

# Fee Arrangements With Clients

by Frederick J. Dennehy

The objective of a fee agreement is not just compliance with specific dos and don'ts contained in the Rules of Professional Conduct or Court Rules. It is unambiguous communication about the basis of the fee arrangement and the services that will be performed for the client. Having a clear and precise fee agreement enables counsel to think more clearly about what he or she is about to undertake for the client. And in some instances it does more. It forces counsel to decide *who is* the client and *who is not* the client.

**I**n the transactional context, for instance, counsel may end up meeting with a number of individuals who want to form a business entity. At that moment, they are all friends and they all have a common goal. But in order to avoid conflicts of interest, the practitioner must decide as soon as possible whether he or she is representing one of them, a limited group of them, or the business entity that they may want to form. The fee agreement forces counsel to that.

The first ethical obligation in the fee context is disclosure. RPC 1.4(b) requires attorneys to provide clients with the information reasonably necessary to permit them to make informed decisions regarding a representation.<sup>1</sup> Without disclosure of all relevant information to the client, the client's choice of a fee arrangement has been held to be "illusory."<sup>2</sup> The second requirement—and the fundamental guideline—in fee arrangements is set forth in RPC 1.5(a). That rule says the fee charged to the client has to be reasonable.

"Reasonable" means at least two things:

1. The *type* of fee arrangement entered into has to be fair; and
2. The *amount* of the fee has to be fair.

## The Reasonableness Requirement of RPC 1.5 Applies to the Type of Fee Arrangement

The leading case on types of fee arrangements is *In re Reisdorf*,<sup>3</sup> where the Supreme Court found that a contingent fee arrangement between a lawyer and widow in a contested probate matter was unfair and unreasonable because there was only a minimal risk of nonpayment assumed by the attorney, and the attorney had not informed the client—who didn't have much money—that under Rule 4:42-9, the attorney's fee may be paid from the estate without regard to the amount of the client's recovery.

*Reisdorf* stands for at least two principles. First, an attorney has to assume *some risk* of nonpayment to justify a fee based on a contingency instead of the value of services rendered.

Second, no type of agreement can be reasonable unless the client knows enough to make an informed choice about it. This applies to all fees, contingent and otherwise.

## The Choice of a Contingency Fee or a Different Arrangement

The first choice typically is whether to employ a contingency arrangement or not.

Court Rule 1:21-7(b) says that contingent fee arrangements cannot be used in a fee agreement *unless* the client is first given a chance to retain the attorney on the basis of the reasonable value of his or her services. This choice has to be mentioned in the engagement letter.

ABA Formal Opinion 94-389 provides a long list of factors that should be reviewed between an attorney and a client before there is agreement upon a contingency arrangement. The opinion isn't binding on New Jersey attorneys, but it is useful as a guideline for discussion, or for an attachment to the engagement letter.

## The Requirement of a Signed Writing

All contingent fee arrangements have to be in writing, and signed by the client, whether the client is a longstanding one or not. A duplicate has to be given to the client. This applies as well to negative contingency agreements or any other

arrangements where a lawyer charges a premium based on the result achieved. This procedure is different from the procedure for non-contingency situations, where the client does not have to sign the agreement, and where a fee agreement may not be necessary for long-standing clients.

### **Alternatives to Contingency Arrangements**

The alternative to a contingency fee is not necessarily a straight hourly rate. The fee can be based on the reasonable value of the services rendered, so it can be a fixed fee that covers either the complete representation, or each portion of the representation, if it is a multipart representation. Fees can be hourly, hourly with caps, or modified contingency fees (a reduced hourly or fixed rate together with a reduced fee contingent on specified results). Fees can also be stated in the alternative. For example, a lawyer can charge the higher of: 1) a rate based on time, or 2) the attorney fees awarded by the court under a fee shifting rule.

### **Non-Refundable Retainers**

RPC 1.16 (d) requires that the lawyer refund “any advance payment of a fee that has not been earned.” Cases decided under the RPCs have ruled that retainers, like other fees, must either be earned or returned.

But a retainer may be deemed earned if the lawyer stands ready to provide the requested representation, or if the lawyer turns down other employment because of a conflict of interest or anticipated time constraints. Retainers, therefore, may be non-refundable. If the fee is not refundable, the attorney has to state as much in the engagement letter.

The New Jersey Supreme Court Advisory Committee on Professional Ethics in its Opinion 644 held that “a retainer may be fully earned and therefore non-refundable when the lawyer stands ready to provide anticipated representa-

tion, whether or not it actually materializes.”<sup>4</sup> Typically, a lawyer who charges a non-refundable fee has special experience or a reputation in the area of practice in question.

Opinion 644, however, also warned that non-refundable retainers are ethical only when the “fee arrangement is fair and reasonable under the circumstances of the particular representation.”<sup>5</sup> In *DeGraaff v. Fusco*,<sup>6</sup> the Appellate Division held that a non-refundable retainer, while not unethical *per se*, was subject to partial return if contravening events should render it “unconscionable” for the attorney to keep it. There, an attorney took \$15,000 to help a woman’s son in a federal criminal matter. It was resolved quickly, with little intervention by the attorney, and there was no explanation of the basis for the fee.

### **Not Only the Type of Fee Arrangement Has to be Reasonable, but the Amount of the Fee Has to be Reasonable**

#### **Factors**

RPC 1.5(a) lists a number of factors to be included in deciding whether the amount of a fee is reasonable or not:

- (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, if apparent to the client, 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.

Bear them clearly in mind when setting the fee, so they can be referenced if the fee needs to be defended to the court or the client.

### **A Written Statement of Basis for Fee Calculation**

Regardless of the type of fee arrangement, RPC 1.5(b) requires that the basis of the fee be communicated in writing to any client the lawyer has not regularly represented. Interpret “regularly” warily—and err on the side of formalizing the agreement. Disclose in the engagement letter *all* charges for which the client will be financially responsible.

Disputes can easily be avoided by providing a clear, written statement to each client at the beginning of each separate matter, describing the precise manner in which payment is expected. It helps the client and the practitioner. The alternative is a good deal of unnecessary grief.

Probably the most comprehensive recent statement on this topic is by the Appellate Division in *Alpert, Goldberg v. Quinn*,<sup>7</sup> which examined a unique form of retainer agreement and the entitlement of a law firm to be paid for work done pursuant to that agreement.

The *Alpert* retainer agreement had set forth the hourly fee to be charged, and the fact that there would be a charge for expenses and a discount based upon timely payment. It also specified that “details on any of the items in our policies will be provided to you upon request; whether or not you request them you will be bound by our standard practices and firm policies in these and other regards, so feel free to ask.”<sup>8</sup> These details were embodied in a so-called master retainer, which consisted of 18 single-spaced typewritten pages. Among the things it provided were:

1. If the firm withdraws from the client’s matter and is further entangled with the client, its time will be billable to and payable by the client, together with expenses;

2. Balances owed and unpaid beyond 30 days would bear interest at the rate of 12%;
3. If there is a fee dispute or any proceedings relating to or arising from the attorney fees and expenses, the client will continue to pay the hourly fees and expenses for any time and expense that continues to be incurred by the firm by virtue of any fee dispute or related proceedings;
4. The client will pay fees for any time and expense incurred by the firm in seeking to be relieved of counsel and in dealing with a successor firm.<sup>9</sup>

The Appellate Division, in reviewing this unusual arrangement, stressed that an attorney, when contracting for a fee, has to act as a fiduciary, and satisfy his or her fiduciary obligation to the client. It said a fee agreement is not circumscribed by the dictates of contract law.

If a client does not know what charges and costs beyond the hourly rate he or she will be exposed to, how can the client be expected to make an informed decision concerning representation? RPC 1.5(b) requires the attorney to present a new client in writing, at the time of retention, *all* of the fees and costs for which the client will be charged, as well as the terms and conditions that would be imposed. A reference in a retainer agreement to another document like a master retainer that would provide details is not sufficient.

Wherever there is a potential for confusion regarding what services will be included within the fee charged, the description is particularly important. If it's not clear, the agreement can be invalidated, or counsel can be held accountable for doing something he or she never intended to do. Counsel may (and should) 'unbundle' services, (*i.e.*, make it clear that a specific task or tasks is being undertaken rather than service as the client's 'general lawyer'). But counsel has to disclose that fact to the client.

If the fee is subject to increase on an annual basis, it should be clearly stated. And when the attorney receives a retainer in advance, RPC 1.5(b) requires that it be specified whether the advance payment is a retainer or a fixed fee.

### **Timing**

Under RPC 1.5(b), the fee arrangement in a non-contingency case has to be made either before or within a reasonable time after beginning the representation. "Reasonable time" simply means a sufficient time to allow for the client to receive the fee letter, review it, and if necessary, contact the attorney to register disagreement. But there is no requirement that the client sign the letter or even acknowledge receipt.

Nor is there a requirement that a letter be sent to a client who is "regularly represented." The idea behind this exception is that an understanding regarding the basis for the fee has already evolved. But it is never a good idea to rely on this. It is best always to send a letter for each matter.

### **Conscionability and Fairness**

As noted above, general contract principles do not trump fiduciary duty in fee agreements. In the case *Cohen v. Radio-Electronics Officers*,<sup>10</sup> there was an agreement for legal services that would be renewed automatically each year unless either party provided written notice of termination six months before the termination date. The agreement called for an attorney fee of \$100,000 per year. The client in *Cohen* terminated the agreement, but not during the specified termination period. The attorney tried to obtain his full \$100,000 fee for the year following the decision by the client to terminate on the grounds that the termination notice didn't comply with the contract. The trial court ruled for the attorney, but the Appellate Division held that general contract principles don't apply to attorney fee agree-

ments, and that to charge \$100,000 knowing the attorney would not be called upon by his client for any services was unconscionable and went against the essence of RPC 1.5.<sup>11</sup>

The Appellate Division has also said that when attorneys can reasonably foresee that anticipated counsel fees are "disproportionate" to the amount in dispute, or that they have exceeded it, the attorney is obligated to communicate that fact to the client.<sup>12</sup>

### **Reasonableness of Contingency Fees**

The reasonableness requirement of RPC 1.5(a) applies to contingent fees as well as hourly fees. Beyond the general reasonableness requirement, Rule 1:21-7(c), which applies to injuries from non-business torts, establishes a sliding scale for certain contingent matters. Furthermore, there is a procedure to ask the court for a higher fee in some instances, under Rule 1:27-7(f). It applies to all attorneys, in New Jersey and out of state.<sup>13</sup>

In the case of a non-business tort matter, expenses must be deducted before calculating the contingent fee. After the contingent fee matter is over, RPC 1.5(c) says the lawyer has to provide the client with a written statement of the outcome of the matter, and, if there is a recovery, show the client how it was determined.

The specific percentage limitations set forth in Rule 1:21-7(c) apply to most negligence matters, including automobile accidents, slip and fall cases and products liability matters. But, they do *not* apply to "business torts" such as fraud or interference with contractual relations or employment cases.

When an attorney in a personal injury case reduces liens, assignments and claims against the proceeds through negotiations resulting in compromise, that additional benefit to the client can be added to the net recovery for the purposes of calculating the attorney's fee. But a provision to that effect must be in the engagement letter.

The net recovery on which the fee is to be based does *not* include *pre-judgment* interest that may be added to the judgment in tort actions through Rule 4:42-11(a)(b). *Post-judgment* interest, on the other hand, *is* included in the net recovery on the basis that delay in payment of a judgment will cause economic harm to the attorney as well as the client.<sup>14</sup>

### **Disbursements**

The reasonableness requirement of RPC 1.5(a) applies equally to charges to clients for services provided by paralegals and other non-attorney personnel. Attorneys cannot delegate tasks to paralegals that the attorneys could perform in a more cost-effective way. But they can charge, at their own hourly rate, for the actual time spent supervising or reviewing the work of paralegals.

If a client has agreed to pay for paralegal time in addition to attorney time, the attorney cannot charge paralegal fees for a task that could have been performed by less skilled workers. Rule 4:42-9(b) governs court-awarded fees for paralegal services, and defines “paraprofessional services” to be “specifically delegated tasks which are legal in nature [performed] under the direction and supervisor of attorneys which tasks an attorney would otherwise be obliged to perform.”

If the client has agreed to pay other types of out-of-pocket expenses after being fully informed, the attorney can recover them as well. This includes filing fees; payment to investigators, experts, and paralegals; and the cost of telephone calls, as well as travel and hotel expenses incurred on behalf of the client. But in *In re Estate of Reisen*,<sup>15</sup> the court said “overhead of the firm,” such as postage, photocopying and telephone, should generally be borne by the firm and not charged to the client. That is, therefore, the default rule.

In *Estate of Reisen*, there was no spe-

cific agreement in the retainer letter about who would be responsible for what. That is the key, and it reinforces the need to include *all* terms in an engagement letter.

There is no New Jersey opinion that addresses whether an attorney can generate a profit on services like photocopying and other expenses. The comment to Model Rule 1.5 says that “a lawyer may seek reimbursement for the cost of services performed in-house, such as copying, or for other expenses incurred in-house, such as telephone charges, either by charging a reasonable amount to which the client has agreed in advance or by charging an amount that reasonably reflects the cost incurred by the lawyer.”<sup>16</sup>

ABA Formal Opinion 93-379 is non-binding in New Jersey, but can serve as a guideline. The opinion approved expense charges for more than the actual cost to the attorney, as long as the client was aware of the amount above the actual cost of the service being charged, and agreed to it. The opinion noted that the lawyer’s stock and trade is “the sale of legal services, not photocopy paper, tuna fish sandwiches, computer time or messenger services.” It also suggested that, *where the client has agreed to it*, the client may be charged for general office overhead, such as “maintaining a library, securing malpractice insurance, renting of office space, purchasing utilities and the like.” Even when photocopying is considered part of overhead and not charged to the client, expenses generated by and “unusual and voluminous number of copies” can be charged.<sup>17</sup>

The most important thing to remember as far as disbursements go is that failure to disclose any of the components of a bill, including a profit margin on reimbursable services and materials, might be construed as overreaching and a violation of RPC 1.5(a), as well as possibly conduct involving dishonesty in violation of RPC 8.4(c).

### **Charges for Divided Time**

An attorney cannot include charges to one client for time spent equally on another client. For example, assume counsel has three separate cases with motions scheduled to be heard in the same court on the same day, and spends a total of three hours in court. Each of the three clients cannot be billed for a full three hours. The total time spent would have to be apportioned to each file. If counsel travels on behalf of one client but uses the travel time to work on another client’s file, both clients cannot be charged for the travel time. And if old work product can be reused, counsel does not re-earn the hours previously billed when the work product was originally generated. ABA Opinion 93-379 states that “a lawyer who has agreed to bill solely on the basis of time spent is obliged to pass the benefits of those economies on to the client.”

### **Termination Letter**

When a matter is concluded, a letter should be sent to the client informing him or her of the fact. It makes it clear duty to the client has ended, and it may prevent future conflicts of interest.

### **Unauthorized Provisions in the Retainer Agreement**

There are a variety of provisions that ethically may not be part of a retainer agreement with a client. These include:

#### **Authorization to Settle**

There can be no language in a retainer agreement or letter of solicitation permitting an attorney to settle a case without first allowing the client to review and approve the terms of the settlement.

#### **Restrictive Termination Provisions**

A client has an absolute right to dismiss an attorney. A restrictive termination provision in a retainer agreement violates public policy and cannot be

enforced by the attorney.

### **Limitations on Liability**

A lawyer cannot enter into an agreement prospectively limiting liability for malpractice, unless: 1) the client fails to act in accordance with the lawyer's advice, and 2) the lawyer's representation of the client continues at the lawyer's request. New Jersey's prohibition is different from the Model Rule version. For example, Model Rule 1.8(h) allows an attorney and a client to limit the lawyer's liability by advance agreement when the client is represented by independent counsel.

### **Collection Fee Provisions**

Where a retainer agreement provides for counsel fees, including collection fees, it is generally enforceable as long as the provision is fair and reasonable.<sup>18</sup>

### **Limitations on Scope of Representation**

When a lawyer and client agree to some form of limitation on the nature of the work to be performed by the lawyer, that agreement should obviously be memorialized in writing, and describe itself plainly as a limitation of services.

### **Commercial Arbitration Provisions**

The Appellate Division, in *Kamaratos v. Palias*,<sup>19</sup> concluded that a retainer agreement may include a provision mandating the commercial arbitration of any fee disputes, as long as the provision in question *sufficiently* discloses its consequences.

Specifically, the provision has to disclose that it eliminates the rights to pursue the dispute in court and through a jury trial. Also, it has to inform the client of the potential additional costs associated with commercial arbitration, and the limitations on the right to appeal an arbitration award. The court also suggested that a valid arbitration

provision would have to set forth the qualifications of the arbitration panel, and disclose that a commercial arbitration might be conducted by non-lawyers. In addition, "an enforceable agreement should contain a clear statement that the client has an absolute right to proceed at the Fee Arbitration Committee level."<sup>20</sup>

Thus, it appears that a commercial arbitration provision in a retainer agreement can ensure that the fee dispute will not be conducted in the courts, although the client, in effect, will be able to select whether the dispute is handled in a court rule-based or other commercial arbitration. If the fee dispute also requires resolution of a malpractice issue through arbitration, the rationale may not apply. *Kamaratos* expressly declined to address that question.

### **Advance Waiver of Conflict**

A number of retainer agreements include a provision for an advance waiver of a conflict that arises after the execution of the retainer agreement. In most jurisdictions, that kind of advance waiver is not enforceable, because the full context is not available to the client when the waiver is being signed. Because it has to be informed, knowing and voluntary, it is doubtful it would be upheld in New Jersey.

### **Billing Standards**

In a recent unpublished opinion, Federal District Court Judge Susan Wigenton slashed approximately 12 percent of a law firm's fee request because the method of billing could have led to or obscured overbilling.<sup>21</sup>

The opinion stated that the application for fees contained billings in 15-minute increments rather than what the judge called the "industry standard" of "six minutes." The judge ruled that, under the practice a billing for 30 minutes could result for something that actually took 20.

Judge Wigenton also sliced off time because of "block billing," which bunches different services together rather than breaking down the time to show how much was spent on each differentiated task. Block billing is not disallowed, but fees billed by that method will be upheld as reasonable only if the listed activities reasonably correspond to the number of hours billed. In other words, they will be more carefully scrutinized.

If there are too many vague entries, the entire entry is not tossed out. Instead, the court determines whether there is a reasonable correlation between the listed activities and the time spent. The court cited Third Circuit precedent that a party blocks bills "at its own peril."

The court also refused to allow fees for preparing the fee application, blaming the inability to agree on the amount of fees on confusion arising out of the law firm's billing practices. The court refused to reward "any ambiguity associated with [the firm's] invoices by awarding fees or costs for the application." ◊

### **Endnotes**

1. Similarly, RPC 2.1 requires an attorney to "render candid advice" in representing a client.
2. *In re Reisdorf*, 80 N.J. 319, 322 (1979).
3. *Id.*
4. 126 N.J.L.J. 966 (1990).
5. *Id.*
6. *DeGraaff v. Fusco*, 282 N.J. Super. 315, 320-21 (App. Div. 1995).
7. 410 N.J. Super. 510 (App. Div. 2009), *certif. den.* 203 N.J. 93 (2010).
8. *Id.* at 520.
9. *Id.* at 521.
10. 275 N.J. Super. 241 (App. Div. 1994), *modified* 146 N.J. 140 (1996).
11. *Id.* at 259-60.
12. *Chestone v. Chestone*, 322 N.J. Super. 250, 259 (App. Div. 1999). The Appellate Division expressed concern about and disallowed fees and

- costs in excess of \$80,000 for handling a motion for modification of child support that was resolved by the judge without testimony when there was no serious dispute about the parties' relative financial situations; see, *Loro v. Colliamo*, 354 N.J. Super. 212 (App. Div. 2002).
13. See *Estate of Vafiades v. Sheppard Bus Service*, 192 N.J. Super. 301 (Law Div. 1983).
14. R. 1:21-7(d).
15. 313 N.J. Super. 623 (Ch. Div. 1998).
16. See ABA Annotated Model Rules of Professional Conduct, Sixth Ed., Comment to R. 1.5, p. 75.
17. *Estate of Reisen*, 313 N.J. Super. at 636.
18. For a case involving an unreasonable collection fee provision, see *Gruber & Colabella, P.A. v. Erickson*, 345 N.J. Super. 248, 252-53 (Law Div. 2001).
19. 360 N.J. Super. 76, 82, 86-87 (App. Div. 2003).
20. R. 1:20A.
21. *USA v. NCH Corporation, et al*, New Jersey District Court, entered Sept. 10, 2010.
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