American Bar Association

CHARGING OF INITIAL FIXED FEE IN TAX CASE WHERE FEE COVERS REPRESENTATION IN THE EVENT OF IRS AUDIT OR TAX COURT LITIGATION

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On behalf of the Committee on Standards of Tax Practice of the Taxation Section of the American Bar Association, you have requested our opinion on the following matter.

Lawyers who engage extensively in counseling and advising clients with respect to tax matters are requested from time to time to advise clients on transactions which are largely tax-motivated. If the client-taxpayer's treatment of the transaction is not challenged by the Internal Revenue Service or if any challenge by the IRS is not sustained either on IRS review or by the courts, the transaction may result in a substantial reduction in taxes to the client. If, on the other hand, the transaction is not sustained, the taxpayer will at least be required to pay the tax he hoped to avoid plus interest and possibly a negligence penalty.

You ask whether it is ethically proper for the lawyer, in advising a client on such a transaction with doubtful consequences, to charge the client a fixed fee which includes not only the planning of the transaction but which would also cover representation of the client in the event the client's return is selected for audit, both before the Internal Revenue Service and in possible litigation before the Tax Court. If either the audit or the Tax Court litigation did not ensue, the lawyer would keep the fee.

DR 2-106(A) provides:
'A lawyer shall not enter into an agreement for, charge, or collect an illegal or clearly excessive fee.'

DR 2-106(B) provides that a fee is 'clearly excessive' when, after a review of the facts, a lawyer of ordinary prudence would be left with a definite and firm conviction that the fee is in excess of a reasonable fee. Factors to be considered as guides in determining the reasonableness of a fee are also set forth in that Disciplinary Rule.

There is nothing improper in a lawyer charging and being paid a fixed fee in advance for legal work on tax matters or litigation before the Tax Court if the client and the lawyer choose to do so and it is fully understood that the fixed fee embraces all work to be done, whether it be relatively simple and of short duration, or complex and protracted.

Also, an attorney can agree with a client on a contingent fee where he is only to be paid if he accomplishes a tax saving for the client. Similarly, an attorney can agree with a client on a fixed fee coupled with a contingency on the outcome of the case providing it is also understood that the fixed fee applies irrespective of the outcome and that the contingency applies only to the tax saving effected.

An attorney can also agree with a client to charge for legal services on an hourly basis for the time expended by his firm on the matter.
If a retainer fee is obtained and the fee is charged on a time-expended basis, it would then be incumbent on the law firm to remit to the client a payment covering any excess, in the event the full amount of the retainer fee was not absorbed in the rendition of the services.

ABA Informal Op. 1389

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