

Approved: \_\_\_\_\_  
Date

MINUTES OF THE HOUSE TAXATION COMMITTEE.

The meeting was called to order by Chairperson Wagle at 9:00 a.m. on March 3, 2000, in Room 519-S of the Capitol.

All members were present except: Rep. Minor - excused  
Rep. Long - excused

Committee staff present: Chris Courtwright, Legislative research Department  
April Holman, Legislative Research Department  
Don Hayward, Revisor of Statutes  
Shirley Sicilian, Department of Revenue  
Ann Deitcher, Committee Secretary  
Edity Beaty, Taxation Secretary

Conferees appearing before the committee:

**HCR 6012 - A resolution requiring the Attorney General to prosecute an action to determine the reasonableness of attorney fees awarded to the local outside counsel in the national tobacco settlement case.**

The Chair explained that this was the bill previously heard. She also told the Committee that due to some concern that if this resolution passed, tobacco money would be placed in jeopardy, she took the letter that the Attorney General had written regarding this to the Revisor. The Revisor spent the last week going over the master settlement for the tobacco case and they have come up with a balloon that protects the tobacco money. (Attachment 1).

A copy of the Revisor's memorandum regarding the consideration of the Draft Resolution was handed out to the Committee. (Attachment 2)

It was moved by Representative Johnston and seconded by Representative Findley that the balloon amendment to HCR 6012 be adopted. The motion carried on a voice vote.

It was moved by Representative Palmer and seconded by Representative Gregory that HCR 6012 be passed as amended. The motion carried on a voice vote.

The meeting was adjourned at 10:20. The next meeting is scheduled for Tuesday, March 7, 2000.

## HOUSE RESOLUTION NO. \_\_\_\_\_

By Committee on Taxation

A RESOLUTION requiring the Attorney General to prosecute an action to determine the reasonableness of attorney fees awarded to the local outside counsel in the national tobacco settlement case.

WHEREAS, The Committee on Taxation received testimony concerning the employment of local outside counsel to represent the State of Kansas in litigation against the tobacco companies; and

WHEREAS, The Committee heard testimony that if another law firm had been employed, Kansas may have received a greater amount of revenue from the National Tobacco Settlement; and

WHEREAS, According to the order issued by the Tobacco Settlement Arbitration Panel that rewarded \$27,000,000 to Kansas local outside counsel, "The role of National Counsel in this state was very prominent and active," "that there was more work spent by National Counsel in Kansas than in several other states," and the National Counsel "provided most of the personnel power and resources for the Kansas effort"; and

WHEREAS, There was limited litigation in Kansas, and in fact, according to the order of the Tobacco Settlement Arbitration Panel, "There was no ruling on the industry's motion to dismiss, there was no discovery, no expert designations, no depositions and no trial date was set"; and

WHEREAS, Rule 1.5 of the Model Rules of Professional Conduct as adopted by rule of the Kansas Supreme Court requires that any fee charged by a Kansas lawyer be reasonable and subject to judicial review; and

WHEREAS, The contract entered into by the State of Kansas and local outside counsel is also subject to such rule; and

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WHEREAS, The fee received by local outside counsel in the amount of \$27,000,000 is unreasonable in light of the lack of expertise and effort by such counsel, and the result obtained thereby: Now, therefore,

Be it resolved by the House of Representatives:

(1) That in accordance with K.S.A. 75-702 the Attorney General [be] directed to bring an action in [the Shawnee County District Court] seeking [judicial] review pursuant to MRPC 1.5 as to the reasonableness of the attorney fees awarded to the local outside counsel;

is hereby

(2) That the Attorney General obtain a copy of the transcript and briefs submitted to the Tobacco Settlement Arbitration Panel and submit such evidence to the [court] or seek a subpoena from the [court] directing production of the same;

an appropriate forum

(3) That the Attorney General submit to the [court] as evidence the entire record of the proceedings of the House Committee on Taxation occurring from February 14, 1999, through February 17, 1999;

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(4) That all evidence submitted to the [court] in such action shall be made available for review by any member of the legislative coordinating council, and the chairperson, vice-chairperson and ranking minority member of the Committee on Taxation;

an order be sought that

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(5) That the Attorney General, in the event that a conflict appears with respect to paragraph (1), shall hire special counsel who will aggressively pursue on behalf of the client, the State of Kansas, that the award of \$27,000,000 for work done on the tobacco case by the local outside counsel is unreasonable and a violation of MRPC 1.5; and

(6) That, in the event any amount of such fee is declared to be unreasonable and excessive,

the Attorney General shall seek from the [court] an  
 order providing that upon receipt, such amount  
 shall be remitted by the local outside counsel to  
 the state treasurer who shall deposit the entire  
 amount thereof in the state treasury to the  
 credit of the children's initiatives fund; and

Be it further resolved: That the chief clerk  
 of the House of Representatives be directed to  
 provide an enrolled copy of this resolution to  
 the Attorney General.

forum

Office of Revisor of Statutes

300 S.W. 10th Avenue  
Suite 322, Statehouse  
Topeka, Kansas 66612-1592  
Telephone (785) 296-2321 FAX (785) 296-6668

MEMORANDUM

**To:** Representative Susan Wagle, Chairperson, House Committee on Taxation  
**Date:** March 2, 2000  
**Subject:** Proposed House Resolution for Review of Attorney Fees in Tobacco Litigation Cases

This memorandum is not intended to be an all-inclusive or exhaustive review and discussion for all the legal issues or policy matters involved in the Draft Resolution being discussed by the House Committee on Taxation. It is intended to assist the Committee in consideration of the Draft Resolution.

**Background of the Lawsuits**

Attorney General Stovall retained outside counsel to represent Kansas in the national tobacco litigation cases (State of Kansas v. R. J. Reynolds Tobacco Company, et al., Shawnee County District Court Case No. 96-CV-919 filed August 26, 1996). The Attorney General entered into the Master Settlement Agreement (MSA) on behalf of Kansas on November 20, 1998, along with 45 other states, to settle the lawsuits brought against tobacco manufacturers. On December 3, 1998, joint motions were filed by the state of Kansas and the defendants for a consent decree and final judgment and approval of settlement agreement.

The motions made by all the parties to the Kansas cases for the issuance of a consent decree and final judgment and approval of settlement agreement and for entry of the agreed dismissal order were sustained by the District Court. The cases and all claims of the plaintiff against all defendants were dismissed with prejudice by the District Court and the order of dismissal was filed on December 3, 1998.

Under the MSA, payments are not made to a state or to retained counsel until the state has attained State-Specific Finality (SSF). [MSA, II Definitions, (ss)] This essentially means that the state has obtained the court's approval of the MSA and the consent decree, the court has entered final judgment dismissing with prejudice all claims and the time for appeal has expired. Kansas attained SSF on January 4, 1999.

After this dismissal with prejudice, the District Court denied two separate motions to intervene. The first was a motion filed December 17, 1998, by a group of Kansas licensed health care facilities. The second was filed on December 21, 1998, by a Wichita attorney requesting a determination of whether the attorneys' fees to be paid to the private counsel of the state are consistent with or repugnant to the Model Code of Professional

Responsibility, specifically Rule 1.5 regarding fees and rule 1.8 regarding conflicts of interest.

These motions were considered and denied by the District Court in memorandum decisions filed on December 23, 1998. The decisions state that no action exists in which to intervene and that, in addition, it appeared to the District Court that the proposed intervenors would lack standing to intervene in an action filed by the Attorney General on behalf of the State of Kansas.

### **Background of the Attorney Fee Agreements**

The Attorney General entered into an "Engagement and Contingency Agreement" with Entz and Chanay, P.A., (lead local counsel) and Scruggs, Millette, Lawson, Boseman & Dent, P.A. and Ness, Motley, Loadholt, Richardson & Poole, P.A. (lead national counsel).

Compensation to the Outside Counsel under the Engagement and Contingency Agreement was contingent upon recovery and collection by counsel of funds by settlement or judgment on behalf of Kansas.

The agreement states in part:

"Counsel Fees shall be determined in accordance with this agreement, 1995 Kan. Ct. R. Anno. 226, MRPC 1.5, by the terms of any settlement agreement or as provided in any other resolution process." [Engagement and Contingency Agreement, Section 3.1]

The MSA provides that:

"The Original Participating Manufacturers agree that ... they will severally pay reasonable attorneys' fees to the private outside counsel, if any, retained by such Settling State ..., in accordance with the terms described in the Model Fee Payment Agreement attached as Exhibit O." [MSA, XVII, Sub (d)]

Under the MSA, the Participating Manufacturers agreed to "pay reasonable attorneys' fees to STATE outside counsel, as provided herein and subject to the *Code of Professional Responsibility* of the American Bar Association." [MSA, Exhibit O, Sec. 2.] The fee paid was to be either a "liquidated fee" (an amount agreed upon by the Manufacturers and Outside Counsel) or a "fee award" (any award of attorneys' fees by the three-member arbitration panel described in section 11 of Exhibit O of the MSA).

The Outside Counsel for Kansas failed to reach agreement with the Manufacturers for a "liquidated fee" and submitted an application for a "fee award" to the arbitration Panel. This was specified in a letter from Entz & Chanay, P.A., to Attorney General Stovall dated November 13, 1999, and signed by Stewart Entz. This letter set forth and confirmed that all Outside Counsel:

"... agree to waive any right of recovery against the State of Kansas pursuant to the Contingency Fee Agreement the firms have with the State for the prosecution of the Kansas tobacco litigation.

"... the three firms will be awarded an attorneys fee through the arbitration process set forth in Schedule O to the Master Settlement Agreement. The three firms agree to accept that amount as payment in full of their attorney fees for all work performed for Kansas in connection with

the tobacco litigation, and agree not to seek recovery against the State's share of the tobacco settlement proceeds pursuant to the Contingency Fee Agreement.

"This agreement and waiver is made effective the 1<sup>st</sup> day of November, 1999, and confirms the earlier oral understanding between the three law firms and the Office of Attorney General." [Entz & Chanay, P.A., letter dated November 13, 1999]

This waiver of any recovery of attorney fees under the original Engagement and Contingency Agreement would preclude the Kansas Outside Counsel from recovering attorney fees from the payments that Kansas receives under the MSA. The only amount that Kansas Outside Counsel may look to for recovery of attorneys fees in these actions is the fee award determined by the arbitration Panel.

The process under the Kansas Counsel Fee Payment Agreement (Exhibit O) is for the Kansas Outside Counsel to apply to the three-member Panel for a fee award. The panel considers the information submitted and information submitted by the Manufacturers, which may contest the requested amount. The participants and Kansas are to "preserve the confidentiality of any attorney work-product materials or other similar confidential information that may be submitted." [MSA, Exhibit O, Sec. 12 (b)] The Panel may conduct a hearing upon the request. The proceedings and the Panel members are subject to the provisions of the *Code of Ethics for Arbitrators in Commercial Disputes* of the American Arbitration Association and the American Bar Association. [MSA, Exhibit O, Appendix, Protocol of Panel Proceedings] Further:

"The Panel is to consider all relevant information submitted in reaching a decision as to a fee award that fairly provides for full reasonable compensation of State Outside Counsel. ...The Panel's decision as to the Fee Award of STATE Outside Counsel shall be final, binding and non-appealable." [MSA, Exhibit O, Sec. 14]

The Panel held a hearing on November 13, 1999, and also received testimony from Attorney General Stovall by telephone. The Panel announced a unanimous award on January 31, 2000. The amount of the fee award for Kansas Outside Counsel was \$54,000,000, of which the Entz & Chanay, P.A., firm is to receive \$27,000,000 in accordance with the fee sharing agreement among Kansas Outside Counsel. [MSA, Exhibit O, Sec. 21 (a)]

From a review of the MSA and Exhibit O, the amounts paid to the States in settlement of the cases and the amounts paid to Outside Counsel, whether as liquidated fees or fee awards, are separate obligations and not from the moneys in escrow contributed to by all Participating Manufacturers and from which payments are made to the States under the MSA. The payment of a fee award is on the basis of each Manufacturer making payments severally and in proportion of its relative market share. [MSA, Exhibit O, Sec. 16 & 23]

Any reduction in the amount of attorney fees paid under the Kansas Counsel Fee Payment Agreement (MSA, Exhibit O) entered into by the Outside Counsel and the Manufacturers would not be paid directly to States under the MSA, except insofar as such a reduction would have the effect of fewer obligations on the moneys of the Manufacturers which might then be available to make payments.

### **The Proposed House Resolution**

The Proposed House Resolution would direct the Attorney General to bring an action in the Shawnee County District Court seeking judicial review pursuant to Rule 1.5 of the Model Rules of Professional Conduct (MRPC) as adopted by the House of Delegates of the American Bar Association, which has been adopted as a Rule of the Kansas Supreme Court (Rule 226). The MRPC were adopted as “general standards of conduct and practice required of the legal profession in Kansas. Violation of such standards constitutes grounds for disciplinary action.” [ Kansas Supreme Court Rule 226, Prefatory Rule]

By its terms, the Draft Resolution would require Attorney General institute an action to determine the reasonableness of the attorney fees in accordance with K.S.A. 75-702. It has been interpreted as mandatory for the Attorney General to represent Kansas when required under this statute by the Governor or either House of the Legislature. There are limited opportunities to challenge to “reasonableness” of the fee award and some are problematic.

### **Payment of Attorney Fees As A Matter of Final Judgment**

A final judgment is an order of a court of competent jurisdiction which decides the rights of the parties as to the matter in dispute including amounts to be paid, legal status or guilt or innocence of a criminal defendant. Wichita Federal Savings and Loan v. North Rock Rd. Ltd. Partnership, 13 Kan. App. 2d 779 (1989) The Master Settlement Agreement (MSA) was final judgment for purposes of this Shawnee County District Court Case, to the extent that it determined the rights of the parties with respect to the payment of money. The consent decree which makes reference to the MSA was filed December 3, 1998. Since that time, the District Court has denied two motions to intervene in the case on the basis that the motions were filed after final judgment had been entered. (Reviewed above in Background of the Lawsuits)

The payment of attorney fees to Outside Counsel was ordered by the District Court through the liquidated fee or fee award arbitration process specified in Exhibit O of the MSA. This reduced the issues surrounding attorneys fees to a final judgment.

As a result, the State is left with three options: Collateral attack on the MSA in the form of a motion seeking to review the reasonableness of the attorney fees, direct attack on the MSA pursuant to K.S.A. 60-260(b), or filing a disciplinary complaint seeking review of the attorney fees pursuant to KRPC 1.5.

### **Collateral Attack**

Collateral attack on a judgment occurs when a party to the judgment files a separate action which requires by implication that all or a part of a final judgment be set aside. Bank IV Wichita v. Plein, 250 Kan. 701 (1992) In order to prevail in such an action, the plaintiff must establish that it has been damaged in some specific way by the existence of the judgment. The judgment may only be overturned in the face of evidence that it was entered under



fraudulent circumstances which the trial court could not have been aware (extrinsic fraud) or that the trial court lacked jurisdiction over the case. Neither of those circumstances appear present in the instant case. In addition, since local outside counsel waived its right to collect fees through its contingency fee agreement with the state, the District Court is without jurisdiction to review the reasonableness of the attorney's fees under the contract since the contract no longer speaks to that issue.

### **Direct Attack**

Direct attack on the MSA is an action brought within one year of the final order seeking to overturn the judgment on any of the grounds set forth in K.S.A. 60-260(b). In re Estate of Newland, 240 Kan. 249 (1986). A court may relieve a party from a final judgment, order or proceeding for the following reasons:

(1) mistake, inadvertence, surprise, or excusable neglect; (2) newly discovered evidence which by due diligence could not have been discovered in time to move for a new trial under K.S.A. 60-259 (b); (3) fraud (whether heretofore denominated intrinsic or extrinsic), misrepresentation, or other misconduct of an adverse party; (4) the judgment is void; (5) the judgment has been satisfied, released, or discharged, or a prior judgment upon which it is based has been reversed or otherwise vacated, or it is no longer equitable that the judgment should have prospective application; or (6) any other reason justifying relief from the operation of the judgment. The motion shall be made within a reasonable time, and for reasons (1), (2) and (3) not more than one year after the judgment, order, or proceeding was entered or taken. A motion under this subsection (b) does not affect the finality of a judgment or suspend its operation. [K.S.A. 60-260(b)]

None of the factors listed in K.S.A. 60-260(b) appear to be present in the instant case. The State's only chance would be to challenge the reasonableness of the attorney fees under the "catch-all" language of subsection (b)(6) of K.S.A. 60-260.

With respect to any attack on the MSA, the District Court might take the position that the state has no standing since the increase or decrease in the attorney fees has no effect on the amount money paid to the State through the MSA. See, Ryder v. Farmland Mutual Ins. Co., 248 Kan. 352 (1991)(client had no standing to dispute fee sharing agreement when total fees to be split did not exceed the 33% limit set forth in contract).

A successful direct attack on the MSA would have the effect setting aside at least part of the judgment. Arguably, this would take Kansas out of "State Specific Finality" and return the matter to District Court thus delaying or abrogating the payment of settlement proceeds. However, the issue of attorney fees could then be reviewed by the District Court.

### **Disciplinary Complaint**

The attorney fees could be reviewed under the Draft Resolution by filing a complaint regarding the reasonableness of the attorney fees with the Disciplinary Administrator pursuant to KRPC Rule 209. It is the duty

of all attorneys licensed or permitted to practice in Kansas courts to adhere to the KRPC, including Rule 1.5 relating to the reasonableness of attorney fees.

**Conclusions**

Under the first two options discussed, direct or collateral attacks on the reasonableness of the attorney fees, a further concern is that, if such attacks were unsuccessful, the other parties to the MSA or the Kansas Counsel Fee Payment Agreement (Exhibit O) might pursue causes of action for malicious prosecution or tortious interference with a contract. This would be in addition to any effect that those courses of action might have upon the receipt of settlement payments by the State under the MSA.

Under the approach of filing a complaint with the Disciplinary Administrator, the law is clear that persons making or providing “complaints, reports, or testimony in the course of disciplinary proceedings” are entitled to absolute judicial immunity under Rule 223 of the Kansas Supreme Court. [See *Jarvis v. Drake*, 250 Kan. 645(1992) (Summary judgment for defendant in action by attorney for malicious prosecution, libel and tortious interference with a contract against complainant in disciplinary case.)]

The Draft Resolution would require the Attorney General to take action to secure review of the reasonableness of the attorney fees awarded to outside counsel under KRPC 1.5 and to attempt to obtain and make available such other information as may be desired. If a certain course of action or result is not desired and is to be avoided, then the Resolution should so specify. The Committee should consider modifying the Draft Resolution to permit the Attorney General flexibility in determining the means and choice of forum in which the review of attorney fees is to be obtained, in the best interests of the state.

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