MONEY IS THE ROOT OF ALL FEES

Risk Managing the Evil

By Del O'Roark

When it is a question of money everyone is of the same religion.

Voltaire

The two most beautiful words in the world in the English language are "Check Enclosed."

Dorothy Parker

INTRODUCTION

Risk managing fees involves two primary considerations. First, lawyers must have a thorough appreciation for the black letter requirements for determining allowable fee arrangements found in the Kentucky Rules of Professional Conduct (hereinafter Rules or Rule), KBA ethics opinions, and case law. Second, lawyers must use sound business and risk management practices in reaching fee agreements with clients.

This article covers both considerations using the following organization:

Fee Fundamentals
Billing
Collections
Special Fee Issues

Space limitations preclude covering all aspects of each subject. The intent here as in all my articles is to, as concisely as is feasible, present useful information applicable to your daily practice with alerts for problem issues requiring further research.

RISK MANAGING FEE FUNDAMENTALS

The Standard For Setting Fees

The overarching rule for fees provided in the 2009 Kentucky Rule of Professional Conduct 1.5, Fees, is that "A lawyer shall not make an agreement for, charge, or collect an unreasonable fee or an unreasonable amount for expenses."(*emphasis added*)[i] This language is an important change from the language in the 1990 Rule 1.5 that provided "A lawyer's fee shall be reasonable."(*emphasis added*)

The point of the change was to overcome the problem that the 1990 Rule did not include a corollary provision prohibiting fees or expenses that were larger than "reasonable." This omission made it more difficult than intended to impose discipline for excessive fees and expenses. Changing the test to "charging an unreasonable fee or an unreasonable amount for expenses" overcomes this omission, thus making it easier to impose discipline. While the changed language may seem subtle, it is a clear signal that disciplinary authorities will aggressively pursue fee and expense abuse. Risk managing fee arrangements is now even more critical to avoiding bar discipline and malpractice claims.

Calculating Fees

Rule 1.5(a) lists these factors in determining a reasonable fee:

(1) the time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly;

(2) the likelihood that the acceptance of the particular employment will preclude other employment by the lawyer;

(3) the fee customarily charged in the locality for similar legal services;

(4) the amount involved and the results obtained;

(5) the time limitations imposed by the client or by the circumstances;

(6) the nature and length of the professional relationship with the client;

(7) the experience, reputation, and ability of the lawyer or lawyers performing the services; and

(8) whether the fee is fixed or contingent.

A business approach in applying these factors makes justification of a challenged fee straightforward. This includes:

Overall Practice Considerations: Start off with some cost accounting - how much is the minimum you have to make to keep the door open (overhead); *i.e.*, your budget.

Market Factors: What is charged in your practice area - the going rate. (no bar rules establishing minimum fee schedules allowed)

Matter Factors: What fees, costs, and expenses are involved?
- medical/legal
- expert/consulting

- court costs
- discovery/investigative
- travel

Recovering Soft Costs: Treat as overhead or charge to client?

- photocopy, binding
- travel, meals
- long distance telephone
- computer assisted legal research
- local messenger service
- courier service
- postage and fax transmissions
- overtime for staff (hourly rate or + benefits cost factor?)
- housekeeping services *(e.g.*, for meetings, luncheons)
- bill preparation time
- document storage
- proofreading
- talking to the media
- credit card service charges

The type of fee agreement selected for a matter provides a formula for fee calculation. The formula should not be a cover for an excessive fee. Examples of types of fees are:

Fixed Fees:

- *Fixed Fee/ Task Billing / Unit Billing / Project Billing*: A fixed fee, agreed upon in advance for handling a specific assignment – *e.g.*, prepare a will, write an environmental regulation action plan for a business, review a contract, or prepare an opinion letter.

- *Fixed Fee with Incentive Bonus*: A fixed fee established at the outset with an incentive bonus if the lawyer obtains specific results (sometimes called value billing).

Percentage: Used in transaction matters, with the fee as a percentage of the amount involved – *e.g.*, 5% of a commercial real estate transaction price. (not to be confused with a contingent fee.)

Hourly Pricing:

- *Billable Hours*: Fees based on a per hour rate for the lawyer's services.

- *Blended Hourly Rates*: A uniform hourly rate, averaged among the partner, associate, and support staff rates.

- *Discounted Hourly*: A reduced hourly rate, often tied to high volume or granted to major clients.

- *Capped Fee*: An hourly rate, but client is guaranteed that total billing will not exceed a predetermined amount.

Contingency Fees:

- *Contingency*: Amount of a plaintiff lawyer's fee is determined by the outcome of litigation.

- *Reverse or Defensive Contingency*: Defense attorney's fee is based on how much the lawyer saves the client. (*See* ABA Formal Ethics Opinion 93-373, Contingent Fees Based on the Amount of Money Saved For the Client)

- *Modified Contingency*: A reduced hourly rate with additional compensation dependent on the outcome of the matter.

Fee Discounting:

- *Off-the-Top Volume Discounts*: A growing technique used by corporate counsel to get reduced fee arrangements with outside counsel. Also comes up frequently in bidding for government work.

Target Fee: Lawyer and client agree on a target amount for a fee, with a bonus for lawyer if charges come in under target, and a discount to the client on charges above target.

Referral Fees: Fees shared with lawyers outside the firm.

It is important to appreciate that each fee type carries with it the potential for abuse. For example:

♦ A fixed fee can lead to cutting corners, over-reliance on boilerplate, assigning the matter to less experienced lawyers – reducing cost at the expense of quality of service.

♦ Priority of resources given to high-dollar contingency fee cases may lead to low priority or procrastination in less lucrative matters, resulting in professional responsibility problems concerning diligence and client communications, as well as violation of advertising and solicitation rules.

♦ Fees based on billable hours can lead to over-practicing a matter. As one sophisticated client put it, "Lawyers can always think of something more to do that is relevant to my case, but is not necessary." Training of new lawyers can

become a problem with billable hour fees because clients won't accept second chairing – this is not a problem with a fixed fee agreement.

Fee Abuse – Gold Rush Lawyers

The landmark ABA Formal Opinion 93-379 (12/6/93), Billing for Professional Fees, Disbursements and Other Expenses, responded to an increasing public furor over fee abuse that accused lawyers of being opportunistic, predatory, and dishonest. This opinion should be required reading for lawyers. The key points from the opinion are:

■ General Overhead: "In the absence of disclosures ... the client should reasonably expect that the lawyer's cost in maintaining a library, securing malpractice insurance, renting of office space, purchasing utilities and the like would be subsumed within the charges the lawyer is making for professional services."

■ 2 for 1 billable hour fees are per se unreasonable – examples are:
- Travel for one client – work on another matter in flight.
- Simultaneous appearance for three clients.
- Recycled work product.

■ Soft Costs: "… the lawyer may recoup expenses reasonably incurred in connection with the client's matter for services performed in-house such as photocopying, long distance telephone calls, computer research, special deliveries, secretarial overtime, and other or similar services, so long as the charge reasonably reflects the lawyer's actual cost for the service rendered. A lawyer may not charge a client more than her disbursements for services provided by third parties like court reporters, travel agents or expert witnesses, except to the extent that the lawyer incurs costs additional to the direct cost of the third party services."

Kentucky authority on soft costs is contained in KBA Ethics Opinion E-303 (1985) citing *Kentucky Bar Association v. Graves*[ii]:

> In affirming the attorneys censure, the court observed, inter alia: ... billing to the escrow account expenses of law clerks, secretarial assistance ... especially in the absence of a specific agreement with respect to those particular items is improper. ... It is difficult for this court to comprehend an attorney with a full-time practice to expect his clients to meet his overhead expenses. ... It is doubtful if any member of the public who needed a lawyer would employ one who was to charge a standard fee for his legal services and then charge the costs of his secretaries and law clerks as expenses of litigation.
>
> ….
>
> In light of the above authorities we conclude that an attorney who has agreed to represent a client for a statutory or a lump sum or contingent fee should not pass on additional charges for law clerk or paralegal services, in the absence

of an agreement. If agreed otherwise, or in instances in which the lawyer charges an hourly rate, charges for law clerk or paralegal services may be separately stated. Of course, a lawyer may absorb such charges as overhead, which is not billed to the client.

In no event should the services of a law clerk or paralegal be billed as attorney time, since this would amount to a representation that such services were rendered by an attorney.

All Fee Agreements Should Be In Writing – Some Must Be In Writing

The fee agreement

The first risk management action that should be taken with every new matter is the preparation of a comprehensive letter of engagement including fee terms and conditions. A fee agreement at a minimum should:

Clearly identify the client or clients represented – it is absolutely necessary to establish whose interest a lawyer represents.

Specify the scope of the representation – what the lawyer is supposed to do for the client and what is excluded from the representation.

Explain the basis for fee charges to include whether a retainer is required and charges for costs and expenses. This explanation should include consideration of other fee types that may be more advantageous to the client.

Explain the firm's billing procedures to include:
- The client's responsibilities for fee payment.
- How often the client will be billed.
- When payment is expected to be made.
- The firm's options when fees and costs are not paid timely.
- Whether interest will be charged for late fee payment.
- What fees are due if the client discharges the lawyer before completion of the representation. [iii]

Limited space precludes going into further detail on drafting fee agreements. *Legal Malpractice* – 2009 Edition (Mallen & Smith), § 2.10 *Initiating and terminating representations – Engagement agreements* is an outstanding treatment of letters of engagement including several model agreements. Fee terms are described in detail. *Legal Malpractice* and the *ABA/BNA Lawyers' Manual on Professional Conduct* are prime resources for developing ethical fee practices and improving fee agreements. Both are recommended.

The Kentucky Rules of Professional Conduct provide the following requirements for written fee agreements that must be carefully risk managed.

General rule

Rule 1.5 (b): "The scope of the representation and the basis or rate of the fee and expenses for which the client will be responsible shall be communicated to the client, **preferably in writing**, before or within a reasonable time after commencing the representation, except when the lawyer will charge a regularly represented client on the same basis or rate. Any changes in the basis or rate of the fee or expenses shall also be communicated to the client." (*emphasis added*)

Rule 1.5, Comment (2) includes this practical guidance: "Generally, it is desirable to furnish the client with at least a simple memorandum or copy of the lawyer's customary fee arrangements that states the general nature of the legal services to be provided, the basis, rate or total amount of the fee and whether and to what extent the client will be responsible for any costs, expenses or disbursements in the course of the representation. A written statement concerning the terms of the engagement reduces the possibility of misunderstanding."

Contingency fees

Rule 1.5(c) permits fees contingent on the outcome of the matter. Specific requirements are:

- The fee must meet the requirements of Rule 1.5(a).
- The fee agreement **must be in a writing signed by the client**.
- The agreement must include the method by which the fee is determined and the percentage or percentages that accrue to the lawyer in the event of settlement, trial or appeal.
- The agreement must cover litigation and other expenses to be deducted from the recovery; and must state whether such expenses are to be deducted before or after the contingent fee is calculated.
- The agreement must clearly notify the client of any expenses for which the client will be liable whether or not the client is the prevailing party.
- Upon conclusion of a contingent fee matter, the lawyer must provide the client with a written statement stating the outcome of the matter and, if there is a recovery, showing the remittance to the client and the method of its determination.

While not stipulated in Rule 1.5, recommended additional matters to cover in contingency fee agreements to avoid disputes are:

- How the lawyer is paid if the client rejects a reasonable settlement offer and the lawyer withdraws.
- How the lawyer is paid if the lawyer is terminated by mutual agreement or if the client unilaterally discharges the lawyer and obtains other counsel.

- Whether the lawyer is obligated to pursue an appeal if there is an adverse judgment.

Rule 1.5(d) prohibits contingency fee agreements in:

- Criminal cases.
- Domestic relations representations involving the securing of a divorce or the amount of alimony, maintenance, support, or property settlement.

Finally, alternative fee arrangements should be offered if a contingency fee is not in the client's best interest.

Division of fees

Rule 1.5(e) covers division of fees between lawyers not in the same firm, sometimes referred to as fee sharing or fee splitting. The key risk management considerations when sharing fees with a lawyer in another firm are:

- The division must be in proportion to the services performed by each lawyer, or each lawyer must assume joint responsibility for the representation.
- The client agrees to the arrangement and **the agreement is confirmed in writing.**
- The total fee is reasonable.

Comment (7) to Rule 1.5 concerning division of fees with another lawyer not in the same firm provides in part: "Joint responsibility for the representation entails financial and ethical responsibility for the representation as if the lawyers were associated in a partnership. A lawyer should only refer a matter to a lawyer whom the referring lawyer reasonably believes is competent to handle the matter." The days of "refer it and forget it except to collect a fee" are over. A referring lawyer dividing fees must carefully monitor a referred matter to prevent malpractice and avoid a claim.

Fees paid with an interest in the client's business or other nonmonetary property

Rule 1.8, Conflicts of Interest: Current Clients: Specific Rules, contains strict guidance on doing business with a client. The concern is expressed in Comment (1) as follows:

> "A lawyer's legal skill and training, together with the relationship of trust and confidence between lawyer and client, create the possibility of overreaching when the lawyer participates in a business, property or financial transaction with a client, for example, a loan or sales transaction or a lawyer investment on behalf of a client.

The Comment expressly includes fees as covered by 1.8(a):

It does not apply to ordinary fee arrangements between client and lawyer, which are governed by Rule 1.5, although **its requirements must be met when the lawyer accepts an interest in the client's business or other nonmonetary property as payment of all or part of a fee.** (*emphasis added*)

Good risk management requires scrupulous compliance with Rule 1.8(a) when accepting an interest in a client's business or other nonmonetary property for a fee.[iv] Specifically, the Rule provides:

(1) the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing in a manner that can be reasonably understood by the client;

(2) the client is **advised in writing** of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent legal counsel on the transaction; (*emphasis added*) and

(3) the client gives informed consent, **in a writing signed by the client**, to the essential terms of the transaction and the lawyer's role in the transaction, including whether the lawyer is representing the client in the transaction. (*emphasis added*)

Do not accept an interest in a client's business or other nonmonetary property as payment of all or part of a fee before you read and comply with Rule 1.8(a) and Comments (1 - 4).

SMART BILLING AVOIDS FEE DISPUTES

The first line of defense in avoiding fee disputes is a comprehensive written fee agreement. The second line is to bill in a way that is fair, understandable to the client, and consistent with good business practices.

Common Billing Mistakes

- The bill is as big as the client’s file – looks like over-practicing the matter.
- Client gets a large bill that is the first thing the client has heard from the lawyer since the initial interview.
- Secret identities – no names and no billing rates for the work done.
- Over-qualified personnel for the work or conversely, charging lawyer rates for administrative work.
- Too many meetings, telephone calls, and research hours – looks like over-practicing the matter.
- Billing for several lawyers reviewing or preparing to discuss the file – looks like over-practicing the matter.

- Billing for several lawyers attending a meeting when one would have been adequate – looks like over-practicing the matter.
- Billing for "soft costs" without the client's prior agreement and general overhead costs (heat, air conditioning, etc.).
- Itemized bills with generic terms such as "phone call" or "meeting" with no substantive information.
- All telephone calls take exactly .3 hours; all dollar amounts are nice round numbers or end in five; and inserted along with all the routine itemized expenses is a charge for expert witness fees of several thousand dollars.
- Billing for billing – this adds insult to injury.
- A too-quick billing reduction if client complains strongly implies that the lawyer must be overcharging.
- Billing out of cycle with the client's preference. [v]

Good Billing Practices

The single best billing practice is to bill early and bill often. Whatever billing cycle you are using, stick to it religiously. The following is a helpful checklist of other good billing practices:

- Improve client communications – at the outset explain the entire billing process.
- Prepare a client for the total cost of legal services being provided.
- Prepare written fee letters outlining the specific terms of an engagement.
- Use retainer arrangements, especially when a client's ability to pay is in question.
- Identify for the client the people being assigned to work on a matter.
- Use the billing process to communicate details of the work performed.
- Reach an agreement about what time and costs will be charged to a client and what will not be charged.
- Discuss billing formats and what information will make invoices easier for the client to process.
- Provide a budget, as a matter of firm policy, on all matters in excess of a specified amount.
- Schedule periodic meetings with clients to discuss ways to improve service.
- Review invoices to ensure that they contain no mistakes.
- Send regular reminders for invoices that remain unpaid. [vi]

Anthony E. Davis, a highly regarded risk management expert, in his article *How to Better Manage the Billing Process*[vii] offers the following advice on how to eliminate billing fraud, avoid fee disputes, and get paid:

Establish strict policies regarding accuracy in timekeeping and recording of time. Do not require minimum hours to be billed to clients. To do so encourages bill padding.

Enforce frequent time reporting – preferably daily.

- Monitor the billing process with internal audits and independent review of all expenses either claimed by a lawyer or billed to a client.

- Send bills that, in addition to reflecting charges, demonstrate the progress made in the client's matter during the billing period.

- Avoid billing for overhead items. Only bill or have the client pay directly out-of-pocket third-party expenses.

- Send a cover letter with a bill that includes:
  1. A thank you for past payments.
  2. A simple "plain English" summary of how the work performed as described in the bill advanced the client's interest toward the desired outcome.
  3. An explanation of the activities planned for the next month and how these advance the client's interest toward the desired outcome.
  4. An invitation for the client to call with any questions regarding the bill.

COLLECTING FEES

The Easy Way – Get a Retainer

A fee agreement on retainers should cover:

- Whether a retainer is refundable.
- Will it bear interest, and if so, for whom.
- Whether the retainer is applicable to fees, expenses or both.
- Whether it must be replenished at some point in time – sometimes referred to as an "evergreen retainer."[viii]

The three basic retainer agreements are:

- ***General Retainer/Right to Call****:* A fixed sum for the right to get immediate service. It is earned when received and deposited in the lawyer's operating account.

- ***Advance Retainer:*** A specified fee in advance for specified services. It is earned as services are provided. It is deposited in the lawyer's client trust account and withdrawn as earned.

- ***Non-refundable Retainer*:** A fee paid in advance of services being rendered and is non-refundable if the client terminates services. It is earned when received and deposited in the lawyers operating account. Rule 1.5 (f) provides: "A non-refundable retainer fee agreement **shall be in a writing signed by the client** evidencing the client's informed consent, and shall state the dollar amount of the retainer, its application to the scope of the representation and the time frame in which the agreement will exist." (*emphasis added*) (*See also* Rule 1.15 on non-refundable retainers.)

Lawyers should get retainers routinely – especially in matters requiring immediate intensive work, or when the ability of a client to pay is questionable. Clients who have not paid a retainer or fee do not yet have a financial stake in the matter. It gives them a different attitude about paying fees. Retainers avoid this attitude and facilitate smooth fee collection.[ix]

The Easy Way – Accept Credit Card Fee Payments

If you are not accepting payment fees, expenses, and retainers by credit card, you are missing one of the surest ways to get paid and avoid fee disputes. KBA E-426 (3/23/2007) describes the conditions for Kentucky lawyers to accept credit card payments. The opinion points out that:

> Consumers rely heavily upon the use of credit cards and other forms of electronic payment and the Kentucky Rules of Professional Conduct authorize lawyers to accept credit cards for the payment of fees. See SCR 3.130(7.05) and KBA E-172 (1977). As the use of credit cards and other forms of electronic payment become more common, lawyers will need to be increasingly cautious in structuring these arrangements to ensure compliance with all of their ethical obligations, particularly those relating to client communication, segregation of client funds and accounting.

The opinion addresses whether credit card service charges may be passed on to the client:

> A number of ethics committees in other jurisdictions have considered this issue and concluded that lawyers may pass reasonable transactional costs of credit card use on to clients if the client agrees to such a charge. …. SCR 3.130(1.5) provides that "the basis or rate of the fee [*and expenses for which the client will be responsible*][x] should be communicated to the client, preferably in writing, before or within a reasonable time after commencing the representation." Because the practice of passing service charges on to the client deviates so dramatically from the commonly accepted practice in the commercial world, lawyers have an unusually high burden in making sure the client fully understands the consequences of electing to use a credit card. The client must be advised that he or she will be responsible for an amount in excess of the billed charge if a credit card is used and what the additional

> charge will be, as well as any other information that may be necessary to adequately inform the client of the nature of the payment arrangement. Moreover, although the current rules do not require that such communications be in writing, it is the Committee's view that, especially where an additional charge is added for credit card use, both clients and lawyers will be best served if the agreement is in writing.

While the soft cost of credit card service charges may be passed on to clients with full disclosure and informed consent, this is not the best business practice and may conflict with some credit card providers' conditions for service. Accept the cost as part of practice overhead expenses.

Read KBA E-426 and get started with credit card fee collection.

The Easy Way? – Novel Fee-Financing Plans

Over the years a number of client fee-financing plans for payment of lawyer fees have been attempted. They usually involve a lawyer referring a client to the financing plan, providing client information to the plan, with some form of fee charged to the lawyer for the client service or payment to the lawyer for a client referral. Space precludes a detailed analysis of financing fees. What follows is a list of the Rules that should be considered before participating in any such plan:

- Disclosing or improperly using client confidential information without consent (Rules 1.6; 1.8(b)).
- Providing financial assistance to client in connection with pending litigation (Rule 1.8(e)).
- Sharing fees with a nonlawyer (Rule 5.4).
- Charging excessive fees (Rule 1.5).
- Retaining unearned fees if lawyer withdraws or is discharged (Rule 1.16(d)).
- Third-party paying fees without the client's permission (Rule 1.8(f)).
- Representing a client when services may be affected by lawyer's own financial, business, or personal interest (Rule 1.7(b)).

When in doubt about a novel fee-financing plan, call the KBA Ethics Hotline for advice.

The Hard Way – Charging Liens

A charging lien is the right of the lawyer to have payment of fees secured by a judgment the client recovers as a result of the lawyer's efforts. Rule 1.16, Declining or Terminating Representation, Comment (10) makes it clear that in Kentucky, lawyers are not allowed to file a retaining lien on the client's file until fees are paid, but may only obtain a charging lien:

> The lawyer may not condition return of the client's file, papers, and property upon payment of a fee. KRS 376.460 gives a lawyer the right to have payment of fees secured by a judgment the client recovers as a result of the lawyer's efforts.

Charging liens are an exception to the rule against taking a proprietary interest in a cause of action as reflected in Rule 1.8(i):

> A lawyer shall not acquire a proprietary interest in the cause of action or subject matter of litigation the lawyer is conducting for a client, except that the lawyer may:
> (1) acquire a lien granted by law to secure the lawyer's fee or expenses. . . .

The Hard Way – Suing A Client For Fees

For a number of years, Lawyers Mutual has advised extreme caution in suing a client for fees. One authority estimates "that at least 20%, and perhaps as much as 30%, of all malpractice claims and counterclaims, are directly or indirectly attributable to disputes over legal fees and expenses."[xi] Many experienced Kentucky lawyers have a policy of never suing a client for fees. One recommended policy is "… a law firm should consider a rule that no suits for fees will be filed to collect fees, and no threats to do so or use collection agencies will be made. Any exception to the rule should be approved by the management committee, another governing body, or another lawyer in a small firm."[xii] In considering an exception to not suing a client for fees, use the following checklist that Lawyers Mutual published in its Spring 2009 newsletter:

- Was a good result obtained in the underlying case?
- Is the size of the fee sufficient to warrant the risk of a malpractice counterclaim?
- Has a disinterested lawyer of experience reviewed the file for malpractice?
- How reasonable were the fees?
- Will work on the matter as reflected on billing withstand cross-examination?
    - Does billing indicate over-practicing?
        - Too many meetings, telephone calls, and research hours.
        - Billing for several lawyers reviewing or preparing to discuss the file.
        - Over-qualified personnel for the work.
    - Are entries vague?
        - No names and no billing rates for the work done.
        - Itemized bills use generic terms such as "phone call" or "meeting" with no substantive information.
    - Subject to being misconstrued?
        - Billing for "soft costs" (copying, fax) and general overhead (heat, air conditioning).
        - All telephone calls take .3 hours; all dollar amounts are nice round numbers or end in five.

- How much non-billable time will be spent defending any malpractice counterclaim?
- Will any judgment obtained be collectible?
- Will you recover more than you spend?

SPECIAL FEE ISSUES

Contract Lawyers

Contract lawyer fee ethics questions concern sharing fees with contract lawyer referral agencies and dividing fees with lawyers not a member of the firm. In *Oliver v. Board of Governors, Kentucky Bar Ass'n*, 779 S.W. 2d 212, (Ky. 1989) the Kentucky Supreme Court provided guidance on both questions:

> ***Referral Agency Fees*****:** The professional responsibility concern is that the referral agency not exercise any control over the contract lawyer's independent professional judgment by controlling the money. In *Oliver* the Supreme Court advised that a referral agency could be paid a fee as a percentage of or in proportion to the lawyer's compensation, provided the hiring firm pays the contract lawyer directly for legal services. If the firm passes on the referral fee to the client, the client must be informed by itemizing it on the bill.
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> ***Division of fees and disclosure to clients*****:** Stories of irate clients learning after the fact that contract lawyers were used in their matter are frequent. Simply put, clients feel cheated. The question of whether this information should be disclosed to clients in Kentucky is answered in *Oliver*. The Supreme Court recommended "disclosure to the client of the firm's intention, whether at the commencement or during the course of the representation, to use a temporary attorney service on the client's case, in any capacity, in order to allow the client to make an intelligent decision whether on not to consent to such an arrangement." This disclosure in a fee agreement should serve to comply with the fee division written disclosure requirements of Rule 1.5(e) (2))…."[xiii]

ABA Formal Opinion 00-420 (11/29/2000) addresses the question of surcharges for use of contract lawyers. I know of no Kentucky authority on point. The ABA opinion concluded that a surcharge could be made if the contract lawyer is billed as legal services and if the fee is not unreasonable. If billed as an expense, the client may be billed only the costs of such services including those associated with obtaining the contract lawyer's services. This is a good question for the KBA Ethics Hotline.

Of Counsel

Of counsel fee questions concern dividing fees with lawyers not a member of the firm, thereby invoking the division of fee requirements of Rule 1.5(e). I can find no Kentucky authority on point. There is a split of authority in other states. A balanced approach is "the rules governing division of fees between lawyers in different firms apply

unless the of counsel lawyer in effect functions as a partner or associate in the affiliated firm." [xiv]

Disclosure of counsel involvement in a letter of engagement is a professionally responsible way of complying with Rule 1.5(e) to include the written fee disclosure requirements of the Rule.

Interim Fee Increase

There is no express prohibition to increasing a fee during a representation, but doing so may not be prudent or good risk management. Modification of a fee agreement to a lawyer's benefit during a representation is generally unenforceable."[xv] Courts are suspicious of fee increases after the representation has begun and the lawyer is in a fiduciary relationship with a client. The client is then perceived as being under a great disadvantage in negotiating an interim increase for fear of the lawyer withdrawing.[xvi] Good risk management is to honor the original fee agreement. If the representation is expected to require a lengthy period to complete, include in the fee agreement conditions for modifying the fee. At a minimum do not surprise a client with a unilateral increase.[xvii]

The one Kentucky case located dealing with an interim increase in fees concerned a lawyer who was suspended from practice for two years in part for attempting to change a fee agreement to a contingency fee after indicating he would charge an hourly rate.[xviii] Lawyers should assume that Kentucky courts will not look favorably on interim fee increases that are not covered in the initial fee agreement and are unfair to the client.

Fee Agreements That Mislead A Client Or Infringe On A Client's Control And Authority Over a Case

It is not uncommon for fee agreements to attempt to usurp a client's unqualified right to decide whether to settle a case. A gross example of such an attempt was a fee agreement that provided that both the lawyer and the client had to consent to settle the claim – a clear violation of Rule 1.2(a).[xix]

Some fee agreements attempt to discourage clients from discharging the lawyer by penalizing them with significant fee and expense increases if they do. This is often seen in contingency fee agreements. Rule 1.16, Declining or Terminating Representation, Comment (4) provides in part: "A client has a right to discharge a lawyer at any time, with or without cause, subject to liability for payment for the lawyer's services." Any client condition on discharge beyond that in a fee agreement is a violation of the Rule.

Finally, some fee agreements have 'escape' clauses that provide that the lawyer may withdraw at any time fees are not paid as agreed. This is a misleading condition because there are circumstances when a lawyer may not withdraw in spite of not being paid. If the matter is before a court, the lawyer must seek permission to withdraw and

may be ordered by the judge to continue the representation. Do not use escape clauses in fee agreements that:

- Purport to authorize lawyer withdrawal under circumstances that the Rules of Professional Conduct do not permit.
- Mislead the client as to the lawyer's fiduciary duty to continue the representation under certain circumstances.
- Use a client consent stipulation authorizing withdrawal under specified circumstances if it implies that the client has no right to object to withdrawal because of material adverse effect.
- Predicate withdrawal on failure to follow advice relating to ethics, strategic, and tactical matters if the effect is to require the client to accept the lawyer's advice on issues that the ethics rules reserve for the client to decide (*e.g.*, settlement).[xx]

SUMMING UP

Reasonable fee agreements that clients understand and accept, even if unorthodox, are your best protection against a fee dispute, bar complaint, or malpractice claim. If your fees: (1) are based on the eight criteria in Rule 1.5; (2) use realistic overhead and expense factors; (3) are covered in a fair fee type; (4) are put in writing; (5) are carefully explained; and (6) are billed using good billing practices, you should have little problem over the reasonableness of your fees or their collection.

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[i] SCR 3.130(1.5) Fees (a).

[ii] 556 S.W.2d 890 (Ky. 1977).

[iii] ABA/BNA Lawyers' Manual on Professional Conduct, Fees, *Fee Agreements*, §41:101 *et seq*. The Manual provides a thorough treatment of fee agreement issues and is the place to start in researching fees.

[iv] Reinforcing this view is ABA Formal Opinion 02-427 (5/31/2002), Contractual Security Interest by a Lawyer to Secure Payment of a Fee, that concluded, "A lawyer who acquires a contractual security interest in a client's property to secure payment of fees earned or to be earned must comply with Model Rule 1.8 (a)."

[v] Amy Stevens (Wall Street Journal), Larry Bodine (Lawyers Weekly USA), and Jay Foonberg (Lawyers Weekly USA) have all written articles listing their 10 favorite "Billing Bloopers." This list is a composite of their ideas and some of my own.

[vi] From Howard L. Murdick's article *Better Communication Increases the Likelihood That Bills Will Get Paid* (The National Law Journal, 12/20/1993, p. S3).

[vii] *Lawyer to Lawyer,* Ed. XIX, 9/2002, Chubb & Son.

[viii] *Legal Malpractice* – 2009 Edition, Mallen and Smith, §2:10, page 137.

[ix] The October 2008 issue of the ALI/ABA *The Practical Lawyer* has the helpful article *"Creating The (Almost) Perfect Retainer Agreement (With Form)"* by Lori A. Colbert. It includes a model form and a practice checklist. It is available on the Internet for $19.00. Just Google *The Practical Lawyer* (last viewed on 8/16/2009.

[x] This language was added in the 2009 revision of the Rules.

[xi] *Legal Malpractice* – 2009 Edition, Mallen and Smith, §2:20, page 217.
[xii] *Ibid* at page 219.
[xiii] This paragraph and the preceding one are extracts from the Bench & Bar article *Barrister in a Box*, KBA Bench & Bar, Vol. 61 No. 2, Spring 1997, page 86. To read the article go to www.lmick.com, click on Risk Management, Bench and Bar Articles, and select the article.
[xiv] ABA/BNA Lawyers' Manual on Professional Conduct, Of Counsel, §91:506, *Division of Fees*.
[xv] ABA Annotated Model Rule of Professional Conduct, 6th Edition, *Modification of Agreements*, page 78.
[xvi] Rule 1.5, Comment (5) adopts this view in the context of fixed fees: "… a lawyer should not enter into an agreement whereby services are to be provided only up to a stated amount when it is foreseeable that more extensive services probably will be required, unless the situation is adequately explained to the client. Otherwise, the client might have to bargain for further assistance in the midst of a proceeding or transaction."
[xvii] *See generally*, ABA/BNA Lawyers' Manual on Professional Conduct, Fees, *Fee Agreements* §41:114 and §41:316.
[xviii] *Ky. Bar Ass'n. v. Basinger,* 53 S.W.3d 92 (Ky. 2001).
[xix] *See generally*, ABA Annotated Model Rule of Professional Conduct, 6th Edition, *Interfering with Client's Control of Case,* page 81.
[xx] See the Bench & Bar article "*How to Fire a Client*" for more information on escape clauses. KBA Bench & Bar, Vol. 65 No. 3, May 2001, page 31. To read the article go to www.lmick.com, click on Risk Management, Bench and Bar Articles, and select the article.