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Trial Notebook

Verdict against game maker reversed because of faulty jury instructions



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In cases where the profits generated by an intentional tort exceed the amount of harm sustained by the plaintiff, restitution provides an important alternative to the traditional remedy of damages.

Reversing the verdict in a commercial bribery case — because of botched jury instructions on the Illinois defenses of ratification and “in pari delicto” — the 7th U.S. Circuit Court of Appeals remanded the case in an opinion with useful hints and guidelines for using the alternative remedy of restitution. *Williams Electronics Games Inc. v. Garrity*, 2004 WL 909162 (April 29).

Williams Electronics, manufacturer of the popular “Mortal Kombat” video game, filed a lawsuit alleging that two of its suppliers — Arrow and Milgray Electronics Inc. — paid more than \$100,000 in cash bribes to one of its buyers, Greg Barry, in return for ordering more than \$100 million in components over a four-year period. One of the defendants, an Arrow employee named James M. Garrity, allegedly paid \$78,000 in bribes to Barry.

Williams permitted its employees to accept Christmas gifts but allegedly not buyers like Barry. At trial, Arrow and Milgray argued that Williams ratified Barry’s conduct and that Williams was in pari delicto. Meanwhile, Milgray filed a counterclaim for fraud against Williams, claiming it was

harmful when Williams purchased components from a company set up by two of Milgray’s employees, Lawrence J. Gnat and Richard S. Slupik.

This article, the first of two on this case, focuses on Judge Richard A. Posner’s analysis of errors in the jury instructions. Wednesday’s Trial Notebook will look at the restitution issues. Here are some highlights of Posner’s discussion, with various omissions not noted in the quoted text.

“Commercial bribery is a garden variety of fraud, here consisting of the suppliers’ concealing from Williams the fact that they were bribing its buyer. The judge gave a standard fraud instruction. It required the jury to find that Williams had justifiably relied on the facts known to it in continuing to purchase from Arrow and Milgray — or in other words that Williams hadn’t known about the bribes.

“At the request of the defendants, however, the judge also gave instructions on the affirmative defenses of ratification and in pari delicto. He instructed the jury that if Williams had known or ‘should have known’ of the defendants’ bribing Barry, it should find that Williams had ratified the fraud and could not recover damages. And likewise if Williams had been in pari delicto (equally at fault) with the defendants, which it would be, the judge told the jury, if Williams either (1) ‘was aware of a general practice of bribery of its buyers by its suppliers’ or (2) ‘knew or was recklessly indifferent to the fact that Greg Barry was soliciting and/or accepting kickbacks from Williams’ vendors.’

“The jury found that Williams had proved fraud, in accordance with the instruction on fraud but also found that the corporate defendants (Garrity

did not assert these defenses) had proved both affirmative defenses; and so Arrow and Milgray were exonerated.

“The instructions on the affirmative defenses were erroneous at a quite fundamental level. As countless cases affirm, a victim’s negligence is not a defense to an intentional tort, such as fraud. (For that matter, it is no longer a complete defense to an unintentional tort, having been replaced by the partial defense of comparative negligence. That should have been a clue as to how the law would treat the victim’s negligence in the setting of an intentional tort.) Yet by instructing the jury that it should return a verdict for the defendants if it found that Williams ‘should have known’ that Barry was taking bribes, the judge allowed the jury to exonerate the defendants on the basis of the carelessness of their victim in failing to discover that it was a victim.

“The error was compounded by a misunderstanding of the legal meaning of ‘ratification.’ Had Williams after discovering Barry’s bribe-taking decided that it was on the whole beneficial to Williams (maybe because it allowed Williams to pay him a lower salary!), and had decided not to fire him or otherwise discipline him, that would be ratification, much as if a restaurant owner decided after discovering that his headwaiter was accepting tips in order to seat patrons to condone the practice (still common, especially in nightclubs). Or as if Barry, as Williams’ agent, had made an unauthorized transaction on Williams’ behalf that Williams, after discovering the transaction, had decided was in its interest after all, and so it would retain the benefits of

continued...

it. Obviously it couldn't retain the profits of the transaction but shuck off the costs on the ground that it had never authorized the transaction and therefore wasn't bound by it.

"But that isn't the defendants' theory. It is that Williams knew all along about Barry's bribe-taking. If so, this would exonerate the defendants, all right, because it would mean there had been no fraud in the first place, not that the fraud had been washed away by ratification.

"No ratification instruction should have been given, let alone one that misstated the law by supposing that ratification can be premised on a careless accident.

"The defense of in pari delicto is intended for situations in which the victim is a participant in the misconduct giving rise to his claim, as in the classic case of the highwayman who sued his partner for an accounting of the profits of the robbery they had committed together. Note, 'The Highwayman's Case,' 9 L.Q. Rev. 197, 197-99 (1893) (*Everet v. Williams* (Ex. 1725)). It has been extended to the case — illustrated not by the in pari delicto defense asserted by Arrow and Milgray but by the separate in pari delicto defense asserted by Milgray — in which each party is accused of having wronged the other; Milgray, as we'll see, claims that Williams committed fraud against it at the same time that it was committing fraud against Williams.

"That is not the character of the in pari delicto defense that Arrow and Milgray asserted jointly against Williams. Clause (2) of the instruction ('knew or was recklessly indifferent to the fact that Greg Barry was soliciting and/or accepting kickbacks from Williams' vendors') barred Williams from recovering against either defendant if the jury found that Williams knew that, or was recklessly indifferent to whether, Barry was taking bribes. This part of the instruction didn't define a defense distinct from ratification, but merely repeated in different words the instruction on ratification, except that for negligence it properly substituted reckless indifference, which the law treats for most purposes including this one the same as knowledge.

"Clause (1) ('was aware of a general practice of bribery of its buyers by its suppliers') likewise repeated the defense of ratification in the guise of in pari delicto (as if it helps a jury to have instructions translated into Latin!), but re-injected negligence as a basis for barring Williams by suggesting that Williams' knowledge of a 'general practice,' presumably a reference to the Christmas gifts, should have alerted it to the possibility that Barry was taking big bribes.

"Apart from the fact that the two affirmative-defense instructions were at once erroneous and confusingly overlapping, they made a confusing mishmash with the instruction on prima facie fraud. The jury found that Williams had been justified in relying on the facts known to it, yet how could it find that and at the same time find that Williams both had ratified the fraud and had been equally at fault with the defendants? There is a possible path, as we're about to see, but we can have no confidence that it is the one the jury actually took.

"So Williams is entitled to a new trial on fraud — but not, as it urges, to a judgment based on the jury's finding of prima facie fraud. The jury may have based its findings of ratification and equal fault simply on negligence by Williams — the instructions would have permitted that — in which event Williams would be entitled to a judgment. But, again given the confusing medley of instructions, we cannot have any confidence that that was the jury's thought process.

"The separate in pari delicto instruction that the judge gave with respect to Milgray's claim against Williams and its former employees required the jury to bring in a verdict for Milgray if it found (as it did) that 'Williams, acting through its agent Barry, knowingly participated in Slupik's and/or Gnat's unlawful diversion of business from Milgray to Microcomp.' (Remember that Gnat and Slupik were employees of Milgray who formed a company that sold components to Williams in competition with Milgray.)

"This instruction did not commit the error of injecting the issue of the

victim's negligence into an intentional tort case, but it had no basis in law, because it required no showing that Williams benefited from, or even knew anything about, Gnat's and Slupik's conduct. All the instruction required the jury to find was that Williams was 'acting through its agent Barry,' which we take to mean, and which the jury probably understood to mean as well, nothing more than that Barry was Williams's agent.

"Barry doubtless harmed Milgray by buying from Microcomp, and Milgray could sue him for that harm. But the fact that Barry was bribed not only by Milgray, to Milgray's benefit, but also by two employees of Milgray, to Milgray's detriment, does not establish fault on the part of Williams. An agent's knowledge is not imputed to his principal when the agent is acting adversely to the principal, as Barry was.

"[I]n general when an agent acts entirely on his own behalf, doing things that could not possibly be interpreted as the merely overzealous or ill-judged performance of his duties as agent, he is acting outside the scope of the agency and the principal is not bound.' *Hartmann v. Prudential Insurance Company of America*, 9 F.3d 1207, 1210 (7th Cir. 1993). It is not as if Gnat's and Slupik's fraud benefited Williams. It made Milgray another victim, along with Williams itself, of Barry's fraud; it did not make Williams equally at fault with Barry. The instruction was an example of blaming the victim, with a vengeance.

"Williams might be liable to Milgray under one theory or another, but it was not a participant in the fraud against Milgray, especially when we consider that, so far as appears, Williams lost, and Milgray on balance benefited, from Barry's conduct. The only fault of Williams mentioned by the instruction is Barry's bribe-taking; the jury was not asked to find that Williams authorized or ratified Barry's conduct or even that it was negligent in failing to prevent it."

Reversing and remanding because of these errors in the instructions, Posner also provided guidelines for handling Williams' alternative claim for restitution, which will be covered in Wednesday's Trial Notebook.