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Why not adopt a loser-pays-all rule in criminal litigation?

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ARTICLE INFO

ABSTRACT

In this paper we consider the potential effects that the application of a loser-pays-all rule may have on criminal litigation, including the decision to prosecute, criminal deterrence and legal error. We find that the effects of fee shifting on deterrence and on miscarriage of justice go in opposite directions. We also look at the effects of this rule on the rate of settlements (plea-bargaining) and when one party is wealth-constrained. We apply the insights of our model to current policy discussions such as the use of RICO proceedings and the financing of enforcement authorities in the United States.

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1. Introduction

Many common law legal systems use loser-pays-all rules in civil litigation. The economic literature refers to the English or the British rule when discussing the situation where the party that loses a civil case pays for the legal fees and the costs incurred by the prevailing party. Most civil law jurisdictions also use some form of the English rule (in some, the fees paid to the lawyers are excluded from the shifting rule or only a percentage of the total costs can be reimbursed). The opposing example is the American rule where each party pays their own costs.

The economic literature on the topic is by now extensive.[1] The controversial issues include the extent to which shifting costs promote settlement, enhance civil litigation, favor more meritorious claims, or decrease the number of nuisance lawsuits.

However, loser-pays-all rules are generally not used in criminal cases. Usually public prosecution bears the cost of its prosecutorial efforts and defendants bear the cost of their defense. A criminal defendant brought to trial and found not guilty is typically not compensated for the defense costs incurred.[2] Likewise, prosecutorial expenses are not compensated by guilty defendants.

There is some evidence that the loser-pays-all rule can be applied to criminal litigation. In Britain, for instance, the recovery of costs is regulated by the Prosecution of Offences Act 1985. Section 16 allows a court order to compensate for defense costs (out of government funds) with a strong presumption that such order will be awarded to favor a defendant who has been acquitted (unless the defense is funded by the government itself).[3] Section 17 regulates the recovery of costs for private prosecutors and Section 18 for public prosecutors. The court can order the convicted defendant to pay for the costs of prosecution for an amount considered reasonable and appropriate.[4] In the case of a guilty plea, the court should adjust the order to take into account that the expenses of the

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   [1] See, among others, Shavell (1982), Bebchuk (1984), Katz (1987), Cooter and Rubinfeld (1989), Hause (1989), Snyder and Hughes (1990), Polinsky and Rubinfeld (1996, 1998), van Wijck and van Velthoven (2000), Hylton (2002), Spier (2007), Garoupa (2009b), and Katz and Sanchirico (2010).

[2] Generally speaking, a defendant who cannot afford a lawyer has a right to one provided by the state. In many jurisdictions, the prosecutor is subject to a rule of mandatory disclosure of evidence. These two rules might be regarded as forms of shifting costs from defendants to prosecutors. However, they are not conditioned on the defendant being acquitted.

[3] We follow Hungerford-Welch (2004), at chapter 13, here. In fact, unless the defendant brought suspicion on himself or the defense is publicly funded, it is expected that the defense costs are borne by the government when a defendant is acquitted. The fact that the prosecution has acted properly or that the defendant was acquitted on a technicality does not allow the court to refuse a cost order favorable to the defendant.

[4] Following Hungerford-Welch (2004), the amount should reflect the ability of the defendant to pay as well as the fine. If the defendant cannot pay both, the fine has precedence.

prosecution have been reduced. Finally, Section 17 of the Access to Justice Act 1999 introduces the possibility of a recovery of defense costs order against defendants funded by the government.[5]

Notwithstanding the statutory developments, the application of such orders is much less common in criminal litigation and subject to the behavior of the parties and the will of the court. There is always the possibility of a claim in torts to sue for compensation and payment of legal expenses, but these claims are occasional.[6]

In the United States, the Hyde Amendment (1997) permits recovery of attorneys' fees by criminal defendants who have been acquitted following a (willful and frivolous) indictment by the government.[7] At the same time, criminally culpable defendants can have fees levied against them in their convictions, so long as there is a statutory basis for it.[8] A loser-pays-all rule is occasionally applied in the context of corporate criminal litigation.[9]

The use of a loser-pays-all rule in criminal litigation should not be confused with compensation for wrongful conviction. In one form or another, all legal systems potentially compensate wrongfully convicted people. However, such compensation has little to do with the legal costs incurred by the accused during trial.[10]

In this paper, we develop an economic model to consider the application of a loser-pays-all rule in criminal litigation. We consider the effects of this hypothetical rule primarily on criminal deterrence and on the possibility of legal error. In the basic model, we investigate the extent to which shifting costs from the loser to the winner provides additional deterrence and reduces miscarriage of justice. Under realistic conditions, shifting legal costs helps deterrence and therefore the English rule should prevail. At the same time, fee shifting increases the frequency of legal error and hence the American rule is more appropriate from that viewpoint.

Our paper also explicitly addresses the situation where defendants do not have resources to reimburse the prosecution in order to assess the effects of an asymmetric application of a loser-pays-all rule. One practical reason why a loser-pays-all rule in criminal litigation might not be frequently considered and applied is that, in a significant proportion of the cases, both sides are funded by taxpayers. Prosecutors are public by nature and operate with a budget financed by taxes. Many defendants in criminal litigation use a form of public funding (legal aid, public defender). In this context, a loser-pays-all rule would just imply a transfer of resources across state bureaucracies. Consequently, it is possible that a loser-pays-all rule in criminal litigation is only politically feasible when the defendant is wealthy. In the context of corporate criminal litigation or wealthy defendants, there is no immediate reason to undermine the application of a symmetric loser-pays-all rule. In fact, we

conclude that a loser-pays-all rule applied only to wealthy defendants helps deterrence.[11]

The paper focuses on deterrence (i.e. crime rates) and legal error (i.e. miscarriage of justice) unlike the literature on civil litigation. The latter is usually more concerned with the impact of loser-pays-all rules on the incentive to litigate and settle (rather than the underlying rate of wrongdoings or the impact on false positives).

As already stated, criminal and civil litigation are not the same. Our model reflects these differences and, in that context, departs from the previous literature that only looks at civil litigation.[12] Civil litigation usually uses contingency fees which are not allowed in criminal litigation. In criminal litigation the objective is twofold: to increase deterrence, on one hand, and to decrease the number of wrongful convictions, on the other hand. Given that it is important to avoid punishing innocent defendants, the standard of proof is higher under criminal litigation. Public enforcement prevails in criminal law. As a consequence, the fine paid by the defendant is not the gain for the prosecutor. The fine is also not the equivalent to compensatory damages in civil litigation. Furthermore, public enforcement is usually financed by public agencies with limited budgets and highly regulated or constrained by guidelines and procedural rules. The wealth constraints for the defendant are more serious in criminal litigation. Finally, plea-bargaining is not exactly the equivalent of out-of-court settlements in civil litigation because the prosecutor is not directly benefited from imposing a higher fine.

Some of the features we derive in our model show similarities with the civil litigation literature. For example, as with the civil litigation literature, we find that fee-shifting will change the incentives for settlements and alter the incentives of defendants to take precaution (in our context, to comply with the law). The direction of these changes is frequently ambiguous and depends on the parameters of the model. The parameters that determine the results are different in our model given the criminal context.

We do not think our model is a mere thought experiment. Although cost-shifting is uncommon in criminal litigation, there are significant applications such as the use of RICO proceedings and the financing of enforcement authorities in the United States.

The basic model is developed in Section 2. A more detailed discussion of our results in terms of policy implications is presented in Section 3. Section 4 provides concluding remarks.

2. Basic model

As in the usual Polinsky and Shavell (2000) framework, we start by assuming that each risk-neutral individual chooses whether or not to commit an offense, for example, an environmental violation or financial fraud. The offender's gain from committing the offense is b, which is distributed across the population according to a probability density function $g(b)$ and a cumulative distribution function $G(b)$, where $b \in [0, \infty)$. The fraction of individuals deriving benefits less than b from the crime is $G(b)$. The size of the population is normalized to one. Each offense generates a social damage given by h. The net social harm from the crime is $h - b$ (we take the usual view that the illegal gain is a social gain), where $h < \infty$.

The decision of whether or not to commit an offense generates a signal γ that can be observed by the prosecutor (such as evidence to be used in a criminal trial), and can be regarded as the prosecutor's expectation of obtaining a conviction. The signal γ is itself a random variable distributed according to a probability density function $r_j(\gamma)$ and a cumulative distribution function $R_j(\gamma)$, where $\gamma \in [0, 1]$ and

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[5] As discussed by Hungerford-Welch (2004), the order could be made up to the maximum of the full cost borne by the government. These orders have been used to avoid abuses by the defendant.

[6] See a summary of remedies in civil action for wrongful or mistaken prosecution in Sanders and Young (2007), at chapter 12.

[7] See Departments of Commerce, Justice, and State, the Judiciary, and Related Agencies Appropriations Act, 1998 sec. 617, 18 U.S.C.A. sec. 3006A note; *Masterson v. U.S.*, 200 F.Supp.2d 94 (2002); *Morgan v. Perry*, 142 F.3d 670, C.A.3 (Pa. 1998). The Hyde Amendment provides in relevant part: during fiscal year 1998, and in any fiscal year thereafter, the court, in any criminal case. . . may award to a prevailing party, other than the United States, a reasonable attorney's fee and other litigation expenses, where the court finds that the position of the United States was vexatious, frivolous, or in bad faith, unless the court finds that special circumstances make such an award unjust. Pub. L. 105-199,111 Stat. 2440, 2519 (1997) (reprinted in 18 U.S.C. §3006A, historical and statutory notes).

[8] See *McCray v. State*, 665 So.2d 384, (Fla. 1st DCA 1995); *Wright v. State*, 654 So.2d 252 (Fla. 1st DCA 1995).

[9] We could not find any quantitative analysis of the Hyde Amendment.

[10] For an economic analysis, see Fon and Schaefer (2007).

[11] Notwithstanding, we acknowledge that our model does away with other complications on the application of criminal corporate liability already identified in the economic literature, hence, tempering our results with caution.

[12] See survey by Katz and Sanchirico (2010).