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February 4, 1997

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TO: Chair, and Members
Council on Court Procedures

Re: ORCP 68--Findings of Fact and Conclusions of Law

Dear Chair and Members:

For the Council's information, enclosed is a copy of Conley v. KCA Financial Services, Inc., which deals with findings of fact and conclusions of law in support of ORCP 17.

Very truly yours,

LANE POWELL SPEARS LUBERSKY LLP

Bruce C. Hamlin

BCH:cjc
Enclosure

PORTLAND:17995 v01

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FILED: January 22, 1997

IN THE COURT OF APPEALS OF THE STATE OF OREGON

B. HARRISON CONLEY,

Appellant,

v.

KCA FINANCIAL SERVICES, INC., INDIANA NATIONAL BANK and FIRST INTERSTATE BANK OF OREGON,

Respondents.

(95C-11618; CA A92185)

Appeal from Circuit Court, Marion County.

Charles P. Littlehales, Judge.

Argued and submitted December 23, 1996.

B. Harrison Conley argued the cause and filed the briefs *pro se*.

John W. Weil argued the cause for respondent KCA Financial Services, Inc. Thomas K. Wolf argued the cause for respondent Indiana National Bank. With them on the brief were Hooper, Englund & Weil and Weinstein, Fischer, Riley, Erickson & Wolf, P.S.

Mark B. Comstock argued the cause for respondent First Interstate Bank of Oregon. With him on the brief was Garrett, Hemann, Robertson, Paulus, Jennings & Comstock, P.C.

Before Riggs, Presiding Judge, and Landau and Leeson, Judges.

LANDAU, J.

Award of attorney fees to defendants reversed and remanded for reconsideration; otherwise affirmed.

DESIGNATION OF PREVAILING PARTY AND AWARD OF COSTS

Prevailing party: Appellant

[ ] No costs allowed.
[X] Costs allowed, payable by: Respondents
[ ] Costs allowed, to abide the outcome on remand, payable by:

LANDAU, J.

Plaintiff initiated this action for unlawful debt collection and claims related to attempts to collect on a debt he had accumulated on a consumer credit account. The trial court dismissed all claims pursuant to ORCP 21. It also ordered plaintiff to pay attorney fees to defendant Indiana National Bank, now known as NBD Bank, N.A. (NBD), and its agent, KCA Financial Services, Inc. (KCA), based on an attorney fee provision in its consumer credit agreement, and it ordered plaintiff to pay attorney fees to defendant First Interstate Bank of Oregon (First Interstate) as a sanction pursuant to ORCP 17. We affirm without discussion the dismissal of plaintiff's claims and reverse and remand for reconsideration the awards of attorney fees to NBD, KCA and First Interstate for the reasons that follow.

We first address the award of attorney fees to NBD and KCA. Plaintiff opened a consumer credit account with defendant NBD. The consumer credit agreement between NBD and plaintiff provides:

> "**Collection Costs.** If we start a collection action, you agree to pay all court costs and collection fees allowed by law, including reasonable attorney's fees."

When plaintiff did not pay on his credit account, NBD engaged KCA to collect the debt. KCA initially demanded that plaintiff pay $1,106.08 but later offered to accept $750 as payment in full. Plaintiff sent a check for $320 with a note written on its face: "Accord Offered in Satisfaction of NBD Card Services Acct." KCA struck out the note on the face of the check and cashed it. When KCA continued to attempt to collect on the account, plaintiff initiated this action, contending, among other things, that the debt had been extinguished by an agreement of

accord and satisfaction.

NBD and KCA did not answer. Instead, they moved for an order of dismissal under ORCP 21 A(8). The trial court granted the motion and dismissed plaintiff's claims against them. NBD and KCA then moved for an order awarding them their attorney fees under the terms of the consumer credit agreement and under ORS 646.641(2) and 15 USC § 1692k. The trial court awarded NBD and KCA their attorney fees, although it did not specify on what basis it did so and made no findings.

On appeal, plaintiff argues that the trial court erred in awarding fees to NBD and KCA. According to plaintiff, the consumer credit agreement affords no basis for an award of attorney fees, because it applies only to a collection action initiated by NBD or KCA. As for the statutory bases for an award of fees, plaintiff contends that both ORS 646.641(2) and 15 USC § 1692k apply only upon a finding that plaintiff filed a frivolous action, and, plaintiff notes, the trial court made no such finding in this case. NBD and KCA argue that, although the consumer credit agreement, by its terms, applies only in the event of an action for collection, we should award fees in this case because they could have counterclaimed for collection of the underlying debt but did not need to do so because they obtained a dismissal of plaintiff's claims, which were, at least indirectly, precipitated by their attempt to collect on the debt. With respect to the statutory attorney fees provisions, NBD and KCA concede that a finding that plaintiff filed a frivolous claim is necessary; nevertheless, they contend that, when the trial court dismissed plaintiff's claims, it commented that plaintiff had no basis in law or in fact to assert them, and

that, under this court's holding in *Morrical v. Zenon*, 140 Or App 444, 914 P2d 1143, *rev den* 323 Or 483 (1996), that comment satisfies the requirement of a finding of a frivolous filing.

We agree with plaintiff that the trial court erred in awarding attorney fees to NBD and KCA. First, the consumer credit agreement does not apply. It plainly states that defendants are entitled to fees only "[i]f we start a collection action." Both NBD and KCA concede that they did not start a collection action. The fact that they *could have* started a collection is immaterial. The agreement does not create a right to attorney fees in the event that they could have theoretically initiated a collection action.

Second, the statutes on which NBD and KCA rely do not apply either. The version of ORS 646.641(2) that applies to this case provides for an award of attorney fees only "if [the court] finds the action to be frivolous."[1] Similarly, 15 USC § 1692k applies only "[o]n a finding by the court that the action * * * was brought in bad faith and for the purpose of harassment * * *." In this case, the court made no finding as to the basis for its award of attorney fees. The trial court's comment that plaintiff's complaint did not state a claim is not sufficient, and our decision in *Morrical* is not to the contrary. In that case, the petitioner argued that the trial court had awarded attorney fees under ORCP 17 without making the findings required by

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[1] In 1995, the legislature amended ORS 646.641(2), effective September 9, 1995, to read:

> "In any action brought by a person under this section, the court may award reasonable attorney fees to the prevailing party."

Or Laws 1995, ch 618, § 99.

the rule. We held that the award was appropriate, because the trial court had found that

> "petitioner's claims had no basis in fact and not 'one scintilla' of proof, and that petitioner was not credible. Its formal findings included that the majority of petitioner's claims were not founded in fact or law, were not made in good faith, and were made in bad faith."

Morrical, 140 Or App at 445. The trial court made no such findings in this case.

We next address plaintiff's contention that the trial court erred in awarding attorney fees to First Interstate. Plaintiff alleged that First Interstate is liable for honoring his check after KCA had stricken out the accord and satisfaction notation that he had written on the face of the check. The trial court dismissed the claims against First Interstate, and plaintiff moved for reconsideration. First Interstate opposed the motion for reconsideration and moved for sanctions. It cited ORCP 17,[2] although it did not specify which portion of that rule supported the imposition of the sanctions it requested. The trial court denied the motion for reconsideration and granted the motion for sanctions, awarding First Interstate attorney fees and costs. The trial court made no findings, commenting only that it based its decision on the request set forth in First Interstate's motion. The order awarding attorney fees, likewise, contains no findings.

On appeal, plaintiff contends that the trial court failed to make findings that are a prerequisite to an award of fees and costs under ORCP 17. First Interstate responds that the comments that the trial court made during argument on the motion for sanctions provide a basis

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[2] In 1995, the legislature also amended ORCP 17, Or Laws 1995, ch 618, § 4, and made the amended rule effective to all actions whether commenced before or after the effective date of the act. Or Laws 1995, ch 618, § 140(2). First Interstate's request for sanctions was filed December 22, 1995, and, therefore, subject to the amended rule.

for concluding that "the court implicitly applied the proper analysis." We agree with plaintiff.

ORCP 17 C provides:

> "(1) An attorney or party who signs, files or otherwise submits an argument in support of a pleading, motion or other paper makes the certifications to the court identified in subsections (2) to (5) of this section, and further certifies that the certifications are based on the person's reasonable knowledge, information and belief, formed after the making of such inquiry as is reasonable under the circumstances.
>
> "(2) A party or attorney certifies that the pleading, motion or other paper is not being presented for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation.
>
> "(3) An attorney certifies that the claims, defenses, and other legal positions taken in the pleading, motion or other paper are warranted by existing law or by a nonfrivolous argument for the extension, modification or reversal of existing law or the establishment of new law.
>
> "(4) A party or attorney certifies that the allegations and other factual assertions in the pleading, motion or other paper are supported by evidence. Any allegation or other factual assertion that the party or attorney does not wish to certify to be supported by evidence must be specifically identified. The attorney or party certifies that the attorney or party reasonably believes that an allegation or other factual assertion so identified will be supported by evidence after further investigation and discovery.
>
> "(5) The party or attorney certifies that any denials of factual assertion are supported by evidence. Any denial of factual assertion that the party or attorney does not wish to certify to be supported by evidence must be specifically identified. The attorney or party certifies that the attorney or party believes that a denial of a factual assertion so identified is reasonably based on a lack of information or belief."

ORCP 17 D further provides, in relevant part:

> "(1) The court may impose sanctions against a person or party who is found to have made a false certification under section C of this rule, or who is found to be responsible for a false certification under section C of this rule."

ORCP 17 D then concludes with the following requirement:

> "(5) An order imposing sanctions under this section must specifically describe the false certification and the grounds for determining that the certification was false. The order must explain the grounds for the imposition of the specific sanction that is ordered."

In this case, the trial court's order imposing sanctions contained none of the findings required by ORCP 17 D(5). That the court commented at the hearing on the motion for sanctions that it based its decision on First Interstate's motion is insufficient. ORCP 17 D(5) requires that the court make findings *in the order imposing sanctions*, and that those findings include "the grounds for determining that the certification [required under ORCP 17 C] was false" and "the grounds for the imposition of the specific sanction that is ordered." The trial court's order in this case contained no such findings.

Award of attorney fees to defendants reversed and remanded for reconsideration; otherwise affirmed.

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July 12, 1996

MEMO TO: COUNCIL ON COURT PROCEDURES

FROM: ORCP 17 COMMITTEE

RE: SANCTIONS

This committee initially undertook to review ORCP 54(E) and 17. We previously concluded that 54(E) properly reflected the legislative intent and turned our attention to ORCP 17. Particularly, we have focused on ORCP 17(D)(4) which allows sanctions which "...may include monetary penalties payable to the court."

One of the specific questions was whether there should be some higher burden of proof to impose such a "penalty", as opposed to the showing necessary to impose other sanctions, such as attorney's fees payable to a party opposing a motion.

ORCP 17 was modeled after FRCP 11, and we thought that the Federal authorities might shed some light on the nature of the proof required for the assessment of a monetary penalty.

Unfortunately, the Federal cases are not of much assistance. The addition of a provision for penalties was added by a 1993 amendment to the Federal rules. The committee notes to such amendment discuss in some detail the fact that the test for imposition of sanctions is an objective one, thus eliminating any "empty-head pure-heart" justification for patently frivolous arguments. However, the history of the rule does not really address any higher burden of proof for the imposition of monetary sanctions on an attorney or a party.

The committee notes to the rule do point out a number of factors to be considered in determining whether to impose a sanction, and the amount of such sanction. The following is a non-exclusive list:

> **Whether the improper conduct was wilful, or negligent; whether it was part of a pattern of activity, or an isolated event; whether it infected the entire pleading, or only one particular count or defense; whether the person has engaged in similar conduct in other**

> **litigation; whether it was intended to injure; what effect it had on the litigation process in time or expense; whether the responsible person is trained in the law; what amount, given the financial resources of the responsible person, is needed to deter that person from repetition in the same case; what amount is needed to deter similar activity by other litigants: all of these may in a particular case be proper considerations. The court has significant discretion in determining what sanctions, if any, should be imposed for a violation, subject to the principle that the sanctions should ont be more severe than reasonably necessary to deter repetition of the conduct by the offending person or comparable conduct by similarly situated persons.**

The notes go on to point out that Rule 7 sanctions are principally to deter rather than to compensate, and feel that any monetary sanction should ordinarily be paid into court as a penalty, unless it would be appropriate to reimburse the opposing party for the costs associated with the defense of a frivolous claim.

Moore's Federal Practice Treatise also discusses sanctions under Rule 11. The only portion which seemed relevant to the issue before the subcommittee is found at pages 11-70 - 11-70.1:

> **"When the sanction to be imposed includes a fine, instead of simple reimbursement for the opposing party's costs and attorney's fees, the sanctioned individuals may be entitled to the protections of Fed.R.Crim.P.42(b), since a fine imposed under Rule 11 is analogous to one imposed for criminal contempt."**

Therefore, there is little guidance that we have found in terms of Federal authorities interpreting the penalty provisions of FRCP 11. It perhaps might be helpful to discuss with the Council at large whether it would nevertheless be appropriate, and within our statutory authority, to propose substantive requirements for the imposition of the penalties now included within the scope of ORCP 17.

In discussing sanctions, there is another matter which the Council may want to address in general. This is beyond the direct scope of the our duties, but has been brought to the attention of this committee. It involves sanctions as they relate to the exclusions in the Professional Liability Fund's policy of insurance.

Exclusion 3(d) to our plan reads as follows:

"This plan does not apply to that part of any claim: 1) asserted directly against a covered party for punitive or exemplary damages, fines, sanctions, or penalties, or 2) asserted directly or indirectly against the covered party, arising out of the imposition on the covered party or others of any attorney's fees, costs, fines, penalties, sanctions, or other amounts imposed under any Federal or State statute, administrative rule, court rule, or case law intended to penalize bad faith conduct and/or the assertion of frivolous or bad faith claims or defenses."

To my knowledge, this exclusion has been present in the PLF policy for some period of time. It certainly predated the recent changes to Rule 17. It probably also predated our own Supreme Court's opinion in the case of Seeley v. Hanson, 317 Or 476, 857 P2d 121 (1993).

The Seeley case, and FRCP 11, clearly point out that sanctions may be imposed due to an "improper purpose", but this is an alternative justification. An objective lack of merit in a claim will also give rise to a potential sanction.

Therefore, an attorney and/or his client may be subject to sanctions for conduct which is neither wilful nor taken in bad faith, but is instead only negligent, or perhaps grossly negligent. Even though there is no deliberate wrongdoing, this sanction is not going to be covered. In other words, the attorney is not protected against innocent wrongdoing. This seems contrary to the purpose for which we purchase insurance.

These sanctions can also create a significant conflict of interest, since they can be imposed against a party or an attorney. There are circumstances where sanctions might be appropriate against an attorney for pursuing a non-meritorious claim, or there may be situations where a sanction may be more appropriately imposed against a party who has supplied inaccurate or false information to an attorney, who relied upon some information in pursuing a claim which then turns out to be without merit. At any rate, when a sanction is imposed against either an attorney or the party, there is an immediate potential for conflict concerning who should bear the sanction. This conflict in and of itself is difficult enough, but it creates even more problems when there is no insurance to potentially cover such loss.

Obviously, neither attorneys nor their clients should be insured for deliberate wrongdoing or other intentional misconduct. However, it might be prudent for the PLF to re-examine its exclusion in light of the development of the current rules and case

law concerning the mental element necessary for sanctions to be imposed. A suggestion from the Council, or another Bar group, might trigger such an inquiry.

JMA/jb