

LOS ANGELES COUNTY BAR ASSOCIATION
PROFESSIONAL RESPONSIBILITY AND ETHICS COMMITTEE

OPINION NO. 517
April 17, 2006

INDEMNIFICATION OF CLIENT'S LITIGATION COSTS

SUMMARY

An attorney may agree to advance the reasonable expenses of prosecuting or defending a client's matter and waiving the right to repayment by the client if there is no recovery. Similarly, at either the inception of the representation or during the course of litigation, an attorney may agree to indemnify the client for court ordered costs if the client is not the prevailing party.

AUTHORITIES CITED

Code of Civil Procedure §§ 998 and 1034

Ripley v Pappadopolous (1994) 23 Cal App. 4th 1616

California Rules of Professional Conduct, Rules 3-310(B) and 4-210(A)

State Bar Formal Opinion 1976-38 and State Bar Formal Opinion 1994-138

Los Angeles County Bar Association, Professional Responsibility and Ethics Committee,
Formal Opinion No. 495

STATEMENT OF FACTS

Attorney seeks to represent clients in civil litigation matters who are unable or unwilling to pay costs in the event they do not prevail in the litigation. Attorney wants to indemnify the clients from any costs that may be awarded by the court if the clients are not a prevailing party. In some cases, the request for an indemnity arises at the inception of the representation and in other cases it arises during the course of the litigation.

QUESTIONS PRESENTED

Is it permissible for a lawyer or law firm to indemnify a client for costs associated with litigation in the event the client loses and the prevailing party files a memorandum of costs?

DISCUSSION

California Rule of Professional Conduct 4-210(A), provides:

A member shall not directly or indirectly agree to pay, guarantee, represent or sanction a representation that the member or the member's law firm will pay the personal or business expenses of a prospective or existing client, except that this rule shall not prohibit a member:

...

(3) From advancing the costs of prosecuting or defending a claim or action or otherwise protecting or promoting the client's interests, the repayment of which may be contingent on the outcome of the matter. Such costs within the meaning of this subparagraph (3) shall be limited to all reasonable expenses of litigation or reasonable expenses in preparation for litigation or in providing any legal services to the client." (emphasis added).

The unambiguous language of Rule 4-210(A)(3) permits an attorney to agree to pay a client's reasonable litigation costs. (See *Ripley v Pappadopolous* (1994) 23 Cal App.4th 1616, 1626, fn. 17 noting that the rule allows "an attorney to advance the costs of prosecuting or defending a claim and also permits repayment to be made contingent on the outcome of the matter.") Additionally, State Bar Formal Opinion 1976-38 provides that Rule 4-210 does not prohibit a lawyer from advancing expenses for which the client is responsible, even when there is a substantial likelihood that the client does not have the means to pay them. (Re-cited by analogy in State Bar Formal Opinion 1994-138). Los Angeles County Bar Association Formal Opinion No. 495 concludes that "an attorney may advance the reasonable expenses of prosecuting or defending an action notwithstanding the client's refusal to pay such costs, after they were incurred and even though the expenses might not be repaid."

Rule 4-210(A)(3) does not expressly address indemnifications of clients for costs if the client does not prevail. However, such an indemnification is not materially different from advancing costs repayment of which is contingent on the outcome¹. To the extent an indemnification is not considered a form of advancing costs through an indirect, potential or ancillary obligation, the Committee believes it is permitted either at the inception of a matter or during the course of litigation under the general exception of "otherwise protecting or promoting the client's interests." Further, since the indemnified expenses of litigation are to be decided by the trial court as mandated under Code of Civil Procedure §§ 1033 and 1034², the amount determined by the court is presumptively reasonable and, therefore, permissible under Rule 4-210(A).

A related question is whether a proposed indemnification of costs agreement between an attorney and client implicates ethical consideration under Rule of Professional Conduct 3-310(B)³ by creating an adverse interest between the attorney and the client. In the Committee's

¹ Unlike costs that are advanced by an attorney, an indemnification by an attorney could still result in liability to the client where the attorney fails to pay, however, the Committee does not believe that this potential distinction is relevant to the applicability of the Rule 4-210(A)(3) exception.

² C.C.P. §§ 1033 and 1034 state that "1033. (a) Costs or any portion of claimed costs shall be as determined by the court in its discretion in a case other than a limited civil case in accordance with Section 1034 where the prevailing party recovers a judgment that could have been rendered in a limited civil case.

(b) When a prevailing plaintiff in a limited civil case recovers less than the amount prescribed by law as the maximum limitation upon the jurisdiction of the small claims court, the following shall apply:

(1) When the party could have brought the action in the small claims division but did not do so, the court may, in its discretion, allow or deny costs to the prevailing party, or may allow costs in part in any amount as it deems proper.

(2) When the party could not have brought the action in the small claims court, costs and necessary disbursements shall be limited to the actual cost of the filing fee, the actual cost of service of process, and, when otherwise specifically allowed by law, reasonable attorneys' fees. However, those costs shall only be awarded to the plaintiff if the court is satisfied that prior to the commencement of the action, the plaintiff informed the defendant in writing of the intended legal action against the defendant and that legal action could result in a judgment against the defendant that would include the costs and necessary disbursements allowed by this paragraph."

"1034. (a) Prejudgment costs allowable under this chapter shall be claimed and contested in accordance with rules adopted by the Judicial Council.

(b) The Judicial Council shall establish by rule allowable costs on appeal and the procedure for claiming those costs."

³ Rules of Professional Conduct, Rule 3-310(b): "(B) A member shall not accept or continue representation of a client without providing written disclosure to the client where:

(1) The member has a legal, business, financial, professional, or personal relationship with a party or witness in the same matter; or

view, the proposed agreement does not create a legal, business, financial, professional or personal relationship with the client in violation of Rule 3-310(B)(1) or Rule 3-310(b)(3), nor does it create a legal, business, financial or professional interest in the subject matter of the representation in violation of Rule 3-310(B)(4). In this instance, the interests of the attorney and the client are the same as they are with any other type of cost or expense associated with a contingency case. The specter of increasing costs, as the case proceeds to trial or in the face of a Code of Civil Procedure § 998⁴ offer, are present in every contingency case. The proposed

(2) The member knows or reasonably should know that:

(a) the member previously had a legal, business, financial, professional, or personal relationship with a party or witness in the same matter; and

(b) the previous relationship would substantially affect the member's representation; or

(3) The member has or had a legal, business, financial, professional, or personal relationship with another person or entity the member knows or reasonably should know would be affected substantially by resolution of the matter; or

(4) The member has or had a legal, business, financial, or professional interest in the subject matter of the representation.”

⁴C.C.P. § 998 provides that “998. (a) The costs allowed under Sections 1031 and 1032 shall be withheld or augmented as provided in this section.

(b) Not less than 10 days prior to commencement of trial or arbitration (as provided in Section 1281 or 1295) of a dispute to be resolved by arbitration, any party may serve an offer in writing upon any other party to the action to allow judgment to be taken or an award to be entered in accordance with the terms and conditions stated at that time. The written offer shall include a statement of the offer, containing the terms and conditions of the judgment or award, and a provision that allows the accepting party to indicate acceptance of the offer by signing a statement that the offer is accepted. Any acceptance of the offer, whether made on the document containing the offer or on a separate document of acceptance, shall be in writing and shall be signed by counsel for the accepting party or, if not represented by counsel, by the accepting party.

(1) If the offer is accepted, the offer with proof of acceptance shall be filed and the clerk or the judge shall enter judgment accordingly. In the case of an arbitration, the offer with proof of acceptance shall be filed with the arbitrator or arbitrators who shall promptly render an award accordingly.

(2) If the offer is not accepted prior to trial or arbitration or within 30 days after it is made, whichever occurs first, it shall be deemed withdrawn, and cannot be given in evidence upon the trial or arbitration.

(3) For purposes of this subdivision, a trial or arbitration shall be deemed to be actually commenced at the beginning of the opening statement of the plaintiff or counsel, and if there is no opening statement, then at the time of the administering of the oath or affirmation to the first witness, or the introduction of any evidence.

(c) (1) If an offer made by a defendant is not accepted and the plaintiff fails to obtain a more favorable judgment or award, the plaintiff shall not recover his or her postoffer costs and shall pay the defendant's costs from the time of the offer. In addition, in any action or proceeding other than an eminent domain action, the court or arbitrator, in its discretion, may require the plaintiff to pay a reasonable sum to cover costs of the services of expert witnesses, who are not regular employees of any party, actually incurred and reasonably necessary in either, or both, preparation for trial or arbitration, or during trial or arbitration, of the case by the defendant.

(2) (A) In determining whether the plaintiff obtains a more favorable judgment, the court or arbitrator shall exclude the postoffer costs.

(B) It is the intent of the Legislature in enacting subparagraph (A) to supersede the holding in *Encinitas Plaza Real v. Knight*, 209 Cal.App.3d 996, that attorney's fees awarded to the prevailing party were not costs for purposes of this section but were part of the judgment.

(d) If an offer made by a plaintiff is not accepted and the defendant fails to obtain a more favorable judgment or award in any action or proceeding other than an eminent domain action, the court or arbitrator, in its discretion, may require the defendant to pay a reasonable sum to cover postoffer costs of the services of expert witnesses, who are not regular employees of any party, actually incurred and reasonably necessary in either, or both, preparation for trial or arbitration, or during trial or arbitration, of the case by the plaintiff, in addition to plaintiff's costs.

indemnity does not present a different ethical result and is simply a contractual expansion of the scope of reasonable expenses of litigation to be encompassed with the ambit of Rule 4-210(A)(3).

This opinion is advisory only. The committee acts on specific questions submitted ex parte and its opinions are based only on such facts as are set forth in the questions submitted.

(e) If an offer made by a defendant is not accepted and the plaintiff fails to obtain a more favorable judgment or award, the costs under this section, from the time of the offer, shall be deducted from any damages awarded in favor of the plaintiff. If the costs awarded under this section exceed the amount of the damages awarded to the plaintiff the net amount shall be awarded to the defendant and judgment or award shall be entered accordingly.

(f) Police officers shall be deemed to be expert witnesses for the purposes of this section. For purposes of this section, "plaintiff" includes a cross-complainant and "defendant" includes a cross-defendant. Any judgment or award entered pursuant to this section shall be deemed to be a compromise settlement.

(g) This chapter does not apply to either of the following:

- (1) An offer that is made by a plaintiff in an eminent domain action.
- (2) Any enforcement action brought in the name of the people of the State of California by the Attorney General, a district attorney, or a city attorney, acting as a public prosecutor.

(h) The costs for services of expert witnesses for trial under subdivisions (c) and (d) shall not exceed those specified in Section 68092.5 of the Government Code.

(i) This section shall not apply to labor arbitrations filed pursuant to memoranda of understanding under the Ralph C. Dills Act (Chapter 10.3 (commencing with Section 3512) of Division 4 of Title 1 of the Government Code)."