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2 JAN 1981

MEMORANDUM FOR ALICE DANIEL
Assistant Attorney General
Civil Division

Re: "Bifurcated" Settlement Negotiations in Cases
Involving Statutorily Authorized Attorneys' Fees

You have asked whether, in civil cases in which the United States or a federal agency is sued under a statute authorizing the award of attorneys' fees to prevailing plaintiffs, the government should always decline in settlement negotiations to discuss the issue of attorneys' fees before the relief to be awarded to the plaintiffs is finally resolved.^{1/} It could be argued, as it has been in a letter to you by the Washington Council of Lawyers, that in every such settlement negotiation in which discussions of the relief and attorneys' fees proceed at essentially the same time, the plaintiff's lawyer is put in an irreconcilable conflict of interest with his client. The conflict would arise in the following way. First, we assume that the plaintiff and his lawyer do not have a clear fee agreement setting the limits of the lawyer's fee, and that the lawyer will receive only a court-awarded fee authorized by statute. We also assume that the lawyer's interest will be to obtain the highest possible fee. In settlement negotiations, the government's interest will be to minimize the total amount that must be paid (or loss incurred) to settle the case. In such a situation, discussion

^{1/} Your memorandum to us of August 4, 1980, asked for a discussion of the ethical issues raised by settling the kinds of cases of concern to the Washington Council of Lawyers. Subsequent conversation with your staff focussed the discussion on this question as the one of central concern.

of attorneys' fees before settlement of the award on the merits might lead a plaintiff's attorney to sacrifice his client's interests in favor of his own interests. Alternatively, to avoid any appearance of such impropriety, the attorney might purposely accept a lower fee than otherwise he would accept, perhaps over the long term jeopardizing his ability to continue to take on such cases however meritorious they may be.

The position of the Washington Council of Lawyers is that these dangers may be -- and should be -- prevented by a flat ban imposed by the Department of Justice on its attorneys on any discussion of fees before final settlement of the award on the merits of such cases. The question for this office is whether such a rule is required by the applicable case law or by the ABA Code of Professional Responsibility governing adversarial legal practice. We believe that it is not. We express no view regarding the policy aspects of the question.

I

The "American rule" on attorneys' fees provides that each party pays its own fees, absent an applicable exception to the general rule. See Alyeska Pipeline Co. v. Wilderness Society, 421 U.S. 240, 247 (1975). One exception fashioned by courts applies to a situation in which plaintiff's efforts lead to the creation of a "common fund" benefitting others as well as the plaintiff. In these cases, courts have allowed plaintiffs to recoup their fees out of the common fund. See id.; Trustees v. Greenough, 105 U.S. 527 (1882). Another class of exceptions involves suits under statutes authorizing the award of attorneys' fees by the defendant to prevailing plaintiffs. There are a large number of such statutes, including Title VII of the Civil Rights Act of 1964, 42 U.S.C. § 2000e-(i), the Civil Rights Attorneys' Fees Awards Act, 42 U.S.C. § 1988, and numerous others.^{2/} The question you have asked involves cases within the latter exception to the American rule.

^{2/} See the partial listing of such statutes in I H. Newberg, Court Awarded Fees in Public Interest Litigation 203-04 (1978).

The view that attorneys' fees should never be discussed until after the question of the relief to be awarded plaintiffs is finally settled rests on two primary arguments. First, it is said to represent the adoption of the Third Circuit's reasoning in Prandini v. National Tea Co., 557 F.2d 1015 (1977). Second, it is said to rest on certain ABA canons and disciplinary rules, which require that an attorney act wholly in the interests of his client (not for his own gain), and that attorneys refrain from circumventing a disciplinary rule through the actions of another. We will discuss each argument in turn.

II

Prandini involved a class action brought to remedy alleged sex discrimination in employment by a private firm. In its decision, the court deemphasized the differences between "common fund" situations, in which an increase in attorneys' fees directly reduces the plaintiff's recovery from the fund, and a case (like Prandini) in which the award of fees is authorized by statute, here the Civil Rights Act of 1964, § 706(k), 42 U.S.C. § 2000e-5(k). The court said that even though the conflict between the plaintiff class and its attorneys may be more "apparent" in the former situation, "[i]t is often present nonetheless" in the latter situation. See 557 F.2d at 1020. In view of the district court's responsibilities to superintend the award of attorneys' fees and ensure fairness to class members, the court of appeals proposed what it called "[a] reasonable solution" to the problem of potential conflicts of interest between the plaintiff class and its attorney: it is "for trial courts to insist upon settlement of the damage aspect of the case separately from the award of statutorily authorized attorneys' fees. Only after court approval of the damage settlement should discussion and negotiation of appropriate compensation for the attorneys begin. This would eliminate the situation found in this case of having, in practical effect, one fund divided between the attorney and client." Id. at 1021. See Note, Attorney's Fees-Conflict Created by the Simultaneous Negotiation and Settlement of Damages and Statutorily Authorized Attorney's Fees in a Title VII Class Action -- Prandini v. National Tea Co., 51 Temple L.Q. 799 (1978).

Reliance on Prandini as support for a broad per se rule favoring bifurcated settlement negotiations ultimately founders for several reasons. First, Prandini's facts are limited, and thus even if we may view the case as adopting a legally-mandated per se rule, it would only apply in limited circumstances. In particular, Prandini involved a class action, and courts have commonly shown special regard for the interests of normally passive, absentee class members by guarding them against the unduly self-interested assertions

of their representatives.^{3/} Given Prandini's emphasis on the need to protect the interests of class members who are not personally involved in the litigation, see id. at 1020-21, it is strained to suggest that the case stands for a per se rule in any other than a class action context.

Moreover, we question whether Prandini does adopt a legally-mandated per se rule at all. Although it rests on the premise that there is little difference between "common benefit" situations and situations involving statutorily authorized attorneys' fees with regard to preventing conflicts of interest between the plaintiff class and class counsel, that premise is in fact qualified in the opinion: the court stated that "often" -- not always -- the conflict between client and attorney may be present in both situations. See 557 F.2d at 1020. Moreover, the court does mention, although it does not fully explain the nature of, "special circumstances, such as those mentioned by the district court in this case", which were of importance in reaching its judgment. See id. at 1021. This is hardly the language of an opinion meant to articulate a sweeping, across-the-board per se rule. Furthermore, the court's language in announcing the policy of bifurcated settlement negotiations is cast in terms of the advisability, not necessarily the legal requirement, for such a policy: "[a] reasonable solution, we [the court] suggest, is..." the adoption of what it called in Prandini II a "supervisory rule." See Prandini v. National Tea Co., 585 F.2d 47, 49 n. 1 (3d Cir. 1978). Viewed by itself, therefore, we do not read Prandini I as imposing a broad per se ban on simultaneous discussion of the relief and of attorneys' fees based on the legal impermissibility of any other result.

This reading is borne out by subsequent Third Circuit decisions. In Prandini II, involving the same matter of attorneys' fees, the court seemed to back away somewhat from the broad language in Prandini I about the essential similarity between "common benefit" situations and situations involving statutorily authorized attorneys' fees. In the latter case, the court, albeit without retreating from the result in Prandini I, noted expressly that the two situations are quite distinct: "[s]tatutorily authorized fees are not paid out of the plaintiffs' recovery, and the attorney in seeking his fee is not acting in any sense adversely to the plaintiffs'".

^{3/} See generally Developments-Class Actions, 89 Harv. L. Rev. 1318, 1595, 1605-10 (1976).

interest," for in such a situation the attorney's fees "do not come out of, nor do they reduce, the plaintiffs' recovery." 585 F.2d at 53; see also Note, Promoting the Vindication of Civil Rights Through the Attorneys' Fees Awards Act, 80 Colum. L. Rev. 346, 362 (1980). In another case involving an individual shareholder's derivative suit that yielded a fund out of which plaintiff's attorneys' fees were agreed to be paid, the Third Circuit chose not to extend the supervisory rule of Prandini I about bifurcated settlement negotiations, but instead distinguished that case on its facts. See Shlensky v. Dorsey, 574 F.2d 131, 150 (1978).

That the reasoning of Prandini I has not been viewed as requiring a general, per se ban on simultaneous settlement discussion of the relief aspect of a case and attorneys' fees is confirmed by Mendoza v. United States, 623 F.2d 1338 (9th Cir. 1980). In Mendoza, a school desegregation case in which the United States intervened on behalf of the plaintiff class, the court took pains to discourage simultaneous settlement negotiation about the relief and about attorneys fees; but at the same time, it expressly disavowed any blanket rule under which courts would be justified in rejecting resulting settlements on the grounds of fatal infection by a conflict of interest between plaintiffs and their counsel. The court wrote:

Whether the existence of this potential conflict [between plaintiff class and its attorney] requires a trial court to reject a settlement proposal depends upon the circumstances of each case. The presence of simultaneously negotiated attorneys' fees should cause the court to examine with special scrutiny the benefits negotiated for the class. It would rarely be an abuse of discretion for a trial court to reject a settlement proposal where such combined negotiation took place. But rejection of a settlement is not automatically required in such cases -- there may be circumstances present which appear to neutralize the potential for impropriety. Such a judgment is appropriately within the sound discretion of the trial judge who can be sensitive to the dynamics of the situation. . . . (emphasis added) 4/

4/ 623 F.2d at 1353. Cf. Regalado v. Johnson, 79 F.R.D. 447, 451 (E.D. Ill. 1978).

In Mendoza, the court emphasized that the presence of the Department of Justice as an intervenor on behalf of the plaintiff class served "to protect the interests of the class against possible improper dealings," and was a "significant factor" in dampening the potential for unfair treatment of the class. 623 F.2d at 1353. Also, the court noted that it is "of some mitigating value that there was statutory authorization for an award of attorneys' fees to plaintiffs." Id. Thus, the court renounced any per se rule invalidating the settlement simply because there had been simultaneous discussion about relief and attorneys' fees.

We likewise find no basis in the cited ABA canons and disciplinary rules for the proposed per se rule. The provisions of the ABA Code on which the Washington Council of Lawyers relies 5/ generally enjoin attorneys to represent their clients honestly and without interference by a competing financial claim on the attorney's part. Also, they caution against one attorney violating the Code by means of the actions of another attorney -- which could be read to cover a situation in which one attorney purposely puts another attorney in a position to violate one of the ethical restrictions. We have no specific facts before us that would lead us to conclude that these principles had been violated in a given case. Rather, we have been asked in effect whether the Code or other applicable law always bars any simultaneous discussion of fees and relief in whatever circumstances. For the reasons cited in Mendoza, namely, that there may well be mitigating factors in any particular situation and in any event the

5/ D.R. 1-102(A)(5) (prohibiting a lawyer from engaging "in conduct that is prejudicial to the administration of justice"); D.R. 1-102(A)(2) (prohibiting an attorney from circumventing a disciplinary rule "through actions of another"); EC 5-1 (calling on an attorney to exercise his judgment solely for the client's benefit); EC 5-2 (calling on attorneys to refrain from acquiring a property right that would make him less protective of the client's interests); EC 2-17 (providing, inter alia, that adequate compensation is necessary for the lawyer to serve his client effectively).

question calls for case-by-case decision-making, we do not find support for such an across-the-board proscription in the cited Code principles.^{6/}

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Office of Legal Counsel

^{6/} Further, we note that the Manual for Complex Litigation takes the position that district court approval of class action settlements pursuant to rule 23(e) of the Federal Rules of Civil Procedure requires disclosure of both damages and attorneys' fees: "Only if the aggregate of all payments to be made by defendants is disclosed in the proposed settlement can the class members and the court make any intelligent judgment as to the fairness and reasonableness of a proposed settlement." 1 Moore's Federal Practice (Manual for Complex Litigation), Part 2, § 1.46, at 74 (1977). A bifurcated settlement procedure is in tension with this recommended approach of having a court evaluate the total settlement. Whatever may be said about this approach as a policy matter, we cannot say that it violates ABA ethical restrictions as a matter of law, at least not at the level of generality with which it deals. Cf. McDonald v. Chicago Milwaukee Corp., 565 F.2d 416, 423-26 (7th Cir. 1977); Grunin v. International House of Pancakes, 513 F.2d 114, 122 (8th Cir. 1975); Foster Boise-Cascade, Inc., 420 F.Supp. 674, 686-87 (S.D. Tex. 1976).