MEMORANDUM

FROM: Alida Kass, Chief Counsel
SUBJECT: Implications of Fee-Shifting
DATE: March 20, 2014

Fee-shifting provisions are showing up in proposed legislation in New Jersey with increasing frequency. These provisions, which allow prevailing plaintiffs to recover attorney's fees and court costs, encourage frivolous litigation, and make settlement more costly and more difficult.

Proponents argue that fee-shifting provisions enhance access to the courts for plaintiffs who might lack the resources to hire an attorney. However, for bills with largely regulatory objectives, consumers can obtain redress far more efficiently, via an administrative remedy with a schedule of fines, likely without even hiring a lawyer.

Fee-shifting provisions, on the other hand, have been interpreted by the New Jersey courts to be a legislative attempt to encourage litigation, and are given an especially expansive interpretation to that end. The New Jersey Civil Justice Institute therefore believes that fee-shifting provisions should be used sparingly, only at the request of the bill sponsor, and only in situations where litigation is necessary to resolving a dispute and compensating an injured party.

Incentive for Litigation:
In situations where the fees at issue vastly dwarf the underlying damages, it is the lawyers who have the greatest incentive to find violations and bring litigation. As a result, these provisions often create not just a remedy but an industry.

Unlike administrative enforcement which could be conducted in the public interest, creating an economic incentive for lawyers to find violations of regulatory statutes does not target enforcement in socially beneficial ways. The prospect of being held responsible for the opposing party’s legal fees over low value claims render many lawsuits impossible to defend in an economically feasible fashion. That reality incentives abuse and essentially operates as a tax on socially desirable business conduct. As a result, these provisions place significant strain on the civil justice system without significant offsetting gains in consumer protection.

Impediment to Settlement:
Fee-shifting also impedes settlement and creates potential conflicts of interest between lawyers and their clients. While the consumer hopes to obtain compensation as quickly as possible, the lawyer whose fees are being covered by someone other than his client has little incentive to settle. Valuing the case is also more difficult, especially when the largest portion of potential

liability is not the underlying value of the dispute but the degree to which billable hours have been accrued.

In addition, New Jersey has an offer of judgment rule which is designed to encourage settlement and discourage rejection of reasonable settlement offers. Fee-shifting provisions nullify this rule. Under the offer of judgment rule, should either party make a settlement offer that is rejected and the outcome is within 20% of the rejected offer, the rebuffing party is responsible for the offering party's attorney fees and court costs incurred from the time the offer was made.

This is a good rule: by encouraging settlements based on the likely value of a case, it ultimately reduces the legal expenses borne by both parties to litigation and reduces the burden on the court system. However, the offer of judgment rule *does not apply* in cases involving a fee-shifting statue. Reasoning that such provisions are meant to *encourage* litigation, the N.J. Supreme Court found that a rule designed to encourage *settlement* would run contrary to legislative intent. (*Best v. C&M Door Controls,* 2009)

As a result, legislation containing fee shifting provisions not only incentivizes more litigation in the simple sense that it dramatically reduces the costs and risks of litigation borne by the plaintiff. It also eliminates the single most powerful tool for encouraging settlement, compounding the incentives toward litigation and against resolution.

Increased costs to defendants in marginal cases:
In New Jersey, fee-shifting provisions also reward attorneys for bringing cases with the least merit.

The standard fee-shifting language authorizes the court to grant "reasonable" attorney's fees to the prevailing party. Both New Jersey and federal courts follow a "lodestar" approach to computing what is reasonable: the appropriate number of hours worked on the case, multiplied by the usual hourly rate. However, New Jersey courts are then permitted to award an "enhancement" of up to an additional 100% of the lodestar to compensate attorneys for the contingency that they might not have been paid for their work had they lost the case. (*Rendine v. Pantzer*, 1995; *Walker v. Giuffre*, 2012)

But because that contingency will be highest in those cases where there was the greatest risk of nonpayment, the most marginal of cases potentially reward the plaintiff's attorneys with the highest fees, leading to a number of perverse outcomes. First, question the equity of a defendant being forced to pay the highest fees to lawyers bringing the least meritorious cases. Secondly, the rule makes it especially difficult to value a case for settlement.

It is worth noting that the federal court system has expressly rejected contingency enhancement for fees under federal fee-shifting. In *Burlington v. Dague,* (1992) and *Perdue v. Kenny A.*, (2010), the U.S. Supreme Court noted the need for objective, predictable criteria to facilitate settlement, and clarified that "reasonable" fees should be sufficient to induce capable attorneys to undertake meritorious cases, not create a financial windfall for attorneys taking a gamble on cases of dubious merit.

Proliferation in State Legislation:

Fee-shifting provisions were initially adopted to facilitate litigation over systemic, serious, abuses such as civil rights violations. That remains the model at the federal level, as is appropriate, given the significant legal ramifications of such provisions. In the state legislature, however, these provisions are increasingly being added to bills targeting a variety of relatively narrow regulatory objectives. Bills with fee-shifting introduced this legislative session include everything from a requirement that digital records be deleted from photocopiers before the machines are discarded, to the regulation of pharmacy internet sales, to limits on rent increases on senior citizens' apartments. In many of these cases, the power of the fee-shifting creates a remedy that is out of scale with the underlying issue being addressed. Where the sponsor feels strongly that the remedy is appropriate, it should of course be included, but sponsors should understand the full extent of the legal implications that follow when the provisions are added to their bills.