F I S C A L I M P A C T R E P O R T

SPONSOR SJC **ORIGINAL DATE** 03/05/11 **LAST UPDATED** **HB**

SHORT TITLE Transparency in Private Attorney Contracts **SB** 461/SJCS

ANALYST Daly

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY11	FY12	FY13	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
Total	NFI	NFI*	NFI*			

(Parenthesis ( ) Indicate Expenditure Decreases)
*****See Fiscal Implications below.

Duplicates HB 386/HBICS
Relates to HB 38, SB 86 and SB 269.
Conflicts with SB 404.

SOURCES OF INFORMATION
LFC Files

Responses Received From

State Investment Council (SIC)
Educational Retirement Board (ERB)

SUMMARY

Synopsis of Bill

The Senate Judiciary Committee Substitute for Senate Bill 461 authorizes the Attorney General, if necessary to perform the duties of that office, to enter into contingency contracts with private attorneys to recover, through litigation or court-approved settlements, monies owed the state or any of its departments, agencies, officer, instrumentalities, institutions or political subdivisions.

SB 461 sets maximum compensation amounts for attorney fees based on different levels of amounts recovered, and sets an absolute fee cap of $20 million. The contracts are subject to the Procurement Code provisions requiring competitive sealed proposals, and cannot be awarded under the sole source, emergency, or existing contract exceptions to that Code. Every contingent fee contract must be posted on the AGO website throughout its duration, as well as any payments made under such a contract.

The Attorney General must make an annual report to legislative leaders on any new or

continuing contingent fee contracts and provide information as specified in the bill.

An "attorney general suspense fund" in the state treasury is created for deposit and distribution of amounts recovered under these contracts.

SB 461 also adds a new provision to the Campaign Practices Act that bars an attorney who has entered into such a contract or has responded or intends to respond to a request for proposals for such a contract from making contributions to or soliciting contributions for 1) a candidate for attorney general or that candidate's campaign committee or 2) a political committee established by or in consultation with the attorney general or an agent of the attorney general or controlled by the attorney general or an agent of the attorney general to aid or promote the nomination or election of any candidate to a state office.

The bill also requires a provision in any contingent fee contract mandating termination of a contingent fee contract if the contractor or any partner, associate or employee violates that new prohibition.

FISCAL IMPLICATIONS

The operating budget impact table above shows no fiscal impact since payments under these contracts come from funds received in satisfaction of a state claim.

There is an additional significant and desired fiscal impact that is not estimated in the table above resulting from the recovery of certain losses to the state's permanent or other funds, or to the funds of a political subdivision of the state, by settlement or judgment.

SIGNIFICANT ISSUES

The SIC sets forth the basic rationale for contingent fee contracts generally:

> As with all contingent fee legislation, SB461 seeks to lessen the state's level of risk and up-front costs associated with litigation, in exchange for what is typically a smaller share of recovery assets post trial or settlement.
>
> Typically, contingent fee arrangements with attorneys can be attractive due to a lack of:
> - Resources required for large cases
> - Expertise specific to complex types of litigation
> - Budget availability to the agency
> - Support from legislative, executive and public bodies
> - Appetite for up-front cost expenditure/risk inherent in any litigation
> - And distaste for or sticker shock over high hourly lawyer fees
>
> These factors and other practical considerations in recent years and during this current legislative session have led multiple state agencies to seek legal authority to enter into appropriate agreements with external attorneys when seeking recovery of state dollars. The Taxation and Revenue Department (TRD) is among the state agencies which already have this authority.

> The alternatives unfortunately are not very attractive. For litigation requiring specialized experience, often attorneys' fees are several hundred dollars or even more than a thousand dollars per hour. The state's qui tam, or fraud against taxpayers act allows private attorneys to pursue litigation on behalf of the state, but does not provide any resources to those attorneys. In some cases, the resources needed to carry a case on through to trial or settlement will be very significant, and may be impossible for an attorney facing significant opposition or a defendant with "deep pockets". There is also not a statutory requirement that qui tam attorneys have the experience, expertise or ability necessary to realistically make recoveries for the state. It should also be noted that qui tam attorneys' share of recoveries by statute can be up to 30% of state recoveries, a significantly higher share of the state's funds than would be capped under SB 461.

Permitting any state agency to enter into contingency fee contracts for litigation services presents the risk of abuse through law firm selection or case selection (or non-selection) involving "pay to play" schemes involving favorable settlement terms. This bill strives to mitigate against this possibility by requiring the AG to post all contracts and payments on the AG website and submit annual reports to the Legislature as well as prohibiting political contributions or solicitations to the AG or a political committee established or controlled, directly or indirectly, by the AG from attorneys who have, or are intending to have, a contingency fee contract with the AG.

There is a clear need for both transparency and strong oversight to avoid these situations and other risks inherent in this method of litigation. Including language in the bill to specify that procurement of services in this way also be subject to the represented agency's review and approval and requiring additional concurrent approval by an outside agency such as the Department of Finance and Administration's Contract Review Bureau or the State Purchasing Agent might help insure that this type of procurement method is only being used for appropriate cases and to maximize possible returns to the state.

The fee structure contained in SB 461 has been the subject of comments by two of the investing agencies that might be represented by the Attorney General under the contingent feet agreements being authorized. The SIC advises that that structure:

> appear[s] to construct a reasonable fee schedule that should allow the state to attract quality firms with appropriate expertise to handle highly specialized litigation (i.e. financial fraud, investment malfeasance, etc), which oftentimes requires significant resources, experience and talent not available in most places across the country, including New Mexico. By using a structured fee schedule such as this, the state avoids paying a risk premium on litigation that may or may not result in recoveries for the state. In exchange for lowering the state's 'skin in the game' it is a simple reality that it must incentivize those who would represent New Mexico's interests through the potential for added benefits down the road.

On the other hand, the ERB expresses these concerns:

> In the area of securities or investment-related litigation, attorney fees are generally based on not only the total damages recovered but also on the stage of the case at which the damages are recovered. In addition, while the dollar limits on the fees in SB 461 appear generous in terms of dollar amounts, attorneys who specialize in this type of litigation have said the fee structure in SB 461could dissuade the most qualified firms from taking many securities and

> investment-related cases, especially those that present more complex legal and factual issues. The fee structure also could work against the state when negotiating fee agreements that take into account not only total recovery but also the stage of the case at which the recovery occurs. If the fees structure is considered very tight, attorneys doing securities or investment-related litigation would be less inclined to negotiate provisions that would further lower the fees based on the stage of at which the case was settled. Finally, as regards securities and investment-related litigation, the fee limits are low enough that they would act as a disincentive to expending more resources to investigate and develop the facts and legal as thoroughly as possible because the time and expenditures necessary to move a case forward could be cost prohibitive in relation to the fees that could be recovered.

Additionally, as to the public notice provisions regarding settlement amounts, the ERB notes:

> SB 46 provides that the amount of any recovery made pursuant to a contingency fee contract shall be included in a report that the Attorney General is to provide annually to the Legislature. The ERB agrees that settlements should be public information; however, the agency notes that in securities and investment-related cases, many defendant firms insist that settlement agreements include a confidentiality provision. Inclusion of that provision could be a material factor in reaching a settlement.
>
> In order to resolve the issue of whether a settlement should be confidential or subject to disclosure under IPRA, the ERB would include a clause in settlement agreement stating that if a request for a copy of settlement agreement is received, a defendant that wishes to keep a settlement confidential could seek court order determining whether the settlement is confidential. The person submitting the IRPA request would be party to that proceeding. The ERB would comply with the court's order regarding whether a settlement, or any part of it, was confidential.

The AGO noted the following issue related to HB 386, which duplicates this bill:

> Requiring the web posting of all contingency fee contracts and payments is of questionable value, particularly considering the applicability of the Inspection of Public Records Act to such contracts.

Additionally, the AGO raises this issue concerning the three provisions of the Procurement Code that remain ineligible for contingency fee contracts:

> The exception of Sections 13-1-126, 13-1-127, and 13-1-129 of the Procurement Code is also potentially problematic. First, the limitation on sole source procurements (Section 13-1-126) could subject the process of hiring an attorney to undue time and expense. While it is unlikely that a piece of litigation could be best handled by only one law firm, such a scenario is not impossible. Second, the exception of emergency procurements (Section 13-1-127) would make it difficult for the Attorney General to timely hire a private attorney when time is of the essence, such as a case in which the statute of limitations is very near. Finally, the exception of procurement under existing contracts (Section 13-1-129) could unnecessarily burden the hiring of a private attorney for litigation that stems from a case the attorney is already handling. If, for example, an attorney is litigating a case against a defendant and learns, during that litigation, that another party should also be a defendant but the time for amending the complaint to add that defendant has passed, this bill would require the Attorney General to bid out

> litigation against that potential defendant. This would be true even though a private attorney is already handling a case investigating the same facts giving rise to liability against the potential defendant.

PERFORMANCE IMPLICATIONS

The SIC notes that it would likely see improved performance with less resources required internally to pursue recovery.

ADMINISTRATIVE IMPLICATIONS

Similarly, the SIC notes that the bill brings a shift in administrative burden from agencies seeking recovery to the Attorney General's Office and its resource pool.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

SB 461 now duplicates HB 386/SBICS.

SB 461, while adopting similar sections in SB 404, still conflicts with that bill, as described by the AG:

> This bill very closely resembles SB 404, which also gives contingency fee authority to the Attorney General. The principal difference between the bills is that this bill requires posting of contingency fee contracts on the Attorney General's website (which SB 404 does not require) and this bill subjects the contracts to the Procurement Code and exempts the application of the three Procurement Code provisions discussed above (which, again, SB 404 does not).

SB 461 relates to SB 269/SJCS (Educational Retirement Board Bank & Attorneys).
SB 461 relates to SB 86 (Investment Council Legal Service Contracts).
SB relates to HB 38 (PERA Custodian Bank and Attorney Fees).

OTHER SUBSTANTIVE ISSUES

The ERB advises:

> The ERB separately has requested authority to enter contingency fee contracts (see SB 269). The ERB is seeking this authority as the Board is the trustee for the Educational Retirement Fund and has the sole and exclusive fiduciary duty and responsibility for administering and investing the Fund. In addition, it has first-hand knowledge of matters related to the Fund's investments and any damages related to an investment that may have been suffered and whether to pursue recovery of those damages where warranted on a contingency fee basis.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

The SIC reports that the state (and local political subdivisions) will be forced to pursue legal remedy on a costly and much riskier hourly basis, or in the alternative, abandon efforts entirely.

MD/bym