Legal Backgrounder

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STATES DISSERVE THE PUBLIC INTEREST WHEN HIRING CONTINGENT FEE LAWYERS

by

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With the Attorney General tobacco lawsuits as a backdrop, and the serious budget problems that most states are facing, there is a growing concern that some state Attorneys General, perhaps with the support of their governors or legislatures, will seek to bridge the budget gap with a lawsuit targeting another industry or industries. Industries sometimes mentioned in this context include prescription drugs, fast-food, processed food, alcohol, medical service providers and SUV manufacturers, to name a few.

The merit, or lack of merit, of these potential lawsuits we leave for another day, although these industries and others certainly should be developing a proactive strategy to deal with this situation. In the end, even if state Attorneys General do not pursue any of theses lawsuits, mass tort attorneys in the private bar almost certainly will.

The question for today and is whether it is sound public policy for a state Attorney General to employ outside counsel on a contingent fee basis to represent the state. In this author's opinion, it is not.

The justification for contingent fee agreements in private practice is that many people are unable to afford to hire a lawyer at an hourly rate to seek compensation for an injury or other wrong which they have suffered. A contingent fee arrangement is the only way that they can go to court to obtain a judicial remedy. Almost by definition, the object of a contingency fee lawsuit is to obtain a money judgment for the injured party.

Even in these financially troubled times, any state that determines to make a particular lawsuit a state priority can afford to pay its attorneys on an hourly basis. The difficulty comes when a state Attorney General wants to undertake an expensive piece of litigation and either knows or assumes that the state legislature will not fund it. The solution that suggests itself is to hire outside counsel on a

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contingent fee basis. That is exactly what many states did in the tobacco litigation.

Virtually every state Attorney General has the authority to hire outside counsel to represent the state when the Attorney General determines it is in the best interest of the state to do so. The check and balance on this authority is that he or she must have an appropriation available to pay the outside counsel.

The power to authorize the expenditure of state funds is placed by every state constitution in the state legislature, subject to the governor's veto authority. This authority is one of the Legislature's most powerful public policy making tools. And since expenditures first require tax revenues, is often times one of the most contentious legislative duties.

When a contingent fee agreement is entered into, the Attorney General's authority to control the state's litigation and appoint outside counsel collides with the Legislature's authority to control the purse. This comes most strongly into focus once a money judgment or settlement has been obtained and it is time to pay the fee.

How can these competing powers be reconciled? While the answer to this question is one of state law which can vary from state to state, the answer in most states is that the Attorney General can employ outside counsel on a contingent fee basis, but the fee will only be paid to the extent, if any, the Legislature appropriates funds for that purpose.

This is consistent with the handling of other state contracts. For example, the State of Nebraska sometimes leases real estate or equipment under a multi-year lease. However, these agreements are subject to state appropriations as a matter of state constitutional law. If funds are not appropriated to pay the lease, the state is no longer obligated on the lease. By analogy, a contingent fee agreement is enforceable only to the extent the Legislature appropriates funds to pay it.

But, of course, the contingent fee may be taken out before the remaining funds are paid to the state. In the case of the tobacco settlement, the tobacco companies agreed to pay the contingent fee attorneys directly, over and above the settlement amounts to be paid to the states. The argument is that these attorney fees never were state funds and therefore are not subject to the appropriations process. (Indeed the tobacco agreement provides that if the attorney fees are found to be unreasonable, the excess portion goes back to the tobacco companies, not to the states!)

Can the legislature's appropriations authority be effectively evaded in this manner? This is a question of state law that could vary from state to state. However, the common-sense answer is that all the money, without regard to whether it was placed in the state treasury, is part of the compensation the state received from the settlement or judgment and therefore is the state's money. Indeed, since the attorneys are not parties to the lawsuit, any provision in the settlement for payment to them is for their service as an agent of the state.

If this principle were established by statute or state court interpretation in a number of states, it would greatly discourage outside counsel from entering into contingent fee arrangements with states because if the case is lost they receive nothing and if they win they get only the compensation the Legislature is willing to give them after the fact.

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Another major difficulty with states using contingent fee lawyers is that the interest of the contingent fee lawyers is to maximize the dollar amount of damages, while the responsibility of the Attorney General is to fairly enforce the state's laws. For example, as a case goes along, the Attorney General may favor a settlement for a significant fine, injunctive relief and the resignation of responsible corporate officers, while a contingent fee attorney would want to seek a much larger financial judgment. If the Attorney General settled the case on his terms, would the state be liable for a percentage of the larger amount of money that could have been obtained?

The American Legislative Exchange Council has proposed model legislation that is intended to address some of the issues that have arisen in the use of outside contingent fee lawyers in some states. The legislation requires competitive bidding, and where the fees can reasonably be expected to exceed $1 million, requires a legislative hearing before a contract for outside attorney services can be entered into. It also limits contingent fees to not more than $1,000 per hour.[1]

While these are certainly improvements, the question remains whether a state with the power to tax should ever enter into a contingent fee agreement. Wouldn't it be even better for state legislatures to enact legislation expressly prohibiting the state from entering into contingent fee agreements? That would certainly be consistent with the legislatures' authority to control the expenditure of public funds.

It is true that some lawsuits, such as the state tobacco lawsuits, might not be pursued by the states in the absence of a contingent fee agreement. In other words, where the initial prospects for success are small, and the cost of a lawsuit will be great, the litigation will in most cases not be filed by the states if they cannot proceed on a contingent fee basis

On the other hand, some of the results of the tobacco lawsuits could have been achieved by state legislatures or the Congress without the need for litigation. Any state could have increased the tobacco tax to reimburse itself for medical expenses caused by tobacco smoking without the need for any attorneys or attorneys' fees at all. And some of the other provisions of the tobacco settlement could have been enacted by state legislatures or the Congress and thus imposed upon tobacco companies without litigation.

Some provisions of the tobacco settlement, especially some of the advertising restrictions, could not been imposed by legislation or by court order because they violate the First Amendment to the U.S. Constitution. But is it really a just thing for a state to impose requirements in a settlement that the Constitution of the United States forbids it to impose by law?

None of this is written for the purpose of criticizing the author's former colleagues in their handling of the tobacco lawsuits. They were and are, as a group, well-intentioned and sincerely concerned about health issues caused by tobacco — and were particularly concerned about children's health. But the tobacco lawsuits were an experience that should be instructive for the future. The vast size of the attorneys' fees in the tobacco cases has been a political liability for Attorneys General in several states. Some states have even been involved in litigation with their former attorneys over the amount owed. Most recently, Massachusetts was sued by its tobacco lawyers for $1.25 billion, which they demand in addition to the $775 million already awarded Massachusetts' contingent fee tobacco

[1]ALEC's Private Attorney General Retention Sunshine Act has been adopted in some form in Colorado (2003), Virginia (2002), Kansas (2000) and North Dakota and Texas (1999).

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lawyers.

More fundamentally, states are not paupers who cannot litigate in the absence of contingent fee agreements. In addition to the ability to appropriate millions of dollars for a lawsuit, states can also oftentimes achieve their policy objectives by legislation directed at the perceived evil. And finally, state Attorneys General, working as a group, can bring enormous resources to a case within their existing budgets without the need for outside contingent fee counsel. On balance, contingent fee agreements will almost never best serve the interest of state Attorneys General, the interests of the states, or the public interest served by placing the power to spend the states' money solely in the hands of the state legislature.

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