

IN THE
SUPREME COURT OF THE UNITED STATES

NO. LH90-111590

AUGUSTUS O. HOWARD FEED COMPANY, INC.,

Petitioner,

v.

BAYOU FEED COMPANY, INC.,

Respondent.

BRIEF FOR RESPONDENT

TABLE OF CONTENTS

	<u>Page</u>
TABLE OF AUTHORITIES.....	iii
QUESTIONS PRESENTED.....	v
STATEMENT OF THE CASE.....	2
SUMMARY OF THE ARGUMENT.....	4
ARGUMENT.....	6
I. The District Court correctly imposed sanctions in the form of attorney's fees, expenses, and costs against Howard and West pursuant to 28 U.S.C. §1927 and Federal Rule of Civil Procedure 11 when directly conflicting state law prohibited the imposition of such sanctions.....	6
A. The District Court correctly imposed sanctions of expenses and costs against West pursuant to 28 U.S.C. §1927.....	6
1. In a diversity case, Federal Statute 28 U.S.C. §1927 supersedes Lewis Hall Statute 59 L.H.C. §1500.....	6
2. Under Federal Statute 28 U.S.C. §1927, the District Court can sanction West for unreasonably and vexatiously multiplying proceedings.....	8
B. <u>Hanna v. Plumer</u> and the Rules Enabling Act provide the proper test for determining whether a Federal Rule of Civil Procedure should supersede a State Rule of Civil Procedure in a diversity action.....	10
1. According to the <u>Hanna</u> three prong test, the sanctions of expenses and costs levied against West are appropriate as Federal Rule of Civil Procedure 11 supersedes Lewis Hall Rule of Civil Procedure 420....	11
2. According to the <u>Hanna</u> three prong test, the sanctions of attorney's fees levied against Howard are appropriate as Federal Rule of Civil Procedure 11 supersedes Lewis Hall Rule of Civil Procedure 420....	13

TABLE OF AUTHORITIES

Cases:	Page
<u>Affholder, Inc. v. Southern Rock, Inc.</u> , 746 F.2d 305 (5th Cir. 1984).....	10
<u>Alyeska Pipeline Co. v. Wilderness Soc'y</u> , 421 U.S. 240 (1974).....	17 22

II. Application of the Erie doctrine shows the trial court did not err in imposing additional attorney's fees against Howard, pursuant to the court's inherent powers, for litigating in bad faith and for vexatious reasons.....	16
A. That a Lewis Hall state law disallowing attorneys' fees conflicts with federal court's use of inherent powers to grant attorneys is not determinative of the court's ability to use its contempt power for abuse of its process where litigant brings the suit in bad faith and for vexatious reasons.....	16
B. Application of the Erie doctrine does not mandate a reversal of the Court of Appeals' award of attorney's fees to Bayou.....	19

<u>Prima Paint Corp. v. Flood & Conklin Mfg. Co.</u> , 388 U.S. 395 (1967).....	8
<u>Roadway Express v. Piper</u> , 447 U.S. 752 (1979).....	18
<u>State Sec. Ins. Co. v. White</u> , 498 F. Supp. 873 (S.D. Ga. 1980), <u>aff'd</u> 667 F.2d 97 (5th Cir. 198?).....	24
<u>Stewart Organization, Inc. v. Ricoh Corp.</u> , 108 S. Ct. 2239 (1988).....	6,7,8
<u>United States v. City of Twin Falls, Idaho</u> , 806 F.2d 862 (7th Cir. 1986).....	22
<u>United States v. Hudson</u> , 7 Cranch 32 (1812).....	18
<u>Walker v. Armaco Steel Corp.</u> , 446 U.S. 740 (1980).....	7
<u>Zaldivar v. City of Los Angeles</u> , 780 F.2d 823 (9th Cir. 1986).....	13

Statutes:

28 U.S.C. §1441.....	21
28 U.S.C. §1927.....	7,8
59 L.H.C. §1500.....	7,19

Rules:

Fed. R. Civ. P. 11.....	11,13
L.H.R. Civ. P. 420.....	11,13,19

QUESTIONS PRESENTED

- I. Whether the District Court erred in imposing sanctions in the form of attorney's fees, expenses and costs against Howard and West pursuant to Federal Rule of Civil Procedure 11 and 28 U.S.C. Sec. 1927 when directly conflicting state law prohibits the imposition of such sanctions?

- II. Whether the trial court erred in imposing additional sanctions against Howard pursuant to the Court's inherent powers when directly conflicting state law prohibits the imposition of such sanctions?

IN THE
SUPREME COURT OF THE UNITED STATES
October Term, 1990

NO. LH90-111590

AUGUSTUS O. HOWARD FEED COMPANY, INC., Petitioner,

v.

BAYOU FEED COMPANY, INC., Respondent.

On Appeal from the State of Lewis Hall
Court of Appeals

Brief for Respondent

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STATEMENT OF THE CASE

On January 25, 1990, Howard Feed Co., the petitioner in this action, entered into a contract for the purchase of a feed processing plant in Louisiana owned by Bayou Feed Co., the respondent in this action. Howard Feed Co. v. Bayou Feed Co., 1022 F. Supp. 1 (1990). Two days after entering into the contract, Howard learned of a feed processing plant in Florida which it could purchase at a lower price than the Bayou plant. Id. Howard then sought to avoid performance of its contractual obligations with Bayou so it could purchase the less expensive plant in Florida. Id. at 1-2.

In an attempt to avoid its obligation under the January 25th contract, Howard created a falsified Industrial Engineer's Report, stating that the Louisiana plant operated at a significantly lower production capacity than stated in the contract. Id. Howard believed that the threat of costly litigation involving claims of fraud would convince Bayou to settle by voiding the contract. Id. Bayou refused to do so. Id. Howard then sued in Lewis Hall State Court. Id.

Defendant Bayou then made a motion to remove the action to Federal District Court on the grounds of diversity; the motion was granted. Id. Following the removal, Howard then falsified a second report, the Economic Report, which asserted that Bayou's plant equipment was 20 years older than Bayou represented it to be. Id. Petitioner's attorney, West, signed and filed an amended complaint with the District Court making two allegations

of fraud. Id. at 2-3.

Bayou answered the Amended Complaint by denying the allegations of fraud. Id. at 3. Bayou moved for dismissal of the action under Fed.R.Civ.P. 12(b)(6), for failure to state a claim. Id. Bayou also moved under Fed.R.Civ.P. 11 and 28 U.S.C. §1927, and the court's inherent powers, for sanctions against Howard and West, in the form of costs, expenses and attorney's fees. Id.

The United States District Court, District of Lewis Hall, granted the motion to dismiss. Id. at 4. That court also imposed sanctions upon West, to pay for Bayou's expenses and costs totalling \$3500, by virtue of its authority under Rule 11 and §1927. Id. The court also sanctioned Howard under Rule 11, requiring Howard to pay \$50,000 in attorney's fees to Bayou. Id. Using the court's inherent powers, the court ordered Howard to pay another \$50,000 in attorney's fees to Bayou. Id. at 5.

The Court of Appeals affirmed the District Court's sanctions under Rule 11 and §1927 as to West, and the sanction against Howard pursuant to Rule 11. Howard Feed Co. v. Bayou Feed Co., 22 F.3d 1 (1990). The Court of Appeals also affirmed the use of the court's inherent powers to provide an extra sanction against Howard for its bad faith conduct in falsifying the reports. Id.

SUMMARY OF THE ARGUMENT

I.

According to the test in Stewart Organization, Inc. v. Ricoh Corp., Federal Statute 28 U.S.C §1927 supersedes Lewis Hall Statute 59 L.H.C. §1500. Federal Statute 28 U.S.C. §1927 sanctions the actions of West, attorney for the Petitioner. Thus, the Court is authorized to grant the Respondent, Bayou, the award of expenses and costs against West.

Under the analysis of Hanna v. Plumer and the Rules Enabling Act, Federal Rule of Civil Procedure 11 supersedes Lewis Hall Rule of Civil Procedure 420. Rule 11 sanctions the actions of both West and the Petitioner Howard. Thus, the Court is authorized to grant to the Respondent, Bayou, the award of expenses and costs against West and attorney's fees against Petitioner Howard.

II.

The Erie doctrine applies in normal diversity cases in federal court, where a state law conflicts with a federal common law. The state law is to prevail in an ordinary situation. However, the state law denying a right to attorney's fees should not prevail over the court's inherent power to grant such fees in a situation where the litigant has brought a fraudulent action in bad faith. Allowing the state law's application in this case

would be to permit the petitioner to abuse the process of the federal court by bringing a baseless claim in bad faith. The use of inherent powers to sanction contempt of the court, used here to grant attorney's fees, should be approved. The bad faith conduct of the petitioner brings this case outside the realm of an ordinary diversity case, so the Erie rule should not prevent the award of attorney's fees.

ARGUMENT

- I. THE DISTRICT COURT CORRECTLY IMPOSED SANCTIONS IN THE FORM OF ATTORNEY'S FEES, EXPENSES, AND COSTS AGAINST HOWARD AND WEST PURSUANT TO 28 U.S.C. §1927 AND FEDERAL RULE OF CIVIL PROCEDURE 11 WHEN DIRECTLY CONFLICTING STATE LAW PROHIBITED THE IMPOSITION OF SUCH SANCTIONS.

With regard to the awards under 28 U.S.C. §1927 and Rule 11, the standard of review is "abuse of discretion." In re TCI Ltd., 769 F.2d 441, 445 (7th Cir. 1985).

- A. The District Court correctly imposed sanctions of expenses and costs against West pursuant to 28 U.S.C. §1927.

1. In a diversity case, Federal Statute 28 U.S.C. §1927 supersedes Lewis Hall Statute 59 L.H.C. §1500.

Stewart Organization, Inc v. Ricoh Corp. states the test used in determining whether federal law in the form of a congressional statute supersedes a state statute in a diversity case. Stewart Organization, Inc v. Ricoh Corp., 108 S. Ct. 2239, 2241-2243 (1988). This test is considerably less intricate than the one which governs the "relatively unguided Erie choice." Id. at 2242 (citing Hanna v. Plumer, 380 U.S. 460, 471 (1965)). The test consists of two prongs:

a. Whether the [federal] statute is sufficiently broad to control the issue before the court?

b. Whether the [federal] statute represents a valid exercise of Congress' authority under the Constitution?

Id.

- a. Federal Statute 28 U.S.C. §1927 is sufficiently broad to control the issue of sanctioning an attorney for a violation.

This first prong involves interpreting 28 U.S.C. §1927 to determine if it covers the point in dispute. Walker v. Armaco Steel Corp., 446 U.S. 740, 750 (1980). This is a "straightforward exercise" which simply asks whether there is a "direct collision" between Federal Statute 28 U.S.C. §1927 and 59 L.H.C. §1500. Stewart, 108 S. Ct. at 2242; Burlington Northern R. Co. v. Woods, 480 U.S. 1, 5 (1986). However, this does not mean that the federal and state law must be perfectly coextensive. Stewart, 108 S. Ct. at 2242 n.4.

Federal Statute 28 U.S.C. §1927 does directly collide with 59 L.H.C. §1500 as each provides a different sanction for the same attorney violation. Section 1927 states that the attorney may be required to satisfy personally the excess costs and expenses reasonably incurred because of [his/her] conduct, 28 U.S.C. §1927, while §1500 sanctions the violating attorney to disciplinary actions to be taken by the Lewis Hall State Bar Association's Ethics Review Committee. 59 L.H.C. §1500.

- b. Federal Statute 28 U.S.C. §1927 does represent a valid exercise of Congress' authority under the Constitution.

Under the second prong, the standard is whether "Congress intended to reach the issue before the District Court and whether it enacted its intention into law in a manner that abides with the Constitution." Stewart, 108 S. Ct. at 2243. Congress intended to reach the issue of attorney's sanctions for

unreasonably and vexatiously multiplying proceedings and thereby enacted this intention into 28 U.S.C. §1927. See 28 U.S.C. §1927. Both the constitutional provision for a federal court system and the Necessary and Proper Clause of Article I, grant to Congress the "power to regulate matters which, though falling within the uncertain area between substance and procedure, are rationally capable of classification as either." Id. at 2245 (quoting Hanna, 380 U.S. at 472). Federal courts are bound to apply those rules enacted by Congress within its legislative authority. Id. (citing Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395, 406 (1967)). Therefore, Congress enacted 28 U.S.C. §1927, which deals with the procedural method of applying attorney sanctions, in accordance with the Constitution, and the federal courts are **bound** to apply said statute.

Since 28 U.S.C. §1927 is sufficiently broad to control the issue at hand as it directly collides with 59 L.H.C. §1500, and Congress enacted §1927 under a constitutional mandate, §1927 supersedes state statute §1500.

2. Under Federal Statute 28 U.S.C. §1927, the District Court can sanction West for unreasonably and vexatiously multiplying proceedings.

Federal Statute 28 U.S.C. §1927 states that a court may sanction an attorney in the form of excess costs and expenses for conduct which unreasonably and vexatiously multiplies the proceedings in any case. 28 U.S.C. §1927. The court in Braley v. Campbell defined the proper standard of a §1927 violation to be such conduct that "viewed objectively, manifests either

intentional or **reckless disregard** of the attorney's duties to the court." Braley v. Campbell, 832 F.2d 1504, 1512 (10th Cir. 1987). The court need not find subjective bad faith to impose sanctions under 28 U.S.C. §1927. Id., (citing In re TCI Ltd., 769 F.2d at 445).

Under the reckless disregard standard, West is in violation of §1927. West did not do **any** legal or factual research before filing the complaint against Bayou, and she did not inquire into the authenticity of either the Engineer's Report or the Economic Report. By not inquiring about the factual foundation of Howard's complaint, West recklessly disregarded her duty to not unreasonably and vexatiously multiply proceedings.

An attorney's reckless behavior may impose considerable costs upon an opposing party. Id. at 1511 (citing TCI, 769 F.2d at 445). Section 1927 places the burden upon the violating attorney to "bear the costs of his own lack of care." Id. Had West properly investigated the Engineer's Report and the Economic Report, she would have discovered their manufactured nature thus saving both the District Court's and Bayou's time and money. To excuse such unreasonable and reckless behavior would be the same as stating that "one who acts with an empty head and a pure heart is not responsible for the consequences." Id. at 1512 (quoting McCandless v. Great Atlantic and Pacific Tea Co., 697 F.2d 198, 200 (7th Cir. 1983)).

The District Court properly sanctioned attorney West to pay \$3,500 in costs and expenses under 28 U.S.C. §1927.

B. Hanna v. Plumer and the Rules Enabling Act provide the proper test for determining whether a Federal Rule of Civil Procedure should supersede a State Rule of Civil Procedure in a diversity action.

The Supreme Court in Hanna v. Plumer stated that the rule of Erie R. Co. v. Tompkins is not the appropriate test when dealing with a conflict between a federal rule and a state rule in a diversity case. Hanna, 380 U.S. at 469-470. Rather, the Rules Enabling Act contains the correct standard to apply when dealing with such a conflict. Id. at 470.

The court in Burlington Northern R. Co. v. Woods interpreted the test of Hanna v. Plumer to include three prongs:

a. Whether the scope of the federal rule is "sufficiently broad" such that it "directly collides" with the state law, or "controls the issue" before the court?

b. Whether the federal rule represents a valid exercise of Congress' rulemaking authority under the Constitution? (Is the rule arguably procedural?)

c. Whether, under the Rules Enabling Act, the federal rule abridges, enlarges, or modifies any substantive right?

Burlington, 480 U.S. at 4-5.

The Rules Enabling Act and Hanna require that the court give deference and strong presumptive validity to a federal rule.

Affholder, Inc. v. Southern Rock, Inc., 746 F.2d 305, 310-311

(5th Cir. 1984). The Supreme Court in Hanna said:

The court has been instructed to apply the Federal Rule, and can refuse to do so only if the Advisory Committee, this Court, and Congress erred in their prima facie judgement that the Rule in question transgresses neither the terms of the Enabling Act nor constitutional restrictions.

Hanna 380 U.S. at 471; see also Burlington, 480 U.S. at 6.

The Court should apply this three prong analysis, with

regard to the above presumption, to the Rule 11 sanctions imposed on both West and Howard.

1. According to the Hanna three prong test, the sanctions of **expenses and costs** levied against **West** are appropriate as Federal Rule of Civil Procedure 11 supersedes Lewis Hall Rule of Civil Procedure 420.

- a. The scope of Federal Rule 11 is sufficiently broad such that it directly collides with Lewis Hall Rule 420.

Federal Rule of Civil Procedure 11 states that, upon a finding of a violation of said rule, the court shall impose an appropriate sanction, upon the person who signed the pleading, which may include the amount of **reasonable expenses** incurred by the other party. Fed R. Civ. P. 11. This Rule directly collides with Lewis Hall Rule of Civil Procedure 420 which states that the appropriate sanction shall be **disciplinary action** taken by the Lewis Hall State Bar Association's Ethics Review Committee. "No court may impose any sanction other than that provided for in this rule." L. H. R. Civ. P. 420.

- b. In accordance with Congress' rulemaking authority under the Constitution, Rule 11 is arguably procedural.

Rules which are indisputably procedural as well as rules that fall "within the uncertain area between substance and procedure" such that they are "rationally capable of classification as either" meet this prong's constitutional constraint. Burlington, 480 U.S. at 5 (citing Hanna, 380 U.S. at 472). Rule 11 is arguably procedural as its "central purpose . . . is to deter baseless filings in district court and thus,

consistent with the Rules Enabling Act's grant of authority, streamline the administration and procedure of federal courts. Cooter and Gell v. Hartmax Corp., 110 S. Ct. 2447, 2454 (1990). Rule 11 simply prescribes a method of enforcing a parties right of not having to spend precious time and money defending frivolous and unfounded claims. The sanction of expenses and costs is such a means of enforcing Bayou's rights under Rule 11.

- c. In accordance with the Rules Enabling Act, Rule 11 does not abridge, enlarge, or modify any substantive right.

Federal Rule of Civil Procedure 11 does not abridge, enlarge, or modify any substantive right as it affects only the process of enforcing Bayou's right and not the rights themselves. See Burlington, 480 U.S. at 8. Both Rule 11 and Rule 420 provide Bayou with the substantive right of not having to spend precious time and money defending frivolous and unfounded claims. The method of enforcing said right does not change in any way the content of the right itself. Id. Rule 11 provides monetary sanctions, while Rule 420 protects said right by disciplinary action. These two rules simply contain different ways of enforcing the same right. As such, the sanction of expenses and costs levied against West for the violation of Rule 11 in no way abridges, enlarges, or modifies any substantive right.

The arguments above and the strong presumption in favor of the Federal Rules maintain that the court should apply Federal Rule 11. With respect to sanctions against West, Federal Rule of Civil Procedure 11 passes all three prongs of the Hanna analysis

and therefore, supersedes Lewis Hall Rule of Civil Procedure 420.

Given that Rule 11 controls, West is liable for expenses and costs as a violation of Rule 11 need not be based on a finding of subjective bad faith. Zaldivar v. City of Los Angeles, 780 F.2d 823, 829-831 (9th Cir. 1986). Rather it is enough that an attorney signs a pleading without having conducted a "reasonable inquiry into whether his paper is . . . without factual foundation." Id. This standard is easily met as West not only made no reasonable inquiry into the factual foundation of Howard's claim, he made no inquiry at all.

2. According to the Hanna three prong test, the sanction of attorney's fees levied against Howard are appropriate as Federal Rule of Civil Procedure 11 supersedes Lewis Hall Rule of Civil Procedure 420.

- a. The scope of Federal Rule 11 is sufficiently broad such that it directly collides with Lewis Hall Rule 420.

Federal Rule of Civil Procedure 11 states that, upon a finding of a violation of said Rule, the court shall impose an appropriate sanction, upon . . . **a represented party**, which may include the amount of a reasonable attorney's fee incurred by the other party. Fed. R. Civ. P. 11. This Rule directly collides with Lewis Hall Rule of Civil Procedure 420 which states that the court shall impose the prescribed sanction **only upon the signer** of the pleading. L. H. R. Civ. P. 420.

- b. In accordance with Congress' rulemaking authority under the Constitution, Rule 11 is arguably procedural.

With regard to the sanctions levied against Howard,

the analysis of the second prong of the Hanna test is the same as that used to analyze West's situation. A rule which falls "within the uncertain area between substance and procedure" such that it is "rationally capable of classification as either" meets this prong's constitutional constraint. Burlington, 480 U.S. at 5 (citing Hanna, 380 U.S. at 472. In either situation, Rule 11 is arguably procedural as its "central purpose is to deter baseless filings in district court and thus consistent with the Rules Enabling Act's grant of authority, streamline the administration and procedure of federal courts." Cooter, 110 S. Ct. at 2454. The sanction of attorney's fees against Howard is a method of **enforcing** Bayou's rights, protected by Rule 11, not to have to spend precious time and money defending frivolous and unfounded claims.

- c. In accordance with the Rules Enabling Act, Rule 11 does not abridge, enlarge, or modify any substantive right.

Eventhough, under 14 L.H.C. §1300, a party must bring a separate action for malicious prosecution in order to recover attorney fees, Howard Feed Co. v. Bayou Feed Co., 22 F.3d 1, 3-4 (1990) (citing McCool Films v. Marlow Rubber and Doll Co., 646 L.H.3d 750 (1989)), the right to be free from frivolous and unfounded claims, under Rule 11 and Rule 420, does not change. If the case at hand is governed by either Rule 11 or a combination of Rule 420 and 14 L.H.C. §1300, Bayou may still recover an award of attorney's fees from Howard. The only difference between the two systems is the procedure Bayou must go

through to claim his award. A rule does not violate the Rules Enabling Act if it only affects the process of enforcing a party's rights and not the rights themselves. Burlington, 480 U.S. at 8.

The court in Burlington, interpreting Hanna with regard to the Rules Enabling Act, stated:

The cardinal purpose of Congress in authorizing the development of a uniform and consistent system of rules governing federal practice and procedure suggests that Rules which incidentally affect litigant's rights do not violate [the Rules Enabling Act] if reasonably necessary to maintain the integrity of that system of rules. See Hanna, 480 U.S. at 464-465.

Id. at 5.

The integrity of the Federal Rules of Civil Procedure, especially Rule 11, would be violated if the Court should allow Howard to sidestep liability by not applying the Federal Rule over the State Rule. Howard's **gross misconduct** is a prime example of why the court should sanction a represented party under Rule 11. Howard Feed Co. v. Bayou Feed Co., 1022 F. Supp. 1, 7-8 (1990). Howard intentionally manufactured false documents solely for the purpose of harassing Bayou into rescinding a valid and binding contract for the sale of the Louisiana feed processing plant. The court cannot allow this type of revolting behavior to escape punishment.

The arguments above and the strong presumption in favor of the Federal Rules maintain that the court should apply Federal Rule 11. With respect to sanctions against Howard, Federal Rule of Civil Procedure 11 passes all three prongs of the Hanna

analysis, and therefore, supersedes Lewis Hall Rule of Civil Procedure 420.

II. APPLICATION OF THE ERIE DOCTRINE SHOWS THE TRIAL COURT DID NOT ERR IN IMPOSING ADDITIONAL ATTORNEY'S FEES AGAINST HOWARD, PURSUANT TO THE COURT'S INHERENT POWERS, FOR LITIGATING IN BAD FAITH AND FOR VEXATIOUS REASONS.

A. That a Lewis Hall state law disallowing attorneys' fees conflicts with federal court's use of inherent powers to grant attorneys is not determinative of the court's ability to use its contempt power for abuse of its process where litigant brings the suit in bad faith and for vexatious reasons.

The Erie doctrine is a federal common law that arises when a case is brought to the federal court system solely due to diversity of citizenship. The purpose of the doctrine is to resolve conflicts between a state law and a federal law. Since such a conflict exists in this case, the Erie doctrine must be applied.

The rule has its origins in Erie R. Co. v. Tompkins, 304 U.S. 64 (1937). The Court decided in this landmark case that, the law of the state, whether statutory or common, is the law to be applied in a diversity case in the federal courts. Id. at 78. Later cases have refined the rule. Erie is now seen to embody two separate, yet similar, ideas. One is "a realization that it would be unfair for the character or result of a litigation materially to differ because the suit had been brought in a federal court" rather than the state court. Hanna v. Plumer, 380 U.S. 460, 467 (1964). The second purpose of the rule is to prevent "forum shopping," the practice of choosing a federal court over a state court based on the remedies available. Id. In effect, a federal court sitting

in diversity adjudicating a state-created right is acting as a state court. Guaranty Trust Co. v. York, 326 U.S. 99, 108 (1949). Since the federal court is acting as a state court, it cannot provide any remedy that is unavailable in the state court, ensuring that the result of the litigation is substantially the same in the federal forum as it would be in the state court. Id.

The instant case involves a conflict between state common law and federal common law. The conflict is whether attorney fees can be awarded to the victorious party in a suit. The courts of Lewis Hall indicate that the state allows for attorney's fees only when a contract or statute specifically provides for them. Glove v. Campbell and the L.S.F.L. Football Comm'n, 872 L.H.3d 1650, 1652 (1989). No law of Lewis Hall provides for an award of attorney's fees when a litigant brings a suit in bad faith for vexatious reasons. Id.

Federal courts follow the "American Rule", which "ordinarily requires parties to shoulder their own counsel fees and litigation expenses absent statutory or contractual authority for an alternative allocation." Lipsig v. National Student Mktg. Corp., 663 F.2d 178, 180 (D.C. Cir. 1980). The "American Rule" is very similar to the law of Lewis Hall, except that the rule as applied by the federal courts allows for several exceptions. One of these exceptions is an assessment of attorney's fees when the "losing party has acted in bad faith, vexatiously, wantonly, or for oppressive reasons." Alyeska Pipeline Co. v. Wilderness Soc'y, 421 U.S. 240, 258-59, (1974). This "bad faith" exception creates the

conflict between the state and federal laws.

Strong policy reasons underly the federal court's exception to the "American Rule." The bad faith exception is an exercise of the court's inherent power to administer legal proceedings. Hanna, 380 U.S. at 472-73. Inherent powers of the federal courts

are those which 'are necessary to the exercise of all others." United States v. Hudson, 7 Cranch 32, 34 (1812). The most prominent of these is the contempt sanction, "which a judge must have and exercise in protecting the due and orderly administration of justice and in maintaining the authority and dignity of the court." Cooke v. United States, 267 U.S. 517, 539 (1925).

Roadway Express v. Piper, 447 U.S. 752, 764 (1979). The inherent power invested in a court is used to manage the affairs of the court in the absence of a statute or rule. Id. at 765.

The facts of this case show that Howard brought this law suit based on evidence fraudulently constructed by Howard himself, for the purpose of enticing Bayou to withdraw from its legal and fair contract with Howard. The state law contract claim asserted against Bayou was no more than an attempt of Howard's to unfairly get out of a binding contract. Bad faith litigation such as this should not be tolerated by the federal court system, even in the event such abuses would be tolerated by the state court system of Lewis Hall. The award of attorney's fees for Howard's bad faith, vexatious litigation is a proper exercise of the federal court's inherent power to manage its affairs and preserve its dignity. "We do not see how the district court's inherent power to tax fees for [bad faith] conduct can be made subservient to any state policy without transgressing the boundaries set out in Erie, Guaranty

Trust Co., and Hanna. Fee-shifting here is not a matter of substantive remedy, but of vindicating judicial authority." NASCO Inc. v. Calcasieu Television and Radio, 894 F.2d 696, 705 (5th Cir. 1990).

Furthermore, the law of Lewis Hall imposes no penalty against a litigant himself for initiating a bad faith, vexatious law suit. The statute and rule of the state discussed in Issue I apply to the attorney, but not the litigant. Thus, under Lewis Hall law, a litigant goes without penalty for abusing the court system, although his attorney may be punished for ethical violations.

There is no indication that either 59 L.H.C. 1500 or L. H. R. Civ. P. 420 anticipated the circumstances addressed by this case, where an attorney, through lack of diligence, allows his client's fraudulent claim to proceed to court. Merely because misconduct by parties, rather than attorneys "had not been found to be sufficiently widespread as to warrant a rule, that hardly compels the inference that when it does occur, the court lacks inherent power to deal with it because the subject was addressed by a rule and the rule omitted parties." Id. at 703. Thus, the failure of the Lewis Hall legislature to anticipate the circumstances of this case does not prevent the ability of the federal court to exercise its inherent powers to award attorney's fees to the prevailing party in a bad faith litigation.

B. Application of the Erie doctrine does not mandate a reversal of the Court of Appeals' award of attorneys' fees to Bayou.

The Erie rule has not been easily applied in the years since

its conception. The first major refinement of the Erie rule came in Guaranty Trust Co. v. York. This case delineates the outcome-determinative test. Id. at 109. The purpose of the test is to decide whether the federal action affects the substantive outcome, or is merely "the manner and means by which a right to recover . . . is enforced." Id. In this sense, the use of inherent powers to levy attorney fees against Howard "is outcome determinative in the sense that [the losing party] owes fees he would not have owed had [state] law applied; but that is not the question after Hanna." NASCO, 894 F.2d at 705. In this sense, every variation in federal court would be outcome determinative. Hanna, 380 U.S. at 468. The outcome determinative test is not to be applied so as to require that every variation in procedure or substance be resolved in favor of state law over federal law. The court in Hanna recognized the need for federal courts to maintain certain rules of procedure and etiquette. The use of inherent powers to prevent abuses of the federal court system is a necessary function of the federal court system that cannot reasonably be stifled by state law. Thus, the Court proposed that the "outcome-determinative" test could not be read without reference to the dual purposes behind the Erie doctrine: prevention of the forum-shopping practice and avoidance of inequitable administration of the laws. Id. at 468.

A balancing test can be constructed using the test developed in Hanna. The Court should balance the policy reasons behind Erie against the interests of the federal courts in maintaining control over its administration and authority. The interest of the federal

court in administering justice and in preserving its authority outweigh the possibility that the defendant in the present case engaged in forum shopping or the possibility that the award of attorney fees would be inequitable. Withholding the authority of the federal court to sanction Howard for his bad faith litigation severely restricts the ability of the court to administer justice to all parties, while any threat to State autonomy is minuscule and evanescent. An analysis of the two-part Hanna test will show that affirmance of the Court of Appeals decision allowing attorney fees in this case will not encourage forum-shopping or result in inequitable administration of the law.

Any assertion that Bayou was forum shopping in having the case removed to federal court is purely speculative. There is no evidence that the case was removed for purposes of gaining an award of attorney's fees, which are allowed in special circumstances in federal court but are disallowed in Lewis Hall courts. Bayou is merely exercising its ability to remove the case to federal court in a diversity of citizenship case pursuant to 28 U.S.C. §1441.

There is no guarantee that a victorious party will receive attorney's fees in federal court. This undermines any contention that Bayou was forum shopping. Attorney fees are awarded only in exceptional circumstances, one of which is bad faith litigation, as is present in this case. "The standards for bad faith litigation are necessarily stringent and the fee-shifting sanction is invocable only for some dominating reason of justice." Lipsig, 663 F.2d at 180. There is no penalty for maintaining an aggressive

litigation posture and good faith claims and defenses are encouraged. Id. at 180-81. "But advocacy simply for the sake of burdening an opponent with unnecessary expenditures of time and effort clearly warrants recompense for the extra outlays." Id. at 181.

The only reason Bayou is a party to this suit is because Howard wanted to get out of his contract with Bayou. If Howard had not fraudulently manufactured documents, there would never have been a lawsuit, and Bayou would not have incurred any attorney fees. Thus, justice requires that the bad faith standard be applied in this case to compensate Bayou for Howard's meritless and baseless lawsuit. Furthermore, Howard himself would not be subject to a sanction of attorney fees but for his bad faith, vexatious conduct. Howard deserves no special lenience.

The second prong of the Hanna test looks to the inequitable administration of the laws. The only basis for the assertion this case results in inequity is a footnote in Alyeska, in which the court states, "[in] an ordinary diversity case where the state law does not run counter to a valid federal statute or rule of court . . . state law denying the right to attorney's fees or giving a right thereto, which reflects a substantial policy of the state, should be followed." Alyeska, 421 U.S. at 259, n. 31. Courts have generally adhered to the requirements of the footnote. E.g. United States v. City of Twin Falls, Idaho, 806 F.2d 862, 869 (9th Cir. 1986). (federal courts must follow state law as to attorney fees in diversity actions.), Kucel v. Walter E. Heller & Co., 813 F.2d 67,

73 (5th Cir. 1987) (the award of attorney's fees in a diversity case depends on the law of the state.) However, few of the cases that follow this footnote involve the bad faith issue that is present in this case.

Recent response to the Alyeska footnote challenges its application to limit the inherent powers of the court. The 5th Circuit, in a 1990 decision, stated, "[w]e are not persuaded that the Court intended to upset the view, nigh unchallenged in the history of the country, that federal courts have inherent power to police themselves by civil contempt, imposition of fines, the awarding of costs and the shifting of fees." NASCO, 894 F.2d at 702.

The facts of NASCO are strikingly similar to the facts of the present case. In NASCO, it was argued that the district court's award of attorneys' fees was not allowed by state law. Id. at 701. The losing party asserted that the federal court in diversity actions could not use their inherent powers to grant attorneys' fees, but had to look to state law under the Alyeska footnote. Id. It was further contended that the state law in question did not recognize an exception for bad faith practice. Id.

The Circuit Court in that case recognized that the Erie doctrine assured a litigant that the outcome in federal court would not differ from the outcome in a state court. Id. at 706. However, the court concluded that "[the Erie doctrine] does not allow him to waste the court's time and resources with cantankerous conduct." Id. The instant case was resolved on similar grounds in the Court

of Appeals. This decision should be upheld and affirmed. In such matters, the decision of the lower court should not be set aside unless the "court's findings are clearly erroneous, or that the court exceeded the bounds of its discretion." Lipsig, 663 F.2d at 181-82. An award of attorney's fees for vexatious conduct is not an abuse of discretion. Capse v. Aaacon Auto Transport, Inc., 658 F.2d 613, 618 (8th Cir. 1981).

An application of the balancing test shows that the interests of the federal court in administering justice and preserving its authority prevail over any imagined threat to the policies underlying the Erie doctrine. An award of attorney's fees will not encourage use of the federal forum to penalize the losing party for litigating, nor will such an award undermine any substantial state policy. Although there is no state statute allowing for fee-shifting, and no contractual provision, "a court may still award attorney's fees through its equitable power Exercise of this power is appropriate only in cases with exceptional circumstances. An unfounded action brought in bad faith would be such a case." State Sec. Ins. Co. v. White, 498 F. Supp. 873, 875 (S.D. Ga. 1980), aff'd 667 F.2d 97 (5th Cir. 1981?).

Howard's actions in this case are the type of unfounded, bad faith actions intended to invoke the use of the court's inherent power to shift attorney's fees. To reverse the Court of Appeals decision awarding the fees would result in an injustice to Bayou, which has been the target of a manipulative, vexatious law suit initiated by an unscrupulous businessman. As Judge Gibbons stated

in his concurrence in Montgomery Ward v. Pacific Indemnity Co., 557 F.2d 51, 61 (3d Cir. 1977): "[c]ertainly the notions of federalism which underly the Erie rule do not require that a federal forum accept the policy of the state in which it happens to sit on a matter such as the award of costs for abuse of its process." Invoking the inherent powers of the court to discourage bad faith litigation will not transgress the boundaries of the Erie rule, and will provide for a more equal administration of justice in the special cases where such powers will be applied.

CONCLUSION

For the reasons set forth above, we respectfully request this Court to affirm the rulings of the Court of Appeals and uphold the award of expenses and costs against petitioner's attorney, pursuant to 28 U.S.C. §1927 and Rule 11, and the award of attorney's fees against petitioner Howard pursuant to Rule 11 and the court's inherent powers.

Respectfully submitted,

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