4-20-2016

Inclusion v. Idaho Dept of Health and Welfare Appellant's Reply Brief Dckt. 42245

IN THE SUPREME COURT OF THE STATE OF IDAHO

INCLUSION INC. an Idaho corporation, INCLUSION NORTH, INC., an Idaho corporation, and INCLUSION SOUTH, INC., an Idaho corporation,

Plaintiffs-Respondents,

v.

IDAHO DEPARTMENT OF HEALTH AND WELFARE and RICHARD ARMSTRONG,

Defendants-Appellants.

Supreme Court No. 42245

APPELLANTS' REPLY BRIEF

Appeal from the District Court of the Fourth Judicial District
of the State of Idaho, in and for the County of Ada
Case No. CV OC 2012-16467

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Honorable Richard D. Greenwood, District Judge, presiding

LAWRENCE G. WASDEN
ATTORNEY GENERAL

STEVEN L. OLSEN, ISB #3586
Chief of Civil Litigation

CARL J. WITHROE, ISB #7051
Deputy Attorney General
954 W. Jefferson Street, 2nd Floor
P.O. Box 83720
Boise, ID 83720-0010
Telephone: (208) 334-2400
Facsimile: (208) 854-8073
Attorney for Defendants-Appellants

DENNIS M. CHARNEY
Charney and Associates, PLLC
1191 East Iron Eagle Drive
Eagle, ID 83616
Telephone: (208) 938-9500
Facsimile: (208) 938-9504
Attorney for Plaintiffs-Respondents

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INTRODUCTION

The district court found that the amount of time prevailing counsel spent on the case and the requested hourly rate—$125 an hour—were reasonable. Tr. (Dec. 3, 2014), p. 33, LL. 2-20; p. 34, LL. 1-8. It nevertheless declined to award the prevailing party—the Idaho Department of Health and Welfare—fees using that hourly rate multiplied by the number of hours spent. It initially did this because it believed that to award more violated a rule of professional conduct prohibiting fee-sharing by lawyers. After the Department sought reconsideration of that ruling, the district court decided that still, the Department could recover no more than the State's internal cost-accounting rate, $51.48 per hour, because, as it said, "[e]xcept where the award of attorney fees is paid to the lawyer, fees awarded to a party should not exceed the amount the client actually paid for the lawyer." Replacement R., p. 125. The court said this was so "whether the prevailing party is a government entity or private party." *Id.* Something other than that, the court said, "is an impermissible penalty and does not serve the purpose of simply making the receiving party whole." *Id.*

In defense of the court's ruling, the providers contend that the district court acted within the bounds of its discretion when it awarded the Department $51.48 an hour—$73 an hour less than the $125 an hour the Department sought. They explain their view that the court considered all the factors in Rule 54(e)(3) and the bases for capping the recoverable hourly rate were appropriate discretionary decisions. The measure of attorney fees may be, they say, limited to the actual cost of legal services, and the decision whether to measure reasonable fees by the prevailing market rate or the actual cost is an appropriate discretionary call that does not conflict with § 12-120(3) or Idaho R. Civ. P. 54(e)(3).

The providers are mistaken. Abuse of discretion is not another way of saying unreviewable: When a district court relies on the wrong legal standard to make a discretionary decision, it abuses its discretion. *Golub v. Kirk-Hughes Dev't, LLC*, 158 Idaho 73, 76, 343 P.3d 1080, 1083 (2015). This Court has free review over questions of law and matters of statutory interpretation. *Intermountain Real Properties, LLC v. Draw, LLC*, 155 Idaho 313, 317-18, 311 P.3d 734, 738-39 (2013). The only two legal bases the district court cited as justifying its cap on the recoverable hourly rate—the fee-sharing problem and the problem of windfalls and penalties—are not legally correct. First, awarding prevailing party fees that may exceed the party's actual expenditure creates no fee-sharing problem because the rule in question, Rule 5.4 of the Idaho Rules of Professional Conduct, does not apply where the party, not the lawyer, owns the right to the fee award. Rule 5.4 is aimed at preventing non-lawyer, non-client third-parties from having a financial interest in the representation in the form of fees paid by the client and shared with them by a lawyer. But where the lawyer never sees the fee award, there is no sharing of fees by a lawyer with a non-lawyer. Rule 5.4 does not prohibit a statutory fee award in litigation that exceeds the amount the party spent on its lawyer.

Second, awarding the Department $125 an hour does not confer any impermissible windfall on the State or exact any unfair penalty on the providers. The statute and rule place the focus on the objective reasonableness of the fee award. The nature of the fee agreement is a factor to consider, but not to the exclusion of the other factors. The nature of the fee agreement may inform reasonableness, but it does not determine it. And the statute is not limited to an amount that simply reimburses costs, contrary to the district court's ruling. Reasonableness seeks to identify a reasonable value—not necessarily the cost—of the services in the particular case, based on the factors identified in Rule 54(e)(3). The district court's reading of § 12-120(3)

to limit fees to the amount spent is erroneous. The providers have no substantial answers for the problems their arguments face. This Court should reverse the judgment of the district court and remand the matter with instructions to award the Department attorney fees of $74,925.00.

ARGUMENT

I. THE DISTRICT COURT'S AWARD OF ATTORNEY FEES AT $51.43 AN HOUR IS AN ABUSE OF DISCRETION

The district court indicated it had considered all the factors that Rule 54(e)(3) requires. Tr. (Dec. 3, 2014), p. 32, LL. 12-16. It found from its consideration of the information before it that the time spent and the hourly rate were reasonable. Tr. (Dec. 3, 2014), p. 33, LL. 2-20; p. 34, LL. 1-8. Each of these factors is expressly provided for in the Rule. Idaho R. Civ. P. 54(e)(3)(A) (time and labor required); (D) (prevailing charges for like work). The court did not identify any factor in the rule that justified awarding fees at less than the $125 an hour that the Department requested. Instead, it based that decision solely on its perception that to award more constituted impermissible fee sharing under Rule 5.4 of the Rules of Professional Conduct and that such an award bestowed an unfair windfall to the Department and imposed a penalty to the providers. The problem with these determinations, though, is that they are incorrect as a matter of law. When they are properly cast aside, there is no other legitimate basis to deny the Department an hourly rate of less than it sought.

A. When the party owns the right to the fee award, awarding that party attorney fees exceeding the amount it spent presents no fee-sharing problem.

The providers do very little in their brief to discuss the fee-sharing issue the district court raised other than to say that the district court had "ethical concerns" about awarding the Department more than it spent. (They do not even mention Rule 5.4 in their brief, and they do not make any argument that an award to the Department the amount requested would violate the

rules of professional conduct.) The district court did little to explain its reasoning other than to generally mention the prohibition on sharing fees with non-lawyers. On appeal though, the providers say that the Department "brushes aside the district court's ethical concerns of fee-splitting with non-attorney entities." Respondents' Brief, p. 7.[1] Whatever role the fee-sharing problem played in the district court's ultimate decision, it is wrong.

As the Department pointed out in its opening brief, the district court seemed to retreat from its view that the Department's requested reward would constitute impermissible fee sharing. Appellants' Brief, p. 6. The Department addressed that concern in a footnote, explaining that there is no fee-sharing problem in this case because the fee award is the property of the client, and Rule 5.4 is aimed at preventing lawyers from sharing attorney fees paid by clients with non-lawyer, non-client third parties. Appellants' Brief, p. 6 n.4. Rule 5.4 states that "[a] lawyer or law firm shall not share legal fees with a nonlawyer," except for some circumstances, inapplicable here, where a lawyer may. This limitation plainly protects *clients* from the potential influence over the lawyer that third-party non-client, non-lawyers may obtain when those third parties have a financial interest in the fee that is earned by the lawyer for providing services to the client. It seeks to protect the lawyer's professional independence and her obligation *to* the client. The obvious purpose of Rule 5.4 is to eliminate any incentive a lawyer may have to charge unreasonably high rates or make professional decisions that are not in the client's best interests. If, as the Department explained in its brief, the lawyer agrees to share her fees with a non-lawyer, non-client third party, the outside interest in the litigation may compromise the lawyer's judgment and independence and her obligations.

[1] Pursuant to this Court's order dated October 13, 2015, references to the parties and their briefs are as follows: The Department is referred to as the Appellants (and their brief Brief for Appellants) and the providers are referred to as the Respondents (and their brief Brief for Respondents).

But here, there is no fee-sharing problem because it is not possible. First, this is an attorney fee award paid by the losing side in a case to the winning party. These awards are not the same as a lawyer collecting her client's fee from the client and then sharing it with someone else, which is what the rule contemplates. Second, the Attorney General is not the recipient of the attorney fee award; the State of Idaho is. Under Idaho Code § 12-120(3), the prevailing *party* owns the right to the fee award. Because the lawyer never sees the money, he literally cannot share it with any non-lawyers. In rejecting an argument that in-house counsel time could only be reimbursed according to in-house counsel's salary, the Seventh Circuit has explained it this way:

> [i]f the victorious litigant owns the money representing the market value of the legal fees, and may pocket the cash without remitting a cent to the lawyer—who may have agreed to work for less, or for free—it is hard to see how there can be a fee-splitting objection. The money is not they lawyer's to start with.

Central States, Se. & Sw. Areas Pension Fund v. Central Cartage Co., 76 F.3d 114, 116 (7th Cir. 1996). The Court further observed that "how the litigant allocates the money between its legal budget is none of the court's business . . . ." *Id.* Awarding the Department $125 an hour in attorney fees is not impermissible fee-sharing. Accordingly, fee-sharing is not a legitimate basis to limit the Department's recovery to the amount it actually spent.[2]

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[2] One case the district court cited, *National Treasury Employees Union v. U.S. Dep't of the Treasury*, 656 F.2d 848 (D.C. Cir. 1981), illustrates the difference between a case like this one, and a case where there may be impermissible fee sharing. There, a union hired a lawyer to represent a union member under the union's prepaid legal services plan. 656 F.2d at 849. The lawyers were compensated by the union at less than the fee request, and the fee award was the property of the union, not, apparently, the lawyer or the client. *Id.* The union was a non-lawyer organization and would have received fees for the lawyer's services in excess of the lawyer's compensation. Here, though, the entity receiving the award—the State, through the Department—*is* the client.

B. Awarding the Department market-based rates that the district court found to be reasonable does not constitute a windfall to the Department or a penalty to the providers.

Neither the district court nor the providers offered any authority for the idea that a party may recover fees only in an amount equal to what it paid for its lawyers. The district court said that "the purpose of attorney fees is to indemnify the prevailing party and not to punish the losing party by allowing the winner a windfall profit." Replacement R., pp. 124-25. Awarding a party more than it spent, "whether the prevailing party is a government entity or a private party," is an "impermissible penalty and does not serve the purpose of simply making the receiving party whole." Replacement R., p. 125. The providers' best argument in support of this view is that it is just not fair to award a party more than it spent. *See* Respondents' Brief, p. 13. But not-fair is not a sufficient argument to overcome the plain language of § 12-120(3) or this Court's cases.

Section 12-120(3) directs the trial courts to award reasonable attorney fees. Idaho R. Civ. P. 54(e)(3) lists several factors for courts to consider in determining a reasonable fee. A reasonable fee may be more or less than the agreement between the lawyer and the client. *See Ada County Hwy. Dist. v. Acarrequi*, 105 Idaho 873, 878, 673 P.2d 1067, 1072 (1983), *overruled in part on other grounds, Dep't of Transp. v. Grathol*, 158 Idaho 38, 343 P.3d 480 (2015) (in condemnation action, Rule 54(e) factors are appropriately considered; but "[w]e caution that the court should not automatically adopt any contingent fee or contractual arrangement, but rather the fee awarded may be more or less than that provided in the lawyer-client contract"); *see also Nalen v. Jenkins*, 114 Idaho 973, 976, 114 P.2d 1081, 1084 (Ct. App. 1988) ("we have previously ruled that a court is *not* prohibited from allowing recovery to the prevailing party in excess of the amount which the party is contractually obligated to pay his attorney"). And fees

may be awarded to a party who incurs no attorney fees at all. *Kidwell v. U.S. Marketing*, 102 U.S. 451, 631 P.2d 622 (1981); *Furtell v. Martin*, 100 Idaho 473, 600 P.2d 777 (1979).

The providers do not have an answer to this. The district court's and the providers' windfall/penalty problem assumes that § 12-120(3) and Rule 54(e)(3) direct courts to determine a fee that reflects the costs incurred by the prevailing party. This assumption is wrong. It overlooks the fact that as we have explained, the fee agreement does not necessarily tie the court's determination of a reasonable fee. If the district court is right, that a fee award cannot exceed what a party actually spent on its layers, then the Court's statements that fees may be more or less than the agreed-upon amount between lawyer and client and that a party may recover fees even if it has incurred none at all would be wrong.

Under § 12-120(3), the fair expectation of a party is that if it loses, it may end up paying "reasonable" attorney fees. If the Court had interpreted "reasonable," as that term is used in § 12-120(3), to mean only the amount the other side's lawyer cost, a fee award exceeding the amount paid without justification based on the factors in Rule 54(e)(3) may well be something beyond what either party may reasonably expect. But the Court has never interpreted § 12-120(3) to mean what the district court said it means. So neither party can fairly expect that an award of attorney fees will necessarily match the fee agreement. Therefore, there is no windfall and no penalty because the parties litigate having evaluated the risk that they may have to pay fees that exceed what the other side's lawyer cost. (And conversely, the lawyers know that they cannot charge unreasonably high rates and expect district courts to allow them. Idaho R. Prof'l Conduct 1.5.) Parties may rely on the district court to police reasonableness by examining the factors in Rule 54(e)(3), but an amount above the fee agreement cannot be unexpected. *See Illinois v. Sangamo Constr. Co.*, 657 F.2d. 855, 862 (7th Cir. 1981) (no windfall to state to award

market rates); *Corbin v. Tocco*, 845 P.2d 513, 518 (Ariz. Ct. App. 1992). Absent justification to award less than an amount the court deemed reasonable, there is no basis to do so.[3]

That is not to say that the amount the party agreed to pay its lawyer is always necessarily entirely irrelevant to the reasonableness inquiry. Evidence of the prevailing charges for like work (Rule 54(e)(3)(D)) may come from an affidavit of a lawyer familiar with the market and the subject matter of the case (or perhaps the prevailing party's lawyer, as is common). The fee agreement itself may be of some relevance to reasonableness in some circumstances. A client voluntarily agreeing to pay a lawyer a certain hourly rate may reflect the going rate in the market. An hourly rate exceeding the prevailing charges for like work may not be justifiable in light of the factors in Rule 54(e)(3). Similarly, there may be any number of reasons why the hourly rate is lower than market, and a request for the market rates may be reasonable. As we have explained, though, a hard rule that the award may be no more than what is spent is incorrect. When a district court finds the hourly rate to be reasonable, and there is no legitimate basis to deviate from it—up or down—any such deviation misapplies the appropriate legal standard and is not the product of an exercise of reason.

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[3] The providers cite two cases that they apparently think demonstrate that courts should limit fee awards to prevent windfalls and penalties. Respondents' Brief, pp. 17, 19. In *Griffith v. Clear Lakes Trout Co., Inc.*, 146 Idaho 613, 200 P.3d 1162 (2009), the Court explained that a party may switch its basis for seeking fees between a contingent basis and fixed hourly rate, and that there may be times "when a party switches the basis of his request for computing fees for the sole purpose of creating a windfall for himself" and that the district court exists to ensure that the fee award is reasonable. 146 Idaho at 623, 200 P.3d at 1172. The Court did not say, however, that awarding fees above what a party spent was necessarily a windfall. In this case, there is no windfall because market rates are, as the district court found, reasonable. The other case, *Zenner v. Holcomb*, 147 Idaho 444, 210 P.3d 552 (2009), concerned the question whether the factors identified in Rule 54(e)(3) applied to a contractual attorney fees provision that called for "actual" attorney fees. The rule did not apply, the Court held, since "actual" meant actual and did not contemplate a reasonableness inquiry called for in Rule 54. 147 Idaho at 451, 210 P.3d at 559. The Court explained that "actual" did not guarantee whatever the contract provided for; like a liquidated damages clause, a contractual fee provision may constitute an "unconscionable penalty." *Id.* But, again, the Court did not say that awarding a fee under § 12-120(3) was an unconscionable penalty.

The providers also do not have an answer for the odd result their and the district court's rationale creates. Limiting fees to the amount spent means that the same work will be compensated differently depending on who the lawyer's employer is. So, for example, if the Department in this case hired outside counsel, the fee request would have likely exceeded $250 an hour. In such a case, the district court would award that amount, but because the State used lawyers on the payroll, it can only recover actual expenses. This does not make sense, and courts have correctly rejected it. For starters, market rates are easy ascertainable, and the cost-based approach is very complicated and costly. *See Illinois v. Sangamo Constr. Co.*, 657 F.2d at 862 (use of generally prevailing market rates is "far preferable to extensive judicial scrutiny of private fee arrangements or the internal economics of the Attorney General's office"); *Corbin*, 845 P.3d at 518.[4]

Additionally, courts have found no basis to treat government counsel differently than private counsel. The skill, time, expertise, and effort necessary to litigate a case for the government is no different than that which is required to litigate a case for a paying client. As a district judge from the Northern District of Illinois put it some time ago, attorney fees are a "two-way street" and it "makes no difference" that the government lawyers are public servants. *Coleman v. McLaren*, 635 F. Supp. 266, 267-68 (N.D. Ill. 1986).

Reading § 12-120(3) to cap fees because that statute exists only to "indemnify the prevailing party" the amount it spent is an erroneous interpretation of § 12-120(3). There is no support for it. Because the district court's interpretation of § 12-120 is erroneous, its windfall/penalty approach is at best a decision driven by the district court's sense of fairness beyond the permissible considerations enumerated in Rule 54(e)(3) and this Court's cases.

[4] As we explained, the record demonstrates that the SWCAP rate is the same for every lawyer; it is not designed to, and does not, capture all costs of using deputy attorneys general to litigate cases. Replacement R., p. 83.

Without an independent basis to justify the court's departure from what it found to be a reasonable rate, the court's sense of the equities is not sustainable on review. *Jorgensen v. Coppedge*, 148 Idaho 536, 541, 224 P.3d 1125, 1130 (2010). Attorney fee awards are "not the proper place to give indirect relief from an adverse judgment" and the "arguably harsh effect of a judgment is not an appropriate 'other' factor to consider in fixing attorney fees under Rule 54(e)(3)." *DeWils Interiors, Inc. v. Dines*, 106 Idaho 288, 291, 678 P.2d 80, 83 (Ct. App. 1984).

II. THE DEPARTMENT SHOULD BE AWARDED ATTORNEY FEES IF IT PREVAILS IN THIS APPEAL; THE PROVIDERS SHOULD NOT RECOVER FEES UNDER § 12-117 EVEN IF THEY PREVAIL.

The Department requested attorney fees in its opening brief under § 12-120(3), since this case concerned a commercial transaction. Appellants' Brief, p. 22. The providers do not contest the applicability of § 12-120(3) on appeal. Ergo, if the Department prevails in this appeal, it should be awarded reasonable attorney fees.

The providers say they are entitled to attorney fees, too. They seek fees under §§ 12-120(3), 12-121, and 12-117. They argue that the Department has pursued this appeal without a reasonable basis in fact or law. Respondents' Brief, p. 20. Should the Department lose this appeal, an award of fees against the Department under § 12-117 is not warranted. First they say that the Department "frames an issue for this Court's review which does not accurately reflect the trial court's decision." Respondents' Brief, p. 20. The Department presented the issue whether the district court erred in applying cost-based limitation on government agencies' ability to recover attorney fees in its notice of cross-appeal. Replacement R., p. 128. It stated the issue on appeal in its opening brief as whether § 12-120(3) and Rule 54(e)(3) limit a prevailing party's recovery to the amount it spent. Appellants' Brief, p. 7. The Department identified and discussed both the original basis for the court's ruling (the fee-sharing problem, Appellants'

Brief, p. 6 n.4) and the basis for the decision on the Department's motion to reconsider. So the Department presented and discussed the bases for the district court's decision. There is no merit in the providers' argument otherwise.

Their next argument in support of a fee award under § 12-117 is that the Department argued that Idaho trial courts should not consider whether a fee award amounts to a windfall, and that the decision whether to award fees exceeding those actually expended is a discretionary call. They are mistaken as to what the Department argued. The Department identified the standard of review, specifically the requirement that the court act consistently with the legal standards applicable to the choices before the court. Appellants' Brief, p. 7. This brief and the Department's opening brief make clear that the Department argued—with discussion of and citation to substantial authority—that there was no legal basis for the district court to award less than the requested rate because neither of the district court's legal justifications were correct.

Third, they say that the Department argued that unless a statute specifies an award of actual fees, the trial court should apply prevailing market fees to the exclusion of the other factors in Rule 54(e)(3). This, too, is defied by a simple reading of the Department's brief. The Department argued that the limitation the district court imposed was an impermissible construction of § 12-120(3), and that in this case, there was no other legitimate basis to award a lesser amount. The Department simply pointed out that this Court has said that "actual" and "reasonable" do not necessarily always align. There is, as the Department pointed out, authority for this argument. *Zenner v. Holcomb*, 147 Idaho 444, 450, 210 P.3d 552, 558 (2009). The providers offered zero authority in their brief to respond to this plain proposition.

Fourth, the providers argue that the Department's appeal "essentially requests that the State profit from its use of in-house counsel and that profit should be re-allocated according to

the state's needs versus deposited in the Attorney General's fund." Respondents' Brief, p. 21. Again, the Department's argument has been consistent: Where a district court finds that the hourly rate is reasonable, and there is no basis to award something less, the hourly rate should be the requested hourly rate. This Court's cases do not limit the recoverable hourly rate to that which the prevailing party spent; what the client may do with it is irrelevant.

And finally, the providers argue that the Department's appeal does no more than invite this Court to second-guess conflicting evidence, and that the law is well-settled and the Department has made no showing that the district court misapplied the law. The Department's briefs speak for themselves. The Court should not take seriously the providers' unfounded claim. Indeed, the providers' brief largely consists of quotes from the district court's decision and comments from the bench, summaries of those comments, some citations to cases, and then offers conclusory pronouncements that the district court got it right. If there is a party in this appeal that is entitled to fees under § 12-117, it is not the providers.

CONCLUSION

This Court should reverse the district court's award of attorney fees and remand with instructions to award the Department attorney fees in the amount requested, $74,925.00. This Court should also award the Department reasonable attorney fees under § 12-120(3).

Dated April 20, 2016.

STATE OF IDAHO
OFFICE OF THE ATTORNEY GENERAL

By: 

CARL J. WITHROE
Deputy Attorney General
Attorneys for Appellants

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on this 20th day of April, 2016, I caused to be served a true and correct copy of the foregoing by the following method to:

Dennis M. Charney
CHARNEY AND ASSOCIATES, PLLC
1191 East Iron Eagle Drive
Eagle, Idaho 83616

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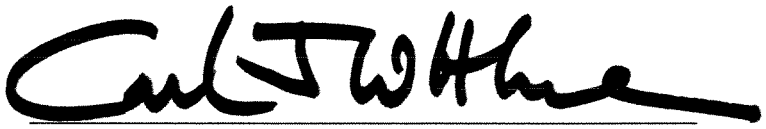

CARL J. WITHROE
Deputy Attorney General