



OUR FIRM

Carr McClellan recently held its annual retreat in the beautiful Napa Valley. Amidst the rolling green hills and yellow blossoming wild mustard our attorneys and their families enjoyed some great meals together, a bit of recreation, and, yes, some wonderful wines. In between the "R&R" we also met to discuss the state of the firm, trends in the legal profession and how we as advisors and advocates for our clients, can make ourselves better. Our focus this year was on mentoring.

As many of you know, during the course of the last several years the firm has added some very bright, capable young lawyers to the cadre of well-established veterans of Carr, McClellan. We are pleased to report that two more joined us this spring as well. **Katy Kim**, a Michigan, Yale and Stanford Law School graduate is the newest member of our real estate group after having practiced for four years at a large law firm in San Francisco. **Jeremy Burns**, a Brown University and Boalt Hall School of Law graduate joins our litigation team from another large law firm in the Silicon Valley. Our focus on mentoring these and our other more recent hires springs from our recognition that really great lawyering comes from the nexus of capability, skill and experience. Mentoring younger less-experienced attorneys hastens the learning curve for them by supplementing their own experiences with those of their mentors. The raw material of younger lawyers' capabilities is honed into skillful practice by the imparted lessons of experience learned by more seasoned counsel.

Our firm is gratified that our clients and allied professional service providers have recognized that our lawyers are exceptional by continuing to ask for our assistance and by referring to us their clients. Carr, McClellan's track record for the past 60+ years has demonstrated that by focusing first, second and third on helping our clients achieve their long term goals we will also achieve our own long term goals. Those goals are to continue to be a valued resource, a trusted advisor and an irreplaceable team member of our clients and to our community organizations. We are focused on mentoring our next generation of Carr, McClellan attorneys so they also will fulfill this responsibility.

Mark Cassanego
President, Carr McClellan

PLANNING FOR YOUR RETIREMENT PLAN BENEFITS

By *Laurelle Gutierrez-Lundquist, Esq.*

Retirement benefits, whether in the form of Individual Retirement Accounts (IRAs), Roth IRAs, or any one of several different types of "qualified" plans, such as corporate or self-employed pension, profit-sharing and stock bonus plans, including the widely known 401(k) plan, provide a terrific method of saving for the future. Perhaps because of this, or because retirement benefits have become such a standard employment benefit in the workplace, the vast majority of clients we advise are participants in a qualified plan or the owners of one or more IRAs. The value of retirement benefits held by those individuals has been steadily increasing, likely because people are attempting to take full advantage the tax-deferred growth of the qualified plan or IRA assets allowed by law. Yet most people do not expend similar efforts to ensure that this tax deferral continues for the longest period allowed to their designated beneficiaries. In fact, most cannot recall who they have designated as the beneficiary of their retirement benefits.

The choice of designated beneficiaries of your retirement benefits can have varied and unexpected consequences that go beyond merely fixing who is to receive the retirement benefits. The rules governing the choice of a designated beneficiary were designed to limit the tax-deferred benefits afforded by qualified plans and IRA accounts to those Congress intended to benefit from retirement plans, namely *retirees and their spouses*, and *not* their descendants. Therefore, if the plan participant or account owner dies prior to receiving all of his or her retirement benefits and names his or her spouse as the designated beneficiary of those benefits, that spouse will enjoy most of the same tax-deferred benefits as were provided the plan participant or account owner.

Historically, Congress has not offered those same tax-favored options for non-spouse beneficiaries. Instead, non-spouse beneficiaries have been forced to begin receiving required distributions from retirement plans within a short period of time following the death of the plan participant or account owner. This generally is not a beneficial result, as each distribution is subject to income tax. Fortunately, that has recently changed.

Below is a quick summary of the issues to consider in designating the beneficiary of your retirement benefits, including a description of

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some recently enacted laws that offer planning opportunities if you are considering naming someone other than your spouse as the beneficiary of your retirement plan benefits.

Naming Your Spouse as the Designated Beneficiary

Naming your spouse as the designated beneficiary of your retirement benefits provides several tax favorable options, including options that allow your spouse to choose the timing of distributions from the qualified plan or IRA account. First, if your spouse is a citizen of the United States, then naming your spouse as your designated beneficiary exempts the retirement plan assets from federal estate tax in your estate by reason of the unlimited marital deduction from estate tax. Second, your spouse can elect to roll over the retirement benefits to another retirement plan, tax-free, and can elect to treat your IRA as his or her own. By doing so, your spouse can delay the onset of the "required minimum distributions" until he or she reaches age 70-1/2 (the "requirement beginning date"), and can designate his or her own beneficiaries. Third, if your spouse does not exercise the roll over option but opts instead to receive the retirement benefits over his or her lifetime, and if you were not yet required to receive distributions from your qualified plan or IRA account when you died, your spouse can delay receiving the required minimum distributions from the plan or account until the later of the year following the year of your death or the year in which you would have reached age 70-1/2 years.

Naming Your Children or Other Non-Spouse Individuals as Designated Beneficiaries

Historically, the only benefits of leaving your retirement benefits to your children or other non-spouse beneficiaries were (i) avoiding having those benefits included in your spouse's taxable estate at his or her later death (if you are survived by a spouse), and (ii) if your children or non-spouse beneficiaries were much younger than you, they could possibly stretch out the required minimum distributions from the qualified plan or IRA account over their much longer life expectancies. However, prior to the enactment of the Pension Protection Act of 2006, non-spouse beneficiaries (e.g., children) who inherited a retirement account were provided limited options for the timing of withdrawals and distributions of the inherited retirement benefits.

First, they could receive the benefits annually over their entire life expectancies, thus deferring the income tax on each distribution for the longest term possible. However, most qualified plans *do not* allow that type of "stretch-out" but instead require lump sum distributions or distributions of all of the retirement benefits within 5 years of the participant's death. Upon such lump-sum or 5-year distribution, the benefits distributed would be subject to federal and state income tax. If those retirement benefits were also subject to federal (and state) estate tax in your estate (i.e., because your taxable estate exceeded your available federal estate tax exemption equivalency amount, or \$2,000,000 in 2007), this could result in a serious

"The choice of designated beneficiaries of your retirement benefits can have varied and unexpected consequences."

tax bill and a corresponding diminution of the value of those retirement benefits as a result of those tax payments.

With the enactment of the Pension Protection Act of 2006, Congress now allows a non-spouse designated beneficiary of an inherited qualified plan that requires a lump-sum or 5-year distribution to transfer those retirement benefits, by means of a direct trustee-to-trustee rollover on or before December 31 of the year following the year of the participant's death, to an inherited IRA established by that beneficiary to receive those retirement benefits. The inherited IRA will then make required minimum distributions to the beneficiary over his or her lifetime, thus enabling the beneficiary to enjoy tax-deferred growth of the assets in the IRA. The drawbacks of this new law are that (i) unlike the spousal rollover, the non-spouse designated beneficiary is not allowed to defer the onset of distributions until his or her own required beginning date, (ii) not all qualified plans currently allow for this direct rollover treatment because this law is so new, and (iii) the rules will be strictly imposed. Therefore, if a rollover is not made through a direct trustee-to-trustee transfer, or if the transfer is made later than December 31 of the year following the year of the participant's death, the entire amount being transferred will be subject to income tax.

Nonetheless, if you or someone you know is the non-spouse designated beneficiary of a qualified plan, you may want to make some inquiries into the possibility of doing such a rollover to an inherited IRA.

Distributions to Charities

You are allowed to designate a charity as the beneficiary of your qualified plans and IRAs. This is a great planning opportunity for those of you who intend to make gifts to one or more tax-exempt charitable organizations at your death. For example, if you were to leave your retirement benefits to individuals and make a gift of other assets to your favorite charitable organization(s), your estate would receive a charitable deduction for the value of the assets passing to the charitable organization, but the retirement benefits would be subject to federal estate tax in your estate *and* each distribution of retirement benefits to your designated beneficiary(ies) also would be subject to income tax.

On the other hand, leaving your retirement benefits to a tax-exempt charitable organization achieves a double benefit since (i) your estate will receive a charitable deduction for federal estate tax purposes equal to the value of the retirement benefits distributable to the charitable organization, *and* (ii) there will be *no income tax* on the distribution of your retirement benefits to the tax-exempt charitable organization(s). Because of the tax-avoidance on the distribution of the retirement benefits to the charitable organization, implementing this strategy can maximize the distributions from your estate to both your charitable and non-charitable beneficiaries.

Many estate planning practitioners and plan participants have sought to obtain the same income tax-avoidance on retirement plan benefits *during the participants' lifetimes* by assigning the retirement benefits to a qualified charitable organization

or directing that distributions be made directly from their qualified plans or IRAs to qualified charitable organizations. However, the IRS has consistently held that such distributions were not tax-free distributions to the charitable organization, but instead were found to be income taxable to the plan participants or account owners.

But wait! For a limited time only, Congress has enacted a law which will allow *certain* distributions of *certain* retirement benefits owned by *certain* account owners to be distributed directly to *certain* charitable organizations without being included in the account owner's gross income. Under the Pension Protection Act of 2006, for distributions made in taxable years 2006 and 2007 only, "qualified charitable distributions" can satisfy the required minimum distribution rules while at the same time being excluded from taxable gross income of the account owner.

Who Will Benefit?

Simply stated, a "qualified charitable distribution" is a distribution (i) from an IRA (sorry, no distributions from qualified plans are included), (ii) that is owned by an individual who has already attained the age of 70-1/2 at the time of the distribution, (iii) made directly to a qualified public charity (excluding, however, any supporting organization or donor advised fund), and (iv) which would qualify for a charitable contribution deduction if made from non-retirement benefit assets. The maximum total amount of qualified charitable distributions that may be excluded from gross income in 2007 is \$100,000 per individual IRA owner. The qualified charitable distribution may be used as a direct gift to a qualified charitable organization or can be used to satisfy a charitable pledge. Lastly, the qualified charitable distribution is not deductible for federal income tax purposes as a charitable contribution, but also is not taken into account when determining the amount of charitable contributions that may be deducted by the taxpayer/account owner for the 2007 tax year.

As you may be able to discern from the specific requirements of a qualified charitable distribution, the benefits of this new law are very limited in their application. However, there are likely many of you who may be able to derive some benefit from this very limited duration opportunity. If you had planned to make a substantial charitable contribution to a public charity in 2007, or to satisfy in whole or in part a pledge to a public charity in 2007, are over the age of 70-1/2 years, and would otherwise have to take a required minimum distribution from your IRA, you should consider taking advantage of this law this year. Otherwise, you may want to consider contacting your Congressman to discuss the advisability of making this law a bit more permanent.

Naming a Trust as Your Designated Beneficiary

The rules governing the consequences of naming a trust as your designated beneficiary are ever changing and frequently subject to new interpretations by the Internal Revenue Service. The main issue in naming a trust as the designated beneficiary of your retirement benefits is that the IRS will look

"Leaving your retirement benefits to a tax-exempt charitable organization achieves a double benefit."

through the trust to the actual beneficiaries of your trust to determine the applicable distribution period (i.e., a 5-year distribution or payments over your remaining lifetime or over the lifetime of an individual beneficiary). Recent guidance issued by the IRS on this issue has indicated that unless all distributions made to a trust from a qualified plan or IRA account are required to be paid out to the current beneficiary of the trust, then *all possible beneficiaries* of the trust must be considered in determining the applicable distribution period.

The application of this new guidance can produce undesirable results. For example, if a charity is a beneficiary of your trust (even if that charity is a remote or contingent beneficiary), then the trust will be deemed to have no designated beneficiary and the payments to the trust will either have to be paid within 5 years of your death (if you had not begun taking your required minimum distributions) or over your remaining life expectancy. In addition, if estate administration expenses and/or estate taxes can or must be paid from retirement benefits, your estate will be deemed to be a beneficiary of your retirement benefits and again, the trust will be deemed to have *no designated beneficiary*. Lastly, the IRS will look to the oldest possible beneficiary of your trust to determine the life expectancy factor to use in calculating the required minimum distributions. Therefore, if your 90 year old great-aunt Nell is a possible remote contingent beneficiary of your trust (e.g., in the event all of your issue are deceased), then the IRS could use her life expectancy factor to determine the required minimum distributions from the qualified plan or IRA account.

Because of the new guidance and its accompanying unexpected and sometimes undesirable consequences, great care should be taken when designating a trust as a beneficiary of your retirement benefits.

Conclusion

Retirement benefits can be a great source of funds for you and your spouse during your golden years and, because of their tax-deferred nature, can be a great investment device. However, because of the income tax burden that each distribution from a retirement plan carries, and the varying benefits or detriments that accompany the designation of certain beneficiaries over others, retirement accounts can become quite a difficult asset to plan. To make the best use of your retirement benefits and avoid unnecessarily losing their tax-deferred nature, you should review your beneficiary designations periodically and consult your advisors to ensure that your designations will have the results you desire.

Laurelle Gutierrez-Lundquist, Esq. is a member of the Estate Planning Group and Valerie Menager, Esq. is a member of the Employment Law Area of our Corporate/Business Group.



THE LEASE WORK LETTER THE “KEY” TO A SUCCESSFUL LONG-TERM LANDLORD-TENANT RELATIONSHIP

By S. Kendall Patton, Esq.

Marriages and Commercial Leases have certain things in common. Both are entered into with high expectations and the desire by both parties for a satisfying and enduring long-term relationship. Unfortunately, a large number of both Marriages and Commercial Leases result in serious disagreements, breakups and, in some cases, legal proceedings within twelve months of “closing the deal.”

I will not attempt to deal with the myriad reasons for the early break-up of a marriage. That is a subject far too complex for a mere 1,500 words. Rather, this article addresses a safe, although not foolproof, way to avoid strife, disagreement and litigation during the first year of a Commercial Lease: a well crafted and comprehensive Lease Work Letter.

A “Lease Work Letter” is the construction agreement between Landlord and Tenant in a Commercial Lease transaction. A well-reasoned, well-drafted construction agreement addresses issues of timing and quality of construction of the following components of a commercial lease transaction:

- a) Base Building Work and Building Systems constructed by Landlord;
- b) construction of the Tenant Improvements (“TIs”) within the Premises by Tenant;
- c) the parties' respective obligations to pay for the TIs; and
- d) the impact of delays by Landlord and Tenant in fulfilling their respective construction obligations and hence, the actual Rent Commencement Date of the Lease and Tenant's obligation to commence paying Rent under the Lease.

The Work Letter discussed herein assumes the common situation where Tenant leases a concrete pad on which Landlord constructs the Base Building Work, comprising the Building in which the Premises are located, and the Building Systems which will service the Premises. Tenant needs the right to terminate the Lease for a failure by Landlord to timely complete the work.

Each issue set forth in the Work Letter will impact the nature and quality of the Building and the Premises leased by Tenant, the quality of TIs constructed by Tenant (and often funded in part by Landlord), and Lease Commencement/Rent Obligations.

The following is intended to be a brief yet informative summary of the components of a well-drafted Work Letter.

*“A safe way
to avoid strife,
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first year of a
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Lease Work
Letter.”*

Landlord's Obligation to Complete

All Base Building Work and Building Systems

- Tenant must specify its requirements/standards for the Base Building Work and Building Systems to be constructed by Landlord (wall and floor condition, HVAC requirements, electrical capacity, life safety systems and the like). Tenant's architect, contractor and engineer (if then retained by Tenant) should approve the same.

- The Base Building Work and Building Systems should be first-class and comply with all applicable laws and codes, including the Americans With Disabilities Act.

- Tenant should require “As-Built” CAD Drawings of all Base Building Work so that Tenant can both intelligently and efficiently build out its TIs.

- Landlord must “Substantially Complete” its Work and deliver the Building and Premises Substantially Complete to Tenant by a certain date (“Substantial Completion”). If Landlord is constructing both the Base Building Work and the TIs, “Substantial Completion” must include:

- a temporary or final certificate of occupancy which permits Tenant to occupy the Premises for Tenant's intended business purpose, subject only to correction by Landlord of minor “punch list” items;

- unfettered access to the Premises;

- the availability of all required utilities to be provided by Landlord under the Lease to the Premises; and

- Landlord's architect's certification that the Premises are “Substantially Complete.”

If Landlord is only constructing the Base Building Work and Building Systems, Landlord should satisfy the foregoing requirements except that the certificate of occupancy and Landlord's architect's certificate of substantial completion would relate only to the Base Building Work and Building Systems so that Tenant can commence and pursue its TIs to completion.

Tenant's Construction of Initial TIs

- A Commercial Lease generally gives Tenant a finite period of time (60-120 days) to complete its TIs before the Commencement Date occurs and the obligation to commence paying Rent begins.

- Tenant should attempt to negotiate a day-by-day extension of the Commencement Date (and additional per diem penalties if Landlord is at fault) if Tenant is delayed in completing its TIs because of Force Majeure Delays (Acts of God, unavailability of permits or materials or other causes beyond Tenant's reasonable control) and/or Landlord Delays in approving Tenant's plans and specifications for the TIs, unreasonable Landlord requirements or Landlord's default under the Lease. Creditworthy Tenants often negotiate “deemed approval” provisions (e.g., Landlord's failure to approve Tenant's plans and specifications within 10-15 business days after receipt by Landlord is deemed approval of such plans and specifications).

- Landlord should approve all plans and specifications for the TIs (reasonably withheld unless the TIs affect the Building Structure or Building Systems, in which event Landlord's approval can be given in its sole discretion). All TIs should be constructed in compliance with plans and specifications approved

by Landlord, in accordance with all applicable laws and codes and in a good and workmanlike manner.

- Landlord should have the right to reasonably approve Tenant's contractor and all subcontractors. Landlord may wish to designate the subcontractors and engineers whose work will affect the Building Structure or Building Systems. Contractors and subcontractors should provide evidence of appropriate liability insurance and worker's compensation insurance. If Tenant or its contractor is weak financially, then Landlord should require payment and performance bonds from Tenant.

- Whether or not Landlord is providing a TI Allowance (discussed below), Landlord must require conditional or unconditional waivers and releases of liens with respect to work supplied, installed, completed and paid for by Tenant. Waivers should be obtained from both the general contractor and from all subcontractors providing more than \$2,000 in services or materials - if the general contractor files bankruptcy, the subcontractors can still lien the Building and the Premises.

- Landlord should request a set of As-Built Drawings for all TIs within 90 days of completion of the TIs.

Tenant Improvement Allowance

- Landlords and Tenants often negotiate a Tenant Improvement Allowance ("TIA") to offset Tenant's initial costs of designing, engineering, permitting and constructing its TIs. In return, Tenant will pay higher Rent for the Premises. The TIA is usually computed on a rentable or useable square foot basis. On a large Lease, the TIA can often reach millions of dollars. If the TIA is large and Landlord is a single purpose entity, Tenant should require a guaranty of Landlord's obligation to fund the TIA from Landlord's parent entity or equity holders.

- The TIA is either disbursed in monthly progress payments (preferable to Tenants) or upon final completion of the TIs (preferable to Landlords). If a Landlord is funding the TIA from its Construction Loan Draws, Landlord (and its attorney) should be extremely sensitive to match the progress payment provisions under the Loan Agreement to monthly progress payment provisions under the Work Letter.

- If Landlord is funding only a portion of the cost of the TIs, Landlord may require Tenant to deposit into an escrow account the balance of construction funds and have funds disbursed proportionally with the TIA on a monthly basis. In the case of Construction Loan funding of the TIA, creditworthy Tenants should insist that the construction lender continue to fund the TIA in the event of a Landlord default under its Loan Agreement. This can be set forth in the lender's Subordination, Non-Disturbance and Attornment Agreement with Tenant.

- If monthly progress payments are being made, Landlord should at a minimum require that (1) the value of TI work completed (as certified by Tenant's architect) exceed the progress payment requested and (2) all applicable lien waivers and releases are received from all contractors and subcontractors.

"Each issue set forth in the Work Letter will impact the nature and quality of the Building and Premises."

- Final disbursement of the TIA Allowance should be conditioned upon the following:
 - Actual completion of all TI work as certified by Tenant's architect and agreed to by Landlord;
 - Landlord's receipt of lien waivers and releases from all contractors and subcontractors;
 - Tenant or its contractor has recorded a notice of completion and the time period for the filing of any liens by Tenant's contractor and subcontractors has expired without the filing of any liens; and
 - Tenant has obtained a certificate of occupancy for the Premises (including the TIs).

Impact of Delays and Tenants Obligation to Commence Paying Rent

- Tenant must be concerned about the timely completion of Landlord's Work. Tenant may have obligations to relocate under its then-existing and expiring lease, business or production constraints or severe holdover penalties under its existing lease (for instance, 200% of stated rent during any holdover period). If Landlord fails to Substantially Complete its Work within 30 to 60 days of the Anticipated Date of Substantial Completion, Tenant should have the right to terminate the Lease and recover any Rent or other sums previously paid by Tenant under the Lease. Tenant may also negotiate a per diem penalty payable by Landlord for late completion.

Carr McClellan's real estate attorneys bring together more than 120 years of collective experience in servicing their real estate clients. We combine construction law experience with leasing expertise on both the Landlord and Tenant sides to craft workable and protective Lease Work Letters. Please don't enter into a bad commercial relationship with your prospective Landlord or Tenant - call us first.

S. Kendall Patton is a member of the Real Estate Group.



NEW DISCOVERY RULES AFFECT YOUR COMPANY'S DATA MANAGEMENT SYSTEM

By W. George Wailes, Esq.

If your company has any electronically stored information – and what company doesn't? – you want to pay special attention to new Federal rules affecting your company's electronic data management system. You and your company risk sanctions and the possible loss of your claim or defense if you become involved in a lawsuit and do not have an information management system that can identify, preserve, and produce electronically stored information about a particular issue.

Identification, Preservation and Production of Electronic Data

The Federal Rules of Civil Procedure were revised in December 2006 to require identification, preservation, and production of electronically stored information, which has been added to the definition of "documents" in the rules. Electronically stored information includes emails, digital voicemails, instant messages, scanned documents, images, word processing documents, PDA data, CAD drawings, dictation, spreadsheets, and all other forms of electronically stored data.

These rules clarify what, up until now, has been a confusing area for companies: what does a company have to do when asked to produce its electronically stored information in a lawsuit? The clarification emphasizes the need to implement data management systems now that will allow you to identify and stop the destruction of data if you become involved in a lawsuit.

Under the new rules, at the early stages of a Federal lawsuit parties must provide a description of their electronically stored information and discuss discovery of the information. In other words, parties must describe how the company will produce the information to the opposing party. The required description includes (1) the format in which the data is stored, (2) what efforts have been made to preserve relevant data during the lawsuit, (3) how the data can be searched, and (4) how the data can be copied and produced. Parties can now be required to produce electronically stored information in its *native format* together with all metadata. Metadata includes information about the author, date drafted, revisions, revisers, dates of revisions, when the document was sent or copied, and much more.

Improper Handling of Electronic Data

Why are these changes to the Federal discovery rules important to businesses that are not currently involved in Federal litigation? They are important because of the sweeping nature of the preservation

"At the early stages of a Federal lawsuit parties must provide a description of their electronically stored information and discuss discovery of the information."

and production requirements and the risk of severe sanctions. Potential sanctions include the loss of the company's claim or defense if the company does not have systems that can isolate and preserve from normal deletion electronically stored information relevant to a dispute, as soon as the company learns of the claim against it. In other words, companies need to adopt electronically stored information storage systems that comply with the new rules now to avoid sanctions when and if the companies become involved in litigation.

There are many examples of the risk of improper handling of electronically stored information after notice of a lawsuit. One defendant was fined \$29 million for deleting electronically stored information after notice of a lawsuit. Another company was fined \$2.75 million for continuing to delete emails following a court order to preserve the information. A jury awarded \$1.45 billion against Morgan Stanley after the judge told the jury they could imply an adverse inference from Morgan Stanley's failure to disclose the existence of backup tapes and a script error in a search program.

Safe Harbor Provision

On the positive side, the new rules set up a safe harbor for companies that have electronic information storage systems that allow them to remove from their normal data deletion process electronically stored information that is relevant to the lawsuit. In addition, the new rules provide that a company does not have to produce electronically stored information that is not reasonably accessible because of the burden or cost. The company still must identify all potentially relevant sources of electronically stored information and explain when information is not being provided because of this burden or cost. The company however has the responsibility of proving that the burden of obtaining the information outweighs the benefit to the adverse party.

A company will not be sanctioned for data lost "as a result of the routine, good-faith operation of an electronic information system." Again, the rule requires companies to adopt an information storage system that preserves relevant information, and the company must immediately stop deletion of relevant electronic information promptly upon notice of a lawsuit.

What Your Company Should Do

Take this issue seriously, especially in light of the risks of not having a system in place that complies with the new rules when you are next involved in a lawsuit. Perform a compliance audit, just as you would for any other regulatory requirement. As you review your systems for organizing and storing electronically stored information, consider implementing a new system designed to comply with these new discovery rules. Ensure that your systems consultant has a working familiarity with the rules and that the consultant confirms that any new system meets the new requirements. Whether or not you implement a new system, ensure that your electronically stored information is maintained in a way that allows it to see *NEW FEDERAL RULES, page 8*



2007 EMPLOYMENT LAW UPDATE

By Valerie Menager, Esq.

The beginning of the year is the ideal time to review your company's Human Resource policies and procedures. Changes in employment laws for 2007, if ignored, could have a dramatic effect on your business' bottom line.

Minimum Wage Impacts Exempt Workers and Exempt Inside Sales Employees

Even if your company has no non-exempt minimum wage employees, the recent increase to California's minimum wage from \$6.75 to \$7.50 per hour in 2007, and \$8.00 per hour in 2008, will directly affect who qualifies as an exempt employee. California law requires exempt employees to be paid a minimum salary of two times the state minimum wage. The increase in the minimum wage will result in an increase in the minimum annual salary for exempt employees from \$28,080 to \$31,200 in 2007, and \$33,280 in 2008.

Your company should conduct a salary review to ensure that the change in California minimum wage laws in 2007 will not convert your exempt and commissioned inside sales employees to non-exempt employees eligible for overtime. Commissioned inside sales employees in many industries who earn more than half their income in commission are exempt from overtime as long as their salary exceeds one and one-half times the minimum wage. The increase in California's minimum wage could result in some inside sales employees becoming eligible for overtime pay. Effective January 1, 2007, commissioned inside sales employees must earn a minimum of \$11.25 per hour or they may be entitled to overtime.

Computer Professionals & Medical Professionals – Are they still exempt?

For 2007, the minimum hourly rate for exempt licensed physicians and surgeons is \$64.18 and the minimum hourly rate for exempt computer professionals is \$49.77. If your company employs computer technology professionals and/or medical professionals who earn less, they cannot be treated as exempt employees and consequently are subject to the applicable wage and hour laws. You should review your company policies and procedures to confirm compliance with these requirements.

2007 Employment Posters

Don't forget to replace your employment posters for 2007! The California Minimum Wage notice and Industrial Welfare Commission (IWC) Wage Orders must be posted in the workplace. You can download these posters for free at: www.dir.ca.gov/iwc/Minwage2007.pdf.

“The recent increase of California's minimum wage... will directly affect who qualifies as an exempt employee.”

Sexual Harassment Prevention Training

California law mandates that all supervisors at companies with more than 50 employees receive sexual harassment prevention training. The law also requires that supervisors receive this training every two years and that employees promoted or hired into supervisory positions receive training within six months of their start date.

What Employers & Supervisors are Covered?

Previously it was unclear whether or not this law required the training of supervisors located out of state for a California based company. A.B. 2095 now specifies that an employer need train only those supervisors who are located in California. This legislation also clarifies that all employees of a company must be counted whether they are in the State of California or not in determining if an employer meets the 50-employee threshold for mandated training.

How do you Track Compliance? Employers have two options for tracking compliance with the two year training requirement. The first option is an “individual tracking” method in which the employer must train an individual supervisor two years from the completion date of the supervisor's last training. The second option is a “training year” tracking method. This allows the employer to designate a training year in which all supervisors will be trained. Retraining will be required by the end of the following two year period.

Subject Matter Experts Must Answer Questions.

New law also indicates that while supervisors may be trained by viewing online materials, questions that arise during training can only be answered by “subject matter experts.” Is your company fulfilling these mandatory requirements? Does your current training program reflect the changes in the law?

Driving while Using a Wireless Telephone

As of July 1, 2008 it will be illegal to drive a motor vehicle while using a wireless telephone. Your company should change its policies now and begin educating employees on the new law in order to limit company exposure when this law goes into effect.

Could Your Arbitration Policy be Expanded into an Employee Class Action?

Recent California Appellate Court precedent has held that an arbitrator may hear a dispute as a “class action” as long as the arbitration policy does not specifically exclude class actions. Your company should review its arbitration policy to determine whether such a prohibition against class actions is appropriate for your company.

Mandated Sick Leave Pay for San Francisco Employers

California and federal laws do not require employers to provide sick leave pay, but as of February 5, 2007 all employers located in the city and county of San Francisco must provide one hour of paid sick leave for every 30 hours worked by an employee capped at 72 hours (or 40 hours for employers with fewer than 10 employees) pursuant to municipal law. This ordinance is the first of its kind see 2007 EMPLOYMENT LAW UPDATE, page 8

be sorted by topics and names. Make certain your system allows you to identify and preserve relevant data in a lawsuit, hopefully in a simple way, rather than a time and labor-intensive process.

Map out where and how electronic information is stored, including email servers, back up tapes, "deleted" data, home computers, PDAs, and data stored at other locations.

Make sure your records retention policy includes and covers all electronically stored information. This should ensure that relevant emails, instant messages, facsimiles, and other data are retained while the vast majority of data, which need not be preserved, is purged on a regular basis. If you are involved in a lawsuit, procedures should be in place before any litigation begins to prevent the loss of relevant electronic information, such as information stored on back up tapes that is normally overwritten.

The changes to the Federal rules were an attempt to clarify what has been a confusing area of the law. Unfortunately, for most companies that do not have new electronically stored data management systems in place, the new rules impose significant burdens to identify, preserve, and produce all electronically stored information relevant to the dispute when involved in a lawsuit. State courts will likely follow with similar rules in the near future, which will increase the urgency for even the smallest companies to upgrade their systems. Consult with a systems management expert or an attorney soon to ensure that your company is not harmed or sanctioned because of the way it stores electronic data when or if it becomes involved in a lawsuit.

W. George Wailes is a member of the Litigation Group.

in the nation, and may lead to similar legislation in other jurisdictions. The new ordinance covers all workers including part-time, temporary, and Welfare-to-Work programs within San Francisco city and county limits.

Employers with existing paid sick leave policies are not required to offer additional paid sick leave to comply with the new ordinance, as long as the existing company policy provides the minimum leave benefits required under the new law. Employees may use the paid sick leave for their own illness or injury as well as to care for an ill or injured child, parent, sibling, grandparent, grandchild, legal guardian or ward, spouse or registered domestic partner or child of a domestic partner. An employee who does not have a spouse or domestic partner may designate another person for whose illness they may use their paid sick leave.

Violations of the mandated sick pay leave ordinance carry a penalty for the amount of paid sick leave illegally withheld, plus three times the paid sick leave or \$250, which ever is greater.

As you begin 2007, please take a few moments to evaluate how these changes in employment law may affect your company. Ignoring these important changes in employment law could result in costly litigation for your business.

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