

ETHICAL SOLUTIONS TO FEE PROBLEMS

CALIFORNIA JOAN DISCUSSES THE IMPACT OF A COURT OF APPEAL DECISION ON WRITTEN FEE AGREEMENTS

By ELLEN R. PECK
© 2007-08. All rights reserved.

California Joan was delighted to receive a call from Every (Eve) Lawyer, a partner in Thomas & Lawyer, LLP and a longstanding client. "Hey, Cali, remember last June when you gave me some advice regarding clients' use of credit cards to pay for legal fees, costs and expenses? I have some good news!"

Cali recalled that she and Eve discussed State Bar Committee on Professional Responsibility and Conduct Formal Opinion 2007-172 (COPRAC Fml. Op. 2007-172), which opined that (1) an attorney may ethically accept client credit card payments for fees not yet earned, earned fees or reimbursements for costs, provided that the attorney maintain confidentiality; and (2) because an attorney must deposit advances for costs and expenses into a client trust account, an attorney may not ethically accept a deposit for advances for costs and expenses from a client by credit card where they are paid through a merchant account subject to the credit card issuer's control and invasion for charges and charge backs.

"What's the good news?" Cali asked.

"I was browsing the Los Angeles County Bar Association Web site and I think I found a merchant account program that solves all the ethical dilemmas in accepting client credit card payments for all fees and costs," Eve told Cali excitedly. Affiniscape Merchant Solutions (affiniscape.com) has offered a new Law Firm Merchant Account™ which permits a law firm to direct client credit card deposits to either a trust account or business/general account in accordance with trust account rules, while subjecting "invasions" for charges and charge backs to sources other than trust accounts."

After looking online at the structure of the account, Cali said, "Assuming the contract is consistent with the online description, this is the type of account that solves the ethical problems raised by Formal Opinion 2007-172. First, this type of merchant account is structured to prevent a credit card issuer's control or invasion of your trust account, since you can designate a source other than the trust account for withdrawals of charges and charge backs. Second, since it permits you to choose whether to deposit client credit card payments into a trust account or a business/operational account, you can deposit advanced costs and expenses directly into your trust account, while depositing payments for earned fees into a general business/operations account. The flexibility permits compliance with all trust accounting duties," Cali said.

Eve breathed a sigh of relief. "Another ethics problem solved!" "Just make sure that the actual contract does these two things, as the description suggests," Cali reminded her as Eve hung up. As she replaced the receiver, Meryl Terpitude sauntered into her office and threw himself into a chair.

Looking a little sheepish, Meryl blurted out, "Cali, in my contingency

fee agreements, I forgot to include the statement, 'The fee is not set by law but is negotiable.' (Bus. & Prof. C. §6147(a)(4)) All my fee agreements are voidable.' (Bus. & Prof. C. §6147(b)) I just settled a big case; the client has gone to another lawyer who wants to see all my billing records to determine the reasonable value of my services.' I did not keep great records of the hours I worked on the case! What can I do?"

"I think you will find some comfort in the story of *Fergus v. Songer* (2007) 150 Cal.App.4th 552 [mod. on den. rev. 6/01/07, rev. den. 7/25/07] (*Fergus*)," Cali said. "In 1995, Songer had been chasing Bordan for 16 years to enforce a judgment for personal injuries for \$308,000, without success, even though a judgment lien had attached on Bordan's Pismo Beach Hotel. Songer consulted Fergus, a lawyer who specialized in commercial collections. In a written contingency fee agreement, Songer agreed to pay Fergus 45 percent of all recoveries made." (*Fergus*, pp. 556-558)

"For the next six years, Fergus represented Songer in a number of legal actions and proceedings. Finally, in late 2001, Songer was able to pur-

chase the Pismo Beach Hotel at a sheriff's sale. However, because he did not have sufficient funds to refurbish and operate the hotel until it could be sold, Songer turned to Fergus for additional legal assistance and loans." (*Fergus*, pp. 558-559)

"Fergus agreed to do additional legal work and loan money if Songer would agree to become equal partners in the hotel or to increase Fergus' legal fee to 50 percent of any recovery. (*Id.* at 558) Although Songer orally promised to sign this written agreement, he never did." (*Id.*)

"Two years later, with Fergus' help, Songer sold the hotel for \$4.8 million but did not share the proceeds with him. Fergus sued Songer for fees and for an interest in the hotel and Songer cross-complained for legal malpractice and breach of fiduciary duty." (*Fergus*, p. 559)

A jury awarded Fergus \$1.2 million as the reasonable value of his services and found against Songer on all causes of action. (*Fergus*, pp. 556-557)

"Fergus had to prove the reasonable value of his legal services to Songer because his first 45 percent written contingency fee agreement did not contain the negotiability clause (Bus. & Prof. C. §6147(a)(4)) and his second 50 percent agreement was not in writing (Bus. & Prof. C. §6147(a)). Thus, both fee agreements were voided by Songer." (Bus. & Prof. C. §6147(b); *Id.* at 558, 570)

Meryl, growing impatient with a tale that did not feature him, inter-

jected, "But he was still entitled to collect a reasonable fee!" (Bus. & Prof. C., §6147(b))

Cali persisted in raising risks. "Meryl, when the client elects to do an oral agreement, there are a number of burdens upon the lawyer, including delay in getting paid, uncertainty and problems of proof concerning the contingency amount and other terms of the oral agreement, the cost of mediation, arbitration and/or litigation, time away from the office working on other cases which could generate fees, the effect upon emotional well-being when subjected to attacks upon the lawyer's integrity, competence and the value of legal services, the almost inevitable counterclaim for legal malpractice and breach of fiduciary and, increasingly, a complaint to the State Bar, both of which generate additional risks and costs. When fee disputes are litigated, there is an added burden to the courts and the administration of justice. Like Fergus, a lawyer may prevail, but it is a long, rocky and costly road."

Meryl conceded, "Can I correct all of my fee agreements that are deficient or are not in writing?"

"In *Fergus*," Cali replied, "the Court of Appeal suggested that contingency fee contracts, like all voidable contracts, may be ratified by the client. (*Id.* at 571) Therefore, you can attempt the ratification process to cure defects in your compliance with §6147, §6148 (all other fee contracts) or the Rules of Professional Conduct (e.g. rule 3-300)."

Meryl's brow wrinkled. "What are the steps I need to take to make the ratification stick?"

Cali set forth the ratification requirements: "First and foremost, the client in a position to elect ratification must be able to make an informed and intelligent choice. (*Ibid.*) Songer's knowledge that the contingency fee was negotiable was insufficient to demonstrate ratification. Instead, the client must know that the fee agreement is voidable, why it is voidable and then elect ratification with that knowledge. (*Id.* 571-572)

"Second, where the statute or rule require the disclosures and/or consent to be in writing, the disclosures and consent to ratification must be in writing," Cali continued.

"In all of these matters, I would want to be able to prove that the client's ratification was intelligent and informed," Meryl exclaimed. "Therefore, as a matter of risk management, I would want to have all disclosures concerning voidability and ratification in writing and signed by the client."

"Generally, a writing in addition to an oral explanation assists a client's comprehension about a transaction," Cali added. "Finally, although not suggested or required by the Court of Appeal, I think a written advisement to seek the advice of independent counsel and affording the client an opportunity to do so would assist in proving that the client consciously elected ratification."

"This gives my clients quite the upper hand in negotiation. What if they do not agree to the ratification?" Meryl asked.

"If your fee agreement is voidable, they already have the upper hand," Cali said sympathetically. "I predict

See ETHICAL SOLUTIONS on Page 10

SELF-ASSESSMENT TEST

READ THIS ARTICLE AND TAKE THE
ACCOMPANYING TEST TO EARN ONE HOUR
OF SELF-STUDY MCLE CREDIT IN LEGAL ETHICS.

FOLLOW INSTRUCTIONS ON TEST FORM

This month's article and test provided by the
California Bar Journal

THOMSON
WEST

ETHICAL SOLUTIONS TO FEE PROBLEMS

CALIFORNIA JOAN DISCUSSES A COURT OF APPEAL RULING ON WRITTEN FEE AGREEMENTS

CONTINUED FROM PAGE 9

that most clients will be amenable to ratification. However, for those who do not agree, this is early warning that they may void your agreement and contest your fees. At least you can take extra precautions in those cases to be able to prove a reasonable fee.

"Well, that takes care of curing the defects in my existing fee agreements," Meryl then asked, "What evidence can I gather or present to prove the reasonableness of my fee where I have not kept the best hourly records?"

"Fergus provides insight on proving the reasonable value of legal services after a client has voided a fee agreement and the lawyer does not have great records of the hours spent," Cali said. "First, the trier of fact may consider the following factors in assessing the reasonable value of legal services:

- The amount of the fee in proportion to the value of the services performed.
- The novelty and difficulty of the questions involved and the skill necessary to perform the legal services properly.
- The likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the attorney.
- The amount involved and the results obtained.
- The time limitations imposed by the client or by the circumstances.
- The nature and length of the professional relationship with the client.
- The experience, reputation and ability of the attorney performing the

services.

- The time and labor required.
 - The informed consent of the client to the fee. (*Id.* at 561, 567-568.)
- "Can the trier of fact consider that the fee agreement was contingent upon recovery, exposing the lawyer to risk of earning no fee at all or a delay in receiving fees?" Meryl asked. "Yes," responded Cali, "but the trier of fact cannot consider the amount of the contingent fee, where the contingent fee agreement is void. (*Id.* at 573)

"Most importantly," Cali went on, "a lawyer is not limited to his or her usual hourly rate. A trier of fact can conclude that a lawyer is entitled to 'considerably more than his normal hourly rate' where there is evidence of (1) extraordinary services; (2) result of the legal services is 'spectacular'; or (3) work on the client's matters is so time consuming that it precluded the lawyer from accepting other employment from which other fees would be generated. (*Id.* at 567-568)

"A lawyer is not limited to the hours which the lawyer recorded on the case. The trier of fact may consider other evidence in arriving at the amount of time spent on a case, including (1) time which was spent on telephone calls and other routine matters, which the lawyer may not have recorded; (2) that time records may have been lost through electronic failure or other means; (3) all records in the files of the lawyer which demonstrate the amount of time performing legal services (e.g., 24 'banker's boxes' of Fergus' work product relating to his representation of Songer, including 390 responsive pleadings and 57 hearings and trials); (4) a summary of the lawyer's work based upon the file materials; and (5) expert opinion concerning the reasonable value of the services based upon a review of the lawyer's file." (*Id.* 567-569)

"What about when my services are terminated before a recovery is reached?" Meryl asked.

"A contingency fee lawyer discharged prior to settlement may recover for the reasonable value of services rendered up to the time of discharge," Cali said. (*Fracasse v. Brent* (1972) 6 Cal.3d 784, 791)

"In determining the amount of a reasonable fee, courts typically start with a calculation providing an objective basis to make an initial estimate

of the value of a lawyer's services: the number of hours expended on the matter multiplied by a reasonable hourly rate. (*Hensley v. Eckerhart* (1983) 461 U.S. 424, 433) The lawyer seeking fees must also demonstrate that the total fees incurred are reasonable and courts generally use some variation of the nine factors cited in *Fergus* to make that assessment. (*Fracasse*, at p. 791)

"Detailed time and billing records are not absolutely essential. A lawyer's testimony concerning the number of hours worked on a case is sufficient evidence to support an award of attorney fees, even in the absence of detailed time records," Cali said. (See Vapnek et al., *Cal. Practice Guide: Professional Responsibility* (The Rutter Group 2006) ¶ 5:1102 et seq; *Mardirossian & Assocs. Inc. v. Ersoff* (2007) 153 Cal.App.4th 257, 269 [rev. den. 10/10/07] (*Mardirossian*) — client substituted a new law firm into contingent fee case nine days before a \$3.7 million settlement was reached.)

"Moreover, precise calculations are not required; fair approximations based upon personal knowledge are sufficient," Cali continued. (*Mardirossian*, at p. 269)

"Finally, expert testimony on reasonableness of hours law firm attorneys spent on a client's contingency fee case is admissible, even when based upon an estimate. In *Mardirossian*, at pp. 272-273, the expert justified that in light of a \$3.7 million settlement obtained by other counsel only a few days after termination of the first lawyers, 3,700 hours of work was reasonable because the case involved much more work than the work product reflected in the file and because of the complexity of issues involved," Cali concluded.

"Thanks, Cali," Meryl said. "This is all good news. I am going to work with my clients to reform mistakes in my fee agreements, and I am going to start gathering evidence of the reasonable value of my services based upon the *Fergus* and *Mardirossian* cases." Meryl left Cali's office whistling, engrossed in calculations.

■ *Ellen R. Peck, a former State Bar Court judge, is a sole practitioner in Escondido and a co-author of The Rutter Group California Practice Guide: Professional Responsibility.*

CERTIFICATION

■ THIS SELF-STUDY ACTIVITY HAS BEEN APPROVED FOR MINIMUM CONTINUING LEGAL EDUCATION CREDIT BY THE STATE BAR OF CALIFORNIA IN THE AMOUNT OF ONE HOUR OF LEGAL ETHICS.

■ THE STATE BAR OF CALIFORNIA CERTIFIES THAT THIS ACTIVITY CONFORMS TO THE STANDARDS FOR APPROVED EDUCATION ACTIVITIES PRESCRIBED BY THE RULES AND REGULATIONS OF THE STATE BAR OF CALIFORNIA GOVERNING MINIMUM CONTINUING LEGAL EDUCATION.

HOW TO RECEIVE 1 HOUR OF MCLE CREDIT

■ Answer the test questions on the form below. Each question has only one answer.

■ Mail form and a \$25 processing fee to:

California Bar Journal / Test State Bar of California 180 Howard St. San Francisco, CA 94105-1639

■ Make checks payable to State Bar of California.

■ Correct answers and a CLE certificate will be mailed to you within four weeks.

NAME _____

LAW FIRM / ORGANIZATION _____

ADDRESS _____

CITY _____

STATE / ZIP _____

STATE BAR NUMBER _____

ANSWER FORM

January 2008

1. True False
2. True False
3. True False
4. True False
5. True False
6. True False
7. True False
8. True False
9. True False
10. True False
11. True False
12. True False
13. True False
14. True False
15. True False
16. True False
17. True False
18. True False
19. True False
20. True False

THOMSON
WEST

JANUARY 2008

SELF-ASSESSMENT TEST

■ Indicate whether the following statements are true or false after reading the MCLE article on ethical solutions to fee problems. Use the answer form provided to send the test, along with a \$25 processing fee, to the State Bar. If you do not receive your certificate within four to six weeks, call 415/538-2504.

1. An attorney may ethically accept a deposit for fees not yet earned, payment of earned fees or reimbursements for costs from a client by credit card, provided that the attorney maintains confidentiality.
2. An attorney may deposit client advances for costs and expenses into a law firm business or operational account.
3. A lawyer may not accept a deposit for advances for costs and expenses from a client by credit card where they are paid through a merchant account subject to the credit card issuer's control and invasion for charges and charge backs against the trust account.
4. An oral contingency fee agreement is voidable at the election of the client.
5. Written contingency fee agreements which do not include the statement, "The fee is not set by law but is negotiable," are permitted.
6. A fee agreement that does not

include all of the statements required by Business and Professions Code §6147 is voidable at the election of the client.

7. If a client voids a fee agreement because it does not comply with Business and Professions Code §6147, a lawyer is precluded from collecting any fee.
8. A sophisticated consumer of legal services who knew that contingent fees could be negotiated and does not void the agreement for six years has ratified the lawyer's failure to comply with §6147(a)(4).
9. In attempting to collect a fee, a lawyer bears a potential risk of client claims for legal malpractice or breach of fiduciary duty.
10. Fee agreements not in compliance with §6147 may be corrected by client ratification.
11. Client ratification requires that the client be able to make an informed and intelligent choice.
12. If a fee statute requires that the agreement be in writing, the ratification can be oral.
13. Unless ratification deals with compliance with CRC 3-300, client ratification of a deficient fee agreement does not require a written advisement to seek the advice of independent counsel and affording the client an opportunity to do so.

14. A client's refusal to ratify a correction of a fee agreement does not mean that the client will void a fee agreement.

15. In determining whether a fee is reasonable, the trier of fact may consider the amount of the fee in proportion to the value of the services performed.
16. The novelty and difficulty of the legal issues involved in a case is irrelevant to the determination of a reasonable fee.
17. In determining a reasonable fee where the contingent fee agreement is void, the trier of fact is prohibited from considering the amount of the contingent fee.
18. Where a contingency fee agreement is void for failure to comply with §6147, a trier of fact can conclude that a lawyer is entitled to more than his or her normal and customary hourly rate.
19. Where a lawyer is trying to prove the reasonable value of her services, detailed time and billing records are absolutely essential.
20. A lawyer's testimony concerning the number of hours worked on a case is sufficient evidence to support an award of reasonable attorney fees, even in the absence of detailed time records.