

SOUTHERN DISTRICT CIVIL PRACTICE ROUNDUP

Expert Analysis

When Misrepresentations During Settlement Conferences Become Sanctionable

Must all material representations made during a settlement conference be truthful? Can a lawyer be sanctioned for misrepresenting a material fact during a settlement conference? Southern District Magistrate Judge James L. Cott recently addressed these questions in *Otto v. Hearst Communications*, 2019 WL 1034116 (S.D.N.Y. Feb. 21, 2019). Although Judge Cott declined to impose sanctions, he characterized plaintiff's counsel's conduct as presenting "a close call." If there had been clear evidence that (1) plaintiff's counsel had, in fact, knowingly made a materially false statement at the settlement conference and (2) defendant had been prejudiced by the false statement (e.g., defendant had agreed to a settlement in reliance on the false statement), Judge Cott likely would have imposed sanctions.

'Otto'

Otto v. Hearst Communications is a copyright infringement case. The

EDWARD M. SPIRO and CHRISTOPHER B. HARWOOD are principals of Morvillo Abramowitz Grand Iason & Anello P.C. Mr. Spiro is the co-author of "Civil Practice in the Southern District of New York," 2d Ed. (Thomson Reuters 2018), and Mr. Harwood is the former Co-Chief of the Civil Frauds Unit at the U.S. Attorney's Office for the Southern District of New York.



By
Edward M.
Spiro



And
Christopher
B. Harwood

matter arose when plaintiff took a photograph of President Trump (the Photograph) with his camera phone while attending a friend's wedding in June 2017 at a Trump-owned golf course. Defendant subsequently obtained the Photograph from a third-party's social media account and published it on one of its websites in an article titled "President Trump Is the Ultimate Wedding Crasher." In response, plaintiff filed suit alleging that defendant committed copyright infringement by displaying the Photograph without a license. On Dec. 10, 2018, Southern District Judge Gregory H. Woods awarded plaintiff summary judgment on liability and scheduled a trial on damages to begin on July 15, 2019.

More than a year earlier, on Oct. 23, 2017, the parties attended an off-the-record settlement conference before Judge Cott. According to defendant, plaintiff's counsel

misrepresented a key fact during that settlement conference. Specifically, at the outset of the conference, plaintiff's counsel allegedly (1) stated that plaintiff was about to execute a license for the Photograph with a third party for \$9,500 (the License), but (2) repeatedly denied that the License was being executed as part

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of the settlement of a similar copyright infringement case that plaintiff had brought against another media company for publishing the same Photograph without a license, *Otto v. Warner Bros. Entertainment*, No. 17-4763 (S.D.N.Y.) (*Warner Bros.*). According to defendant, plaintiff's counsel's representations were material to the parties' settlement positions at the settlement conference.

Notwithstanding plaintiff's counsel's representations, four days after the settlement conference, on Oct. 27, 2017, plaintiff entered into a confidential settlement agreement resolving the *Warner Bros.* case, and the executed License was attached as an exhibit to that settlement agreement.

On Dec. 7, 2017, during discovery in the case before Judge Cott, plaintiff's counsel produced a copy of the executed License from the *Warner Bros.* settlement agreement. Plaintiff's counsel produced the License as a stand-alone document, however, without any indication that it was part of the settlement agreement in the *Warner Bros.* case. During plaintiff's deposition on Dec. 11, 2017, plaintiff was questioned about the relationship between the License and the *Warner Bros.* case and he denied that the License "was ... part of the settlement of that lawsuit." 2019 WL 1034116, at *4. Four days after plaintiff's deposition, on Dec. 15, 2017, in response to a demand for all settlement agreements related to the Photograph, plaintiff's counsel produced the *Warner Bros.* settlement agreement (with the same License that had been produced as a stand-alone document on Dec. 7, 2017 attached as an exhibit).

On March 27, 2018, defendant moved for sanctions against plaintiff and his counsel, claiming that they repeatedly misrepresented the nature of the License—first at the settlement conference, then through their initial document production, and finally at plaintiff's deposition.

Applicable Standards

In evaluating whether to impose sanctions, Judge Cott identified four

sources of authority under which sanctions could potentially be imposed: (1) Rule 16(f) of the Federal Rules of Civil Procedure (Rule 16(f)), (2) the court's "inherent powers," (3) 28 U.S.C. §1927, and (4) N.Y. Rule of Professional Conduct 4.1 (Rule 4.1). Judge Cott addressed the standards for imposing sanctions under each authority.

With respect to Rule 16(f), Judge Cott observed that a court may impose sanctions "if a party or its attorney ... does not participate in good faith ... in [a pretrial] conference,' including a settlement conference." 2019 WL 1034116, at *5 (quoting Fed. R. Civ. P. 16(f)(1)(B) (alterations in original)). Judge Cott noted, however, that "in the context of a court-ordered settlement conference, courts have interpreted good faith narrowly to require compliance with orders to attend [a settlement conference], provide pre-[settlement] memoranda, and in some cases, produce organizational representatives with sufficient settlement authority." *Id.* (citations omitted; alterations in original).

Judge Cott next confirmed that a court can impose sanctions pursuant to its "inherent powers" for misconduct during a settlement conference or discovery, but he noted that "this power [should be exercised] with restraint and only upon the finding of bad faith," which "requires clear evidence that the challenged conduct [was] ... taken for improper purposes." *Id.* at *6 (citations omitted). Judge Cott then observed that "a court [also] has the inherent power to sanction a party for perpetrating a fraud on the court," and he identified five factors that a court should consider in determining whether to

impose such a sanction: "(1) whether the misconduct was the product of intentional bad faith; (2) whether and to what extent the misconduct prejudiced the other party; (3) whether there is a pattern of misbehavior ... ; (4) whether and when the misconduct was corrected; and (5) whether further misconduct is likely to continue in the future." *Id.* (citations omitted). Judge Cott cautioned, however, that a court should only impose sanctions pursuant to its inherent authority if "it finds, by clear and convincing evidence, that a party or attorney knowingly made ... [a] materially false or misleading [representation] ... as part of a deliberate and unconscionable scheme to interfere with the Court's ability to adjudicate the case fairly." *Id.* (citation and alterations omitted).

Turning to §1927, Judge Cott noted that "[t]he standard for sanctions pursuant to [this statute] is identical to the standard under the court's inherent power," with "[t]he only meaningful difference ... [being] that ... [sanctions] under [§]1927 are made only against attorneys or other persons authorized to practice before the court[] while [] [sanctions] made under the court's inherent power may be made against an attorney, a party, or both." *Id.* (citations omitted). Finally, Judge Cott observed that a court may impose sanctions under Rule 4.1 if "a lawyer ... knowingly make[s] a false statement of fact or law in a negotiation." *Id.* at *11.

Judge Cott ultimately decided to "analyze [defendant's] sanctions motion under [the court's] inherent powers, as doing so [would] best enable [him] to efficiently and comprehensively assess both the conduct of [plaintiff] and his counsel during

both the settlement conference and the course of discovery.” Id. at *7.

Judge Declined to Impose Sanctions

Although Judge Cott stated that he was “troubled by the allegations surrounding [plaintiff’s counsel’s] purported misuse of the Warner Bros. [L]icense ... at the settlement conference,” he declined to impose sanctions for the alleged settlement conference-related misconduct for three reasons. Id. First, the settlement conference was off-the-record, and therefore plaintiff’s counsel’s alleged misrepresentations were not memorialized or recorded, leaving Judge Cott with an insufficient basis to confirm that the alleged misrepresentations had, in fact, been made. Id. Second, no settlement was reached based on plaintiff’s counsel’s purported misrepresentations, and “[defendant] therefore did not suffer any prejudice in this respect.” Id. at *8. Third, even if plaintiff’s counsel had, in fact, stated during the settlement conference that the License was not part of the settlement of the *Warner Bros.* case, defendant did not disprove that statement “with evidence that existed at the time the [alleged statement was] made,” and it is at least possible that the alleged statement was accurate at the time it was made since the settlement “with Warner Bros. was not executed until [four days after the settlement conference].” Id.

Judge Cott also declined to impose sanctions for the alleged discovery and deposition misconduct. Judge Cott reasoned that, even if plaintiff’s counsel’s production of the License as a stand-alone document on Dec. 7, 2017 constituted bad faith, it did not amount to sanctionable conduct

because any misrepresentation was corrected eight days later (when the full settlement agreement from the *Warner Bros.* case was produced) and “[defendant] did not suffer any significant prejudice.” Id. at *10. Similarly, Judge Cott stated that, even if plaintiff had perjured himself during his deposition, sanctions would not be warranted because, among other things, there was no evidence of “a pattern of misbehavior” and any misrepresentation “was corrected four days later, and [defendant] acknowledge[d] that it suffered relatively little prejudice.” Id. (citations omitted).

Judge Cott characterized his decision not to impose sanctions as “a close call,” and “strongly caution[ed] [plaintiff’s counsel] to be mindful of overplaying [his] hand[] (or worse)

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during settlement negotiations.” Id. at *12. “If a license ha[d] been obtained as part of [the *Warner Bros.*] settlement,” Judge Cott added, “then [plaintiff’s counsel] should [have been] transparent in that regard and not tr[ie]d, as leverage, to pawn [the] license off as something other than a settlement.” Id.

‘Puffery vs. Actionable’ Misrepresentations

As Judge Cott observed, lawyers routinely engage in “posturing and puffery ... during settlement negotiations.” Id. at *1. There is a line, however, between “posturing or puffery” and actionable misrepresentations,

and that line is crossed when a lawyer knowingly misrepresents a fact that is material to the resolution of the case. See *Ausherman v. Bank of Am.*, 212 F. Supp. 2d 435, 443-52 (D. Md. 2002) (referring attorney to disciplinary committee for knowingly making material misrepresentation during settlement negotiations). In the context of settlement negotiations, “[a] fact is material ... if it reasonably may be viewed as important to a fair understanding of what is being given up and, in return, gained by the settlement.” Id. at 449. Both “federal and state courts have been ready to discipline or hold liable attorneys who make knowing, material misrepresentations to third persons during settlement negotiations.” Id. at 446-48 (citing cases); see *Slotkin v. Citizens Cas. Co. of N.Y.*, 614 F.2d 301, 307-08, 314 (attorney appropriately held liable in fraud for misrepresenting the existence and extent of his client’s insurance coverage during settlement negotiations); see generally Barry R. Temkin, *Misrepresentation by Omission in Settlement Negotiations: Should there Be a Silent Safe Harbor?*, 18 Geo. J. Legal Ethics 179, 192-201 (2004) (citing cases where attorneys have been disciplined or held liable for material misrepresentations in settlement discussions).

Conclusion

Lawyers should beware that making material misrepresentations during settlement conferences may result in sanctions.