

# Restoring the Benefit of the Bargain

## North Carolina Permits Limited Attorneys' Fees Recovery in Business Contracts

*By Stephen F. Later*

The common law of North Carolina provides that awards of attorneys' fees by litigants are, notwithstanding any contractual provision, limited to recoveries that are specifically authorized by statute. Our Supreme Court observed that "[e]ven in the face of a carefully drafted contractual provision indemnifying a party for such attorneys' fees as may be necessitated by a successful action on the contract itself, our courts have consistently refused to sustain such an award absent statutory authority therefor."<sup>1</sup>

The traditional rationale for this rule, the application of which has not necessarily been consistent with its intention, was public policy that sought to protect parties with less bargaining power or a lower level of sophistication.<sup>2</sup> There is, for example, a longstanding statutory exception that validates contractual provisions for reimbursement of attorneys' fees of the prevailing party in agreements that qualify as a promissory note, conditional sale contract or other "evidence of indebtedness."<sup>3</sup> However, N.C.G.S. § 6-21.6 became effective October 1, 2011, and it provides that "[r]eciprocal attorneys' fees provisions in business contracts are valid and enforceable for the recovery of reasonable attorneys' fees and expenses only if all of the parties to the business contract sign by hand the business contract."<sup>4</sup>

The enactment of N.C.G.S. § 6-21.6 in June 2011 stemmed from the efforts of the Subcommittee on Proposed Legislation to Validate Enforcement Expense Provisions in Business Contracts (the "Committee") of the Business Law Section of the North Carolina Bar Association. Its 2007 report outlined a proposed revision to the North Carolina General Statutes to validate the enforceability of contractual provisions in business contracts that would obligate a party to reimburse the other party for the legal costs incurred by the other party in enforcing the terms of the business contract. The Committee reported that the prevailing view in the business community was that, even if the injured party prevails in litigation, the injured party will not be made whole if unable to tax the breaching party with attorneys' fees as possible in most other states.<sup>5</sup>

### ***Business Contracts***

The statute defines a business contract, and thus the scope of the statute, as "a contract entered into primarily for business or commercial purposes"<sup>6</sup> and clarifies that consumer contracts,<sup>7</sup> employment contracts,<sup>8</sup> and contracts "to which a government or a governmental agency of this State is a party"<sup>9</sup> are excluded from the scope of the statute. The intention of the Committee, the NCBA, and, of course, the sponsors of the legislation was to limit the applicability of the statute to sophisticated commercial parties.

Although limited to business contracts, N.C.G.S. § 6-21.6 will not trump attorneys' fees provisions otherwise applicable to consumer

contracts, employment contracts, and contracts that involve governmental units "[i]f the business contract is also a note, conditional sale contract, or other evidence of indebtedness that is otherwise governed by G.S. 6-21.2."<sup>10</sup>

### ***Reciprocal Provisions.***

N.C.G.S. § 6-21.6 defines "reciprocal attorneys' fees provisions" as "[p]rovisions in any written business contract by which each party to the contract agrees..., upon the terms and subject to the conditions set forth in the contract that are made *applicable to all parties*, to pay or reimburse the other parties for attorneys' fees and expenses incurred by reason of any suit, action, proceeding, or arbitration involving the business contract."<sup>11</sup>

The common law of North Carolina precludes enforcement of contractual attorneys' fees provisions, and, therefore, it is likely that unambiguous compliance with this provision is required to ensure enforcement, and any attempt to include terms and conditions that are not equally applicable to all parties is likely to be fatal to enforcement of a provision that is otherwise within the scope of N.C.G.S. § 6-21.6. It is thus unlikely that an attorneys' fees provisions that is deemed to be materially reciprocal or substantially reciprocal will be enforceable.

Further, as indemnification provisions in business contracts are rarely identical and often set forth in discrete paragraphs or subparagraphs of the contract, an attorneys' fees provision included as a component thereof may not be deemed to be reciprocal due to differences in the liabilities that trigger the indemnification obligations. The prudent practitioner may thus choose to insert the reciprocal attorneys' fees provision, in a form equally applicable to all parties, in a distinct section of the business contract.

### ***Recovered Amounts***

N.C.G.S. § 6-21.2, which sanctions the recovery of attorneys' fees in the enforcement of evidences of indebtedness, is a mandatory statute that compels the award of attorneys' fees in, generally, a fixed amount. However, N.C.G.S. § 6-21.6 is a permissive statute, which invests the court with substantial latitude in whether to award a fee, how much to award as a fee, and which factors to consider in determination of how much to award as a fee.<sup>12</sup>

The statute specifically provides that, in its determination of "reasonable attorneys' fees" for purposes of an award, the court "may consider all relevant facts and circumstances, including, but not limited to" (a) "[t]he amount in controversy and the results obtained," (b) "[t]

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he reasonableness of the time and labor expended, and the billing rates charged, by the attorneys,” (c) “[t]he novelty and difficulty of the questions raised in the action,” (d) “[t]he skill required to perform properly the legal services rendered,” (e) “[t]he relative economic circumstances of the parties,” (f) “[s]ettlement offers made prior to the institution of the action,” (g) “[o]ffers of judgment pursuant to Rule 68 of the North Carolina Rules of Civil Procedure and whether judgment finally obtained was more favorable than such offers,” (h) “[w]hether a party unjustly exercised superior economic bargaining power in the conduct of the action,” (i) “[t]he timing of settlement offers,” (j) “[t]he amounts of settlement offers as compared to the verdict,” (k) “[t]he extent to which the party seeking attorneys’ fees prevailed in the action,” (l) “[t]he amount of attorneys’ fees awarded in similar cases,” and (m) “[t]he terms of the business contract.”<sup>13</sup> The factors emphasize efforts of the parties to conserve litigation and judicial resources, and, indeed, these factors attach substantial importance to the conduct of the parties after the disintegration of their business relationship.

The statute further provides that “[r]easonable attorneys’ fees and expenses shall not be governed by (i) any statutory presumption or provision in the business contract providing for a stated percentage of the amount of such attorneys’ fees [e.g., the 15 percent presumption of N.C.G.S. § 6-21.2] or (ii) the amount recovered in other cases in which the business contract contains reciprocal attorneys’ fees provisions.<sup>14</sup> Although the statute states that the fee award shall not be “governed” by “the amount recovered in other cases in which the business contract contains reciprocal attorneys’ fees provisions,” the “[t]he amount of attorneys’ fees awarded in similar cases” is a factor to be considered by the court, so, although not dispositive, it is indeed relevant. “The allowance of attorney fees is in the discretion of the presiding judge,”<sup>15</sup> and, yet, the discretion of the court “is not unbridled.”<sup>16</sup> The court is obligated “to consider the entire record in properly exercising its discretion”<sup>17</sup> and to address all relevant factors under applicable statute and case law.

Further, despite the discretion of the court related to the fee award, the statute caps attorneys’ fees awards in actions “primarily for the recovery of monetary damages.” It does so, however, in two inconsistent provisions. G.S. § 6-21.6(b) provides that “the award of reasonable attorneys’ fees may not exceed the monetary damages awarded,” and, yet, G.S. § 6-21.6(f) provides that, “the award of reasonable attorneys’ fees may not exceed the amount in controversy.” The conflict resulted from an amendment filed during committee consideration of the bill that added the “amount in controversy” cap and the “monetary damages awarded” cap, and, although the conflict may be resolved through subsequent legislative action, the “monetary damages awarded” cap was passed six days after the “amount in controversy” cap. However it is possible to interpret the statute to impose the lesser of the two figures as the effective cap in a manner consistent with the view of our Supreme Court that “[a] statute should not be interpreted in a manner which would render any of its words superfluous. We construe each word of a statute to have meaning, where reasonable and consistent with the entire statute, because it is always presumed that the legislature acted with care and deliberation.”<sup>18</sup>

The cap applies to actions “primarily for the recovery of monetary

damages.” It is thus possible that inclusion of claims for non-monetary damages, in a manner sufficient to overcome characterization of the action as one “primarily” for recovery of monetary damages, may result in an award that excludes the cap but nonetheless remains subject to judicial determination of reasonableness.

### ***“Sign by Hand” Requirement***

The prerequisites for enforcement require that “all of the parties to the business contract sign by hand the business contract.”<sup>19</sup> This provision was inserted by the principal Senate sponsor of the legislation in response to requests to avoid its application to “click wrap” and similar agreements. The understanding of the author is that the amendment was not intended, and should not be construed, to preclude application of the statute to agreements executed by manual signatures that are thereafter transmitted and delivered by .pdf or other electronic reproductive image thereof. The statute further requires “all parties” to the contract, rather than the party against which enforcement is sought, to “sign by hand” so it is essential<sup>20</sup> that all parties indeed so execute the agreement.

### ***Scope of Contractual Flexibility***

As attorneys’ fees provisions are limited to those with a statutory basis,<sup>21</sup> rather than a contractual basis, it appears likely that strict compliance with the terms of N.C.G.S. § 6-21.6 is required and any contractual agreement outside the scope of the statute is likely unenforceable. It further appears likely that any effort to opt in to the statute under circumstances that are not in strict compliance therewith will be deemed to be unenforceable as it seeks, in effect, to create a contractual right that conflicts with applicable state law.

N.C.G.S. § 6-21.6 is not an attorneys’ fees recovery statute. It is, rather, enabling legislation that permits enforcement of contractual “[r]eciprocal attorneys’ fees provisions” and thus entitles the parties to the business contract to draft attorneys’ fees provisions suited to the particular circumstances. There is tension, however, between the broad discretion afforded to the court and the rights of the parties to incorporate contractual provisions including, for example, baskets, caps, and triggers in the provision.

The statute provides that, “[i]f a business contract governed by the laws of this State contains a reciprocal attorneys’ fees provision, the court... may award reasonable attorneys’ fees *in accordance with the terms of the business contract*”<sup>22</sup> and thus implies that the contractual provision establishes the boundaries of the fee award. However, as the statute further provides that, “[i]n determining reasonable attorneys’ fees and expenses... the court... may consider all relevant facts and circumstances” including the 13 enumerated factors<sup>23</sup> as well as factors that are not set forth in the reciprocal attorneys’ fees provision.

### ***N.C.G.S. § 6-21.2***

It is likely that some agreements will be subject to N.C.G.S. § 6-21.2 as well as N.C.G.S. § 6-21.6 and, in this event, the enforcing party is entitled to choose the preferred route to recovery. The statute states that, “[i]f the business contract is also a note, conditional sale contract, or other evidence of indebtedness that is otherwise governed by

G.S. 6-21.2, then the parties that are entitled to recover attorneys' fees and expenses may elect to recover attorneys' fees and expenses either under this section or G.S. § 6-21.2 but may recover only once for the same attorneys' fees and expenses."<sup>24</sup>

The statute includes no requirements related to the nature or timing of the election, and, although it is likely that counsel may face discovery requests directed at the statute under which attorneys' fees may be thereafter sought, it is also likely that counsel can respond that this request is premature and is not obligated to select between N.C.G.S. § 6-21.2 and N.C.G.S. § 6-21.6 until the post-judgment hearing on its motion for fees and costs.

**Effective Date.** N.C.G.S. § 6-21.6 "becomes effective Oct. 1, 2011, and applies to business contracts entered into on or after that date." As it appears likely that strict compliance with the terms of N.C.G.S. § 6-21.6 is required and any contractual agreement outside the scope of the statute is likely unenforceable, an effort by parties to a business contract consummated prior to Oct. 1, 2011 to opt in to the statute likely requires the agreement to be amended and restated in a substantial manner that permits the agreement to be deemed to be a business contracts entered into on or after Oct. 1, 2011.

N.C.G.S. § 6-21.6 is an effective tool for business lawyers and their clients to mitigate the costs of litigation intended to ensure that parties to a business contract receive the benefit of their bargains. It appears likely, however, that strict compliance with the requirements of N.C.G.S. § 6-21.6 will be a prerequisite to enforcement of attorneys' fees provisions intended to fall within its scope. •

### ***End Notes***

1. **Stillwell Enterprises, Inc. v. Interstate Equipment Co.**, 300 N.C. 286, 289, 266 S.E.2d 812, 814-15 (1980).

2. *Id.* at 289, 266 S.E.2d at 814-15 (discussing the policy rationale in **Tinsley v. Hoskins**, 111 N.C. 340, 16 S.E. 325 (1892)).

3. N.C.G.S. § 6-21.2 An "evidence of indebtedness" also includes guaranty agreements, **FNB Southeast v. Lane**, 160 N.C. App. 535, 586 S.E.2d 530 (2003), personal services contracts being enforced by the party seeking payment for services rendered, **Southland Amusements v. Rourk**, 143 N.C. App. 88, 96, 545 S.E.2d 254, 258 (2001), and equipment leases being enforced by the lessor, **Stillwell Enterprises, Inc. vs. Interstate Equipment Co.**, 300 N.C. 286, 266 S.E.2d 812 (1980). However, construction contracts, **Yeargin Construction Company, Inc. v. Futren Development Corporation**, 29 N.C. App. 731, 225 S.E.2d 623 (1976), asset purchase agreements, **Lee Cycle Center v. Wilson Cycle Center**, 143 N.C. App. 1, 545 S.E.2d 745 (2001), and personal service contracts, **Delta Environmental v. Wysong**, 132 N.C. App. 160, 510 S.E.2d 690 (1999), being enforced by the party who received the services or purchased the assets have been interpreted as not qualifying as an evidence of indebtedness. Additional statutory provisions that provide for the recovery of attorneys' fees include, for example, N.C.G.S. § 25-5-111 (repudiation of letter of credit); N.C.G.S. § 78A-56 (action regarding the offer or sale of securities); N.C.G.S. §§ 50-13.6 and 50-16.4 (litigation concerning alimony and child custody); N.C.G.S. § 6-19.1 (parties appealing or defending against agency decision); N.C.G.S. § 6-21 (court's discretion to allow or apportion attorneys' fees in certain proceedings); N.C.G.S. § 6-21.1 (certain actions involving insurance companies); N.C.G.S. § 6-21.3 (remedies for returned check); N.C.G.S. § 6-21.4 (certain cases involving principals or teachers and corporal punishment); N.C.G.S. § 44A-35 (statutory liens on real property or model payment and performance bonds); N.C.G.S. § 6-21.5 (nonjusticiable cases); N.C.G.S. § 75-16.1 (unfair trade practice ac-

tion); N.C.G.S. § 143-318.16B (open meetings laws); N.C.G.S. § 47F-3-107 (collection of obligations to homeowners' associations); N.C.G.S. § 113A-50 (certain actions under the Sedimentation Pollution Control Act of 1973).

4. N.C.G.S. § 6-21.6(b).

5. The states of Delaware, South Carolina, Tennessee, New York and Virginia enforce contractual attorneys' fees provisions. Georgia appears to be the exception and is the state most closely aligned to North Carolina, and, yet, Georgia allows recovery of attorneys' fees when the defendant has acted in bad faith, has been stubbornly litigious, or has caused the plaintiff unnecessary trouble and expense.

6. N.C.G.S. § 6-21.6(a)(1).

7. N.C.G.S. § 6-21.6(a)(2) (defining a consumer contract as one "entered into by one or more individuals primarily for personal, family, or household purposes.").

8. N.C.G.S. § 6-21.6(a)(3) (defining an employment contract as one "between an individual and another party to provide personal services by that individual to the other party, whether the relationship is in the nature of employee-employer or principal-independent contractor.").

9. N.C.G.S. § 6-21.6(a)(1).

10. N.C.G.S. § 6-21.6(e). The statute also does not affect the validity of a contractual provision falling within N.C.G.S. § 6-21.2 and, in fact, provides that "[n]othing in this section shall in any way make valid or invalid attorneys' fees provisions in consumer contracts or in any note, conditional sale contract, or other evidence of indebtedness that is otherwise governed by G.S. 6-21.2." *Id.*

11. N.C.G.S. § 6-21.6(a)(4) (emphasis added).

12. N.C.G.S. § 6-21.6(c) ("[T]he court or arbitrator... may award reasonable attorneys' fees in accordance with the terms of the business contract.") (emphasis added).

13. N.C.G.S. § 6-21.6(c)

14. N.C.G.S. § 6-21.6(d).

15. **McDaniel v. N.C. Mutual Life Ins. Co.**, 70 N.C.App. 480, 483, 319 S.E.2d 676, 678, *disc. review denied*, 312 N.C. 84, 321 S.E.2d 897 (1984). See **State v. Hennis**, 323 N.C. 279, 285, 372 S.E.2d 523, 527 (1988) (requiring a showing that the trial court's award of attorneys' fees was "manifestly unsupported by reason or is so arbitrary that it could not have been the result of a reasoned decision.").

16. **Washington v. Horton**, 132 N.C. App. 347, 351, 347, 513 S.E.2d 331, 334 (1999) (considering award of attorneys' fees pursuant to N.C.G.S. § 6-21.1).

17. *Id.*

18. **State v. Coffey**, 336 N.C. 412, 417-18, 444 S.E.2d 431, 434 (1994).

19. N.C.G.S. § 6-21.6(b) (emphasis added).

20. See, e.g., **Union Carbide Corp. v. Offerman**, 351 N.C. 310, 526 S.E.2d 167 (2000) (holding that where the language of a statute is clear and unambiguous, there is no room for judicial construction and the courts must give the statute its plain and definite meaning, and are without power to interpolate, or superimpose, provisions and limitations not contained therein).

21. **Baxter v. Jones**, 283 N.C. 327, 330, 196 S.E.2d 193, 196 (1973) ("Except as so provided by statute, attorneys' fees are not allowable.").

22. N.C.G.S. § 6-21.6(c) (emphasis added).

23. N.C.G.S. § 6-21.6(c) (emphasis added).

24. N.C.G.S. § 6-21.6(e). The new statute also does not affect the validity of a contractual provision falling within the older statute: "Nothing in this section shall in any way make valid or invalid attorneys' fees provisions in consumer contracts or in any note, conditional sale contract, or other evidence of indebtedness that is otherwise governed by G.S. 6-21.2." *Id.*

***Later practices with Robbins May & Rich in Pinehurst.***