



Attorney fee awards and the common fund doctrine: Hands in the plaintiffs' pockets?

With the expansion of the common fund doctrine has come the diminishment of ethical and statutory requirements governing recovery of attorney's costs and fees.

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The right to attorney's fees

Under the American Rule, parties generally bear their own costs of litigation, and the attorneys and client ordinarily negotiate a rate at which they will work. There is an established practice in the private legal market to reward attorneys for taking the risk of non-payment by paying them a premium over their normal hourly rates for winning contingency cases.¹ Contingent fees that may far exceed the market value of the services if rendered on a non-contingent basis are accepted in the legal profession as a legitimate way of assuring competent representation for those plaintiffs who could not afford to pay on an hourly basis.² If this methodology did not exist, few lawyers could afford to represent clients given the investment of substantial time, effort, and money, especially at the risk of recovering nothing.³

The well-established and oft-described "exception" to the American Rule is the common fund. In fact, however, the fund is consistent with the American Rule in that it does not tax the losing party with the victor's attorney's fees.⁴ The United States Supreme Court created the common fund doctrine, as a source of attorney's fees. If attorneys' efforts create a

fund or benefit for others in addition to their own client, the court is empowered to award fees from that fund.⁵

The doctrine of compensating an attorney from a fund created or preserved by an attorney's services is most often applied in class actions, where an attorney or attorneys acted on behalf of a plaintiff who recovered a fund as a representative of the interests of a group of individuals. This doctrine, however, is not limited to class actions, and has long been applied beyond such cases.

The common fund doctrine is based upon equitable principles

An attorney's right to common fund fees arises from equitable principles of restitution. The common fund "exception" to the American Rule is grounded in the equitable powers of the courts under the doctrines of quantum meruit and unjust enrichment. An award of attorney's fees from a common fund depends on whether the attorney's specific services benefited the fund – whether they tended to create, increase, protect or preserve the fund.

Unlike statutory fee-shifting cases, where the winner's attorney's fees are paid by the losing party, attorney's fees in common fund cases are not paid by the losing defendant, but by members of the

plaintiff class, as it may be, who shoulder the burden of paying their own counsel out of the common fund. How the fund is divided between members of the class and class counsel should be of no concern whatsoever to the defendant(s) who contributed to the fund.

Although the common fund doctrine does not permit the *shifting* of the burden of the litigation expenses to the losing party, it does permit the burden to be *shared* among those who are benefited by the litigant's efforts.⁶ The doctrine rests on the understanding that those who obtain the benefit of a lawsuit without contributing to its costs are unjustly enriched at the successful litigant's expense. Such an inequitable result is easily avoided if a court has control over the fund – even one created pursuant to a settlement – and assesses the litigation expenses against the entire fund so that the burden is spread proportionally among those who have benefited.⁷

Courts have held that class members other than the representative plaintiffs can avoid court-awarded fee disbursements from their portion of the fund by hiring their own attorneys and participating in the litigation. The represented class member enjoys this immunity because one who hires and pays his own lawyer is not a free rider if the attorney is a contributor to the final results.⁸ In other



words, the ride for that litigant is not free and has, in fact, contributed to the final result.

The Second Circuit recently declared that the common benefit fund is a holdback, not a levy.⁹ And that the holdback amount represents the maximum that plaintiffs' counsel may receive from the fund.¹⁰ Regardless, a lawyer is not entitled to compensation from a common fund for work the attorney did not perform or hours he did not spend.¹¹ Nor is an attorney entitled to compensation for hours a reasonable lawyer would not have spent, hours unreasonably spent, or work done so poorly that it is of no value to the common benefit.¹² Because the fund is a set-aside and not a disbursement, no amounts are paid to attorneys from the set-aside fund until the attorneys demonstrate that they have worked for the common benefit.¹³

The origins of the common fund doctrine

In 1881, the United States Supreme Court recognized that a litigant or a lawyer who recovers a common fund for the benefit of persons other than himself or his client is entitled to reasonable attorneys' fee from the fund.¹⁴ In *Trustees v. Greenough*, a creditor sued on behalf of himself and other creditors for his and their own benefit in order to reclaim and rescue a trust fund. The Court found that not allowing reimbursement, either out of the fund itself, or by proportional contribution from those who accept the benefit of his efforts, would "not only be unjust to him, but it would give to the other parties entitled to participate in the benefits of the fund an unfair advantage."¹⁵

Over 50 years later, in *Sprague v. Ticonic Nat'l Bank*,¹⁶ the plaintiff who prosecuted litigation to a successful conclusion, from which other persons would benefit, petitioned the district court for allowance of attorney's fees and expenses. The Court found that while the party neither purported to sue for a class

nor formally established a fund for the class, its discretion allowed for the grant of reimbursement(s) under equitable grounds. The Court reasoned that when such a fund is for all practical purposes created for the benefit of others, the formalities of the litigation – the absence of an avowed class suit or the creation of a fund – hardly touch the power of equity in doing justice as between a party and the beneficiaries of his litigation.¹⁷ The Court held that reimbursement was permitted under equitable principles and reversed the lower court's ruling.

The doctrine was again discussed by the United States Supreme Court in *Boeing Co. v. Van Gemert*, *supra*. In *Boeing*, a class action was initiated to recover for Boeing's failure to give adequate notice of intention to call convertible debentures. The district court ordered Boeing to pay a sum of money and assessed undetermined attorney fees against the entire fund. Boeing appealed, arguing it stripped it from any present interest in the fund. The Court found that the doctrine reflects "the traditional practice in courts of equity" and rests on the perception that persons who obtain the benefit of a lawsuit without contributing to its cost are unjustly enriched at the successful litigant's expense.¹⁸ Most significantly, the Court held that jurisdiction by the Court over the fund would prevent this inequity or impliedly, any inequity.

Designating counsel who will benefit from the fund

Multiparty litigation requires that the court establish certain committees of counsel in an effort to coordinate litigation activities. Courts traditionally appoint lead and liaison counsel and management committees. Committees are most commonly required when group members' interests vary. The functions of the various committees and counsel are often set forth in a court order or separate document for judicial approval. It is essential that the scope and responsibility of the designated counsel's authority be delineated to avoid any unnecessary in-

ternal disputes between plaintiffs and/or plaintiffs' counsel. Obviously, counsel in these leadership groups should keep other counsel informed and advised on the progress of the litigation and any settlement negotiations or resolutions.

Such committees receive compensation for their services to the other members and their counsel. Early in the litigation, it is advisable for the court to determine the method of compensation, including establishment of a fund to which designated parties should contribute specified proportions. It is without question that a court has the power to award fees from a common fund to designated counsel who performed tasks on behalf of the group.

Designated counsel's fiduciary and ethical duty to their client

Counsel designated by the court assume a responsibility to the court and an obligation to act fairly, efficiently, and economically in the interests of all parties and parties' counsel.¹⁹ Additionally, Mode Rule of Professional Conduct Rule 3.2 requires lawyers to make "reasonable efforts to expedite litigation consistent with interests of the client."

Committees made of counsel representing individual plaintiffs and their attorneys assume a "fiduciary-like" appointment. They accept fees and represent both individual plaintiffs and their attorneys. "Whether or not there is a direct or formal attorney-client relationship between plaintiffs and the [Committee], the [Committee] and its [individually retained plaintiffs' attorneys] members necessarily owed a fiduciary obligation to the plaintiffs."²⁰

In cases where a dispute arises among those vying for a share of the common fund, a special fiduciary obligation is placed on the court because beneficiaries are unrepresented in such a dispute.²¹ Accordingly, a conflict arises between plaintiffs and appointed counsel and the court must assume a fiduciary obligation to protect the interests of plaintiffs.



Further, Rule 1.8(a) prohibits a lawyer from knowingly acquiring an ownership, possessory, security or other pecuniary interest adverse to a client *unless* among other things, the terms of the transaction are fair and reasonable and “are fully disclosed and transmitted in writing to the client in a manner which can be reasonably understood by the client.” While the Rule does allow a lawyer to “advance court costs and expenses of litigation, the repayment of which may be contingent on the outcome of the matter,” this does not, on its face, include attorney’s fees. Any committee’s attempt to obtain fees in excess of what is reasonable, particularly without Court approval, shows a lack of consideration for the duty of trust between lawyer and client that finds expression in Rule 1.8(a).

In addition, Rule 1.5 provides that a lawyer *shall* not make an arrangement for, charge, or collect an unreasonable fee or unreasonable amount for expenses. The prohibition on acquisition of a proprietary interest in a litigation has its basis in common law concepts of champerty and maintenance. It is a rule intended to prevent conflicts of interest between lawyer and client that could interfere with the lawyer’s exercise of free judgment on behalf of the client.

Twenty years ago, the Second Circuit addressed a conflict that arose when certain members of a class committee made an agreement to receive threefold on their investment out of the fee settlement. In *Agent Orange Product Liab. Litig.*,²² the court found such an agreement invalid and would not allow enforcement in view of its potential for

creating conflict between counsel and the class of plaintiffs. The court found that in reviewing the agreement, which was upheld by the district court, the effect that such an agreement could have on the rights of a class must be considered.

Attorneys have a duty to not only ensure that the court passing on the fee application has all the facts but also a fiduciary duty not to overreach. The agreement in *Agent Orange Product Liab. Litig.* provided an incentive for the committee to accept an early settlement— an incentive that compromised the class’s interest. The court concluded that a risk for such an adverse effect on the settlement process provides adequate grounds for invalidating the agreement as being inconsistent with the interests of the class.

Conclusion

While judicial solicitude for the interests of the legal profession have long supported recovery of fees on the theory of a common fund, conflicting interests may arise between client and counsel. Recovery on the basis of common fund is based on principles of restitution, which is best implemented by placing the court in control of the fund for distribution to claimants and counsel. With the expansion of the common fund doctrine has come the diminishment of ethical and statutory requirements governing recovery of attorney’s costs and fees. While the law of restitution allows for counsel to recover for the cost of securing a successful resolution, it does not permit counsel to be unjustly enriched at the expense of the client.

Endnotes:

¹ *In re Washington Public Power Supply System Securities Litigation*, 19 F.3d 1291, 1299 (9th Cir. 1994).

² *Ibid*

³ *Id.* at 1300.

⁴ *Boeing Co. v. Van Gemert* (1980) 444 U.S. 472, 481.

⁵ *Boeing Co.* (1980) 444 U.S. at 478; *Sprague v. Ticonic Nat’l Bank* (1939) 307 U.S. 161, 167; and *Trustees v. Greenough* (1882) 105 U.S. 527.

⁶ *Paul, Johnson, Alston & Hunt v. Gaulty*, 886 F.2d 268, 271 (9th Cir. 1989).

⁷ *Ibid.*

⁸ *In re Air Crash Disaster at Florida Everglades* (5th Cir. 1977) 549 F.2d 1006, 1019.

⁹ *In re Zyprexa Prods. Liab. Litig.* (2d. Cir. 2006) 467 F.Supp.2d 256, 266.

¹⁰ *Id.* at 267.

¹¹ *In re Coordinated Pretrial Proceedings in Petroleum Products Antitrust Litig.* (9th Cir. 1997) 109 F.3d 602, 608.

¹² *Ibid.*

¹³ *Turner v. Murphy Oil* (E.D.La 2006) 422 F.Supp.2d 676, 681.

¹⁴ *Trustees v. Greenough* (1881) 105 U.S. 527, 533.

¹⁵ *Id.* at 532.

¹⁶ 307 U.S. 161 (1939).

¹⁷ *Id.* at 167.

¹⁸ 444 U.S. at 478.

¹⁹ *Manual for Complex Litigation* § 10.221 (2007).

²⁰ *In re San Juan Dupont Plaza Hotel Fire Litig.* (1st Cir. 1997) 111 F.3d 220, 234, citing *In re Agent Orange Prod. Liab. Litig.* (2d Cir. 1987) 818 F.2d. 216, 223 (noting that lead counsel owes fiduciary duty to class plaintiffs).

²¹ *In re Wash. Pub. Power*, 19 F.3d at 1302.

²² 818 F.2d 216 (2d. Cir. 1987).

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