar to litigating at all.

The embrace of choice of forum clauses

The seminal case that marks the beginning of the elevation of forum selection clauses from an unenforceable attempt to “oust” a court from its jurisdiction to a virtually unassailable, irrevocable agreement is *M/S Bremen v. Zapata Offshore Company.* The case involved a towing contract that required a tow of an oil rig from the Gulf of Mexico to the Adriatic Sea. The rig was lost in a storm in the Gulf of Mexico. The agreement, negotiated in Europe, had a forum selection clause requiring arbitration in England. Zapata sued the towing company, Unterwesser, in the Federal Court of the Southern District of Florida, which denied Unterwesser’s motion to dismiss, on the grounds that the forum selection clause was ineffective.

The Supreme Court held that the District Court, in treating Unterwesser’s motion as a matter of *forum non conveniens,* had given “far too little weight and effect … to the forum clause in resolving this controversy. It reasoned, “We cannot have trade and commerce in world markets and international waters exclusively on our terms, governed by our laws and resolved in our courts.” The Court observed that the contract was made by two sophisticated business entities and that its performance required the rig to go through international waters and the waters of many different countries. The Court also suggested that if the forum clause were unreasonable and unfair, a court could decline to enforce it. The Court concluded that the party seeking to avoid the enforcement of a choice of forum clause must carry a “heavy burden” to establish that the clause was so unreasonable as to effectively deprive it of its day in court, was affected by fraud, undue influence or overweening bargaining power.

It found nothing in the record to support that heavy burden. Even in such a case, if it appeared (as in the case before the court) that the parties reasonably contemplated such an inconvenience, there would be little reason to relieve the parties from their agreement. The facts that the contract was the result of negotiation between sophisticated business entities and the international nature of this maritime contract drove the decision.

In later cases, courts have enforced clauses in contracts that had little or no international scope and were not negotiated in any meaningful sense. The defenses mentioned in the dicta of the *Bremen* decision — fraud, unfairness, overweening power — rarely have been effective. Commercial predictability appeared to have trumped them all.

Avoiding the forum selection clause in the federal courts—fraud in the inducement

*Scherk v. Alberto-Culver Co.* involved a claim of fraud in the inducement of a contract to license trademarks that Scherk, a citizen of Germany, falsely represented were unencumbered. The contract had a choice of forum clause that designated the International Chamber of Commerce in Paris for arbitration. Alberto-Culver sued for rescission. The Supreme Court reversed the decisions of the District Court and Court of Appeals for the plaintiff and held that the international nature of the contract and the U.S. Arbitration Act required recognition of the forum selection clause.

The Supreme Court stated in a footnote:

> In *The Bremen* we noted that forum-selection clauses ‘should be given full effect’ when ‘a freely negotiated private international agreement (is) unaffected by fraud’ … [citations omitted]. This … means that an arbitration or forum-selection clause in a contract is not enforceable if the inclusion of that clause in the contract was the product of fraud or coercion.

The *Bremen’s* footnote 14 has been the foundation of a virtually impregnable defense of forum selection clauses from claims of fraud in the inducement. The Arbitration...
The inducement renders a contract voidable. A fundamental principle of contract law is that fraud in the inducement renders a contract voidable only if the fraud induced the party entering into the contract to the terms of the contract for passage did not fairly allow the Casavants “the option of rejecting the contract with impunity” as did the contract in Shute. The court held that a passenger would not be bound to a forum selection clause unless given a reasonable time within which to reject the ticketing clause seems a weak argument. Federal Rule of Civil Procedure 9 and many state rules require that allegations of fraud be particularized. Those procedural rules combined with the power of the court to sanction, under Rule 11 bad faith allegations and even shift expenses (including counsel fees) should be protection enough. Moreover, with careful analysis, courts have been able to determine whether a claim was for fraud or breach of contract by discerning the true nature of the case through an analysis of the contracts and the relief that the plaintiff seeks.

Massachusetts—fraud in the inducement

The Massachusetts Supreme Judicial Court, in Jacobson v. Mailboxes Etc. USA Inc., explicitly accepted the U.S. Supreme Court holding in M/S Bremen v. Zapata Offshore Company and The Restatement (Second) of Conflict of Laws §80 (1988 revision) (“The parties’ agreement as to the place of the action will be given effect unless it is unfair or unreasonable.”), abandoning its older precedents disfavoring choice of forum and choice of law ex ante agreements. In Jacobson v. Mailboxes, the Supreme Judicial Court dealt with a franchising contract that stipulated two provisions: First, that the contract was to be construed under and governed by the laws of California, and second, that California was to be the forum to enforce the contract. The plaintiff claimed that he was led into the contract by fraud and that the defendant had engaged in the pre-contract violations of G.L. c. 93A and breached various obligations of the franchise agreement.

The Supreme Judicial Court held that if the pre-contract claims were not contract claims mislabeled “fraud,” California would not recognize and enforce a choice of forum clause in an action based on pre-contract wrongs. The Court remanded the case with instructions to the Superior Court to determine if “the greater focus of the plaintiff claims” was on the defendants’ misleading conduct that induced the agreement” and other unfair or deceptive pre-contract conduct. If so, “the judge should not enforce the forum selection clause by banishing contract enforcement claims to California for separate treatment,” otherwise it should decline, on the grounds of forum non conveniens, to permit any part of the action to be maintained in Massachusetts.

The defendant cited Scherk arguing, unsuccessfully, that “unless there is some showing that fraud or undue influence induced the party opposing a forum selection clause to agree to inclusion of that provision (emphasis in the original), a general claim of fraud or misrepresentation as to the entire contract does not affect the validity of the forum selection clause.” Enforcing a forum selection clause in the face of well-pleaded, specific allegations of fraud seems to be contrary to the public policy of requiring good faith and fair dealing in every contract. In at least one egregious case, the Federal Trade Commission has held that the use of a forum selection clause as part of a pattern of oppressive and fraudulent business dealings was a violation of the Federal Trade Commission Act by Leasecomm, a business opportunity lender.

Defenses to forum selection clauses — when enforcement is unreasonable and unjust

Many courts have said, but few cases have held, that a forum selection clause in an oppressive and unreasonable contract of adhesion is unenforceable. Establishing that a contract with a burdensome forum selection clause is a contract of adhesion may be a necessary element for the avoidance of the disadvantageous forum, but it is rarely a sufficient one.

In Casavant v. Norwegian Cruise Line, Ltd., the Appeals Court refused to enforce a choice of venue forum tucked away in the back of a ticket. In that case, the defendant sent the ticket to the customer only two weeks before the scheduled departure on Sept. 16, 2001. The Casavants, about a week after having received the tickets, asked that they be allowed to reschedule the cruise because of their anxiety for safety following the Sept. 11 attack on the World Trade Center. The court distinguished Shute on the basis that “the manner and means of the delivery of the terms of the contract for passage did not fairly allow the Casavants “the option of rejecting the contract with impunity” as did the contract in Shute. The court held that a passenger would not be bound to a forum selection clause unless given a reasonable time within which to reject the ticketing
contract and forum selection clause without incurring disproportionate penalties.

Few cases have spelled out the factors that determine whether a forum selection clause is fair and reasonable. Judge Bruce M. Selya of the Court of Appeals for the First Circuit, while a District Court judge, distilling federal cases, endeavored to do that in D'Antuono v. CCH Computax Systems, Inc.\textsuperscript{22} Some of the factors are the relationship of the contract to the selected forum—what law governs the contract, where the contract is to be performed and where it was executed.\textsuperscript{24} The relationship of a party seeking enforcement of a forum selection clause with the contractually designated forum is another factor of some importance.\textsuperscript{25} One factor that should weigh heavily is the importance of the forum selection clause to the agreement taken as a whole.\textsuperscript{26} Some courts have weighed the fairness of the forum and the public policy of the forum chosen by the plaintiff (if different from the contractually selected jurisdiction).\textsuperscript{27} No one factor, other than perhaps violation of a strong public policy, fraud or gross oppression, appears to be determinative.

**Forum non-conveniens\textsuperscript{28} — and other escape hatches**

Courts may refuse to enforce a forum selection clause when the burden on one party is truly oppressive.\textsuperscript{29} If there is also no rational connection between the contractually chosen forum and the contract or its performance, courts have used *forum non conveniens* as the tool to avoid enforcing an oppressive forum selection clause, such as in United Rentals Inc. v. Pruett.\textsuperscript{30} In Pruett, the District Court, relying on Stewart Organization Inc. v. Ricoh Corporation, 487 U.S. 22 (1988), in which the Supreme Court held whether a clause would be transferred was a federal question, governed by statute and not by state law or the contract between the parties, refused to enforce the forum selection clause. The Supreme Court had held that although an enforceable forum selection clause should be the significant factor on whether to transfer the case to another district, a district court must take into account other important considerations other than those that bear solely on the parties. These various factors — convenience of the witnesses, systemic integrity, fairness — come under the heading of the “interest of justice.”\textsuperscript{31}

Because the Pruett had no contacts with Connecticut and all other relevant contacts with California, the District Court found no interest of justice factors that favored keeping the case in Connecticut. Of particular importance to the court was that California had a particular interest in the issues of the case because California held that restrictive covenants and employment contracts were contrary to its public policy. The court combined traditional *forum non conveniens* analysis with consideration of the interest of the state where the contract was performed.

In Lata Laundry, Inc. v. Daniels Equipment Company, Inc.\textsuperscript{32} the defendant, using very aggressive and somewhat disingenuous sales tactics, took an order from the plaintiff for laundry equipment. After the plaintiff signed the order, the defendant gave him a copy of the order that had on its back a “boiler plate” forum selection clause, naming New Hampshire as the forum where any dispute must be litigated. Judge Raymond J. Brassard refused to enforce the clause. He reasoned that the court must look to the law of the selected state to see if the clause would be enforced. New Hampshire had adopted the Uniform Model Choice of Forum Act. The New Hampshire Supreme Court in Stafford Technology, Inc.\textsuperscript{33} had held that the purpose of the statute was “to enforce forum selection clauses that are bargained for by contracting parties.”\textsuperscript{34} Since the parties did not bargain for the forum selection clause, the judge concluded that New Hampshire would not enforce it. Therefore, a Massachusetts court should not implement it.\textsuperscript{35}

*Forum non conveniens* in Massachusetts is governed by its Long Arm Statute, which provides in its relevant part, “When the court finds that in the interest of substantial justice the action should be heard in another forum, the court may stay or dismiss the action in whole or in part on any conditions that may be just.”\textsuperscript{36} However, the court can impose conditions to assure that the plaintiff will have a suitable forum, such as requiring the defendant to waive the statute of limitations defense. When considering a motion to dismiss, the most important issue for a Massachusetts court is the availability of another suitable forum. Green v. Manhattanville College.\textsuperscript{37}

**Perceived ambiguity**

When there is a great disparity of power between the parties, the forum selected in the contract bears little relationship to the dispute and the choice of forum appears to be burdensome or unfair, courts have found ambiguities in the clauses, which they construe against the clause.\textsuperscript{38} The word “may” will often prevent a party from suing in a different court from that specified in the contract. Even the word “shall” may not be determinative. Thus, a clause that states that courts of a particular jurisdiction “shall” have jurisdiction over any dispute may be read as non-exclusive of other jurisdictions. In King v. PA Consulting Group,\textsuperscript{39} a case in which the consulting firm attempted to enforce a non-compete agreement, the employer sought to enforce a forum selection clause that provided:

This agreement and all matters arising in connection with . . . shall be subject to the jurisdiction of the New Jersey Courts.

The court held that the contract provision only meant that the jurisdiction of the New Jersey courts was unchallengable, but it did not require that venue was exclusive in New Jersey.\textsuperscript{40} A year earlier, the court, citing a dictum in Paper Express, Ltd. v. Pfankuch Maschinen GmbH,\textsuperscript{41} stated:

Generally speaking, the courts that have addressed the issue are in agreement that where venue is specified [in a forum selection clause] with mandatory or obligatory language, the clause will be enforced; where only jurisdiction is specified [in a forum selection clause], the clause will generally not be enforced unless there is some further language indicating the parties’ intent to make venue exclusive.\textsuperscript{42}

Would not predictability be better served if courts, rather than straining to find ambiguities, explicitly declined to enforce forum clauses that were unfairly and unreasonably burdensome to one of the parties or had the effect of diminishing substantive rights? If courts were explicit about the reasons for the refusal to enforce these clauses, they would
articulate principles that guided their decisions. If parties knew the kinds of circumstances and the boundaries of acceptability for these clauses, they could draft clauses that would withstand critical scrutiny.

It is noteworthy that both Pruett and King involved attempts by an employer to prevent an employee from working for a competitor. Just as courts approach differently non-compete clauses when the ability of an employee to earn a living is at issue than when the seller of a business agrees not to compete against the buyer, the nature of the litigation often does and should affect how a court handles a forum selection issue.

Conclusion

Forum selection clauses are useful and, in this writer’s judgment, salutary devices to enhance predictability, so necessary for commercial life. Enforcement of these clauses also validates the important liberty of freedom of contract. On the other hand, courts need to recognize that fairness and honesty are also important, not only as moral imperatives, but as lubricants for the functioning of commerce. The existence of the Federal Trade Commission Act and the many state “little” FTCAs are ample evidence of the strong public policy favoring fairness and honesty in business dealing. Public confidence in the business community, now at a nadir, is not enhanced by the rigorous enforcement of contract provisions so oppressive that they effectively prevent the redress of wrongs. Forum selection clauses in consumer contracts should be enforced if there is complete openness and disclosure.

Endnotes

2. *Id.*
3. *Id.* at 9.
4. In *Hourihan v. GT Group Management SDN BHD et al.*, the court in the Business Litigation Session upheld a forum selection clause in a severance agreement between a Massachusetts resident and a Malaysian corporation on the grounds that the contract was an international contract negotiated by sophisticated parties who were aware of the clause. *Hourihan v. GT Group Management SDN BHD et al.*, 02-1255 BLS (Super. 2002) http://sociallaw.gvpi.net/sll/lpext.dll/sll/lblt?templates&fn=main.htm
7. *Scherk*, 417 U.S. at 519 (The Court characterized the arbitration clause as a “specialized” forum selection clause).
8. *Id.* at 519 n. 14.
10. *Int'l Harvester Co. of America v. Rieke* 9 F. 2d 776, 780 (1925). See also *Strong v. Repide* 213 U.S. 419, 429 (1909); *Nash v. Trustees of Boston University*, 946 F.2d 960, 966 (1st Cir. 1990) (“We discern no sound reason that a failure to satisfy so central a contract principle, foreordaining the absence of any meaningful meeting of the minds, should not be considered a baseline element in any coherent body of federal common law developed under the congressional charter implicit in ERISA.”).
14. *Supra.*
17. *Id.* at 21.
22. *Id.* at 788.
24. *Id.* at 712.
25. *Id.* at 714. See also *Granger & Sons, Inc. v. Rozac Co.*, 885 F. Supp. 319 (D. Mass. 1995) (Massachusetts general contractor with projects in many states and subcontractors from different states on each project).
29. The financial difficulty that a party might
have in litigating in the selected forum is not a sufficient reason, by itself, for refusal to enforce a valid forum selection clause. E.g. Bonny v. Soc'y of Lloyd's, 3 F. 3d 156, 160 (7th Cir. 1993); Moses v. Bus. Card Exp., Inc. 929 F.2d 1131, 1138-39 (6th Cir., 1991); However, great disparity of financial resources is a factor that courts do consider when faced with a motion to transfer under 28 U.S.C. §1404(a). Compare Holmes v. Freightliner, LLC, 237 F. Supp. 2d 690, 692 (M.D. Ala. 2002) (a factor) and Houk v. Kimberly Clark Corp., 613 F. Supp. 923, 929 (D. Iowa 1985) (a factor, but not entitled to great weight).


31. Id. at 228.


34. Lava, 18 Mass. L. Rptr. at 1.


40. Judge Van Gestel, sitting in the Business Litigation Session of the Massachusetts Superior Court in a commercial performance bond case, ruled that the use of the words “shall...only” be instituted in the courts of Florida was mandatory. Ionics, Inc. v. Liberty Mutual Insurance Company 15 Mass.L.Rptr. 508, 2-3 (Mass. Super. Ct. 2002).


42. K & V Scientific Co., Inc. v. Bayerische Motoren Werke Aktiengesellschaft, 314 F.3d 494, 499 (10th Cir., 2002). But see Davis Media Group, Inc. v. Best Western Int'l, Inc., 302 F. Supp.2d 464, 468-69 (D. Md. 2004) (“[A]ll suits...shall be subject to the jurisdiction of the Courts...of Arizona” held to be a “mandatory” forum selection clause.). This case should be viewed with caution. Most of the cases it relies on are distinguishable.

43. E.g., Boulanger v. Dunkin' Donuts, 442 Mass. 635, 639 (Mass. 2004); H & R Block Tax Services, Inc. v. Circle A Enterprises, Inc., 269 Neb. 411, 417, 693 N.W.2d 548, 554 (Neb. 2005) (“Nebraska courts are generally more willing to uphold promises to refrain from competition made in the context of the sale of goodwill as a business asset than those made in connection with contracts of employment”).
Practical implications of the electronic discovery-related Federal Rules of Civil Procedure amendments

By Grace Bacon Garcia, Esq., and Kenneth V. Nourse, Esq.

While the recent Federal Rules of Civil Procedure amendments concerning electronic discovery have not changed what constitutes electronic evidence best practices, the mandatory early examination of electronic discovery-related issues in federal litigation raises several new considerations. The following are three examples of issues to which practitioners should give some attention early in the case.

I. Be proactive with your clients

Even before your client is under a duty to preserve documents as the result of either litigation or an investigation, outside counsel should reach out proactively to clients to determine what the client’s document retention policy is and how that policy is actually implemented in practice. Be aware that, more often than not, a discrepancy exists between the policy as written and as technically implemented. Because of this discrepancy, e-mails, files stored on file shares, and loose files and archived e-mails stored on employees’ laptops and desktops persist despite having a creation date well beyond the official retention period.

This, of course, leads to electronically stored information (ESI) that should have been destroyed in compliance with the retention policy having to be preserved and ultimately produced if relevant and not privileged. It is not uncommon, for example, for companies that employ a third-party, offsite, Internet-based e-mail archiving solution to rely unknowingly on that third-party’s default retention period, which is often not in sync with the company’s. Consequently, counsel need to work with their clients to ensure that the document retention policy is in fact being followed in order to avoid additional costs and time when litigation arises.

In the absence of a retention policy, counsel should encourage and facilitate the creation and implementation of one. Failing that, counsel would serve a client well to at least learn how that client determines what electronic information is retained and how decisions are made to discard that information. Of course, the entire point of these efforts is to ensure that your client has on hand only as much ESI as is necessary for business purposes.

II. Removal considerations

When a case is filed in state court, one early decision a defendant makes is whether to remove the case to federal court. After determining whether the case meets the jurisdictional requirements, there are several other factors considered in deciding to remove. For instance, a decision to remove may be made based on a belief that a federal court judge may be better able to handle your case, or decide a dispositive motion. Removal also may be made if an attorney believes he or she would obtain a more conservative jury in federal court than in the state court. Also, one may remove if one believes that the Federal Rules of Procedure will benefit their client in the progress of the case. Attorneys have always assessed what rules of
procedure — the state or federal — would be more advantageous to their client in deciding whether to remove a case from state to federal court. Now that the Rules of Civil Procedure have been amended, however, this determination may be more critical as the amendments place clear burdens on parties and their counsel.

Some state courts, such as Texas, have already promulgated rules that include ESI discovery issues. See, e.g., Tex. R. Civ. P. 193.3 and 196.4. Other states have not adopted any new rules that specifically address ESI. Regardless, in August 2006, the Conference of Chief Justices approved Guidelines for State Trial Courts Regarding Discovery of Electronically-Stored Information. These guidelines, which were disseminated to all state trial courts, “are intended to help reduce uncertainty in state court litigation by assisting trial judges faced by a dispute over e-discovery in identifying the issues and determining the decision-making factors to be applied.” Although the guidelines are quite similar to the federal amendments, the difference is that the guidelines are not rules and thus, unlike the federal amendments, cannot be counted on to be followed in each case.

Whether the case is in state or federal court, parties have clear discovery and preservation obligations, and the issues of spoliation are the same. However, the way in which the rules, guidelines (if implemented) and case law handle these obligations may give counsel significant considerations in deciding whether to remove a case from state to federal court.

As a result, ESI issues may be handled quite differently in state court than in federal court. The federal rules can be very onerous on parties and their counsel. Depending on the state court, the court may not place the same burdens on parties. Counsel needs to find out whether the particular state court is following the guidelines on a routine basis, or if they are simply treating ESI in the same fashion as all other discovery. Thus, in deciding whether to remove, attorneys should assess which court, the state or federal, will be more receptive to arguments for cost shifting or for limiting discovery.

Additionally, if the state court does not require automatic disclosures, and if the client is not quite up-to-date with respect to ESI, it may be better to stay in state court, to avoid the federal automatic disclosures of ESI and give both counsel and the client more time to assess, gather, review and produce the necessary information.

As stated above, the implantation of the rule amendments makes this a good time to get in touch with your clients, if you have not already, to learn about their document retention policy and determine if they are in fact following their policy. Determining whether your client is on the ball with ESI issues, or whether your client needs more time to properly deal with such issues, is important to your assessment of whether to remove a case to federal court.

III. Settlement considerations

An early assessment of a client’s ESI facilitates a better grasp of the client’s settlement position as well. Before the amendments, counsel usually would not delve into the specifics of what ESI the client may have on hand until discovery had already begun. This, however, has changed. An upfront inventory of a client’s ESI in preparation for the Rule 16 meet and confer allows for more accurate estimates of costs associated with the collection, filtering, processing, review and production of ESI. Prior to the amendments, often these costs were not fully understood when counsel and client waited until discovery was underway to face the issue. On many occasions, counsel and client were surprised well into the game to learn of the sheer volume of potentially relevant ESI for review and ultimate production. Thus, the new amendments require parties to think about these costs at the start of litigation.

In addition to the direct costs, clients may be faced with the necessity of paying a significant retainer to hire a reputable company to deal with all or some of the collection, processing and hosting of ESI for review. The assessment of the ESI-related cost is germane, first, to assessing the client’s settlement strategy and position, and second, to calculating an accurate settlement offer if and when figures were discussed. This consideration allows counsel and client to operate with more complete information in settlement negotiations.

For example, knowing the extent and nature of a client’s ESI and costs associated with handling that ESI may lead to a settlement offer augmented by $25,000 to stave off potential ESI-related costs of $50,000. The early assessment of costs is critical to all parties who may have to pay these ESI discovery costs up front. Accordingly, in order to make better economic decisions regarding a case, settlement options should be thoroughly assessed early on, based on the cost of litigation, which may be significantly increased due to ESI.
Using health care law to overcome obstacles to service for children with mental health needs – Health Law Advocates Inc.’s experience in the juvenile courts

By Rebecca J. Rodman

Health Law Advocates Inc. is a public-interest law firm affiliated with Health Care For All, a statewide consumer advocacy organization that promotes health care reform in Massachusetts. Founded in 1996, HLA is committed to ensuring universal access to quality health care in Massachusetts, particularly for those most at risk due to such factors as race, gender, disability, age or geographic location. HLA’s mission is to provide legal representation to vulnerable Massachusetts residents who are at or below 300 percent of the federal poverty line who have been denied access to health care.

The surgeon general has reported that 4 million children and adolescents suffer from a major mental illness, and that less than 20 percent of those children receive the mental health treatment or services they need. HLA has learned that Massachusetts is not immune to this problem and is failing its children with mental illnesses.

HLA has witnessed firsthand the difficulties families have accessing services when their children are mentally ill. There are numerous barriers that prevent families from getting their children much needed mental health services. Among them are the dearth of child psychiatrists, psychologists and social workers; the perception that treatment is ineffective; the stigma associated with mental health services; and the cost of treatment. In response to this need, HLA created the Children’s Mental Health Access Project. The project’s goal is to use HLA’s broad experience in legal advocacy to expand and improve the delivery of mental health services to children throughout Massachusetts.

To achieve this goal, HLA has developed a multi-pronged approach: (1) Provide direct representation to children who are being denied access to mental health services; (2) Establish a network of pro bono attorneys who will accept children’s mental health access cases and provide those attorneys with training and support; and (3) Identify systemic problems that inhibit access and challenge them through class action lawsuits and other broad legal strategies.

As part of the project, HLA represents children with unmet mental health needs who appear in juvenile court in Fitchburg and Dudley, Massachusetts. These children evidence the enormous social cost of not treating childhood mental illness, and the simple fact that children whose mental illnesses are not treated often enter and remain in the juvenile justice system and then later become embroiled in the adult criminal justice system. Indeed, there is a high rate of major mental illness among children in the juvenile justice system, and most of the children so afflicted are not receiving services. One study found that 20 percent of those in the juvenile justice system had a major mental illness or serious emotional disturbance, and another study reported that between 40 percent and 50 percent of the children in the juvenile justice system have some form of mental illness.

Judge Luis Perez, who presides over the Worcester County Juvenile Courts, has recognized this significant problem. He reports that many of the children who appear before him in the juvenile court are in need of mental health services, but they lack legal representation to help them obtain the services they are entitled to under state and federal laws. Although their attorneys are zealous advocates, they simply do not have the expertise in health law or experience working with state agencies to ensure that the children they represent receive the mental health services they need. As a result of their unmet mental health needs, many of these children end up in the custody of the Department of Social Services (DSS) or incarcerated in a Department of Youth Services (DYS) facility.

To keep these children in their homes rather than in the custody of the commonwealth...
or incarcerated, two things are critical: (1) the mental health care services themselves, and (2) advocates to help the children and their families access those services. Perez approached HLA about these issues, and together, we created the Fitchburg and Dudley Juvenile Court Projects as part of the larger Children’s Mental Health Access Project.

**Juvenile Court Project — mental health guardians ad litem**

HLA staff regularly attend juvenile court sessions in both Fitchburg and Dudley. By maintaining a presence in those courts, HLA has become known to the attorneys and advocates (as school counselors and DSS social workers) who appear before the juvenile courts, as well as the probation officers and court personnel. Juvenile court judges now often appoint an HLA attorney as guardian ad litem (GAL) when a child who may have unmet mental health needs appears in court on a delinquency matter or after a Child In Need of Services (CHINS) petition has been filed. The GAL’s charge is to work with the child’s attorney and the other professionals involved in the child’s life to determine if there are unmet mental health needs, and if so, what those needs are and who should be providing those services. After making those determinations, the GAL works to make sure the services are actually provided to the child.

The GAL, who is not paid, does not represent the child in the delinquency or CHINS matter and does not represent the parents or guardians. Instead, the GAL is responsible to the court to ensure that the child’s mental health needs are met. This division of responsibilities ensures that the GAL’s focus is on the best interests of the child in terms of mental health services, and allows the child’s attorney to focus on the legal issues before the court. Although HLA attorneys are not mental health clinicians, they are well experienced in making sure mental health services are in fact provided, and in a timely manner. HLA reports to the court not only on what services are needed, but also what progress is being made in getting those services to the child.

The project started in the Fitchburg Juvenile Court in 2005, expanded to the Dudley Juvenile Court in September 2006 and has achieved positive results. One indicator of the success of the project is that the attorneys who regularly appear in those courts and have seen the results HLA has obtained have begun requesting that those courts appoint a mental health GAL when they have a client with unmet mental health needs.

**Using health care laws to assist children in the juvenile justice system**

The children HLA has represented have a variety of unmet mental health needs, and the strategies for meeting those needs also vary. The premise underlying HLA’s work is that children who are mentally ill must get appropriate, timely and effective mental health services. To reach this goal, HLA negotiates with private and public insurers, state agencies that work with children, such as DSS and the Department of Mental Health (DMH), and mental health care providers.

**Public health insurance**

Children who have health insurance, whether public or private, are entitled to an array of mental health services. However, many families are not aware of their children’s rights and are not aware of how to advocate to ensure the insurers provide covered services. HLA has expertise in both public and private insurance matters and has successfully used that expertise to benefit children in the juvenile justice system.

Children who are on the commonwealth’s Medicaid program, called MassHealth, have a very broad entitlement to medically necessary mental health services. There is a federal mandate called Early, Periodic Screening, Diagnostic & Treatment Services (EPSDT) that requires that states that accept federal Medicaid funds must provide all Medicaid members under the age of 21 with certain services (including vision and dental) that are medically necessary to correct or ameliorate physical and mental illnesses discovered by the screening services, and provide them in a timely manner. This is a wide-reaching mandate, and if a child who appears before the juvenile court has MassHealth and is not receiving needed mental health services, HLA attorneys pursue those services immediately and aggressively.

In order to comply with the EPSDT mandate, MassHealth enacted a regulation that states that if a child needs a medically necessary service that is not already specifically included as a covered service under MassHealth regulations, a provider may submit a request for prior authorization for the service. Unfortunately, many providers are unaware that they can request payment for a service that is not listed, so HLA helps to make them aware of this regulation and encourages them to submit such requests.

**Private health insurance**

Private health care insurers also must provide a range of mental health services and do so in a reasonable time period. However, getting services in a reasonable time period is one of the biggest hurdles for children with mental illness, because there are very few providers who specialize in treating children, and even fewer of these accept health insurance of any kind. In fact, months-long waiting lists are common for children seeking psychiatric services. Because children in crisis cannot wait that long, HLA attorneys fight to break down these barriers.

For example, “CG,” a 15-year-old girl, appeared before the juvenile court on a CHINS petition brought by her school after she had been repeatedly absent. CG had become severely depressed and rarely left her room at home. She would not attend school, socialize with her friends or participate in family life. Everyone was concerned for her safety and well-being and agreed that she needed to see a psychiatrist experienced in treating adolescents suffering from depression. CG’s insurer provided the family with a list of six psychiatrists who purportedly treated adolescents. However, of the six, one no longer accepted that insurance; two were not accepting new cases; two did not treat anyone under 18 years of age; and the last one had a waiting list of eight months. CG’s parents put her name on the long waiting list, began waiting and worried. It was at this stage that CG appeared in juvenile court and an HLA attorney was appointed as GAL. The HLA attorney contacted CG’s insurance company and convinced it to request that one of the psychiatrists who was not accepting new cases agree to see CG. Within two weeks, CG had seen the psychiatrist and was making sig-
significant, positive strides.

Had CG's insurer been unable to find a psychiatrist in its network willing to treat her, HLA would have insisted that the insurer agree to pay an out-of-network provider to work with CG. There are several legal arguments that can be used in such negotiations. The Massachusetts Health Insurance Consumer Protection statute and the Massachusetts Mental Health Parity Law require that providers offer, on a nondiscriminatory basis, adequate access to a full range of services for mental health needs. Requiring a deeply depressed child to wait eight months before seeing a psychiatrist likely does not comply with this requirement. Also, an insurer that holds itself out as possessing a full range of services for mental health needs, when in fact none of those providers are accepting new patients, may be engaging in an unfair and deceptive business practice under M.G.L. Ch. 93A.

State agencies

Many, if not most, of the children who appear in juvenile court do not have health insurance. Instead, they receive mental health services through a state agency, most often DSS. HLA attorneys regularly help children and their representatives navigate the bureaucracies of the state agencies. The greatest barrier to getting help through state agencies is navigating the system itself. Although DMH would appear to be the agency most likely to help children with mental illness, very few children are actually receiving adequate services through DMH. Even a child eligible for DMH services is not entitled to those services unless DMH determines that the child cannot receive similar services from another source (e.g. a private insurer, DSS or the child's school). In addition, DMH services are subject to funding on a geographic basis, so even if a child is eligible and needs the services, DMH might not have services available in that child's location. In several such instances, HLA attorneys have pushed DMH to ensure that the eligible child actually receives the services he or she needs.

Many more families turn to DSS, rather than DMH, for assistance with their mentally ill children. With DSS, the difficulty is not obtaining eligibility for a child, but getting him or her the appropriate services, which is highly dependent upon identifying the mental illness from which the child suffers. The following example helps explain this difficulty.

Children who appear in juvenile court pursuant to a CHINS petition are often placed in the custody of DSS. The DSS social worker assigned to a particular child's case must create a service plan describing in detail the tasks to be undertaken and the services to be provided to either strengthen the family unit, provide an alternative permanent home for the child or enable a mature minor to live independently. But DSS's regulations do not require any type of mental health evaluation, let alone a full diagnostic evaluation. The only circumstances under which DSS is required to conduct a specific diagnostic evaluation are when DSS places a child who has sexually abused someone or committed arson in a foster-care home.

Without a mental health evaluation, the accuracy of any diagnosis is dubious. And, without an accurate diagnosis, DSS cannot, and frequently does not, identify the appropriate placement or services for a child in its custody. This means that families which have turned to the court and DSS through the CHINS process to obtain necessary mental health services for their children have no assurance that DSS will recognize the need or provide the services.

The details of a recent case elucidate well this problem. An HLA attorney represented "RC," a 14-year-old girl who had been in DSS custody for more than six months at the time of the appointment. DSS took custody after RC assaulted her mother during a family therapy session, and then moved her from one failed placement to another. Each placement failed because of RC’s behavioral issues. RC is mentally ill, but instead of recognizing that her behavioral problems stemmed from her mental illness, a DSS social worker assigned to RC's case overlooked her mental illness and stated repeatedly, both in juvenile court and in team meetings, that the problem with finding a stable placement for RC was entirely RC's fault.

When RC had first appeared in juvenile court on a CHINS petition, Judge Perez ordered the Worcester County Juvenile Court Clinic to evaluate her. The clinician recommended that she undergo an intensive diagnostic evaluation and predicted that the evaluation would conclude that RC needed a long-term placement in a therapeutic residential setting. Unfortunately, DSS ignored the clinician's recommendation. After RC bounced from one foster home to another, DSS sent her back home to her biological mother, although there had been no improvement in RC's behavior. RC was then charged with assault and battery stemming from another fight, and ended up in the custody of the Department of Youth Services. The HLA GAL assigned to RC encouraged DSS to conduct psychiatric diagnostic evaluations in order to develop a long-term treatment plan. Eventually, the GAL's persistence paid off, and DSS arranged for the evaluations. Once the evaluations were completed, it was clear that RC needed intensive therapeutic services and a focused residential program. When she was released from DYS custody, DSS placed her in an excellent community group home with therapeutic services on-site. RC is now doing very well in that placement.

In RC's case, as in the case of many children in DSS custody, once the diagnosis was made, there was no debate about what kind of placement and services were needed. However, without the intervention of an HLA attorney, RC likely would have continued to bounce around from foster care to shelter care to DYS and back again, repeatedly found herself in trouble with the law, and never received the care she needed.

To help RC, HLA needed to persist with one agency until the agency gave the child the services she needed. In many instances, however, children need help navigating among several different agencies. In those cases, it is vital that the family have the assistance of an attorney who is familiar with the resources and eligibility requirements of all the relevant agencies. An attorney who understands health law and state agency regulations can bring all the potential providers to the table to help get the child all the services to which the child is entitled. Working with each service provider separately likely will not give the child as comprehensive a service plan as working with all the providers in a unified way and pulling together services from the different sources.

Conclusion

Children with mental health needs face a
variety of obstacles to getting proper and effective services. Even when services are available, without an advocate who is familiar with the laws and regulations governing the various service providers, a child may not receive the appropriate services, or receive them soon enough to prevent dire consequences, such as progressively worsening mental illness, failure in school and incarceration. HLA’s Juvenile Court Project has successfully broken down barriers for a number of children. As we reach out to additional courts and train other attorneys to represent children with mental health needs, we hope that more children will receive much-needed mental health treatment.
Introduction

In April 2007, the U.S. Supreme Court announced its ruling in Gonzales v. Carhart, 127 S.Ct. 1610 (2007), its most recent decision on abortion restrictions. The controversial 5-4 decision upheld the Partial-Birth Abortion Ban Act of 2003 (codified at 18 U.S.C. §1531), a federal law prohibiting a specific abortion procedure usually reserved for the second trimester. Justice Anthony M. Kennedy wrote the majority opinion, to which Chief Justice John G. Roberts Jr. and Justices Antonin Scalia, Clarence Thomas and Samuel A. Alito Jr. joined. Justice Ruth Bader Ginsburg wrote the dissenting opinion to which the remaining three justices joined.

Gonzales is the Roberts court’s first foray into the highly charged abortion-jurisprudence battle and the first case decided by the Supreme Court upholding a legislative ban of a specific abortion procedure. Supporters of both the pro-life and pro-choice movements have called Gonzales a landmark decision and expect that the case will have a significant impact on abortion law in the future, from both the legislative and judicial perspectives.

This article examines the legislative and judicial paths leading up to Gonzales, reports the highlights of the decision, and discusses both the practical implications of the decision and the future of abortion law.

Background on abortion

Before turning to the Gonzales decision itself, some background on abortion and the Court’s prior decisions is helpful to better understand the import of the Court’s ruling.

According to The New England Journal of Medicine, 35 percent of women in the United States undergo an abortion before they reach 45 years of age, and approximately 90 percent of abortions are performed during the first trimester (0-12 weeks). Only a very small percentage (estimated at less than 1 percent) of abortions are performed after viability begins, which is usually between 24 and 28 weeks.

During the first trimester, most abortions are performed using a method whereby a vacuum tube is inserted into the woman’s uterus and suctioned out the fetus. But, once a fetus is approximately 12 weeks old, it has usually grown too large for this procedure to be successful, and surgical options are preferred. The most commonly performed second-trimester (13-27 weeks) abortion procedure is called dilation and evacuation. D&E is a generic term for a variety of surgical procedures and accounts for about 95 percent of all abortions performed from 12 to 20 weeks. Although there are variations of D&E, the procedure usually involves dilating the woman’s cervix, reaching into her uterus and grasping the fetus with forceps and pulling. When the fetus becomes lodged in the cervix, the friction causes the fetus to tear apart. The fetus is then taken out piece-by-piece until it is completely removed. In most instances, the fetus is torn into 10 to 15 pieces, and it bleeds to death. At the end of the procedure, the physician suctioned or scrapes out any fetal material remaining in the woman’s uterus.

One particular variation of D&E is termed dilation and extraction, or intact D&E, and it is generally used only between 20 to 24 weeks. What differentiates D&X from D&E is that with D&X, the physician collapses the fetus’ skull (because it is too large to pass through the cervix) and then extracts the fetus intact or largely intact, rather than removing the fetus piece-by-piece. Because some of the fetus’ body parts are outside the woman when the physician performs the specific act that kills the fetus (i.e., collapsing the skull), this abortion method is referred to by some as a “partial birth” abortion. I will refer to this procedure as D&X, as the Supreme Court did in the first case in which
it dealt with this procedure, and because, as Ginsburg has noted, the term “partial-birth abortion” is neither recognized in the medical literature nor used by physicians who perform abortions. Estimates of the number of D&amp;X abortions performed annually range between 640 and 5,000.

The path to Gonzales v. Carhart — Roe, Danforth, Casey and Stenberg

In Roe v. Wade, 93 S.Ct. 705 (1973), the Supreme Court first declared the constitutional right to an abortion and it created a framework, divided into the three trimester periods of a pregnancy, by which future abortion restrictions would be evaluated. Three years later, in Planned Parenthood of Central Mo. v. Danforth, 96 S.Ct. 2832 (1976), the Court invalidated a Missouri ban on the then-primary method of second-trimester abortion, in part because it forced women to terminate pregnancies in the second trimester by a method that was more dangerous to their health than the method banned.

Some erroneously predicted that Roe would be overturned by the Supreme Court in 1992 when it decided Planned Parenthood of Southeastern Pennsylvania v. Casey, 112 S.Ct. 2791 (1992) and was presented with challenges to a variety of abortion restrictions enacted by the Commonwealth of Pennsylvania, some of which the Court found constitutional and others unconstitutional. In Casey, although the Court did reject Roe’s trimester framework, it reaffirmed Roe’s central holdings that a state may not prohibit abortion prior to viability, and that subsequent to viability, a state may regulate or ban abortion altogether, except where it is necessary for the preservation of the life or health of the mother.

Less than a decade later, the Supreme Court grappled, for the first time, with the constitutionality of a legislative ban on D&amp;X. Stenberg v. Carhart, 120 S.Ct. 2597 (2000). The Nebraska law outlawed “partial birth abortion,” which it defined to mean “deliberately and intentionally delivering into the vagina a living unborn child, or a substantial portion thereof, for the purposes of performing a procedure that the person performing such procedure knows will kill the unborn child and does kill the unborn child.” The statute classified a violation as a Class III felony, authorized a prison term of up to 20 years and provided for an automatic revocation of a doctor’s license to practice medicine in Nebraska. Although the law contained an exception allowing D&amp;X procedures when performed to preserve the mother’s life, it contained no exception for preserving the mother’s health, and made no distinction between pre-viability and post-viability procedures.

In defending the law, Nebraska claimed that it was showing concern for the life of the unborn, preventing cruelty to “partially born children,” preserving the integrity of the medical profession and erecting a barrier to infanticide. Nebraska also argued that no health exception was necessary because safe alternatives to D&amp;X were still available.

The Supreme Court disagreed with Nebraska and held that the statute violated the U.S. Constitution for two reasons: it lacked a constitutionally mandated health exception and imposed an undue burden on a woman’s ability to choose abortion. Justice Stephen G. Breyer wrote the majority opinion, which was joined by Justices Ginsburg and John Paul Stevens, Sandra Day O’Connor and David H. Souter. Kennedy, Thomas, Scalia and Chief Justice William H. Rehnquist dissented, each one penning his own dissenting opinion.

The majority reasoned that three established principles determined the case’s outcome. First, before viability, the woman has a right to choose to terminate her pregnancy. Second, a law designed to further the state’s interest in fetal life that imposes an undue burden on the woman’s decision before fetal viability is unconstitutional. And third, a state may not regulate abortion “where it is necessary, in appropriate medical judgment, for the preservation of the life or health of the mother.”

The Court found the lack of a health exception greatly troubling and explained that “since the law requires a health exception in order to validate even a post-viability abortion regulation, it requires, at a minimum, the same in respect to pre-viability regulation.” The Court announced that the governing standard, taken from Casey, requires an exception because a state may not “endanger a woman’s health when it regulates the methods of abortion.”

Significant to its decision, the Court noted that the record demonstrated a lack of medical consensus as to the merits of D&amp;X. Some experts had testified that D&amp;X is in fact safer than D&amp;E because it reduces operating time, blood loss and risk of infection; reduces complications caused by bony fetal parts; reduces damage to the uterus and cervix; prevents the most common causes of maternal mortality; and reduces the chance of adverse consequences from leaving fetal parts in the woman. Other experts testified that D&amp;X offered no safety advantages and was never necessary to preserve the life or health of a woman. The Court found that this disagreement militated in favor of striking down the law: “The uncertainty means a significant likelihood that those who believe the D&amp;X is a safer abortion method in certain circumstances may turn out to be right. If so, then the absence of a health exception will place women at an unnecessary risk of tragic health consequences.” The Court then held that Casey required the Nebraska law to have a health exception, because “substantial medical authority” supported the proposition that banning D&amp;X could endanger women’s health.

As stated above, the Court also held that the Nebraska law was unconstitutional because it caused an undue burden on a woman’s right to make an abortion decision. It arrived at this conclusion after determining that the language of the statute was so broad and imprecise, in large part because it did not track the medical differences between D&amp;E and D&amp;X, that it could be read to prohibit D&amp;E as well as D&amp;X. As a result, physicians who performed D&amp;E would fear prosecution, conviction and imprisonment under the unclear law, which in turn would create an undue burden upon a woman’s right to make an abortion decision.

In his concurring opinion, Stevens persuasively wrote that the D&amp;X procedure is no “more brutal, more gruesome or less respectful of potential life” than the D&amp;E procedure. He further opined that “the notion that either of these two equally gruesome procedures performed at this late stage of gestation is more akin to infanticide than the other, or that the State furthers any legitimate interest by banning one but not the other, is simply irrational.”

Even Kennedy and Thomas, who dissented, acknowledged the unpleasantness
of D&E. Kennedy described the procedure as causing the fetus to bleed to death as it is “torn limb from limb,” and Thomas characterized D&E as “so gruesome that its use can be traumatic even for the physicians and medical staff who perform it.”

Kennedy’s lengthy dissent is also noteworthy. Foreshadowing his opinion in *Gonzales*, Kennedy argued that the Nebraska statute was not vague, did not ban D&E and did not need a health exception. He criticized the majority for misapplying *Casey*, impermissibly substituting its own judgment for that of Nebraska, deciding unnecessary constitutional questions and ignoring the principle that statutes should be interpreted to avoid constitutional difficulties. He also stated that “courts are ill-equipped to evaluate the relative worth of particular surgical procedures,” and castigated the majority for refusing to recognize the state’s “right to declare a moral difference between the procedures… where high medical authority is in disagreement.” In addition, Kennedy exhibited his disdain for D&X by saying that D&X “perverts the natural birth process to a greater degree than D&E, and more strongly resembles infanticide,” and his distrust of physicians by saying that any ban which depends on the “appropriate medical judgment” of a physician is no ban at all.

The history of the Partial Birth Abortion Act

In both 1996 and 1997, Congress passed prohibitions on so-called “partial-birth abortions,” but President William J. Clinton vetoed them. After Clinton left office, Congress passed the Partial-Birth Abortion Act of 2003 and President George W. Bush signed it into law.

Under the act, a physician who knowingly performs a “partial-birth abortion” is subject to two years in prison, a hefty fine and monetary damages for any psychological injury caused to the pregnant woman’s husband or parents. A pregnant woman who undergoes the procedure is not subject to any criminal penalty. The act is similar to the Nebraska law struck down in *Stenberg* in that it permits D&X when necessary to save the life of a pregnant woman, but contains no exception for a D&X necessary to preserve the woman’s health. Many supporters of the Act believed that a health exception could be interpreted so broadly that it would render the legislation superfluous.

The act defines a partial-birth abortion as one in which the doctor “deliberately and intentionally vaginally delivers a living fetus until, in the case of a head-first presentation, the entire fetal head is outside the body of the mother, or, in the case of breech presentation, any part of the fetal trunk past the navel is outside the body of the mother, for the purpose of performing an overt act that the person knows will kill the partially living fetus; and performs the overt act, other than completion of delivery, that kills the partially delivered living fetus.”

The act contains 14 detailed findings, the last of which has 15 sub-paragraphs. The first finding states that a “moral, medical and ethical consensus exists that the practice of performing a partial-birth abortion… is a gruesome and inhumane procedure that is never medically necessary and should be prohibited.” Another claim that “there exists substantial record evidence upon which Congress has reached its conclusion that a ban on partial-birth abortion is not required to contain a ‘health’ exception, because the facts indicate that a partial-birth abortion is never necessary to preserve the health of a woman, poses serious risks to a woman’s health and lies outside the standard of medical care.” Ten of the 14 findings are devoted to discussing the *Stenberg* decision and arguing that the Supreme Court should review factual findings by Congress with great deference. The findings also describe D&X as involving “piercing of the skull” and “sucking out the brain” and constituting the “killing of a child that is in the process, in fact mere inches away from, becoming a ‘person.’” On the basis of this description, Congress found the procedure akin to infanticide, and contends in yet another finding that “implicitly approving such a brutal and inhumane procedure by choosing not to prohibit it will further coarsen society to the humanity of not only newborns, but all vulnerable and innocent human life, making it increasingly difficult to protect such life.”

The act fails to describe D&E, which, as stated above, is the most common alternative abortion procedure, and a piece appearing in *The New York Times* described the act as forbidding “doctors from crushing the skull of the fetus, but permit[ing] them to poison and dismember it.”

Congress concludes the findings portion of the act

For these reasons, Congress finds that partial-birth abortion is never medically indicated to preserve the health of the mother; is in fact unrecognized as a valid abortion procedure by the mainstream medical community; poses additional health risks to the mother; blurs the line between abortion and infanticide in the killing of a partially-born child just inches from birth; and confuses the role of the physician in childbirth and should, therefore, be banned.

Nine medical associations, including the American Public Health Association and the American College of Obstetrics and Gynecology, opposed the act because they believe, like some of the experts who testified at the *Stenberg* trial, that D&X provides safety advantages over all other alternative procedures for some women. The American Medical Association, in contrast, believes D&X is medically unnecessary, but concedes that there is no consensus among obstetricians on this point.

On the day President Bush signed the act into law, LeRoy Carhart, M.D., a physician who performs abortions and was the lead plaintiff in *Stenberg*, along with several co-plaintiffs, filed suit seeking an injunction against enforcement of the act.

Lower court rulings

Before *Gonzales v. Carhart* reached the Supreme Court, all three federal district courts and all three circuit courts of appeals that were presented with challenges to the act held that the act was unconstitutional. For the most part, these courts had before them the same medical evidence as contained in the record before the Supreme Court in *Stenberg*.

In striking down the act, the Eighth Circuit Court of Appeals reasoned that “when substantial medical authority supports the medical necessity of a procedure in some instances, a health exception is constitutionally required,” and “when a lack of consensus exists in the medical community, the Constitution requires legislatures to err on the side of protecting women’s health by
including a health exception.” As detailed below, the Supreme Court justices would indeed read the congressional record and agree that there was no constitutional need for a health exception, although they would dispute the veracity of some of Congress’s findings.

**Gonzales — The majority opinion**

Although the three district courts and the three courts of appeals unanimously found the act to be unconstitutional, the act met a different fate with the Supreme Court and its two newest members. Since the Court decided *Stenberg*, Roberts filled the vacancy left by Rehnquist after he passed away in 2005, and Alito replaced O’Connor, who retired in 2006.

Kennedy, who wrote the majority opinion in *Gonzales*, was appointed to the Supreme Court in 1988 by Ronald Reagan, and is often called “the swing vote.” This tag, which had been born by O’Connor before she retired, has been pinned on Kennedy because in many cases he casts the deciding vote that swings the balance of the Court in one direction or another. Indeed, he swung the *Stenberg* minority into the majority position in *Gonzales*.

Although the parties advanced similar arguments in *Gonzales* as they had in *Stenberg*, the Court was more receptive to those by the defendants of the D&X ban the second time around and found the act to have cured the constitutional infirmities that riddled the Nebraska law at issue in *Stenberg*. First, the Court held that the federal act is not constitutionally vague, and thus does not cause an undue burden on women seeking an abortion, because it sets forth clear guidelines as to what conduct is prohibited, and provides objective criteria to evaluate whether a doctor has performed a criminalized procedure. The act earns these favorable appraisals because (1) it explicitly differentiates D&X and D&E using anatomical landmarks, (2) requires a physician to perform an overt act that kills the fetus after it has been partially delivered, and (3) has a scienter requirement.

As to the second area of improvement, the act’s greater precision in differentiating D&X and D&E assuaged the Court’s concern voiced in *Stenberg* that the ban was written in such a broad fashion that it could be read to prohibit D&E as well. As to the third area of improvement, the Court places great emphasis on the scienter requirement in rejecting the challengers’ argument that a physician could inadvertently perform a D&X and unwittingly violate the law. The Court explains that under the act, a doctor who intends to perform a D&E and remove the fetus in parts, but winds up performing a D&X, will not have the requisite intent to incur criminal liability. Together, the three improvements persuaded the Court to dismiss the contention that the act placed an undue burden on women seeking an abortion, and the opinion then turns to the stronger attack on the act — its lack of a health exception.

The Supreme Court first proclaims that it is not bound by Congress’s findings, and in fact disagrees with several of them, including the one that no health exception is necessary. Another particularly relevant finding the Court disputes is the one that provides that medical consensus exists that D&X is never medically necessary. In fact, at least 22 physicians and a number of professors of obstetrics and gynecology from many of the nation’s leading medical schools testified before Congress that D&X is necessary in at least some circumstances.

Although the Court refuses to completely defer to and blindly follow Congress’s conclusion that a health exception is not necessary, the Court analyzes the health exception issue differently in *Gonzales* than it had in *Stenberg* and arrives at the same end result as Congress did. More specifically, despite conceding that there was evidence that D&X may be the safest method of abortion, and that “there is documented medical disagreement whether the act’s prohibition would ever impose significant health risks on women,” the Court abandons its belief that the lack of a medical consensus is a fatal blow to a legislative ban of D&X. Furthermore, the Court adopts the opposite view and says that state and federal legislatures have “wide discretion to pass legislation in areas where there is medical and scientific uncertainty.”

The Court reasons that the division of medical opinion over whether the act’s prohibition creates significant health risks yields a sufficient basis to conclude that the act is not unconstitutional when it is attacked fa-
cially. The dissenters call this holding “bewildering” and defiant of the Court’s longstanding precedent affirming the necessity of a health exception.

The majority opinion also repudiates the type of challenge — facial rather than as-applied — the plaintiffs brought to the act. Interestingly, the Court expressed no similar vexations in either Danforth or Stenberg where it embraced the facial challenges asserted to bans on particular abortion procedures. The dissenters find this holding especially “perplexing,” given the Court’s declaration in Stenberg that the Nebraska act was facially unconstitutional for not having a health exception, and call this holding a grave mistake because it jeopardizes women’s health and places doctors in an “untenable” position by risking criminal prosecution if they “exercise their best judgment as to the safest medical procedure for their patients.” Nevertheless, by limiting its holding to rejecting the facial attack on the act, the Court does leave open future as-applied challenges to the law.

Notably, Kennedy’s opinion on behalf of the Court’s majority spotlights emotions not discussed in Stenberg, namely, love, regret and depression. For example, Kennedy writes that “[r]espect for human life finds an ultimate expression in the bond of love the mother has for her child,” and that “it seems unexceptionable to conclude some women come to regret their choice to abort the infant life they once created and sustained. Severe depression and loss of esteem can follow.” He also comments that it is “self-evident that a mother who comes to regret her choice to abort must struggle with grief more anguished and sorrow more profound when she learns [how the D&X procedure was performed on her child].” As discussed in greater detail below, statements such as these draw particular ire from Ginsburg in her dissent.

Kennedy claims that the majority’s decision is faithful to Casey. “Whatever one’s views concerning the Casey joint opinion, it is evident a premise central to its conclusion—that the government has a legitimate and substantial interest in preserving and promoting fetal life—would be repudiated were the Court now to affirm the judgments of the Courts of Appeals.” The dissent impugns this argument as well.

**Gonzales — Thomas’ concurring opinion**

In his dissenting opinion in Stenberg v. Carhart, Thomas described the Court’s abortion jurisprudence as a “particularly virulent strain of constitutional exegesis.” He continues his attack on the Court’s prior rulings in abortion cases in his four-sentence concurring opinion in Gonzales in which he reiterates his view that “the Court’s abortion jurisprudence, including Casey and Roe…., has no basis in the Constitution.” Very curiously, he also notes that the “exercise of Congress’ power under the Commerce Clause is not before the Court. The parties did not raise or brief that issue; it is outside the question presented; and the lower courts did not address it.” One cannot help but wonder whether Thomas might be persuaded, in future cases, that federal abortion regulations run afoul of the Commerce Clause.

Scalia joined Thomas’ concurrence, and the two continue to be the Court’s staunchest supporters of abortion restrictions. In his dissenting opinion in Stenberg, Scalia stated that Casey must be overruled and wrote, “I am optimistic enough to believe that one day, Stenberg v. Carhart will be assigned its rightful place in the history of this Court’s jurisprudence beside Korematsu [upholding internment of Americans of Japanese descent during World War II] and Dred Scott [rejecting a slave’s claim for freedom and holding men of the “African race” are not citizens of the United States and therefore cannot bring suit in U.S. courts].” Because Gonzales may have relegated Stenberg to the annals of irrelevant decisions, Scalia’s hopes may have been realized in just seven short years. Scalia, however, chose not to author a separate concurring opinion in Gonzales expressing his thoughts on this issue.

The fact that neither Alito nor Roberts joined Thomas’ concurrence may indicate that the two newest members of the Court are not prepared to go as far as overruling Roe. On the other hand, their silence may also simply indicate a belief that there was no need at this time for them to disclose their opinions.

**Gonzales — Ginsburg’s dissent**

It is extremely difficult, if not impossible, to reconcile the Supreme Court’s ruling in Gonzales with its statement in Stenberg that “a statute that altogether forbids D&X creates a significant health risk. The statute consequently must contain a health exception.” Therefore, although Gonzales does not explicitly overrule Stenberg, there is a strong argument that it effectively does so for at least the part of Stenberg requiring a health exception.

Ginsburg wrote a scathing dissent, to which Stevens, Souter and Breyer joined, which acknowledges the significant difficulty in reconciling the decisions. In the dissent, she calls the majority decision “alarmingly” and berates it as dishonoring precedent and not taking Casey and Stenberg “seriously,” and describes the Court’s justification for upholding the act “flimsy and transparent.”

In addition to Casey and Stenberg, Ginsburg relies on Danforth for precedence and summarizes the Court’s ruling in Gonzales as upholding a law that does nothing to preserve fetal life, but bars a woman from choosing a procedure her doctor reasonably believes will best protect her. She restates the medical evidence establishing the safety benefits of D&X, noting that it fills hundreds and hundreds of pages of oral testimony, and argues that the act “scarcely” furthers its claimed interest in protecting the life of a fetus, because “the law saves not a single fetus from destruction.”

In response to the majority’s invocation of the emotional harm which may befall women who undergo abortions and the implicit contention that the act serves to protect women, Ginsburg retorts that “this way of thinking reflects ancient notions about women’s place in the family and under the Constitution—ideas that have long since been discredited.” She explains that “eliminating or reducing women’s reproductive choices is manifestly not a means of protecting them,” and blasts the majority for depriving women of the right to make an autonomous choice.

In her concurring opinion in Stenberg, Ginsburg referenced an observation by Seventh Circuit Court of Appeals Chief Judge Richard A. Posner that legislators were prohibiting D&X, not because of any belief that it is a crueler or more painful or more disgusting method of terminating a pregnancy, but because they sought to “chip away at the private choice shielded by Roe v. Wade.” Ginsburg then echoes this belief in
her Gonzales dissent, saying that the majority’s defense of the act “cannot be understood as anything other than an effort to chip away at a right declared again and again by this Court.” Indeed, she finds “the Court’s hostility to the right Roe and Casey secured is not concealed.”

Gonzales — the Alito and Roberts effect

Legal analysts who have addressed the issue of how the Supreme Court’s composition affects its rulings on abortion have concluded that the replacement of Chief Justice Rehnquist with Chief Justice Roberts will not have a significant impact on future rulings. This was quickly born out in Gonzales. Given that Rehnquist dissented in Roe and Stenberg, he almost certainly would have voted with the majority in Gonzales, like Roberts did, had he still been on the Court. The substitution of Alito for O’Connor, however, most probably turned the Stenberg minority into the Gonzales majority, because O’Connor would have likely voted against the act, given that in Stenberg she voted with the majority and wrote a concurring opinion emphasizing the constitutional necessity of health exceptions in abortion-regulation legislation. Alito’s appointment, therefore, had an immediate, weighty impact on the Court’s abortion jurisprudence.

More changes to the Court’s composition?

Stevens, who has been a member of the Supreme Court for more than 30 years, is now 87 years old, and there is speculation that he may retire soon. Although he was appointed by a Republican president, Gerald R. Ford, he is often described as a liberal justice, and he voted against the abortion restrictions in both Stenberg and Gonzales. Should he retire before the end of President Bush’s term, or while another president who disfavors abortion is in office, abortion-rights proponents may find the Court even less responsive to their arguments in the future than the Court was in Gonzales.

Practical implications of Gonzales v. Carhart

While the general consensus is that Gonzales signals a major change in direction on abortion by the Supreme Court, the case also creates a number of practical quandaries for women seeking abortions and their physicians. For example, will women who are advised that D&X is the safest procedure for them forego that option and undergo a D&E (or other procedure), seek a physician willing to perform a D&X and risk prosecution, pursue as-applied constitutional challenges to the act, or decide not to go forward with the abortion?

Moreover, although the Supreme Court did leave open as-applied challenges to the act, the practical reality is that there will be few, if any, brought. A pregnant woman and her physician would likely not determine that a D&X would be beneficial until late in the second trimester, allowing for very little time for a lawsuit to run its course through the courts, due to the inherent time constraints involved with litigation, before the window of opportunity for the abortion had closed. As Ginsburg laments in her dissent in Gonzales, “A woman suffering from medical complications needs access to the medical procedure at once and cannot wait for the judicial process to unfold.”

Physicians who perform abortions also face certain dilemmas created by the Court’s ruling. Now, when a physician determines that a D&X is the safest and most prudent procedure for the patient, how is that physician to reconcile choosing between obeying the law and treating the patient in the safest manner? Will the physician even counsel a patient that D&X is an option to D&E?

In an article published on the Web site of The New England Journal of Medicine, Michael F. Greene, M.D., a professor of obstetrics, gynecology and reproductive biology at Harvard Medical School, wrote that the ruling “creates an intimidating environment surrounding pregnancy terminations at more advanced gestational ages” and “lacking confidence in the judicial system, physicians may choose to avoid performing second-trimester surgical abortions, thus restricting access to them, perhaps even if the mother’s life is in jeopardy.” Others have similarly remarked that the decision will have a “chilling effect” on physicians’ decision-making, given the prospect of incarceration and large financial repercussions. Dr. Carhart would agree, and has predicted that “most physicians are not going to risk their careers to prove a woman’s condition is life-threatening.”

A similar adverse effect resulted from the case of Dr. Kenneth Edelin, a Massachusetts physician who was indicted for and convicted of manslaughter after he performed an abortion in 1973, eight months after the Supreme Court decided Roe. Edelin is renowned for having served as chairman of the Department of Obstetrics and Gynecology at Boston University School of Medicine and chairman of the board of Planned Parenthood Federation of America, the largest private family-planning agency in the United States. But at the time of his prosecution, he was only a resident in obstetrics and gynecology. Edelin recalls that “Once I was indicted, hospitals up and down both coasts stopped performing second-trimester abortions.” The Massachusetts Supreme Judicial Court eventually reversed his conviction and acquitted him, but not before the case had such a wide-reaching impact.

What the future of abortion law may hold

A recent article in The New York Times reports that “only some 3,200 of the 1.3 million abortions performed annually in the United States involve the banned procedure.” Because the number of D&X procedures performed is low and alternative procedures are still available, the ruling may truly impact only a relatively small number of women.

Nevertheless, both sides of the abortion debate have proclaimed the great significance of the decision. Jay Sekulow, chief counsel of the American Center for Law and Justice, which filed an amicus brief in support of the act, commented after the decision that “this is a monumental victory for the preservation of human life.” On the opposing side, Nancy Northup, president of the Center for Reproductive Rights, which was one of the act’s challengers, said, “It took just a year [for the Roberts Court] to overturn three decades of Court precedent.”

There is no denying that abortion-foe lawmakers have been active and unthwarted by prior Supreme Court rulings striking down various restrictions over the last 30 years. For example, in early 2006, the South Dakota Legislature went so far as to pass a bill making it a felony for doctors to perform any
abortion except to save the life of a pregnant woman. The bill was designed to challenge \textit{Roe}, and was signed into law by the governor of South Dakota. But opponents of the law successfully forced a referendum, and in the November 2006 statewide vote, South Dakotans rejected the ban and repealed the law.

Now, with a victory in their pockets from the \textit{Gonzales} case, pro-life advocates will likely press state legislators to draft laws that will revive “partial-birth abortion” laws and further narrow women’s abortion rights, and \textit{Gonzales} will undoubtedly embolden state legislatures to craft further abortion restrictions. Indeed, some states are already considering requiring a doctor to show a pregnant woman an ultrasound image of the fetus before proceeding with an abortion.

On the national front, as expected, President Bush was pleased with the ruling, saying that “the Supreme Court’s decision is an affirmation of the progress we have made over the past six years in protecting human dignity and upholding the sanctity of life. We will continue to work for the day when every child is welcomed in life and protected by law.”

Thereafter, at the first debate among Republican Party candidates for the presidency, nine of the 10 presidential hopefuls voiced their agreement with the proposition that the day \textit{Roe} is repealed would be a “good day for America.” Three of the candidates also attended the National Right to Life Committee’s 2007 convention, vying for the organization’s support. At that event, U.S. Sen. Sam Brownback promised that if elected president, he would appoint the next Supreme Court justice who would form the majority needed on the Court to overturn \textit{Roe}.

On the other side of the political fence, U.S. Sen. Barack Obama teamed with Ginsburg and described the ruling as signaling “an alarming willingness on the part of the conservative majority [on the Supreme Court] to disregard its prior rulings respecting a woman’s medical concerns and the very personal decisions between a doctor and patient.”

It is clear that the next appointment to the Supreme Court, regardless of which president makes it and who is replaced, will have a significant impact on the future of abortion law, because the Court has been so closely divided in its recent decisions on abortion.

\textbf{Conclusion}

In \textit{Stenberg}, the Supreme Court described the two sides of the abortion debate as “virtually irreconcilable points of views,” and Scalia likened the Court to abortion umpires. These descriptions are no less accurate seven years later, and although many describe \textit{Gonzales} as a watershed decision and the first meaningful setback for the pro-choice movement after the Supreme Court decided \textit{Roe}, many chapters of the abortion legal saga remain unwritten.
I. Introduction
Suppose a high-ranking executive is accused of sexual harassment in the workplace by a subordinate. What are some of the key considerations the employer’s attorney needs to be aware of when counseling the employer on how to respond? Conversely, what claims may the accused executive bring against the employer if he or she is terminated in response to the allegations? As demonstrated by the hypothetical below, an employer’s interests may be best served by thoroughly investigating the allegations and evaluating the rights of the accused executive prior to taking any remedial action. If the employer does not consider the rights of the accused executive, the employer could be faced with a litany of claims asserted by the executive arising out of his or her termination.

This article will examine: (1) the potential steps that employers and their counsel can take during an investigation in order to avoid liability from the accused executive; (2) an executive’s potential claims if the employer fails to appropriately address such a situation; and (3) how the executive’s termination will be perceived within the company in terms of fairness and precedence, and the potential costs associated with such termination.

II. Hypothetical
Jane Jones, a budget analyst at Acme Supply Company, contacted human resources to complain that her 63-year-old boss, Bob Smith, Acme’s highly compensated and notoriously demanding chief financial officer, inappropriately touched her and made sexual comments to her as she was standing at the water cooler. Smith has been employed by Acme for 20 years. Acme’s HR director, Wendy Williams, who has had a long-standing and well-known feud with Smith, interviewed Jones concerning her complaint. Upon conclusion of her interview with Jones, Williams recommended to the board of directors that Acme terminate Smith.

III. Tips to avoid liability from the accused executive related to an investigation
While Williams’ recommendation to terminate Smith may be an appropriate course of action, Acme would be well advised to conduct a fair and impartial investigation prior to terminating Smith. Indeed, failure to undertake a thorough investigation may expose Acme to liability. Moreover, employers should be careful not to rely on recommendations for terminations from employees with an axe to grind.

While Acme’s counsel is likely to advise the company to conduct a thorough and impartial investigation before taking action against Smith, Acme may want to consider the following tips in relation to the investigation. Before commencing the investigation, Acme should consider whether it is beneficial to bring in an outside investigator. This may reduce the risk that Smith will contend that the investigation was flawed or biased. Once the investigator is in place, he or she should develop a plan, considering the individuals to be interviewed, where the interviews will take place and whether counsel for the accused may be present for the interviews. Acme’s investigator should interview both Jones and Smith. Acme should not con-
duct itself in a manner in which Smith could claim that he was denied any rights he might have under Acme’s policies, procedures and/or other documents. Accordingly, Smith should be made aware of the allegations and given an opportunity to give his side of the story. It may also be necessary to speak to others, such as witnesses and/or co-workers who work in Acme’s finance department. It should be made clear to all individuals involved that unprofessional conduct and acts of retaliation will not be tolerated.

Generally, the complainant should be interviewed first, followed by the accused, and then other witnesses. During the interviews, the alleged events should be explored in detail. The investigator should lead with open-ended questions and follow up with closed and direct questions when appropriate. The investigator should also review and analyze any relevant documents and/or communications that may exist. These steps are more likely to result in a factually accurate record of the event in question. At the conclusion of the investigation, Acme should consider the findings of the investigator prior to making a decision to take action, up to and including termination, against Smith.

IV. Evaluating potential legal claims of the accused executive

Prior to supporting the recommendation to terminate Smith, Acme’s counsel should also evaluate and consider Smith’s potential legal claims against Acme and/or individual employees. Such claims can be found in contract, tort or statutory rights.

1. Breach of express and implied contracts

Assume for purposes of the hypothetical that Smith’s alleged conduct took place during the term of his three-year employment agreement with Acme, which provided that Acme may only terminate him within that three-year period “for cause.” If Acme’s termination of Smith violates the terms of his employment agreement, Smith may have a viable claim for breach of contract against Acme. Accordingly, before making the decision to terminate Smith, Acme and its counsel must make a careful assessment as to whether it has “cause,” as defined under the terms of his employment agreement (and possible other applicable agreements) to support the decision. The threshold standards to establish cause can be quite varied and can range from the narrowly tailored “conviction of a felony or crime of moral turpitude” to the more general “any misconduct by the employee detrimental to the company.” In cases where the employment agreement is silent as to the definition of cause, courts are likely to apply the common law standard: (1) a reasonable basis for employer dissatisfaction, and (2) grounds for discharge reasonably related, in the employer’s honest judgment, to the needs of the business. Furthermore, as an executive’s overall compensation is often tied to various deferred compensation and/or stock option plans, it is also important to analyze any “termination for cause” language found in these plans and its relation to the relevant vesting and forfeiture provisions of such plans. In any situation, an assessment of whether the conduct in question truly rises to the level of cause is essential.

Suppose in the hypothetical that Acme had previously provided Smith with an employee handbook. Acme’s handbook contained a progressive discipline policy requiring that Acme’s employees be provided with oral and written warnings prior to termination. The handbook also provided an explicit disclaimer stating that its policies are not terms and conditions of employment. If Acme terminates Smith without applying its progressive discipline measures, a potential contract claim may arise notwithstanding the explicit disclaimer. Accordingly, Acme should consider strictly following its internal policies and procedures.

2. Breach of covenant of good faith and fair dealing

In addition to the express breach of contract claim set forth above, Smith’s termination may give rise to a claim for breach of the covenant of good faith and fair dealing, which requires that “neither party shall do anything that will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract.” Based on the doctrine of good faith and fair dealing, Acme cannot act in such a manner that would unjustifiably deprive Smith of the benefits of his employment agreement.

3. Statutory claims

Based upon the fact that he is over the age of 40, Smith qualifies for protection under state and federal age anti-discrimination laws. Accordingly, Acme should be advised not to engage in conduct which could be used by Smith to support a claim for age discrimination. For example, if Acme did not apply its progressive discipline policy to Smith prior to his termination, but had applied it in the past to employees under the age of 40, Smith may be able to demonstrate that Acme’s failure to adhere to its policies is evidence of discriminatory animus in support of his discrimination claim.

4. Tort claims

Assume for purposes of the hypothetical that Smith heard from an Acme board member that Williams referred to him as a “serial groper who needs to be let go” during her presentation to the board recommending Smith’s termination. Based upon such conduct, Smith may attempt to pursue tort-based claims. For example, Smith may assert a claim of tortious interference with contractual relations claim against Williams. As the Massachusetts Supreme Judicial Court recently clarified, in order to prevail on a tortious interference claim, Smith would be required to establish that Williams was motivated by actual malice, i.e., a spiteful malignant purpose, unrelated to the legitimate corporate interest of the employer. In the context of discrimination cases, it is worth noting that an individual’s discriminatory intent may constitute malice for purposes of tortious interference.

Furthermore, Williams and Acme could potentially face a defamation claim if her comments to the board about Smith damaged his reputation and caused him to suffer economic harm. While Acme has a conditional privilege to disclose defamatory information about an employee when necessary to serve its legitimate interests, such privilege can be lost if the information is published recklessly, i.e., it was unnecessary, unreasonable or excessive.
V. Equitable considerations

In addition to recognizing Smith’s potential legal claims, Acme would be well advised to consider how its actions will be perceived by its employees. If Acme quickly and decisively takes action against Smith prior to conducting a full and thorough investigation, similarly situated executives may be concerned that any accusations against them in the future, valid or not, will lead to their abrupt termination, which could lead to eroding morale. Moreover, there may be fairness issues that arise if Acme summarily dismisses Smith, who during his 20-year career made significant contributions to the company, without conducting an impartial investigation and balancing all of the interests involved. It is important to keep in mind that Acme’s actions will set a precedent for the future. Moreover, as noted above, deviation from these practices in the future could expose Acme to potential liability down the road. Acme should also consider the cost of terminating Smith. Assume that Smith’s employment agreement provides him with substantial severance payments or accelerated vesting of company stock or options upon termination in certain circumstances. His termination could result in a costly payout for Acme. Additionally, Acme will also have to bear the costs of finding a replacement for Smith.

VI. Conclusion

This article is intended to provide a practical roadmap to attorneys who may be confronted with a similar workplace misconduct scenario. While each case is unique, counsel for the employer and the accused will be in a better position to protect and serve the interests of their clients by considering the potential issues and claims raised here.

Endnotes

2. Aviles v. F.L. Roberts & Co., 28 MDLR 146 (2006) (finding employer liable for relying upon statements of a supervisor with discriminatory animus in making termination decision); Equal Employment Opportunity Comm’n v. BCI Coca-Cola Bottling Co., 450 F.3d 476, 485 (10th Cir. 2006) (finding that under Title VII an employer may be liable for a subordinate employee’s prejudice even though the ultimate decision maker lacked discriminatory intent).
3. See Boothby v. Texon, 414 Mass. 468, 480-482 (1993) (applying the common law definition of cause, the court ruled that the employer did not have cause to terminate a high-ranking executive for his refusal to obey the CEO’s instructions to terminate a subordinate).
8. Smith would only be able to assert a tortious interference claim against Williams, not Acme. See Appley v. Locke, 396 Mass. 540, 543 (1986) (noting that employer cannot be liable for tortious interference with employment relationships between itself and its employees).
11. An employer’s physical actions witnessed by others, without the presence of written or spoken communication, may also suffice to establish defamatory publication. See Phelan v. May Dep’t Stores, 443 Mass. 52, 57 (2004).
Schussing down the slippery slope of lifestyle discrimination

By Harvey A. Schwartz

Some cases are impossible to turn down. Ring, ring, ring.
“Hello?”
“I just got fired.”
“Too bad. What happened?”
“I flunked a drug test.”
“Sorry, but those things happen.”
“I tested positive.”
“Well, don’t do the crime if you can’t do the time.”
“Positive, positive for nicotine. They don’t employ smokers. Makes their insurance too expensive, they said.”
“When can we get together?”

Thus was spawned Rodrigues v. The Scotts Company, LLC in federal court in Boston, a case in which Scotts, the world’s leading grub killer and lawn seed purveyor, boasts of its refusal to hire or employ smokers. Among the corporation’s justifications for this policy, besides its beneficent concern for its workers’ health, is fear of increased medical insurance costs.

The specter of rising medical insurance costs haunts every employer, or at least every employer that still provides some measure of insurance benefits. This case will test just how terrifying that specter is, and whether it can be used to justify until-now unheard of intrusions into the private, away-from-the-workplace activities of employees. This case perches at the peak of what could be a black diamond slippery slope down which we can expect:

- “Sorry Joe, but your cholesterol came in awfully high. You’ve got two months to get it under 200 or we’ll have to let you go.”
- “Sally, it’s come to our attention that your husband was seen smoking. You know company policy is that nobody on our health plan is allowed to smoke. If you want to keep your job, he’ll have to submit weekly urine samples.”
- “John, putting on some weight there. The company nurse says your body-mass index is in the red zone. We can’t have that. Shape up or ship out, buddy.”
- “Jane, sky diving? Really, now. You don’t expect your fellow employees to have to carry the medical expenses if you land in the hospital, do you? One more jump and we’ll have to let you go.”
- “Phil, congratulations on the new baby. Here is your severance agreement. You know how unfair it would be to everybody else here if our insurance costs went up because of all the medical costs for children. You knew when you joined this company that we have a no-parent policy.”

Paranoia? Rantings from the far left of employees’ rights? Perhaps, but 20 years ago, virtually everybody would have hung the same label on speculation about a “we don’t employ smokers” policy. The business justification — and legal support — for firing a smoker is identical to that for firing an overweight, compulsive eater with high cholesterol. Both are engaging in harmful, socially-frowned-upon, yet entirely voluntary activities, taking actions that are fairly certain to imperil their health and increase the cost of providing health care, costs borne by their employer.

What are the legal grounds for opposing such policies?

Rodrigues’ first defense is that old friend of employees (choke choke), ERISA, the Employee Retirement Income Security Act, a bugaboo employees usually flee from as if it were Godzilla strolling through downtown Tokyo. ERISA Section 510, 29 USCS §1140, states,

It shall be unlawful for any person to discharge, fine, suspend, expel, discipline, or discriminate against a participant . . . for the purpose of interfering with the attainment of any right to which such participant may become entitled under the plan . . .

To prevail in such a claim, a plaintiff must show that her employer took an adverse action against her “with the specific intent of interfering with the employee’s ERISA benefits.” Barbour v. Dynamics Research Corp., 63 F.3d 32, 37 (1st Cir. 1995). A paradigm
example of a §1140 violation was stated in Fleming v. Ayers & Assoc., 948 F.2d 993 (6th Cir. 1991), in which the Sixth Circuit had no difficulty finding wrongful ERISA discrimination where a woman was hired one day and then fired the next day after the employer learned that she had recently given birth to a child with hydrocephalus and had incurred more than $80,000 in medical fees. Similarly, in Fitzgerald v. Codex Corp., 882 F.2d 586 (1st Cir. 1989), the First Circuit held that a complaint stated a Section 510 violation when it alleged that an employee was fired because the employer did not want to be compelled to provide medical insurance coverage to the employee’s former wife, who was suing the company for such coverage. Firing an employee because the employer wants to avoid providing benefits to that employee (or his family) is the classic Section 510 violation.

Scotts’ CEO acknowledges this ERISA hurdle. In a cover story about the Rodrigues case in BusinessWeek, Scotts Chief Executive Officer James Hagedorn said, “If you choose to smoke, then don’t ask me to cover your insurance. Well, some federal laws say we can’t do that. They say we can’t transfer the risk to the person behaving in a way that will cost more. The rules are lining up so you can’t assign the risk where it belongs.”

When business leaders complain about “the rules” costing them — and, presumably, their lawn-seed-spreading customers — serious money, Congress tends to listen, and rework “the rules.” It will be unfortunate if the solution to the health care cost crisis turns out to be to punish people who get sick. Such a “solution” will not solve anything, except maybe employers’ health care costs. If the country is in the midst of a “crisis” now because so many people are uninsured, what will the “crisis” escalate to when these people become not only uninsured, but also unemployed because corporations refuse to hire those people who will incur the greatest medical expenses?

Rodrigues offers other legal grounds for opposing Scotts’ nicotine-free workplace. Mandatory urine testing for the presence of nicotine violates Massachusetts’ privacy statute, G.L.c. 214 §1B, he claims. That statute says,

A person shall have a right against unreasonable, substantial or serious interference with his privacy. The superior court shall have jurisdiction in equity to enjoin such right and in connection therewith to award damages.

When workplace drug testing was in its infancy, the privacy statute was held up by employees as their bulwark. Employees tended to do poorly in these claims, however, with decision after decision finding that an employer’s need to know whether its employees were impaired by illegal substances outweighed employee privacy interests. The high-water mark for employee privacy was in Webster v. Motorola, Inc., 418 Mass. 425, 637 N.E.2d 203 (1994). In that case, two Motorola employees were randomly selected to provide urine samples for testing for marijuana, cocaine, opiates, phencyclidine (PCP) and amphetamines. One employee tested positive; the other refused to participate in the testing.

The Supreme Judicial Court resolved the case in a fact-specific, finely tuned decision, setting a standard that continues to be applied. One plaintiff, Webster, worked in outside sales and drove a company car as part of his job. The SJC held that the company’s need to know if he was too impaired to safely operate the vehicle outweighed his privacy interests.

The other employee, Joyce, however, sat at a keyboard and wrote user manuals and software documentation. Even though these manuals were used by the military and the Federal Aviation Administration, the SJC found that his privacy interests outweighed Motorola’s right to compel him to urinate in a cup. The Court said,

We have recognized that requiring an employee to submit to urinalysis involves a significant invasion of privacy. The act of urination is inherently private, and beyond the act itself, individuals have a privacy interest in what may be detected through urine testing. Additionally, to the extent that it may be requested to rebut an initial positive test result, information concerning an employee’s medical conditions is also within the realm of one’s privacy interest.
from employment or take any adverse action against any employee with respect to compensation, terms, conditions or other privileges of employment because that person does or does not smoke or use other tobacco products, unless the employer has a rational basis for doing so which is reasonably related to the employment, including the responsibilities of the employee or prospective employee.” N.J. Stat. §34:6B-1 (2007).

Some statutes go beyond the bounds of tobacco. Minnesota law, for example, states,

An employer may not refuse to hire a job applicant or discipline or discharge an employee because the applicant or employee engages in or has engaged in the use or enjoyment of lawful consumable products, if the use or enjoyment takes place off the premises of the employer during nonworking hours. For purposes of this section, “lawful consumable products” means products whose use or enjoyment is lawful and which are consumed during use or enjoyment, and includes food, alcoholic or non-alcoholic beverages, and tobacco.


A few states, including New York, California and Colorado, out and out protect employees’ rights to engage in any lawful, out-of-work activity. New York law, for example, makes it “unlawful for any employer . . . to refuse to hire . . . or to discharge from employment or otherwise discriminate against an individual . . . because of [among other activities]:

b. an individual’s legal use of consumable products prior to the beginning or after the conclusion of the employee’s work hours, and off of the employer’s premises and without use of the employer’s equipment or other property; or

c. an individual’s legal recreational activities outside work hours, off of the employer’s premises and without use of the employer’s equipment or other property.”

NY CLS Labor §201-d (2007).

Regardless of the outcome of the Rodrigues case (and a decision on the corporation’s motion to dismiss is pending), Massachusetts law is noteworthy for its failure to offer similar protection to employees. The right to do what the law permits is a fundamental freedom, including activities that some employers might believe to be dangerous, ill advised, unhealthy or unpleasant. Employers purchase their workers’ time and skill, not the right to control their private lives. That relationship was called something else, something other than employment, something that was banned by the 13th Amendment.

Employers’ efforts to control their employees’ private lives are nothing new. When Henry Ford raised his workers’ wages to $5 a day, he also established Ford’s “Sociological Department” to make sure they didn’t blow the money on booze and vice. He banned smoking because he thought that tobacco was unhealthy. “I want the whole organization dominated by a just, generous and humane policy,” he said. He implemented this policy by having the department make surprise visits to workers’ homes and firing men who had problems with finances, gambled or got drunk.

Ford’s “innovations” at the beginning of the last century are surfacing again at the beginning of the present century. This time, employers are cloaking their paternalism in the rubric of good business sense. Scotts argued to the federal court that its policy of not employing smokers addressed “sound business concerns” and was simply a means of “controlling the ever-increasing cost of health and disability insurance.” Most laws that protect workers were designed to protect them from such sound business decisions, from policies that benefited the employer’s bottom line at the expense of workers.

Massachusetts should have a similar law protecting workers’ rights to engage in lawful, private activities. What employees do in their private lives, on their private time, that has no effect on their job performance is, quite simply, none of their employer’s business.
You just successfully represented your biggest client in an arbitration hearing out of state. Still reveling from the closing argument you gave, you receive an unexpected phone call. It’s opposing counsel and he has called to inform you that he will be filing a motion to vacate the arbitration award on the ground that you engaged in the unauthorized practice of law. Instantly, you wonder, can he do this? More importantly, you wonder about the possible effects. As you know, a finding by the court that you engaged in the unauthorized practice of law may not only lead to the award being vacated, but it also implicates the ethical rules.

Whether the motion will succeed may depend on, of all things, where the arbitration was held. For example, effective Jan. 1, 2007, the Massachusetts Supreme Judicial Court adopted the American Bar Association’s Model Rule 5.5, entitled Unauthorized Practice of Law; Multijurisdictional Practice of Law. The new Rule 5.5 of the Massachusetts Rules of Professional Conduct, which allows an attorney unlicensed in Massachusetts to represent a client here in an arbitration, states in relevant part:

A lawyer admitted in another United States jurisdiction, and not disbarred or suspended from practice in any jurisdiction, may provide legal services on a temporary basis in this jurisdiction that are in or reasonably related to a pending or potential arbitration, mediation, or other alternative dispute resolution proceeding in this or another jurisdiction, if the services arise out of or are reasonably related to the lawyer’s practice in a jurisdiction in which the lawyer is admitted to practice and are not services for which the forum requires pro hac vice admission.


Under the new Rule 5.5, and in the absence of another forum rule or an express enforceable contract provision, pro hac vice admission in Massachusetts will only be required for “court-annexed arbitration or mediation.” Comment 12 to Rule 5.5, which further elaborates on the provision of temporary legal services by out-of-state attorneys, specifically requires pro hac vice admission in those particular circumstances.

Paragraph (c)(3) permits a lawyer admitted to practice law in another jurisdiction to perform services on a temporary basis in this jurisdiction if those services are in or reasonably related to a pending or potential arbitration, mediation, or other alternative dispute resolution proceedings in this or another jurisdiction, if the services arise out of or are reasonably related to the lawyer’s practice in a jurisdiction in which the lawyer is admitted to practice. The lawyer, however, must obtain admission pro hac vice in the case of a court-annexed arbitration or mediation or otherwise if court rules or law so require.

The American Arbitration Association rules do not include a requirement of pro hac vice admission in the state where an arbitration is being conducted. Accordingly, out-of-state attorneys may represent their Massachusetts clients in AAA arbitrations here without fear of disqualification or the threat of a bar disciplinary complaint in their home state for engaging in the unauthorized practice of law.

Arbitration proceedings in Massachusetts prior to the enactment of the new Rule 5.5 on Jan. 1, 2007

In 2006, the SJC decided two cases under the prior Rule 5.5 that involved lawyers who participated in arbitrations in Massachusetts but who were not licensed to practice here. In the first of these cases, Superadio Limited Partnership v. Winstar Productions, 446 Mass. 330 (2006), the losing party at arbitration petitioned the Court to have the arbitral award vacated. The appellant’s key argument before the Court was that the lawyer representing the appellee was not licensed in Massachusetts, and therefore, he engaged in the unauthorized practice of law by representing the appellee in a Massachusetts arbitration.

The SJC did not resolve the issue of whether an attorney licensed out of state was authorized to participate in arbitration proceedings in state because the Court was
Representing your clients in out-of-state arbitrations

Not every state has been as receptive as Massachusetts to out-of-state attorneys representing clients in arbitration matters. For example, in Birbrower, Montalbano, Condon & Frank, P.C. v. Superior Court, 17 Cal.4th 119, cert denied, 525 U.S. 920 (1998), the Supreme Court of California held that out-of-state attorneys, who had prepared to arbitrate a case before an AAA panel, engaged in the unauthorized practice of law. The case itself never got as far as an arbitration hearing. Still, the court found that the two attorneys, neither of whom were licensed to practice in California, but who met with their clients in California, met with the opposition in California, and discussed a proposed settlement and made recommendations relating to it (also while in California), had engaged in the unauthorized practice of law. The Birbrower court declined in that case “to craft an arbitration exception” to California’s prohibition on the unauthorized practice of law. Birbrower, 17 Cal.4th at 133-34 (1998). Perhaps even worse for these attorneys, the Birbrower court barred them from recovering the legal fees they had incurred in providing legal services in California and allowed recovery of only those limited legal fees for the services that they provided in New York. Subsequent to the Birbrower case, the California Legislature adopted a law specifically authorizing out-of-state attorneys to represent clients at arbitrations after filing a certificate, which must be approved by the arbitrator; a requirement similar to pro hac vice admission. See California Code of Civil Procedure §1282.4 (1998).

States such as New York and Illinois have allowed out-of-state attorneys to represent clients in arbitration proceedings. In Williamson v. John D. Quinn Construction Corp., 537 F. Supp. 613 (1982), the U.S. District Court for the Southern District of New York was presented with the issue in the context of a fee dispute. The defendant, John D. Quinn Construction Corp., was represented by plaintiff Donald J. Williamson PA, a New Jersey law firm, in an arbitration hearing held in New York. Williamson comprised only two attorneys, both of whom worked on the Quinn Construction arbitration but only one of whom was licensed to practice law in New York. Following the arbitration, which Quinn Construction lost, Williamson filed suit against Quinn Construction to collect more than $40,000 in unpaid fees. As part of its defense, Quinn Construction argued that Williamson was not entitled to collect the fees earned by the Williamson attorney who was not licensed to practice in New York, on the basis that the attorney had engaged in the unauthorized practice of law.

The U.S. District Court for the Southern District of New York disagreed. In holding that the Williamson attorney was within his right to participate in the New York arbitration, the court explained that an “arbitration tribunal is not a court of record; its rules of evidence and procedures differ from those of courts of record; its fact-finding process is not equivalent to judicial fact-finding; and it has no provision for the admission pro hac vice of local or out-of-state attorneys.” Williamson, 537 F. Supp. 613, 616 (1982). The court in Williamson also noted that the Association of the Bar of the City of New York had addressed the issue of legal representation before arbitration tribunals and concluded that “the Committee is of the opinion that representation of a party in an arbitration proceeding by a non-lawyer or a lawyer from another jurisdiction is not the unauthorized practice of law.” Williamson, 537 F. Supp. 613, 616 (1982).

Likewise, when an Illinois appellate court was presented with this question, it declined to vacate the arbitral award based upon the appearance of out-of-state counsel for one of the parties. In Colmar, Ltd. v. Fremantlemedia North America, Inc., 344 Ill. App. 3d 977 (Ill. App.1 Dist. 2003), appeal denied, 208 Ill.2d 535 (Ill. 2004), the plaintiff filed an action to have an arbitral award vacated based, in part, on the fact that Fremantlemedia’s (“FMNA”) attorney was not admitted to practice in Illinois. The trial court affirmed the arbitrator’s award. The Illinois appellate court, in affirming the trial court’s order, concluded that the issue of whether FMNA’s attorney was admitted in Illinois was not determinative. The appellate court noted the general rule in Illinois that judgments are void if they are the result of a claim brought by an attorney who is unlicensed in Illinois. But, it determined that the rule should not be extended to arbitration proceedings for several reasons. First, the parties are both bound, by contract, to the rules of the AAA and the AAA does not require either party to be represented by an attorney. Next, the “modern trend of multijurisdictional practice” supports this holding. Finally, the Illinois appellate court agreed with plaintiff Colmar in stating that arbitration is not a judicial proceeding and the differences between the two proceedings were significant.

Similar to the Association of the Bar of the City of New York, the New Jersey Supreme Court Committee on Unauthorized Practice
opined in 1994, in response to an inquiry, that “an out-of-state attorney may represent a party in an arbitration proceeding conducted under the auspices of the AAA in New Jersey.” 1994 WL 719208, N.J. Unauth. Prac. Op. No. 28 (1994). As the New Jersey Supreme Court Committee explained, this would include presenting evidence and arguing substantive legal issues. Relying on the reasoning of the U.S. District Court in the Williamson case, the committee found that arbitration’s “informal nature” could not be reconciled with a requirement that attorneys must be admitted to practice in-state before participating in an arbitration.

If confronted with such a challenge to an arbitral award, there are many useful policy arguments advanced by the ABA’s Commission on Multijurisdictional Practice in its comprehensive 2002 Report of the Commission on Multijurisdictional Practice. As the commission explained, there are circumstances where the client benefits if the client’s attorney is permitted to render these services. Perhaps the most obvious benefit to the client is the freedom to be represented by someone with whom the client has built a relationship and in whom the client has vested his or her trust and confidence. The commission also found that, in the arbitration arena, admission to a particular jurisdiction may be relatively unimportant because the law in the jurisdiction where the proceeding takes place may be unrelated to the law governing the proceeding. This statement is particularly applicable to labor and employment arbitration where the language of the collective bargaining agreement effectively governs the dispute. Further, the parties to arbitration proceedings may simply choose to arbitrate at a particular location because that location is most convenient. If the arbitration site is selected as a matter of convenience, then the location is unlikely to bear any relationship whatsoever to the underlying dispute. Thus, familiarity with the laws and procedure of that jurisdiction is unnecessary as a practical matter.

Conclusion

Although many states allow attorneys who are not licensed in state to represent clients in arbitration proceedings, without pro hac vice admission, the rules from state to state are not uniform. Before entering a state to represent a client at an arbitration, prudent practitioners will review the state’s ethical rules and any relevant statutes relating to the unauthorized practice of law in that jurisdiction. The ABA maintains a chart that identifies what form of Rule 5.5 each state has adopted. See www.abanet.org/cpr/jclr.

Alternative dispute resolution is an area of the law that will continue to provide limitless opportunities for solo and small firms to expand their law practices. A few hours of research will ensure that you take advantage of those opportunities without forfeiting hard-earned legal fees or facing bar disciplinary action.

Endnotes

1. The activities that constitute the practice of law in California were discussed in the Birbrower case in the context of the California Business and Professions Code §6125, which prohibits the unauthorized practice of law.
Not quite 100 years ago, presumably to the chagrin of scriveners, someone had the idea of standardizing the essential elements of conveyancing by defining in the General Laws terms such as “warranty covenants” and “quitclaim covenants” for use in deeds, and “mortgage covenants,” “statutory condition” and “statutory power of sale” for mortgages. These statutorily defined terms became fundamental to Massachusetts conveyancing by their uniform, efficient, clear communication of central elements of the parties’ legal rights and obligations in a particular transaction.

Another property interest, the affordable housing restriction, is coming into ever-wider use as more communities adopt the Community Preservation Act. In addition, Chapter 40B developments continue to be a major engine for housing development; The ever-increasing demands being placed on land make it unlikely that the need for housing restricted for persons of modest income is a passing fancy. This article proposes that it is time to provide a similar statutory structure for affordable housing restrictions.

Under the sponsorship of Citizens Housing and Planning Association, some attorneys who practice in this area have drafted proposed new sections of General Laws, Chapter 183 to define the terms “statutory housing covenants,” “statutory housing conditions” and “statutory housing power to sell” for use in housing restrictions. To illustrate, in a structure mirroring the statutory condition for mortgages, the proposed “statutory housing condition” would require the owner to live in the house as principal residence, to pay all debt secured by the property, not to encumber the property beyond its affordable value and to convey the property only to another eligible household as their principal residence for an amount not exceeding the affordable (that is, restricted) value.

While it takes 248 words to say this with full legal precision in the proposed legislation, the job could be done in any housing restriction simply by using the phrase “statutory housing condition.” And just as a completely valid mortgage can be created using the statutory form set out in paragraph five of the appendix to Chapter 183, the legislation includes a statutory form for creating a complete and functional affordable housing restriction simply by saying that the grant is “with statutory housing covenants and on the statutory housing condition for any breach of which the holder shall have the statutory housing power to sell.” Twenty-five words doing the job of . . . well, we won’t go into that. The good news is that those 25 words will create and communicate efficiently uniform core legal rights for all housing restrictions in which they appear without standing in the way of other terms and conditions the parties wish to include. Here are some details.

The proposed “statutory housing covenants” mirror quitclaim covenants using a format similar to “mortgage covenants.” As noted above, the proposed “statutory housing condition” requires that the household owning the home live there as their principal residence, pay the debt secured by the home, not mortgage the home for more than its affordable value and sell the home at not more than the affordable value to another income-qualified household for use as their principal residence. The proposed “statutory housing power to sell” provides authority and structure, similar to the mortgagee’s power of sale, that will enable a holder of a housing restriction, when necessary, to preserve the restriction by transferring ownership and occupancy away from a breaching owner at the affordable value, with that owner having rights and remedies, including opportunity to cure, similar to those a mortgagor has in the case of alleged breach of the mortgage.

Essential terms such as “area median income” and “household income” are also defined, but the statute seeks to deal only in the essentials for the purpose of making the statutory structure universally applicable, leaving the parties in the transaction free to make their agreement on relevant terms and conditions. So, for example, the level of income that would qualify a household to own and live in the house is not defined, leaving this central issue to be tailored to the circumstances (not above 80 percent area median income in a 40B project but up to 100 percent area median income allowed under CPA). Universal application can be achieved only by distinguishing those elements that are in fact universal from those which, if imposed uniformly, would have the effect of limiting other useful choices. So the legislation is enabling, but not regulatory.

Specific provisions establish the long-term validity of the statutory housing covenant and facilitate creating a functional relationship with mortgagees. Under the legislation, a statutory housing restriction will satisfy the requirements of G.L. c 184, sec. 32 for continued enforceability without requiring DHCD approval (although any non-statutory elements of the restriction would need DHCD approval to achieve that status). The legislation also accommodates mortgagees, who face confusion from the myriad of restrictions resulting from local action, by
providing that when the statutory housing structure is used in a restriction that is senior to the mortgage, the statutory components of the restriction will survive foreclosure but the non-statutory portion will be extinguished, allowing the mortgagee to resell the property subject only to the uniform statutory elements of the restriction. (The parties can alter this result by agreement.)

The statutory form, enabling a grant “with statutory housing covenants, on the statutory housing conditions and with the statutory housing power to sell,” will be equally effective if it is set out independently, for instance, in a deed or, more likely, as part of a separate affordable housing restriction. Just as one typically finds “mortgage covenants,” “statutory condition” and “statutory power of sale” appearing as centerpieces in widely varying mortgage documents because they ensure a valid mortgage while not standing in the way of the transaction being agreed by the parties, one assumes the dominant use of the statutory housing covenant, conditions and power to sell will be similar, and that they will most often appear in the text of a longer document as a foundation for the parties’ legal relationship as regards the property.

A mortgage which includes the statutory power of sale has the benefit of clearly established, functional remedies for breach and rights to cure set out in General Laws, Chapter 244, with foreclosure by public auction leading the list, entry typically acting like a statute of limitations against defects in the foreclosure sale, and court proceedings available when needed by either party. To meet a similar need in the event a statutory housing restriction is not being honored, the legislation includes a new Chapter 244A that creates such rights and remedies, largely incorporating relevant provisions of Chapter 244, resulting in a new set of remedial rights that will be familiar almost before one uses them for the first time. The major difference from the mortgage context is that transfer of a housing restriction as a remedy for the owner’s breach must occur at the affordable value, not at a discounted value, as typically occurs in mortgage foreclosure, and mortgagees who lent within the affordable value must be paid in full.

The task at hand for the community of real estate attorneys, along with others interested in affordable housing restrictions, is to review, discuss, modify if useful, and support the proposal now before the Legislature. The Massachusetts Bar Association can be an important forum for that discussion. If the bar does its job as well as those who created the existing statutory covenants nearly 100 years ago, the resources Massachusetts law offers to assist us in addressing fundamental and important needs of our clients will have been enriched.

The proposed legislation can be found at Senate Bill #754.
A primer on the New Markets Tax Credit

By Thomas G. Collins

The New Markets Tax Credit program provides an incentive to stimulate private investment in low-income communities. Attorneys whose clients are seeking additional tax advantaged investments should consider bringing the NMTC to the attention of their clients. In addition, the clients of attorneys representing low-income community businesses may benefit from the investment capital provided by community development entities that are able to raise funds from investors seeking the NMTC. This article sets forth the basic NMTC rules.

Section 1(a)(7) of Public Law 106-554, 114 Stat. 2763 (Dec. 21, 2000) added Section 45D to the Internal Revenue Code of 1986, as amended, which code section provides for the NMTC. The mechanism of enactment was to incorporate by reference (as appendix G to Public Law 106-554) the provisions of H.R. 5662, the Community Renewal Tax Relief Act of 2000, as introduced on Dec. 14, 2000. Section 121 of the CRTRA contains the NMTC provisions, 114 Stat. 2763A-605 through 2763A-611.

Basic NMTC rules

The NMTC is one of the general business tax credits of Section 38 of the code, and is thus subject to the rules governing the use of general business credits. For example, under Section 38(c)-(d) of the code, the NMTC is a non-refundable tax credit and is subject to the general business tax credit ordering rules. The NMTC does benefit from the one-year business credit carryback and 20-year business credit carryforward provisions of Section 39 of the code.

To be eligible for the NMTC during a taxable year, a taxpayer must under Section 45D(a)(1) of the code hold a “qualified equity investment” on a “credit allowance date” of such investment. The amount of the NMTC under Section 45D(a)(1) of the code equals the “applicable percentage” of the “amount paid” to a “qualified community development entity” for such investment at its original issue. The “amount paid” includes underwriter’s fees. Section 1.45D-1(b)(4) of the regulations promulgated by the U.S. Department of the Treasury under the code. Pursuant to Section 45D(a)(2)-(3) of the code, the “applicable percentage” is 5 percent for the first three “credit allowance dates” (a “credit allowance date” being the date of initial investment and each of the next six anniversary dates), and 6 percent for the next four credit allowance dates.

Section 45D(b) of the code sets forth the parameters for determining whether an investment is a “qualified equity investment.” These parameters are as follows:

• The taxpayer must acquire an “equity investment” in a “qualified community development entity” at its original issue (directly through an underwriter) solely in exchange for cash, or, in the case of a taxpayer who is a subsequent purchaser that would qualify under these rules except for failing the original issue test, such taxpayer must acquire an investment that was a “qualified equity investment” in the hands of the seller.

• Substantially all of such cash must be used by the “qualified community development entity” within 12 months of the date of receipt of the cash to make “qualified low-income community investments.” Section 1.45D-1(b)(5)(iv) of the Treasury regulations. “Substantially all” means at least 85 percent for each of the first six years of the credit period and at least 75 percent for the final year of the credit period. See Section 1.45D-1(b)(5)(v) of the Treasury regulations.

• The “qualified community development entity” designates such investment for code purposes on its books and records using any reasonable method. See Section 1.45D-1(c)(1)(iii) of the Treasury regulations.

• An “equity investment” means any stock (other than nonqualified preferred stock as defined in Section 351(g)(2) of the code) in a corporation and any capital interest in a partnership. The investor may derive the funds to make an equity investment from a loan including without limitation a non recourse loan. Revenue Ruling 2003-20, 2003-1 C.B. 465. Under Section 1.45D-1(c)(2) of the Treasury regulations, the general entity classification rules of Sections 301.7701-1 through 301.7701-3 of the Treasury regulations are used to determine whether an entity qualifies as a corporation or a partnership. However, the “qualified community development entity” may not issue more equity investments than the amount allocated to said entity by the Treasury secretary or the Treasury secretary’s designee. In addition, if a “qualified community development entity” issues an investment more than five years after the date of allocation receipt, such investment will not qualify for the NMTC. An equity investment by a “qualified community development entity” in another one does not qualify for the NMTC if the investing entity has received an allocation. See below for a...
discussion of the allocation procedures.

- The redemption limitations of Section 1202(c)(3) of the code apply to redemptions by “qualified community development entities” of stock of investors seeking the NMTC.

Under Section 45D(c)(1) of the code, a “qualified community development entity” is a domestic corporation or partnership if (i) its primary mission is serving or providing investment capital for “low-income communities” or low-income persons, (ii) it maintains accountability to residents of “low-income communities” through representation on any entity governing board or entity advisory board, and (iii) it is certified by the Treasury secretary or the Treasury secretary’s designee for purposes of code Section 45D as a qualified community development entity. These requirements are treated as met by any specialized small business investment company (as defined in code Section 1044(c)(3)) and by any community development financial institution (as defined in Section 103 of the Community Development Banking and Financial Institutions Act of 1994). Section 45D(c)(2) of the code.

The four types of investments, each of which constitutes a “qualified low-income community investment,” are set forth in Section 45D(d)(1) of the code. These types are as follows:

- Any capital or equity investment in, or loan to, any “qualified active low-income community business.”
- The purchase by a qualified community development entity of a loan from another CDE, which loan itself is a “qualified low-income community investment.”
- Financial counseling and other services specified in Treasury regulations to businesses located in, and residents of, low-income communities. Under Section 1.45D-1(d) (7) of the Treasury regulations, such services consist of advice provided by the CDE relating to the organization or operation of a trade or business.
- Any equity investment in, or loan to, any CDE.

Pursuant to Section 45D(d)(2) of the code, any for-profit or nonprofit corporation, any proprietorship and any partnership may constitute a “qualified active low-income community business” if for the taxable year in question the following standards are met (either with respect to all trades or businesses carried on by the entity in question or with respect to any trade or business which if separately incorporated would qualify under the following standards):

- The entity derives at least 50 percent of its total gross income from the active conduct of a “qualified business” within any “low-income community.”
- A substantial portion (under Section 1.45D-1(d)(4)(i)(B)(1) of the Treasury regulations, a substantial portion being at least 40 percent) of such entity’s use of owned or leased tangible property is within any “low-income community.”
- A substantial portion (under Section 1.45D-1(d)(4)(i)(C) of the Treasury regulations, a substantial portion being at least 40 percent) of the services performed for such entity by its employees are performed in any “low-income community.” For an entity with no employees, such entity is deemed to meet both this test and the 50 percent total gross income test if at least 85 percent of such entity’s use of owned or leased tangible property is within any “low-income community.”
- Less than 5 percent of the average of the aggregate unadjusted bases of such entity’s property is attributable to collectibles (as defined in code Section 408(m)(2)) other than collectibles held primarily for sale to customers in the ordinary course of said business.
- Less than 5 percent of the average of the aggregate unadjusted bases of such entity’s property is attributable to “nonqualified financial property” (as defined in code Section 1397C(e)). Thus, “nonqualified financial property” means debt, stock, partnership interests, options, futures contracts, forward contracts, warrants, notional principal contracts, annuities and other similar property. Section 1.45D-1(d)(4)(i)(E) of the Treasury regulations. Reasonable amounts of working capital held in cash, cash equivalents or debt instruments with a term of 18 months or less, and accounts or notes receivable acquired in the ordinary course of trade or business for services rendered or from the sale of inventory or inventory-type property, are not classified as “nonqualified financial property.” Id. Under this definition of nonqualified financial property, banks and other financial institutions generally would not constitute qualified active low-income community businesses.

A “qualified business” means (i) any trade or business that is not (A) a real property rental business (with the exception noted in “(ii)” below), or (B) the operation of any private or commercial golf course, country club, massage parlor, hot tub facility, suntan facility, racetrack or other gambling facility or liquor store (any activity described in this clause “(i) (B)” constituting a “prohibited activity”), or (C) farming, and (ii) a real property rental business as long as (A) the property is not residential rental property (as defined in code Section 168(e)(2)(A)) or the rental to a lessor engaged in a prohibited activity and (B) there are substantial improvements located on the real property. Sections 45D(d)(3) and 1397C(d) of the code, and Section 1.45D-1(d)(5) of the Treasury regulations.

An entity is treated as engaged in the “active conduct” of a trade or business if, at the time of the CDE’s investment in or loan to such entity, the CDE reasonably expects that the entity will generate revenues (or, for a nonprofit corporate entity, engage in an activity furthering its nonprofit purpose) within three years after the making of said investment or loan. Section 1.45-1(d)(4)(iv) of the Treasury regulations.

In general, a “low-income community” means any of the following: (i) a population census tract with a poverty rate of at least 20 percent, (ii) a non-metropolitan area population census tract in which the median family income does not exceed 80 percent of statewide median family income, (iii) a metropolitan area population census tract in which the median family income does not exceed 80 percent of the greater of (A) statewide median family income or (B) metropolitan area median family income, and (iv) certain targeted populations treated as low-income communities pursuant to Treasury regulations. Section 45D(e)(1)–(2) of the code. For areas not tracted for population census tracts, equivalent county divisions are used for purposes of determining poverty rates and median family income. Section 45D(e)(3) of the code. There are special rules for population census tracts with populations of less than 2,000 and for census tracts within high mi-
The NMTC is subject to recapture if at any time during the seven-year period beginning on the date of the original issue of a qualified equity investment in a CDE, (i) such CDE ceases to so qualify, (ii) less than substantially all of the cash received from said investment is used to make qualified low-income community investments, or the entity redeems said investment. Section 45D(g) of the code. Other than for the purpose of determining the partial gain exclusion for gain from the sale or exchange of qualified small business stock under Section 1202 of the code, and for determining qualified capital gain for purposes of the zero qualified capital gain rate from the sale or exchange (A) of any DC Zone asset held for more than five years pursuant to Section 1400B of the code or (B) of any qualified community asset held for more than five years under Section 1400F of the code, the basis of a qualified equity investment is reduced by the amount of the NMTC determined under code Section 45D. Section 45D(h) of the code.

Taxpayers claim the NMTC on Form 8874. A CDE must notify a taxpayer acquiring a qualified equity investment in the CDE at its original issue that the taxpayer is entitled to claim the NMTC. Section 45D(i)(4) of the code and Section 1.45D-1(g)(2) of the Treasury regulations. The notice must be provided no later than 60 days after the investment date and must include the amount paid to the CDE for the qualified equity investment and the CDE’s taxpayer identification number. Id.

Section 45D(i)(1) of the code authorizes the promulgation of Treasury regulations limiting the NMTC for investments that are directly or indirectly subsidized by other federal tax benefits including the low-income housing tax credit under code Section 42 and the tax-exempt bond exclusion under code Section 103. However, the current Treasury regulations prohibit “double dipping” only with respect to the low-income housing tax credit. Section 1.45D-1(g)(3) of the Treasury regulations.

Credit allocation limitation and CDE designation

The amount of investments that CDEs may designate as qualified equity investments is subject to a calendar year limitation under Section 45(f) of the code. The limitation for 2007 is $3.5 million. Section 45(f)(1)(D) of the code. The Treasury secretary or the Treasury secretary’s designate is required to allocate the limitation among CDEs selected by the Treasury secretary or the Treasury secretary’s designee, who is required to give priority to any CDE (i) with a record of successful provision of capital or technical assistance to disadvantaged businesses or communities, or (ii) which intends to satisfy the requirement that substantially all of the qualified equity-generated cash acquired by the CDE be used to make qualified low-income community investments by making said investments to one or more businesses in which persons unrelated to such CDE (within the meaning of code Section 267(b) or 707(b)(1)) hold the majority equity interest. Section 45D(f)(2) of the code. Unused limitation increases next year’s limitation amount, except that no carryover is allowed to a calendar year after 2014, Section 45D(f)(3) of the code.

The Treasury secretary has delegated to the Community Development Financial Institutions Fund (CDFIF) in the U.S. Treasury Department the responsibility for certifying organizations as CDEs and for allocations to CDEs of the national investment limitations. See Guidance, New Markets Tax Credit Program, 66 Fed. Reg. 21846 (May 1, 2001). For information on the application process to be designated as a CDE, and on amounts allocated to existing CDEs, go to the following Web address: www.cdfifund.gov/what_we_do/programs_id.asp?programID=5.

The CDFIF Web site includes the necessary CDE certification and allocation application materials, a frequently asked questions document, U.S. Government Accountability Office reports on the NMTC, notices of recent NMTC developments, IRS materials and other materials that will be helpful to investors seeking NMTCs, to community development organizations seeking CDE certification and to community-based businesses seeking capital or organizing and operating advice.
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