IN THE SUPREME COURT FOR THE STATE OF MISSISSIPPI
NO. 2010-CA-00362

STACEY PICKERING, in his capacity as Auditor for THE STATE OF MISSISSIPPI, **APPELLANT**

VS.

THE LANGSTON LAW FIRM, PA, JOSEPH C. LANGSTON, TIMOTHY R. BALDUCCI, STATE OF MISSISSIPPI, LUNDY & DAVIS, LLP and AYLSTOCK, WITKIN, KREIS & OVERHOLTZ **APPELLEES**

APPEAL FROM THE CIRCUIT COURT OF HINDS COUNTY, MISSISSIPPI FIRST JUDICIAL DISTRICT

REPLY BRIEF OF APPELLANT

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ARGUMENT IN REPLY

I. *De Novo* review requires review of the entire record for all issues raised by the parties.

The parties agree that interpretation of Miss. Code Ann. 7-5-7 requires *de novo* review. However, the Langston firm mistakenly asserts that the Mississippi Supreme Court may not address matters not specifically discussed in the final opinion. In a *de novo* review, the Mississippi Supreme Court sits in the same position as the trial court and reviews all matters raised by the parties in the underlying cause. *Stockstill v. State*, 854 So. 2d 1017 (Miss. 2003). For example, one of the primary grounds asserted by the Auditor for his position was the case of *Pursue Energy Corporation v. Mississippi State Tax Commission,* 816 So.2d 385 (Miss. 2002). Although that case was never discussed by the lower court in its opinion, surely it is not suggested that the Mississippi Supreme Court cannot now address this opinion and the issues raised therein on appeal.

The "Statement of Issues" presented by the Auditor in this appeal are as follows with record citations to at least one occasion where each was raised by the Auditor in the court below:

1) Whether the Attorney General's authority regarding the source of payment for special counsel hired by his office has been expressly limited by Miss. Code Ann. § 7-5-7? (C.P. 170-73)

2) Whether the Langston Firm's negotiation and receipt of $14 million in the MCI/Worldcom Settlement Agreement was illegal under Miss. Code Ann. § 7-5-7, and therefore, void as a matter of public policy? (C.P. 170-73)

3) Whether the Retention Agreement with the Langston Firm was illegal for failure to include any mechanism for legislative approval of the compensation provided therein? (C.P. 170-73)

4) Whether the case of *Pursue Energy Corporation v. Mississippi State Tax Commission,* 816 So.2d 385 (Miss. 2002) prohibited the diversion of funds directly to special counsel to the Attorney General from the opposing party during a settlement with the State of Mississippi? (C.P. 177, 694-95)

5) Whether the $14 million obtained by the Langston Firm as a result of the State of Mississippi's settlement with MCI/Worldcom constituted public funds? (C.P. 700-03)

6) Whether outside special counsel may negotiate directly with an opposing party during settlement discussions with the State of Mississippi in order to bypass the requirements of Miss. Code Ann. § 7-5-7? (C.P. 702, 1596-98)

7) Whether the State Auditor has the right and obligation to seek the return of misspent public funds pursuant to Miss. Code Ann. § 7-7-211(g)? (C.P. 178)

8) Whether the State Auditor waived any right to seek the return of public funds obtained by the Langston firm in a cause of action in bankruptcy court in New York to which the State Auditor was not made a party? (C.P.696-700)

9) Whether the payment of funds to special counsel to the Attorney General directly from the opposing party in a settlement with the taxpayers of the State of Mississippi was a violation of the Mississippi Constitution and the separation of powers doctrine? (C.P. 175-78)

10) Whether the reasonableness of the fees paid to special counsel is an inherent issue to be determined by the Mississippi Legislature during the appropriations process mandated by Miss. Code Ann. § 7-5-7? (C.P. 1600)

Because all of these issues were raised by the Auditor in the court below, they are all properly before the Mississippi Supreme Court in this *de novo* review.

II. Historic lien law is irrelevant and remains unaltered by the facts of this case.

The Langston firm claims it holds a lien against any funds held in its possession for legal fees earned for services rendered to the State of Mississippi under the Retention Agreement. *See Collins v. Schneider*, 192 So. 20 (Miss. 1939). This argument places the cart before the horse. A valid lien could exist only if the underlying basis for the fees, i.e the Retention Agreement and Settlement Agreement, was valid and legal.

Here, the Auditor has specifically challenged the legality of both the Retention Agreement and the Settlement Agreement under Miss. Code Ann. § 7-5-7 which provides that "compensation

of appointees and employees made hereunder shall be paid out of the attorney general's contingent fund, or out of any other funds appropriated to the attorney general's office." As set forth in the court below by the Auditor:

> The contingency agreement was upheld [in *Pursue Energy Corporation v. Mississippi State Tax Commission,* 816 So.2d 385 (Miss. 2002)] only because it provided for legislative approval of any payment made thereunder. Because there was no similar provision allowing for Legislative approval here, the $14 million must be returned so the Mississippi Legislature can review and lawfully make an appropriation based upon the Attorney General's recommendation. However, in no event was the Langston Firm to have been paid directly by MCI/Worldcom without Legislative oversight. Pursuant to longstanding principles concerning the separation of powers in this State, summary judgment is appropriate and should be entered in favor of the State Auditor.
>
> *Pursue Energy Corporation v. Mississippi State Tax Commission,* 816 So.2d 385 (Miss. 2002), expressly confirms that any retention agreement that does not specifically allow for legislative oversight is invalid as a matter of law. There are no exceptions.
>
> * * *
>
> The Attorney General once again mistakenly presupposes that there is no contest to the Retention Agreement. As testified to by the former Attorney General Moore, a retention agreement that provides for a contingency fee is invalid, unless the contingency agreement expressly allows for legislative approval of final payment. Here, it should also be noted that even the terms of the Retention Agreement between the Attorney General and Langston as written were violated since it never provided for direct receipt of settlement funds by the attorneys representing the State Tax Commission. The Retention Agreement and the payments made as a result thereof are most certainly being challenged in this lawsuit.

(C.P. 1177) The cases cited by the Langston Firm now concern the satisfaction of fees in which there was no contest to their legality. Accordingly, the State Auditor's position in this case does nothing to alter historical lien law.

Accepting the Attorney General's argument as true that his office did not ultimately compensate his special assistants from the settlement proceeds, then the proposed theory of a lien

against those proceeds does not apply. The Attorney General cannot have it both ways -- arguing that it was a separately negotiated fee obtained directly from the opposing party, then claim it was purely a contingency fee for purposes of applying a common law lien against the settlement proceeds. Common law notions of liens must also yield to Miss. Code Ann. § 7-5-7 which places additional limitations on the sources for payment of contingency fees to special assistant attorney generals. Express statutory provisions trump any common law lien analogies proposed by the Attorney General now. Accordingly, the resort to basic historical lien law concerning the legal fees at issue in this case is unhelpful to resolving this dispute.

III. The Settlement Agreement was specifically drafted in a manner to hide "public funds" from the taxpayers and bypass the requirements of Miss. Code Ann. § 7-5-7.

The Attorney General would have this Court believe that it negotiated a complete and finalized agreement with MCI/Worldcom separately, with a concession by the Langston Firm that it would independently negotiate legal fees at a later time with the possibility that it might get nothing. The Attorney General cannot make this argument with a straight face. The agreement for the Langston Firm to received $14 million was obviously made in conjunction with and simultaneously to MCI/Worldcom's overall decision to settle fully and finally, as evidenced by the executed Settlement Agreement that followed.

In its ruling, the circuit court found as follows:

> There is no question that if the attorneys fees are paid by the State, then such fees must be paid in accordance with the clear dictates of Miss. Code Ann. § 7-5-7. Since the subject attorney's fees were not paid by the State, and did not come out of any state funds, this Court finds that there is absolutely nothing improper or illegal about MCI's payment of attorney's fees to the Langston Law firm.
>
> (C.P. 1715)

The mechanics of the transfer was nothing more than a hat trick by the parties designed to hide public funds from the Legislature and avoid the mandate of Miss. Code Ann. § 7-5-7. There would have been no funds but for the claims of the only real party in interest, the State Tax Commission. Despite the mechanics of the bank transfers directly to the Langston Firm, the Settlement Agreement provided that all settlement proceeds paid by MCI/Worldcom were in consideration for the release of all MCI/Worldcom's tax liability to the State of Mississippi and the State Tax Commission. Understanding the mandates of Miss. Code Ann. § 7-5-7 through its own personal experience in getting the fees appropriated in *Pursue Energy Corp.*, the Attorney General's office employed an elusive shell game designed solely to bypass the scrutiny of the Legislature and taxpayers of this State.

Nixon v. American Tobacco Co., 34 S.W.3d 122, 135 (Mo. 2001) recognized the fallacy of the claim that such funds are not public:

> [W]e find Respondents' argument unpersuasive, as it relies on an elusive shell game that misdirects the nature of the attorney fees. While it is true that these funds do not originate in the state treasury, our analysis does not end there. Instead, we look to the method by which parties settle disputes. When considering whether to make an offer to settle, a litigant establishes a monetary amount that reflects, among numerous other factors, both his potential loss should he continue litigation and the risk that he may not succeed on the merits. This adjusted figure represents that litigant's maximum settlement price. Once the litigant has negotiated a settlement amount he finds favorable, it is of absolutely no consequence to him how the settlement is divided among various parties.
>
> We view with suspicion Respondents' contention that theses attorneys fees are not state funds for purposes of justiciability. We find that to characterize these funds as wholly private funds places form before substance, as it is these parties that negotiated the funds in this manner. . . for purposes of justiciability, it suffices to point out that the tobacco companies would owe Strong nothing if he were not representing the State of Missouri as to the merits of the controversy between the State and the tobacco defendants. For this reason, justiciability is established and we address the merits.

Id. at 135.

Here, the lower court placed form over substance in its finding that the mandates of Miss. Code Ann. § 7-5-7 may be avoided solely by the chosen procedure for transferring the settlement funds. There would have been no settlement funds or transfers to anyone but for the claims of the State of Mississippi. Because the funds at issue here are "public" funds, the State Auditor does have authority to seek their return under Miss. Code Ann. § 7-7-211.

The legislative appropriation mandated by Miss. Code Ann. § 7-5-7 is obviously intended to prevent outside counsel from placing their own interests before his client. As expressly recognized by the *Nixon* Court,

> There is a potential danger in an agreement where a plaintiff's attorney's fee is to be paid by defendants. The danger is that the lawyer's own interest will prevail over the client's- or to put it another way, that the lawyer might be unduly influenced by an oversized fee to recommend an inadequate settlement for the client.

Nixon, 34S.W.3d at 135.

The Langston Firm elevated itself to the position of a party litigant during the settlement discussions. This is confirmed by the Affidavit of Jim Hood wherein he has openly admitted allowing the Langston Firm to negotiate directly with MCI/Worldcom on their own behalf. (C.P. 1306) The Attorney General's claim now that a Settlement Agreement would have been subsequently signed by the State of Mississippi and MCI/Worldcom regardless of whether the Langston Firm earned anything is disingenuous.

Although the Settlement Agreement may have been designed to avoid Miss. Code Ann. § 7-5-7 and *Pursue Energy*, the direct negotiations and payment also violated the Attorney General's own Retention Agreement with the Langston Firm. The Retention Agreement never permitted Langston to negotiate its fees directly with the opposing party as was done here. Accordingly, the

mechanics of the transfer to the Langston Firm was insufficient to transform this money into something other than public funds or validate the direct negotiation of fees with an opposing party.

IV. The rationale for requiring presentation of the contingency fee to the Legislature for final review is sound but nevertheless irrelevant.

It is a fundamental and constitutional principal of law that while the Attorney General's Office has general authority to pursue litigation of behalf of the State of Mississippi, it must yield to any express statutory limitations by the Legislature on that authority. *Frazier v. State ex rel. Pittman*, 504 So. 2d 675, 687-90 (Miss. 1987)("all public officers, including the Attorney General, are subordinate to the laws of this State"); *State v. Warren*, 180 So. 2d 293, 300 (Miss. 1965)(Attorney General clothed with common law powers "except insofar as they have been restricted or modified by *statute* or the State Constitution"). Here, the Attorney General's authority regarding the source of final compensation of outside counsel is one of those aspects that has been expressly limited by the Legislature, a limitation that is consistent with the Legislature's authority to control the purse strings of the State. *See In re Hood v. State of Mississippi,* 958 So. 2d 790, 812 (Miss. 2007); *see Belmont v. Miss. State Tax Commission*, 860 So.2d 289, 306-07 (Miss. 2003); *see also Myers v. City of McComb*, 943 So.2d. 1, 4 (Miss. 2006)(emphasizing the importance of separation of powers doctrine and holding that "legislative department alone has access to the pockets of the people" and "judicial branch cannot perform a clearly legislative branch function"); *see also King's Daughter Medical Center, et al. v. Haley Barbour, et al.*, Cause No. G-2006-1621, Chancery Court of Hinds County, Mississippi, First Judicial District (July 10, 2008)(declaring Division of Medicaid assessment void as matter of law in violation of Miss. Code Ann. § 43-13-11(18)(b) since it usurped legislative authority to control purse strings of State).

Recognizing the Legislature's authority to impose limitations, the Attorney General questions the Legislature's reasons for allowing contingency fee agreements if the final fee must also be presented to the Legislature for final appropriation. The Attorney General and the Langston Firm suggest to the Court that the two mandates of the statute cannot co-exist. To the contrary, the obvious rationale is to maintain transparency with the Legislature and the taxpayers of this State as to the various lawsuits being asserted by the State of Mississippi and the identity of outside counsel profiting therefrom.

Regardless of this rationale, it is not the job of the courts to question the Legislature's reasoning for permitting contingency agreements but also requiring final legislative appropriation for payment. Where the language used by the legislature in a statute is plain and unambiguous and conveys a clear directive, it must be strictly construed. *Miss Power Co. v. Jones*, 369 So. 2d 1381, 1388 (Miss. 1979); *Forman v. Carter*, 269 So.2d 865 (Miss. 1972); *State v. Heard*, 246 Miss. 774, 151 So.2d 417 (1963); *Harrison County School District v. Long Beach School District* 700 So. 2d 286, 288-89 (Miss. 1997). The fact that contingency agreements are permitted does not automatically suggest that another express provision in the statutes should be ignored. By ignoring the source of funds requirement in Miss. Code Ann. § 7-5-7, it is instead the Attorney General and the Langston Firm that seek to read certain portions in isolation. The Attorney General's plea for deference is not permitted when the statute addresses the precise issue on the subject. *See Chevron USA Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-43 (1984)(deference is granted only if statute is silent or ambiguous with respect to the specific issue being disputed). Pursuant to the plain and unambiguous terms of Mississippi Code Ann. § 7-5-7, compensation of all special assistants "shall" be paid directly from the attorney general's contingent fund or out of

funds appropriated to his office. It is a fundamental rule of statutory interpretation in Mississippi that "shall" means absolutely mandatory. *Franklin v. Franklin*, 858 So. 2d 110, 115 (Miss. 2003). Accordingly, the Langston Firm must take its alleged war over the fees to the Legislature where it was intended to be fought.

V. Miss. Code Ann. § 7-5-5 is not applicable to this case.

Miss. Code Ann. § 7-5-5 provides the following:

> The attorney general shall appoint nine (9) competent attorneys, each of whom shall be designated as an assistant attorney general. The assistants shall each possess all of the qualifications required by law of the attorney general and shall have power and authority under the direction and supervision of the attorney general to perform all of the duties required by law of that officer; and each shall be liable to the pains and penalties to which the attorney general is liable. The assistants shall serve at the will and pleasure of the attorney general, and they shall devote their entire time and attention to the duties pertaining to the department of justice as required by the general laws. The compensation of the within enumerated assistant attorneys general and all other regular assistants authorized by law, shall be fixed by the attorney general not to exceed the compensation fixed by law for such assistants.
>
> The attorney general is hereby authorized, empowered, and directed to designate three (3) of the said assistant attorneys general to devote their time and attention primarily to defending and aiding in the defense in all courts of any suit, filed or threatened, against the state of Mississippi, against any subdivision thereof, or against any agency or instrumentality of said state or subdivision, including all elected officials and any other officer or employee thereof. When the circumstances permit, such assistants may perform any of the attorney general's powers and duties, including but not limited to engaging in lawsuits outside the state when in his opinion same would help bring about the equal application of federal laws and court decisions in every state and guaranteeing equal protection of the laws as guaranteed every citizen by the United States Constitution. To further prosecute and insure such purposes, the attorney general is hereby further expressly authorized, empowered, and directed to employ such additional counsel as special assistant attorneys general as may be necessary or advisable, on a fee or contract basis; and the attorney general shall be the sole judge of the compensation in such cases.
>
> The attorney general may discharge any assistant attorney general or special assistant attorney general at his pleasure and appoint another in his stead. **The assistant attorneys general shall devote their entire time and attention to the duties**

pertaining to the department of justice under the control and supervision of the attorney general. (emphasis added)

Although Miss. Code Ann. § 7-5-5 still fails to address the issue regarding the source of the funds to pay special assistants which is addressed in § 7-5-7,[1] the primary issue in this case, this statute nevertheless concerns attorneys that "devote their entire time and attention to the duties pertaining to the department of justice under the control and supervision of the attorney general." The State Auditor does not dispute the fact that the Attorney General may be the sole judge of the levels of compensation of his full time attorneys that fill his state office. Here, we are instead dealing with private lawyers and private law firms with separate ongoing practices hired on a part-time basis by the Attorney General solely for the purpose of handling a single case. There has never been any dispute that outside counsel representing the State against MCI were hired as "special counsel" pursuant to Miss. Code. § 7-5-7. As discussed above, that statute expressly provides that the "compensation of appointees and employees made hereunder shall be paid out of the attorney general's contingent fund, or out of any other funds appropriated to the attorney general's office." Whether they were paid out of the attorney general's contingent fund or other appropriation under Miss. Code Ann. § 7-5-7 is the fundamental issue of this case. That issue is not addressed by Miss. Code Ann. § 7-5-5.

VI. The cases raised by the Langston Firm from other jurisdictions do not apply.

The Attorney General cites 7 Am. Jur. 2d § 5 (2007) as its principal authority in this case. However, that section is derived from the case of *Pursue Energy Corporation v. Mississippi State Tax Commission,* 816 So.2d 385 (Miss. 2002). With all due respect to the authors of Am. Jur. 2d,

[1] It is noted that the funds utilized to compensate these full time employees are also from amounts appropriated by the Mississippi Legislature.

this Court is capable of interpreting the holding of that case. That case did not hold that the legislature could be bypassed in the final appropriation of contingency fees. It held that a Retention Agreement providing for a contingency fee that was modified to include legislative review and appropriation as the source of funds was permissible under Miss. Code Ann. § 7-5-7.

In *Nixon v. American Tobacco Co.*, 34 S.W.3d 122 (Mo. 2001), also a source for the Am. Jur. 2d authors, the Missouri Supreme Court ultimately ruled that the issue of the direct payment of special assistants by the opposing party should nevertheless go before the Missouri General Assembly, which was allowed by the court until December 31, 2001 to enact legislation that prohibited the arrangement if there was any disagreement as to the source of funds for payment. *Id.* at 139. The basis of this ruling was Missouri Rule of Ethics 4-1.8(f) wherein the client, which the Court determined could only be the Missouri General Assembly since it was the public body that spoke for the citizens of State of Missouri, could withhold its consent to a settlement proposal. *Id.* at 136. Similarly here, this Court could order that the Mississippi Legislature review the fee and accept or reject all or part by the close of the next legislative session, thereby effectively complying with the mandate of Miss. Code Ann. § 7-5-7 and our similar rules of ethics.

In *State of Rhode Island v. Lead Industries Ass'n*, 951 A.2d 428 (R.I. 2008), the analysis centered upon the common law powers of the Attorney General versus a general statute punishing with treble damages "every clerk, officer, or other person who shall neglect or refuse to pay into the state treasury any money belonging to the state." There was no express statute specifically referencing the precise source of funds that could be used for compensation of special assistants to the Attorney General such as we have here under Miss. Code Ann. § 7-5-7. It is also interesting that the Rhode Island Court ruled that the fee under these circumstances should be subjected to court

scrutiny and oversight *before* payment. *Id. at* 47-48. It is this judicial review that is expressly avoided in Mississippi through application of Miss. Code Ann. § 7-5-7 by legislative review.

In *State v. Hagerty*, 580 N.W2d 139 (N.D. 1998) and the *Lead Industries Ass'n* case, the Court also never faced the situation where the special assistants had negotiated their attorneys' fees outside their retention agreement and directly with the opposing party. *See Hagerty*, 580 N.W2d at 148; *Lead Industries Ass'n*, 951 A.2d at 481. In those cases, the Court merely held that contingency fee agreements were an acceptable means for employing such counsel. *Id.* Here, the State Auditor has never contested the hiring of special assistants under a contingency fee arrangement, just the manner in which the Langston Firm obtained direct payment of fees from the opposing party during settlement negotiations without the final legislative oversight expressly required by Miss. Code Ann. § 7-5-7. Even the *Nixon* Court above refused to cut out the legislature from review and consent of such an arrangement.

People v. Philip Morris, 759 N.E.2d 906 (Ill. 2001) concerned the issue of whether the Circuit Court versus the Illinois Court of Claims had jurisdiction to hear a fee dispute involving private attorneys hired by their attorney general in the tobacco litigation. The Supreme Court of Illinois merely held that the Circuit Court had jurisdiction to adjudicate whether the lien against the settlement proceeds was valid. Not only was there no comparable statute providing strict mandates on the source of payment of private attorneys, the Illinois Supreme Court never adjudicated whether the lien was valid but merely remanded for resolution by the Circuit Court. Reliance upon dicta in a case concerning jurisdiction of the circuit court is not helpful here because the State Auditor has already selected the jurisdiction of the Circuit Court for a determination of the validity of the receipt of the $14 million by the Langston Firm under Miss. Code Ann. § 7-5-7.

In *Conant v. Robins, Kaplan, Miller & Ciresi, LLP*, 603 N.W.2d 143 (Minn. Ct. App. 1999), the issue was whether taxpayers or one state senator had standing to challenge the manner of payment of private attorneys by the attorney general. Here, the State Auditor is proceeding under direct authority of Miss. Code Ann. § 7-7-211(g), which provides him with the express authority and standing to bring such matters before the circuit court for adjudication. Like all other cases cited by the Langston Firm, the statute relied upon in this Minnesota case gave no instruction on payment of private attorneys hired on a contingency basis. Here, Miss. Code Ann. § 7-5-7 gives specific instruction.

Similarly, in *Philip Morris Incorporated v. Glendening*, 709 A.2d 1230, 1235 (Md. Ct App. 1998), the Court affirmed the trial court because "the plain language of subsection (b)(2)(ii) [the statute allowing payment of private attorneys] did not place any limitation on the source of the funds from which the Attorney General may compensate outside counsel." Obviously here, the statute in question provides the only two sources for payment of outside counsel, neither of which were utilized to pay the Langston Firm.

Despite the Langston Firm's claims now, the Auditor fully addressed and rebutted these foreign cases in the circuit court. (C.P. 700-03) Despite the fundamental differences of this case from these foreign decisions, there still is no need or basis for this Court to rely on anything other than Miss. Code Ann. § 7-5-7 and *Pursue Energy* in Mississippi.

VII. There was no waiver by the State Auditor who has the independent statutory authority and duty to seek return of misspent public funds.

A. There is no waiver and estoppel against a government's right to seek return of funds obtained illegally.

There is no waiver and estoppel against the government acting in its sovereign capacity. The public policy rationale behind this was discussed in detail by the United States Supreme Court in

Heckler v. Community Health Services of Crawford County, Inc., 467 U.S. 51, 104 S. Ct. 2218 (1984). In that case, the Supreme Court held that United States Secretary of Health and Human Services had not waived and was not estopped from recovering federal funds improperly paid to a health care provider, even though the provider was previously instructed by a government agent that the expenditure was proper. The Court stated:

> When the Government is unable to enforce the law because the conduct of its agents has given rise to an estoppel, the interest of the citizenry as a whole in obedience to the rule of law is undermined. It is for this reason that it is well settled that the Government may not be estopped on the same terms as any other litigant.

Id. at 2224. The Court held a party who receives payment of government funds that is invalid under the law cannot establish either reasonable reliance or detrimental change in position, the primary elements of a waiver and estoppel defense:

> To analyze the nature of a private party's detrimental change in position, we must identify the manner in which reliance on the Government's misconduct has caused the private citizen to change his position for the worse. In this case the consequences of the Government's misconduct were not entirely adverse. Respondent did receive an immediate benefit as a result of the double reimbursement. Its detriment is the inability to retain money that it should never have received in the first place. Thus, this is not a case in which the respondent has lost any legal right, either vested or contingent, or suffered any adverse change in its status. . . . The question is whether the Government has entirely forfeited its right to the money. A for-profit corporation could hardly base an estoppel on the fact that the Government wrongfully allowed it the interest-free use of taxpayers' money for a period of two or three years . . . .

Id. at 2225. The Court held that parties that deal with the government do so with the risk that a government agent or employee may act outside the scope of his or her authority. Those parties are charged with knowing the statutes and regulations that control their dealings with the government. The Court opined as follows:

> Men must turn square corners when they deal with the Government . . . This observation has its greatest force when a private party seeks to spend the Government's money. Protection of the public first requires that those who seek public funds act with scrupulous regard for the requirements of the law . . . This is consistent with the general rule that those who deal with the Government are expected to know the law and may not rely on the conduct of Government agents contrary to the law . . . . . As a participant in the Medicare program, respondent had a duty to familiarize itself with the legal requirements for cost reimbursement.

104 S. Ct at 2225-26; *see State v. Ex. rel.* Rice, 4 So. 2d 270, 277 (Miss. 1940)("the state cannot abdicate its duty as trustee of property in which the whole people are interested, any more than it can surrender its police powers in the administration of government and in the preservation of peace and order"); *see also Office of Personnel Management v. Richmond,* 496 U.S. 414, 110 S. Ct. 2465 (1990)(payment of money from the public treasury contrary to statutory appropriation is prohibited by the Appropriations Clause of the Constitution, which provides that such money may be paid out only as authorized by statute, and the judicial use of estoppel could not grant the respondent a money remedy that Congress did not authorize); *Dun & Bradstreet Corporation Foundation v. United States Postal Service*, 946 F. 2d 189 (2nd Cir. 1991)(estoppel claim that will require the payment of government funds in contravention of statute will fail); *In re Yachthaven Restaurant, Inc.*, 103 B.R. 68, 78 (E.D.N.Y. 1989) (estoppel may not be invoked against a municipality to enforce an agreement which violates express statutory provisions because to do so would give vitality to illegal acts.)

The relevant facts of *Heckler* are strikingly similar to the contested issues in this case. The United States Supreme Court concluded that the defense of estoppel was precluded as a matter of law because unlawful receipt of funds can hardly constitute detrimental reliance, and any alleged reliance was not reasonable given the recipients duty to familiarize itself with the laws which apply to its very own business. Similarly, the issue here is whether the Langston attorneys were entitled

to the money in the first place. Their use of the funds can hardly be said to be detrimental if receipt of those funds is proven unlawful under the Mississippi Code.

The Attorney General's cases regarding waiver and estoppel by commercial parties to a contract are not applicable in this governmental setting. *See Setinel Indus. Contracting Corp. v. Kimmins Indus. Serv.* Corp., 743 So. 2d 954, 964 (Miss. 1999); *Eastline Corp. v. Marion Apartments, Ltd.*, 524 So. 2d 582, 584 (Miss. 1988). Here, the Langston Firm knew they were being hired by the government as special assistants to the Attorney General and were, or should have been, familiar with the statutes governing their retention and payment from government funds. *In Re Nextwave Personal Communications*, 244 B.R. 253 (Bankr. S.D.N.Y. 2000) found waiver against a governmental entity only because it was acting in a commercial capacity. *In Re Nextwave* distinguished between commercial and sovereign conduct as follows:

> Proprietary governmental functions include essentially commercial transactions involving the purchase or sale of goods and services and other activities for the commercial benefit of a particular government agency. Whereas in its sovereign role, the government carries out unique governmental functions for the benefit of the whole public, in its proprietary capacity the government's activities are analogous to those of a private concern.

244 B.R. at 279. *In re Nextwave* is distinguishable because the FCC was acting in a commercial role and even had authority under the applicable regulations to waive payment of licensing fees. *In re Refco, Inc.*, 505 F.3d 109 (2d Cir. 2007) does not apply either because it involved a private party to a previous settlement agreement with clear authority and discretion to waive all objections on behalf of its liquidators. Because the State Auditor is performing his sovereign duty for the benefit

of the Mississippi taxpayers as a whole, neither the Attorney General, the State Tax Commission nor the State Auditor have discretionary authority to waive the provisions of Miss. Code Ann. § 7-5-7.

B. The State Auditor was not a party to the Bankruptcy Proceedings, Settlement Agreement, or Settlement Approval Process.

Despite the inability to assert estoppel waiver against the government in its enforcement of governing statutes, it is well documented in the Performance Audits requested by the Mississippi Legislature that the State Auditor was first requested to review the settlement only after the bankruptcy proceedings had concluded on May 12, 2005. The first request for review came from the Legislature on June 28, 2005. (C.P. 1345, 1357) Nearly a year later, on June 5, 2006, the State Auditor was first requested by the Office of the Governor to conduct a performance review. (C.P. 1368) Thus, the initial requests to audit the settlements came only after the settlement order had been executed and approved, all without any notice or participation by the State Auditor as a party to the bankruptcy proceedings.

As to the initial findings in those audits following conclusion of the bankruptcy proceedings, the Attorney General fails to point out to this Court now the State Auditor's original Finding No: 2:

> **The contingency fee received by the private attorneys retained by the State of Mississippi was never deposited in to a public account, appropriated or audited.**

(C.P. 1356, 1367) Although the final recommendation to the Office of the Governor also suggested the remedy for the violation, the original finding was unchanged. (C.P. 1383) The Attorney General's attempts to turn this case into a political dispute is merely an attempt to distract from the sole issue in this case - the application of Miss. Code Ann. § 7-5-7.

As to the findings by the Bankruptcy Court and the Federal District Courts regarding waiver and *res judicata*, the State Auditor stands by the judicial excerpts already provided to the Court in Appellant's Brief. In its affirmation of the Bankruptcy Court's decision to abstain, the New York District Court also held the following:

> As this Court discussed earlier, this action is not a core proceeding and its resolution will not have any effect on the administration of the estate. Neither the Debtors nor any property of the estate is involved in this action. In addition, this Court agrees that the issues raised in this action are remote from the bankruptcy case and will likely hinge on Mississippi state law regarding the payment of legal fees, which is best handled by the Mississippi state court. The State has commenced an action in Mississippi state court, which will be able to resolve this dispute. Accordingly, the Bankruptcy Court did not abuse its discretion in abstaining pursuant to 28 U.S.C. 1334(c)(1).

The Bankruptcy Court had no reason to know there was an issue concerning the diversion of settlement proceeds directly to outside counsel representing the State Tax Commission. The entities that knew or should have known of the issue -- the Langston Firm and the Attorney General -- certainly did not raise it. The only "parties" to the Settlement Agreement were those "set forth on the signature pages hereto" – MCI, Inc., on behalf of itself and the Reorganized Debtors, and the State of Mississippi. The Settlement Agreement represented a compromise of the Proofs of Claim filed by the State Tax Commission. The claims released were "the Reorganized Debtors' obligation to pay all taxes, interest, and penalties relating to the Royalty Program [as defined therein]" and the only "Released Parties" were the Debtors. The State Auditor was never a party to any of this. Because neither the State Auditor nor the Langston Firm were party litigants to the prior proceedings or the Settlement Agreement, this cause of action between them simply did not arise until after the funds were received by the Langston Firm.

Reliance on Bankruptcy Rule 9024 for the assertion of waiver is misplaced for the same reasons. First and foremost, the State Auditor was not a party to the bankruptcy proceedings so as to fall under the rule. Second, this rule provides a one year limitation only for grounds of mistake, inadvertence, surprise or excusable neglect. *See e.g. Warren v. Garvin,* 219 F.3d 111 (2d Cir. 2000). None of those grounds are at issue here. *In Re AMC Realty Corp.,* 270 B.R. 132, 145 (Bankr. S.D.N.Y. 2001) confirms that Rule 9024 "does not impose a time limit" as to any other grounds for a party to seek relief from a court order, such as the assertion by the State Auditor here that it was void as against public policy. There is certainly no authority for the proposition that Rule 9024 can be used to prevent a governmental agency challenge to the illegal receipt of government money.

The Langston Firm suggests that the State Auditor could have demanded the Attorney General object on his behalf, "just like he demanded that the Attorney General file this lawsuit on his own behalf." This mistakenly assumes that the State Auditor was part of the settlement proceedings. Nevertheless, when the State Auditor did demand that the Attorney General file this lawsuit, he refused to do so or provide the State Auditor with any representation herein. Since that is his position now, the result would obviously have been the same had the State Auditor been made a party to the proceedings and objected. If the State Auditor was nevertheless a "party in interest" to the bankruptcy proceedings as claimed now by the Attorney General, then why was he not included as a party or on the service list for the bankruptcy proceedings. Under these recalcitrant circumstances created by the Attorney General, the State Auditor's only remaining remedy may be found in Miss. Code. Ann. § 7-7-211.

State officers and agencies have no privity with one another when their interests are divergent, their roles are different, and one does not adequately represent the interests of the other.

See Cleveland County Association for Government By The People v. Cleveland County Board of Commissioners, 142 F. 3d 468, 474 (D.C. Cir. 1998) (holding that *res judicata* did not apply where the interests of the two entities were divergent, because otherwise "consent decrees to which the government was a party would be immune from challenge"); *United States v. Alkay Enterprises, Inc.*, 969 F. 2d. 1309 (1st Cir. 1992) (finding insufficient identity, and hence no privity between the Interstate Commerce Commission ("ICC") and the United States Government, because the ICC's enforcement role was different from that of the Attorney General of the United States); *City of New York v. Beretta U.S.A. Corp.*, 315 F. Supp. 2d 256 (E.D.N.Y. 2004)(a final decision on the merits that is binding on one governmental agency or official is not binding on another agency or official if the second action involves an agency or official whose functions and responsibilities are so distinct from those of the agency or official in the first action that applying preclusion would interfere with the proper allocation of authority between them). If the State Auditor could be bound by the Attorney General's agreement to let a portion of the settlement proceeds be diverted directly to the Langston Firm, it would interfere with the State Auditor's unique duty and authority to oversee the disbursement of public funds pursuant to Mississippi Code Ann. § 7-7-211(g).

The Langston Firm also suggests that the State Auditor is bound by the Settlement Agreement because the Settlement Agreement expansively defined the "State" as including "all subdivisions, agencies, officers and representatives of the State, including, without limitation, the Mississippi State Tax Commission and the Office of the Attorney General." Since the State Auditor was not involved with the creation of this definition or made a party to the settlement agreement, the Attorney General had no more authority to bind the State Auditor to this definition than he did to authorize the payment in the first place.

As confirmed by the Bankruptcy Court, the claims asserted in this action were not part of the bankruptcy proceedings. The present cause of action was brought under Mississippi Code Ann. § 7-7-211(g) which gives the State Auditor the authority to seek return of misspent state funds. The Bankruptcy Court would certainly not have abstained and given deference Mississippi's state court if any of these issue had been waived through the bankruptcy approval process. Accordingly, there was no waiver by the State Auditor.

VIII. Constitutional issues concerning impairment of contracts or property rights were not raised in the court below.

The Attorney General argues that voiding the direct payment of fees to the Langston Firm by the opposing party violates the constitutional prohibition on impairment of contracts and would constitute an unlawful taking of property from the Langston Firm. These issues were not raised in the court below. (C.P. 1289-1302, 1691-1708) Case law is established that a party may not pursue arguments in the Mississippi Supreme Court for the first time on appeal, whether appellant or appellee. *See Fidelity & Deposit Co. of Maryland v. Ralph McKnight & Son Const., Inc.*, 28 So. 3d 1382, (Miss 2010)(Supreme Court does not consider matters not decided by trial court); *Corporate Management, Inc. v. Greene County*, 23 So. 3d 454 (Miss. 2009)(issue must first be presented to trial court before being raised to appellate court); *Mathis v. ERA Franchise Systems, Inc.*, 25 So. 3d 298 (Miss. 2009)(absent extraordinary circumstances, Supreme Court will not consider issues raised for first time on appeal); *Pittman v. Dykes Timber Co., Inc.*, 18 So. 3d 923 (Miss. App. 2009)(appellate courts will not put trial courts in error for issues not first presented to trial court for resolution); *Estate of Johnson v. Adkins* 513 So. 2d 922 (Miss.1987)(party must pursue appeal on same legal theory advanced in trial court); *Estate of Myers v. Myers,* 498 So. 2d 376, 378 (Miss.1986)("One of

the most fundamental and long established rules of law in Mississippi is that the Mississippi Supreme Court will not review matters on appeal that were not raised at the trial court level"). This should be especially true when a party attempts to raise constitutional issues for the first time on appeal. Legality would nevertheless be a prerequisite to having lawful contract or property rights in the first place. Accordingly, these issues raised for the first time on appeal have no merit.

IX. The State Auditor has a legal right to challenge the validity of the Retention Agreement and Settlement Agreement which were prohibited by Statute.

The Attorney General argues that only parties to a contract or those with a legal right to challenge a contract may seek to negate it on the basis of illegality. However, pursuant to the express authority of Miss. Code Ann. § 7-7-211, the State Auditor has the legal right to challenge the Langston Firm's Retention Agreement and direct negotiation of fees from the opposing party under the Settlement Agreement. Regardless, illegal provisions of a contract are void as a matter of public policy, not merely voidable. *Price v. Purdue Pharma Co.*, 920 So. 2d 479, 484 (Miss. 2006); *Morrissey v. Balogna*, 123 So. 2d 537 (Miss. 1960)(court will not aid litigant whose actions are in violation of statute); *Lowenberg v. Klein*, 87 So. 653, 654-55 (1921)(contract provisions in violation of state or federal statute will not be enforced). As to portions of a contract that violate state or federal statute, courts will not enforce those provisions "but will leave the parties where found, - insofar as any illegal items or portions are concerned." *Chas. Weaver & Co. v. Phares*, 188 So. 12, 13 (Miss. 1939); *see Attaché v. Golden*, 133 A.D. 2d 596, 519 N.Y.S.2d 702 (2nd Dept. 1987)(Where agreement consists in part of unlawful objective and in part of lawful objectives, court may sever illegal aspects and enforce legal ones, so long as illegal aspects are incidental and not main objective of agreement); *Kidder Peabody v. IAN International*, 28 F. Supp. 2d 126, 139

(S.D.N.Y. 1998)(conclusion that portion of contract is illegal does not preclude enforcement of legitimate provisions of agreement).

Citing *Seymour v. Evans*, 608 So. 2d 1141 (Miss. 1992), the Attorney General argues that the Retention Agreement and Settlement Agreement may have been *malum prohibitum*, but not necessarily inherently evil so as to constitute a basis for voiding the contracts. However, *Seymour* ultimately concluded that there was no merit to an attack on a real estate contract, and more specifically the warranty that the property was free from encumbrances, because at the time of the execution of the contract the alleged zoning violations did not exist. *Id.* at 1148. It was only after the execution of the sales contract that the purchaser proposed a use for the property that did not comply with zoning ordinances. *Id* at 1142.

The Auditor asserts that the Retention Agreement and Settlement Agreement were illegal at the time of their formation. This lawsuit constitutes a direct attack on both for failure to include a provision that any fees be obtained through the appropriations process in the Mississippi Legislature. Because it is alleged that the formation of these contracts was prohibited by Miss. Code Ann. § 7-5-7, the *Seymour* analogy proposed by the Attorney General is not applicable. Accordingly, the decision of the lower court should be reversed and rendered.

CONCLUSION

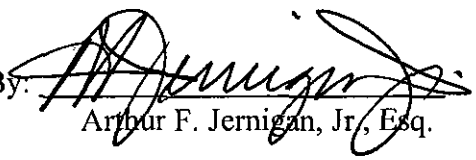
The Langston Firm was not paid out of the Attorney General's contingent fund, or out of any other funds appropriated to the attorney general's office, in violation of Miss. Code Ann. § 7-5-7. Any provisions in the Settlement Agreement or Retention Agreement allowing the $14 million paid to the Langston Firm to bypass the general fund and legislative appropriation were illegal and unenforceable as a matter of public policy. The State Auditor did not waive his authority under

Miss. Code Ann. § 7-7-211(g) to seek return of these funds since no government may waive the enforcement of its statutes. Strict interpretation of Miss. Code Ann. § 7-5-7 is consistent with the constitutional right and duty of the legislative branch of government to control the public treasury.

WHEREFORE, the judgment of the Circuit Court of Hinds County should be REVERSED and RENDERED.

Respectfully submitted the 21st day of March, 2011.

STACEY PICKERING, in his capacity as
Auditor for THE STATE OF MISSISSIPPI

By: 
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CERTIFICATE OF SERVICE

I, Arthur F. Jernigan, Jr. do hereby certify that I have caused to be served this date, via U.S. Mail, postage prepaid, a true and correct copy of the above and foregoing instrument to the following counsel of record:

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THIS, the 21st day of March, 2011.

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