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EARLY OFFERS AS CONTINGENT FEE REFORM

*Jeffrey O'Connell**

Do contingent fees in personal injury cases pose enough of a problem to warrant significant reform, either by legislation or court rule? In thinking about the need for reform in any area, one must admittedly keep in mind the dangers of unanticipated second and third order effects from change. Thus, a problem must be significant indeed in order to justify significant reform.

So, is there a significant problem? If so, what kind of significant reform will improve things? After extensive empirical research (by his own admission on a shaky database) Professor Herbert Kritzer seems of two minds as to whether there is a problem.¹ The thrust of his remarks seems at best doubtful about the extent of the problem, but then he abruptly turns around and proposes some very drastic reforms which will cause gross upheavals in the way payment is to be made for legal services to personal injury claimants. For example, Professor Kritzer proposes that nonlawyers be allowed to compete with lawyers in settling personal injury cases.² Already, however, there are many and widespread complaints of the activities of lawyers (and their agents) insensitively harassing accident victims in order to represent victims' claims. Already the airwaves are filled with annoying ads by lawyers to actual and potential accident victims trumpeting lawyers' claims services. Professor Kritzer apparently wants much more of all of this—indeed under his proposal we will probably not only get much more of it, but it will also be implemented more insensitively by individuals *totally* unconstrained by *any* professional canons of ethics.³ Witness, for example, complaints by high school and college athletes of the intrusive tactics by would-be agents to repre-

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1. Herbert M. Kritzer, *The Wages of Risk: The Returns of Contingency Fee Legal Practice*, 47 DEPAUL L. REV. 267 (1998); see George C. Leef, *Lawyer Fees Too High? The Case for Repealing Unauthorized Practice of Law Statutes*, 21 REG. 33 (1997).

2. Kritzer, *supra* note 1, at 308-09 & n.120.

3. Cf. Nina Bernstein, *Battles over Lawyer Advertising Divide the Bar*, N.Y. TIMES, July 19, 1997, at A1 (describing the "patchwork" of state rules regulating lawyers' advertisements).

sent them in contracts for professional football or basketball. Witness too, the countless interruptions of so many of us by phone calls from stockbrokers and other financial consultants importuning us to take over our investments.⁴ Witness also the activities of claims adjusting services which purport to represent insureds in their fire insurance claims—activities that stain such personnel as the lowest level in the whole insurance chain (none too imposing at the top).⁵ Query: Even assuming the abandonment of limitations on the unauthorized practice of law as to personal injury cases is politically feasible (*very* doubtful for the above and other reasons), is *this* a solution to the current problems engendered by the personal injury contingent fee?

But at least Professor Kritzer is sufficiently concerned about the inadequacies of the present operation of the contingent fee to indicate that consumers are not being given sufficient information so as to exact fair fees from counsel.⁶ And Professor Kritzer is not alone at this Symposium in pointing to the lack of information to the legally unsophisticated injury victim vis-à-vis the professionally trained lawyer as a key problem. But as Malcolm Wheeler tells us in his perceptive remarks, even very sophisticated business clients dealing with business problems (the parameters of which are often more certain than personal injury claims) find it extremely difficult, if not impossible, to bargain with precision for contingent or other legal fees.⁷ The variables, Mr. Wheeler indicates, are just too vast. So simply increasing the information to personal injury claimants is surely no solution, Wheeler says, even assuming the personal injury lawyer can be given an incentive to provide it.⁸ Ex ante even personal injury lawyers themselves may lack sufficient information to fairly appraise, at the moment of hire, the value of their services. Thus, the ex ante solution of more information seems chimerical.

So, in turn, even by Professor Kritzer's somewhat begrudging acknowledgment, there seems to be a problem of overreaching by con-

4. "Complaints about unsolicited 'cold calls' from stockbrokers selling investments rose 23% during the first six months of [1997] . . . from a year earlier, the SEC said. An SEC study [also] found that these phone calls make up the fastest-growing category of investor complaints." *Digest*, WASH. POST, Sept. 23, 1997, at C1.

5. Peter Hellman, *Your Policy Is Hereby Canceled*, N.Y. TIMES, Nov. 8, 1970, § 6 (Magazine), at 32, 126. All this is not to say that there may not be other means of lessening lawyer oligopoly. I hope to make some proposals concerning this shortly.

6. Kritzer, *supra* note 1, at 289-90.

7. Malcolm Wheeler, Comments at the Third Annual Clifford Seminar on Tort Law and Social Policy (April 4, 1997). Wheeler is a lawyer with the firm of Pacel, Mauro, Hultin, and Spaanstra in Denver, Colorado.

8. *Id.*

tingent fee lawyers⁹—and that is certainly the position of knowledgeable and unbiased critics such as Derek Bok, former President and Law School Dean of Harvard.¹⁰

Two candid admissions made at this Symposium by eminent personal injury lawyer Robert Clifford would seem to buttress that view.¹¹ If the incentives currently engendered by the contingent fee cause lawyers even in dealing with themselves to openly and grossly violate their own canons of ethics, there would indeed seem to be a problem. Clifford admits that contingent fee personal injury lawyers are unilaterally and improperly robbing Peter to pay Paul: overcharging some clients in order to undercharge others.¹² Now some cross subsidization is inevitable in pricing many types of services. But when charges of a third or more of recovery are admittedly being improperly charged by professional fiduciaries, that has to be a cause of great concern for the profession thus misbehaving and for society in general. Furthermore, query whether contingent fee lawyers generally do pass the excessive fees charged to some claimants on to still other claimants as opposed to retaining the improper gains for themselves. Such eleemosynary behavior is “inconsistent with the routine process by which attorneys screen prospective clients to determine whether the risk-reward ratios of accepting each new case . . . [are] favorable.”¹³ Moreover, even assuming such cross subsidies take place, attorneys could not justify them any more than they could falsely double the claimed time spent on behalf of hourly rated fee clients on the grounds that this practice generates increased pro bono service by the overcharging attorney. Robbing Peter to (maybe) pay Paul is simply inconsistent with the attorney’s fiduciary duty to deal fairly with each of his or her clients.¹⁴

Secondly, Clifford alludes to the practice of personal injury trial lawyers unfairly rebating one-third of their own one-third fees to lawyers who refer cases to them.¹⁵ Under the canons of ethics, such referral fees can only be justified by the bona fide efforts of the referring

9. Kritzer, *supra* note 1, at 285-90.

10. DEREK BOK, *THE COST OF TALENT* 140 (1993). For further criticism of Professor Kritzer’s work, see *Hearings on Liability Reform Before the Subcomm. on Telecomm., Trade and Consumer Protection of the House Comm. on Commerce*, 105th Cong. (1997) (testimony of Lester Brickman).

11. Robert Clifford, Comments at the Third Annual Clifford Seminar on Tort Law and Social Policy (April 4, 1997). Clifford is the founding attorney of the Clifford Law Offices in Chicago, Illinois.

12. *Id.*

13. LESTER BRICKMAN ET AL., *RETHINKING CONTINGENCY FEES* 23 (1994) (citation omitted).

14. *Id.*

15. Clifford, *supra* note 11.

lawyer in aiding in the actual prosecution of the case.¹⁶ But, as Clifford candidly admits, such efforts by the referring attorney are almost uniformly fictitious. The only service the referring lawyer performs is the routine forwarding itself. If lawyers are thus routinely behaving unethically by their own lights as between each other, one is entitled, is one not, to question how ethically they are behaving toward non-lawyers in matters (such as the size of the fee) where there is an obvious conflict of interest? A corollary of such rebates, after all, is that there is so much padding in the fee charged by the actual trial attorney that there is plenty left over to pay the referring attorney relatively lavishly for services not rendered.

Such referrals do not seem to bother Professor Bruce Hay in his intriguing remarks at this Symposium.¹⁷ (Hay did not address the problem that they are in naked violation of the canons of ethics.)¹⁸ At least, he argues, such referrals provide an incentive on the part of the relatively inexperienced referring lawyer to forward the case to a more expert one.¹⁹ But here, Professor Hay seems at odds with his Harvard

16. The ethical quicksand presented by so-called referring fees was "revealed in an embarrassing case in Miami." JEFFREY O'CONNELL, *THE LAWSUIT LOTTERY: ONLY THE LAWYERS WIN* 143 (1979).

Attorney Edward Strickland received a "forwarding fee" of \$25,333 from a leading personal injury lawyer, Perry Nichols. Nichols had won a \$190,000 verdict for a widow whose husband had been killed in an automobile accident. Nichols took the standard 40 percent, or \$76,000, with Strickland getting the customary one-third of Nichols's fee for forwarding the case. The sticking point was that Strickland was a judge and thus was violating the law if he was practicing law on the side. Caught in this bind, Strickland resorted to honesty about how little a forwarding lawyer does. He protested that "the mere referral of the case on the telephone did not take one minute. I played no part in the case, gave no advice, prepared no pleadings." Thus his defense was in effect that referring a case does not rise to the dignity of practicing law! [True enough,] . . . but it took a strange twist of affairs to get . . . [such an admission].

Id. at 143-44 (quoting MURRAY TEIGH BLOOM, *THE TROUBLE WITH LAWYERS* 144 (1968)).

17. Bruce Hay, Comments at the Third Annual Clifford Seminar on Tort Law and Social Policy (April 5, 1997). Hay is a Professor of Law at Harvard Law School.

18. *Id.*

19. *Id.* The problems of *not* referring a case are illustrated by lawyers who will hold onto a case without being experienced in personal injury practice and will thereafter negotiate or litigate the matter without being qualified to do so.

One of the most respected federal trial judges in the country—formerly a leading trial lawyer as well as scholar—commenting . . . on Chief Justice Burger's estimate that one-third to one-half of American lawyers are not properly qualified for trial advocacy, said that:

[T]he biggest cause of inept trial lawyering is the non-personal injury lawyer who reads in the Jury Verdict Reporter newsletter that some big name lawyer like Philip Corboy has won a \$450,000 verdict for a broken leg. The kid next door then breaks his leg on a skateboard and such a lawyer thinks it's worth \$450,000 out of which he's going to net, say, \$150,000. (That's a lot of real estate closings!) But his case is not a \$450,00 case—it's a \$1,500 case at the

colleague, Professor Robert Mnookin.²⁰ Mnookin acknowledges, but is not all that impressed by the problem of the contingent fee. Rather, he focuses on the overall problems of the costs of personal injury litigation, of which the contingent fee is obviously only a part.²¹ Mnookin focuses on more general problems of the present system.²² But solving the overall problems of personal injury tort law's inefficiencies is something society has balked at doing for generations.²³ To attack a significant piece of the problem—excessive contingent fees along with some corollary baneful disincentives on the defendants' side²⁴—seems worthier to some of us than to Professor Mnookin. In other words, Mnookin is right: the problem *is* bigger than the contingent fee but that does not necessarily mean it does not make sense to address its abuses.

Turning from *ex ante* solutions, like more information or more competition from nonlawyers, to *ex post* solutions, the remarks here of Judge Charles Kocoras confirm that we cannot expect the judiciary to

most. But with stars in his eyes he refuses a reasonable settlement. In fact professionally and temperamentally he's totally inadequate for trial work. He hates the combat and is completely out of his element. But, not being willing to settle, he comes to court along with his client, and they both take an awful beating. That's where inadequate trial work stems from.

At the other end of the spectrum is the lawyer who knows he is inadequate to appear in court and who is known by insurance companies to be inadequate. And yet out of greed he keeps his own personal injury cases and settles them for a pittance, rather than share a fee with an expert trial lawyer whose efforts could insure a proper settlement. Furthermore, some lawyers will "wholesale" their cases with insurance companies. That means that they will settle all claims of their clients against a given company in a package deal, often for a fraction of their combined value, unconscionably mixing the solid claims with the shaky. After taking his own very substantial cut, such a lawyer then assumes arbitrary power to distribute what is left to individual clients. In view of the wide differences possible even in experts' appraisal of tort cases, the clients have little basis for . . . [knowing they've been maltreated].

O'CONNELL, *supra* note 16, at 144-45 (citations omitted).

20. Robert H. Mnookin, *Negotiation, Settlement and the Contingent Fee*, 47 DEPAUL L. REV. 363 (1998).

21. *Id.* at 369-70.

22. *Id.* at 363-69.

23. The huge problems plaguing auto insurance claims including fortuity of payment, long delays, huge transaction costs, and over- and underpayment of claims, were documented two-thirds of a century ago in 1932 by the prominent "Columbia Report." COLUMBIA UNIVERSITY COUNCIL FOR RESEARCH IN THE SOCIAL SCIENCES, REPORT BY THE COMMITTEE TO STUDY COMPENSATION FOR AUTOMOBILE ACCIDENTS (1932). For a description of the subsequent extensive literature similarly outlining the problem and proposing similarly sweeping solutions as of 1965, see ROBERT KEETON & JEFFREY O'CONNELL, BASIC PROTECTION FOR THE TRAFFIC VICTIM ch. 4 (1965). For a more recent capsule summary of the various auto no-fault plans, see IRVIN E. SCHERMER, AUTOMOBILE LIABILITY INSURANCE ch. 14 (3d ed. 1995) and FOWLER V. HARPER ET AL., THE LAW OF TORTS § 13.8 (2d ed. 1986 & Cum. Supp. 1 1997).

24. See *infra* note 26 and accompanying text.

address an excessive contingent fee after the settlement of a case.²⁵ Judges are already overwhelmed by the small percentage of personal injury cases filed that they actually try: less than five percent. Can we expect them to reopen the over ninety-five percent of cases settled in order to, in effect, review their merits so as to appraise, in turn, the risks assumed by the plaintiff's attorney in order to appraise, still further in turn, the appropriateness of the contingent fee? To expect such efforts seems totally unrealistic.

So, if both such *ex ante* and *ex post* solutions for contingent fees do not seem all that promising or likely, what if anything can be done? Lester Brickman, Michael Horowitz, and I have suggested the following: defendants in personal injury cases would be authorized, under either legislation or court rule, to make an early settlement offer, say within sixty days. If no offer is made, the claimant's lawyer is free to negotiate a fee just as he or she does today. But if such an offer is made and accepted, the compensation to a claimant's lawyer would be limited to a reasonable hourly rate or ten percent of the gross settlement, whichever is less. Furthermore, if an early offer was made and refused, the offer would become the basis on which a contingency fee would be computed. For example, if the defense offered \$90,000 and the plaintiff declined and the case was later settled for \$100,000, then the maximum the claimant's lawyer could charge would be ten percent of the \$90,000 plus a third or more of \$10,000, representing the difference between the \$90,000 offer and the \$100,000 that was later won. Note that by the same token this early offer system reduces defendants' incentive to harass claimants by stalling or other obstructive behavior.²⁶ An early offer of, for example, \$10,000 yields \$9,000 for the claimant after attorney's fees, whereas in the absence of an early offer delivering the same \$9,000 to the plaintiff later on, when the lawyer typically can claim, say, forty percent of the payout, would cost the defense \$15,000.²⁷

If it is feared, as some have alleged, that defendants would "game" the system by, for example, making unduly low offers which would

25. The Honorable Charles Kocoras, *Contingent Fees—A Judge's Perch*, 47 DEPAUL L. REV. 421 (1998).

26. A defendant today can harass claimant's counsel by delaying things through motions and discovery that significantly cut into counsel's take from his contingent fee. After all, every hour not spent in enhancing recovery is money lost for claimant's counsel.

27. For a complete draft of the contingency fee proposal adaptable either as legislation or court rule, see Lester Brickman et al., *The Proposal, with Section-by-Section Commentary*, appearing in Michael Horowitz, *Making Ethics Real, Making Ethics Work: A Proposal for Contingency Fee Reform*, 44 EMORY L.J. 173, app. at 194-211 (1995). For the terms of a federal bill, see S. 1861, 104th Cong. (1996).

unduly disadvantage a claimant's lawyer, the system could be limited to being effective only when the early offer is accepted.²⁸ In other words, only when an early offer is made and accepted, would the offer become the basis on which the lower fee would be computed. In turn, the defendant's incentive to make early offers large enough to be likely accepted would be enhanced.

Professor Kritzer objects to this early offer solution as "mechanistic."²⁹ But rules are, by their nature, likely to be mechanistic. A net in tennis is mechanistic, as is a statute of limitations. The question is: Does the rule work? Given the dimensions of the present problem and the huge difficulties of other solutions outlined above, the early offer solution would seem to deserve a try.

28. As to the objection that "defendants [may] exploit the inherent conflict-of-interest exist[ing] in all contingen[t] fee cases between plaintiffs and their counsel by making . . . sub-optimal early offers [which are] designed to make what is left of the case less than worthwhile for claimants' counsel to pursue," note that this conflict is inherent in all settlement offers. BRICKMAN ET AL., *supra* note 13, at 37. All offers to settle "by defendants under today's system are designed to make [any] additional . . . [amount] . . . too small" to justify the risks necessary to obtain anything higher. *Id.* The Brickman-Horowitz-O'Connell proposal, by way of contrast, encourages offers to be made at a very early stage in the process of "achiev[ing] both earlier payments . . . [for claimants along with] . . . substantial transaction cost savings . . . and . . . do[es] so without imposing greater burdens or risks on plaintiffs than . . . [are] currently face[d]. *Id.* As the authors have put it:

[A]ny time a settlement offer is made—whether at the courthouse steps or during or even after trial (in the latter case pending an appeal)—the defendant purports to offer just enough so that what remains unmet of the claimant's demand will not be deemed worth fighting further about. By placing the most attractive moment to achieve a settlement at an early point in the proceedings[,] however, the [Brickman-Horowitz-O'Connell] proposal has the powerful virtue of allowing the parties (and the judicial administration system) a means of escape from the delays, costs and other burdens of litigation that beset the present system.

Id. at 37-38.

29. Kritzer, *supra* note 1, at 307.

