SURROGACY WARS THE IRA-TOLLAH CLINTON'S LAWYERS

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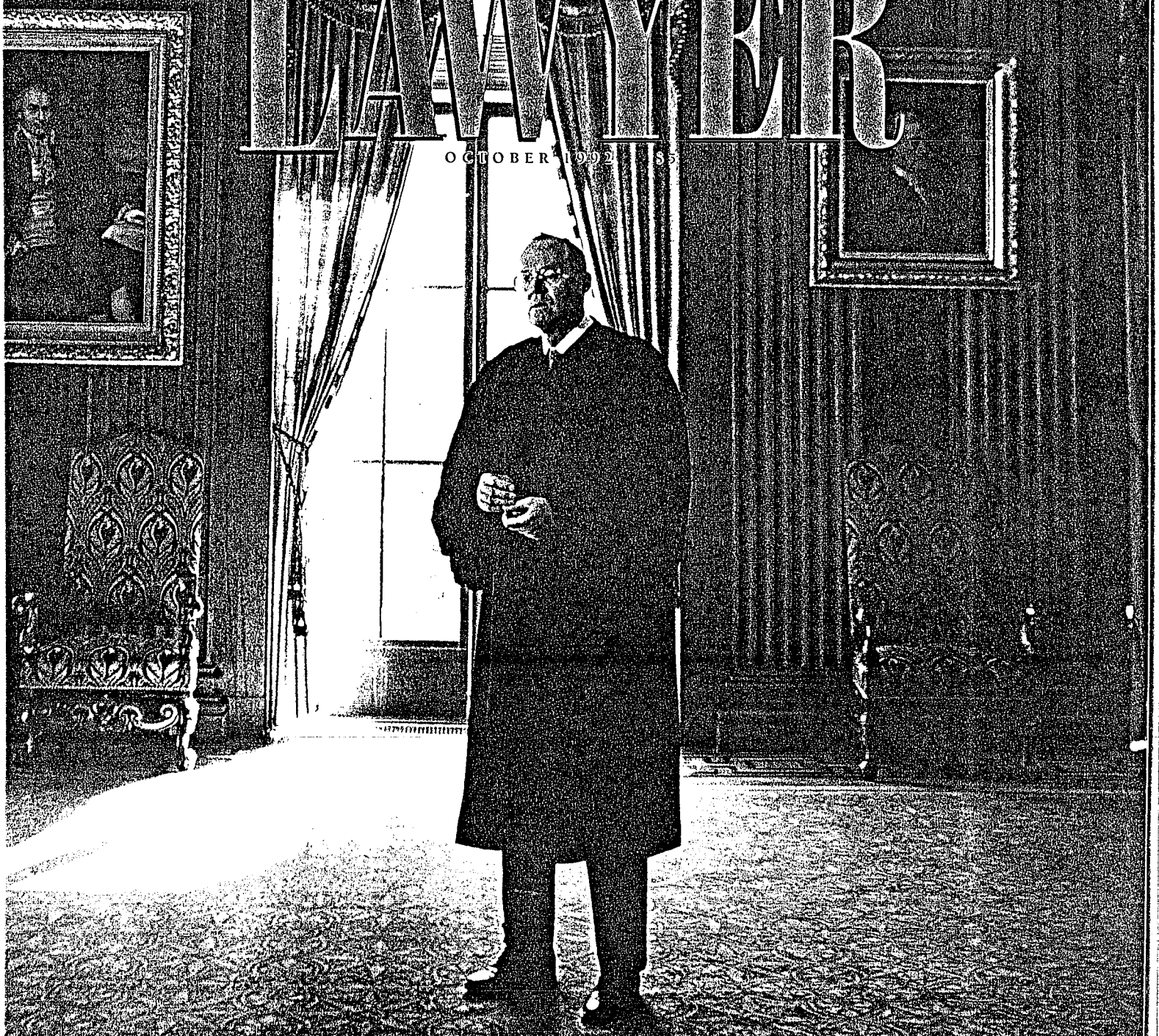
LAWYER

OCTOBER 1992 $3.5



MAN IN THE MIDDLE

Anthony Kennedy is the justice to watch this term

Drafting Airtight Fee Agreements

Statutory requirements go beyond what form books have to offer.

BY RICHARD A. ZITRIN

ALMOST EVERY California form book contains sample fee agreements. The State Bar also has published fee-agreement forms. Yet when lawyers fold these forms into their own fee contracts, the results often fail to measure up to the requirements of the Business and Professions Code. Why do California lawyers have so much trouble drafting proper fee agreements? And how can they do a better job?

The answers to these questions are important for both clients and lawyers. As the State Bar points out in its fee-form booklets, Business and Professions Code sections 6147 (governing contingency fee contracts) and 6148 (covering hourly fees) are "consumer protection legislation" and therefore "must be examined in the light most favorable to the client." This means that in addition to a recitation of the fee, the client is entitled to an agreement containing "all additional information necessary to make the disclosure complete, accurate, and not misleading."

This heightened scrutiny puts attorneys on notice that their obligations to their clients include observing the statutes' disclosure requirements. In addition, failure to abide by the requirements can have serious financial consequences. Noncompliance "with any provision" of either section makes the fee contract voidable. The lawyer is still entitled to collect a "reasonable fee," but that may be very different from the benefit of the bargain set forth in the agreement.

Generally fee agreements are governed by rule 4-200 of the Rules of Professional Conduct, which prohibits "unconscionable" fees or fee contracts. "Conscionability" is determined according to 11 factors listed in rule 4-200(B). But when the client voids an agreement under section 6147 or 6148, the only benchmark is the "reasonable fee" language of the code, and there is no definition of what is "reasonable." As a practical matter, this issue will ultimately be decided by a jury in a fees lawsuit—a jury whose members are far more likely to be peers of the client than of the lawyer.

Lawyers can avoid fees lawsuits and mandatory fee arbitrations by following two straightforward rules: First, never assume the form you are using is correct; second, read the code sections carefully and draft agreements accordingly.

One problem with using printed or published fee-agreement forms is that many are obsolete. Sections 6147 and 6148 are relatively recent statutes.

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Forms that predate them are obviously suspect and should be discarded or at least studied carefully.

In addition, some forms—usually those handed down from generation to generation—are simply wrong. For example, some of them still contain "retaining liens," which permit a lawyer to keep a client's file until the bill is paid; yet California courts and ethics committees have consistently come out against retaining liens, holding that the file belongs to the client.

Finally, most form agreements are not designed to cover many of today's fee arrangements. The author of the numerous fee agreement forms contained in Matthew Bender's three-volume *California Attorney Practice* has acknowledged that the forms were intentionally kept simple and should be used only for guidance. Indeed, the publisher has announced it will no longer update these volumes, allowing them too to become obsolete.

In 1987 the State Bar approved hourly and fixed fee forms to coincide with the passage of section 6148, the hourly fee statute. Contingency fee contracts usually require more sophisticated drafting skills. Only in March of this year, however, 10 years after section 6147 was passed, did the bar publish contingency fee contract forms. Both sets of forms are very general and are preceded by numerous disclaimers, including this one: "[These] are not mandatory forms. They enjoy no preferred status. They create no minimum standards. They do not presume to address every setting...nor do they contain every term...."

This disclaimer alone is enough to make one wonder if using the forms is worth the trouble. And yet the disclaimer is understandable, since the forms are basic, unlike computer forms, which provide paragraph choices enabling an agreement to be tailored to individual needs.

LAWYERS MUST recognize that anything more complicated than a simple hourly, fixed or contingency fee contract between a client and a single law firm will require more work than just filling in a form. Nowadays agreements may need to cover such situations as hybrid hourly and contingency fees, fee payments in structured settlements, fees paid by another or involving indemnification, different fee schedules for different causes of action or for different attorneys, and awards of statutory fees. A look at a few contingency fee situations will illustrate the problems lawyers face in ensuring their fee agreements pass muster.

In response to the increasing costs and problematic results of contingency case litigation, many lawyers have begun charging reduced hourly rates plus a contingency fee if the case is successful. Unless these agreements give the client a simple credit against the contingency fee for the hourly sums paid ("If we win, the $100 per hour you paid me will be credited against my percentage fee"), careful drafting is necessary to provide the full and accurate disclosure that section 6147 requires. A lawyer who intends to keep the hourly payment while charging an additional percentage of the recovery must unambiguously set forth that understanding.

A more subtle, but necessary, component of such an agreement is defining the method used to compute the contingency fee. For example, if the recovery is $100,000 after costs, and the client has paid $20,000 in hourly fees, will the contingency fee be computed on $100,000 or $80,000? Merely saying the computation will be based on the "net recovery," or a similar term, does not clarify the situation since the lawyer may see the net as $100,000, while the client may consider the net $80,000, after costs and fees are deducted.

Section 6147(a)(2) requires a fee agreement to contain "a statement as to how disbursements and costs incurred...will affect the contingency fee and the client's recovery." This means not only that the method of computation must be clear and unambiguous but that an explanation of the effect on the client's eventual recovery must also be included. In the example above, the fee agreement must explain, first, that the contingency fee will be based on the total recovery after costs are deducted but without deducting the fees already paid; and, second, that this method of calculation will give the client a lower recovery than if the percentage fee were computed after deducting the hourly fees.

Other fee-agreement problems can be resolved only by anticipating outcomes that may not be obvious at the time the agreement is reached. For instance, structured settlements are far more common these days than they were 20 years ago. If there is *any* possibility of a structured settlement and the lawyer expects to get the entire fee as soon as the case settles, the fee agreement must explicitly provide for this. Again, the agreement must explain how the computation of the attorney's fee will affect the client's recovery, by diminishing the amount available for annuity or by deferring some or all of the client's compensation until the lawyer is fully paid. Lawyers also must take care to avoid creating a conflict of interest between the attorney, who wants all fees at settlement, and the client, who may best be served by a structured annuity that provides little "up-front" money.

Similarly, if there is any possibility, however remote, of receiving statutory fees, the fee agreement should provide for this. Statutory fees usually arise in such cases as workplace discrimination, section 1983 civil rights claims and Song-Beverly "lemon law" matters. At the least, an addendum should be drafted as soon as the lawyer realizes a statutory fee could be awarded.

Ordinarily it is clear what is meant by a percentage of a "recovery," "settlement" or "judgment." This clarity disappears, however, when lawyer and client are left trying to determine if an award of statutory fees is part of the recovery or a direct payment to the lawyer. And if the fees are awarded to the attorney, are these fees a bonus above the contingency percentage or must the client be credited for these sums?

Suppose, for example, that in an age-discrimination case with a one-third contingency fee, a client gets a $100,000 judgment and the attorneys are awarded $35,000 in fees. Do the attorneys receive only the $35,000, since that sum is more than one-third of $100,000? Are they entitled to $45,000, representing one-third of the total awarded, judgment plus fees? What if the fee award was $65,000? Are they entitled to keep it all, since it was awarded to them? Or may they only receive one-third of the total of $165,000, or $55,000? What if these sums are not awards but settlement offers?

These and other questions can be answered only by a fee contract that contains an explicit and unambiguous explanation of how the fees and the client's recovery will be computed. Since the agreement will be interpreted "in the light most favorable to the client," anything less could have expensive consequences for the lawyer. ❖