PROFESSIONAL RESPONSIBILITY

LEGAL FEES AWARDED IN THE STATE TOBACCO SUITS AND OTHER MASS TORT AND CLASS ACTION CASES FACE NEW ETHICS AND LEGAL CHALLENGES

*BY MARGARET A. LITTLE**

Some recent court proceedings that have received little attention in the mainstream news media suggest that the enormous wealth transfers to trial lawyers that have taken place in the context of class action, tobacco, and other suits brought by or on behalf of government entities – usually the states – are coming under new and refreshing critical legal scrutiny. In Manhattan, Supreme Court Justice Charles E. Ramos has asked the New York attorney general's office and several law firms awarded $625 million in attorney's fees by the Tobacco Fee Arbitration Panel – reportedly $13,000 per hour – as part of New York State's $25 billion tobacco settlement to explain why this fee award should not be set aside. Justice Ramos, who has raised the issue *sua sponte*, noted that the arbitrators who awarded such enormous fees may have "manifestly disregarded well established ethical and public policies." Justice Ramos suggested that his court had the power not only to set aside the award of such fees, but to vacate the entire $25 billion state settlement, approved by another judge in 1998, if such action was warranted.[1]

At a hearing in late July, the proceedings became explosive with one attorney, Harvey Weitz, angrily shouting at Justice Ramos that he was being "sandbagged"; Mr. Weitz was later escorted from the courtroom under threat of contempt. Another attorney walked out of the proceedings and still others directed imperious demands and wounded invective at Justice Ramos — such as calling him "reprehensible." One of the few reporters to cover these proceedings described the hearing as "unparalleled for its vitriol, much of it aimed at the judge," and noted that the hearing "took on an air of unreality" with the judge becoming the butt of angry accusations and bitter complaints and the lawyers imploring him to end the inquiry, or at worst, refer the matter to the secret and largely unreviewable world of attorney disciplinary proceedings.[2] As any lawyer knows, that self-regulated arena operates in near total secrecy, lacks the jurisdiction and powers of a court and meaningful appellate review. The attorneys were particularly concerned about how the press got wind of the judge's order to show cause and argued strenuously that any proceedings should be confidential, without press or public scrutiny.

In California, citing an "unreal world of greed" in which class-action firms such as New York's Milberg Weiss Bershad Hynes & Lerach are being awarded fees in arbitration, a state appeals court upheld a trial court ruling vacating an $88.5 million fee awarded by a three man arbitration panel to Milberg Weiss and four other law firms, holding that it was an unconstitutional gift of public funds, unauthorized by law, to which neither the state, the legislature nor any court could lawfully agree.[3] In Texas, a series of judges are juggling the "political hot potato" of claims asserted by Houston attorneys Joseph Jamail and Wayne Fisher that former Texas attorney general Dan Morales had demanded a $1 million campaign contribution and the "fronting" of the state's legal expenses from any firm seeking to be awarded the job of representing the State of Texas in the tobacco suits.[4] The fees awarded to the Texas attorneys in arbitration came to $3.3 billion – or $92,000 per hour – to five law firms, all major Democratic party donors.[5]

Justice Ramos initiated his inquiry into the New York tobacco fees *sua sponte* because neither the tobacco companies paying the arbitration awards nor the attorney general's office have contested these excessive and ethically indefensible fees. This is because the tobacco companies explicitly agreed not to oppose the fee applications in arbitration as part of the tobacco settlement. Practically speaking, the attorneys presenting their claims before the Tobacco Fee Arbitration Panel are arbitrating against no one. Nonetheless, the absence of an opposing party in the fee arbitrations does not appear to be protecting these politically well-connected profiteers from judicial scrutiny. These state-sponsored lawsuits were brought in the state courts, which have plenary authority to regulate the conduct of attorneys practicing before them. And, as attorneys representing the public as special attorneys general, and as officers of the court, the attorneys owed the highest duties of loyalty and honesty to their clients. Rule 1.5(a) of the Rules of Professional Conduct provides that "[a] lawyer's fee shall be reasonable." ABA Model Code Disciplinary Rule 2-106 requires that a "lawyer shall not enter into an agreement for, charge, or collect any illegal or clearly excessive fee." The leading treatise on legal ethics notes: "The requirement that a fee be reasonable in amount overrides the terms of the contract, so that an 'unreasonable' fee cannot be recovered even if agreed to by the client."[6]

Even more fundamental, the contingency fee contracts entered into by the states with their attorneys are unlawful and unethical. State and federal case law and statutes widely recognize that attorney's fees awarded in any action belong to the party, not his attorney,[7] and that it is unlawful for any governmental agency to make or authorize an expenditure or contractual obligation without an existing legislative appropriation.[8] The purported contractual obligation to pay state funds made by the attorney general's signature on the original contingency fee contract, the obligations of which are now arbitrated before the Tobacco Fee Arbitration Panel, not only committed the state to pay the private law firms' fees and expenses in excess of appropriations, but in the absence of any appropriation at all. No state official has this power.

The contingency fee contracts also violated state codes of ethics, rules of professional conduct and constitutional limitations of power in that they conferred a direct and substantial personal financial stake in the litigation upon outside counsel prosecuting these state sovereign actions. State codes of ethics prohibit anyone performing such governmental functions from having any direct monetary gain or loss at stake by reason of his official activity.[9] Further, long-established Supreme Court law consistently holds that private entities are forbidden to perform governmental functions on a contingency fee basis because it constitutes a violation of state and federal constitutions' guarantees of due process before the law.[10] The Supreme Court has unequivocally held that the appointment of an interested prosecutor fundamentally undermines the integrity of a judicial proceeding, violates due process, and further, that the "mere existence" of such an unethical situation "calls into question the conduct of an entire prosecution."[11] Contingency fee arrangements are simply not consistent with the duty of public attorneys to pursue equity, justice and fairness on behalf of the people they represent.

The importance of this rule regarding legislative approval and oversight of such contracts and gifts to the open and ethical conduct of our political branches is obvious. One of the most disturbing consequences of these contingency fee agreements occurred when Maryland's contingency fee counsel, Peter G. Angelos, bartered half of his 25 percent contingency fee in exchange for retroactive changes in the law that would assure him a win in court:

> Mr. Angelos…agreed to accept 12.5 % if and only if we agreed to change tort law, which was no small feat. We changed centuries of precedent to ensure a win in this case. [12]

Peter Angelos essentially purchased the law that would be applied to his case – with the state's own money.

Given these manifold illegalities and constitutional infirmities, it is far easier to see why these fee awards should be vacated than to put forth any justification for them. Perhaps this is why, when Fox News invited legal affairs commentator and Manhattan Institute fellow Walter Olson, a long-time critic of these class action and tobacco fees, and the attorneys receiving the fees and/or a representative of the American Trial Lawyers Association to debate the question, only Mr. Olson was willing to appear.[13]

Indeed, the state attorneys general tacitly understood that their original fee contracts were unenforceable when, in 1998, they awoke to the fact that the mind-boggling 25% fee typically awarded under the contracts, or the transfer of some $61.5 billion dollars of a $246 million settlement to private citizens (and in most cases their political cronies), was simply politically untenable. The state attorneys general openly took the position that they were no longer bound by the contracts. While lawsuits to enforce the contracts proliferated, most of the private attorneys agreed as part of the settlement, to seek their fees, at least in the first instance, in arbitration in which the tobacco companies were bound not to oppose the application.

Nearly every disinterested commentator that has taken the time to bring some transparency to these proceedings has come to understand that the fee arbitration is a subterfuge, a secretive process that shields from public view distribution of funds belonging to the state extracted from the tobacco companies through the exercise of the state's enforcement powers. Public health advocates that had been so crucial to the success of the state lawsuits have consistently leveled sharp criticisms at the legal fees, noting that they are totally out of control.[14] A permanent class of state-enriched tycoons has been established using public funds. Nationwide, these lawyers, many of whom bankrolled the attorneys generals' political campaigns, will split a $750 million pot every year during the first five years of the settlement, which then declines to $500 million annually payable for untold years to come. Further, even the mainstream press has come to understand that the Master Settlement Agreement has been cynically used as an off-budget revenue cash cow funding otherwise unbudgeted state programs that increase the size of state government with no budgetary controls. In at least in one state, North Carolina, close to 73% of the funds paid to date are being spent on tobacco marketing and production.[15]

What is less generally understood is that the suits and their settlements should be found to violate the federal constitution's taxation, commerce and compacts clauses (among others), their own state laws and constitutional doctrines of separation of powers. The MSA has created a tobacco cartel with the state managing the diversion of the cartel's monopoly profits into their own treasuries, the hands of the trial lawyers and the tobacco companies. Smaller companies that did not consent to the agreement and new market entrants, who did not even exist at the time of settlement and have engaged in no misconduct, are required under the settlement agreement to pay huge damages into escrow to cover any future liability from smoking related illnesses. These barriers to entry for new market entrants and non-settling tobacco companies were obviously designed to prevent such companies from undercutting the collusively raised tobacco prices and diminish, or extinguish, the market share of the big tobacco companies and to protect the flow of the cartel profits to the states, their attorneys and the tobacco companies. As law professor Michael DeBow has noted: "In a nutshell, the tobacco litigation meant *de facto* increases in cigarette taxes, obscene enrichment of politically connected trial lawyers, and states acting as cartel managers for giant cigarette makers."[16] The MSA represents an agreement among the states to repeal the Sherman Act for the tobacco industry and further effectively levies interstate taxation and imposes interstate regulation beyond the territorial reach of the states. The compacts clause of the federal constitution provides that "[n]o state shall, without the consent of Congress…enter into any Agreement or Compact with another State," and the taxation and commerce clauses grant Congress the exclusive power to levy national taxes and regulate interstate commerce.

The effects of these state-sponsored redistributions of wealth to a core group of politically well-connected lawyers are certain to affect judicial appointments and elections. Economists at Emory University who have been studying the legal profession over the decades note that the law has come to

favor the economic interests of attorneys, and they add that lobbying a legislature with respect to a particular industry is less effective than lobbying to obtain favorable appointments or elections of judges, because greater economies of scale apply to a judiciary that can change the law on any issue the lawyers bring before them.[17]

The class-action, mass tort and tobacco lawyers are collecting billions of dollars and openly announcing their intention to expand their prosecution of these mega-torts to new industries. They are routinely hired by the state attorneys general that made them millionaires or billionaires, with the states' attorneys general unleashing them on the asbestos, firearms, lead paint, latex, and HMO industries. New York State Comptroller, H. Carl McCall was just recently reported to have hired three firms, including Milberg Weiss, to sue industries on behalf of the state in matters where the fee awards have in some instances come to more than $10,000 per hour.[18]

These lawyers are among the most generous contributors to political and judicial candidates. From 1999 to the beginning of 2002 contributions from trial lawyers to candidates of all political parties reportedly totaled close to $13 million, with tobacco settlement lawyers prominent among the top givers.[19] Former President Clinton's videotape in support of the $3.4 billion fee application by the consortium of attorneys (that came to include his brother-in-law, Hugh Rodham), who were seeking fees for early-settling states including Florida and Texas was reported last year.[20] Democratic National Committee chairman Don Fowler's 1995 call sheet to solicit long-time Democratic donor Walter Umphrey, one of the Texas lawyers who was awarded the tobacco work, read "Sorry you missed the vice president: I know [you] will give $100K when the President vetoes tort reform, but we really need it now. Please send ASAP if possible."[21] President Clinton vetoed federal tort reform legislation in the spring of 1996.

Inevitably some large portion of these fees will get channeled back to candidates who are committed to the expansion of this disturbing recent phenomenon of regulation by litigation. Democratic Senator Joseph Lieberman, a supporter of tort reform, has characterized trial lawyers as "a small group of people who are deeply invested in the status quo, who have worked the system very effectively and have had a disproportionate effect."[22]

This new phenomenon of state-sponsored regulation by litigation reflects a profound cultural illiteracy with respect to our state and federal laws and constitutions, even, or perhaps one should say especially, among many who possess a legal education. These new judicial inquiries and recent opinions represent a hopeful turn in this dangerous development in our political and legal affairs of state-sponsored litigation pursued in open contempt of the citizens' state and federal laws and constitutions. These inquiries also represent the fulfillment of observations made in 1999 by Palm Beach County Circuit Judge Harold J. Cohen, the presiding judge in the Florida governmental tobacco case, when he called the Florida fee demands "unconscionable" and presciently warned that "[i]f you ever put any of these issues to a public vote, they will come down hard on the lawyers and on the courts… . [t]he reverberations go way beyond this case."[23] At the time of the tobacco settlement, former Health Education and Welfare Secretary Joseph Califano acidly observed that the lawyer's fees in the tobacco settlement represent "the most sordid piece of money-changing in the temple of the American bar."[24] The outrageous courtroom misbehavior and vitriol directed towards the Manhattan judge questioning these arrangements and the attorneys' desperate pleas for secrecy reflect nothing more than a visceral acknowledgement that these transactions will not withstand public scrutiny and judicial oversight and review. Of course these inquiries should take place in court before judges sworn to uphold the laws and constitutions of this nation and who are members of an independent constitutional branch and are publicly accountable and subject to press oversight and appellate review.[25] It is precisely the backroom dealmaking and secrecy in which these settlements, fee agreements and arbitrations were engineered that has led to these fee debacles. A wit once noted that "greed, like the love of comfort, is a kind of fear"[26] and as Edmund Burke has amplified, "[n]o passion so effectually robs the mind of all its powers of acting and reasoning as fear."[27] At long last, it looks as if the judiciary is starting to scrutinize this scandalous blot on the American legal landscape. One can only hope that these courts and judges will have the courage and wisdom to cast a fearless eye on these arrangements and rise above efforts at invective and intimidation by financially interested parties hopelessly entwined in these unethical, unlawful and unconstitutional affairs.

Editor's Note:

As this article was going to press, a September 27, 2002 report in The New York Law Journal reported that a nearly $1.3 billion attorney fee award to a consortium of attorneys in the California tobacco litigation issued by an arbitration panel in connection with the 1998 nationwide settlement of state litigation against the tobacco industry was overturned on September 25th by Manhattan Supreme Court Justice Nicholas Figueroa. The judge noted that the amount of the award was "irrational" and that the arbitrators had exceeded their powers in awarding this sum to the consortium.

Sources: Daniel Wise, *$1.3 Billion Tobacco Attorney Fee Overturned,* New York Law Journal, 9/27/02; William McQuillen *Court Throws Out $1.25 Billion Award to California Tobacco Lawyers,* Bloomberg.com, 9/26/02.

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Footnotes

1. Daniel Wise, New York Law Journal, 6/20/02 and 7/12/02. The three New York law firms defending their 45% of the $625 million fee award are Schneider, Kleinick, Weitz, Damashek, & Shoot ($98.4 million), Sullivan Papain Block McGrath & Cannavo ($98.4 million) and Albany law firm, Thuillez, Ford, Gold & Johnson ($84.3 million). The three national firms awarded the remaining $343.8 million of fees in the New York settlement are Ness, Motley, Loadhoalt, Richardson & Poole, of Charleston, S.C., The Scruggs Law Firm of Pascagoula, Miss. and Hagens & Berman of Seattle, Wash. *See also*, *Tobacco Settlement a Windfall for Lawyers,* Fox News, 8/01/02.

2. Daniel Wise, *New York Tobacco Fee Hearing Has Lawyers Smoking,* New York Law Journal, 7/26/2002.

3. *Jordan v. California Dept. of Motor Vehicles,* 2002 Cal. App. LEXIS 4421.

4. Clay Robison, *Morales' Tobacco Fee Under Fire,* Houston Chronicle 7/12/02, JoAnn Zuñiga, *Judge Delays Decision on Questioning Lawyers About Fees in Tobacco Case,* Houston Chronicle 8/13/02. *See also* Daniel Fisher, *Smoke This*, Forbes 8/15/02.

5. Marianne Lavelle & Angie Cannon, *A Handful of Trial Lawyers Are Rocking CEOs and Politicians,* U.S. NEWS & WORLD REP., Nov. 1, 1999, at 36 (reporting that "[l]awyers representing the first three states that settled—Florida, Mississippi, and Texas—were awarded $8.2 billion in legal fees"); Bob Van Voris, *That $10 Billion Fee*, NAT'L L.J., Nov. 30, 1998, at A1 (reporting that in Texas the hourly rate in the tobacco settlement was calculated at $92,000 per hour).

6. G. Hazard, Jr. & W. Hodes, The Law of Lawyering 1, 5:205 *Fee Litigation and Arbitration,* at 120 (1998 Supp.).

7. *Venegas v. Mitchell,* 495 U.S. 82, 87-88 (1990); *Erickson v. Foote*, 112 Conn. 662, 666 (1931) ("The costs allowed in an action belong to the party and not to his attorney.") ; *See also, Brown v. General Motors Corp.* 722 F.2d 1009, 1011 (2d Cir. 1983) (The prevailing party, not the attorney is entitled to award of attorneys' fees.) 7A C.J.S. *Attorney and Client* §283 (1980) ("A judgment for costs and attorney's fees is the property of the client, and not the attorney.)

8. State law uniformly provides that state funds may only be expended through the appropriations process. 63 Am.Jur.2d Public Funds §37 (1984) ("The power of the legislature with respect to the public funds raised by general taxation is supreme, and no state official, not even the highest, has any power to create an obligation of the state, either legal or moral, unless there has first been a specific appropriation of funds to meet the obligation….The object of such [legal] provisions is to secure regularity…in the disbursement of public money, and to prohibit expenditures of public funds at the mere will and caprice of those having the funds in custody, without direct legislative sanction therefor.") This firm rule applies equally to all state funds and not just funds raised through taxation. *See, e.g.,* 81A C.J.S. States, §233 (1977)("General funds, available for general state purposes, which are deposited in the state treasury, are subject to constitutional requirements as to appropriations with respect to their disbursement, and this is true regardless of the source from which such funds are derived.")

9. *See, e.g.,* 63A Am.Jur.2d *Prosecuting Attorneys* § 20 (1984). ("Those powers and duties imposed upon a prosecuting attorney by law which require the exercise of judgment and discretion…cannot be delegated to another without express legislative authority."). *Young v. United States,* 481 U.S. 787, 804, 809-10 (1987).

10. *Marshall v. Jerrico, Inc.,* 446 U.S. 238, 249-50 (1980); 63C Am.Jur.2d *Prosecuting Attorneys* §26 (1997) ("A trial court has the power to disqualify a prosecuting attorney…where he or she has a pecuniary interest in the outcome.") For a recent application of this constitutional principle, see, *Yankee Gas Company v. City of Meriden,* 2001 Conn. Super. LEXIS 1119.

11. *Young v. United States*, 481 U.S. at 808-814 (1987).

12. Statement of Maryland State Senate President Thomas V. Mike Miller, Jr. reported in Daniel LeDuc, "Angelos, Md. Feud Over Tobacco Fee, $4 Billion Payout to State Will Be on Hold as Lawyer Argues for 25%," *Washington Post*, Oct. 15, 1999, B1. Ironically, despite the public announcement of this 12.5% fee surrender to purchase the retroactive law that would assure him of a win in his case, Mr. Angelos persisted in seeking the entire 25% fee, or $1 billion, and only recently resolved his fee claim with the state.

13. *Tobacco Settlement a Windfall for Lawyers,* Fox News, August 1, 2002.

14. David Kessler has described the lawyer fee requests as "outrageous. . . [a]ll the legal fees are out of control." Barry Meier, *Case Study in Tobacco Law: How a Fee Jumped in Days*, N.Y. TIMES, Dec. 15, 1998, at A16. (Noting that one firm, Milberg Weiss Bershad Hynes & Lerach, raised its fee request for public relations work attacking Joe Camel from $50 million to $650 million; "Rightly or wrongly," said the attorney, "I decided to ask for hundreds of millions of dollars so that I won't be crushed by the amounts other people were asking for." That attorney stated that he would be "crazy" not to take his fees into arbitration given the prior awards.).

15. Seth Mnookin, *The Tobacco Sham*, Newsweek 8/19/02, p.33.

16. Michael DeBow, *Out of Control AGs,* National Review, 5/21/2002.

17. Paul H. Rubin & Martin J. Bailey, *The Role of Lawyers in Changing the Law,* 23 J. Legal Stud. 807, 813, 827 (1987).

18. Shaila K. Dewan, *Donors to McCall Profit in Cases State Pursues Against Corporate Wrongdoers,* N.Y. Times, 8/14/02 p. B4. The three law firms, Bernstein Litowitz Berger & Grossmann, of New York, Barrack, Rodos & Bacine of Philadelphia and Milberg Weiss of New York are all major contributors to Comptroller McCall's campaign for candidacy for governor of New York.

19. American Tort Reform Foundation, *Tracking the Trial Lawyers,* available at http://atrf.trkcinc.com.

20. Barry Meier, *Rodham and Group Seeking Legal Fees Uses Clinton Testimonial*, N.Y. TIMES, Mar. 8, 2001, at A15.

21. Kate O'Beirne, *Cash Bar – How Trial Lawyers Bankroll the Democratic Party,* National Review, August 20, 2001.

22. Id.

23. John Gibeaut, "Getting Burned" *ABA Journal,* Sept. 1998, 44. In the 1999 Florida proceedings, Judge Cohen denounced the state's twenty-five percent contingency contract that came to $233 million per lawyer, which "shocked the conscience of the Court." He calculated that if the state's lawyers had worked twenty-four hours per day, seven days per week for the forty-two months they had represented the state, they still would earn $7,716 per hour. "No evidentiary basis can possibly exist for fees of that nature and this Court can never enter an order justifying such hourly rates on any grounds." *Id.*

24. Joseph A. Califano, Jr., *Tobacco: The Moral Issues,* America, August 15, 1998.

25. As Justice Ramos noted, the requirement that a *judge* review and approve a fee award in a class action is "a slam dunk." *Supra*, note 2. Fee awards under class action, trade regulation and other statutory enforcement proceedings are routinely subject to judicial review.

26. Cyril Connolly, *The Unquiet Grave,* pt.1 (1944).

27. Edmund Burke, *The Origin of our Ideas of the Sublime and Beautiful,* pt.2, ch.2 (1756).