PLAINTIFFS' OFFERS OF JUDGMENT IN FEDERAL DIVERSITY CASES GOVERNED BY SOUTH CAROLINA SUBSTANTIVE LAW

by Bert G. Utsey, III

For almost fifteen years, plaintiffs in South Carolina courts have enjoyed the right to serve Offers of Judgment on defendants and to obtain certain benefits if they succeed at trial after those offers are rejected. In the right case, an Offer of Judgment can be a powerful weapon in the arsenal of a plaintiff's attorney.

But what happens when a case is removed to federal court based on diversity jurisdiction? Does the plaintiff lose this right? Arguably not, as the genesis of the rule, the nature of the right, and the implications of the *Erie* doctrine[1] demonstrate.

In 1985, the South Carolina Supreme Court adopted Rule 68, SCRCP, when it promulgated the South Carolina Rules of Civil Procedure. The rule replaced a state statutory scheme governing "offers to compromise" and was similar to Federal Rule of Civil Procedure 68.[2] Rule 68 gave state court defendants the ability to use Offers of Judgment to gain leverage in settlement negotiations via the threat of cost-shifting penalties for plaintiffs who declined their offers.

In 2005, the Supreme Court amended Rule 68 to grant a similar right to plaintiffs. At the same time, as part of its Tort Reform Act, the General Assembly enacted S.C. Code Ann. § 15-35-400, which mirrors the language of amended Rule

68. Under the amended rule and statute, "any party may … file with the clerk of the court a written offer of judgment signed by the offeror or his attorney, directed to the opposing party, offering to take judgment in the offeror's favor, or as the case may be, to allow judgment to be taken against the offeror, for a sum stated therein…." By their express terms, the amended rule and the statute grant to both plaintiffs and defendants the right to file an Offer of Judgment.

A potential conflict arises because, unlike South Carolina's Rule 68, its federal counterpart does not contain a provision allowing plaintiffs to serve Offers of Judgment. Thus, defendants often argue a plaintiff has no right to offer a judgment in federal court.

Under the well-known Erie doctrine, federal courts are to apply state substantive law and federal procedural law when addressing state-law claims.

Classification of a law as "substantive" or procedural" for Erie purposes is sometimes a challenging endeavor. Guaranty Trust Co. v. York, 326 U.S. 99 (1945), an early interpretation of Erie, propounded an "outcome-determination" test: "[D]oes it significantly affect the result of a litigation for a federal court to disregard a law of a State that would be controlling in an action upon the same claim by the same parties in a State court?" … [T]he Court said in Guaranty Trust: "[W]here a federal court is exercising jurisdiction solely because of the diversity of citizenship of the parties, the outcome of the litigation in the federal court should be substantially the same, so far as legal rules determine the outcome of a litigation, as it would be if tried in a State court." … [T]he "outcome-determination" test must not be applied mechanically to sweep in all manner of variations; instead, its application must be guided by "the twin aims of the Erie rule: discouragement of forum shopping and avoidance of inequitable administration of the laws."[3]

Accordingly, when sitting in diversity, a federal court should undertake an inquiry of whether its failure to apply a state law would either unfairly discriminate against a forum state party or be likely to cause one of the parties to choose federal court over state court.[4]

That analysis, put into the context of plaintiffs' Offers of Judgment, raises the questions of whether a federal court's refusal to recognize the right granted to plaintiffs by South Carolina Rule 68 and Code Section 15-35-400 would unfairly discriminate against a South Carolina plaintiff and/or would lead a defendant to favor federal court over state court.

> ***… plaintiffs' attorneys should be prepared to argue the substantive nature of the right when opposing a motion to strike an Offer of Judgment or in support of a motion for prejudgment interest following a verdict that exceeds the amount of the offer.***

Notably, the fact plaintiffs' right to serve an Offer of Judgment is included in a state rule of civil procedure does not automatically mean it is a procedural right. "Whether a state law provision is substantive or procedural depends *not on where that law is found*, but rather … on whether that particular provision either creates rights and obligations or is so 'bound up with [state-created] rights and obligations' that it must be considered substantive."[5] Therefore, the *Erie* analysis must go beyond the rule's label.

On the other hand, the fact the right is also codified in statute is persuasive evidence that it is a substantive right. By simultaneously enacting Section 15-35-400, the Legislature arguably intended to create an additional substantive right in favor of plaintiffs – that is, the right to recover prejudgment interest on verdicts that exceed offers of judgment. The fact this right was not only included in the amended version of Rule 68 but also in a statute suggests the Legislature intended for it to be a substantive right applicable in courts other than those specifically governed by the South Carolina Rules of Civil Procedure. Otherwise, there would have been no reason for it to codify the amended rule.

Support for this conclusion can be found in a growing number of federal courts which have applied state rules and statutes that grant plaintiffs the right to make an offer of judgment in diversity cases. "[T]he judicial reaction has generally been to apply state law with regard to statutory provisions attaching consequences to rejection of offers [of judgment] made by plaintiffs. This tendency may best be justified on the view that the state provisions genuinely are substantive in that they are intended to and do modify the remedy available under state law."[6]

In fact, the United States Supreme Court appears to have agreed with this conclusion and to have approved this practice. In *Gasperini v. Center for Humanities,* the Court spoke to circumstances when a Federal Rule of Civil Procedure and a state law address the same subject matter – thereby triggering an *Erie* "substantive versus procedural" analysis – and noted: "Federal courts have interpreted the Federal Rules, however, with sensitivity to important state interests and regulatory policies."[7] One of the federal cases the *Gasperini* court cited in support of this conclusion was *S.A. Healy Co.* v. *Milwaukee Metro. Sewerage Dist.,*[8] the holding of which it summarized as: "[S]tate provision for offers of settlement by plaintiffs is compatible with Federal Rule 68, which is limited to offers by defendants."[9]

In *Healy,* writing for the Seventh Circuit Court of Appeals, Judge Posner specifically found that Fed. R. Civ. P. 68 did not preclude operation of a state rule allowing plaintiffs to make offers of judgment. He concluded the state rule did not directly conflict with Federal Rule 68 (or any other Federal Rule of Civil Procedure) and instead reasoned:

Is the Wisconsin rule so likely to dictate outcomes that it will cause a lot of forum shopping (or, if forum shopping is somehow infeasible, cause like cases to be decided differently) unless it is made applicable to diversity cases and so ceases to be a factor in the choice between state and federal court? Is it so entwined with procedures prescribed by the federal rules that it is likely to impair the integrity of federal procedure if it is applied in diversity cases? If the answer to the first

question is 'yes' and to the second 'no,' then we can be reasonably confident that application of the Wisconsin rule in diversity cases would be consistent with the principles of *Erie* and the Rules Enabling Act. Those in fact are our answers, just as they were the answers the Supreme Court gave in [*Walker v. Armco Steel Corp.,* 446 U.S. 740 (1980)] to the question whether a state's rule on when a lawsuit commences for purposes of tolling the statute of limitations is binding in a diversity suit, and just as they are the answers given by the courts that have dealt with rules similar to the Wisconsin rule at issue in the present case.[10]

In addition to *Healy*, many courts that have addressed this specific issue have ruled that state court laws permitting plaintiffs to make offers of judgment create substantive rights which federal courts must recognize and apply under the *Erie* doctrine. *See, e.g., Scottsdale Ins. Co. v. Tolliver,* 636 F.3d 1273 (10th Cir. 2011); *Elgard Corp. v. Brennan Constr. Co.,* 388 F.3d 30 (2d Cir. 2004); *Garcia v. Wal–Mart Stores,* 209 F.3d 1170 (10th Cir. 2000); *Fauber v. KEM Transp. & Equip. Co.,* 876 F.3d 327 (3d Cir. 1989) (holding Pennsylvania Rule of Civil Procedure 238(f) was substantive and applied its "delay damages" provisions in a diversity case); *Armacost v. Amica Mut. Ins. Co.,* 821 F. Supp. 75 (D.R.I. 1993), *aff'd,* 11 F.3d 267 (1st Cir. 1993); *Datapoint Corp. v. M & I Bank of Hilldale,* 665 F. Supp. 722 (W.D. Wis. 1987); *Murphy v. Marmon Group,* 562 F. Supp. 856 (D. Conn. 1983); *Frenette v. Vickery,* 522 F. Supp. 1098 (D. Conn. 1981).

Similarly, other courts have held in different contexts that state law offers of judgment are substantive in nature under an *Erie* analysis. *See, e.g., Horowitch v. Diamond Aircraft Indus.,* 645 F.3d 1254 (11th Cir. 2011); *MRO Communications v. Am. Tel. & Tel. Co.,* 197 F.3d 1276 (9th Cir. 1999); *Tanker Mgmt. v. Brunson,* 918 F.2d 1524, 1527 (11th Cir. 1990); *Kearney v. Auto-Owners Ins. Co.,* 713 F. Supp. 2d 1369 (M.D. Fla. 2010); *see also Sberbank of Russia v. Traisman,* 2016 U.S. Dist. LEXIS 48229 (D. Conn. 2016) (awarding plaintiff interest in light of defendant's rejection of plaintiff's offer of judgment under state statute).
Notwithstanding these authorities, there is no federal case from South Carolina that has specifically ruled on this topic. Therefore, practitioners can anticipate objections to this practice by defendants as well as possible resistance from Federal District Courts.[11]

Defense objections are typically based on the argument that Federal Rule 68 in effect "preempts" South Carolina Rule 68 and/or the rulings by a minority of courts which have accepted the argument that federal courts sitting in diversity should refuse to recognize plaintiffs' offers of judgment although authorized by state law. The most frequently cited of such cases are distinguishable.

For example, *Klawes v Firestone Tire & Rubber Co.*[12] is of questionable validity in light of the Seventh Circuit's later decision in *Healy*, as well as the District of Wisconsin's subsequent criticism in *Datapoint Corp. v. M & I Bank of Hilldale,* wherein the court noted: "The intent of the *Erie* decision was to insure that in all diversity cases, the outcome of the litigation in the federal court should be substantially the same, so far as legal rules determine the outcome of the litigation, as it would if it were tried in a state court. … I conclude that the purpose of the *Erie* decision will be served if [the state offer of judgment statute] is applied in this case…."[13]

Similarly, the holding in *Home Indem. Co. v. Lane Powell Moss & Miller*[14] is cast into doubt by the Ninth Circuit's subsequent opinion in *MRO Communications v. Am. Tel. & Tel. Co.* In *MRO*, the court authorized application of a state offer of judgment statute that permitted recovery of attorneys' fees even though such a recovery was not authorized under Fed. R. Civ. P. 68, finding that

a contrary result "would be unjust and a violation of" the *Erie* doctrine "simply because the forum is federal."[15]

Accordingly, when appropriate, plaintiffs' attorneys should consider filing Offers of Judgment – as authorized by South Carolina rule and statute – in federal diversity cases because the right to do so is substantive in nature and is not precluded by Fed. R. Civ. P. 68. When filing, they should cite S.C. Code Ann. § 15-35-400 in an effort to avoid a knee-jerk reaction that the offer is based upon a procedural rule which does not apply in federal court.

Finally, plaintiffs' attorneys should be prepared to argue the substantive nature of the right when opposing a motion to strike an Offer of Judgment or in support of a motion for prejudgment interest following a verdict that exceeds the amount of the offer.

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1. *See Erie R. Co.* v. *Tompkins,* 304 U.S. 64 (1938) and its progeny.
2. The Reporter's Note states it was "not identical to the Federal Rule" but, per the South Carolina Court of Appeals, there was no discernible substantive difference between the original version of the state rule and the federal rule. *Black v. Roche Biomedical Labs.,* 315 S.C. 223, 433 S.E.2d 21 (Ct. App. 1993).
3. *Gasperini v. Center for Humanities,* 518 U.S. 415, 427-28 (1996) (footnotes and some citations omitted).
4. 12 Wright & Miller, Fed. Prac. & Proc. Civ. § 3001.2 (3d ed., Aug. 2019 update); *see also* J.F. Boyd & R.F. Tarnofsky, *Settlement Agreements in Com. Disputes*, § 20.08 (2d ed. 2019); Note, *Rule 68 and the High Cost of Litigation*, 10 Charleston L. Rev. 475, 492-93 (2010); T.R. Guy & M. Hartmann, *Finding an Erie Conflict Where None Exists – State Offer of Judgment Rules Overwhelmingly Apply in Diversity Cases,* https://works.bepress.com/michelle_hartmann/1/ (Mar. 28, 2008)
5. *Gasperini,* 518 U.S. at 427 n. 7.
6. 60 F.3d 305 (7th Cir. 1995)
7. *Gasperini,* 518 U.S. at 427 n. 7
8. *Healy*, 60 F.3d at 310-11

9. Anecdotally speaking, the author has filed multiple Offers of Judgment on behalf of plaintiffs in the United States District Court for the District of South Carolina, with varying reactions. There is no clear electronic filing category for a plaintiff's Offer of Judgment, which may prompt some administrative confusion or even initial disapproval (for what it's worth, my assistant recommends filing under "Other Filings>Other Documents>Reply>Not to a Motion"). Some federal judges and clerks have rejected electronic filings of plaintiffs' Offers of Judgment; but others have not. Regardless, Rule 68 only requires that a plaintiff file and serve the offer; so, even if an electronic filing is ultimately rejected, one can still argue a plaintiff has complied with the rule.
10. 572 F. Supp. 116 (D. Wis. 1983).
11. *Datapoint Corp.,* 665 F. Supp. at 728-29
12. 43 F.3d 1322 (9th Cir. 1995)
13. *MRO*, 197 F.3d at 1283.
14. 43 F.3d 1322 (9th Cir. 1995)
15. MRO, 197 F.3d at 1283.