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Simplifying Legal Fees

By defining basic types of fee arrangements, a strong foundation can be laid to understand legal fees

By David M.M. Bell

This article continues the commentary on attorney-client fees and fee agreements. Last month's article, "The Rigors of Fee Agreements," focused on written fee agreement requirements and on fee amounts.

This month, I address fee arrangements and fee payments, including situations where an attorney takes an "advanced" or "nonrefundable" fee from a client. How a legal fee is characterized - what it is called - makes a huge difference. It affects how and when the legal fee is earned. It affects how and when fee payments are taken. It affects the degree to which fee payments may be refundable to clients.

I have lectured attorneys on fees, trained fee arbitrators for the State Bar's fee arbitration program and responded to questions from innumerable attorneys on the State Bar's Ethics Hotline regarding fees and fee agreements. My experience is that many attorneys are unclear regarding the nature and effect of different types of legal fees and fee arrangements. They do not understand the distinctions between fee types, and often confuse and mischaracterize them. Attorneys have complained to me that they find the entire subject of legal fees to be unnecessarily complicated and complex.

This should not be. In my opinion, legal fees and fee arrangements can be comprehended and presented in a way that eliminates much of the confusion.

To begin, one must break down fee arrangements into their generic types. By identifying and defining basic generic types of fee arrangements, a simple, yet strong foundation can be built to a better understanding of legal fees.

Types of fee arrangements

Attorneys employ a wide variety of terms in naming their fees and fee arrangements. I have heard of "flat," "fixed" "hourly," "contingent," "true retainer," "classic retainer," "retainer," "minimum," "non-refundable," "advance," "security," "mixed," and "evergreen" fees.

With so many different terms being tossed about (often loosely or incorrectly), it is imperative to define a common terminology. This gets everyone on the same page, using the same language, and permits coherent discussion.

The most concise description of generic fee arrangements that I have found is in proposed California Rule of Professional Conduct 4-110 (Advance Payment of Legal Fees). This proposed

rule, circulated for public comment in 1997, concerned the handling and placement of advance fee payments. Although the proposed rule was controversial and was never adopted, the discussion section to the proposed rule provides an excellent commentary on fees and fee arrangements.

The discussion states: There are four basic types of generic fee arrangements: hourly, flat/fixed, contingency, and true retainer. All fee arrangements, however characterized, fall into one or more of these four categories:

1. An hourly fee arrangement is one in which the lawyer agrees to provide legal services at a defined hourly rate. The fee may be paid prior to or following performance of services.

2. A fixed or flat fee arrangement is one in which the lawyer agrees to provide a specific service, result or product for a predetermined fee. The fee may be paid prior to or following performance of services.

3. A contingency fee arrangement typically provides that if the client is successful in the matter being litigated or negotiated, the lawyer will receive a defined percentage of the recovery. During the course of representation, the lawyer does not bill the client for services but takes his or her fee out of the settlement or judgment recovered for the client. This fee arrangement may include a security payment to guarantee the future payment of the contingency fee.

4. A true retainer fee arrangement provides for a fee paid to the lawyer solely for the purpose of ensuring that availability of the lawyer for the client's matter or for a specific period of time and is not tied to the performance of any specific legal service. (See rule 3-700(D)(2).)

Where the fee is tied to some specific service, such as reviewing or drafting client documents or representing or advocating on behalf of the client, it is not a true retainer fee arrangement, but is either an hourly or flat fee arrangement. A true retainer is considered to be earned upon receipt and, therefore, is not a fee paid in advance. (See *Baranowski v. State Bar* (1979) 24 Cal.3d 153 [154 Cal.Rptr. 752].)

An individual fee arrangement may provide for any combination of an hourly, flat/fixed, contingent or true retainer fee arrangement.

I agree with this. Leaving aside pro bono representations, where there is no fee, I agree that there are just four basic types of generic fee arrangements. I believe that all fee arrangements, however characterized, will always fall into one of these four basic categories.

I also agree that an attorney may ethically combine different types of generic fee arrangements within a single fee contract. Thus, an attorney's fee contract may call for a true retainer to secure the attorney's availability while simultaneously providing for an hourly or flat fee to cover specific services.

A fee contract may combine a contingency and hourly fee arrangement. Such "mixed" fee arrangements can benefit both attorney and client and are not improper.

Attorneys should review their standard fee contracts with these four generic fee arrangements in mind. They should identify and verify their underlying fee arrangement(s).

Is your contract really saying what you want it to? Make sure that your contract terminology correctly describes and matches your underlying fee arrangement(s).

Distinguishing fee payments from generic fee arrangements

A mistake some attorneys make is to consider "advance fees" and "non-refundable fees" as generic types of fee arrangements. These terms denote types of fee payments and should not be confused with terms describing types of fee arrangements.

When used in a fee contract, terms such as "advance" and "non-refundable" are better recognized as contractual fee payment conditions. They address the timing and refundability of fee payments. They do not constitute the underlying fee arrangement(s).

Advance fees

Where a fee contract calls for an "advance fee" payment, the underlying fee arrangement could be either an hourly or flat/fixed fee arrangement. The term "advance fee" means only that the legal fee is to be paid in advance of the provision of legal services. The term "advance fee" does not, by itself, define or describe the underlying fee arrangement.

In practice, it is common for attorneys to take advance fee payments in hourly and flat fee representations. They may charge against the advance fee (commonly done in hourly fee representations) or otherwise use the advance fee during the course of representation.

Attorneys may require their clients to replenish advance fees continuously as they are depleted - this is sometimes called an "evergreen" fee arrangement.

A "true retainer fee" is often wrongly thought to be a type of advance fee. This is because the "true retainer fee" is traditionally paid to the attorney in advance of the attorney's period of availability. A "true retainer fee," however, unlike an advance fee paid pursuant to an hourly or flat fee arrangement, is considered earned upon receipt and, therefore, is not an advance fee. (See *Baranowski v. State Bar* (1979) 24 Cal.3d 153 [154 Cal.Rptr. 752].)

(A "true retainer fee" is sometimes also called a "classic retainer fee." (See *T & R Foods Inc. v. Rose* (1996) 47 Cal.App.4th Supp. 1, 7.) However, "true retainer fee" is the more common term because it is used in the California Rules of Professional Conduct. (See California Rule of Professional Conduct 3-700(D)(2).))

An "advance fee" is not found in a contingency fee arrangement. A contingency fee is never paid in advance of services, but is paid from the settlement or judgment proceeds after the attorney obtains them for the client. Note, however, that a contingency fee arrangement may include an advance "security payment" to guarantee the future payment of the contingency fee. (See discussion to proposed Rule 4-110.)

Sometimes, attorneys will call such security payments "security fees," but this is a misnomer. A security payment is not a fee payment at all; it is a guarantee payment. (See *T & R Foods Inc. v. Rose*, supra, 47 Cal.App.4th Supp. at p. 7.)

Non-refundable fees

It is common for attorneys to make advance fee payments "non-refundable" to clients. Contractually, the term "non-refundable" means that the fee payment, once paid by the client to the attorney, will not be refunded to the client. The term, by itself, does not define or describe the underlying fee arrangement(s), which could be either an hourly or flat/fixed fee arrangement.

The term "non-refundable" is also used commonly where an attorney takes a "true retainer fee" to ensure the attorney's availability. Although technically a "true retainer fee" is not an advance fee under *Baranowski* (and refundability, therefore, should not come into play), attorneys will often make their true retainers "non-refundable" to emphasize to the client that the true retainer is earned by the attorney upon receipt and will not be returned.

In contingency fee arrangements, "non-refundable" fees do not come into play because no fees are advanced. Sometimes the attorney will simply take an advance "retainer."

By this term, does the attorney mean a "true retainer" fee, a "non-refundable" fee, or an "advance" fee? In one case where the attorney used the term "retainer," the court considered how the attorney had described and used the fee (the attorney charged services against it) in

determining that the "retainer" was, in fact, an advance fee payment. (See *T & R Foods, Inc. v. Rose*, supra, 47 Cal.App.4th Supp. at p. 7.)

Even where an attorney has denoted a particular fee payment as "non-refundable" in a fee contract, the attorney has a duty under California Rule of Professional Conduct 3-700 (D)(2) to "[p]romptly refund any part of a fee paid in advance that has not been earned" upon termination of employment. (Note that this provision is not applicable to a "true retainer fee," which is paid solely for the purpose of ensuring the attorney's availability (see Rule 3-700 (D)(2)).) Thus, attorneys can be required to refund contractually "non-refundable" fees in situations where fees have been advanced by the client, but not earned by the attorney. (See *Matthew v. State Bar* (1989) 49 Cal.3d 784.)

This is also true where the attorney has taken a non-refundable "minimum" fee from the client. (See *In the Matter of Fonte* (Review Dept. 1994) 2 Cal. State Bar Court Rptr. 752.)

A complete discussion of refundability factors is beyond the scope of this article. The point here is that such terms represent fee payment conditions and do not represent or describe the underlying fee arrangement(s).

A second point is that such terms, as contractual fee payment conditions, are not ironclad.

Writing a better fee contract

Fee contracts can be extremely detailed and complex. They can contain innumerable clauses, terms and conditions. They can be filled with minutia. In writing this article, I have attempted to simplify legal fees and fee arrangements, so that they can be understood in overview.

It is useful to comprehend the "forest" of fee arrangements before getting lost examining individual trees. Attorneys who understand the basic precepts presented above should always have their bearings straight in the fee forest. The ultimate goal, of course, is for attorneys to write accurate and clear fee contracts. A clear, unambiguous fee contract is always in an attorney's best interest. It can be invaluable to the attorney in the event of a fee dispute. More importantly, it can help avoid a fee dispute in the first place by eliminating ambiguous or inconsistent contract language that can lead to attorney-client quarrels. Fee contracts should identify and describe underlying fee arrangements accurately and clearly. All contract terminology should conform precisely to, and not conflict with, the underlying fee arrangement(s). Attorneys should proceed in accordance with their fee contracts, making sure that fee payments are taken and handled in conformity with the underlying fee arrangement(s). These tasks all start with, and require, a basic understanding of generic fee arrangements. In my opinion, an attorney who has this understanding has a tremendous head start in drafting a clearer, better fee contract.

David M.M. Bell, now in private practice, formerly was State Bar director of professional competence, overseeing rule development and the Ethics Hotline. He can be reached at dmbell@dnai.com.

Test — Legal Ethics

1 Hour MCLE Credit

This test will earn 1 hour of MCLE credit in Legal Ethics.

1. True/False. How a legal fee is characterized does not make that much of a difference regarding how legal fees are earned or how fee payments are taken.
2. True/False. Attorneys employ a wide variety of terms in naming their fees and fee arrangements.
3. True/False. California Rule of Professional Conduct 4-110 (Advance Payment of Legal Fees) was adopted in 1997.
4. True/False. There are seven basic types of generic fee arrangements: hourly, flat/flat, contingency, security, classic retainer, advance retainer, and true retainer.
5. True/False. A fixed or flat fee arrangement is one in which the lawyer agrees to provide a specific service at a predetermined hourly rate.
6. True/False. A contingency fee arrangement typically provides that if the client is successful in the matter being litigated or negotiated, the lawyer will receive a defined percentage of the recovery.
7. True/False. A contingency fee arrangement may include a security payment to guarantee the future payment of the contingency fee - this security payment is a type of advance fee.
8. True/False. A true retainer fee arrangement provides for a fee paid to the lawyer solely for the purpose of ensuring that availability of the lawyer for the client's matter - the true retainer fee is not tied to the performance of any specific legal service.
9. True/False. A "true retainer fee" is more appropriately called a "classic retainer fee."
10. True/False. A true retainer fee payment is considered earned upon receipt.
11. True/False. An attorney may ethically combine different types of generic fee arrangements within a single fee contract.
12. True/False. Advance fee payments are commonly taken in hourly, flat/flat, and true retainer fee arrangements.
13. True/False. A "non-refundable fee" arrangement means that the attorney is working on an hourly basis for the client.

14. True/False. When an attorney's contract calls for a "retainer," the attorney means a "true retainer fee" that is earned upon receipt.
15. True/False. An attorney has a duty, upon termination of employment, to promptly refund any part of a fee paid in advance that has not been earned.
16. True/False. The duty, upon termination of employment, to promptly refund any part of a fee paid in advance that has not been earned does not apply to a "true retainer fee" which is paid solely for the purpose of ensuring the attorney's availability.
17. True/False. Attorneys can be required to refund contractually "non-refundable" fees in situations where fees have been advanced by the client, but not earned by the attorney.
18. True/False. An attorney can be required to refund a non-refundable "minimum" fee to the client.
19. True/False. In a contingency fee arrangement, the lawyer will bill the client for services during the course of representation.
20. True/False. Many attorneys find the entire subject of legal fees to be unnecessarily complicated and complex.

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