# NOTES & TRENDS

## CIVIL LITIGATION

JUDICIAL LAW

■ **SERVING REMOVAL PAPERS FROM CONCILIATION COURT TO DISTRICT COURT; RULES OF CIVIL PROCEDURE.** The Minnesota Court of Appeals recently held that, after a contested conciliation court hearing, a party seeking to remove the matter to district court must serve the removal papers in compliance with the Rules of Civil Procedure. In the case at issue, the plaintiff and defendant had dueling claims and counterclaims. The conciliation court issued a judgment that awarded no damages to either party. Thereafter, the plaintiff filed a demand for removal to district court and served it via first-class mail as provided by Minn. R. Gen. Pract. 521(b) (the conciliation court rule regarding removals). He did not enclose an acknowledgment of service form, as required by Minn. R. Civ. P. 4.05. The conciliation court rule is silent regarding whether or not an acknowledgment of service is required. The Supreme Court relied upon two prior cases relating to service issues on cases removed from conciliation court, and extended the law to require that after a contested case hearing in conciliation court, Minn. R. Civ. P. 4.05 applies to the proper service of a removal notice from conciliation court. The Court relied upon Minn. R. Civ. P. 81.01(a), which provides that the Rules of Civil Procedure apply to all suits of a civil nature, subject to express exemptions which do not include conciliation court proceedings. Judge Lansing dissented on the grounds that Rule 81.02 states that the rules do not supersede provisions of statutes relating to appeals to the district courts. Because Minn. Stat. 491A.02 states that removal from conciliation court to district court is governed by rules promulgated by the Supreme Court, and General Rules of Practice are so promulgated, the conciliation court removal rule should not be trumped by the Rules of Civil Procedure. Judge Lansing noted that the Rules of Civil Procedure should apply only *after* the case has been removed. ***Roehrdanz v. Brill***, CX-03-137 (Minn. App. 08/25/03). *http://www.lawlibrary.state.mn.us/archive/ctappub/0308/op030137-0826.htm*

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## CRIMINAL LAW

JUDICIAL LAW

■ **EVIDENCE; REVERSE *SPREIGL* VERSUS THIRD PARTY PERPETRATOR; STANDARDS FOR ADMISSION.** This case discusses the evidentiary foundational requirements for the admission of third-party-perpetrator evidence versus reverse *Spreigl* evidence. The concurring opinion makes clear that there is a distinction between these two types of evidence: third-party-perpetrator evidence is that which connects the third party to the offense with which the defendant is charged, such as testimony physically placing the third party at the scene, fingerprints, DNA, admission or confession, etc.; reverse *Spreigl* is evidence that a third party committed other bad acts in addition to the charged offense, for the traditional *Spreigl* purposes. Third-party-perpetrator evidence requires only ordinary evidentiary standards for admission, and not the heightened "clear and convincing" standard for *Spreigl* evidence. ***State v. Paul Gutierrez, Jr.***, C5-02-908 (Minn. 08/21/03). *http://www.lawlibrary.state.mn.us/archive/supct/0308/op020908-0821.htm*

■ **EVIDENCE; POLYGRAPH; REFERENCE TO TAKING TEST; PLAIN ERROR.** During trial, the district court, without objection, admitted into evidence a taped transcript of the appellant's police interview which had repeated references to what a polygraph would "show." At one point, the police officer asked: "... do you think you'd take the polygraph about being truthful .. ?", to which the immediate response was: "Nope." Held, admission of the appellant's police interview, without redacting all references to the polygraph, constitutes plain error, even though not objected to. Minnesota courts have, with one narrow exception, refused to admit into evidence polygraph tests. The inference of

the questioning with regard to the polygraph is that if the appellant had not been guilty, he would have submitted to the test. ***State v. Richard Edward Winter***, CX-02-1911 (Minn. App. 09/02/03). *http://www.lawlibrary.state.mn.us/archive/ctappub/0309/op021911-0902.htm*

■ ***SPREIGL*** **STANDARD VERSUS PRIOR ACTS OF DOMESTIC ABUSE.** In a prosecution for 911 interference and domestic assault, the state attempted to introduce evidence of a prior assault on the victim by the defendant under Minn. Stat. §634.20. This statute permits the court to admit evidence of similar prior conduct, but is silent as to the evidentiary standard for such admission. Under the classic *Spreigl* requirement of Minn. Rule of Evid. 404(b), evidence of past misconduct must be proven by clear and convincing evidence before it is admissible.

The state contends in this appeal that the heightened standard of Rule 404(b) is not applicable, and the only issue is similarity. Appellant contends that §634.20 violates the separation of powers doctrine. Without reaching the constitutionality issue, the Court of Appeals holds that §634.20 evidence of prior acts of domestic abuse must be shown by clear and convincing evidence before they are admissible, the same as *Spreigl* evidence. The court reaches this decision, in contradistinction to dicta found in *State v. Hansen*, 543 N.W.2d 84 (Minn. 1996), by examining the legislative committee meeting transcripts. The sponsoring prosecuting attorney specifically stated that under the statute, such prior incidents must be shown by clear and convincing evidence. ***State v. Tyrone S. McCoy***, C4-02-1788 (Minn.. App. 09/09/03). *http://www.lawlibrary.state.mn.us/archive/ctappub/0309/op021788-0909.htm*

■ ***MIRANDA*****; STUDENT; IN-SCHOOL POLICE INTERROGATION; CUSTODY; COERCION.** The appellant was removed from a classroom, with the permission of his stepfather but not his biological parents, in order to speak with police officers regarding unauthorized use of a motor vehicle. Although he was told that he was not under arrest, and that the stepfather had given permission for the interview, the appellant was not told that he did not have to talk with police, and was not given the *Miranda* warning. At no time during the interview did the appellant ask to leave or speak with a parent. At the end of the interview, the appellant filled out a written statement and was given a hall pass to return to class. At the suppression hearing, the appellant testified that he did not think he was free to leave, and that he felt he had to answer all of the officers' questions. Additionally, he was not told that he was free to refuse to answer questions. He was not asked if he wished to speak with his parents or return to class. Held, under the circumstances, this 14-year-old appellant, a child of average intelligence and maturity, was in custody, and should have been given a *Miranda* warning. As a separate reason for suppression, his statements were not voluntary. The circumstances under which the statements were given were so coercive and intimidating that the defendant was unable to make a free-will decision. ***In Re M.A.K.***, C9-03-16 (Minn. App. 08/19/03). *http://www.lawlibrary.state.mn.us/archive/ctappub/0308/op030016-0819.htm*

■ **FORFEITURE; FLEEING FORFEITURES VERSUS GENERAL FORFEITURES; REDEMPTION OPTION.** Under the general forfeiture rules of 609.531, subd. 5A(b), the owner of a motor vehicle seized under that section may seek possession of the vehicle while the forfeiture action is pending by surrendering the certificate of title. When a forfeiture is for fleeing, pursuant to Minn. Stat. §609.5312, subd. 4, there is no provision for tendering the certificate of title in exchange for the temporary repossession of the vehicle. Under a fleeing forfeiture, the vehicle may be returned only after a hearing if the district court finds that the prosecution has not charged the predicate fleeing felony, the owner has demonstrated a defense to the forfeiture, or the owner has demonstrated that seizure created an undue hardship. Here, it was appropriate for the prosecuting authorities to deny return of the vehicle in exchange for a tender of the title. Minn. Stat. §609.5312, subd. 4 exclusively controls forfeiture proceedings where the accusation is fleeing a police officer in a motor vehicle. ***Susan Gaertner v. One 1999 Dodge Pickup Truck***, C2-03-66 (Minn. App. 08/26/03). *http://www.lawlibrary.state.mn.us/archive/ctappub/0308/op030066-0826.htm*

■ **FORFEITURE; VEHICLE; INSURANCE PROCEEDS; DOUBLE JEOPARDY.** Under Minn. Stat. §609.5312, which provides that "all money and other property, real and personal, that represent proceeds of a designated offense ... are subject to forfeiture," the state may take the insurance proceeds representing settlement for the destruction of a car which was used by a defendant resulting in a conviction for criminal vehicular operation. Such forfeiture does not violate state and federal prohibitions against double jeopardy because the settlement, approximately $9,000, was not so excessively punitive as to render the proceedings criminal rather than civil. ***Randy John Schug v. $9,916.50***, A03-198 (Minn. App. 09/23/03) *http://www.lawlibrary.state.mn.us/archive/ctappub/0309/opa030198-0923.htm*

■ **Criminal Sexual Conduct; Mistake of Age Defense; Burden Shifting.** The appellant was convicted of third-degree criminal sexual conduct involving a 15-year-old and penetration. At the time, the appellant was approximately 60 years old. At a bench trial, the appellant contended that once he asserted his belief that the victim was 17 years old at the time they had sex, the court must require the state to rebut his affirmative defense by proof beyond a reasonable doubt. Held, the mistake of age defense, as provided in Minn. Stat. §609.344, subd. 1(b), does not require a shifting of the burden of proof to the state. Reversion to the state of proof beyond a reasonable doubt arises only in cases where the defendant makes a *prima facie* showing that the mitigating circumstances disprove or negate an element of the crime charged. The elements of criminal sexual conduct, as charged, do not address the knowledge or intent of the defendant. Hence, the burden of persuasion with regard to the mistake of age affirmative defense was properly allocated to, and remained with, the appellant. ***State v. Douglas Howard Kramer***, C8-02-2054 (Minn. App. 09/02/03). *http://www.lawlibrary.state.mn.us/archive/ctappub/0309/op022054-0902.htm*

■ **Prosecutorial Misconduct; Reference to Court Spectators; Insinuation of Accomplices Present.** Appellant was on trial for first-degree aggravated robbery. The accusations were that the appellant and two unapprehended accomplices had beaten and robbed the victim. The accomplices were not caught, but had been described as African-American males with "Rastafarian" hair. During trial, the prosecuting attorney asked the appellant whether he recalled seeing a group of spectators in the back of the courtroom who were African-American and had braids. The clear insinuation was that there was a connection between the appellant and the victim's as yet unidentified assailants.

Held, it was prosecutorial misconduct for the prosecution to make an unfounded insinuation concerning the unapprehended assailants. Such misconduct entitles the appellant to a new trial. ***State v. Tony Terral Kelly***, C1-02-1912 (Minn. App.09/02/03). *http://www.lawlibrary.* state.mn.us/archive/ctappub/0309/op021*912-0902.htm*

■ **Controlled Substance; School Zone; Intent; Equal Protection.** Minn. Stat. §152.023, subd. 2(4) does not violate the equal protection clause of the Minnesota Constitution. A rational basis exists to distinguish between those who possess drugs in general, and those who possess drugs in a school zone. Drug offenders pose risks to children in schools, beyond just the sale of drugs, and even those who are in transit through school zones may be prosecuted under the statute. Next, the state need not prove that the defendant knew he was in, or intended to be in, a school zone. Language of the statute is clear, and does require that the defendant had such an intent when he possessed drugs. Accordingly, the district court did not err by refusing to allow the appellant to argue his lack of intent, and by failing to instruct the jury as to intent. ***State v. Steven Allen Benniefield***, C1-02-1991 (Minn. App. 09/09/03). *http://www.lawlibrary.state.mn.us/archive/ctappub/0309/op021991-0909.htm*

■ **Sentence; Jail Credit; Residential Treatment Center; St. Peter.** Following *Asfaha v. State*, 665 N.W.2d 523 (Minn. 2003), the Court of Appeals holds that the intensive treatment program for sexual aggressiveness (ITPSA) at the Minnesota Security Hospital in St. Peter is the functional equivalent of a jail, workhouse or correctional facility, and that the appellant is entitled to more than four years of jail credit against a prison sentence which was ultimately imposed for a probation violation. The court notes that the facility is surrounded by a security fence, has a central control center managing all access points electronically, has a sally port door, closed circuit television, strict daily schedules, patient rooms with bars on the windows, armed guards accompanying inmates when they are transported, and submission to pat-down searches. ***State v. Robin John Razmyslowski***, A03-38 (Minn. App. 09/16/03). *http://www.lawlibrary.state.mn.us/archive/ctappub/0309/opa030038-0916.htm*

■ **Kidnapping; Momentary Confinement Insufficient.** In the course of attacking and murdering the victim, the appellant momentarily blocked the doorway to prevent the escape of the victim. The attack of the victim had already been underway. The Supreme Court, in revisiting prior decisions, clarifies the kidnapping law because of significant new consequences not present at the time of the prior decisions. The Court holds that for a kidnapping conviction to justify a separate sentence, the confinement or removal must be criminally significant in the sense of being more than merely incidental to the underlying crime, particularly in order to justify a separate criminal sentence. ***State v. Darnell Christopher Smith***, C8-02-1292 (Minn. 09/25/03). *http://www.lawlibrary.state.mn.us/archive/supct/0309/op021292-0925.htm*

■ **Search and Seizure; Open Boat; Fish and Game Search; Refusal to Allow Inspection.** The Supreme Court reverses the Court of Appeals in holding that it is permissible for a

conservation officer to conduct a lawful nonconsensual inspection of an open boat used to store or transport fish, and the respondent may permissibly be convicted of refusal to submit to such a search under Minn. Stat. §97A.251, subd. 1(3). Here, the DNR officer walked up to an already stopped boat that rested on a trailer of a parked truck; hence there was no seizure for 4th Amendment purposes when an officer walks up to an already stopped vehicle. Also, the Court holds that the statute allowing searches without probable cause is constitutional because the respondent had no reasonable expectation of privacy in the areas of his open boat or other conveyance used to typically store or transport fish. The Court notes that a high degree of regulation over the "privilege of hunting" reduces participant's reasonable expectations of privacy. ***State v. John Mark Colosimo***, C7-01-2181 (Minn. 09/25/03).*http://www.lawlibrary.state.mn.us/archive/supct/0309/op012181-0925.htm*

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## EMPLOYMENT & LABOR LAW

JUDICIAL LAW

■ **CLOSE CORPORATIONS.** A minority shareholder in a closely held corporation who had reasonable expectation of continued employment was entitled to a temporary injunction and reinstatement to his employment after he was terminated by the corporation. The Court of Appeals affirmed a lower court ruling granting a temporary injunction in favor of a minority shareholder, who was also a cofounder of the company, a director and officer, and guarantor of corporate debt, after he was removed from his job in an effort to force him to sell his shares, because of financial exigencies. The court deemed that the ousted shareholder suffered sufficient irreparable harm to warrant temporary injunctive relief by reinstating him to his position. ***Haley v. Forcelle***, 2003 Minn. App. LEXIS 1163 (Minn. App. 2003). *http://www.lawlibrary.state.mn.us/archive/ctappub/0309/opa030182-0923.htm*

■ **INDEMNITY.** An employer has a duty to indemnify an employee from legal expenses, even though the employee was working for a "borrowed" employer at the time the litigation arose. The appellate court ruled that an employee is entitled to indemnification for attorney's fees and costs under Minn. Stat. §181.970 (2002), which imposes a statutory duty of indemnification upon the employer. The court ruled against the employer even though the lawsuit arose out of alleged negligence of the employee while working for another company, which reimbursed the employer for the employee's salary and benefits on a temporary basis. The indemnification statute applies to the underlying employer, despite the fact that another employer may be liable for the employee's wrongdoing under the Loaned-Servant Doctrine. ***Ag Partners Coop v. Pommerening***, 2003 Minn. App. LEXIS 1166 (Minn. App. 09/23/03) (unpublished). *http://www.lawlibrary.state.mn.us/archive/ctapun/0309/op030084-0923.htm*

■ **UNEMPLOYMENT COMPENSATION.** A photo laboratory employee who violated her employer's policy against providing free photocopies and reproduced a photograph that stated "Not to copy" on it was properly terminated for "misconduct," and therefore, ineligible for unemployment compensation benefits. The employee who gave the free copy and allowed the impermissible photographic reproduction was aware of the employer's policy. The intentional violation of that policy rendered her ineligible for unemployment compensation benefits. ***Dalin v. Qualex, Inc.***, 2003 Minn. App. LEXIS 1182 (Minn. App. 09/23/03) (unpublished).*http://www.lawlibrary.state.mn.us/archive/ctapun/0309/op030204-0923.htm*

Similarly, an employee who violated company policy by attesting to seeing a scientific procedure being performed, without personally observing it, was disqualified for unemployment compensation benefits on grounds of "misconduct." The employee, who worked for a company that produced personal health care products, signed a statement that he saw a chemical component added to a batch, which was required by company policy. He did so even though he did not personally observe the process. The employee acknowledged that he was aware that he violated the company's policy by signing the statement without actually observing the mixture, which warranted disqualification from unemployment compensation benefits. ***Jennings v. Diamond Products Co.***, 2003 Minn. App. LEXIS 1153 (Minn. App. 09/16/03) (unpublished). *http://www.lawlibrary.state.mn.us/archive/ctapun/0309/op022196-0916.htm*

An employee who quit ostensibly because of sexual harassment following the company's investigation and disciplinary action against a coworker was ineligible for unemployment compensation benefits. The employer properly and timely investigated the employee's claim of sexual harassment and took disciplinary action against a coworker. It also repeatedly asked the claimant if there were continuing difficulties and the claimant did not indicate any problems. After the employer learned

of the continuing problem, through another employee, it again investigated and dismissed the offending coworker. The claimant's resignation at this stage, without notice, did not constitute "good reason" to quit because the employer had taken timely and proper action. Therefore, the employee was not entitled to unemployment compensation benefits. ***Thomas v. St. Paul Harley-Davidson, Inc.***, 2003 Minn. App. LEXIS 1179 (Minn. App. 09/23/03) (unpublished). *http://www.lawlibrary.state.mn.us/archive/ctapun/0309/op030291-0923.htm*

An employee who quit after she was told that she would be demoted, given a pay cut of nearly 15 percent, and required to work less desirable weekend hours was judged entitled to unemployment compensation. Because the change in wages and hours was "substantial" the employee had "good reason" to quit and was eligible for benefits under Minn. Stat. §268.095, Subd. (1). ***Rootes v. Wal-Mart Associates, Inc.***, 2003 WL 27233833 (Minn. App. 09/30/03). *http://www.courts.state.mn.us/opinions/coa/current/opa030233-0930.html.*

■ **TAX DEDUCTION.** A business that sponsors fishing trips for its sales personnel is entitled to take a tax deduction for the expenses, which do not constitute wages to the employees. The 8th Circuit Court of Appeals held that because the company, which manufactures printing devices, had a specific "business purpose" for these trips, the costs were "reasonable and necessary" business expenses." Accordingly, those who attended the fishing outings did not have to include the costs as taxable wages, and the sponsoring company could deduct the expenses as reasonable business expenses. ***Townsend Industries, Inc. v. United States of America***, 2003 U.S. App. LEXIS 19055 (8th Cir. 2003). *http://caselaw.lp.findlaw.com/data2/circs/8th/023756p.pdf*

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## ENVIRONMENTAL LAW

### JUDICIAL LAW

■ **ENVIRONMENTAL REVIEW; REMAND OF DM&E APPROVAL.** The 8th Circuit Court of Appeals remanded for additional consideration the federal Surface Transportation Board's (STB's) final approval of the Dakota, Minnesota & Eastern Railroad Corporation's (DM&E's) proposal to construct approximately 280 miles of new rail line to reach the coal mines of Wyoming's Powder River Basin (PRB) and to upgrade nearly 600 miles of existing rail line in Minnesota and South Dakota. Numerous petitioners, including the city of Rochester and the Mayo Foundation, claimed that the STB's approval violated 49 U.S.C. §10901 (requiring the STB to find that projects are consistent with public convenience and necessity), the National Environmental Policy Act (NEAP), the National Historic Preservation Act, and the Fort Laramie Treaty of 1868.

The Court of Appeals, in a lengthy decision, rejected the petitioners' claims that the STB violated 49 U.S.C. §10901, the National Historic Preservation Act and the Fort Laramie Treaty. It also rejected the majority of the claims that the final approval violated NEAP. The Court of Appeals did find the approval was deficient on three NEAP-related bases, however. The STB failed to give sufficient attention to the issue of mitigation of horn noise that would result from the increased railroad traffic through the city of Rochester. It did not respond to evidence provided by the city of Rochester regarding the impact on households that will experience both noise and vibration effects from the increased traffic. Finally, the STB failed to consider the effects on air quality that an increased supply of low-sulfur coal to power plants would produce. DM&E, as an intervenor in the appeal, argued that STB had no obligation to consider this issue because the exact locations of where the transported coal would be used in the future were unknown. Thus, it argued, the effects of any increased coal usage on air quality are too speculative to form any part of the STB's decision at this time. The Court of Appeals rejected this argument by pointing out that NEAP and the relevant Council on Environmental Quality rules required the STB to consider the direct and indirect adverse environmental effects of a proposal. "Indirect effects" are defined under the CEQ regulations are being those that may affect the environment "later in time or farther removed in distance, but are still reasonably foreseeable." The Court of Appeals concluded that while the *extent* of the effect of increased sulfur-coal supplies may be speculative at this time, the *nature* of that effect is not. Thus, the STB had an obligation to consider the effects of increased coal consumption on air quality at the present time. The Court of Appeals vacated the final approval and remanded it to the STB for additional consideration of the above three areas. ***Mid States Coalition for Progress v. Surface Transportation Board***, Nos. 02-1359, 02-1481, 02-1482, 02-1767, 02-1785, 02-1792, 02-1794,

02-1804, 02-18630, 2003 WL 22251298 (8th Ct. 10/02/03).
*http://caselaw.lp.findlaw.com/data2/circs/8th/021359p.pdf*

■ **CLEAN WATER ACT; FEDERAL JURISDICTION OVER WETLANDS.** The 4th Circuit Court of Appeals affirmed the U.S. Army Corps of Engineers' ability to bring a civil enforcement action under the Clean Water Act against developers who drained wetlands with a connection to navigable water. The wetlands in question historically had a natural hydrologic connection to Stony Run, a navigable waterway-in-fact in Virginia, prior to the construction of a nearby interstate. Following construction of the interstate, the wetlands remained connected to Stony Run by the intermittent flow of surface water through approximately 2.4 miles of natural streams and manmade ditches. The developers believed, and the district court later agreed, that the Supreme Court's decision in *SWANCC v. U. S.*, 531 U.S. 159 (2001) invalidated the Corps jurisdiction over the developers' property.

The Court of Appeals found the reliance on the SWANCC decision to be inappropriate in this case. In SWANCC, the Supreme Court rejected the Corps' assertion of jurisdiction of wetlands on the basis of its Migratory Bird Rule. Here, the Corps asserted jurisdiction over the wetlands because they were adjacent to a tributary to a navigable-in-fact waterway. The Supreme Court upheld the Corps jurisdiction over such wetlands in a prior case, *U.S. v. Riverside Bayview Homes, Inc.*, 474 U.S. 121 (1985), a point that the Court itself reaffirmed in its SWANCC decision. The Court of Appeals found the fact that the "tributary" to which the wetlands were adjacent was not natural but was instead a man-made ditch running parallel to the interstate to be an "irrelevant distinction." The Court of Appeals reversed and remanded to the district court for further proceedings. ***Treacy v. Newdunn Associates, LLP***, 2003 WL 22093616 (4th Cir. 2003). *http://caselaw.lp.findlaw.com/scripts/getcase.pl?court=4th&navby=case&no=021480P*

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## FEDERAL PRACTICE

JUDICIAL LAW

■ **REARGUMENT V. RENEWAL; CLASS CERTIFICATION MOTIONS.** Plaintiffs' motion for class certification was denied in January, 2003. In August, 2003, plaintiffs filed a "renewed" motion for class certification. Defendants then moved to strike plaintiffs' renewed motion, arguing that the "renewed" motion was an attempt to circumvent the limitations on motions for reconsideration under Local Rule 7.1(g).

Acknowledging that Fed. R. Civ. P. 23(c)(1) creates an exception to the law-of-the-case doctrine because it permits courts to "alter or amend" their class certification decisions at any time based on "fuller development of the facts," Judge Kyle noted that the plaintiffs had advanced "both factual and legal bases for their renewed motion." Finding that Rule 23's exception to the law-of-the-case doctrine is intended to "apply to facts, but not to law," Judge Kyle granted defendants' motion to strike in part, allowing plaintiffs to renew their motion for class certification, but limiting plaintiffs to addressing matters "uncovered through discovery" conducted since the denial of their previous class certification motion. Judge Kyle also found that if plaintiffs wanted to submit new authority to the court, "the proper means to do so" was through a request for reconsideration under Local Rule 7.1(g).

This decision goes a long way toward drawing a line between renewal and reargument, and should be mandatory reading for anyone involved in class certification battles. ***Gardner v. First American Title Ins. Co.***, 2003 WL 22172347 (D. Minn. 09/18/03).

■ **FIRST-FILED RULE; FILING TAKES PRIORITY OVER SERVICE.** ADM commenced an action against Slidell in the Northern District of Iowa on December 6, 2002, but did not effect service until January 9, 2003. Slidell sued ADM in the District of Minnesota on December 18, 2002, and served ADM the following day. ADM brought a motion in the District of Minnesota seeking to dismiss, transfer or stay the Minnesota action based on its first-filed Iowa action. Opposing ADM's motion, Slidell argued that it is service, not filing, that is the key event in determining which action should have priority under the so-called "first-filed" rule.

Both parties cited numerous cases alleged to support their respective positions, and Judge Davis noted the absence of any decision from the 8th Circuit directly addressing this issue. Judge Davis concluded that "the filing of the complaint is the key event that commences a civil action" and entitles the first-filed action to "primacy," and that this rule "best effectuates the plain language of the Federal Rules of Civil Procedure."

The upshot of this decision is that litigants in the District of Minnesota can continue to rely on the "first-filed" rule rather than a new "first-served" rule. ***Slidell, Inc. v. Archer Daniels Midland Co.***, 2003 WL 22050776 (D. Minn. 09/02/03).

■ **OTHER NOTEWORTHY DECISIONS.** Applying the fraudulent joinder standard set forth by the 8th Circuit in *Filla v. Norfolk Southern Ry. Co.* (discussed in this column in September, 2003), Judge Tunheim remanded an action to the Minnesota courts, finding that one of the plaintiff's claims against the non-diverse defendant was "colorable." ***Kaleb E. Lindquist American Legion Post #24 v. Lake of the Woods Agency, Inc.***, 2003 WL 22076615 (D. Minn. 09/03/03).

Judge Tunheim denied plaintiff's motion to remand based on alleged lack of diversity, finding that the presence of a non-diverse escrow agent did not destroy diversity because the escrow agent was a "nominal party." ***Shoreview Assocs., LLC v. Wells Operating Partnership, L.P.***, 2003 WL 22076610 (D. Minn. 08/24/03).

Despite finding that the conduct of plaintiff's counsel was "reprehensible," Judge Magnuson denied defendants' motion for sanctions under Fed. R. Civ. P. 11 and 28 U.S.C. §1927, agreeing with previous decisions by Judges Kyle and Doty that a warning letter does not comply with the "safe harbor" requirement of Fed. R. Civ. P. 11(c)(1)(A), and that there was insufficient evidence of "subjective bad faith" to warrant sanctions under 28 U.S.C. §1927. ***Mortice v. Providian Financial Corp.***, 2003 WL 22213108 (D. Minn. 2003).

Judge Davis denied a motion for class certification, finding that plaintiffs had met the numerosity and commonality requirements for certification of a personal injury class, but could not satisfy the typicality requirements for class certification. Judge Davis also rejected attempts to certify medical monitoring, refund and punitive damages classes. ***In Re Baycol Products Lit.***, 214 F.R.D. 542 (D. Minn. 2003).

Judge Tunheim awarded more than $250,000 in attorneys' fees to a prevailing plaintiff in an ERISA case, finding hourly rates as high as $325 per hour to be "reasonable." ***White v. Martin***, 2003 WL 22076609 (D. Minn. 09/03/03).

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## INTELLECTUAL PROPERTY

JUDICIAL LAW

■ **PATENT LITIGATION; JURISDICTION; CONTROLLING PRECEDENT IN PROCEDURAL MATTERS.** Recent patent decisions offer warnings for the unwary. Judge Davis and the Court of Appeals for the Federal Circuit ("CAFC") remind litigants that many procedural issues in patent litigation are decided under Federal Circuit law, not regional circuit law. Similarly, a recent CAFC decision reminds litigants that there are only four ways to establish appellate jurisdiction in a patent case.

In ***Travel Tags, Inc. v. Digital Replay, Inc.***, 02-CV-4276 (D. Minn. 09/15/03), Judge Davis applied Federal Circuit law, not 8th Circuit law, to determine that defendant had sufficient contacts with Minnesota to support personal jurisdiction. Digital Replay relied on 8th Circuit law in arguing that a distinction exists between patent infringement and patent invalidity for personal jurisdiction requirements. In correcting the defendant, the court reminded litigants that it applies Federal Circuit law, not regional circuit law, in determining even personal jurisdiction in patent cases — despite the literal words of the choice-of-law test.

In ***Dana v. E.S. Originals, Inc., et al.***, 02-CV-1531 (Fed. Cir. 09/08/03), the CAFC restated the choice-of-law test: "On procedural issues not unique to [patent law], we apply the law of the regional circuit." The substantive issue was whether the district court properly applied offensive collateral estoppel to bar the defendants from relitigating infringement and invalidity — claims that had been decided against defendants in an earlier action involving the same patent but a different plaintiff. The CAFC applied regional law and affirmed. However, it is far from clear that collateral estoppel and *res judicata* issues are always "procedural issues not unique to patent law." In a concurring opinion, Judge Dyk points to cases in which issues of *res judicata* and collateral estoppel were decided under Federal Circuit law. He advocates for application of Federal Circuit law to all issues of collateral estoppel and *res judicata* because it will reduce forum shopping caused by differences in regional law.

The moral: research which law applies to all procedural issues in patent cases, even those issues that on their face do not appear to be unique to patent law.

Finally, be certain that the CAFC has jurisdiction before you appeal your client's patent case —

and especially before oral argument. Failure to do so could make for a long, uncomfortable trip home from the Court of Appeals. In ***Nystrom v. Trex***, 03-CV-1092 (Fed. Cir. 08/08/03), the CAFC dismissed Nystrom's appeal — after it was fully briefed and on the morning of oral argument — for lack of appellate jurisdiction. The problem: issues of patent invalidity had not been *finally* decided by the trial court before it entered final judgment. Nystrom sued Trex for patent infringement. Trex brought a counterclaim that *all* of the patent claims were invalid. After construing the patent-claim terms, the trial court granted summary judgment of noninfringement, invalidity of three of the 20 patent claims, and final judgment. In such a situation, not uncommon in patent cases, where issues of invalidity remain after a finding concerning infringement, appellate jurisdiction can be achieved in one of only four ways. First, the trial court can dispose of the validity issues on the merits. Second, the trial court can dismiss the remaining claims, usually without prejudice. Third, the trial court can expressly direct entry of final judgment on fewer than all claims under Federal Rule of Civil Procedure 54(b). Fourth, the losing party can seek permission to immediately appeal under 28 U.S.C. 1292. The trial court in *Nystrom* stayed the remaining claims. Citing the final judgment rule, the CAFC "declined to entertain" the appeal because the stay did not dispose of the remaining claims and was not final. I am certain the parties were not entertained.

— TONY ZEULI
— NANCY PARSONS
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## JUVENILE LAW

JUDICIAL LAW

■ **TERMINATION OF PARENTAL RIGHTS; INCARCERATED PARENT.** In a published decision addressing the difficult issue of terminating the parental rights of a parent who is incarcerated, the Court of Appeals criticized the trial court for applying the Minnesota Supreme Court's decision of *Matter of Welfare LAF*, 554 N.W.2d 393, 398 (Minn.1996) to hold that there is no statutory requirement that the county social services facilitate contact between a parent and the children to aid the parent in complying with a reasonable case plan. The Court of Appeals observed that there is no case law that supports the trial court's conclusion that the father's incarceration vitiated his ability to comply with a case plan.

With regard to the abandonment analysis, the Court of Appeals cited longstanding Minnesota case law that provides that incarceration alone is not sufficient to constitute abandonment. The trial court found that the incarcerated parent made specific efforts to maintain a relationship with his children, but found actual desertion by reason of the father's incarceration. Concluding that this finding of desertion was predicated solely on the fact that the father was incarcerated, the Court of Appeals said that was wrong as a matter of law.

The Court of Appeals also criticized the trial court for reasoning that the incarcerated father somehow "planned" abandonment; the trial court had reasoned that the father, by committing an intentional criminal act, had been aware that consequences might include incarceration and a finding that he had abandoned his children. Judge Randall boldly stated that "this reasoning does not persuade us." The trial court was further criticized by the Court of Appeals for not addressing the requirement that the parent be both *physically* and *financially* able to provide for his children. The Court of Appeals concluded that because of the incarceration, the father was not in a position to physically provide for his children and was not able to financially provide for them; thus, the provisions of the statute allowing termination of parental rights for failure to comply with the duties imposed upon the parent by the parent/child relationship could not be met.

Ultimately, the Court of Appeals concluded that essentially this case represented a clash between an incarcerated parent's rights and statutes designed to give young children some stability in life. Viewing the case in terms of the best interests of the minor children, the appellate court considered that the mother had voluntarily terminated her parental rights, the incarcerated father still had at least two more years to serve in prison, and — while the appellant could not be barred from contesting the termination of his parental rights because he was incarcerated — incarceration in this case was a significant factor. Ultimately, the Court of Appeals affirmed the trial court's decision to terminate parental rights, noting that the reality in this case was that these children would have no parents now and would have to wait at least two years before they might have one. Hence, the court could not find, when taking into account the best interests of these children, that the district court overstepped the bounds of its discretion when it terminated the father's parental rights. ***In the***

***Matter of the Children of Richard Wildey***, A03-262 (Minn. App. 09/30/03). *http://www.courts.state.mn.us/opinions/coa/current/opa030262-0930.html*

■ **TERMINATION OF PARENTAL RIGHTS; REASONABLE EFFORTS TO ASSIST.** In a case originating out of Hennepin County the decision to terminate parental rights was affirmed when the mother repeatedly attempted suicide since her child was born in 2001; failed to complete recommended treatment; continued to abuse alcohol despite being advised of its harmful affects on her mental state; remained impulsive and lacked insight into her behavior. The court concluded that the county engaged in reasonable efforts to provide assistance to her. ***In the Matter of the Welfare of the Child of Kuschill***, C0-03-311 (Minn. App. 09/23/03) (unpublished). *http://www.lawlibrary.state.mn.us/archive/ctapun/0309/op030311-0923.htm*

■ **TRANSFER OF CUSTODY; PERMANENCY DETERMINATION; BEST INTERESTS.** In a juvenile court decision where a mother challenged a district court's transfer of legal and physical custody of her children as a permanency determination after a CHIPS petition was filed, the Court of Appeals addressed the applicability of the best interest factors of Minn. Stat. §518.17 where transfer of custody is the permanency option in a CHIPS proceeding. The court held that Minn. Stat. §260C.201 only requires the court to "follow the standards applicable under this chapter and chapter 260." Under that set of criteria, the transfer of custody was affirmed. ***In Re the Children of Oja***, C5-03-238, C7-03-239, and C3-03-240 (Minn. App. 09/02/03). *http://www.lawlibrary.state.mn.us/archive/ctapun/0309/op030238-0902.htm*

■ **TERMINATION OF PARENTAL RIGHTS.** In another unpublished termination of parental rights case, the Court of Appeals affirmed a district court's termination of the mother's parental rights where the district court found that the mother was palpably unfit to parent her seventh child (her previous six children had been either given up for adoption, removed from her home, or parental rights terminated) because she had "demonstrated no insight into the reason for the previous terminations and presented no evidence that she could properly parent her seventh child now or in the foreseeable future." ***In Re the Child of Spencer***, C9-03-355 (Minn. App. 09/02/03) (unpublished). *http://www.lawlibrary.state.mn.us/archive/ctapun/0309/op0303550902.htm*

■ **TERMINATION OF PARENTAL RIGHTS; PROCEDURE.** In a procedurally significant unpublished decision, the Court of Appeals reviewed parents' challenge to the district court's termination of their parental rights after the trial court vacated an order transferring legal custody to a relative as the permanency determination in a CHIPS proceeding. These parents had five children. The county had petitioned to terminate the parents' rights to all five children, but the mother and the attorney for the two oldest children filed motions to transfer legal custody to a relative. The parties agreed to try the termination petition and the custody motions together. After trial, the district court found evidence existed to terminate the parents' parental rights, but also found that it was in the children's' best interests to transfer custody to the relative.

Within one month of that decision, the relative who was awarded custody brought one of the children to a shelter and refused to take him back. At a hearing, the relative testified that she had not wanted custody of the two older children, but she stated that she had sought custody because she thought the court would not award her custody of only three of the five children. The court found this to be a fraud upon the court; it vacated the custody transfer order and continued the review hearing. After the continued hearing, the court held that it retained jurisdiction to terminate the parents' parental rights, it terminated their parental rights, but stayed entry of the judgment to allow them to make additional motions.

While the attorneys for the parents reiterated their objections to jurisdiction and argued that the parties would have offered different evidence at trial if a transfer of custody had not been a viable option, they offered no additional evidence or offers of proof regarding what evidence they would present.

The Court of Appeals affirmed the finding that trial court had jurisdiction to terminate parental rights. It stated that once the custody transfer order was vacated, it was as if that disposition had never existed. The findings of fact and conclusions of law that grounds existed to terminate parental rights, which the parents did not challenge, remained. Further, considering that only one month elapsed between the custody transfer order and the vacation of that order, the Court of Appeals held that the district court could terminate parental rights without an additional evidentiary hearing. ***In Re the Welfare of the Children of Traylor***, C5-03-398 (Minn. App. 09/16/03). *http://www.lawlibrary.state.mn.us/archive/ctapun/0309/op030398-0916.htm*

■ **CHIPS; PRIOR DETERMINATION OF ABUSE; COLLATERAL ESTOPPEL.** In a case where the trial court had found three children in need of protection or services, the father argued that the trial court erred in concluding he was collaterally estopped from litigating whether he had sexually abused one of his stepchildren. The abuse of his stepchildren was an earlier determination being used against him in the present proceeding. Because he was a party to an earlier proceeding in which his abuse of the stepchild was litigated, and because he had a full and fair opportunity to litigate that allegation of abuse, the trial court did not err as a matter of law in giving the findings of the earlier determinations preclusive effect. This prior determination was, according to the Court of Appeals, appropriately used as a basis for adjudicating the father's own children's need of protection or services as children residing with a perpetrator of domestic child abuse. ***In the Matter of the Children of Shannon Barrington and James Barrington***, A03-13 (Minn. App. 09/02/03).
*http://www.lawlibrary.state.*
*mn.us/archive/ctapun/0309/op030013-0902.htm*

■ **SURROGATE PARENT; MEDICAL INSURANCE; "COVERED PERSON"; SOUTH CAROLINA.** In a case addressing a rather significant issue that occurs in assisted reproductive technology cases throughout the county, the United States District Court for the District of South Carolina ruled in July of this year that medical expenses incurred by a surrogate mother on behalf of the infant she bore are not covered under her husband's family health insurance. The court, in noting that the surrogate and her husband do not contest the fact that the child is the biological offspring of the married couple who contracted with the surrogate to carry and then give birth to their natural child, stated that the child is not the "dependent" of the policy holder (the surrogate's husband) and thus is not a "covered person" under his insurance. This case should provide a note of caution to attorneys practicing in this area to be sure and address the insurance costs at the outset of the ARTS procedures being undertaken. ***Mid-South Insurance Co. vs. Doe***, 2:02-1789-18, 274 F.Supp.2d 757 (D.S.C. 07/29/03).

TRENDS AND DEVELOPMENTS

According to a national study, counties throughout the country are abandoning large children's shelters in favor of relatives, friends of the family, foster homes, and smaller group settings for children removed from their homes. According to officials, these alternatives are cheaper and allow children to heal more quickly from abuse and parental separation. The monthly costs for group care can be six to ten times higher than the family foster care, and data on the outcomes of children living in institutions showed that these children have poorer educations and higher arrest and substance abuse rates as adults. The San Jose *Mercury News*, 09/11/03, as reported in the weekly news summary of the National Center for Adoption Law and Policy, 09/11/03.

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## REAL PROPERTY

JUDICIAL LAW

■ **MECHANIC'S LIEN.** Phenix planned to develop distinctive particleboard products that required custom-made equipment and manufacturing plant. In December 1996, construction of the plant commenced. However, in the spring of 1997, construction ceased due to Phenix's financial problems. Phenix pursued financing from Lender. Before giving the loan to Phenix, Lender required a contractor give a statement pertaining to its work. This contractor gave a sworn statement on February 6, 1998, representing the work remaining and amount due on its contracts. The contractor also waived claims of priority over the mortgage. The loan closed and Lender recorded its mortgage on April 20, 1998. Early in 1999, Phenix defaulted on the loan and failed to pay its contractors. The contractors filed mechanic's liens and one contractor initiated this lawsuit to enforce its lien rights. Phenix subsequently entered into a forbearance agreement with the contractor. The contractor secured the agreement with 11 personal guarantees. Thereafter, the guarantors formed a limited liability partnership and the contractor assigned the lien statement to the LLP. Lender challenged the priority of the liens. The district court found that the project had been effectively abandoned in April 1997, so the mortgages recorded after the work was abandoned but before construction recommenced have priority over the subject mechanic's liens.

The Court of Appeals upheld the district court ruling. The court agreed that the contractors abandoned the project in the spring of 1997 when they terminated their work, Phenix barricaded the site

and posted 'no trespassing' signs, and Lender took steps to ensure all prior liens were paid off before the closing by obtaining a valid contractor's sworn statement. Because the contractors abandoned the project, the liens subject to this action relate to work performed after the refinancing and do not relate back to the original start of construction. Therefore, the mortgages have priority over the liens. ***Langford Tool & Drill, Co. vs. Phenix Biocomposites, LLC et al.***, C2-02-2146 (Minn. App. 09/09/03). *http://www.lawlibrary.state.mn.us/archive/ctappub/0309/op022146-0909.htm*

■ **CONDEMNATION.** Owners of a business that quarries, sells and transports sand and gravel to nearby construction sites utilized a bridge over Crow River to deliver their products. In 1994, as a result of bridge deterioration, Hennepin County imposed load restrictions on the bridge. Under the restrictions Owners' trucks could only cross the bridge if they were empty. In 2000, Hennepin County further reduced the load limits to an amount that prevented Owners' trucks from using the bridge, whether loaded or empty. An alternative route used by the truckers increased their drive by 16 miles round trip, thereby increasing Owners' costs and expenses. Consequently, Owners brought this inversion condemnation action against Hennepin County. The district court dismissed Owners' action with prejudice finding that Hennepin County legitimately exercised its police power by imposing the load limits on the bridge and Owners "'are non-abutting owners with no injury distinct from that of the general public.'" The Court of Appeals affirmed the district court decision. The court held that while the Minnesota Constitution provides landowners with just compensation for any taking, for public use, of the owner's right to reasonable and suitable access to and from her property, these owners are not entitled to compensation simply because a more convenient route has been denied them. Moreover, Owners' land does not abut the road subject to this dispute. Lastly, the restrictions imposed by Hennepin County do not exclusively affect Owners but impact all motorists. ***Scherber et al. vs. Hennepin County***, A03-60 (Minn. App. 09/16/03). *http://www.lawlibrary.state.mn.us/archive/ctapun/0309/opa030060-0916.htm*

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## TAX

JUDICIAL LAW

■ **REAL PROPERTY VALUATION: FAIR MARKET VALUE AND UNEQUAL ASSESSMENT.** The Minnesota Tax Court held that the fair market value of the property at issue as of January 2, 1999, was $4,525,000. The parties' real property valuations under the comparable sales and replacement cost methods ranged from $3.5 million to $5.5 million. In addition, the court reduced the fair market value by 14.4 percent because of discriminatory and unequal valuation under the sales ratio studies provided for in Minn. Stat. §278.05(4 (95% less 80.60% equals 14.4% — the reduction equal to the difference between 95% and the median ratio). ***SPX Corp. v. County of Steele***, C1-00-350, 2003 WL 21729580 (Minn. T. Ct. 07/23/03).

■ **REAL PROPERTY TAX INCREASE.** The Minnesota Tax Court held that the valuation of an office/warehouse property located in Burnsville, Minnesota should be increased to a value of $2,800,000 from the estimated value as placed by the assessor of $2,671,200 in January 2, 2001. The court dismissed the value of the taxpayer's expert and his value of the property at $2,512,900. The taxpayer's expert was not qualified as being an expert under Minn. R. Evidence 702 but the court accepted his testimony as a lay witness. The proposed expert's extensive experience in real estate investment did not make him a real estate market expert on property valuation and appraisal methods. ***WLPT Cliff Six LLC v the County of Dakota***, C9-02-7384, 2003 WL 22037632 (Minn. T. Ct. 08/20/03).

■ **REAL PROPERTY; UNEQUAL ASSESSMENT; DISCRIMINATION**. The Minnesota Tax Court held that the taxpayer failed to meet its burden of proving a value different from the assessed value of $1,099,000 even though its expert testified that the property had a value of $545,000. The court dismissed the taxpayer's expert because he relied on listing prices, not consummated purchase agreements which the court found were not sales under the law. However, the court took judicial notice of the 2001 Assessment Sales Ratio Study for a nine-month period and found that the median ratio for real estate in Shorewood was 86.0 percent and therefore, unequal assessment relief under Minn. Stat. §278.05(4(d) was called for. Accordingly, the court reduced the estimated market value by 9.0 percent. ***Malcolm D. Reid and Katherine S. Flom v. County of Hennepin***, No. 29750, 2003 WL 22037630 (Minn. T. Ct. 08/18/03).

■ **DISCOVERY REQUEST FOR DEPOSITIONS ON DEPARTMENT'S OFFICIALS DENIED.** The Minnesota

Tax Court denied a *pro se* taxpayer's discovery request for depositions of two Revenue Department officials, who signed orders assessing him with taxation. The court indicated that it had adopted a broad policy on discovery so long as the requested discovery appeared to lead to admissible evidence under Minn. R. Civ. P. 26.02(a). There is an exception to the general principle of wide-ranging discovery where administrative executives and other governmental officials are involved. In those situations, the court will exercise its discretion by placing reasonable limits upon the taxpayer's access to the officials and its concomitant disruption of the government's function. The court did permit deposition discovery on a Revenue Department employee who had personal knowledge of the taxpayer's file and the returns. ***Frederick O. Bond v. Commission of Revenue***, No. 7555, 2003 WL 21729446 (Minn. T. Ct. 07/22/03),

■ **FOREIGN CORPORATION; ENTITLEMENT TO DIVIDEND RECEIVED DEDUCTION.** The Minnesota Tax Court determined that a foreign sales corporation (FSC), which had qualified as a foreign operating corporation (FOC), did not receive the special dividend received deduction normally provided for a deemed dividend distribution from the FOC to its recipient under Minn. Stat. §290.21, Subd. 4(e). ***Hutchinson Technology, Inc. v. Commissioner of Revenue***, Nos. 7398-R and 7504-R, 2003 Minn. Tax LEXIS 37 (Minn. T. Ct. 09/15/03).

■ **MICHIGAN SINGLE BUSINESS TAXES NOT CREDITABLE FOR MINNESOTA SUBCHAPTER S CORPORATION.** The Minnesota Tax Court held that Minnesota residents owning a Subchapter S corporation which paid the Michigan Single Business Taxes ("Michigan SBT") was not allowed to claim an individual income credit for such taxes on their Minnesota income tax returns. Minnesota law provides in Minn. Stat. §290.06(22(g) for a personal credit against Minnesota income taxes for shareholders when the S corporation pays to another state taxes which are on or measured by net income. Although the Michigan SBT begins with federal taxable income, the court held that that was just the starting point since numerous additions and subtractions were made to what is economically considered to be a value-added tax. The court also found persuasive authorities in other courts holding that the Michigan SBT was a value-added tax and not a tax based on net income as required by Minnesota law. ***Robert and Virginia Carlson v. Commissioner of Revenue***, No. 7443, 2003 WL 21729573 (Minn. T. Ct., 07/24/03).

■ **TAX PROTESTER'S MINNESOTA INCOME HELD SUBJECT TO TAXATION.** The Minnesota Tax Court held that a taxpayer, who filed federal returns for 1999 through 2001 containing only zeros, was required to file a Minnesota income tax return and pay income taxes on his income. Additionally, the taxpayer's conduct and tax returns were deemed to be frivolous and penalties were imposed. The court rejected the taxpayer's argument that income taxes are voluntary and he chose not to "volunteer". ***Craig Steven Walquist v. County of Hennepin***, No. 7560, 2003 WL 21729715 (Minn. T. Ct., 07/24/03).

■ **SALES TAX; CAPITAL EQUIPMENT; SERVICE BUSINESS.** The Minnesota Tax Court held that equipment purchased for use in providing telecommunications services before August 1, 2001, was not eligible for the capital equipment exemption under Minn. Stat. §297A.01, Subd. 16(a) and Minn. Stat. §297A.25, Subd. 42. ***XO Communications, Inc. v. Commr. of Rev.***, Nos. 7430-R; 7442-R, 2003 WL 22038358 (Minn. T. Ct. 08/27/03).

■ **SALES TAX: EQUIPMENT AND MATERIALS FOR PROCESSING FOOD; ELIGIBILITY FOR REFUND.** The Minnesota Tax Court held that the cost of equipment and materials used by Leeann Chin's food-processing facility to convert raw chicken into marketable chicken intended for sales to either third parties and/or Leeann Chin's own restaurants was exempt from Minnesota sales and use taxes. Therefore, Leeann Chin was eligible for sales tax refunds under the Equipment Exemption in Minn. Stat. §297A.01, Subd. 16 and the Industrial Production Exemption in Minn. Stat. §297A.25, Subd. 9. ***Leeann Chin v. Minnesota Commissioner of Revenue***, No. 7384-R, 2003 WL ____ (Minn. T. Ct. 09/04/03).

■ **SALES TAX; CAPITAL EQUIPMENT; SERVICE BUSINESS.** The Minnesota Tax Court found that Sprint was ineligible for the capital equipment refund since it was not engaged in the "manufacturing, fabricating, or refining" of "tangible personal property." ***Sprint Spectrum LP v. Commissioner of Revenue***, No. 7299-R, 7308-R, 7309-R, 2003 WL 21246600 (Minn. T. Ct. 05/23/03).

■ **LAWYERS; GRAMM LEACH BLILEY PRIVACY NOTICES; FTC.** The April 2002 opinion letter issued by the Federal Trade Commission ("FTC") and defining lawyers who provide real estate settlement, tax planning, and tax preparation services as "financial institutions" subject to consumer privacy notice requirements of the Gramm-Leach Bliley Act ("GLBA") may violate the Administrative Procedure Act as arbitrary and capricious agency action or agency action in excess of statutory juris-

diction. "The FTC's interpretation of the GLBA's applicability to attorneys seems to ignore the plain language of the statute's regulatory scheme," the court said. Under the arbitrary and capricious standard, agency actions are measured in the light of the thought process engaged in by the agency in making its decision. In the instance case, the court found that the FTC [had] failed to articulate any explanation, let alone a satisfactory one, for its interpretation. ***New York Bar Association v. Federal Trade Commission***, No. 02-801 (RBW) (D.D.C. 08/11/03).

■ **GOVERNMENT'S MOTION TO COMPEL TAX TRANSACTION DOCUMENTS.** IRS's motion to compel production of plaintiff's documents, which centered on creation of entity to manage health care benefits of plaintiff's employees and retirees and which generated large capital loss and federal tax refund of $57 million for tax years 1995 through 2000, was denied. Documents were privileged under either opinion work product or fact work product doctrines. ***Black & Decker Corp. v. United States***, No. WDQ-02-2070. (D. Md. 09/15/03).

■ **CLAIMS COURT; RECAPTURE OF WAGE DEDUCTION CALCULATING AMT.** Taxpayers taking advantage of the targeted jobs credit to reduce regular tax liability must incorporate the IRC Section 280C(a) wage-deduction limitation into their computation of taxable income for regular income tax and the Alternative Minimum Tax ("AMT"). The court, agreeing with the IRS, decided that the same deductions claimed for the regular income tax base must also be used in determining the AMT base. The court made the following conclusions:

- The basis of AMT income is regular taxable income;
- Adjustments to regular taxable income for purposes of computing AMT income are permitted only to the extent that they are allowed by the Tax Code; and
- The result is consistent with the fact that the AMT was enacted to serve as a safeguard within the regular income tax system.

Looking to IRC Section 55, the court found that the AMT base computation begins with the taxable income of the taxpayer for the taxable year. Since the wage-expense limitation of IRC Section 280C(a) is part of that taxable income calculation, the limitation imposed by IRC Section 280C(a) must, by definition, be carried through to the calculation of the AMT base. Therefore, the taxpayer's refund claim was denied. ***Ventas Inc.***, (No. 01-31, 92 AFTR 2d 2003-5711, Fed. Cl., 07/30/03).

■ **LIMITATIONS PERIOD FOR ERRONEOUS REFUND SUIT.** Erroneous refund suit brought by IRS was filed within two years from date of payment by U.S. Treasury, therefore it was timely filed. ***United States v. Greene-Thapedi***, No. 01 C9129, 91 AFTR 2d 2003-910 (N.D. Ill. 09/03/03).

■ **BUSINESS PURPOSE ESTABLISHED FOR ANNUAL EMPLOYEE FISHING TRIPS.** Taxpayer presented adequate evidence to substantiate the business purpose of annual fishing trips to a Canadian resort for its employees where business discussions were conducted on an ongoing basis. Taxpayer was not required to treat the per-employee trip expenses as wages and to withhold income and Social Security taxes. ***Townsend Industries Inc. v. United States***, No. 02-3756, 92 AFTR 2d 2003-6096 (8th Cir. 09/15/03).

■ **ATTORNEY'S FEES FROM SETTLEMENT NOT INCLUDABLE IN CLIENT'S INCOME.** The 9th Circuit affirmed the Tax Court's judgment that economic and punitive damage awards are includable in an individual's income and that alternative minimum tax was constitutionally applied in this case. The court reversed the judgment including attorney's fees in the individual's income because they were paid directly to the attorney and under Oregon law the attorney lien took priority over the taxpayer's claim. ***Sigitas Banaitis v. Commissioner***, No. 02-70421, 92 AFTR 2d 2003-5834 (9th Cir. 08/27/03).

■ **ESTATE TAX VALUE OF FUTURE LOTTERY PAYMENTS; ANNUITY TABLES**. Reversing the Tax Court, the 2nd Circuit Court of Appeals has held that installments of lottery winnings remaining unpaid as of decedent's death did not have to be valued for estate tax purposes using the Code Sec. 7520 valuation tables. ***Estate of Gribauskas***, No. 01-4189, 92 AFTR 2d 2003-5914 (2nd Cir. 08/26/03).

■ **DEFAULTED STUDENT LOAN; OFFSET AGAINST INCOME TAX REFUND.** Plaintiff's claim against Department of Education ("DOE") arising from offset of defaulted student loan against income tax refund is dismissed. IRC Section 6402(d) authorizes any federal agency that is owed a legally enforceable debt to, upon notice to the debtor, apply to the Department of Treasury for an offset from the debtor's tax refund. Because DOE did not act outside its authority in this case, plaintiff cannot state a claim for injunctive relief under the Administrative Procedure Act. ***Shabatai v. Department of Education***, No. 2 Civ. 8437 (LAP) (S.D. N.Y. 08/20/03).

■ **XEROX'S CASH BALANCE PLAN VIOLATES ERISA.** The 7th Circuit held that Xerox's method of determining an exemployee's benefit, if a lump-sum benefit is chosen on leaving before retirement, violates ERISA, but that the lower discount rate applied only to exemployees with account balances under $25,000. The court found that Xerox's plan conditions employees' right to future interest credits on the form of the distribution that they elect to take, which is forbidden under ERISA. ***David Berger, et al. v. Xerox Corporation Retirement Income Guarantee Plan***, No. 02-3674 (7th Cir. 08/01/03).

■ **PAYMENTS TO SHAREHOLDER/EMPLOYEE AS ROYALTIES AND RENT WERE WAGES.** The Tax Court held that amounts paid by a corporation to its shareholder/employee and designated as royalty and rent payments were, in fact, wages subject to withholding employment taxes. ***Charlotte's Office Boutique, Inc.***, 121 TC No. 6 (2003).

■ **PRIVILEGE WAIVED: GOVERNMENT MAY DEPOSE OUTSIDE TAX COUNSEL.** A U.S. district court, granting the IRS's motion to compel discovery and denying debtor's motion to bifurcate, held there was a subject-matter waiver of all communications between two corporations and their outside tax counsel about a shelter transaction for which they asserted an affirmative defense against the IRS's penalties. The debtors' communications with their Arthur Andersen tax consultant on the tax treatment of the transaction are not protected by *Kovel* rules, 296 F.2d 913 (2nd Cir. 1961). The court also ordered disclosure of all relevant communications between the debtors and their outside counsel, William S. McKee and William F. Nelson, who provided tax planning for the 1990 transaction, including drafting the partnership agreement and an opinion letter. Even though Nelson was representing G-1 Holdings in litigation before the Tax Court, the court said that the IRS may depose the attorneys, because the debtors "created the very prejudice of which they complain." ***In re G-1 Holdings Inc. et al.*** No. 02-3082 (D. N.J. 07/18/03).

■ **NOL CARRYBACK MAY MAKE 'HOT INTEREST' RATE INAPPLICABLE.** A net operating loss ("NOL") carryback is taken into account for purposes of determining whether a large corporate tax underpayment exists. Therefore, the additional or "hot interest" imposed on large corporate tax underpayments does not apply if an NOL carryback reduces an underpayment of tax below $100,000. ***Med James Inc. v. Commissioner***, 121 T.C. No. 9 (09/09/03).

## ADMINISTRATIVE MATTERS

■ **INCOME TAX — EXPLANATION OF K-12 EDUCATION CREDIT.** In Minnesota Department of Revenue Notice No. 03-05 (06/03/03), the commissioner explained the specific requirements that must be followed if a vendor offers a package of educational services and products to a purchaser for the K-12 Education Credit. The Revenue Notice also discusses the K-12 Education Credit allowance for payments made for "education-related expenses in the tax year" and the purchaser borrowing money for the purchase of a qualified educational product by assigning the right to their Minnesota income tax refund to the lender to guarantee repayment.

■ **MINNESOTA GRANTS INCOME TAX RELIEF FOR BLACKOUT VICTIMS.** New Release (08/26/03), announced that the commissioner will abate late filing or payment penalties for taxpayers affected by the recent blackout caused by a breakdown in the electrical grid in the Northeast.

■ **SALES AND USE TAX; MASSAGE THERAPY.** In Minnesota Department of Revenue Notice No. 03-09 (09/08/03), the commissioner clarified that massage therapy provided by licensed or registered healthcare providers was subject to the MinnesotaCare tax or the Minnesota sales tax. A massage therapist, who is also a licensed or registered healthcare provider, collects the sales tax and does not pay the MinnesotaCare tax, if the massage is not for the treatment of an illness, injury or disease. If the massage is provided as treatment of an illness, injury or disease, it is subject to the MinnesotaCare tax. All massage services are presumed to be subject to sales tax unless the massage therapist can show that the service was for treatment of illness, injury or disease. This Revenue Notice also supplements Revenue Notice 02-08 (06/24/02).

■ **SALES AND USE TAX; TELECOMMUNICATIONS SERVICES.** In Minnesota Department of Revenue Notice No. 03-10 (09/08/03), the commissioner explained the sales tax treatment of telecommunication services, including Internet access charges, hotel and motel telephone charges, bundle services, and telecommunications equipment. This Revenue Notice revoked Revenue Notice 91-18 (12/02/91).

■ **DEPRECIATION RULES UNDER 2002 AND 2003 TAX RELIEF LEGISLATION.** The IRS issued proposed and temporary rules giving taxpayers long-awaited guidance on business depreciation relief enacted under the Jobs and Growth Tax Reconciliation Act of 2003. That law, which expanded relief first provided by the Job Creation and Worker Assistance Act of 2002, allows taxpayers to deduct an additional 30 percent or 50 percent first-year depreciation allowance for certain deprecia-

ble property. The guidance provides the requirements for depreciable property to qualify for the first-year depreciation deduction. It instructs taxpayers how to calculate the additional first-year deduction and the amount of depreciation otherwise allowable for the property. In general, the rules apply to depreciation of computer software and property eligible for the Modified Accelerated Cost Recovery System (MACRS) under IRC §§167 and 168. REG 157164-02, T.D. 9091 (09/08/03).

■ **CHANGES IN REPORTING GAINS FOR CERTAIN FISCAL YEAR ENTITIES.** The IRS provided guidance on reporting of capital gains by individuals and certain entities, who use a 2002-2003 fiscal year that ends after May 5, 2003. IRS Announcement 2003-56.

■ **JGTRRA CHANGES TO INFORMATION REPORTING RULES.** The IRS provides guidance to brokers and individuals on provisions in the Jobs and Growth Tax Relief Reconciliation Act of 2003 ("JGTRRA") that affect information reporting for payments in lieu of dividends. JGTRRA reduced the tax rate for qualified dividends paid to an individual shareholder to the same tax rate as capital gains. The notice announces the IRS's intention to exercise its authority under IRC §6724(a) to waive penalties under IRC §§6721 and 6722 for information returns with respect to calendar year 2003 payments if a broker makes a good faith effort to satisfy its information-reporting obligations in a way that is consistent with the statutory changes effected by the JGTRRA.

■ **CRACKDOWN ON SHELTERS VIA INFORMATION SHARING.** The IRS is joining forces with states nationwide to crack down on abusive tax shelter schemes by sharing information much earlier in the investigation process. Under new agreements signed with 40 states and the District of Columbia, IRS will share information with states on questionable tax schemes and participants at the outset of an audit, rather than after a corresponding audit at the state level has concluded. 2003 BNA *Daily Tax Report* at 6-8 (09/17/03) and IRS News Release IR-2003-111 (09/16/03).

■ **JOINT COMMITTEE ON TAXATION; IRC SECTION 6505.** The Office of Chief Counsel issued a notice explaining the role of the Joint Committee on Taxation regarding refunds and credits of tax under IRC §6405, and clarifying the procedures the IRS uses to comply with this section. CC 2003-023.

■ **COPIES OF TAX RETURN INFORMATION.** Taxpayers have two options for requesting copies of their tax return information — by phone or mail. To get them by calling just call (800) 829-1040 and follow the prompts in the recorded message. To get them by mail send Form 4506 to the IRS address shown in the instructions. They ask that you allow two weeks for transcripts to be delivered by mail. Three different types of tax data are available: tax return transcripts, tax account transcripts, and photocopies of tax returns.

■ **WHERE TO FILE INDIVIDUAL INCOME TAX RETURNS IN 2004.** Here is where individual tax returns will be filed in 2004:

Andover — ME, MA, NH, NY, VT
Atlanta — AL, FL, GA, MS, NC, RI, SC, WV
Austin — AR, CO, KY, LA, NM, OK, TX, TN
Fresno — AK, AZ, CA, HI, ID, MT, NV, OR, UT, WA, WY
Kansas City — DE, IL, IN, IA, KS, MI, MN, MO, NE, ND, SD, WI
Memphis — OH, VA
Philadelphia — CT, MD, NJ, PA

■ **E-FILE HELP FOR TAX PROFESSIONALS.** The IRS has released a new centralized free number for the IRS e-Help desk. The new number is (866) 255-0654. The IRS e-Help desk supports IRS e-file, the Electronic Federal Tax Payment System (EFTPS), TeleFile, and future IRS e-services customers. Callers from outside of the 50 U.S. states and/or U.S. territories should use the international phone number (512) 416-7750. This number is not toll free. IRS e-Help assistors are ready to respond to enrolled agents, reporting agents, electronic return originators (EROs), certified public accountants, software developers, and transmitters with non-account related questions and issues concerning IRS e-products. *See www.irs.gov/efile/article/0,,id=109708,00.html* for times the service is available.

■ **WEB LINKS.** Looking for a quick way to navigate the IRS Digital Daily Web pages? Go to the site map: *www.irs.gov/sitemap/index.html* The Digital Daily site map lists IRS topics and subtopics in alphabetical order. Try it, you'll like it.

■ **PUBLICATIONS OF INTEREST.** The IRS *Payroll and Professional Partners Headliners* are online information packages, which will keep you apprised of important IRS messages impacting you as a tax professional. They are located at: *www.irs.gov/businesses/small/article/0,,id=102669,00.html.*

The SSA/IRS *Reporter* summer 2003 edition is available online at: *http://www.irs.gov/businesses/small/article/0,,id=98451,00.html* or *www.ssa.gov/employer/pub.htm*.

### Legislation

■ **Ethics Rules on Confidentiality, Corporate Clients; More Disclosures**. The ABA approved a package of recommendations designated to help lawyers deal with clients' fraud — especially wrongdoing within corporations. Proponents said that changes made in the Rules of Professional Conduct 1.6 and 1.13 are necessary in light of recent corporate fraud scandals. Opponents argued they will turn attorneys into whistleblowers whom clients will not trust with sensitive information. Model Rule 1.6 was amended to permit lawyers to reveal information normally protected by client-attorney confidentiality in order to prevent a client from committing financial fraud or to mitigate injury from a financial fraud. Changes to Model Rule 1.13 require lawyers representing organizational clients to report law violations by officers or employees up the ladder to higher authorities in the organization in certain circumstances. They further provide that if internal reporting is insufficient to protect the entity client from substantial harm, the lawyer may report wrongdoing to people outside the organization. Congress enacted the 2002 Sarbanes-Oxley Act, which, among other things, directed the Securities and Exchange Commission to promulgate rules of professional conduct for lawyers appearing before the agency. Those rules went into effect earlier this year and they require lawyers to report to the highest levels of corporate authority violations of the securities laws and other failures of legal compliance. The SEC rules also permit lawyers to disclose client fraud to third parties to prevent substantial injury to a corporation or investors.

### Looking Ahead

■ **Multistate Commission Moves Ahead on Unitary Business Proposal.** The Multistate Tax Commission ("MTC") moves closer toward adopting a proposed regulation that sets forth principles for identifying a unitary business. The MTC held a meeting in August, 2003 on the proposed regulation. A unitary business can include different segments of a company's business operations located in different state jurisdictions, if the segments are sufficiently related. 2003 *BNA Daily Tax Report* at 6-2 (08/08/03). The hearing notice and the proposed regulation are available at *http://www.mtc.gov/MEETINGS/NoticeOfHearing08-07-03&08-11-03.pdf*.

■ **Permanent Extension of Internet Tax Moratorium?** In July, 2003, a Senate committee approved S.150, which permanently would extend the ban on state taxes on Internet access. The "Internet Tax Nondiscrimination Act," formerly the "Internet Tax Freedom Act," also includes a ban on any "multiple and discriminatory "state taxes on both electronic commerce and Internet access. The measure parallels a similar bill (H.R. 49) making its way through the House. The two bills split on the issue of states that already tax access. The Senate's bill provides the handful of states that collected access taxes before the original Freedom Act became law in 1998 a sunset period to phase-out those taxes. The House bill gives no such latitude. The major sticking point of the Internet Tax Nondiscrimination Act is the murkiness of the definition of "Internet access." Many fear that it is too broad and could open a Pandora's Box of tax bans that could conceivably allow telephone charges to become exempt from state taxes when offered together or bundled with Internet access services. The current moratorium expires on November 1, 2003.

■ **Tax Incentives For Charitable Giving.** The House approved a $12.6 billion package of charitable giving incentives (H.R. 7). The bill contains a wide range of tax incentives for charitable giving, including a deduction for certain cash donations by individuals who do not itemize their taxes. The bill also would allow qualified taxpayers aged 70 1/2 or over to roll over their IRAs for charitable purposes without suffering tax consequences, and increase the cap on corporate donations to charity from 10 percent to 20 percent of modified taxable income.

— Jerry Geis
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## TORTS & INSURANCE

### Judicial Law

■ **Subrogation; Medical Assistance; Future Medical Interest.** When, as a condition for receiving Medical Assistance, the recipient assigns to the state "any rights to medical support and third party payments," the rights to payment of future medical expenses are included in the assignment.

Guzman, a minor, was struck by a U.S. West truck and suffered permanent injuries, including brain

damage. Experts predicted her lifetime medical costs to be $5.7 million. At the time of her accident, Guzman did not have medical insurance. Her mother applied for and obtained Medical Assistance from the state and, as a condition of eligibility, assigned to the state "any right to medical support and third party payments." The state filed a Medical Assistance lien on any cause of action arising out of the accident and settled with U.S. West for all past, present, and future claims. Guzman reached a separate settlement with U.S. West for the remaining claims, with the exception of future medical expenses. U.S. West moved to dismiss Guzman's claims for future medical expenses. The district court granted U.S. West's motion to dismiss, holding that future medical expenses had been assigned to the state.

The Court of Appeals affirmed, holding that Guzman's claim for future medical benefits was extinguished. A condition of Medical Assistance eligibility under federal and Minnesota law was the assignment "to the State any rights ... to support and to payment from any third party." The court held that such an assignment included her rights to recover both past and future medical expenses. The Court of Appeals recognized that requiring an assignment of future medical benefits seems unfair in this context, but nonetheless it was lawful. ***Anissa Maria Guzman, a minor, by Rebecca Z. Lasoya v. U.S. West, Inc.***, C9-03-310 (Minn. App. 08/19/03).
*http://www.lawlibrary.state.mn.us/archive/ctappub/0308/op030310-0819.htm*

■ **SEXUAL EXPLOITATION BY CLERGY.** When a cleric and a colleague engage in discussions about their personal problems, their conversations are not "psychotherapy" within the meaning of Minn. Stat. Ch. 148A, which provides a cause of action for sexual exploitation by a psychotherapist.

F.P., a priest, was assigned to Doe's parish. F.P. got to know Doe in her capacity as a part-time musician for the parish and became a friend of the Doe family. F.P. and Doe met weekly to plan music for services. They mutually discussed the intimate details of their lives, including F.P.'s sexual relationships with other women and Doe's dissatisfaction with her marriage. F.P. advised Doe to see a counselor for her family problems. F.P. and Doe eventually began a sexual relationship.

Doe and her family sued F.P. and the diocese under Minn. Stat. Ch. 148A, alleging that F.P. was practicing psychotherapy during the time that he had a sexual relationship with Doe. The district court dismissed all of Doe's claims, finding first that F.P. was not a psychotherapist under Minn. Stat. §148A.01 and second that Minn. Stat. §§609.344 and 609.345, making certain sexual contact a crime when committed by a member of the clergy, were unconstitutional.

The Court of Appeals affirmed summary judgment on the claims under Minn. Stat. Ch. 148A, finding that the communications between F.P. and Doe did not constitute psychotherapy. The court reversed the holding that Minn. Stat. §§609.344 and 609.345 violated the Establishment Clause. Holding that the statutes did not foster excessive entanglement with religion, the court remanded Doe's claims for negligent hiring and retention, negligent supervision, loss of consortium, and strict liability. ***Mary Doe v. F.P.***, CX-03-333 (Minn. App. 08/19/03). *http://www.lawlibrary.state.mn.us/archive/ctappub/0308/op030333-0819.htm*

■ **INSURANCE COVERAGE — PRO RATA TIME ON RISK NOT APPLICABLE.** This declaratory judgment action was brought by several of 3M's high-level, excess-layer, occurrence-based policy insurers, seeking to clarify coverage obligations in 3M's ongoing silicone breast implant mass tort litigation.

The Supreme Court refused to allocate damages *pro rata* by time on the risk. Distinguishing prior cases in which the damages were allocated over policy periods, the Court found that when a discrete and identifiable event can be determined, the *pro rata* by time on the risk allocation is inapplicable. If a court can identify a discrete originating event that allows it to avoid allocation it should do so. The Court affirmed the denial of attorney's fees and costs, holding that an agreement to reimburse an insured for defense costs by its high-level, excess-layer insurance providers does not involve the promise to relieve the insured from the burdens of litigation. ***In re: Silicone Implant Insurance Coverage Litigation***, C5-01-1546, et al. (Minn. 08/21/03).
*http://www.lawlibrary.state.mn.us/archive/supct/0308/op011546-0821.htm*

■ **MEDICAL MALPRACTICE; STATUTE OF LIMITATIONS; WRONGFUL DEATH.** The statute of limitations for actions for wrongful death claims premised on medical malpractice commenced between August 1, 1999, and July 31, 2002, is four years from the date the claim accrues. For claims brought on or after August 1, 2002, the statute of limitations is three years from the date of death, but no more than four years from the date the claim accrues. ***Murphy v. Allina Health System***, C1-03-124, C1-03-213 (Minn. App. 08/26/03). *http://www.lawlibrary.state.mn.us/archive/ctappub/0308/op030124-0826.htm*

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