Study J-901 August 9, 1999

First Supplement to Memorandum 99-32

Award of Costs and Contractual Attorney's Fees to Prevailing Party: Comments on Scope of Study

The Commission has received the following letters commenting on the scope of its study, which currently focuses on revising the definitions of "prevailing party" in Civil Code Section 1717 and Code of Civil Procedure Section 1032:

This supplement discusses those comments and other recent developments in the area of contractual attorney's fees.

DEFINITION OF PREVAILING PARTY: DISMISSAL

Bet Tzedek Legal Services (hereafter, "Bet Tzedek") raises one issue that is clearly within the scope of this study: Whether to revise Section 1717's mandate that there is no prevailing party in the event of a voluntary dismissal or dismissal pursuant to a settlement. Bet Tzedek urges the Commission to reexamine this rule, because it "can lead to one-sided results." (Exhibit p. 6.) Specifically,

> [a] plaintiff can file a case, vigorously litigate it, and then dismiss it at the eleventh hour after it becomes apparent that the defendant is about to prevail. We have seen this happen in unlawful detainer cases after a summary judgment motion has been filed, and even after the trial has started. Some judges are willing to accept a voluntary dismissal without prejudice even after issuing a tentative ruling for the tenant. A landlord can thus file a frivolous eviction case with impunity, with no risk of paying attorneys' fees even if the tenant and his or her attorney have to expend considerable resources to contest the case.

(*Id.*)

Bet Tzedek suggests amending the first paragraph of Section 1717(b)(2) as follows:

> (b)(2) Where an action has been voluntarily dismissed or dismissed pursuant to a settlement of the case, there shall be no prevailing party for purposes of this section. This exception shall not apply if the action is voluntarily dismissed after trial has commenced or after the filing of but before a ruling on a demurrer or summary judgment motion.

To the staff's knowledge, Bet Tzedek did not have a copy of Memorandum 99-32 at the time that it made this suggestion. We are interested to know Bet Tzedek's reaction to the alternative approach proposed at pages 17-18 and 22-26 of that memorandum: Establishing a general rule that where a claim covered by an attorney's fee clause is voluntarily dismissed, the court should determine the prevailing party based on the extent to which each party realized its litigation objectives. Generally, such an approach should yield the same result as Bet Tzedek's proposal when an action is voluntarily dismissed after trial has started or a dispositive motion has been filed. It would, however, afford the court latitude to determine that the dismissal was due to factors such as insolvency of the defendant or mootness of the claim, rather than the impending adjudication of the merits. For this reason, **the staff continues to favor the more flexible approach proposed in Memorandum 99-32**. The Commission should, however, keep Bet Tzedek's more bright-line proposal in mind as we proceed with the drafting process.

SCOPE OF STUDY

Two separate sets of issues have been raised concerning the scope of this study: (1) Whether the study should address the extent to which pro bono and public interest attorneys may recover attorney's fees under Section 1717, and (2) whether the study should be expanded to include reassessment of the justice system as a whole. These issues are discussed in turn below.

Application of Section 1717 to Attorneys Who Do Not Charge a Fee or Charge Only a Nominal Fee

Bet Tzedek "would like to see section 1717 amended to make clear that parties represented by public interest organizations or pro bono attorneys are entitled to fees if they are the prevailing party and would otherwise be entitled to seek such

an award." (Exhibit p. 3.) Likewise, the Western Center on Law and Poverty is concerned about the state of the law in this area and urges the Commission to study the issue. (Exhibit pp. 7-8.)

As is more thoroughly explained in the attached memorandum by the Commission's summer legal assistant (Exhibit pp. 9-21), the problem arises because attorney's fees must be "incurred" to be recoverable under Section 1717. In *Trope v. Katz*, 11 Cal. 4th 274, 902 P.2d 259, 45 Cal. Rptr. 2d 241 (1995), the Supreme Court determined that a law firm representing itself in pro per could not recover fees under Section 1717, because it did not "incur" any fees. Relying on *Trope*, the court in *San Dieguito Partnership v. San Dieguito River Valley Regional Open Space Park Joint Powers Authority*, 61 Cal. App. 4th 910, 918, 72 Cal. Rptr. 2d 91 (1998), expressed doubt about whether pro bono attorneys could recover fees under Section 1717, but did not actually resolve the issue. This dictum is troubling to Bet Tzedek and Western Center, because it raises the specter that "low income residential tenants will again become the victims of one-way fee agreements." (Exhibit p. 7.) As Bet Tzedek explains:

> The fundamental purpose of section 1717 is to address the inequality in bargaining positions that results in contracts having one-sided attorneys' fees provisions. Providing attorneys' fees to poor litigants represented free of charge fulfills this purpose by ensuring that both sides have access to counsel and both sides bear an equal risk of paying the other side's fees if they breach the contract. If pro bono attorneys are excluded from the ambit of the provision, parties will bear little risk in suing the indigent or the elderly, and those with the least access to justice will find themselves to be even more attractive and defenseless targets.

(Exhibit p. 4.)

The problems are not limited to the context of pro bono and public interest attorneys. There is also uncertainty about the extent to which a party represented by in-house counsel may recover fees, because in-house counsel typically do not charge fees in the usual sense. Although recovery of such fees under Section 1717 was permitted in a recent decision (*PLCM Group, Inc. v. Drexler*, 1999 Daily Journal D.A.R. 5126 (June 1, 1999)), the facts of that case were unusual and it is not clear whether courts will reach the same result in other cases involving in-house counsel. (See Exhibit p. 18.) In some instances, it may also be difficult to distinguish between an in-house counsel and a pro per attorney. (See *id.* at 18-19, 21.)

Additionally, it may even be worth reexamining the principle that pro per attorneys and other pro per litigants are not entitled to fees under Section 1717. Just recently, the Supreme Court again reaffirmed that the "goal of section 1717 is full mutuality of remedy between parties to a contract, whether plaintiffs or defendants, in the matter of attorney fees." *Scott Co. of California v. Blount, Inc.*, 1999 Daily Journal D.A.R. 7311 (July 19, 1999). Denying fees to pro per attorneys and other pro per litigants is inconsistent with that principle. While calculating fees for pro per litigants would raise issues, these may not be insurmountable. *See, e.g.*, Waldman, *Pro Se Can You Sue?: Attorney Fees for Pro Se Litigants,* 34 Stan. L. Rev. 659 (1982) (proposing a basis for valuing awards to pro se litigants).

In sum, **the staff is convinced that this area — recovery of attorney's fees under Civil Code Section 1717 by pro per litigants, in-house counsel, pro bono attorneys, and public interest attorneys charging nominal fees — is ripe for clarification**. It would be hard to revise the definitions of prevailing party in Civil Code Section 1717 and Code of Civil Procedure Section 1032 without getting into these issues. **The Commission should tackle them head-on in this study**.

Expansion of This Study to Include Reassessment of the Justice System

Luther Avery of Avery & Associates in San Francisco writes that "a study of attorney's fees and related issues is probably too limited; what is needed is revision of the whole of the alleged justice system and its cost to society." (Exhibit p. 1.) He explains:

> In my youth I used to think the British system of awarding costs to the prevailing party would cure the U.S. problem of excess fees and costs. After considerable study I am now convinced that the British example will not solve the problem, for two reasons: (1) the U.S. problem of costs of litigation cannot be solved by retaining the present system of dispute resolution, and (2) the British rule has not solved the same problems in Britain or elsewhere in the world, the British example has exacerbated the cost problem.

(*Id.*)

As currently conceptualized, this study would not involve reassessment of the American and the British rules for recovery of attorney's fees. Rather, the Commission is focusing on more technical issues relating to recovery of contractual attorney's fees under Civil Code Section 1717 and costs under Code of Civil Procedure Section 1032. **We believe this scope is appropriate**.

Addressing these more technical issues may not fix the justice system as a whole, but it may eliminate some injustices and reduce inefficiencies stemming from lack of clarity in the current statutes.

The Commission is already engaged in another study more along the lines that Mr. Avery suggests: Its joint study with the Judicial Council on revising California procedure to take advantage of trial court unification. The sources that Mr. Avery cites in his letter (Exhibit p. 2) may be helpful in that endeavor. As the Commission develops proposals, it should also keep in mind his advice that the "issue of the CLRC should not be to control costs but to eliminate costs without injury to society or the participants." (*Id.*)

OTHER DEVELOPMENTS

The law on recovery of attorney's fees and costs is rapidly evolving. In the time since the staff wrote Memorandum 99-32, we have learned of several new court of appeal decisions touching on issues relevant to this study. See *Nelson v. Anderson*, 84 Cal. Rptr. 2d 753 (1999) (full costs award where defendant won suit against nonsettling plaintiff but waived costs in settlements with two other plaintiffs (see Memorandum 99-32, pp. 14-15)); *Agrarian v. Rattan*, 1999 Daily Journal D.A.R. 7833 (July 30, 1999) (pro per attorney may recover costs but not attorney fees after successful discovery motion); *PLCM Group, Inc. v. Drexler*, 1999 Daily Journal D.A.R. 5126 (June 1, 1999) (recovery of attorney's fees by in-house counsel under Section 1717); see also *Kyle v. Carmine*, 84 Cal. Rptr. 2d 303 (1999) (discussing but not resolving SLAPP procedural issue described at pages 34-35 of Memorandum 99-32).

In addition, the Supreme Court decided *Scott Co. of California v. Blount, Inc.*, 1999 Daily Journal D.A.R. 7311 (July 19, 1999), which discussed the prevailing party requirements of Civil Code Section 1717 and Code of Civil Procedure Section 1032, and clarified the relationship between those provisions and Code of Civil Procedure Section 998. As we work on this study, it may be appropriate to codify the result in *Scott*, or at least refer to the decision in a Comment. The Commission need not decide that matter now; the staff will raise it again as we get into the drafting process.

The critical point for the time being is that we need to be alert to new developments and account for them as we proceed. The staff encourages Commissioners and other interested persons to provide information on

significant new cases and other developments, to help ensure that important considerations are not inadvertently overlooked.

Respectfully submitted,

Barbara S. Gaal
Staff Counsel

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June 23, 1999

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Re: Attorney's Fees

Dear Ms. Gaal:

Your letter arrived June 18 while I was out of town and described a public meeting June 24-25, 1999 in Sacramento. I will be out of the country at that time.

By reason of the fact I've taught law office economics and management in three California law schools, and I've practiced law for 47 years, and for many other events that qualify me as an expert, I am qualified to express an opinion on attorney's fees (law and fact). Yes, I would like to be on the mailing list.

Unfortunately, a study of attorney's fees and related issues is probably too limited; what is needed is revision of the whole of the alleged justice system and its cost to society. I'm also an expert qualified on that subject. I say the study is too limited because your letter enclosed a copy of Memo 99-32, "Award of Costs and Contractual Attorney Fees to Prevailing Party." In my youth I used to think the British system of awarding costs to the prevailing party would cure the U.S. problem of excess fees and costs. After considerable study I am now convinced the British example will not solve the problem, for two reasons: (1) the U.S. problem of costs of litigation cannot be solved by retaining the present system of dispute resolution, and (2) the British rule has not solved the same problems in Britain or elsewhere in the world, the British example has exacerbated the cost problem.

Aside from volunteering, which I hereby do (against my rule from military service to never volunteer for government service), what do you want, if anything? Are you simply notifying me I can complain as I seem to do about other works by CLRC? Or, are you

suggesting that I appear June 24-25, which I cannot do because of prior commitments. Or, are you seeking ideas, which you may or may not welcome? Or, what?

Incidentally, I assume you understand by saying there is a problem for greater than shifting costs and fees, I assume the present justice operations cost too much to everyone. However, the last thing I would support would be price controls. In fact, as to shifting of costs and fees, I invite your attention to de Kieffer, How Lawyers Screw Their Clients (Barricade Books, Inc., N.Y., 1995). Moreover, as a clear exposition of the nature of the real problem, I invite your attention to Olson, The Litigation Explosion (Dutton, N.Y., 1991). And, in addition, for potential areas of solution, I invite your attention to Epstein. Simple Rules For A Complex World (Laissez-Faire Books, 24). In fact, you should also review Tullock, Trials on Trial (Columbia U.P., N.Y., 1980) on pure economic theory relating to trials, and Kubey, You Don't Always Need A Lawyer (Consumer Reports Books, 1991).

The issue of the CLRC should not be to control costs but to eliminate costs without injury to society or the participants.

I have opinions on Memorandum 99-38 which you also sent me. There my views relate to Probate Law, another area in which I believe I qualify as an expert. But I must restrain myself.

Very truly yours,

Luther J. Avery

LJA cet

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July 8, 1999

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Re: Study of Attorneys' Fees and Related Issues

Dear Ms. Gaal:

We understand that the California Law Review Commission is currently studying proposals for legislation in the area of attorneys' fees. We would like to request that the Commission consider two amendments to Civil Code § 1717, which deals with attorneys' fees awarded under a contract.

Attorneys' fees for public interest organizations or pro bono lawyers

First, we would like to see section 1717 amended to make clear that parties represented by public interest organizations or pro bono attorneys are entitled to fees if they are the prevailing party and would otherwise be entitled to seek such an award.

Civil Code § 1717 establishes a reciprocal right to attorneys' fees even if the contract itself provides attorneys' fees only to one party. In Beverly Hills Properties v. Marcolino, 221 Cal.App.3d Supp. 12, 270 Cal.Rptr. 605 (1990), the Court of Appeals held that a prevailing party is entitled to attorneys' fees under section 1717 even if that party is represented by a public interest organization that does not charge its clients. That ruling was consistent with the reciprocity rationale underlying section 1717.

We believe that Marcolino is still good law. However, in San Dieguito Partnership v. San Dieguito River Valley Reg'l Open Space Park Joint Powers Authority, 61 Cal.App.4th 910, 91 Cal.Rptr.2d 91 (1998), the Court of Appeals questioned the viability of Marcolino in light of Trope v. Katz, 11 Cal.4th 274, 45 Cal.Rptr. 2d 241 (1995).

Trope held that a law firm representing itself in pro per could not recover fees. San Dieguito refused to award fees above the below-market rate actually charged by

counsel. Although neither case involved public interest or pro bono attorneys, Marcolino is in jeopardy in light of both cases' focus on the requirement in the statute that attorneys' fees be "incurred" by the party seeking a fee award.

We believe that providing attorneys' fees to public interest firms or pro bono attorneys who do not charge their clients is completely consistent with, and in fact is required by, the legislative purpose of mutuality underlying section 1717. Without fees in such circumstances, poor litigants would be unable to obtain or compensate their counsel. Although fees are available under section 1717 if there is a contingent fee agreement, see Gonzales v. Personal Storage, Inc., 56 Cal.App.4th 464, 65 Cal.Rptr.2d 473 (1997); Stafford v. Sipper, 76 Cal.Rptr.2d 723 (1998), this does not help a poor litigant if the amount in dispute is too small, or if the prevailing party is the defendant, who does not recover anything.

The fundamental purpose of section 1717 is to address the inequality in bargaining positions that results in contracts having one-sided attorneys' fees provisions. Providing attorneys' fees to poor litigants represented free of charge fulfills this purpose by ensuring that both sides have access to counsel and both sides bear an equal risk of paying the other side's fees if they breach the contract. If pro bono attorneys are excluded from the ambit of the provision, parties will bear little risk in suing the indigent or the elderly, and those with the lease access to justice will find themselves to be even more atrractive and defenseless targets.

We suggest one of the following amendments to section 1717(a):

"In any action on a contract, where the contract specifically provides ~~that~~ for an award of attorneys' fees and costs~~, which are incurred to enforce that contract, shall be awarded~~ either to one party or to the prevailing party, then the party who is determined to be the party prevailing on the contract, whether he or she is the party specified in the contract or not, shall be entitled to reasonable attorney's fees in addition to other costs."

OR:

"Attorneys' fees and costs shall be deemed to be incurred for purposes of this section even if the party is represented free of charge by a public interest law firm or a pro bono attorney."

Attorneys' fees when case is dismissed

Section 1717 also provides that "Where an action has been voluntarily dismissed or dismissed pursuant to a settlement of the case, there shall be no party prevailing on the contract for purposes of this section." Civil Code § 1717(b)(2). In Santisas v. Goodin, 17 Cal.4th 599, 71 Cal.Rptr.2d 830 (1998), the California Supreme Court held that fees are unavailable if the case is dismissed, even if the contract says otherwise.

Here again, this can lead to one-sided results. A plaintiff can file a case, vigorously litigate it, and then dismiss it at the eleventh hour after it becomes apparent that the defendant is about to prevail. We have seen this happen in unlawful detainer cases after a summary judgment motion has been filed, and even after the trial has started. Some judges are willing to accept a voluntary dismissal without prejudice even after issuing a tentative ruling for the tenant. A landlord can thus file a frivolous eviction case with impunity, with no risk of paying attorneys' fees even if the tenant and his or her attorney have to expend considerable resources to contest the case.

We recommend that section 1717(b)(2) be amended to add the following:

"This exception shall not apply if the action is voluntarily dismissed after trial has commenced or after the filing of but before a ruling on a demurrer or summary judgment motion."

Mailing list

We would appreciate being added to your mailing list and being kept informed of any developments in the area of attorneys' fees.

If you need any further information, please feel free to contact David Lash at (323) 549-5812 or Lauren Saunders at (323) 549-5878. Thank you very much for your consideration of these proposals.

Yours very truly,

David A. Lash
Executive Director

Lauren K. Saunders
Directing Attorney
Housing Conditions Project

/lks

cc: Richard Rothschild

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June 24, 1999

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Re: Law Revision Commission Study of Attorney's Fees

Dear Ms. Gaal:

Thank you putting me on the mailing list for the Law Revision Commission's study of attorneys' fees awarded by contract. As we discussed on the telephone, I propose that the Commission include within its study an analysis of problems that have arisen because of Trope v. Katz, 11 Cal.4th 274 (1995). In Trope, the California Supreme Court held that since Section 1717 speaks of attorneys' fees "incurred," a law firm suing on its own behalf is not entitled to a fee award under that statute.

I will leave to private attorneys discussion of how Trope may affect their practice (e.g., by encouraging costly hiring of outside firms to collect fees). My concern is Trope's possible effect on nonprofit legal services programs that represent consumers and tenants. A pre-Trope case, Beverly Hills Properties v. Marcolino, 221 Cal.App.3d Supp. 7 (1990), held that non-profit legal services programs such as (in that case) Bet Tzedek Legal Services are entitled to a fee award under Section 1717 even though Bet Tzedek does not charge its clients fees. In a later case, however, the Court of Appeal in dictum stated that Beverly Hills Properties "is not persuasive" in light of Trope. San Dieguito Partnership v. San Dieguito River Valley Regional Open Space Park Joint Powers Authority, 61 Cal.App.4th 910, 918 (1998).

While it is by no means clear that the San Dieguito dictum accurately states the law, it is troubling that a court could even question in dictum that legal services programs are not entitled to fees under Section 1717. The very purpose of Section 1717 was to level the playing field--at least for attorneys' fees--when parties to a contract have unequal bargaining power. Yet, if the San Dieguito dictum becomes law, low income residential tenants will again become the victims of one-way fee agreements. Landlords can use leases specifying that in the event of litigation fees "incurred" will be awarded to the prevailing party, knowing that their tenants cannot afford to pay an attorney and will be represented, if at all, pro bono. A prevailing landlord will be awarded fees, while no fees will be awarded if the tenant prevails. This

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"heads the landlord wins, tails the tenant loses" result was not one the Legislature intended. The Law Revision Commission should study this issue.

Very truly yours,

Richard A. Rothschild
Director of Litigation

Lauren Sanders
Richard Pearl

RAR/ac

August 9, 1999

To: California Law Revision Commission

From: Julian M. Davis

Re: Recovery of contract attorney fees under Civil Code § 1717

Introduction

Civil Code Section 1717 (hereafter, "Section 1717") allows parties to a contract to recover attorney fees when the contract specifies that at least one of the parties may recover attorney fees from litigation to enforce the contract. The intent of the statute is to provide a reciprocal right to recover when attorney fees are available for only one party to "prevent oppressive use of one-sided attorney fee provisions"[1], particularly those used in adhesion contracts. *In International Industries Inc. v. Olen,* the court stated the purpose of Section 1717 is to build "a reciprocal right to attorney's fees into contracts" which reflects "legislative intent that equitable considerations must prevail over both the bargaining power of the parties and the technical rules of contractual construction."[2]

The Western Center on Law and Poverty and Bet Tzedek Legal Services are concerned about language in recent court decisions construing Section 1717, which might (but need not necessarily) be interpreted to mean that *pro bono* and public interest attorneys and their clients are not entitled to recover attorney fees even though the other party to the contract may recover fees. The current state of public interest, *pro bono* and in-house attorneys' ability to recover under Section 1717 is confused. The problem centers on the construction given to Section 1717 by the California Supreme Court in *Trope v. Katz*[3]. This memo discusses the state of the law before *Trope*, describes the decision in *Trope*,

[1] Milman v. Shukhat, 22 Cal. App. 4th 538, 543, 27 Cal. Rptr. 2d. 526 (1994)(paraphrasing Reynolds Metals Co. v. Alpherson, 215 Cal. 3d. 124, 128, 158 Cal. Rptr. 1 (1979)).
[2] International Industries Inc. v. Olen, 21 Cal. 3d. 218, 224, 145 Cal. Rptr. 691, 577 P.2d 1031 (1978).
[3] 11 Cal. 4th 274, 45 Cal. Rptr. 2d 241, 902 P.2d 259 (1995).

and then analyzes the more recent cases, concluding with recommendations on Section 1717.

Pre-*Trope* Cases

Civil Code Section 1717 was enacted in 1968. It has been amended four times, yet "all courts agree that the purpose of the statute when it was enacted, after the amendments and now is to establish mutuality of remedy when the contract makes recovery of attorney fees available to only one party."[4] Since its inception, Section 1717 had been construed expansively to insure a reciprocal right to recover where at least one of the parties has such a right under the contract.[5] However, the law was unclear on whether Section 1717 applied to attorneys appearing *in propria persona.*

California courts had previously denied attorneys representing themselves a recovery of attorney fees under analogous fee shifting provisions.[6] The question of whether attorney fees were recoverable under Section 1717 for attorneys appearing *in propria persona* was answered affirmatively in *Renfrew v. Loysen*[7]. *Renfrew's* holding was based on a footnote in *Consumer's Lobby Against Monopolies v. Public Utilities Commission*.[8] The issue in *Consumer's Lobby* was whether the Public Utilities Commission could award attorney fees in an administrative proceeding to a non-attorney who obtained a favorable ruling that created a public benefit. Opponents of the award argued that past precedents were against awarding of attorney fees to non-attorneys as well as attorneys representing themselves. Although not on point in the decision, the Court stated in a footnote that "although such an attorney does not pay a fee or incur any financial liability therefor to another, his time spent in preparing and presenting his case is not somehow rendered less valuable because he is representing himself rather than a third

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[4] Deborah K. Orlick, Renfrew v. Loyson: Birth, Life and Death of an Erroneous Decision, 31 Beverly Hills B.A.J. 19, winter/ spring (1997).
[5] *See e.g.*, Reynolds Metals Co. v. Alperson, 25 Cal. 3d 124, 158 Cal. Rptr. 1, 599 P.2d 536 (1979)(nonsignatory to contract may recover attorney's fees under Section 1717).
[6] *See* Patterson v. Donner, 48 Cal. 369 (1874); City of Long Beach v. O'Donnell, 91 Cal. App. 760 (1928); O'Connel v. Zimmerman, 157 Cal. App. 2d 330 (1958).
[7] Renfrew v. Loysen, 175 Cal. App. 3d 1105, 222 Cal. Rptr. 413 (1985).
[8] 25 Cal. 3d 891, 603 P.2d 41, 160 Cal. Rptr 124 (1979).

party."[9] The footnote went further stating, "it would appear he [the attorney] should be compensated when he represents himself if he would otherwise be entitled to such compensation."[10] *Renfrew* and *Leaf v. City of San Mateo*[11] together elevated this footnote into precedent.

In *Leaf,* the First District Court of Appeal broke from the general rule of no recovery of attorney fees for *pro per* attorneys established in past precedents. The court cited the *Consumer Lobby* footnote as evidence that a majority of the justices of that court questioned the logic of past decisions.[12] *Leaf* then held that a *pro per* could recover reasonable attorney fees in an inverse condemnation proceeding.

Renfrew was the first case to decide the issue of recovery of attorney fees for *pro per* attorneys under Section 1717. *Renfrew* relied heavily on the reasoning contained in the *Consumer's Lobby* footnote to hold that attorneys representing themselves may recover reasonable attorney fees under Section 1717. In abandoning the general rule against *pro per* recovery, the *Renfrew* court stated "the soundness of this rule has been seriously questioned by the California Supreme Court", citing *Consumer's Lobby*.[13] *Renfrew* served as precedent for fee recovery under Section 1717 for almost a decade before the *Trope* decision. Following *Renfrew,* most litigants, with the exception of *pro se* non-attorneys, could recover reasonable attorney fees under Section 1717 as long as at least one party to the contract could recover fees.

Six years after *Renfrew*, Section 1717 was construed to give the right of recovery of attorney fees to a litigant tenant who was represented *pro bono*. In *Beverly Hills Properties v. Marcolino* [14] the court rejected the notion that fees had to actually be incurred by the party. The court stated: "Section 1717 does not expressly require the prevailing party to incur legal expenses". Rather, "the statute simply provides that a prevailing party is

[9] *Id.* at 915 n. 13.
[10] *Id.*
[11] 150 Cal. App. 3d 1184, 198 Cal. Rptr. 447 (1984).
[12] *Id.* at 449-450.
[13] *Renfrew*, 175 Cal. App. 3d at 1108.
[14] 221Cal. App. 3d Supp. 7, 270 Cal. Rptr. 605 (1990).

entitled to attorney fees and costs" related to the enforcement of the contract, but for no other litigation between the parties.[15] The court felt the statute was ambiguous because it "does not state who, the prevailing party or the attorney representing him, must incur the legal fees and costs."[16] The *Marcolino* court interpreted the statute as providing a reciprocal right to recover attorney fees based on equitable principles. To effectuate the purpose of the statute (providing a reciprocal right of recovery for parties in unequal bargaining positions) the court concluded that it is the litigant's attorney who must incur costs and fees. According to *Marcolino,* the statute allows recovery for a prevailing party "whose attorneys have incurred costs and expenses in defending the prevailing party on the underlying agreement."[17]

Underlying the decision was the realization that the landlord would have been able to recover attorney fees from the tenant had the landlord won the unlawful detainer action. This factor weighed heavily in favor of the court's ruling. Under the ruling it mattered little whether a party achieved representation under a contingent fee, through *pro bono* representation, or had sufficient resources to retain counsel. So long as the attorney was put to expense in litigating the claim, there was a right to recover under Section 1717.

While *Marcolino* did not rely on *Renfrew* in the holding, a later case would rely on both *Renfrew* and *Marcolino* to extend Section 1717 recovery to in-house counsel. In *Garfield Bank v. Folb,*[18] the Second District Court of Appeal found that Stanley Folb, represented by in-house counsel Bradley Folb, could recover attorney fees against Garfield Bank for the bank's unsuccessful suit of Stanley involving a lease agreement. The court reasoned that since attorneys could recover for representing themselves, in-house counsel should be allowed to recover under the same statute. Further, since *Marcolino* reasoned that Section 1717 does not "expressly require the prevailing party to incur legal expenses", it is not critical to recovery that the defendant would have not incurred great expense from

[15] *Id.* at 11.
[16] *Id.*
[17] *Id.*
[18] 25 Cal. App. 4th 1804, 31 Cal. Rptr. 2d 239 (1994).

the use of in-house counsel.[19] The court also relied on similar cases in other states as well as federal cases that allowed recovery for non-profit legal services and in-house counsel. As in *Renfrew* and *Marcolino*, the statute was construed to effectuate its purpose that the right to recover be "reciprocal and reasonable."[20]

Thus, before *Trope*, Section 1717 was construed to give litigants a reciprocal right to recover whether they were charged fees or not. The determination was based on an effort to keep fees reciprocal between litigants when at least one of the parties would be liable, as well as a desire to allow recovery to attorneys whose clients may not be able to pay for legal representation. As a result, in-house counsel, *pro se* attorneys, *pro bono* attorneys and public interest firms could all recover reasonable attorney fees under Section 1717. Only *pro se* non-attorneys were not included in the statute's protection.

Trope

After *Renfrew*, *pro per* attorneys could recover fees under Section 1717 but still could not under similarly worded fee-shifting statutes. Further, in early 1994 the Third District Court of Appeal ruled that non-attorneys could not recover under Section 1717 where the contract specified that the party could recover only "attorney fees" as opposed to "legal services fees".[21] The law in California under Section 1717 was not settled, although it was clear that the trend was for inclusiveness to effectuate the reciprocity purpose behind the statute.

In *Trope*, the California Supreme Court was asked to revisit the issue of attorney fee recovery for *pro per* attorneys under Section 1717. The law firm of Trope & Trope filed suit to recover fees from defendant Katz for services rendered during Katz's divorce proceedings. Katz cross-complained, maintaining that Trope & Trope charged excessive fees for representation. The trial court ruled in favor of Trope & Trope but also found that the fees were excessive. The firm's overall recovery was reduced from $163,000 to

[19] *Id.* at 1807 (quoting *Marcolino*, *supra* note 14, at 11).
[20] *Id.* at 1809.
[21] See Jacobson v. Simons Real Estate, 23 Cal. App. 4th 1285, 28 Cal. Rptr. 2d 699 (1994).

$44,500. Trope & Trope then moved for an award of attorney fees pursuant to its fee agreement with Katz. The law firm had represented itself throughout the litigation. A special referee found against Trope & Trope on the issue of recovery of attorney fees. The special referee found *Patterson* and its progeny persuasive and declined to follow *Renfrew*. The referee's decision was affirmed by the court of appeal, thus establishing two lines of cases, those that followed *Renfrew* and those that followed the old rule from *Patterson*.

The California Supreme Court decided the conflict by looking to legislative intent, giving the terms in the statute their "usual and ordinary" meaning.[22] The court focused on the terms "incurred" and "attorney fee". The court found "incur a fee" to mean "to become liable for it" or "to become obligated to pay it".[23] Similarly, the court found "attorney fee" to mean "the consideration that a litigant actually pays or becomes liable to pay in exchange for legal representation".[24] The court found that a *pro se* attorney "pays no such compensation" and thus cannot recover under Section 1717. The court reaffirmed *Patterson* and its progeny holding that attorneys appearing *in propria persona* cannot recover attorney fees "under either a statutory exception to the American rule or under a contractual attorney fee provision".[25]

The court reasoned in *Renfrew* that the *Consumer's Lobby* footnote called into question the logic of *City of Long Beach v. Sten*[26] and *Patterson*. *Renfrew* declined to follow the older cases and charted a new course for *pro se* fee recovery under Section 1717. *Trope* pointed out that *Sten* and *Patterson* were binding precedent in *pro se* fee recovery suits. The *Consumer's Lobby* footnote was mere dicta that did not have the force

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[22] *Id.* at 280.
[23] *Id.* [quoting from Webster's New International Dictionary (3d ed. 1961)].
[24] *Id.*
[25] *Id.* at 281.
[26] 206 Cal. 473, 274 P. 968 (1929) (holding that an attorney representing himself in a condemnation proceeding cannot recover attorney fees under Civil Procedure section 1255a, thus extending ban on pro se recovery of attorney fees to cover statutory cases as well as contractual cases [*See Patterson*, *supra* note 6]).

of law necessary to overturn past precedent. Thus, the *Trope* court reasoned, it was error for *Renfrew* and *Leaf* to decline to follow precedent.

The Court's reliance on the *Sten* and *Patterson* line of cases is significant, because they stand for the proposition that "the usual and ordinary meaning of the phrase 'reasonable attorney's fees' is the consideration that a litigant pays or becomes liable to pay in exchange for legal representation."[27] Since a *pro per* attorney does not become liable to pay an attorney fee to another, the attorney may not recover under the statute.

The *Renfrew* decision was based in part on the notion that, if the court had ruled otherwise, one of the parties would be entitled to attorney fees but the other party would not. In *Trope*, however, the Court expressed concern about allowing *pro per* attorneys to recover and not non-attorneys. This would create an imbalance between attorney *pro se* litigants and other non-attorney *pro se* litigants "and grant different rights and remedies to each."[28] In addition, *Trope* seems to imply that the *party* incur the fee as opposed to the *attorney*, a significant distinction for *pro bono* litigants. The overruling of *Renfrew* meant cases relying on its reasoning were now suspect in light of *Trope*.

Post-*Trope* decisions

Trope specifically declined to decide the issue presented in *Garfield Bank*: whether in-house counsel could recover reasonable attorney fees under Section 1717. Also left undecided was whether *pro bono* and public interest firms that did not charge their clients fees could recover reasonable attorney fees under Section 1717. The reasoning of *Trope* suggests that if the client did not pay or become liable to pay attorney fees to the attorney, reasonable attorney fees could not be recovered. The decision suggests that it is the client that has the right to recover and not the attorney. Though *Trope* professed to decide the narrow issue of *pro per* recovery, in fact its language has proven to be sweeping, affecting all parties under Section 1717.

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[27] *Id.* at 282.
[28] *Id.* at 277.

In 1996, the Bankruptcy Appellate panel of the Ninth Circuit had to decide whether an attorney who represented himself before the *Trope* decision could be barred from recovery through retroactive application of *Trope*. The panel not only concluded that *Trope* could be applied retroactively, but also reasoned that "the fact that [the *pro per* attorney] did not bill the other defendants (whom he claimed he represented) is critical because the California Supreme Court based its decision on strict statutory construction of the words 'incur' and 'attorney fees'."[29] Since the other defendants "were not contractually obligated to pay", the panel declined to award attorney fees under Section 1717.[30]

The *pro per* attorney (Albertini) contended that since he used associates in his law firm to litigate part of the case, he could recover under an in-house counsel theory based on *Garfield Bank*. While acknowledging that *Trope* was intentionally silent on the issue of in-house counsel, the panel stated that it was not at all clear whether Trope & Trope had any employees other than its partners to whom it was liable for fees. The panel also said that "Albertini is Albertini & Gill" and "no distinction can be made between them."[31] The court rested its final determination based on reasoning from the "binding portion" of the *Trope* decision:

> Albertini has incurred an obligation to pay his associates, but that duty arises out of the fact that he hired them to work for his firm, not because he specifically hired them in this litigation. ...The fact that Albertini chose to divert his associates from work for his clients to work for himself does not change his obligation to his associates and therefore does not cause him to have incurred attorney's fees to his associates.[32]

The panel in *In re Job* thus took a literal reading of *Trope*, and extended *Trope*'s reasoning in denying recovery under *pro per* and in-house arguments. In doing so, *In re Job* called into question the holding of *Garfield Bank*.

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[29] *In re Job*, 198 B.R. 763, 767 (1996).
[30] *Id.* at 768.
[31] *Id.*
[32] *Id.* at 769.

Another case, *San Dieguito Partnership v. San Dieguito River Valley Regional Open Space Park Joint Powers Authority*,[33] has called into question *Marcolino* and may well bar recovery for public interest firms and *pro bono* attorneys that do not charge at least a nominal or contingent fee. In *San Dieguito*, the San Dieguito River Valley Regional Open Space Park Joint Powers Authority (JPA) successfully defended an action against it. The JPA moved for attorney fees under a settlement agreement entered into prior to the underlying suit. The underlying agreement provided that the prevailing party may recover "an award in the amount of attorneys' fees and costs incurred in connection with the prosecution or defense of such action."[34] Attorneys for JPA only billed JPA $110 per hour in attorney fees when the going rate for their services was $180-$190.[35]

The court denied JPA's request for both an enhancement of the fees and a lodestar determination of reasonable attorney fees. Citing *Trope*, the court reasoned that the purpose of recovery of reasonable attorney fees under Section 1717 "is to reimburse a party for attorney fees the party has paid, or to indemnify the party for fees the party has become liable to pay, provided the fees so paid or incurred are reasonable."[36]

As interpreted in *San Dieguito*, Section 1717 only allows recovery by parties who were actually charged an attorney fee for representation, because only such a party would be in need of reimbursement or indemnification. Section 1717, under the *San Dieguito* interpretation, does not allow recovery for fees the court considers to be unreasonable.

San Dieguito states that *Marcolino* "is not persuasive" because *Marcolino* reasoned that the determination of whether fees were incurred should focus on whether the fees were incurred by the attorney, as opposed to the litigant. According to the court in *San Dieguito*, the *Marcolino* argument "was repudiated by the California Supreme Court in *Trope*" because that court read Section 1717 as specifying that attorney's fees "are the consideration that a *litigant* actually pays or becomes liable to pay", not the *litigant's*

[33] 61 Cal. App. 4th 910, 72 Cal. Rptr. 2d 91 (1998).
[34] *Id.* at 914.
[35] *Id.* at 916.
[36] *Id.* at 918.

attorney.[37] *San Dieguito* thus suggests, although in dicta, that *Trope* has disapproved of *Marcolino's* reasoning and holding, leaving no protection for *pro bono* or public interest attorneys to recover fees.

In *PLCM Group Inc. v. Drexler*[38], the Second District Court of Appeal recently revisited the issue of fees for in-house counsel, this time with respect to corporate in-house counsel. The court allowed the plaintiff subsidiary of a larger parent corporation to recover reasonable attorney fees, principally because it used the larger corporation's in-house counsel department to litigate the case. The court found that although *Trope* disapproved of aspects of *Garfield Bank*, *Trope* specifically left undisturbed the question of whether in-house counsel may recover attorney fees under Section 1717.[39] However, the court also concluded that "under our Supreme Court's definition of 'incurred' and 'attorneys fees', expenses for work in-house legal counsel performs are recoverable as attorney fees under Civil Code Section 1717 to the extent they constitute consideration that the litigant became liable to pay in exchange for counsel's representation."[40]

The in-house recovery allowed in *PLCM* differs from the in-house representation discussed in *In re Job* and *Trope*, in that *PLCM* involves corporate in-house counsel and not the in-house counsel of a law firm. The distinction is significant because the parent corporation of PLCM establishes costs and billing for its in-house services to each subsidiary on the basis of the number and complexity of the subsidiary's usage of the legal services department. There is a correlation between the compensation the subsidiary must pay to in-house counsel and the amount of billable hours in-house counsel works on a particular case. This arrangement closely mirrors that of a separate law firm. It was not a stretch to determine that the litigant, PLCM, incurred a fee for the legal services of its parent corporations in-house counsel. Such a billing arrangement may not be the norm,

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[37] *Id.* (emphasis added).
[38] 1999 Daily Journal D.A.R. 5126 (1999).
[39] *Id.* at 5128.
[40] *Id.*

however, particularly for smaller corporate firms or law firms. It is unlikely that the recovery of fees for in-house counsel will be uniform.

Current State of Section 1717

This survey of cases and trends reveals growing ambiguity and uncertainty under Section 1717. At first it was hardly doubted that public interest and *pro bono* litigants could recover attorney fees. A literal interpretation of *Trope* would preclude recovery by any organization or individuals providing free legal representation, unless they charge a nominal fee or their clients enter into a contingency fee agreement. The legislative intent of Section 1717 to aid persons in unequal bargaining positions by providing a reciprocal right to recover is arguably in doubt. Several difficulties now exist with the application of this statute.

1. There is difficulty in defining in-house counsel and acknowledging whether a firm's corporate structure allows it to recover attorney fees under Section 1717.
2. There is a disincentive to provide public interest agencies with discounted legal fees because, under the current construction of the statute, only the fees actually charged are recoverable.
3. The statute no longer protects those who are in need of free legal service, but these individuals are usually most in need of protection from attorney fee shifting contracts and most often find themselves in an unequal bargaining position.
4. It is difficult to distinguish between an attorney appearing *in propria persona* and in-house counsel for a law firm.

It seems ironic that *pro bono* and public interest litigants would not be able to recover reasonable attorney fees while the other party to the contract may, since the other party is far more likely to hold the bargaining advantage in the underlying contract. Section 1717 was intended to rectify this imbalance. It should be mentioned that *Trope* was intended to apply to the contentious issue of *pro per* attorney's fee recovery. It is unfortunate that the

language the court chose to preclude *pro per* recovery has also made it difficult for *pro bono* and public interest litigants to obtain recovery.

Reasonable Attorney Fees

Determining how to calculate reasonable attorney fees has grown more uncertain following *Trope*. Previously, when recovery was allowed for *pro per, pro bono,* in-house, and public interest attorneys, the court had to decide how to calculate reasonable attorney fees. *Sternwest Corp. v. Ash* held that cases decided under Section 1717 must use the lodestar method.[41] The lodestar figure represents "the number of hours reasonably expended multiplied by a reasonable rate" in that area.[42] Some courts add to the lodestar calculation on the basis of the difficulty of the issues involved in the case or the extraordinary relief the attorney was able to obtain. The focus in calculating the lodestar is to approximate what a practicing attorney would charge a fee-paying client.

Trope's focus on fees "incurred" has shifted the determination of reasonable attorney fees away from a lodestar determination. Two lines now emerge. Some courts follow a literal interpretation of the *Trope* decision in assessing fees, as well as in determining if a party may recover at all. In *San Dieguito*, for example, the court allowed the JPA to recover only those fees actually charged to the client in the litigation and the firm's costs. This method would be a simple calculation based on the books.

In contrast, *PLCM* read *Trope* as only deciding the narrow issue of whom should recover stating:

> [T]he holding of Trope is not that Civil Code Section 1717 requires a fee award to equal the exact amount of dollars paid by a litigant; rather it is that to be eligible for a fee award, a litigant must become liable to pay some consideration for legal representation….[43]

[41] 183 Cal. App. 3d 74, 227 Cal. Rptr. 804 (1986); see also Richard M. Pearl, California Attorney Fee Awards, September 1998, §11.2.
[42] PLCM Group Inc v. Drexler, 1999 D.A.R. 5129, 5126 (1999).
[43] *Id.* at 5129.

The court went on to hold that "[i]n California, any fee-setting inquiry begins with the lodestar"[44] based on the prevailing market rate for the area.

Conclusion

While *Trope* decided the contentious issue of *pro per* recovery of attorney fees under Section 1717, it has caused uncertainty and unease with respect to other parties. It is clear that the intent of Section 1717 was to provide a reciprocal right to recover when a contract specifies recovery for at least one party. It is also clear that the chief motivation for this statute was the protection of consumers who were in unequal bargaining positions. A literal interpretation of *Trope* would leave these individuals unprotected if they could not afford to retain an attorney. Further, an attorney who offers a reduced fee to represent such clients will be penalized for this charity by not being allowed to recover market value for the attorney's services. In all cases, however, the drafter of the fee shifting agreement will be allowed full recovery should the drafter win in the litigation. The result may be either a chilling effect on litigating meritorious claims because of the prohibitive cost of retaining an attorney, or coercive settlements because the poorer litigant cannot afford to go to trial.

Bet Tzedek Legal Services and the Western Center on Law and Poverty request that the Law Revision Commission look into amending or revising Section 1717 to better effectuate its intent and to protect *pro bono* and public interest attorneys that rely on fee recoveries to finance the cost of litigating in the public interest. The Commission should also look into the issue of recovery by in-house counsel. I recommend revising Section 1717 to explicitly cover in-house counsel, public interest, and *pro bono* attorneys and firms, though defining in-house counsel may be challenging.

[44] *Id.* at 5129, *quoting* from Mangolin v. Regional Planning Commission, 134 Cal. App. 3d 999, 1004 (1982) .