Revitalizing FRCP 68: Can Offers of Judgment Provide Adequate Incentives for Fair, Early Settlement of Fee-Recovery Cases?

Friday, February 17, 2006

Luncheon Speaker

William W Schwarzer*

MS. MCKELVEY: Good afternoon again everyone. At this time it is my pleasure and honor to introduce you once again to Judge William W Schwarzer who has come all the way from California to offer his credentials and expertise to our Symposium. We really don't need an introduction for him. Judge Schwarzer is such a legend in our profession. However, I want to highlight just a few things about the Judge that are especially important.

As U.S. Supreme Court Justice Anthony Kennedy said, "Judge Schwarzer has been a brilliant, distinguished, and passionate servant of the law and has served as a federal judge for nearly three decades."[1] Members of the bench and bar nationwide are indebted to Judge Schwarzer for his example and his service, and for his remarkable contributions to the judiciary of the United States and to the law. He

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1. *Presentation of the Edward J. Devitt Distinguished Service to Justice Award*, American Judicature Society (2004), *available at* http://www.ajs.org/ajs/awards/Devitt%20Award/Schwarzer_whole%20bk/t_short_final.pdf.

has served as the director of the Federal Judicial Center. In 1987 Chief Justice William Rehnquist appointed him to chair the newly established Judicial Conference Committee on Federal and State Jurisdiction. And in addition to that, as if he wasn't busy enough, he has authored more than seventy-five books, monographs, and manuals regarding case management and rules of procedure.

So at this time if we could welcome Judge William Schwarzer.

JUDGE SCHWARZER: Thank you, Rebecca and thank you for this invitation to the deep south. It's a long way from northern California in more ways than one.

Well, it's always difficult to follow an introduction such as you just heard because whatever I say is going to be a letdown after the buildup Rebecca has given me. She asked me to say a few words about the Federal Judicial Center before I talk about Rule 68.[2]

The Federal Judicial Center where I served as director from 1990 until 1995 is an agency within the judicial branch designed to provide training, education, research, and planning. The Center has about one hundred employees, and it operates under the direction of a board of directors, which is composed of six judges appointed by the U.S. Judicial Conference and chaired by the Chief Justice.

The Center provides education and training for all of the judges in the judicial branch: appellate judges, district judges, magistrate judges, and bankruptcy judges, as well as court managers, court personnel, probation officers, and pre-trial services offices. It provides about fifty education programs each year serving about two thousand people. So the Center has a broad mission.

The flagship program is the training of newly-appointed district judges. It is a one-week seminar in Washington in which judges are introduced to civil and criminal case management, as well as some of the substantive areas like the ones you talked about today: civil rights, employment discrimination, and various aspects of criminal law and constitutional law. The focus, however, is not really on substantive law because you can't do that much in a week, but rather the focus is to prepare judges to deal with these issues.

In addition, the Center does workshops and conferences and special programs. Some of the programs are in association with universities and other think tanks.

During the time I was at the Center, I focused particularly on case management. One of the items we produced was a new manual for

2. FED. R. CIV. P. 68.

complex litigation which some of you may have encountered in your work. The purpose is to help judges deal with complex cases and manage them effectively. The other area that was of particular interest to us was the growing role that science plays in the work of federal courts. We obviously could not teach people the science they encountered, but we designed the Reference Manual on Scientific Evidence.[3] How many of you have run across the Reference Manual on Scientific Evidence? It is designed to introduce judges to various scientific disciplines such as toxicology, epidemiology, DNA, statistical evidence, and the like. It is not designed to teach them the substance of these areas, but to teach them how to approach it: what questions to ask, how to think about it and what the logical analysis is for issues of the kind that fall within this area of expertise.

But my particular interest was in case management, and in connection with that, I had the opportunity to spend a couple of weeks with an Anglo-American legal exchange in London. While I was there, I ran across the practice that is in use in the trial courts in England called "payment into court." This permits the defendant to pay into court the sum that the defendant believes the plaintiff will recover. If the offer is rejected, they go to trial, and the plaintiff does not do as well; then the plaintiff does not recover the fees and pays all of the defendant's fees. Of course, that works within the fee-shifting environment in England where the loser pays the fees.

That got me interested in the possibility of amending Rule 68 to make it a fee-shifting offer of judgment rule. Now, I should say at the outset that I'm not going to talk about what you talked about this morning, that is the application of Rule 68 to the civil rights or employment discrimination cases. And mind you, I believe the *Marek*[4] case was wrongly decided. I would amend Rule 68 to eliminate its application to cases under fee-shifting statutes for two reasons: first, because it contradicts the Federal congressional policy of creating private attorneys general to enforce these laws; and second, because it's not necessary. In the event that fees are awarded, the court can, and will, take into account the extent to which the fees were reasonably incurred. If there was a settlement offer that would not necessarily defeat the application of fees but would influence the decision of the judge about the level of fees the plaintiff should recover, the court will consider that, as well.

So my interest in Rule 68 was to amend it to make it a useful device in general civil litigation in the federal courts by creating a fee-shifting mechanism to produce the sort of coercive system that would force people

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3. FED. JUDICIAL CTR., REFERENCE MANUAL ON SCIENTIFIC EVIDENCE (2000).
4. Marek v. Chesny, 473 U.S. 1 (1985).

to take a hard look at the possibility of settling because of the risks they could incur by not settling.

My purpose in doing this is not so much to increase the number of settlements. As was said this morning, almost all the cases in the federal courts are disposed of without trial. About half of them are settled and about half of them fall by the wayside as a result of motions or because they are abandoned. We do not need a rule to make people settle their cases. The key is to get them to settle earlier. My view of Rule 68 is that it should serve as a device to reduce the cost of litigation, and particularly the cost of discovery and motion practice.

Now, the Advisory Committee on civil rules has been working on this issue of discovery and litigation costs for years and has adopted various amendments such as limiting the scope of discovery and enlarging judicial control. But, unfortunately, discovery costs continue to spiral. Cases that do not go to trial often go through expensive motion practice and discovery before settlement. We needed a rule that provides an incentive to bring cases to resolution earlier. And the question is whether Rule 68 can be revised to achieve that purpose. That certainly is not the case with the present rule because the exposure to having to pay costs is not much of an incentive to settle early.

A revision of Rule 68 to make it a fee-based rule would be consistent with the Federal Rules because there are at least two rules that now provide for the recovery of fees: Rule 37(b)[5] in connection with discovery abuse and Rule 11(c)[6] in connection with the duty under Rule 11 to conduct a reasonable pre-filing investigation. But my view of Rule 68 is that it should not serve as a sanction, but rather as an incentive. People should not be sanctioned for not wanting to settle their lawsuits because there are all kinds of good reasons why a case may not settle. Instead, Rule 68 should be seen as providing an incentive to minimize discovery costs by bringing about early settlements.

Faced with the risk of having to pay the opponent's fees, defendants will think about applying some of the cost savings realized by avoiding lengthy discovery to make, to increase the settlement offer; and, therefore, make it more attractive. Conversely, the plaintiff would moderate his or her demand because of the amount of money that would be saved by avoiding unnecessary discovery. That should enhance the prospects for discovery.

Making such a revision of the rule applicable to general civil litigation would seem to me to result in sweetening the defendant's offer and moderating the plaintiff's demands. Now, of course, the coercive effect

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5. FED. R. CIV. P. 37(b).
6. FED. R. CIV. P. 11(c).

will diminish as the size of what is at stake in a lawsuit increases. In large cases, the discovery costs are not a factor, so the rule will not have a coercive effect in those kinds of cases. But in my experience, there are many cases in the federal courts that are about moderate amounts such as two hundred and fifty thousand dollars or less. In those cases, the costs of discovery can easily make the litigation uneconomical.

A system to bring cases to early settlement can actually open the courthouse door to meritorious claims which the plaintiff would otherwise regard as unaffordable. Under the fee-based incentive rule, a plaintiff would have a better chance of getting a favorable settlement because the defendant could no longer rely on litigation costs as a deterrent to the plaintiff's prosecuting his or her case. And, of course, as I said, with an early settlement the plaintiff would be able to reduce his or her costs which would help moderate the settlement demand.

In addition to that, of course, the plaintiff facing the risk of fees will not want to make an excessive demand which he might not match if the case went to trial. From the defendant's perspective, in turn, his settlement offer may be improved by the savings the defendant would realize in discovery costs from an early settlement. So, in substance, the key is that the coercive effect of a fee-based rule would be to sweeten the settlement fund at no real cost to the defendant while moderating the plaintiff's demand to avoid the effect of fee shifting sanctions.

I would make some additional changes. I have already indicated that I would eliminate the rule's application to civil rights and employment cases and generally to cases under fee-shifting statutes, and there are about a hundred of those statutes. They are listed in Justice Brennan's dissent in *Marek*.[7] Some of those are private attorney general statues. Others are simply fee-shifting statutes like the patent statute, where there are not the same policy considerations as in employment discrimination and civil rights cases. But I have not figured out a way to distinguish the private attorney general's statutes from the other statutes, so we may just have to eliminate fee-shifting statutes altogether from the rule.

The rule should also have safeguards. As my article[8] described, an award against a plaintiff should be limited to the amount of any judgment so the plaintiff does not have to dig into his or her pocket to come up with payment of fees if Rule 68 is applied. Conversely, the award to the defendant should be capped so as to credit against that award what the defendant would have paid had his or her offer been

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7. 473 U.S. at 43-51 (Brennan, J., dissenting).

8. William W Schwarzer, *Fee Shifting Offers of Judgment—An Approach to Reducing the Cost of Litigation*, 76 JUDICATURE 147 (1992).

accepted. So the amount of the offer that was rejected has to be subtracted from the fee award because that is the amount of money that the defendant saved by not having the offer accepted.

Finally, any award should be subject to judicial scrutiny if either party seeks it so that there is a built-in safeguard that any award be fair and reasonable. Either party could ask the court to review the award.

Another objective of this rule would be to reduce the role of discovery as a profit center for lawyers. We heard some reference to that this morning. If a Rule 68 offer is made, the client will obviously be brought into the discussion whether the offer should be accepted or not, and the calculation in the making of that decision takes into account the amount of discovery that the lawyer intends to conduct if the offer is rejected. In effect, the client is brought into the decision-making process about how much ongoing discovery should be conducted, which is not generally the case in ordinary litigation. So the rule would call upon clients, as well as lawyers to focus hard on the economics of continuing the litigation versus accepting the offer of settlement.

Finally, I wanted to point out that there appears to be strong support among the bar for a rule that is two-way and involves fee shifting. The Federal Judicial Center conducted a survey of some eight hundred civil cases, and nearly three-fourths of the responding attorneys, which was a high rate of response, favored an amendment to Rule 68 to allow for two-way offers. The majority favored an amendment allowing at least a portion of the offering party's post-offer fees. According to the lawyers responding to the survey, if such a rule had been in effect, it would have achieved a sizeable reduction in litigation expenses in thirty percent of civil cases and would have expedited disposition in sixty percent of the cases by having cases settled earlier. There was also strong support for precluding an award of expenses in excess of a plaintiff's recovery because such a safeguard would encourage litigation of small, but strong claims.

That's my case for amending Rule 68. Does anyone have any questions? If you want to point out the flaws in my proposal, I'll be glad to listen.

AUDIENCE: Judge, could you tell us what piece of that proposal, if any, came before the Federal Civil Rules Committee?

JUDGE SCHWARZER: Ed Cooper is better able to answer that.

MR. COOPER: Short answer is the whole thing. The only draft we considered was one where you subtract from the fee award the difference between the offer and the judgment, as Judge Schwarzer has described,

and the cap. The plaintiff does not have to pay out of pocket, and the symmetrical defendant does not have to pay more than the amount of the judgment. An alternative provision for statutory fee-shifting cases is simply taking them out or treating them in different ways. But the enterprise was launched because of Judge Schwarzer's article, and the draft was modeled very much on his proposal.

JUDGE SCHWARZER: And it ended up being tabled. Not rejected, but tabled.

AUDIENCE: Judge, I gather that your proposal for change would apply to serious personal injury cases; if so, and a plaintiff guesses wrong, he or she will be subject to fees. How do you balance the rule's saying that there is going to be fee shifting against the plaintiff, and perhaps, the plaintiff's need to pay serious medical expenses out of any verdict or judgment that occurs in the case?

JUDGE SCHWARZER: Well, I think my only answer to that is the plaintiff will never be called on to pay attorney fees other than out of the recovery in the lawsuit.

AUDIENCE: Which could include the medicals, right?

JUDGE SCHWARZER: Well, I didn't really focus on that, but probably it would because it's part of the verdict. So that is obviously going to be problematic, but that is the whole idea of this rule, to get people to think about settling their cases and avoiding expense. But it can be problematic. I do not doubt that. Yes.

AUDIENCE: Judge, was there any specific consideration of how the proposal would apply in class action cases?

JUDGE SCHWARZER: The draft excluded class actions. I don't think it would work in class actions. It is hard enough to make it work in two-party cases. Any other thoughts? Yes.

AUDIENCE: Judge, was there any consideration of the fact that if you had a fee and then you add attorney fees to it, it could hinder settlements? If the defendant comes in with a real low number, the plaintiff starts with a real high number, and you start working towards the middle; is that essentially making it more difficult to meet the original burden at trial? So, if the defendant started out with a ten thousand dollar offer, by the end of it, he may have raised it to a

hundred thousand dollars. Now the plaintiff has to deal with a hundred thousand dollar offer for judgment, rather than the original ten thousand?

JUDGE SCHWARZER: Well, the rule contemplates that new offers can be made as the case goes along. I don't know if that answers your questions, but it contemplates that there would be a series of offers and demands from both sides, which you have to do in order to make it effective and reflect the products of discovery.

AUDIENCE: Right. But with new offers, essentially you're bidding against yourself in one sense. If the defendant gives a new offer, now the plaintiff has a more difficult burden to reach if he does decide to go try the case.

JUDGE SCHWARZER: That is true. That is in the nature of the rule.

AUDIENCE: Right. But it might deter settlement in some sense if the plaintiff is then saying he does not want to try to get the defendants to raise their offer early on because that just makes the burden harder for him in the long run.

JUDGE SCHWARZER: Well, I guess that is right. I don't think I have an answer to that. Yes.

AUDIENCE: Do you have any view about whether the ten-day current window for acceptance should be somewhat longer, either in the kind of diversity litigation that was principally addressed by your proposal or in federal fee recovery litigation?

JUDGE SCHWARZER: I heard that discussion this morning. I think it is a dilemma. But if you give them ninety days, you can conduct a lot of discovery in that ninety-day period. That may be productive, but it would also be undermining the whole notion of fee-shifting offers of judgment. Perhaps you could extend it to twenty-one days. I don't know. It is one of those questions that would be best answered by empirical evidence, which you cannot get. Yes.

AUDIENCE: What would you think about a system where some core discovery was done, and then, instead of the rule, or perhaps in conjunction with the rule, you go to the United States magistrate judge to mediate a settlement conference? I don't know how you define "some

core discovery," but some amount of depositions so that both parties feel that they've done due diligence, at least enough to measure the claim in their minds and in the minds of their client. I think at least those conferences have indicated that the clients appreciate the judgement of the magistrate judge based on facts that come out in that kind of core discovery. I know we have done that in some civil rights cases. But, don't you think that is maybe more effective than just lobbing Rule 68 offers, even if it became bilateral?

JUDGE SCHWARZER: Well, they are not mutually exclusive. My approach to case management has always been to sit the lawyers down early in the case, shortly after the filing, and try to identify what would be the key discovery, the key witness, and the key information they need to evaluate their case, rather than just having them flounder around. In most cases, they've got an idea pretty quickly about what the value of the case would be by focusing on discovery with a minimum of expense. That would be the time for Rule 68 offers to be exchanged. I mean it's not very desirable to have Rule 68 offers continue to be lobbed back and forth as discovery goes on. It is best to focus on the critical pivotal discovery early on. But I do not think you could adopt a rule that establishes that procedure. It is judicial case management that sets the case up for effective approaches to settlement. Yes.

AUDIENCE: This is really just a comment, Judge, but the rules are being amended in the next couple of months to add the use of electronic discovery. Electronic discovery has added a tremendous burden and tremendous expense to litigation, so I don't know how that might relate to your proposal. The purpose of my comment is simply to say that the trend of increasing costs of discovery seems to be going against what we are all trying to do, what we're talking about today, because I think the amendments are going to put increased burdens on both parties.

JUDGE SCHWARZER: Well, the cost of discovery has been going up, as I have been saying, and this will just accelerate the trend. But the rule contemplates that there will be some early definition of the scope of permissible electronic discovery, so they won't just run wild, and identify what can be done within reason and consistent with what is at stake in the lawsuit. I think that is really an underlying purpose of these rules. But we will see. It would be nice if all the e-mails were automatically eliminated after one year.

AUDIENCE: Yes, I agree.

JUDGE SCHWARZER: Well, thank you again.