Study K-410 June 21, 1999

First Supplement to Memorandum 99-23

Confidentiality of Settlement Negotiations: Comments on Draft of Recommendation

The Commission has received a number of new letters on the staff draft recommendation attached to Memorandum 99-23, concerning the admissibility, discoverability, and confidentiality of settlement negotiations. Most of these letters concern the definition of "settlement negotiations" in proposed Evidence Code Section 1130. A letter from Judge Chavez (Presiding Judge, Los Angeles Superior Court) comments on proposed Evidence Code Section 1137 (cause of action, defense, or other legal claim arising from conduct during settlement negotiations). This supplement analyzes the comments on these two provisions.

The following letters are attached as Exhibits (two letters by Commission staff are included for purposes of context):

PROPOSED SECTION 1130. DEFINITIONS

Proposed Section 1130 provides:

> 1130. As used in this chapter:
> (a) "Evidence of settlement negotiations" includes but is not limited to a settlement agreement.
> (b) "Settlement negotiations" means any of the following:

> (1) Furnishing, offering, or promising to furnish, a valuable consideration in compromising or attempting to compromise a disputed claim.
>
> (2) Accepting, offering to accept, or promising to accept, a valuable consideration in compromising or attempting to compromise a disputed claim.
>
> (3) Conduct or statements made for the purpose of or in the course of compromising or attempting to compromise a disputed claim, regardless of whether a settlement is reached or an offer of compromise is made.

Duane Shinnick of Silldorf, Shinnick & Duignan, LLP, comments that this provision "contains in our opinion too broad a definition of 'settlement negotiations.'" (Exhibit p. 2.) He explains that it "would potentially make inadmissible evidence of residential construction repairs by the developer or subcontractors, if such companies conducted such repairs with an eye towards compromising a homeowner's potential construction defect claim." (*Id.*) He points out that such repairs have traditionally been admissible for a number of purposes, and cautions that as "the section now stands, a contractor could simply years later declare that it intended its promises of repairs or even its repairs to be settlement negotiations, thus making inadmissible the very heart of the evidence of lulling or estoppel to toll statutes of limitations." (*Id.* at 2-3.)

These concerns are very similar to ones previously raised by another construction defect attorney, Douglas Grinnell of Epsten & Grinnell, which the Commission already attempted to address in a number of ways. Commission staff brought this to Mr. Shinnick's attention, and requested input from both Mr. Shinnick and Mr. Grinnell on whether the revisions the Commission had made in response to Mr. Grinnell's concerns were sufficient to address the situation. (Exhibit pp. 4-5.)

Mr. Shinnick (Exhibit p. 6) and Mr. Grinnell (Exhibit pp. 7-8) both replied that those revisions were not sufficient. As Mr. Shinnick wrote, "it is apparent that evidence which has traditionally been not only relevant but also crucial to the successful prosecution of cases on behalf of homeowners would likely be barred by the proposed statute." (Exhibit p. 6.) Both he and Mr. Grinnell suggested approaching "the matter from the other direction and [stating] that comments made or actions taken during settlement negotiations are not admissible as an admission of liability, but are admissible for any other relevant purpose." (Exhibit p. 6; *see also id.* at 7.)

The staff responded by pointing out that Evidence Code Sections 1152 and 1154 follow that approach, but do not explicitly state that evidence of settlement negotiations is admissible for purposes other than proving liability. (Exhibit p. 9.) The staff drew attention to the portion of the draft recommendation criticizing the current approach on a number of grounds. (*Id.*) We then suggested several means of addressing the concerns raised by Messrs. Shinnick and Grinnell regarding prelitigation conduct in construction defect cases, and solicited their input on the relative merits of these options. (*Id.* at 9-10.)

Mr. Shinnick (Exhibit p. 11) replied by expressing support for the first option suggested by the staff: Limiting the Commission's proposed new rules on admissibility, discoverability, and confidentiality to settlement negotiations occurring after a lawsuit has been filed. The current approach would continue to apply to prelitigation negotiations. This could include an express statutory provision that evidence of prelitigation negotiations is inadmissible on the issue of liability, but admissible for other purposes. (*Id.* at 9.)

As Mr. Shinnick observes, this solution "has the advantage of being a 'bright line' rule." (*Id.* at 11.) He requested input on it from Mr. Grinnell and from Nancy Peverini of the Consumer Attorneys of California ("CAOC"). (*Id.*) As yet, however, we have not received such input.

The staff concurs in Mr. Shinnick's assessment that differentiating between prelitigation and post-litigation negotiations is the best alternative, because it would establish a bright line rule. The other approaches suggested by the staff would entail line-drawing problems or other difficulties. (See *id.* at 10.) The Commission has struggled to define the degree of dispute necessary to trigger its proposed new provisions on admissibility, discoverability, and confidentiality of settlement negotiations. (See Memorandum 99-4, pp. 1-8.) Restricting the new provisions to post-litigation negotiations would eliminate this problem. It may not facilitate settlement negotiations as much as may ultimately be desirable, but it would still be a major step forward, encouraging frank communications that would promote mutually beneficial settlements and reduce court congestion.

Revising the Commission's proposal to implement this approach would require considerable tinkering. Rather than trying to settle on precise language at this point, **the staff would prepare a new draft along these lines for the Commission's next meeting**. This would afford additional opportunity for comment before the Commission finalizes its recommendation, particularly if the staff sends out the draft well before the meeting.

SECTION 1137. CAUSE OF ACTION, DEFENSE, OR OTHER LEGAL CLAIM ARISING FROM CONDUCT DURING SETTLEMENT NEGOTIATIONS

Article 2 of the draft recommendation (proposed Evidence Code Sections 1132-1134) sets forth general rules governing the admissibility, discoverability, and confidentiality of evidence of settlement negotiations. Proposed Section 1137 is one of a number of exceptions to these general rules. It provides:

> **§ 1137. Cause of action, defense, or other legal claim arising from conduct during settlement negotiations**
>
> 1137. Article 2 (commencing with Section 1132) does not apply where a settlement agreement or other evidence of settlement negotiations is introduced or relevant to support or rebut a cause of action, defense, or other legal claim arising from conduct during the negotiations, including a statute of limitations defense.
>
> **Comment.** Section 1137 recognizes that the public policy favoring settlement agreements has limited force with regard to settlement agreements and offers that derive from or involve illegality or other misconduct. See D. Leonard, The New Wigmore: A Treatise on Evidence, *Selected Rules of Limited Admissibility* § 3.7.4, at 3:98-1 (1999) ("If the primary purpose of the exclusionary rule is to encourage parties to reach compromise and thus avoid protracted litigation, it follows that the rule should not apply to situations in which the compromise the parties have reached, or have sought to reach, is illegal or otherwise offends some aspect of public policy."). For example, evidence of sexual harassment during settlement negotiations should be admissible in an action for damages due to the harassment. Similarly, evidence of a low settlement offer should be admissible to establish an insurer's bad faith in first party bad faith insurance litigation. *See, e.g.*, White v. Western Title Ins. Co., 40 Cal. 3d 870, 887, 710 P.2d 309, 221 Cal. Rptr. 509 (1985). Likewise, where efforts to repair defective construction constitute settlement negotiations covered by this chapter, evidence of any harm resulting from those efforts would nonetheless be admissible pursuant to this section.
>
> Evidence admitted pursuant to Section 1137 may only be used for the purposes specified in the provision. A limiting instruction may be appropriate. See Section 355.
>
> See Section 1130 (definitions). See also Section 1131 (application of chapter).

Judge Chavez (Presiding Judge, Los Angeles County Superior Court) is "in general agreement" with the Commission's proposal, but Section 1137 does give him "some difficulty." (Exhibit p. 1.) He explains:

> Comments to this section indicate that the purpose of this section is to make clear that settlement agreements and negotiations which are in themselves illegal or negotiations during which illegal conduct occurred are not included within the general exclusionary rules of Section 1132. My problem with the proposed section is that in my view the language utilized is insufficient to accomplish that purpose.

(*Id.*) He suggests revising Section 1137 to read:

> 1137. Article 2 (commencing with Section 1132) does not apply where:
>
> (a) A cause of action, defense, or other claim is sought to be supported or rebutted by a settlement agreement that derives from or involves illegal conduct.
>
> (b) A cause of action, defense, or other claim is sought to be supported or rebutted by evidence of illegal or other misconduct occurring during the settlement negotiations.

(*Id.*)

Judge Chavez's comments are perceptive. Although Section 1137 is primarily intended to focus on illegality or other misconduct occurring during settlement negotiations, that focus is not immediately apparent from the proposed statutory language. The language has, however, survived quite a number of drafts (with slight modifications), and has held up well in considering numerous hypotheticals. It was chosen after other language proved unsatisfactory. (See Memorandum 98-14, attachment pp. 14-16; Minutes, March 19-20, 1998, p. 13.) The staff is hesitant to change it at this point, particularly because Judge Chavez's proposed alternative does not seem broad enough to cover a statute of limitations defense arising from conduct during settlement negotiations, a point that was specifically raised as a concern. (See Memorandum 99-4, attachment pp. 31-32; Minutes, Feb. 4-5, 1999, p. 11.) Accordingly, **we would leave the provision as is, but encourage interested parties to comment on Judge Chavez's suggested alternative.**

Respectfully submitted,

Barbara S. Gaal
Staff Counsel

The Superior Court
LOS ANGELES, CALIFORNIA 90012
CHAMBERS OF
VICTOR E. CHÁVEZ
PRESIDING JUDGE

TELEPHONE
(213) 974-5600

April 23, 1999

Law Revision Commission
RECEIVED
APR 28 1999
File: K-410

Ms. Barbara S. Gaal
Staff Counsel
California Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, California 94303-4739

Re: Law Revision Commission Study on Admissibility Discoverability, and Confidentiality of Settlement Negotiations

Dear Ms. Gaal:

I am in general agreement with the proposed statutory amendments and I believe for the reasons stated, by the Commission, are most appropriate.

The section which does give me some difficulty is 1137. Comments to this section indicate that the purpose of this section is to make it clear that settlement agreements and negotiations which are in themselves illegal or negotiations during which illegal conduct occurred are not included within the general exclusionary rules of Section 1132. My problem with the proposed section is that in my view the language utilized is insufficient to accomplish that purpose.

I would appreciate it if you would consider a revision as follows:

"Article II (commencing with Section 1132) does not apply where:
(a) a cause of action, defense or other claim is sought to be supported or rebutted by a settlement agreement that derives from or involves legal conduct.
(b) a cause of action, defense or other claim is sought to be supported or rebutted by evidence of illegal or other misconduct occurring during the settlement negotiations.

Very truly yours,

Victor E. Chávez
Presiding Judge

VEC:gp

SILLDORF, SHINNICK & DUIGNAN, LLP

HOWARD J. SILLDORF
DUANE E. SHINNICK
LAWRENCE D. DUIGNAN

THERESA M. FILICIA
KIMBERLY J. WIND *
ERIK R. BASIL
LUKE P. RYAN
FRANKLIN C. AGHASSI
* ALSO ADMITTED TO THE NEVADA BAR

ATTORNEYS AT LAW
1810 STATE STREET
SAN DIEGO, CALIFORNIA 92101-2539

(619) 239-5900/FAX (619) 239-1833
(800) 253-9741/ www.ssdlaw.net

IRVINE:
(949) 752-5676/FAX (949) 752-0923

GOLDBERG & GAGE
(818) 340-9252/FAX (818) 340-9088

OF COUNSEL: MADDOX & ASSOCIATES
(702) 366-1900/FAX (702) 366-1999

REPLY TO FILE

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April 13, 1999

Arthur K. Marshall, Chairperson
California Law Revision Commission
4000 Middlefield Rd., Room D-1
Palo Alto, CA 94303-3739

Re: Study K-410/Memorandum 99-23/Draft version of Evidence Code 1130

Dear Chairperson Marshall:

The proposed Evidence Code section 1130, which makes inadmissible evidence of "settlement negotiations", contains in our opinion too broad a definition of "settlement negotiations." The proposed version would potentially make inadmissible evidence of residential construction repairs by the developer or subcontractors, if such companies conducted such repairs with an eye towards compromising a homeowner's potential construction defect claim.

Such repairs have traditionally been admissible to toll statutes of limitations under the theories of lulling and estoppel. (See, e.g., Cascade Gardens Homeowners Association v. McKellar & Associates, (1987) 194 Cal.App.3d 1252) Such repairs have also traditionally been admissible to determine whether a defect was a latent or patent defect if repairs did indeed not fix the problem. (See, e.g., Baker v. Walker & Walker, Inc. (1982) 133 Cal.App.3d 746, 758-760.) Such repairs have also traditionally been admissible to determine whether similar proposed repairs are adequate if the past, similar repairs did not correct the problem.

While genuine settlement negotiations can be protected either by a specific letter or by a document, conduct which is clearly relevant to estoppel, tolling of statutes of limitations, latency or patency of a defect, adequacy of repairs, or the like should not be discarded. At a minimum, written notice to the offeree that some proposed conduct constitutes settlement negotiations and would be inadmissible in any future proceedings should be required. As the section now stands, a contractor could simply years later declare that it intended its promises of repairs or even its repairs to be settlement negotiations, thus making

inadmissible the very heart of the evidence of lulling or estoppel to toll statutes of limitations. Surely this is not what the Commission intends.

Sincerely,

SILLDORF, SHINNICK & DUIGNAN, LLP

Duane E. Shinnick
Attorney At Law

DES:jav

STATE OF CALIFORNIA
CALIFORNIA LAW REVISION COMMISSION
4000 MIDDLEFIELD ROAD, ROOM D-1
PALO ALTO, CA 94303-4739
650-494-1335

April 19, 1999

Duane E. Shinnick
Silldorf, Shinnick & Duignan
1810 State Street
San Diego, CA 92101-2359

Re: Law Revision Commission Study on Admissibility, Discoverability, and Confidentiality of Settlement Negotiations

Dear Mr. Shinnick:

Thank you very much for your letter dated April 13, 1999, expressing your concerns about the breadth of proposed Evidence Code Section 1130 in the Law Revision Commission's proposal on admissibility, discoverability, and confidentiality of settlement negotiations. The Commission will consider your letter at its next meeting, which is scheduled for June 24-25, 1999, in Sacramento. Your letter will be attached to and discussed in a memorandum that we will circulate to the Commission and other interested persons before the meeting. We will send you a copy of the memorandum when it is ready.

The issues you raise in your letter are similar if not identical to ones raised by Douglas Grinnell of Epsten & Grinnell in a letter to the Commission dated July 28, 1998. A copy of that letter and an excerpt from a staff memorandum discussing it (Memorandum 98-62, pp. 8-15) are enclosed for your reference, along with a second letter we received from Mr. Grinnell and another excerpt from a staff memorandum (Memorandum 99-4, pp. 1-8). We are very interested to know your reaction to these materials. Are the revisions the Commission made in response to Mr. Grinnell's letters sufficient to address the construction defect situation, or are further revisions necessary? If the latter, what specific revisions do you suggest?

It would be very helpful to know your thoughts on these matters by mid-May, so that we can incorporate them in the memorandum for the Commission's June meeting. I am also sending Mr. Grinnell a copy of your letter, so that he can consider it and share his thoughts. I hope that if all three of us think constructively about the issues, we can come to consensus on a workable approach to propose to the Commission.

Fax: 650-494-1827 Website: http://www.clrc.ca.gov Email: bgaal@clrc.ca.gov

Once again, thank you for taking the time to review and comment on the Commission's proposal. Participation by informed persons such as yourself is crucial in our process of developing proposals to improve California law.

Sincerely,

Barbara S. Gaal
Staff Counsel

cc (w/enc.): Douglas Grinnell
Nancy Peverini (CAOC)

File: K-410
Enc.

SILLDORF SHINNICK AND DUIGNAN
LLP, Attorneys at Law

1810 State Street, San Diego, California 92101-2539
(619) 239-5900
(800) 253-9741
(619) 239-1833
www.ssdlaw.net
Member of CAI and CACM

April 22, 1999

Arthur K. Marshall, Chairperson
California Law Revision Commission
4000 Middlefield Rd., Room D-1
Palo Alto, CA 94303-3739

Re: Study K-410/Memorandum 99-23/Draft version of Evidence Code 1130

Dear Chairperson Marshall:

Thank you for your letter of April 19, 1999. I do not believe the various problems I previously mentioned are addressed in the proposed revisions to the statute, nor do I think I know every exception or reason that words or actions might otherwise be admissible even though they might fit within the definition of "settlement negotiations" in the proposed statute.

Perhaps it would be simpler to approach the matter from the other direction and to state that comments made or actions taken during settlement negotiations are not admissible as an admission of liability, but are admissible for any other relevant purpose.

I am sorry I do not have more time to devote to this topic now, but it is apparent that evidence which has traditionally been not only relevant but also crucial to the successful prosecution of cases on behalf of homeowners would likely be barred by the proposed statute.

Sincerely,

SILLDORF, SHINNICK & DUIGNAN, LLP

Duane Shinnick

Duane E. Shinnick
Attorney At Law

DES:jav

cc: Douglas W. Grinnell, Esq.
Nancy Peverini, CAOC

EPSTEN & GRINNELL APC
ATTORNEYS SERVING COMMUNITY ASSOCIATIONS™

555 West Beech Street, Suite 500 Tel 619.239.1704
San Diego, California 92101-2995 Tel 800.300.1704
epstenandgrinnell.com Fax 619.239.0403

ATTORNEYS AT LAW
Jon H. Epsten
Douglas W. Grinnell
James F. Darrow
Mary M. Howell
Thomas S. Gatlin
Susan Hawks McCuntic
Shiana L. Ballmer
J.W. Hansen
Deborah M. Zumwalt
Kieran J. Purcell
Antonina C. LoCoco
Luis L. Ventura
Vincent J. Sroček

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Rancho Bernardo
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April 26, 1999

Law Revision Commission
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MAY - 3 1999

File: K-410

Barbara Gaal, Staff Counsel
CALIFORNIA LAW REVISION COMMISSION
4000 Middlefield Road, Room D-1
Palo Alto, California 94303-4739

Dear Ms. Gaal:

Thank you for your letter of April 19, 1999. I enclose attorney Duane Shinnick's letter to Arthur Marshall, with which I agree.

I tend to believe that "settlement negotiations" (as broadly defined by the present proposal) should be statutorily inadmissible to prove a party's admission of liability, but that an explicit caveat needs to be inserted into the text of the statute itself which provides that the statute does not render inadmissible "negotiations" if they are relevant for some purpose other than to prove a party's admission. In conjunction with Evidence Code section 351, the trial court could make the call on an issue by issue basis.

Absolute inadmissibility of "settlement negotiations" is something to which we strongly object, particularly given the breadth of the definition of "negotiations." Perhaps the definition could be narrowed to specific settings. Thank you for your consideration of this matter.

Sincerely,

EPSTEN & GRINNELL, APC

Douglas W. Grinnell

DWG:dlr

Enclosure

cc: Nancy Paverini, CAOC
Duane Shinnick

SILLDORF
SHINNICK
AND
DUIGNAN
LLP, Attorneys at Law

1810 State Street, San Diego, California 92101-2539
(619) 239-5900
(800) 253-9741
(619) 239-1833
www.ssdlaw.net
Member of CAI and CACM

April 22, 1999

Arthur K. Marshall, Chairperson
California Law Revision Commission
4000 Middlefield Rd., Room D-1
Palo Alto, CA 94303-3739

Re: Study K-410/Memorandum 99-23/Draft version of Evidence Code 1130

Dear Chairperson Marshall:

Thank you for your letter of April 19, 1999. I do not believe the various problems I previously mentioned are addressed in the proposed revisions to the statute, nor do I think I know every exception or reason that words or actions might otherwise be admissible even though they might fit within the definition of "settlement negotiations" in the proposed statute.

Perhaps it would be simpler to approach the matter from the other direction and to state that comments made or actions taken during settlement negotiations are not admissible as an admission of liability, but are admissible for any other relevant purpose.

I am sorry I do not have more time to devote to this topic now, but it is apparent that evidence which has traditionally been not only relevant but also crucial to the successful prosecution of cases on behalf of homeowners would likely be barred by the proposed statute.

Sincerely,

SILLDORF, SHINNICK & DUIGNAN, LLP

Duane E. Shinnick
Attorney At Law

DES:jav

cc: Douglas W. Grinnell, Esq.
Nancy Peverini, CAOC

STATE OF CALIFORNIA
CALIFORNIA LAW REVISION COMMISSION
4000 MIDDLEFIELD ROAD, ROOM D-1
PALO ALTO, CA 94303-4739
650-494-1335

May 20, 1999

Douglas W. Grinnell
Epsten & Grinnell
555 West Beach Street, Suite 500
San Diego, CA 92101-2995

Duane E. Shinnick
Silldorf, Shinnick & Duignan
1810 State Street
San Diego, CA 92101-2359

Re: Law Revision Commission Study on Admissibility, Discoverability, and Confidentiality of Settlement Negotiations

Gentlemen:

Thank you both for responding to the letters I sent you on April 19, 1999. I am trying to figure out the best way to accommodate your concerns, so I seek your advice on a number of possible approaches.

In your responses, each of you mentions the possibility of making evidence of settlement negotiations inadmissible for purposes of proving and disproving liability, but not for other purposes. As you know, Evidence Code Sections 1152 and 1154 follow that approach, but do not explicitly state (as Mr. Grinnell proposes) that evidence of settlement negotiations is admissible for purposes other than proving liability. That prong of the doctrine is clear from judicial decisions interpreting the provisions. See, e.g., White v. Western Title Ins. Co., 40 Cal. 3d 870, 889, 710 P.2d 309, 221 Cal. Rptr. 509 (1985) (purpose of Section 1152 is "to bar the introduction into evidence of an offer to compromise a claim for the purpose of proving liability for that claim, but to permit its introduction to prove some other matter at issue."); Lemer v. Boise Cascade, Inc., 107 Cal. App. 3d 1, 9, 165 Cal. Rptr. 555 (1980) (Section 1154 "has no application where the evidence is not tendered as an admission of weakness by the party who settled or offered to settle, but for some other purpose.").

As set forth at pages 7-9 of the draft attached to Memorandum 99-23, the current approach to evidence of settlement negotiations can be criticized on a number of grounds. A major problem is that evidence of settlement negotiations tends to be prejudicial as to liability, even if it is not introduced for that purpose and a limiting instruction is used.

The Commission does not propose to replace the current approach with a rule of absolute inadmissibility (which Mr. Grinnell strongly opposes), but rather with a general rule of inadmissibility, subject to various exceptions. In light of the concerns both of you have raised regarding pre-litigation conduct in construction defect cases, the following alternatives have occurred to me:

Fax: 650-494-1827 Website: http://www.clrc.ca.gov Email: bgaat@clrc.ca.gov

(1) Limiting the proposed new rule to settlement negotiations occurring after a lawsuit has been filed. Continuing to apply the current approach to prelitigation negotiations. This could include an express statutory provision that evidence of prelitigation negotiations is inadmissible on the issue of liability, but admissible for other purposes.

(2) Making the proposed new rule inapplicable to construction defect cases. Continuing to apply the current approach to such cases.

(3) Applying the proposed new rule only where the parties affirmatively elect to apply the rule to their negotiations. Continuing to apply the current approach to other negotiations. (Based on input previously received, I am not optimistic about the prospects for this option.)

(4) Applying the proposed new rule to settlement offers and settlement discussions, but not to settlement-related conduct. Continuing to apply the current approach to settlement-related conduct. (This approach may entail some difficult distinctions.)

(5) Making evidence of a settlement offer absolutely inadmissible. Continuing to apply the current approach to other evidence of settlement negotiations. See Gov't Code § 11415.60. (This option would not do much to alleviate the Commission's concerns regarding the current approach.)

At this point, I do not know which, if any, of these options would be of interest to the Commission. I would much appreciate hearing your thoughts on their relative merits, or any other ideas you may have. Please feel free to call me or send an e-mail message (bgaal@clrc.ca.gov) if it is easiest to express your thoughts in that manner.

Thank you very much for your courtesy and attention.

Sincerely,

Barbara Gaal

Barbara S. Gaal
Staff Counsel

cc: Nancy Peverini (CAOC)
File: K-410

SILLDORF SHINNICK AND DUIGNAN
LLP, Attorneys at Law

1810 State Street, San Diego, California 92101-2539
Telephone: (619) 239-5900
Toll Free: (800) 253-9741
Facsimile: (619) 239-1833
Web Site: www.ssdlaw.net
Member of CAI and CACM

May 25, 1999

Barbara S. Gaal, Staff Counsel
California Law Revision Commission
4000 Middlefield Rd., Room D-1
Palo Alto, CA 94303-3739

Re: Study K-410/Memorandum 99-23/Draft version of Evidence Code 1130

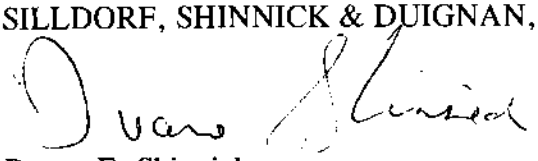
Dear Ms. Gaal:

Thank you for your letter of May 20, 1999, which contains five suggested approaches to the issue of admissibility of settlement negotiations. Based in part on your comments about other concerns and other problems, it may be that alternative (1), limiting the change in law to post-filing negotiations, is the only practical solution. It has the advantage of being a "bright line" rule. By copy of this letter, I am informing Mr. Grinnell and Ms. Peverini of this first reaction and would request their comments if there are disagreements about the meaning or impact of alternative (1).

Thank you for your prompt responses.

Sincerely,

SILLDORF, SHINNICK & DUIGNAN, LLP



Duane E. Shinnick
Attorney At Law

DES:jav

cc: Douglas W. Grinnell, Esq.
Nancy Peverini, CAOC