

Contingency Fee Arrangements for Public Entities

Setting Parameters Can Help Ensure Government Neutrality

Summary

Civil litigation is a consistent concern amongst California businesses, given the cost, time, and strain it creates. This concern is significantly enhanced when the State of California or another governmental entity is the party pursuing litigation, as it has more power, more authority, and potentially more resources than just a private plaintiff.

In 2010, this threat of litigation was exacerbated by the California Supreme Court decision in *County of Santa Clara v. Atlantic Richfield Company*, which held it was proper for a public entity to utilize private attorneys through a contingency fee arrangement to represent the entity in civil litigation. Although it still is unclear the extent to which a private attorney may be utilized through a contingency fee arrangement with a public entity, the door has been opened by the Supreme Court, leaving an area ripe for either litigation or the Legislature to set forth the parameters of such relationships to ensure the integrity and neutrality of the government is not jeopardized.

Contingency Fee Arrangements with Public Entities in California

County of Santa Clara v. Atlantic Richfield Co.

In March 2000, the County of Santa Clara filed a class action against Atlantic Richfield Company that ultimately alleged a cause of action for public nuisance and abatement with regard to the defendant's use of lead paint in homes. Throughout the litigation, the county was represented by private attorneys through a contingency fee arrangement, meaning the attorneys would be compensated for their time by receiving a percentage of any recovery obtained from the litigation. Contingency fee arrangements create an automatic financial incentive for the attorney in the litigation, as the attorney has a personal stake in getting the highest award of damages possible.

The defendant filed a motion to bar the county from using a private attorney through a contingency fee arrangement on the grounds that such an arrangement eliminates the absolute neutrality of the representation required for the prosecution of a public nuisance action, due to the private attorney's personal financial interest in the litigation. The defendant compared the relationship to paying a prosecutor a contingency fee based upon the number of convictions obtained, rather than protecting the public interest. The county disagreed, claiming such a fee arrangement was not a complete bar to private representation of public entities, thereby leaving the question to the California Supreme Court to answer.

On July 26, 2010, the Supreme Court ruled that there is no automatic bar to public entities hiring private attorneys through a contingency fee arrangement. *County of Santa Clara v. Atlantic Richfield Co.*, 50 Cal.4th 35 (2010).

Although the court did not suggest that such an arrangement would always be acceptable, especially where criminal liability is involved, in this particular case, the court deemed it OK. Unlike prior cases in which a contingency fee with a public entity was held as improper given criminal liability, loss of property, or the interruption of business operations, the defendant in this case was not at risk of losing its property or business. Rather, the public nuisance claim was focused on the use of lead paint that was already illegal. Moreover, due to contractual provisions that could be placed in the contingency fee arrangement on remand, which would dictate the county retain absolute control over the litigation, the court determined that the fee arrangement with the county was not improper. The plaintiffs ultimately were awarded approximately \$1.15 billion in damages against the paint company.

Although the defendant filed a petition for writ of certiorari with the U.S. Supreme Court, asking it to decide the constitutionality of such agreements, the U.S. Supreme Court denied review in July 2011.

Post-County of Santa Clara v. Atlantic Richfield Co.

Since the *County of Santa Clara* decision, Santa Clara County has partnered with private law firms to file at least eight other lawsuits alleging public nuisance, according to a July 14, 2014 article on *Legal News Line*, "Opioid Suit is Latest Brought by Calif. County with Help From Contingency Fee Attorneys," by Amanda Robert. The legal actions included a lawsuit filed with Orange County against five opioid pharmaceutical manufacturers. In this lawsuit, the counties alleged that the drug manufacturers violated California's false advertising and unfair competition laws, and created a public nuisance by persuading doctors to prescribe opioids

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for long-term use even though the manufacturers knew the opioids were ineffective, addictive and unsafe. The counties sought to collect damages from the manufacturers to pay for such things as emergency room costs and treatment programs for individuals addicted to prescription drugs. On August 27, 2015, the judge presiding over the case dismissed it without prejudice, meaning the counties could revive the case again, until the Federal Drug Administration completes its review of painkillers and appropriate regulations of such medicine.

In July 2015, the City of San Jose, represented by a private law firm, filed a public nuisance lawsuit against Monsanto, a manufacturer of polychlorinated biphenyl (PCBs), alleging that Monsanto should have to pay for the cleanup of waterways and the San Francisco Bay due to PCB pollution. Initially, the judge dismissed the case as there was no allegation or evidence that Monsanto had actually placed any PCBs into the waterways/ Bay. In 2016, however, the Governor signed two pieces of legislation that opened the door for San Jose, and other cities, including Oakland and Berkeley, to refile these cases.

In August 2013, the City of Richmond hired a private law firm to sue an oil refinery for damages related to a refinery fire. The private law firm retained by the City of Richmond advertises on its website about its expertise in representing public entities in litigation.

Government Use of Contingency Fee Arrangements: Good or Bad?

As demonstrated by the *County of Santa Clara* decision, the public entity that seeks to use private attorneys through a contingency fee arrangement believes that such arrangements are in fact proper and necessary. Arguments in support include: 1) it enhances the public entity's limited budget by obtaining subject matter legal experts whom the entity does not have to compensate until the litigation concludes; 2) it assists the public entity in matching the potential resources of a defendant corporation; and 3) contractual provisions maintain the neutrality necessary to advocate on behalf of the government.

There is no question that representing a public entity is a lucrative arrangement for a private attorney. The fee awards are significant, as the underlying damages are based upon representing the public rather than a single plaintiff, notes the Legal Backgrounder by Victor E. Schwartz, Kevin Underhill, Cary Silverman and Christopher Appel, "Government's Hiring of Contingent Fee Attorneys Contrary to Public Policy."

An example of such awards are the tobacco litigation cases wherein the fees awarded to private attorneys that were hired in various states on behalf of the attorney generals ranged from \$27 million to \$150 million.

Confirming this advantage, Douglas McMeyer, Lise T. Spacapan and Robert George state in "Contingency Fee Plaintiff's Counsel and the Public Good": "[last], but certainly not the least benefit to the plaintiffs' bar, is the likelihood that the private contingency fee lawyer can recover even greater awards when representing the state than he or she could when representing the corresponding private plaintiffs' class."

Representing the state can provide procedural advantages as well. McMeyer, et al., list several of these benefits in their article: 1) broader causes of action that are not well-defined and lead to more liberal interpretations, such as public nuisance vs. private nuisance; 2) some defenses applicable to private parties are not applicable to the state; 3) recovery is based upon public interest, not individual injuries; and 4) defendants, especially corporate defendants, are not likely to litigate against the state and will often settle, as "[f]ew corporations 'are capable and willing to risk trial when the plaintiff is a state (or a consortium of state attorneys general operating in concert) that may collect billions of dollars as a result of harms allegedly suffered by millions of its residents.'"

Opponents to this type of arrangement, however, raise a number of concerns, including: 1) the loss of significant revenue to the government and therefore public programs, from the payout of the contingency fee to a private attorney; 2) the inability to ensure that contractual provisions dictating who maintains control of the litigation are actually followed; and 3) the potential for corruption with regard to the public entity involved and the private attorney retained, especially when political contributions are involved.

Two attorneys who specialize in public nuisance law, David Axelrad and Lisa Perrochet, outlined the use of contingency fee arrangements with government entities and highlighted several of these concerns, including the lack of neutrality as well as the potential for conflict:

"Those who favor the use of contingent-fee arrangements in prosecuting public nuisance actions argue that the standard of neutrality advocated by contingent fee opponents is unrealistic and unobtainable, pointing out that no advocate can be completely indifferent to success in a particular case. That argument is a straw man. The issue, however, is not whether an advocate can be perfectly disinterested. All advocates have an interest in winning their cases. The neutrality demanded of an attorney enforcing public rights does not require complete indifference to the

outcome of the case. However, when the same attorney has a financial stake in the outcome of that case, the potential for the attorney to act out of self-interest rather than the public interest creates an indelible appearance of impropriety that erodes public confidence in the integrity of the prosecution. As Justice Robert H. Jackson recognized in another context, 'If we were to add motives of personal avarice to other prompters of official zeal the time might come when the scandals of law-enforcement would exceed the scandals of its violation.'" (citations omitted). (David Axelrad and Lisa Perrochet, "Public Nuisance: Public Entity Litigation and Contingency Fee Counsel," <http://www.nuisancelaw.com/learn/contingency-fee-counsel>)

These legal experts also noted the potential for conflicts of interest to arise from contingency fee arrangements, such as when the public good would be served by obtaining nonmonetary relief, yet the contingency fee attorney who is compensated by obtaining the highest monetary relief pursues monetary damages. The author of a law review article explained this conflict with regard to environmental remediation: "The government attorney is a salaried official whose fee is not formally tied to the damage award. The environmental special counselor, on the other hand, derives a fee from the damage award and is thus interested in monetizing that award to maximize personal gain. Rather than planting trees or remediating a spill, the environmental special counselor is personally interested in the monetary value of that construct to draw a contingency fee award." (Julie Steiner, "Should 'Substitute' Private Attorneys General Enforce Public Environmental Acts? Balancing the Costs and Benefits of the Contingency Fee Environmental Special Counsel Arrangement," Western New England University School of Law, 2011.)

Additional conflicts also can arise when the process utilized to retain the law firm to represent the public entity is tainted. As Axelrad and Perrochet commented: "[w]ith 'hundreds of millions in contingent fees' at stake, there is a real danger that contingent fee counsel will 'pay to play' and that the government official in charge of hiring 'will select the private counsel most willing to bribe him with either an under-the-table payment or a legally permissible political contribution.'" (citations omitted).

This concern was highlighted in an October 25, 2012 *Wall Street Journal* article by James V. Grimaldi and Alicia Mundy, "Nice Payday for 'Toxic' Work." The article reported that the National Credit Union Administration contracted with private attorneys to pursue litigation for \$6 billion–\$9 billion in damages against several credit unions. The article noted that the two firms hired by the agency were involved in political contributions.

Based upon these concerns, Axelrad and Perrochet concluded in their article that contingency fee arrangements with public entities should not be allowed:

"When public enforcement actions are at issue, regardless of whether the government has the legal authority to retain outside counsel, the fundamental public interest in a neutral and dispassionate prosecutor requires that the financial motivation of a contingent fee counsel must not be allowed to taint the prosecution of public nuisance claims. 'The focus must be on whether the arrangement 'might lead' the layman to conclude that the appearance of impropriety exists. The emphasis is on perception of citizens, not that of litigants, their counsel or elected officials, because it is the citizen's confidence that is at stake and it is the citizen's resources which are at risk.'" (citations omitted)

Federal Activity

In May 2007, President George W. Bush issued Executive Order 13433, "Protecting American Taxpayers from Payment of Contingency Fees," in which he prohibited the U.S. government from contracting with private attorneys on an hourly or contingency fee to represent the government in litigation or other proceedings. President Barack Obama did not rescind this Executive Order.

California Legislative Activity

Since the use of contingency fee agreements with government entities began in approximately 1980, the recognition of the potential conflict-of-interest between a private attorney and the government has motivated several states to take action. So far, 10 states have passed legislation regarding the use of private attorneys by government entities. Some of the enacted laws cap the hourly fee and total recovery to the private attorney, while other laws focus on transparency to the public of the arrangement and limitation of political contributions to government officials.

In 2016, Assemblymember Cheryl Brown (D-San Bernardino) introduced AB 2804, which would have required cities and counties utilizing contingency fee arrangements with private law firms to comply with bidding requirements to make the process more transparent to the public, as well as include specific

contractual provisions in these contingency arrangements to try to ensure the governmental entity retains control over the litigation. AB 2804 did not move through the legislative process.

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Position**

Litigation with a government entity is daunting enough for any defendant without the fear of the litigation being influenced by the financial interest of a private attorney. If California continues to condone the use of private attorneys to represent government entities through contingency fee arrangements, there must be enhanced contractual requirements, ethical standards, and required disclosures to ensure the neutrality of the government is not jeopardized by such arrangements, thereby placing the defendant at a completely unfair disadvantage.

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