

1 I. INTRODUCTION AND PROCEDURAL BACKGROUND

2 On July 29, 2002, plaintiff S [REDACTED] complaint against Bradford Baugh  
3 for legal malpractice with regard to [REDACTED] dissolution proceeding with her  
4 former husband, N.A. [REDACTED] October 31, 2002, plaintiff filed her First  
5 Amended Complaint against Michael S. Thompson and his firm, Greco, Filice & Thompson, for  
6 accountant malpractice in the same dissolution proceeding.<sup>1</sup>

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8 The primary claim in the complaint against Mr. Baugh and Mr. Thompson is that they  
9 negligently prepared a vesting schedule for stock options and stock compensation grants that Swami  
10 obtained as a result of his employment with Johnson & Johnson. Plaintiff further contends that Mr.  
11 Baugh and Mr. Thompson did not conduct a proper investigation in order to trace when the options  
12 and grants were exercised and when the shares acquired were sold. Plaintiff also asserted that Mr.  
13 Baugh and Thompson used the wrong formula to determine the character of the shares acquired  
14 through the exercise of the options. Plaintiff contends that as a result of this negligence, the family  
15 law court awarded all of the Johnson & Johnson shares, 21,000, to Swami as a separate property on  
16 May 25, 2000 (Exhibit "A" to the Declaration of Jerry R. Hauser ("Hauser Dec.")), which was  
17 affirmed on appeal. (Hauser Dec., Exhibit "B") Plaintiff has also asserted claims against Thompson  
18 unrelated to Mr. Baugh.

19 The vesting schedule that was used in the underlying family law proceeding was prepared by  
20 Thompson, the parties' joint accountant, whose scope of duties included investigating the parties'  
21 assets and conducting discovery to determine what was separate (SP) and community (CP) property.  
22 The vesting schedule prepared by Thompson established that all shares acquired through the options  
23 and stock compensation grants were SP, except for 5,871 shares. These CP shares were acquired  
24 through stock compensation grants, but the majority of the shares that remained as of the date of  
25 separation were acquired through the exercise of stock options. Based on Thompson's vesting

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27 <sup>1</sup> Thompson has filed a motion for Summary Judgment to be heard on December 5, 2005, primarily based on the claim he  
28 is immune from liability.

1 schedule, the parties entered into a stipulation with regard to the characterization of the shares  
2 acquired before separation (Hauser Dec., Exhibit "C"). The only issue to be tried by the family law  
3 court was whether the 5,871 shares that Thompson found to be community property were sold during  
4 the marriage and, if so, the remaining shares, 21,000 as of the date of separation, would be Swami's  
5 separate property.

6 At the trial of the action, Swami testified that all of the stock options were exercised and  
7 acquired prior to marriage and the CP shares acquired through stock compensation grants were sold  
8 during the marriage. Swami presented absolutely no documentation to back up his testimony. Mr.  
9 Baugh argued that without the proper documentation, the presumption should be that the community  
10 property shares, which were co-mingled with SP shares, were not sold. This argument was rejected  
11 by the trial court and the Court of Appeal.

12 During the course of this litigation, plaintiff established that Thompson used the wrong  
13 vesting schedule for the options; and the proper vesting schedule would have shown that a  
14 substantial portion of the Johnson & Johnson options vested during the marriage, and at least 11,628  
15 of the remaining shares as of the date of separation were CP. Based on Swami's testimony there  
16 would have been no need for a trial on whether the CP option shares were sold, because he admitted  
17 that the only shares sold during the marriage were obtained through the grants. Further, a proper  
18 vesting schedule would have also established that a portion of Swami's SP options vested after  
19 marriage and therefore CP funds were used to exercise them creating a CP interest in said shares.

20 The damages in this case are based on the lost value of plaintiff's community property interest  
21 in the Johnson & Johnson shares that were awarded to Swami as a result of the erroneous vesting  
22 schedule. There are many different ways to value the lost interest, but for settlement purposes only  
23 the parties agreed that the damage range is \$675,000 to \$993,000. The damage range is primarily due  
24 to how to value the use of CP funds to exercise SP options. In addition to damages stemming from  
25 plaintiff's lost interest in the Johnson & Johnson shares, plaintiff is also seeking \$100,000 as damages  
26 from Thompson unrelated to Mr. Baugh.

1 In an attempt to settle the case, the parties retained the Honorable Michael Ballachey to  
2 conduct a mediation. The parties were unsuccessful in reaching a global settlement at the mediation.  
3 Mr. Thompson's counsel will not agree to waive the confidentiality provisions with regard to the  
4 mediation, so Mr. Baugh is precluded from setting forth the mediator's recommendation or  
5 Thompson's response. In separate negotiations after the mediation, with the assistance of Judge  
6 Ballachey, plaintiff and Mr. Baugh agreed to use \$800,000 as the appropriate figure for plaintiff's  
7 damages, for settlement purposes only, and as the basis for the guarantee in the sliding scale  
8 agreement. In these subsequent negotiations, plaintiff also indicated that the \$800,000 number  
9 represented what she would accept for a global settlement. The key terms of the settlement are as  
10 follows (a copy of the agreement is attached as Exhibit "D" to the Declaration of Jerry R. Hauser):

11 I. Settlement Amount. The Baugh Defendants, through Lawyers'  
12 Mutual Insurance Company ("LMIC"), shall pay to Plaintiff, the sum of TWO  
13 HUNDRED THOUSAND DOLLARS (\$200,000) (the "Settlement Amount").  
14 The Settlement Amount shall be paid by a check made payable to Plaintiff and  
15 her attorneys and delivered to Plaintiff's Attorneys within 10 business days of  
the entry of order finding this settlement to be in good faith pursuant to  
paragraph 19 herein.

16 II. Additional Payment. (a) The Baugh Defendant will agree to pay  
17 Plaintiff an additional sum, not to exceed FOUR HUNDRED THOUSAND  
18 DOLLARS (\$400,000) based on the difference between the amount of any  
19 judgment Plaintiff receives against the Thompson Defendants, plus the  
20 Settlement Amount, and EIGHT HUNDRED THOUSAND DOLLARS  
21 (\$800,000) (the "Additional Sum"). The amount of the potential judgment  
22 against the Thompson Defendants used to compute the amount of the  
23 Additional Sum shall be before any offsets and include any prejudgment interest  
24 that may be awarded. For example if a judgment is rendered against the  
25 Thompson Defendants, including prejudgment interest, in the amount of  
26 \$600,000 or more, then there will be no Additional Payment; if the judgment is  
27 for \$400,000, then the Additional Payment would be \$200,000; and if the  
28 judgment is \$200,000 or less, then the additional payment would be \$400,000.  
(b) If Plaintiff settles with the Thompson Defendants prior to a judgment being  
rendered, then the amount of the Additional Sum shall be based on the  
difference between the amount of any settlement with the Thompson  
Defendants, plus the Settlement Amount, and EIGHT HUNDRED  
THOUSAND DOLLARS (\$800,000), but under such circumstances the  
Additional Sum shall not exceed TWO HUNDRED THOUSAND DOLLARS  
(\$200,000). For example, if Plaintiff settles with the Thompson Defendants for  
\$600,000 or more, then there will be no additional payment; if the settlement is

1 \$400,000 or less than the Additional Payment will be \$200,000. Any judgment  
2 rendered pursuant to CCP § 998 shall be considered to be a prejudgment  
3 settlement for purposes of calculating the Additional Payment. (c) The payment  
4 of the Additional Payment referred to in this paragraph shall be made at the  
5 following times: 1. Within 30 days of written notice of a settlement prior to the  
6 rendition of a judgment; or (2) Within 30 days of written notice that final  
7 judgment has been entered against the Thompson Defendants.

8 Since Mr. Baugh agreed that if Mr. Thompson enters into a settlement within 30 days of the  
9 good faith finding, he will pay an additional \$200,000, the value of the settlement is \$400,000 until  
10 30 days after a good faith finding and \$200,000 thereafter.<sup>2</sup> The settlement between Mr. Baugh and  
11 plaintiff is clearly in good faith, especially since Thompson's conduct prevented the global  
12 settlement. This is not even a close call. Mr. Baugh is paying \$200,000 regardless of the outcome and  
13 has the potential to be liable for an additional payment up to \$400,000. The primary, if not the sole  
14 cause of the stock loss was the erroneous vesting schedule for the Johnson & Johnson options  
15 prepared by Mr. Thompson. Even though Mr. Baugh maybe be held liable to plaintiff for failing to  
16 discover Mr. Thompson's error, Mr. Thompson is still primarily liable under the doctrine of equitable  
17 apportionment. Mr. Baugh's share of any liability for the Johnson & Johnson loss is less than 50%,  
18 and at worse is 50%. Mr. Thompson had an opportunity to enter into a reasonable settlement and  
19 chose not to.

## 20 II. FACTUAL BACKGROUND

21 Prior to Mr. Baugh's retention, plaintiff and Swami agreed to retain a CPA to act as a joint  
22 accountant to determine the nature and extent of the community and separate property of the parties;  
23 the value of the community property; the extent of the community property interest in such property  
24 if, in fact, the community had an interest; and the equal division of the community assets (Hauser  
25 Dec., Exhibit "E"). Pursuant to that stipulation, plaintiff and Swami jointly retained Mr. Thompson  
26 in August of 1997 (Hauser Dec., Exhibit "F"). This stipulation and retention of Mr. Thompson was

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27 <sup>2</sup> In the negotiations subsequent to the mediation, Mr. Baugh agreed that if plaintiff could reach a settlement with  
28 Thompson, he would be willing to pay 50% of the amount, \$800,000, plaintiff needed to reach a global settlement.  
Plaintiff's council had direct communications with Thompson's malpractice carrier after the mediation, but Thompson's  
carrier was not willing to pay an amount necessary to reach the global settlement number.