No. 16-16103

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

AMERICAN BANKERS MANAGEMENT COMPANY, INC.,
Plaintiff-Appellant,
v.
ERIC L. HERYFORD, in his official capacity as District Attorney, Trinity County, California
Defendant-Appellee.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF CALIFORNIA

BRIEF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AND THE PHARMACEUTICAL RESEARCH AND MANUFACTURERS OF AMERICA AS *AMICI CURIAE* IN SUPPORT OF APPELLANT AND IN SUPPORT OF REVERSAL

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rules of Appellate Procedure 26.1 and 29(c)(1), *amici curiae* hereby submit the following corporate disclosure statement:

1. *Amicus curiae* The Chamber of Commerce of the United States of America does not have a parent corporation; nor does any publicly held corporation own 10% or more of its stock.
2. *Amicus curiae* The Pharmaceutical Research and Manufacturers of America does not have a parent corporation; nor does any publicly held corporation own 10% or more of its stock.

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STATEMENT OF INTEREST

The Chamber of Commerce of the United States of America ("Chamber") is the world's largest business federation, representing 300,000 direct members and representing indirectly the interests of more than three million companies and professional organizations of every size, in every industry sector, and from every geographic region of the United States. An important function of the Chamber is to represent the interests of its members by participating as *amicus curiae* in cases involving issues of national concern to American business, such as this one. The Chamber's members operate in nearly every industry and business sector in the United States. These members have an interest in vindicating bedrock principles of due process and ensuring that defendants are afforded a neutral tribunal in cases brought against the Chamber's members by or on behalf of governmental entities.

The Pharmaceutical Research and Manufacturers of America ("PhRMA") is a voluntary, nonprofit association of the country's leading research-based pharmaceutical and biotechnology companies. PhRMA's mission is to advocate public policies encouraging the discovery of life-saving and life-enhancing new medicines. PhRMA's member companies are devoted to inventing medicines that allow patients to live longer, healthier, and more productive lives, and have led the way in the search for new cures. Member companies have invested over $500

billion in research and development into medical innovations since 2005 and approximately $58.8 billion in 2015 alone.[1]

The Chamber and PhRMA have a strong interest in this case because their members are increasingly the targets of suits involving contingency-fee arrangements between attorneys general and private counsel. In addition, their participation as *amici* is desirable because the law in this area remains unsettled, and their unique perspective and expertise can help elucidate the significant due-process issues raised by the parties' briefing.[2]

SUMMARY OF THE ARGUMENT

This case presents the Court with a prime opportunity to address a troubling trend in our judicial system in which state attorneys general delegate quasi-criminal enforcement powers to private attorneys who litigate multiple claims against corporate defendants. In nearly every such case, including *California ex rel., Eric L. Heryford, District Attorney, Trinity County v. Discover Financial*

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[1] *See* PhRMA, *2016 Profile: Biopharmaceutical Research Industry*, Key Facts 2016, at 1 (2016), http://www.phrma.org/sites/default/files/pdf/biopharmaceutical-industry-profile.pdf (last visited Sept. 30, 2016). These research and development investments led to 56 new medicines being approved in 2015 alone. *See id.*

[2] Pursuant to Federal Rule of Appellate Procedure 29(c)(5), counsel for *amici curiae* states that no counsel for a party in this case authored this brief in whole or in part, and no party or counsel for a party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amici curiae*, their members, or their counsel made a monetary contribution to the brief's

(cont'd)

Services et al., No. 2:16-cv-00468-KJM-CMK ("the UCL suit"), the private attorneys enter into a contingency-fee agreement with the state, under which they are to be paid only if they win; and if they do win, they are paid more and more for each additional dollar they recover.

The problem with these arrangements is self-evident: they entrust the duty of impartially administering justice to attorneys with an overwhelming incentive to "win" the case – even if it is entirely bereft of merit. As a result of these pressures, the neutral forum assured to defendants by basic principles of due process is incurably tainted. Given the personal interests of counsel, defendants have no hope of persuading them to abandon a meritless case because the quest for a high-dollar recovery becomes the paramount consideration, no matter how unreasonable the underlying litigation. And if the state prevails, it inevitably seeks highly inflated penalties, placing additional burdens on court dockets and harming American businesses.

The district court failed to grapple with these fundamental issues in dismissing American Bankers Management Company, Inc.'s ("American Bankers") complaint under 42 U.S.C. § 1983, allowing the dubious financial arrangement between the Trinity County District Attorney and outside counsel in a quasi-

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preparation or submission. *Amici* have moved for leave to file this brief. They sought consent of all parties but defendant/appellee did not consent.

criminal proceeding to go forward unabated. The Court should reverse the lower court's ruling and adopt a *categorical* bar on the use of contingency-fee counsel in cases, like this one, that are quasi-criminal in nature, under the auspices of the constitutional guarantee of due process. Such a ruling could help stem the tide of use of contingency-fee counsel by state attorneys general in quasi-criminal enforcement actions in this Circuit and around the country – a practice that has generally escaped appellate review by the federal circuit courts.

ARGUMENT

I. A CATEGORICAL BAR AGAINST THE USE OF CONTINGENCY-FEE COUNSEL APPLIES IN QUASI-CRIMINAL CASES LIKE THIS ONE.

Due process includes the right to an impartial tribunal and to prosecution by a lawyer for the government whose judgment is unclouded by any financial or other personal stake in the outcome. *See Marshall v. Jerrico, Inc.*, 446 U.S. 238, 249-50 (1980); *Tumey v. Ohio*, 273 U.S. 510, 535 (1927). Pursuant to this principle, Supreme Court decisions have adopted a "categorical" rule against the use of prosecutors who have a financial incentive to obtain a conviction – be they government attorneys or private, retained counsel – a rule that other courts have extended to quasi-criminal enforcement actions. (*See* Pl.'s Br. at 20-23.)

Despite the clarity of the Supreme Court's "categorical" approach, some courts have concluded that attorneys general may retain private counsel on a

contingency-fee basis as long as the attorney general retains "control" of the litigation. (*See id.* at 23-26.) But even these courts have in most cases recognized that a categorical bar on such arrangements remains necessary in quasi-criminal enforcement proceedings like this one. A pair of California Supreme Court cases are illustrative. First, in *People ex rel. Clancy v. Superior Court*, 705 P.2d 347 (Cal. 1985), the City of Corona, California, sought to enjoin a bookstore from selling sexually explicit materials. *Id.* at 348. The City hired outside counsel to prosecute abatement actions under a theory of public nuisance, *id.* at 348-49, agreeing to double the private firm's hourly rate if the City prevailed (as long as the court ordered the losing party to pay the City's attorneys' fees). *Id.* at 350. The California Supreme Court rejected this arrangement, finding that the retention agreement "[o]bviously" gave outside counsel "an interest extraneous to his official function in the actions he prosecutes on behalf of the City." *Id.* at 351. The court held that such an interest was "antithetical to the standard of neutrality that an attorney representing the government must meet when prosecuting a public nuisance abatement action." *Id.* at 353.

As part of its rationale, the court explained that the abatement proceeding closely resembled a criminal prosecution, in which principles of neutrality and impartiality are of paramount importance. *See id.* at 352-53 & n.4. In particular, both in *Clancy* and in a subsequent case describing it, the California Supreme

Court emphasized the quasi-criminal nature of the proceeding: (1) the lawsuit was "brought in the name of the People," *id.* at 352, and "on behalf of the public," *Cty. of Santa Clara v. Superior Court*, 235 P.3d 21, 34 (Cal. 2010); (2) it sought not compensatory but injunctive relief, which would impinge upon "the continued operation of an established, lawful business," *Santa Clara*, 235 P.3d at 32; (3) the suit "implicated both the defendants' and the public's constitutional free-speech rights" because the materials at issue "involved speech that arguably was protected in part," *id.* at 32-33; and (4) the City sought a "'remedy [that] is in the hands of the state,'" *id.* at 33 n.10 (quoting *Clancy*, 705 P.2d at 353), and "carried the threat of criminal liability," *id.* at 33.

Based on these characteristics, the California Supreme Court determined that the close relationship between the nuisance action and a criminal proceeding "supports the need for a neutral prosecuting attorney," and "*[a]ny* financial arrangement that would tempt the . . . attorney to tip the scale cannot be tolerated." *Clancy*, 705 P.2d at 352-53 (emphasis added). The court therefore disqualified the counsel. *Id.* at 353.

Years later, when the same court embraced the control test in a different case, it was careful to point out that *Clancy*'s categorical bar would continue to apply in quasi-criminal cases. In *Santa Clara*, the California Supreme Court confronted another nuisance action, this time by various municipalities against former

manufacturers of lead paint. 235 P.3d at 21. The municipalities sought to have the manufacturers remove or pay for the removal of lead paint. *See id.* at 25, 34. While the court concluded that *Clancy*'s rule of "automatic disqualification" was "unwarranted," *id.* at 32, it did so only because the hallmarks of the quasi-criminal proceeding in *Clancy* were absent: (1) "no ongoing business activity [would] be enjoined" since the manufacture of lead paint had already been illegal for decades, *id.* at 34; (2) "the *remedy* [would] not involve enjoining current or future speech" and thus could not "prevent defendants from exercising any First Amendment right or any other liberty interest," *id.*; (3) the suits posed "neither a threat nor a possibility of criminal liability," *id.*; and (4) the proposed remedy would "result, at most, in defendants' having to expend resources to abate the lead-paint nuisance they allegedly created" – "the type of remedy one might find in an ordinary civil case." *Id.*

Under these particular circumstances, the court held that the attorney general's office could hire private counsel on a contingency-fee basis, but only if it retained "'*absolute and total control over all critical decision-making*.'" *Id.* at 36 (quoting *Rhode Island v. Lead Indus. Ass'n*, 951 A.2d 428, 475 (R.I. 2008)). Importantly, however, the court distinguished the case before it and underscored the vitality of *Clancy*'s rule of "automatic disqualification" in quasi-criminal cases. *Accord, e.g.*, David M. Axelrad & Lisa Perrochet, *The Supreme Court of*

California Rules on Santa Clara *Contingency Fee Issue – Backpedals on* Clancy, 78 Def. Couns. J. 331, 343 (2011) ("The [*Santa Clara*] court found the *determinative* factor in the case . . . to be the difference between 'the types of remedies sought and the types of interests implicated' in *Clancy* and in *Santa Clara*." (emphasis added) (citation omitted)).[3]

Here, even if the Court were to conclude that a control test might be appropriate in some circumstances, *Clancy's* categorical rule should apply in these circumstances because, for the reasons elaborated in plaintiff's brief, "[t]he UCL suit is much closer in kind to the quasi-criminal law enforcement action prosecuted in *Clancy* than it is to the more 'ordinary civil case' prosecuted in *Santa Clara*." (Pl.'s Br. at 26.)

The district court held otherwise, finding that "[t]he level of neutrality implicated here is similar to that in *Santa Clara*" – *not Clancy*. (ER 16.) The only

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[3] Other cases have acknowledged this same distinction. *See, e.g.*, *City & Cty. of San Francisco v. Philip Morris, Inc.*, 957 F. Supp. 1130, 1135 (N.D. Cal. 1997) ("This lawsuit, which is basically a fraud action, does not raise concerns analogous to those in the public nuisance or eminent domain contexts discussed in *Clancy*. Plaintiffs' role in this suit is that of a tort victim, rather than a sovereign seeking to vindicate the rights of its residents or exercising governmental powers."); *Lead Indus.*, 951 A.2d at 475 nn.48 & 50 (A categorical bar was inappropriate because "the case presently before us is completely civil in nature," but "we are unable to envision a criminal case where contingent fees would ever be appropriate[.]"); *Philip Morris Inc. v. Glendening*, 709 A.2d 1230, 1242-43 (Md. 1998) (distinguishing *Clancy* in part because "there are no constitutional or criminal violations directly implicated here").

basis the district court offered for its holding was that American Bankers "cite[d] no case law to support a conclusion that conduct giving rise to an action under the UCL, targeting deceptive marketing of ancillary products and services, is protected by the First Amendment, in contrast to the well-established First Amendment protection afforded to the *Clancy* plaintiff's right to distribute adult materials." (*Id.*)

This conclusion was incorrect because speech in connection with marketing is clearly protected by the First Amendment. Notably, in *Clancy* it was sufficient that the proposed injunctive relief would have affected speech (in the form of sexually explicit materials) that was "*arguably* . . . protected in part." *Santa Clara*, 235 P.3d at 32-33 (emphasis added). Here, the liberty interest at stake is at least as strong, as there is no question that commercial speech is protected. (*See* Pl.'s Br. at 37-40 ("'The First Amendment requires heightened scrutiny whenever the government creates a regulation of speech because of disagreement with the message it conveys. Commercial speech is no exception. A consumer's concern for the free flow of commercial speech often may be far keener than his concern for urgent political dialogue.'") (quoting *Sorrell v. IMS Health Inc.*, 131 S. Ct. 2653, 2664 (2011) (some internal quotation marks and citations omitted)).)

The district court apparently concluded that the allegations here that American Bankers's marketing was deceptive altered the analysis because

deceptive speech is not protected (ER 16), but *Clancy* cannot be distinguished on this basis. There the allegation was that the defendants were involved in the sale of materials that were obscene and thus outside the protection of the First Amendment. *See* 705 P.2d at 348 (noting that a subpoena had been served on a store clerk demanding that he appear in court with 262 publications "to permit the court to determine whether the publications [were] obscene" as defined by California Penal Code § 311.2); *see also generally Bloom v. Municipal Court*, 545 P.2d 229, 236 (Cal. 1976) (expressly concluding that § 311.2 does not violate the First Amendment because there is no right to sell obscene materials). Thus, in determining whether liberty interests were sufficiently at stake, *Clancy* did not assume the truth of the City's allegations; neither should the district court have done so here. Indeed, the district court's approach would strip the due-process principles at issue here of all protection because a defendant would not be able to prove that the relief sought jeopardized important rights unless and until it won the underlying case – at which point the prejudice inherent in the use of an interested prosecutor would be complete and irremediable. Accordingly, the district court's effort to distinguish *Clancy* from the present case on the sole ground that the underlying proceeding does not implicate American Bankers's First Amendment rights is illogical and contrary to law.

Moreover, the district court overlooked the nature of the requested relief in the underlying proceeding – "the *determinative* factor" in resolving whether the case should be governed by *Clancy* or *Santa Clara*. Axelrad & Perrochet, *supra*, at 342 (emphasis added). Specifically, apart from implicating American Bankers's free-speech rights, the UCL suit also involves a request for penalties – a remedy that (like the one in *Clancy*) rests exclusively in the government's hands. *See Santa Clara*, 235 P.3d at 33-35 (contrasting the state's exclusive remedies with ordinary compensatory relief, which is all that was sought in *Santa Clara*). The purpose of penalties is not to compensate but to punish and deter, giving them a quasi-criminal character akin to punitive damages. *See, e.g.*, *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. 408, 417 (2003) (noting that punitive damages "serve the same purposes as criminal penalties"). Indeed, the California Supreme Court has expressly recognized the "penal objective of civil penalties under the UCL," which is to "punish and deter unlawful conduct." *State v. Altus Fin., S.A.*, 36 Cal. 4th 1284, 1308, 1291 (2005).

Importantly, the penalties remedy is particularly prone to abuse. Ordinary compensatory relief is, by its nature, limited by the extent of damage actually sustained by the state or its citizens, reducing the risk of "governmental overreaching or economic coercion." *Santa Clara*, 235 P.3d at 34. But penalties are not so limited, affording essentially unbridled discretion to a private lawyer to

seek to maximize the number and amount of penalties, regardless of any damage allegedly sustained. *See, e.g.*, Axelrad & Perrochet, *supra*, at 342 (noting that "a penalty that is not tied to an amount needed to cure or abate harm caused by the defendant" is a consideration weighing against the application of *Santa Clara*'s control rule).

In sum, basic principles of due process compel application of a per se rule against retention of private counsel on a contingency-fee basis in cases where – as here – the underlying proceeding is quasi-criminal in nature. Because the district court erroneously failed to apply that rule in this case, its order dismissing plaintiff's § 1983 action should be reversed.

II. THE USE OF CONTINGENCY-FEE COUNSEL IN QUASI-CRIMINAL ENFORCEMENT SUITS IS A GROWING PROBLEM THAT NEEDS TO BE ADDRESSED.

The Court should also reverse the lower court's ruling because it gives a green light to the practice of outsourcing quasi-criminal litigation to profit-seeking attorneys, a recurring problem that reflects poorly on the judicial system. The UCL suit is just one of a growing number of cases in which state attorneys general or municipal attorneys have abdicated their duties by delegating quasi-criminal enforcement power to self-interested private attorneys. These arrangements promote unseemly quid pro quo relationships between government officials and

private lawyers and undermine public confidence in the justice system, underscoring the need for strict judicial oversight.

Over the past few decades, contingency-fee arrangements have led to "the creation of a new model for state-sponsored litigation that combines the prosecutorial power of the government with private lawyers aggressively pursuing litigation that could generate hundreds of millions in contingent fees." Richard O. Faulk & John S. Gray, *Alchemy in the Courtroom? The Transmutation of Public Nuisance Litigation*, 2007 Mich. St. L. Rev. 941, 968. The genesis of this practice can be traced to litigation in the 1980s, when Massachusetts hired outside counsel on a contingency-fee basis to prosecute claims over asbestos removal. *Id.*

Since then, state attorneys general have used this model to mount aggressive enforcement actions against the entire spectrum of the business community. *See* Martin H. Redish, *Private Contingent Fee Lawyers and Public Power: Constitutional and Political Implications*, 18 Sup. Ct. Econ. Rev. 77, 80 (2010) ("In the last ten years, state governments have increasingly resorted to this practice in their efforts to pursue 'big money' claims against alleged tortfeasors."). For example, the state of Rhode Island employed outside counsel to sue former manufacturers of lead paint and pigment from 2003 to 2008. Leah Godesky, *State Attorneys General and Contingency Fee Arrangements: An Affront to the Neutrality Doctrine?*, 42 Colum. J.L. & Soc. Probs. 587, 589 (2009). Similarly,

Oklahoma's Attorney General hired outside firms to sue poultry companies that allegedly polluted the state's waterways with chicken manure. *See id.* Additionally, attorneys general have entered into contingency-fee contracts with outside counsel to prosecute a wide range of lawsuits against the pharmaceutical industry, alleging failure to warn, fraudulent advertising or off-label promotion of prescription medications. *See* Lise T. Spacapan, Douglas F. McMeyer & Robert W. George, *A Threat to Impartiality: Contingency Fee Plaintiffs' Counsel and the Public Good?*, In-House Def. Q., Winter 2011, at 12, 14.

The breadth of the practice cannot be overstated: in one recent study of the 50 states and the District of Columbia, 36 attorney general offices reported using contingency-fee counsel. *Id.*[4] Such reliance on outside counsel can be expected to increase as state legislatures increasingly call on attorney general consumer-protection and Medicaid-fraud units to contribute to their own budgets or become self-funded. *See* Dave Boucher, *Attorney General Outlines Changes; Legislation Aims to Alter Way Official Handles Money from Settlements*, Charleston Daily Mail, Apr. 24, 2013, at P1A, http://web.wvgazettemail.com/News/201304230240 (referencing a bill passed by the West Virginia legislature that would take $7.46 million from the attorney general's Consumer Protection Fund and distribute it

elsewhere in the state budget). This is all the more true because Congress has increasingly given state attorneys general authority to enforce federal laws.[5] And there will be no shortage of private lawyers eager to take on those representations. As one commentator noted in the *Wall Street Journal*:

> Trial lawyers love these deals. Even aside from the chance to rack up stupendous fees, they confer a mantle of legitimacy and state endorsement on lawsuit crusades whose merits might otherwise appear chancy. Public officials find it easy to say yes because the deals are sold as no-win, no-fee. They're not on the hook for any downside, so wouldn't it practically be negligent to let a chance to sue pass by?

Walter Olson, *Tort Travesty*, Wall St. J., May 18, 2007, at A17, http://www.wsj.com/articles/SB117944943332207043.

The growth of this practice has adversely affected the public's perception of the justice system. In particular, contingency-fee arrangements with private counsel create an opportunity for unseemly liaisons between public enforcement officials and private, profit-motivated lawyers. In Mississippi, for example, the Attorney General, Jim Hood, retained 27 law firms to represent Mississippi in 20 separate lawsuits over a five-year span, and "some of Mr. Hood's largest campaign

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[4] This number does not include the use of contingency-fee counsel in the tobacco litigation during the 1990s. *See* Spacapan, McMeyer & George, *supra*, at 14.

[5] For example, state attorneys general are authorized to enforce the Truth in Lending Act's mortgage mandates, 15 U.S.C. § 1640(e), and the Health Insurance Portability and Accountability Act's privacy provisions, 42 U.S.C. § 1320d-5(d).

donors are the very firms to which he's awarded the most lucrative state contracts." Editorial, *Lawsuit Inc.*, Wall St. J., Feb. 25, 2008, at A14, http://www.wsj.com/articles/SB120389878913889385.

Concern over the effects of such liaisons has generated substantial criticism over the last few years. As one former attorney general who has been an outspoken critic of these liaisons observed, "'[t]hese contracts . . . create the potential for outrageous windfalls or even outright corruption for political supporters of the officials who negotiated the contracts.'" Adam Liptak, *A Deal for the Public: If You Win, You Lose*, N.Y. Times, July 9, 2007, at A10, http://www.nytimes.com/2007/07/09/us/09bar.html?_r=0 (quoting Hon. William H. Pryor, Jr.).

Further, contingency-fee counsel have incentives that, under any "'realistic appraisal of psychological tendencies and human weakness,'" *Marshall*, 446 U.S. at 252 (citation omitted), create a structural conflict between the pursuit of justice and their personal interest in obtaining a substantial financial recovery. In particular, contingency-fee counsel "have a financial incentive to maximize money recoveries, an incentive that would be congruent with a client's interests in private actions but is frequently in tension with a State's public interest role." *Contingent Fees and Conflicts of Interest in State AG Enforcement of Federal Law: Hearing Before the Subcomm. on the Constitution of the H. Comm. on the Judiciary*, 112th

Cong. 48 (2012) (testimony of James R. Copland, Director and Senior Fellow, Center for Legal Policy, Manhattan Institute for Policy Research).

These concerns, coupled with the threat to important due-process rights as highlighted in the previous section and in American Bankers's appellate brief, underscore the importance of developing meaningful judicial limitations on the use of contingency-fee counsel by state attorneys general or other government attorneys. At a minimum, the Court should hold that such arrangements are invalid in quasi-criminal enforcement suits like this one, in which the public's interest in seeing that justice is done and the defendant's interest in receiving the full protections of due process are at their apex. Absent such a standard, liaisons like the one here – between private contingency-fee counsel and state attorneys general or district attorneys – will continue unabated, fueling unreasonable verdicts, eroding public trust in judicial proceedings and undermining due process.

CONCLUSION

For the foregoing reasons, the Court should reverse the judgment of the district court.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

Counsel certifies as follows:

1. This brief complies with the type-volume limitations of Federal Rules of Appellate Procedure 29(d) and 32(a)(7)(B) because this brief contains 3,924 words, excluding the parts of the brief exempted by Federal Rule of Appellate Procedure 32(a)(7)(B)(iii).

2. This brief complies with the typeface requirements of Federal Rule of Appellate Procedure 32(a)(5) and the type-style requirements of Federal Rule of Appellate Procedure 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Microsoft Office Word 2003 in 14-point Times New Roman font.

/s/John H. Beisner
John H. Beisner

9th Circuit Case Number(s) 16-16103

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