

BUSINESS LITIGATION

Are Corporate Leaders Vulnerable Under CUTPA?

COURTS WEIGH IN ON ISSUE OF PERSONAL LIABILITY FOR CERTAIN CONDUCT

By DAVID L. BELT

One reason individuals set up a corporation or a limited liability company to conduct their businesses is to shield themselves from personal liability for obligations of their businesses. Generally, an officer of a corporation is not personally liable for torts or contract breaches of a corporation merely because of his or her position. However, a corporate officer, director or employee may personally be liable for tortious conduct in which he or she participates. Nevertheless, several recent trial court decisions have held that personal liability may not be imposed on an officer or employee for violating the Connecticut Unfair Trade Practices Act (CUTPA). This is important because CUTPA provides for the imposition of punitive damages and attorneys' fees in addition to actual damages.

In one such case, *Metcoff v. Lebovics*, 51 Conn. Sup. 68, 87-88 (2007), the court held that "the actions of an officer, director or employee taken on behalf of the corporation and within the context of his corporate responsibilities are ordinarily outside of CUTPA's application." The court reasoned that "an officer, director or employee of a corporation primarily provides services to the corporation and therefore is not engaged 'in the conduct of any trade or commerce' within the meaning of CUTPA." The scope of CUTPA is not unlimited. It prohibits only "engag[ing] in unfair methods of competition and unfair or deceptive acts or practices in the conduct of any trade or commerce."

The court held that its conclusion followed from decisions holding that an officer, director or employee of a corporation provides services to the corporation "and is not, therefore, engaged in the conduct of 'any trade or commerce' within the meaning of CUTPA. The court concluded

that the "corporation itself may be engaging in a trade or business in commerce, but not the individual who is merely working for or on behalf of the corporation." In reaching its conclusion, the court appeared to have been swayed by its concern that to hold otherwise would mean "any employee or officer of a corporation would . . . simply by going to work, be individually subjected to the provisions of CUTPA."

Other trial court decisions have held that CUTPA liability may indeed be imposed on an officer, director or employee if the person personally participates in the violation. See *Pabon v. Recko*, 122 F.Supp. 2d 311, 313 (D. Conn. 2000). These decisions follow the general rule that an officer of a corporation may incur personal liability for torts in which he or she participates.

Pabon also addressed the "trade or commerce" issue by noting that decisions holding that the relationship between employer and employee is not trade or commerce should not be taken to mean that employees may not be sued under CUTPA. This conclusion is supported by the language of the Act, which prohibits a "person" from engaging in certain acts or practices in "any trade or commerce." "Person" is defined in the Act to include both corporations and individuals. And, rather than prohibiting the proscribed conduct in the violator's trade or commerce, it prohibits that conduct in "any trade or commerce."

Another trial court has indicated that CUTPA liability may be imposed on an employee, but only where his or her participation was knowing and intentional. *Pfeifer v. Logault & Sons Construction*, 2000 WL 3290545 at 3 (Conn. Super. Ct. Oct. 26, 2006). This approach is supported by the common law principle that an agent is not normally liable for innocent misrepresentations made in the course of the agent's employ-

ment, at least where the agent did not have a direct pecuniary interest in the transaction.

Going beyond the decisions specifically addressing personal liability under CUTPA, the federal courts have held that an individual who participates in a violation may be held personally liable under the Federal Trade Commission Act. See *F.T.C. v. World Media Brokers*, 415 F.3d 758, 764 (7th Cir. 2005); although the wording of the federal statute, which prohibits "[u]nfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce" is somewhat broader than that of CUTPA. Courts in other states with statutes similar to CUTPA have reached differing conclusions concerning whether personal liability can be imposed on employees who participate in prohibited conduct.

Still Unresolved

In a 2010 decision, the Connecticut Supreme Court went out of its way to note that it "express[ed] no opinion regarding what our law is or should be with regard to an individual's liability for a corporation's violation of CUTPA." *Sturm v. Harb Development LLC*, 298 Conn. 124, 139 (2010). In that case, neither party raised or briefed the issue and seemed to assume the ex-



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istence of an individual's liability for a corporation's violation of CUTPA. The court concluded that it would "leave the resolution of this issue for another day," indicating that it is aware of this issue, but that it was still unresolved at an appellate level in Connecticut.

The Appellate Court has just addressed this issue in *Cohen v. Roll-A-Cover LLC*, a decision officially released in September. In *Cohen*, the Appellate Court affirmed a trial court decision holding the president of an LLC individually liable under CUTPA. The court applied the principle that when an agent or officer commits or participates in the commission of a tort, or directs that a tortious act be done, he or she is liable to third persons injured.

Although quoting from the Supreme Court's decision in *Sturm*, the Appellate Court did not note the Supreme Court's express reservation of opinion as to whether individual liability can be imposed on officers and directors under CUTPA. Nor did the Appellate Court address whether an individual officer or director was acting in trade or commerce, the requirement focused on in *Metcoff*. The trial court in *Cohen* had discussed *Metcoff*, but only to distinguish it on the grounds that the defendants in *Metcoff* had not been alleged to have engaged in conduct directly against the plaintiff.

In light of the Appellate Court's decision in *Cohen*, it appears that individual officers, directors and employees may have personal liability under CUTPA for violations in which they participate unless and until the Connecticut Supreme Court takes up this issue and reaches a contrary conclusion. ■

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Are Your State Law Claims Preempted By Federal Law?

LACK OF EXPLICIT STATEMENTS FROM CONGRESS CAN LEAD TO LITIGATION

By JOSEPH CHERICO

If you are representing clients in litigation where state law claims are asserted but federal law is potentially implicated, then it is important to analyze whether those state law claims are altogether preempted by federal law, particularly in light of recent decisions by the U.S. Supreme Court. In fact, various cases in Connecticut have been dismissed based on the doctrine of federal preemption.

The question of preemption is one of federal law, arising under the supremacy clause of the U.S. Constitution. As the Connecticut Supreme Court has noted, determining whether Congress has exercised its power to preempt state

law is a question of legislative intent. Preemption may be either "express" or "implied."

Express preemption occurs where federal law expressly directs that state law is to be ousted to some degree from a certain field. For example, in 1990, Congress amended the federal Food, Drug and Cosmetic Act (FDCA) by enacting the Nutrition Labeling and Education Act (NLEA), which expressly provides that state law is preempted where it seeks to impose requirements regarding certain food labels if those requirements are not identical to the requirements imposed by federal law.

Similarly, Congress had previously amended the FDCA by enacting the Medical Device Amendments (the MDA), which expressly

provides that state law is preempted where it seeks to impose requirements relating to the safety or effectiveness of a medical device if those requirements are different from or in addition to the requirements imposed by federal law.

Implied preemption occurs absent an explicit statement from Congress that it intends to preempt state law where Congress nonetheless has legislated comprehensively to occupy an entire field of reg-



Joseph Cherico

ulation or where the state law at issue conflicts with federal law. State law conflicts with federal law where it is impossible to comply with both or where the state law otherwise stands as an obstacle to the objectives of federal law.

Even where an express preemption provision exists, there are often questions regarding the scope of its application. Thus, for example, there have been various lawsuits to determine whether a cause of action based on state law seeks to impose requirements that are "identical" to federal law as reflected in the NLEA or seeks to impose requirements that are "different from or in addition to" the requirements imposed by federal law under the MDA.

Not surprisingly, the application of implied preemption principles is heavily litigated as well, particularly because that doctrine is defined by its lack of any explicit statement from

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Re-Shaping Businesses To Eliminate Fraud Triangle

WEAK INTERNAL CONTROLS CAN LEAD TO WHITE COLLAR CRIME

By MICHAEL D. FRENZA

White collar criminals (or fraudsters) are not easily picked out from a crowd. They blend in seamlessly with society and do not look like criminals. They are likely educated, with no criminal record, and probably do not abuse drugs or alcohol.

Fraudsters do not linger in dark alleys wearing a trench coat while they prey on

elements in most fraud cases. Fraud perpetrators usually have a non-sharable *pressure*; they recognize a perceived *opportunity*; and then they *rationalize* their actions. These three traits are commonly known as the "Fraud Triangle."

Examples of non-sharable pressures include excessive debt, addiction (for example, gambling) and status-seeking. Once an employee has a non-sharable pressure, they must find an opportunity to remedy their problem.

organizations to proactively recognize pressures facing employees by being vigilant.

Red Flags

Non-sharable pressures may not ordinarily be observed in employees until after a fraud has been discovered. Only after a fraud is perpetrated do the pieces of the puzzle get put together and tell the whole story. Therefore, it is imperative that organizations *know their employees*. Prior to hiring an employee, that individual should have a background check performed. If he or she will be in a position to handle finances, a credit check should be done. After all, if someone previously filed for bankruptcy or had credit problems, that person probably shouldn't be appointed in charge of paying the organization's bills.

The organization should be rational about employees' work habits. For instance, an employee who gets to work early, stays late and rarely takes vacation should raise a red flag. While workaholics may be lauded as "model" employees, a smart organization would ask, "Why is this employee working so hard? What is his or her motivation?"

The organization should observe if employees are gamblers, have large financial losses or are deep in personal debt. Do they appear to live beyond their means? Do they discuss their problems at work? The more an organization knows about an employee, the more likely they are to recognize the symptoms of financial pressure.

The organization's *greatest* control over the three Fraud Triangle components is to minimize the opportunity to commit a theft. Everything starts with leading by example. If management is dishonest or absentee, then the risk of theft by employees is greater.

Second, effective control activities and procedures should be in place, such as segregation of duties. Segregation of duties ensures that one person does not manage an entire process. Ideally, three people should participate in a control process. For example, one person collects cash,

a second counts the cash and a third posts the cash to the accounting records. Control procedures should ensure that transactions are properly authorized.

Third, the organization should have adequate documents and records and maintain physical control over those records. This assures an adequate audit trail exists. Fourth, independent checks—such as detection controls—may not only detect fraud but increase the perception that fraud will be discovered to *deter* fraudulent behavior. While no system of internal controls is perfect, it should periodically be reviewed, tested and modified to verify that any weaknesses are promptly identified and corrected. Too many organizations focus on revenue-generating activities and neglect a strong system of internal controls.

Lastly, hiring an independent third party to analyze internal controls and provide recommendations for improvement through a fraud risk assessment may help to identify fraud risks.

While addressing fraud risks, organizations should examine the cost-versus-benefit to ensure they concentrate on areas where the most vulnerability exists. Organizations need to take the emotional aspect out of their decisions to implement controls (e.g., "Suzy the bookkeeper is a longtime employee, she would never steal."). By proactively addressing each leg of the Fraud Triangle, organizations can better identify red flags of fraudsters, reduce their exposure to fraud risk and avoid becoming another victim. ■



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victims. They disguise themselves as college graduates, churchgoers or even Employees of the Month. In other words, they look "normal," with traits that organizations look for in potential employees.

That said, how can organizations become more vigilant in recognizing the signs of a fraudster? And how can an organization protect itself from becoming a victim?

An organization must recognize the common

An astute fraudster will find an opening in the organization, exploit it and feed their appetite until they are caught. Opportunity comes in many forms, including:

- Weak or non-existent internal controls which fail to prevent or detect fraud.
- Lack of oversight by supervisors.
- Failure to discipline past perpetrators (i.e., no fear of reprisal)
- Lack of an audit trail.

After a fraudster takes advantage of an opportunity, he or she typically rationalizes his/her actions. This takes the form of an excuse used by the perpetrator to alleviate his/her guilt. Since most fraudsters are first-time offenders, they do not view themselves as criminals. They rationalize their actions using typical excuses: "I will borrow the money now and pay it back once I turn things around."

An organization usually has the *least* control over the rationalization component of the Fraud Triangle, since it is up to the fraudster to justify his actions. The pressure component of the Fraud Triangle is typically not easily controlled by organizations. Therefore, it is important for

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Congress regarding its intent to preempt state law claims. The importance of that doctrine is evidenced by the recent attention that it has been given by the U.S. Supreme Court. Indeed, at the end of its most recent term, the Supreme Court issued a significant decision with respect to the doctrine of implied preemption.

Drug Labels

On June 23, 2011, the Supreme Court issued its decision in *Pliva Inc. v. Mensing*, 131 S.Ct. 2567 (2011). In *Pliva*, plaintiffs were individuals who began to suffer from a particular disorder after years of taking a certain generic prescription drug. Plaintiffs sued the manufacturers of that drug, alleging liability under state law for failure to include a warning label regarding the increased risks of developing that disorder. The manufacturers argued that plaintiffs' state law claims were preempted by federal law. The Court ruled in favor of the manufacturers.

In reaching its decision, the Court explained that, under federal law, a manufacturer seeking Food and Drug Administration approval to market a new drug must prove that the drug is safe and effective and that the proposed label is accurate and adequate. The manufacturer of a generic drug, however, can gain FDA approval by simply showing equivalence to a drug that has already been approved by the FDA, in which case the generic drug manufacturer is required to use the same label approved for the brand-name drug. Moreover, according to the FDA, generic drug manufacturers cannot

change the label without FDA approval, even if the intention is to provide a stronger warning.

In this case, there was no dispute that the manufacturers used the same label that had been approved for use with the brand-name drug. There was also dispute that, in light of the federal regulatory structure, the manufacturers could not unilaterally change their labels to provide the stronger warning that was required by state law. As a result, the Court determined that it was impossible for the manufacturers to comply with both state and federal law. The Court therefore held that state law directly conflicted with the federal regulations applicable to generic drug manufacturers and, thus, plaintiffs' claims were preempted.

As the Court explained, its decision in *Pliva* is consistent with the Court's prior decision in *Wyeth v. Levine*, 129 S.Ct. 1187 (2009). *Wyeth* likewise involved the claim that a drug manufacturer failed to include an adequate warning label in violation of state law. There, however, the drug in question was a brand-name drug, and FDA regulations allow brand-name drug manufacturers to unilaterally strengthen their warning labels. As a result, the Court held that it was not impossible for the manufacturer to comply with both state and federal law in that case and, thus, the Court rejected the argument that plaintiff's claims were preempted.

Importantly, Connecticut courts recognize that state law claims may be preempted by federal law. For example, in *Cardinale v. Quorn Foods Inc.*, 2011 WL 2418628 (Conn. Super. Ct. May 19, 2011), plaintiff brought a putative class action against the manufacturer of a meat-free food product, alleging that the manufacturer

failed to include a label warning consumers that the primary ingredient in that product may cause an allergic reaction. The Court held that plaintiff's claims were preempted by federal law.

In particular, the Court noted that the product ingredient was "generally recognized as safe" under FDA regulations, and that plaintiff was, in essence, asking the Court to revoke that status and to impose a labeling requirement that was inconsistent with a finding that the ingredient was safe. The Court explained that the FDA has specialized knowledge regarding the safety of food products, that Congress had legislated to ensure uniform labeling requirements throughout the country for food products containing potential allergens, and that the safety of this particular ingredient was already under consideration by the FDA.

The Court further explained that the question of a food product's safety and labeling requirements should not be addressed on an ad hoc basis by each of the 50 states, because that could lead to inconsistent rulings. Accordingly, the Court granted the manufacturer's motion to dismiss the complaint in its entirety based on the doctrine of federal preemption.

In short, as a practical matter, attorneys involved in litigation that implicates federal law must be careful to first analyze whether any state law claims are expressly preempted by federal law and, second, even if not expressly preempted, whether those state law claims are impliedly preempted based on congressional intent to regulate an entire field or based on an outright conflict between the state law requirements sought to be imposed and federal law. ■

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Recent Developments Regarding Preferential Transfers

COUNSEL MUST CAREFULLY CONSIDER WHETHER COMPLAINT IS ADEQUATELY PLEADED

By IRVE GOLDMAN

The potential for recovering payments received by a creditor within 90 days of its debtor's bankruptcy filing is a familiar aspect of bankruptcy law.

Familiarity aside, preference law, which has as its rationale equality of distribution among all of a debtor's creditors, is never easily justified to a creditor who is asked to contribute even more to a debtor's bankruptcy cause. Recent developments in preference law, however, can at least give the defending counsel some additional tools to work with in warding off a preference recovery.

Pleading Requirements

In *Ashcroft v. Iqbal*, 129 S. Ct. 1937 (2009), the U.S. Supreme Court ruled that its decision in *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007), which imposed heightened pleading requirements for an anti-trust complaint, applied to all civil complaints by operation of Federal Rules of Civil Procedure 8(a)(2).

Also according to *Iqbal*, "[t]hreadbare recitals of the elements of a cause of action, supported by mere conclusory statements, do not suffice."

As confirmed by recent bankruptcy decisions, the more stringent pleading requirements brought about by *Twombly* and *Iqbal* apply equally to preference complaints brought in bankruptcy court. Such complaints, like any other complaint filed in bankruptcy court, are governed by Rule 8 of Federal Rules of Civil Procedure, which applies to adversary proceedings filed in bankruptcy court pursuant to Rule 7008 of the Federal Rules of Bankruptcy Procedure.

Even before *Twombly* and *Iqbal*, most courts held that to adequately plead a cause of action for a preferential transfer, the complaint must identify each transfer, usually a payment, by date, amount, name of transferor and name of transferee. See, for example, *In re Valley Media, Inc.*, 288 B.R. 189, 192 (Bankr. D. Del. 2003). But after *Twombly* and *Iqbal*, the pleading requirements for preference complaints have become more exacting.

For example, when there is a multi-debtor, jointly administered bankruptcy case or more than one possible transferee defendant, it will not be sufficient to allege that "one or more of the debtors" made a preferential transfer. See *In re Crucible Materials Corp.*, 2011 WL 2669113 at *4 (Bankr. D. Del. July 6, 2011); *In re Tweeter Opco*, 452 B.R. 150, 154-55 (Bankr. D. Del. June 14, 2011), or that "one or more of the defendants" received a preferential transfer. See *In re WBE, LLC*, 2011 WL 2607090, at *3 (Bankr. D. Del. June 30, 2011). The specific transferor and transferee need to be identified.

It is also no longer sufficient to parrot the statutory requirement that a transfer have been "for or on account of an antecedent debt owed by the debtor before such transfer was made." 11

U.S.C. §547(b) (2). An "antecedent debt" is simply a debt of the debtor that existed prior to the challenged transfer. Bankruptcy courts now require that a preference complaint contain factual detail explaining the nature and amount of the "antecedent

debt" that was paid by the challenged transfer, such as "any contracts between the parties or [a] description of the goods and services exchanged." *In re Crucible Materials Corp.*, 2011 WL 2669113, at *4 (Bankr. D. Del. July 6, 2011); *In re Tweeter Opco*, 452 B.R. 150, 155 (Bankr. D. Del. June 14, 2011). See also *In re Hydrogen LLC*, 431 B.R. 337, 355 (Bankr. S.D.N.Y. 2010) (dismissing preference claims because "no allegation has been made that any transfer was made for or on account of a specific and identifiable antecedent debt").

Transfers to an "insider" of the debtor may also be captured if made between 90 days and one year before a bankruptcy filing, but for these types of transfers, unlike transfers within the 90-day period, the statutory element of insolvency is not presumed. As a result of *Twombly* and *Iqbal*, at least one court has held that for insider transfers, "the trustee must allege facts sufficient to show that such insolvency is plausible." *In re Caremerica*, 409 B.R. 737, 752 (Bankr. E.D.N.C. 2009). In addition, the complaint must set forth a factual basis for the conclusion that the recipient of the transfer is an "insider." *In re Sand Hill Capital Partners III*, 2010 WL 4269622, at*2 (Bankr. N.D. Cal. Oct. 25, 2011); *In re Caremerica Inc.*, 415 B.R. 200, 206 (Bankr. E.D.N.C. 2009).

While pleading a preference cause of action has become more demanding, courts have been liberal in allowing amendments to the complaint to cure the deficiencies. Whenever an amendment to a complaint is requested after the statute of limitations has expired, however, there is an issue of whether the proposed amendment relates back to the timely filed complaint.

The statute of limitations for bringing a preference action is generally the later of two years after a bankruptcy is filed or, if a trustee is appointed within that two-year period (as in the case of the appointment of a Chapter 11 trustee when the case is originally administered by a debtor-in-possession), one year after the trustee's appointment. In many cases, the plaintiff in a preference action will commence the action shortly before the statute of limitations has expired, so the relation-back issue has a tendency to occur with greater frequency in preference litigation.

The general rule is that a proposed amend-



Irve Goldman

ment will relate back to the original pleading under FRCP 15(c), made applicable to adversary proceedings by FRBP 7015, if it "spells out the details of the transaction originally alleged..." *In re Austin Driveway Services Inc.*, 179 B.R. 390, 395 (Bankr. D. Conn. 1995). The originally plead transfer in a preference complaint, however must at least be detailed enough on its face to disclose that it is seeking recovery of the same transfer set forth in the proposed amendment. *In re Austin Driveway Services* (quoting *Dworsky v. Alanjay Bias Binding Corp.*, 182 F. 2d 803, 805 (2d Cir. 1950)). Depending on the circumstances, therefore, a proposed amendment to a preference complaint could be barred by the statute of limitations.

Ordinary Course

One of the more common defenses to a preference is that it was made in the "ordinary course of business." 11 U.S.C. §547(c)(2). Prior to the 2005 amendments to the Bankruptcy Code, this defense required proving that the transfer was "ordinary" between the parties themselves as well as "ordinary" according to industry standards. The 2005 amendments made this for-

merly conjunctive test a disjunctive one.

A significant development under this defense for creditors with a longer-term relationship with the debtor was ushered in by the decision in *In re Archway Cookies*, 435 B.R. 234 (Bankr. D. Del. 2010). There, the bankruptcy court found it relevant to consider the length of the relationship between the debtor and creditor and "a debtor's need to maintain constructive relationships with certain creditors" in determining whether to protect a payment from avoidance. According to the court, a creditor whose relationship with the debtor "has been cemented long before the onset of insolvency," should be given greater leeway in deciding what is "ordinary" between the parties.

Conclusion

Creditors' counsel defending a preference action should now carefully consider whether the complaint adequately pleads the elements of a preference. If the client is an important or long-standing vendor of the debtor, counsel should be aware that this relationship might be a basis for receiving greater leeway in asserting the "ordinary course of business" defense. ■



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Hyped Rulings Have Caused Little Actual Change

THERE'S BEEN NO RADICAL INCREASE IN NUMBER OF CASES DISMISSED

By **THOMAS ROHBACK**

When the Supreme Court issued its decision in *Bell Atlantic Corp. v. Twombly*, the legal community was flooded with pundits predicting radical changes in the way federal district courts would rule on motions to dismiss. Two years later, the Court's decision in *Ashcroft v. Iqbal* amplified the din. More recently, the Supreme Court's "landmark decision" in *Wal-Mart v. Dukes* has been portrayed as the death knell for massive class actions.

Reality, however, does not reflect this hysteria. The three rules at the heart of these decisions – Federal Rules of Civil Procedure 8, 12(b)

plaint must have more than "threadbare" allegations of the legal elements of a cause of action and that the factual allegations need to describe a "plausible" cause of action. Interestingly, Justice David Souter wrote the Court's opinion in *Twombly*, but dissented in *Iqbal*. Arguably, he was right both times.

In *Twombly*, the complaint had nothing but the formulaic recitation of legal elements and failed to state a "plausible" claim because there were no facts to flesh out the legal frame. In contrast, the complaint in *Iqbal* did have detailed factual allegations, and the Court of Appeals affirmed the denial of a motion to dismiss after *Twombly*. The Supreme Court, how-

ever, and especially with *Iqbal*, is that these decisions require courts to make subjective "plausibility" determinations. But in some sense, courts were doing this long before *Iqbal*. They ruled on motions to dismiss by assessing "the legal

feasibility of the complaint" and by drawing "all reasonable inferences" from all "well-pleaded allegations." See *Ryder Energy Distrib. v. Merrill Lynch Commodities Inc.*, 748 F.2d 774, 779 (2d Cir. 1984); *Boursiquot v. Citibank F.S.B.*, 323 F. Supp. 2d 350, 353 (D. Conn. 2004); *Duse v. Int'l Bus. Machines Corp.*, 748 F. Supp. 956, 959 (D. Conn. 1990).

In *Thornberry v. Tolisano*, No. 3:06-cv-1375, 2007 U.S. Dist. LEXIS 28810 (D. Conn. Apr. 16, 2007), U.S. District Judge Warren Eginton granted a motion to dismiss a Connecticut Unfair Trade Practices Act and Fair Debt Collection Practices Act complaint in language that sounds as if it came right from *Iqbal*: "Defendant argues that plaintiff's complaint cannot withstand a motion to dismiss because it is merely a skeletal outline that sets forth bald conclusory accusations that defendant violated federal and state law. Both counts of the complaint are completely devoid of any factual allegations to support plaintiff's claims of any statutory violations. While plaintiff does cite statutes which he claims defendant violated, he provides no substance to his claims. 'Conclusory allegations or legal conclusions masquerading as factual conclusions will not suffice to prevent a motion to dismiss.'" *Smith v. Local 819 I.B.T. Pension Plan*, 291 F.3d 236, 240 (2d Cir. 2002).

As this language and analysis suggests, federal district courts required more than "threadbare" conclusory allegations before *Twombly* and *Iqbal*. (*Thornberry* was decided on April 16, 2007; *Twombly* was decided on May 21, 2007.)

So too, after *Twombly* and *Iqbal*, complaints have not been dismissed where the allegations are more than legal conclusions. In *Empower Health LLC v. Providence Health Solutions LLC*, No. 3:10-cv-1163, 2011 U.S. Dist. LEXIS 60142 (D. Conn. June 3, 2011), the court, citing *Iqbal*, refused to dismiss a host of claims. U.S. District Judge Janet Hall explained that the challenged complaint contained sufficient factual allegations that were more than a formulaic recitation of the legal elements. In contrast, Judge Hall granted the motion to dismiss in *Gabriele v. Sanzaro*, No. 3:10-cv-38, 2010 U.S. Dist. LEXIS 72546 (D. Conn. July 19, 2010), because, although the veil piercing claim "allege[d] all the elements" of the cause of action, it contained no factual allegations, merely a recitation of the instrumentality rule. This same analysis and result would have occurred before and after *Twombly*.



Thomas Rohback

The 2nd Circuit Court of Appeals opinion in *Arista Records LLC v. DOE 3*, 604 F.3d 110 (2d Cir. 2010), makes it clear that *Twombly* and *Iqbal* are not a radical break from the notice pleading requirements of Rule 8: "First, the notion that *Twombly* imposed a heightened standard that requires a complaint to include specific evidence, factual allegations in addition to those required by Rule 8, . . . is belied by the *Twombly* opinion itself. . . ."

"The *Twombly* plausibility standard does not prevent a plaintiff from 'pleading facts alleged upon information and belief' where the facts are peculiarly within the possession and control of the defendant or where the belief is based on factual information that makes the inference of culpability plausible. . . ."

Although a 2010 statistical study concluded that *Twombly* and *Iqbal* resulted in a greater percentage of motions to dismiss being granted, the author's conclusions were based on motions with leave to amend. (Patricia Hatamyar, "The Tao of Pleading: Do *Twombly* and *Iqbal* Matter Empirically?" *American University Law Review*, 553, 556 (2010))

According to the study, the percentage of motions granted without leave show that a smaller percentage were granted after *Iqbal*. (40 percent before *Twombly*; 39 percent after *Twombly*; and 37 percent after *Iqbal*). The Federal Judicial Center confirms that "there was no increase in the rate of grants of motions to dismiss without leave to amend" and "there was no increase from 2006 to 2010 in the rate at which a grant of a motion to dismiss terminated the case."

The statistics for business cases are particularly revealing. In segregating contract actions (without distinguishing between dismissals with or without leave to amend), 32 percent of all 12(b)(6) motions were granted before *Twombly*; 35 percent granted after *Twombly*; and 32 percent granted after *Iqbal*. Even if there are some areas where complaints are becoming more likely to be dismissed, this may not be true for commercial contract cases.

Class Actions

Just as *Twombly* and *Iqbal* have been trumpeted in the press as revolutionizing pleading standards in federal court, the Supreme Court's recent decision in *Dukes* has been decried as the end of massive class actions. The decision, however, is not really surprising, and turns on the specific facts of that case.

In *Dukes*, a putative class of 1.5 million current and former female employees of Wal-Mart sought class certification under Rule 23(b)(2). In looking at the threshold question under Rule 23(a), the Court found a lack of a common question of law or fact. The problem with certification was that there were "literally millions of employment decisions" that were "generally committed to local managers' broad discretion" in some 3,400 stores throughout the country. The Court held that the plaintiffs had failed to come forward with proof of any employment practice "that ties all their 1.5 million claims together."

In *Ramos v. SimplexGrinnell LP*, No. 07-cv-981, 2011 U.S. Dist. LEXIS 65593 (E.D.N.Y. June

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(6), and 23 – remain intact. These rules have not been amended, and courts have, quite properly, continued to apply the rules as written. In most cases, it is hard to see how these supposedly earth-shattering Supreme Court decisions have altered the rulings by district courts.

'Threadbare' Allegations

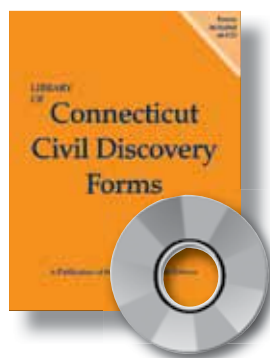
Both *Twombly* and *Iqbal* hold that a com-

ever, determined that these factual allegations (that the U.S. attorney general was aware of, approved of, and was the "architect" of, harsh conditions of confinement based on religion, race, and national origin) were "conclusory" and therefore not entitled to a presumption of truth. The remaining factual allegations were rejected as not "plausible."

The legal community's concern with *Twom-*

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Retired Judge Still Handles Commercial Disputes

NEVAS WEIGHS BENEFITS OF ADR IN CONVERSATION WITH TWO LAWYERS

The ADR Section of the Connecticut Bar Association considers it a key part of its mission to provide lawyers in our state with information about what it is like to practice in the field of Alternative Dispute Resolution.

With this in mind, two members of the ADR Section, Steve Rolnick and Bill Whittemore, had an opportunity this summer to meet and talk with retired Senior U.S. District Judge Alan H. Nevas. Since retiring from the bench in 2009, Judge Nevas has been serving as both an arbitrator and a mediator in a broad range of commercial disputes. Here are excerpts from that conversation:

QUESTION: What are the differences between being a judge and an arbitrator?

ALAN NEVAS: Not that different. I am still dealing with lawyers, interesting issues and function much as I did for 25 years. There is more variety because I am not limited to federal issues, but you are treated differently as an arbitrator than as a judge. You are not up on the bench and not wearing a robe. That makes a difference.

Q: What types of disputes have you dealt with?

NEVAS: All types. I've even had a medical malpractice case. That said, commercial cases are the most common.

Q: How do disputes get referred to you?

NEVAS: I do get referrals from dispute resolution services but I also get referrals directly from lawyers I have known over the years — particularly for mediation.

Q: What is your relative focus on arbitration

vs. mediation?

NEVAS: It is approximately evenly divided between the two.

Q: Are there disputes that are suitable and not suitable for ADR?

NEVAS: Just about any dispute can be suitable for ADR. Even matrimonial cases, although I don't handle them myself I know there is a great deal of divorce mediation and I don't see why an experienced neutral could not arbitrate a contested divorce.

Q: What about the cost and time involved with ADR vs. litigation?

NEVAS: I am aware of the concerns that arbitration has become as costly and time-consuming as litigation. It may be easier for me to do this as a former judge, but I try to remind the lawyers that it is not a courtroom, it is arbitration and get them to focus on the real issues. I do a lot of phone conferences and always make myself available to resolve disputes and move things along.

Q: What is your opinion of court-annexed/mandatory ADR vs. private/contractual ADR?

NEVAS: The main problem I see with court annexed mandatory ADR, which some states have, is that the arbitrators may not be that well qualified. If they are not experienced and knowledgeable the process is not going to work.

Q: Are there ways in which mediation and arbitration might be integrated?

NEVAS: I recall one case as a judge where I both attempted to settle and got them to stipulate to the facts so that when the case did



Alan Nevas, a former federal judge, says he's aware of complaints that it can take as long to mediate a case as it does to litigate it, and so he tries various ways to 'move things along.'

not settle I was able to render a decision. But that was an unusual case because I knew the lawyers and that created a comfort level with them. It would be more difficult with lawyers I do not know. I am currently assigned as a single arbitrator and I recently heard from counsel that they would like me to mediate the matter. If unsuccessful, they will stipulate that I can continue as the arbitrator. So, I believe the two procedures can be integrated with the right case and the right counsel.

Q: How do you handle preliminary conferences in arbitration?

NEVAS: They are similar to status conferences in court. I prefer to do them by telephone which most often works very well for the arbitrator and for the parties' attorneys. The main thing I do is get a final hearing date from them. It can be as far out as they want but once it is set that is firm. One advantage I think is that you have more flexibility in that

respect in arbitration than you do in court.

Q: What are your views regarding mediation styles, e.g. facilitative vs. evaluative?

NEVAS: A good mediator would utilize a variety of methods depending on the dispute, the parties and even the stage of the process. I'll never forget a mediation I had where both parties to the dispute had known each other as youngsters, then were separated for many years and then reunited, whereupon they went into business together. Their business dispute was hotly contested, with a lot of money at stake, and they were represented by high-powered attorneys.

Still, ultimately it wasn't until I got them into a room together without their attorneys present that I was able to get them to shake hands. Then I left the room and they settled the matter by themselves. The lesson is, there's an art to mediation, and sometimes hands-off is the right thing and sometimes not.

Q: How do you deal with evidentiary matters in arbitration?

NEVAS: I tell the lawyers beforehand that almost everything will come in and I will give it the weight it deserves. If they really strenuously object to something they can but rarely do.

Q: Do you think there is a potential role for Connecticut-based attorneys as conflict-free ADR neutrals for disputants in adjoining states?

NEVAS: That is definitely something that would be attractive to lawyers in adjoining states. ADR has to be promoted by reaching lawyers and not just the general public. ■

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21, 2011), decided within a week after *Dukes*, the court found that: "The relevant facts and circumstances in *Wal-Mart* have little bearing here...[T]here is little discretion or subjective judgment in determining an employee's right to be paid prevailing wages . . ."

As the Court in *Ramos* concluded, "although the efforts of the *Wal-Mart* plaintiffs to prove their case with statistical evidence failed, plaintiffs here have come forward with class-wide proof . . ."

In short, *Dukes* did not foreclose class certification (even in employment cases) where the harm suffered by all class members came from the same cause.

Even before *Dukes*, a number of courts had ruled that a class could not be certified where the class members were spread over various locations and the decision makers were exercising independent judgment. See *Garcia v. Johanns*, 444 F.3d 625, 632 (D.C. Cir. 2006) ("Establishing commonality for a disparate treatment class is particularly difficult where, as here, multiple decisionmakers with significant local autonomy exist").

Beyond the *Dukes* Court's sharply divided interpretation of the commonality requirement in the context of Rule 23(a) (which may have more academic than practical implications), the court also held, unanimously, that substantial monetary claims could not be advanced by a class certified under Rule 23(b)(2). This represented no change in the law.

As to class actions seeking predominantly monetary damages under Rule 23(b)(3), *Dukes* has no impact since Rule 23(b)(3) requires that "questions of law or fact common to class members predominate . . ." Federal Rules of Civil Procedure 23(b)(3) (emphasis added).

This point was recently emphasized in *Public Employees' Retirement System of Mississippi v. Merrill Lynch & Co.*, No. 08-cv-10841, 2011 U.S. Dist. LEXIS 93222 (S.D.N.Y. Aug. 22, 2011). In that case, Judge Jed Rakoff brushed aside the Rule 23(a) commonality argument of the defendants under *Dukes*: "not only do common questions exist in this case, but they in fact predominate over any questions affecting only individual members." For most business cases where monetary damages is the primary relief sought under Rule 23(b)(3), *Dukes* is not particularly relevant. ■

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