Equal Access To Justice Acts: Regulatory Relief For Small Business

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A small business owner's worst nightmare may be to wake up one day and find that he is getting involved in a government enforcement action, especially when he believes that he has done nothing wrong. Small businesses live on the edge. Small businesses succeed by focusing their attention and precious financial resources on their immediate business objectives. At a minimum, agency attention means diverting the owner's focus away from making and selling a product or service. Just attending the meetings involved in an enforcement action or agency proceeding can place a serious drain on a business. When an agency takes an unreasonable position and insists on taking its case to court, the financial strain can become unbearable. Factor in attorney's fees, tests, studies, and reports and over the long haul taking on someone with infinite resources and no conception of time can drag a business to ruin.

Federal and state "Equal Access to Justice Acts" (EAJAs) may provide some relief to beleaguered business owners. In 1980, small business lobbying stimulated Congress to pass the "Equal Access to Justice Act" (EAJA) to help protect small businesses from unjustified agency action. Following the federal action, many states created their own EAJA laws.

The federal and state EAJA laws represent side skirmishes in a much larger legal debate about the pros and cons of litigation and role of the judiciary in the American legal system. Critics of the current system have proposed fee-shifting statutes, like EAJAs, to cut back high levels of litigation. Fee-shifting statutes place the burden of paying attorney’s fees and costs to the opposing party in litigation. This article examines the federal EAJA, provides a brief overview of how various states have approached these laws and then reviews how the State of Minnesota's law was applied against the lead state environmental agency in a recent environmental enforcement case.

The case under Minnesota's EAJA involved a small petroleum recycling company nearly pushed to ruin by an overly aggressive state agency action. In the end, the court vindicated the business owners and awarded them a portion of their attorney's fees.

Federal Equal Access to Justice Act

The need for EAJAs grows out of the so-called "American Rule" which means that parties to administrative or judicial proceedings pay their own way. Under the American Rule, private parties ordinarily cannot recover attorney fees when they prevail in an administrative or judicial proceeding.

Many European countries and the British Commonwealth follow the English Rule. Under the English Rule, the loser in a legal dispute pays the winner's attorney's fees as well as their own. Supporters of the English Rule believe that the fear of losing and having to pay the other side's attorney's fees cuts down on nuisance lawsuits. It also opens the courts to people with valid claims who would otherwise be deterred by the fear of high attorney's fees.

1980 EAJA

Federal and state EAJAs only apply to cases involving government agency administrative or judicial actions. They generally restrict the eligible entity or individual based on size, set criteria for the recovery of awards and place certain restrictions on the amount of the claim. These laws grew out of the climate of deregulation that was prevalent during the early 1980s.

Driven by small business interests, Congress passed the federal EAJA in 1980 to help small businesses defend themselves against unreasonable government regulation. The 1980 Act allowed "prevailing parties" to recover some of their fees and other expenses in actions brought by and against federal agencies. The EAJA partially waives the federal government's sovereign immunity by allowing the recovery of fees if a party meets certain statutory criteria. The EAJA and most of the state equivalents do not permit recovery of attorney's fees and costs in cases involving torts or personal injuries. The 1980 Act provides a means of recovery in both administrative and judicial proceedings.

The federal EAJA limits recoveries to eligible parties who meet the following criteria:

1. Individuals whose net worth was $2 million or less at the time proceedings were initiated;

2. Owners of unincorporated businesses or partnerships, corporations, associations, units of local government, or organizations with a net worth of $7 million or less and not more than 500 employees;

3. Tax exempt organizations; and

4. Agricultural cooperatives.

General Accounting Office figures show that from 1982 through 1994 under the 1980 EAJA, aggrieved parties sought recovery from federal government agencies in administrative matters on average of 133 occasions per year. Approximately 40 percent of these succeeded, averaging $7,500 per claim. Judicial proceedings saw much higher levels of activity over the same period -- averaging over 560 claims per year. About 83 percent of claimants succeeded in receiving fee awards, resulting in an average settlement of $5,200. The total fees recovered topped $33 million, with $4.2 million going to administrative applicants and $29.2 million awarded to judicial claimants.

1996 Amendments

By 1996 EAJA supporters expressed growing concerns about the Act's effectiveness. While $33 million represents a fair sum of money in recovered fees, stretched over a 12-year period and compared with the total amount of federal government regulatory activity affecting small businesses, its size is actually not that impressive. The Act's original supporters had expected claims to annually exceed the 12-year figure. Small business supporters believed the Congress had set the standards used to show government unreasonableness too high. They charged that government agencies had adopted a scatter gun approach throwing 10 to 100 or more claims against the wall to see, what would stick. If the agency could prevail in even 1 minor claim, the company would not be the prevailing party and could not recover fees. They also believed that Congress had set the hourly rate for recoverable fees at too low of a level.

Congress amended the EAJA in the Contract with America Act of 1996 Subtitle C. These amendments strengthened the EAJA in three important ways:

1. added "excessive demand" to the "prevailing party" avenue for recovering fees;

2. increased the level of eligible fees, and

3. expanded the number of parties eligible to recover fees.

By adding the "excessive demand" avenue for recovering fees to the EAJA, Congress intended to compensate a party for those fees and expenses, which it would not have incurred, but for the government's excessive demand. Under the "excessive demand" provision, an Agency alleging multiple offenses against a small business could still be liable for a portion of the business' attorney's fees if too great a disparity exists between the agency's initial claim and final settlement. For example, an agency alleges multiple violations with fines exceeding $100,000. Administrative or judicial review finds in favor of the agency on only a handful of minor charges with fines less than $5,000. Under this scenario, the small business owner could file an EAJA claim for the portion of fees relating to the defense of the excessive demand even though the court or administrative law judge may not ultimately determine the business to be the prevailing party.

The 1996 EAJA amendments raised the cap on attorney's fees from $75 to $125 for the successful claimant. The Act does permit recovery of fees at a higher hourly rate when a party can show that some level of specialized expertise is required to defend the government's legal or administrative action. They also expanded the class of litigants eligible to recover fees by adding "small entities" to the list of eligible claimants. Small entities are essentially the same as the government's definition of small business. The 1996 amendments also apply to civil actions and adversary adjudications.

Although the 1996 amendments have made it easier for small businesses to collect attorney's fees, even when they prevail or can 'show' that fees were incurred as a result of an excessive demand, they do not always get their fees reimbursed. In a recent FAA case, an administrator ruled that even though the claimant prevailed, the Agency was substantially justified and had acted properly.

The United States Supreme Court has held that the government's position is "substantially justified" if it is "justified to a degree that could satisfy a reasonable person and . . . if it has a reasonable basis in law and fact." *Pierce v. Underwood*, 487 U.S. 552, 565-66 n. 2 (1988). Courts reviewing EAJA fee applications must apply their discretion in reviewing the threshold issue relating to the "substantially justified" determination. The inability to satisfy this requirement, which is the subject of judicial interpretation, has barred many prospective EAJA applicants from obtaining the relief they have sought.

Other States

Since 1980, over 30 states have enacted EAJAs patterned after the federal act. Unlike many statutory remedies, there is no uniform law covering recoveries against state government agencies. Instead, the states, which are often termed the laboratories for democracy, have crafted a variety of remedies for parties who face unreasonable or unwarranted governmental action.

Like the federal Act, state EAJAs only apply to litigation with the government they do not apply to litigation between private parties. In an interesting twist from the Act's original intention, three states -- Hawaii, Tennessee and Wisconsin -- allow the state to collect from private parties. About a third of the states with EAJAs only cover business (excluding small cities, individuals and associations). Some states restrict eligible parties to businesses registered in that state. A few states have broadened the scope of their laws to permit recoveries against local units of government.

Like the federal Act, nearly two-thirds of states with EAJAs place limits on the size of the business and the wealth of the individual that can place a claim. Most of the states that have enacted EAJA laws seek to protect the interests of small businesses. Eleven states go further and grant to protections to individuals who meet certain criteria. In New York, an individual with less than $50,000 net worth may recover. Missouri is more generous, granting a remedy to individuals whose net worth is up to $2 million.

All state EAJAs apply to administrative hearings. Several states exempt specific administrative hearings such as rate-fixing or certain types of licensing proceedings. Many states limit the size of recovery. For example, ten states limit the recovery to $7,500. Six others limit total recoveries to $10,000.

Perhaps the most difficult hurdle for a party seeking to recover fees from the government to overcome is the standard that one is required to meet. Most states have a variation or reiteration of the "substantially justified" term that appears in the federal EAJA. To meet this standard, a party must demonstrate that the government had no reasonable basis in either law or fact to assert the claim. In two states, Montana and Texas, a party seeking to recover must go further and meet the more difficult standard that the government's position was taken in bad faith, groundless or frivolous. Because of the variations in state laws, businesses facing an unreasonable demand must carefully examine the law in their state. State EAJAs may set a very high standard to recover an award of fees and costs.

Minnesota

A recent Minnesota case illustrates how state EAJA laws can benefit a regulated party. In addition to farming near rural Osakis, Minnesota, Roland Walsh owned and operated Rollies Sales & Service (Rollies), a small petroleum services company with his son Dale. The company services included the salvaging tanks and recycling the recovered petroleum.

In June 1992, the Minnesota Pollution Control Agency (MPCA) inspected Rollies for the first time. After the MPCA inspection, the MPCA alleged the company had nine hazardous waste violations. In response to the state action, Rollies quit this part of their business.

Following a growing trend, the State not only charged the company but also named and sought to collect civil penalties from the President, Dale Walsh and a former shareholder in the company, Roland Walsh. The State named the individuals under the "responsible corporate officer" doctrine, which has found its way into various environmental laws and in court decisions.

The MPCA initially sought a $59,000 penalty from Rollies and both individuals in an administrative settlement. Rollies and the individuals found the State's penalty demand to be unreasonable and declined to pay.

In 1995, after negotiations broke down, the State of Minnesota filed a complaint in Douglas County District Court. The State alleged that Rollies, Dale Walsh, and Roland Walsh, had

each violated state environmental laws. The State's complaint asked the court to impose penalties of $25,000 per day per violation or over $250,000 on the defendants. The State also sought an unspecified amount of attorney's fees from each of the defendants.

The State pursued the case vigorously engaging in lengthy discovery. The State deposed several former employees and brought various pre-trial motions before the court. As the case dragged on, the cost of defending the State's action grew exponentially.

The State maintained that Rollies was operating a hazardous waste facility without a permit and that releases from the tanks had caused contamination. The defendants hired a consultant to investigate whether soils at the site had actually been impacted by alleged releases. After the tests showed no measurable impact, the State acknowledged that no further investigative or cleanup work would be required. Despite these findings, the State held fast to its demand that the defendants, specifically the two individuals, pay the penalty as well as the State's mounting attorney's fees. Minnesota has a law that provides that the State can collect its fees from a defendant in an environmental case where it can show that the violations were "willful."

In response to the State's 1995 lawsuit, Rollies and the individual defendants sought an award of attorney's fees under the Minnesota Equal Access to Justice Act (MEAJA). The Minnesota Legislature enacted MEAJA in 1986 to allow eligible small businesses and their owners to seek an award of fees and costs in cases where they prevail against the State. Parties eligible for a MEAJA award include businesses and partnerships with fewer than 50 employees and annual revenues of less than $4,000,000 at the time when the civil action was commenced. At the time the complaint was filed Rollies had 29 employees and met the revenue criteria. Under MEAJA, officers and shareholders of eligible companies, such as the Walshes, are eligible to seek an award.

Court Findings

Although the Minnesota District Court found that Rollies had violated several state environmental regulations, the court viewed these violations as "minor." The court determined that the vast majority of the petroleum-related material that Rollies handled was "product" and not "waste" that was subject to regulation. Judge Paul Ballard applied what he termed a "velvet hammer," imposing a $3,400 penalty on Rollies for management violations. Most importantly, the court found that neither Dale nor Roland Walsh had committed any of the violations. Judge Ballard concluded that it is in the State's best interests to encourage the recycling efforts of petroleum tank salvagers such as the Rollies operation. The court noted that:

> "There was limited potential to harm the environment from these violations and no actual harm to the environment occurred as a result of these violations. There were no prior violations by Rollies and its non-compliance was of short duration. Rollies invested $500,000 into its petroleum recycling operations branch of its business, which Rollies abandoned as a result of this action by the State."

MEAJA entitles small businesses, their owners and officers to an award of attorney's fees when they can convince the court that the State's case against them was "substantially unjustified." Under Minnesota law, the term "substantially justified" is defined to mean that the State's position had a reasonable basis in law and fact, based on the totality of the circumstances both before and during the litigation. Minn. Stat § 15.471, subd. 8 (1998).

Judge Ballard concluded that an award was appropriate because "the State's position against both Dale and Roland Walsh did not have a reasonable basis in law and fact before and during the litigation." Specifically, the State had failed to prove that Roland and Dale Walsh were personally liable for any of the alleged violations. The court found that rather than naming Dale and Roland Walsh as defendants, the State should have directed its attention and considerable litigating resources to another individual, the person charged with overseeing the company's environmental compliance.

In a December 30, 1998 order Judge Ballard awarded Dale and Roland Walsh each, $31,469.16 in attorney's fees. The court also awarded Rollies $3,041.85 for expenses it incurred defending the individuals in a lawsuit brought by the State. The court ordered the MPCA and the Attorney General's Office to pay the fees and expenses directly to the individuals and to Rollies. The State decided not to appeal the case. The $66,000 award is the largest award ever made under MEAJA. Given the range of awards that have been reported and the caps on attorney's fees that appear in various state's EAJA laws, this award may well be one of the largest granted against a state environmental agency.

Minnesota Amendments

Following the successful attempt to recover Rollies's attorney's fees, their counsel, Joe Maternowski, a shareholder at Moss & Barnett, helped to prepare amendments to the MEAJA allowing small businesses to recover expenses. The National Federation of Independent Business, a proponent of Minnesota's existing law as well as the changes in the federal EAJA, actively supported the effort to strengthen Minnesota's law.

The amendments, which Governor Jesse Ventura signed in April 2000, allow the prevailing party to recover the reasonable costs of any study, analysis, engineering report, test, or project that the party has done in response to the state's action. The existing MEAJA law limited the amount of attorney's fees to $100 per hour. The amendments permit recovery of attorney's fees up to $125 an hour. The Minnesota amendments significantly expand coverage to small businesses with up to 500 employees and annual revenues not exceeding $7 million. Previously the law covered businesses with up to 50 employees and annual revenues less than $4 million.

The amendments won bipartisan support in both the Minnesota House of Representatives and Senate. The Minnesota Legislature reaffirmed its commitment to supporting the rights of small businesses and others who face unwarranted government action.

Conclusion

While the EAJA laws enacted on the state and federal level may not level the playing field, they should cause agency management to pay very close attention to staff actions against small businesses and other individuals who may find themselves facing an enforcement action. Although no business who is subject to regulation relishes a confrontation in court with governmental authorities, the EAJA laws and the potential for fee shifting should work to discourage government from pursuing cases and positions that are without merit.

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