

# AMERICAN BAR ASSOCIATION

STANDING COMMITTEE ON ETHICS AND PROFESSIONAL RESPONSIBILITY

**Formal Opinion 94-389**  
**Contingent Fees**

**December 5, 1994**

*It is ethical to charge contingent fees as long as the fee is appropriate and reasonable and the client has been fully informed of the availability of alternative billing arrangements. The fact that a client can afford to compensate the lawyer on another basis does not render a contingent fee arrangement for such a client unethical. Nor is it unethical to charge a contingent fee when liability is clear and some recovery is anticipated. If the lawyer and client so contract, a lawyer is entitled to a full contingent fee on the total recovery by the client, including that portion of the recovery that was the subject of an early settlement offer that was rejected by the client. Finally, if the lawyer and client agree, it is ethical for the lawyer to charge a different contingent fee at different stages of a matter, and to increase the percentage taken as a fee as the amount of the recovery or savings to the client increases.*

## **A. Introduction**

The term contingent fees evokes an almost instantaneous visceral response among lawyers. Some view the contingent fee as the salvation of the impecunious,<sup>1</sup> a means to redress great wrongs, vindicate rights and reform the law.<sup>2</sup> Others view it as an inducement to frivolous lawsuits which abuse tort laws,<sup>3</sup>

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1. As stated by the Pennsylvania Supreme Court:

If it were not for contingent fees, indigent victims of tortious accidents would be subject to the unbridled, self-willed partisanship of their tortfeasors. The person who has, without fault on his part, been injured and who, because of his injury, is unable to work, and has a large family to support, and has no money to engage a lawyer, would be at the mercy of the person who disabled him because, being in a superior economic position, the injuring person could force on his victim, desperately in need of money to keep the candle of life burning in himself and his dependent ones, a wholly unconscionable meager sum in settlement or even refuse to pay him anything at all. Any society, and especially a democratic one, worthy of respect in the spectrum of civilization, should never tolerate such a victimization of the weak by the mighty. *Richette v. Solomon*, 187 A.2d 910, 919 (Pa.1963).

2. See Comment, *Judicial Regulation of Contingent Fee Contracts*, 48 J.Air L. & Comm. 151, 158 (1982); Pollack, *Book Review*, 90 Harv.L.Rev. 482, 484 (1976); Corboy, *Contingency Fees: The Individual's Key to the Courthouse*, 2 *Litigation* 27 (1976); R. Keeton, *Venturing To Do Justice: Reforming Private Law* (1969).

3. See Statements of Barry Keene, leader of the Association for California Tort Reform, that restrictions on contingent fees are necessary to "reduce financial incentives that encourage lawyers to file unnecessary, unwarranted and unmeritorious suits." 9 ABA/BNA *Lawyers' Manual on Professional Conduct* No. 20 at 320 (1993).

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and a means of exacting outrageously high fees for already overpaid lawyers.<sup>4</sup> This Committee does not propose in this opinion to take a role in this often intense public policy debate, which has been and will continue to be played out in Congress, state legislatures and other places in the political arena and within the profession.

Rather, the Committee confines its discussion here, in accordance with the specific question addressed to it, to the circumstances under which the charging of contingent fees could violate either the ABA Model Rules of Professional Conduct (1983, as amended) or the ABA Model Code of Professional Responsibility (1980). In particular, the Committee has been asked if it is an ethical violation for a lawyer to charge a contingent fee a) to a client who can otherwise afford to pay on a non-contingent basis or b) in a matter where liability is clear and some recovery is likely. The Committee has also been asked c) whether a personal injury lawyer operating under a contingent fee agreement is obligated to solicit an early settlement offer and d) whether the same lawyer can charge a contingent fee on the amount of recovery that was the subject of a rejected early settlement offer. Finally, the Committee has been asked if it is ethical to charge a contingent fee whose percentage increases e) as the litigation proceeds and f) as the recovery increases.

These are all appropriate questions of professional ethics, properly addressed to this Committee. Without taking sides on the inflammatory and divisive policy issues these questions may evoke, the Committee can answer the questions in the hope of reminding the profession of important client safeguards that come into play in the contingent fee area. These safeguards, if followed, may go a long way toward reducing the larger controversy generated by contingent fees.

In the opinion of the Committee, the charging of a contingent fee, in personal injury and in all other permissible types of litigation, as well as in numerous non-litigation matters, does not violate ethical standards as long as the fee is appropriate in the circumstances and reasonable in amount, and as long as the client has been fully advised of the availability of alternative fee arrangements. The mere fact that liability may be clear does not, by itself, render a contingent fee inappropriate or unethical. Nor does the possibility that, as some have suggested, the profession's obligation to assure appropriateness and reasonable-

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4. See Brickman, *Contingent Fees Without Contingencies: Hamlet Without the Prince of Denmark*, 37 U.C.L.A.L.Rev. 29, 32-33 (1989); Grady, *Some Ethical Questions About Percentage Fees*, 2 *Litigation* 20 (1976). A study by the Rand Corporation, however, suggests that compensation received by attorneys on a contingent fee basis, if averaged over all cases, is similar to that received by attorneys compensated on an hourly basis. See P. Danzon, *Rand Corporation Institute for Civil Justice, Contingent Fees for Personal Injury Litigation*, Govt. Publication No. R-2458-HCFA at viii (June 1980). The study also suggests that prohibitions on contingency fees are likely to produce suboptimal compensation for plaintiffs and, hence, suboptimal deterrence of negligent actions because a substantial number of low and middle income plaintiffs would be deterred from filing suit. *Id.* See also Report of the Secretary's Commission on Medical Malpractice, U.S. Dep't. of Health Education and Welfare, *The Medical Malpractice Legal System* at 87, 154 (Jan. 16, 1973).

ness is sometimes honored in its breach mean that contingent fees are inherently ethically questionable. Rather, any lapse from the applicable requirements by some members of the profession simply suggests that the profession should redouble its efforts to assure that the ethical obligations associated with entering into a contingent fee arrangement are fully understood and observed.

### **B. Contingent Fees Are Employed in Multiple Situations**

It should be recognized at the outset that when we address contingent fees we are talking about a wide variety of situations. Contingent fees are no longer, if ever they were, limited to personal injury cases. Nor are contingent fees limited to suits involving tortious conduct. Contingent fees are now commonly offered to plaintiff-clients in collections, civil rights, securities and anti-trust class actions, real estate tax appeals and even patent litigation.

Nor is this compensation arrangement limited to plaintiffs. In this Committee's recent Formal Opinion 93-373, the Committee considered the ethical issues raised by the increasingly employed so-called "reverse contingent fees," in which defendants hire lawyers who will be compensated by an agreed upon percentage of the amount the client saves. The Committee concluded that as long as the fee arrangement reached between the lawyer and client realistically estimates the exposure of the defendant client, such a fee is consistent with the Model Rules.

Moreover, contingent fees are not limited to litigation practice. Fees in the mergers and acquisitions arena are often either partially or totally dependent on the consummation of a takeover or successful resistance of such a takeover. Additionally, fees on public offerings are often tied to whether the stocks or bonds come to market and to the amount generated in the offering. Banks are also hiring lawyers to handle loan transactions in which the fee for the bank's lawyers is dependent in whole or part on the consummation of the loan.

The use of contingent fees in these areas, for plaintiffs and defendants, impecunious and affluent alike, reflects the desire of clients to tie a lawyer's compensation to her performance and to give the lawyer incentives to improve returns to the client. The trend also may reflect a growing dissatisfaction with hourly rate billing.<sup>5</sup> Because of the growing importance and widespread use of contin-

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5. For example, Zoe Baird, General Counsel of Aetna Casualty & Surety Co., at the 1992 ABA Annual Meeting asserted that billing based on hourly fees is a "deeply flawed economic system" which instead of focusing lawyers on resolving client problems, encourages "too much time spent on discovery, complicated and unproductive meetings, and long uncommunicative briefs". See ABA/BNA Lawyers' Manual on Professional Conduct, 8 Cur.Reps. 286-87 (9/9/92).

Shelby Rogers, General Counsel of Texas Commerce Bancshares, and Francis H. Musselman, Managing Partner of Milbank, Tweed, Hadley & McCoy, have similarly criticized the present system of hourly billing and advocated the use of contingent fees and "success bonuses" as a means of ensuring a correlation between attorney work and value received by the client. See ABA/BNA Lawyers' Manual on Professional Conduct, 9 Cur.Reps. 254-55 (9/8/93); see also Salop & Litan, *More Value for the Legal Dollar: A New Look at Attorney Client Fees and Relationships* (Brookings Institute 1992).

This Committee has recently identified some ethical abuses that can accompany hourly billing in ABA Standing Committee on Ethics and Professional Responsibility Formal Opinion No. 93-379 ("Billing for Professional Fees, Disbursements and Other Expenses").

gent fees, the Committee will first address in detail the factors that should be considered before a lawyer and client enter into such a fee arrangement, and then address the specific questions occasioning this opinion.

**C. The Decision by the Client to Enter Into a Contingent Fee Agreement Must Be an Informed One**

Nothing in the Model Rules expressly prohibits a lawyer from entering into a contingent fee agreement with any client. Nevertheless, the lawyer must recognize that not all matters are appropriate for a contingent fee. For example, Model Rule 1.5(d) makes it clear that a contingent fee may never be agreed to, charged or collected in a criminal matter or divorce proceeding.<sup>6</sup> More to the point, in Informal Opinion 86-1521 this Committee concluded that, "when there is any doubt whether a contingent fee is consistent with the client's best interest," and the client is able to pay a reasonable fixed fee, the lawyer "must offer the client the opportunity to engage counsel on a reasonable fixed fee basis before entering into a contingent fee arrangement" (emphasis added). The Opinion pointed out that a client with a meritorious claim is entitled to representation and should not be required to relinquish a share of the claim to get representation if the client has the money to pay a reasonable fixed fee and is willing to assume the contingency risk. It may also be in some cases that a contingent fee arrangement is the only practical basis upon which a matter can be handled, but that decision should be made after consideration of the relevant facts and circumstances in consultation with the client....

In other words, regardless of whether the lawyer, the prospective client, or both, are initially inclined towards a contingent fee, the nature (and details) of the compensation arrangement should be fully discussed by the lawyer and client before any final agreement is reached.

The extent of the discussion, of course, will depend on whether it is the lawyer or the client who initiated the idea of proceeding with the contingent fee arrangement, the lawyer's prior dealings with the client (including whether there has been any prior contingent fee arrangement), and the experience and sophistication of the client with respect to litigation and other legal matters.<sup>7</sup> Among the factors that should be considered and discussed are the

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6. The Model Code contains similar provisions in DR 2-106(C) and EC 2-20.

7. This procedure meets the lawyer's fiduciary obligations to the client without unnecessarily interfering with the lawyer's right to charge reasonable fees, Model Rule 1.5; ABA Standing Committee on Ethics and Professional Responsibility Formal Opinion 329; or the freedom of contract enjoyed by both lawyer and client. See *Venegas v. Mitchell*, 495 U.S. 82, 88 (1990) (parties are free to assign part of their recovery to an attorney if they believe that the contingency agreement will increase their likelihood of recovery); *Wells v. Sullivan*, 907 F.2d 367, 369-370 (2d Cir.1990) ("absent fraud or overreaching, courts must enforce such private contingency fee agreements, which are, after all, embodiments of the intentions and wishes of the parties.... [T]o deny [plaintiffs] the option of entering contingent fee arrangements would tend to defeat the general remedial purpose of the statute by unnecessarily restricting claimants' options in securing adequate counsel or counsel of their choice").

following:

- a. The likelihood of success;
- b. The likely amount of recovery or savings, if the case is successful;
- c. The possibility of an award of exemplary or multiple damages and how that will affect the fee;
- d. The attitude and prior practices of the other side with respect to settlement;
- e. The likelihood of, or any anticipated difficulties in, collecting any judgement;
- f. The availability of alternative dispute resolution as a means of achieving an earlier conclusion to the matter;
- g. The amount of time that is likely to be invested by the lawyer;
- h. The likely amount of the fee if the matter is handled on a non-contingent basis;
- i. The client's ability and willingness to pay a non-contingent fee;
- j. The percentage of any recovery that the lawyer would receive as a contingent fee and whether that percentage will be fixed or on a sliding scale;
- k. Whether the lawyer's fees would be recoverable by the client by reason of statute or common law rule;
- l. Whether the jurisdiction in which the claim will be pursued has any rules or guidelines for contingent fees; and
- m. How expenses of the litigation are to be handled.

Notwithstanding the foregoing, however, the inquiries prompting this opinion take the position that there are two particular circumstances where contingent fee arrangements are inappropriate. To these we now turn.

#### **D. Contingent Fees May Be Appropriate when the Client Can Afford to Pay on Another Basis**

Is a contingent fee appropriate when a client can afford to pay the lawyer on a non-contingent basis? Some commentators have suggested that because one of the fundamental reasons for allowing contingent fees is that they provide the poor equal access to the court system, such a fee may be inappropriate and unethical when the client is relatively well off or otherwise able to afford a lawyer.<sup>8</sup> However, as discussed above, there is nothing in the Model Rules to prevent a lawyer from entering into a contingent fee agreement with any client, regardless of the client's means, so long as the client's decision to enter into the arrangement is an informed one.

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8. See G. Hazard, W.W. Hodes, 2 *Law of Lawyering* § 1.5 at 118, 122-23 (1993 Supp.) (suggesting that lawyers should use a different fee system for clients who can afford to bear costs); J. O'Connell, *The Injury Industry* 48 (1971) ("[L]awyers will not normally take a personal injury case on other than a contingency fee no matter how wealthy the client ... [this] suggests ... that its use is so widespread today because it is profitable for lawyers"); Comment, *Are Contingent Fees Ethical Where Client is Able to Pay a Retainer?* 20 *Ohio St.L.J.* 329 (1959).

Moreover, to state that contingent fees are only appropriate for the indigent would ignore the reality of how expensive present day litigation can be. It is not uncommon for expenses and legal fees to total hundreds of thousands of dollars through trial.<sup>9</sup> Also, it is often difficult at the outset of a matter for the lawyer to estimate accurately how much time will be expended. Therefore, it may very well be in the client's best interests, whatever the client's apparent ability to pay the fee, to agree to pay a fixed percentage of any possible recovery, rather than assume liability for a possibly prohibitively expensive legal bill that will be owed even if the client recovers nothing.

The contingent fee system essentially shifts the risk of litigation or other legal endeavor from a risk averse client to the lawyer who may be more risk neutral because of his ability to recoup his losses through his handling of other legal matters on a contingent basis.

Even for those who can well afford to pay legal fees on a pay as you go basis, such as large corporations, the client's best interests may still be served by a contingent fee arrangement. In this way the corporation can use its financial resources, which would otherwise be spent in paying for legal services, for other business purposes until such time as the merger may be consummated or an identifiable fund is available from the proceeds of a public offering.

Furthermore, both the wealthy and the impecunious client may share the desire to give their lawyers the incentive to increase the actual proceeds to the client. At least some clients think contingent fee agreements are the best, if not the only way, to give such incentives. In their view the interests of the lawyer and the interests of the client are only in true alignment when the lawyer's fee is totally contingent on a successful outcome for the client.

Thus, as discussed above, while the client's inability to pay legal fees on a non-contingent basis may be the determining factor in a conclusion that a contingent fee is appropriate, the fact that the client is able to pay such fees does not necessarily make a contingent fee inappropriate. Barring contingent fees for other than the impecunious would deny important benefits to which the well-to-do as well as the poor client are clearly entitled.

**E. In a Case in Which Liability Is Clear and Some Recovery Is Certain, a Fee Based on a Percentage of the Recovery Can Be Ethically Proper**

The Committee has also been asked to consider whether it is ethical for a lawyer to accept a matter on a contingent fee basis when liability is clear and some recovery is certain. The argument put forward is that since the lawyer is sure that the matter will result in some recovery, there is no real contingency; thus, there is no justification for a contingent fee arrangement. A variation of this argument discussed more fully under caption G below, is found in a

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9. Fees and expenses can be especially high in certain hard fought and groundbreaking litigation. A prime example is the cigarette liability litigation which has cost law firms working on a contingent fee basis millions of dollars that has not been offset by any judgment or settlement. See *The Heat Is On*, ABA Journal, Sept. 1994, at 59.

recent inquiry to this Committee which asks whether a lawyer to be compensated under a contingent fee arrangement is ethically obligated to solicit early settlement offers and whether a lawyer should be prohibited from charging a contingent fee on the amount of such offer, even if it is not accepted and the same amount is recovered after the case must go to trial.<sup>10</sup>

First, neither the Model Rules nor the Model Code mention any requirements regarding solicitation of early settlement offers and there is no valid basis for inferring such a requirement. See ABA Formal Opinion 329 (1972) (no reasonable method of fixing fees which takes into account the relevant factors set forth in the ethical rules is proscribed).

Second, the Committee is of the view that the argument may rest on a faulty notion as to the number of cases regarding which at the onset of the engagement the lawyer can say with certainty that the client will recover.<sup>11</sup> Defendants often vigorously defend and even win cases where liability seems certain.<sup>12</sup> Additionally, a previously undiscovered fact or an unexpected change in the law can suddenly transform a case that seemed a sure winner at the outset of representation into a certain loser. See, e.g., *Central Bank of Denver v. First Interstate Bank of Denver*, 114 S.Ct. 1439 (1994) (where the Supreme Court held that a private plaintiff may not maintain an aiding and abetting suit under  $\beta$  10(b) of the Securities Act of 1934, overruling every circuit court which for decades had allowed such suits).

Moreover, even in cases where there is no risk of non-recovery, and the lawyer and client are certain that liability is clear and will be conceded, a fee arrangement contingent on the amount recovered may nonetheless be reasonable.<sup>13</sup> As the increasing popularity of reverse contingent fees demonstrates,

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10. See Brickman, Horowitz & O'Connell, *Rethinking Contingency Fees*, at 28 (The Manhattan Institute 1994) (proposing that "[w]hen plaintiffs reject defendants' early offers, contingency fees may only be charged against net recoveries in excess of such offers").

11. A recent study indicates that the probability of recovery is presently decreasing, rather than increasing, in many types of lawsuits that are traditionally handled on a contingent fee basis. See *Stingier Jurors Doling Out Fewer Awards*, ABA Journal, Sept. 1994 at 20. This study shows that in medical malpractice cases the probability of recovery at trial has decreased from 37% to 31%, and, in products liability cases from 51% to 43%. *Id.*

12. In a study of 8,231 closed medical malpractice cases in the State of New Jersey from 1977 to 1992, almost 10% of patients received no recovery at all in cases where the defendant doctors' conduct was rated indefensible. See M.I. Taragin, L.R. Willet, A. Pwiltzek, R. Trout and J.L. Carson, *The Influence of Standard of Care and Severity of Injury on the Resolution of Medical Malpractice Claims*, 1992 *Annals of Amer.Med.* 780-784.

13. Evidence that, in such cases, free market forces may result in a substantially reduced contingent fee can be found in airline liability cases. In cases where airline insurers voluntarily sent out the "Alpert letter" which makes an early settlement offer and concedes all legal liability, average contingent fee rates dropped to 17% and were often only charged on a portion of the recovery. See L. Kriendler, *The Letter: It Shouldn't be Sent*, 12 *The Brief* 4, 38 (November 1982).

for almost all cases there is a range of possible recoveries. Since the amount of the recovery will be largely determined by the lawyer's knowledge, skill, experience and time expended, both the defendant and the plaintiff may best be served by a contingency fee arrangement that ties the lawyer's fee to the amount recovered.<sup>14</sup>

Also, an early settlement offer is often prompted by the defendant's recognition of the ability of the plaintiff's lawyer fairly and accurately to value the case and to proceed effectively through trial and appeals if necessary. There is no ethical reason why the lawyer is not entitled to an appropriate consideration for this value that his engagement has brought to the case, even though it results in an early resolution.

Given the foregoing, the Committee concludes that as a general proposition contingent fees are appropriate and ethical in situations where liability is certain and some recovery is likely.

That having been said, there may nonetheless be special situations in which a contingent fee may not be appropriate. For example, if in a particular instance a lawyer was reasonably confident that as soon as the case was filed the defendant would offer an amount that the client would accept, it might be that the only appropriate fee would be one based on the lawyer's time spent on the case since, from the information known to the lawyer, there was little risk of non-recovery and the lawyer's efforts would have brought little value to the client's recovery.<sup>15</sup> And even if, in such circumstances, after a full discussion, it were agreed between lawyer and client that a contingent fee was appropriate, the fee arrangement should recognize the likelihood of an early favorable result by providing for a significantly smaller percentage recovery if the anticipated offer is received and accepted than if the case must go forward through discovery, trial and appeal.<sup>16</sup>

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14. Similarly, in the case of reverse contingent fee arrangements, some savings from the amount the plaintiff demands is almost always a certainty, yet as this Committee opined in Formal Opinion 93-373, there is nothing ethically improper about entering into a fee agreement that compensates the lawyer based on a percentage of the total saved.

15. Similar reasoning has led many courts to find that it is inappropriate to charge a contingent fee in cases involving first party insurance benefits where there is no risk of non-recovery and the lawyer merely submits the claim on behalf of the client. But courts have also found that contingent fees may be appropriate in these types of cases, if the lawyer performs additional services relating to the recovery by the client. See *In re Doyle*, 581 N.E.2d 669 (Ill.1991).

16. A recognition of the amount of additional work required to take a case through trial and appeals is reflected by several states which cap percentage fees in certain types of cases but allow the percentage charged to rise after certain milestones, i.e., 25% if settled before trial, 33 1/2 if tried. See New Jersey Ct.R. 1.27(C)(f) (limiting fees in tort cases involving minors). States have also mandated differing percentages depending on the amount recovered. See N.Y.Jud.L. § 474-A (McKinneys 1994 Supp); Conn.Gen.St. Ann. § 52-251(c)(1991).



**F. Following an Early Settlement Offer Which the Client Rejects, It Is Ethical for a Lawyer to Collect a Contingent Fee Based on the Entire Recovery, Including That Portion Which Was the Subject of an Early Settlement Offer**

The analysis in the preceding section regarding early settlement offers, however, does not mean, as an inquirer<sup>17</sup> has suggested, that in order to pass ethical muster a contingent fee agreement must limit the percentage recovery on the amount originally offered to the same small percentage suggested in Part E, if the client rejects the early offer, takes the case to trial and recovers no more than what was originally offered. In that example it would be ethical for the lawyer to provide for a significantly higher percentage contingent fee on the amount originally offered if the client chooses to go the full trial route. This higher fee would recognize the substantial time and effort that is required to take the matter to trial as well as the lawyer's assumption of the real risk that the plaintiffs will lose on the merits or that any judgment at trial may be less than the early offer.

The problem created by the inquirer's proposed limitation of the lawyers' contingent fee is that such a limitation penalizes both plaintiff and lawyer in cases where, even though liability is clear, there is an honest disagreement between the parties as to the amount owed in damages. Under those circumstances the plaintiff is entitled to reject the early offer and take his claim to a judge or jury represented by a fully compensated lawyer of his choosing. The circumstance that the fact finder eventually agrees with the defendant's evaluation of the case provides no ethical reason to interfere with a mutually agreed-upon contingent fee arrangement that was reasonable and appropriate at the onset of representation.<sup>18</sup> Such interference is particularly inappropriate given the fact that Model Rule 1.2 makes it clear that all decisions regarding the objectives of representation, including the acceptance and rejection of settlement offers, are solely those of the client. It is the lawyer who is bound by the client's decision, not the other way around. The inquirer's proposal, however, results in the lawyer being penalized because she is required to pass on the client's rejection of the early offer and press forward with the litigation to a stage of the proceedings that the client chooses.

The argument for limiting contingent fees on the amount of an early offer finds no support in the ethical rules and seems to be based on the assumption that by making an early offer the defendant is conceding all liability up to that amount, thereby eradicating the possibility of non-recovery by the plaintiff.

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17. See note 10, *supra*.

18. It should be noted that under one suggested proposal the plaintiff's lawyer is penalized even if the fact finder agrees with the plaintiff's valuation of the case, because the proposal would limit any fee on the portion of the judgment which equals the early settlement offer even if much more is awarded after trial. See Brickman et al, *supra* note 10.

But early settlement offers are made for numerous reasons besides a concession of liability. And as any experienced trial lawyer knows, once an early settlement offer is rejected, the defendant and its lawyer will, in most cases, do their best to defend both against the fact of liability and the amount of damages owed. There is generally a real risk to the client and to the lawyer being paid on a contingent fee basis that such a defense will be successful. It is ethical for the lawyer to be compensated for both the time she expends to defeat any such defenses and the risk she assumes that the plaintiff will not prevail at trial or that a judgment awarded may never be collected.

The lawyer is also being compensated for the risk she assumes that the client will fire the lawyer, a right the client might exercise at any time. See *Hiscott & Robinson v. King*, 626 A.2d 1235 (Pa.Super.1993); *Covington v. Rhodes*, 247 S.E.2d 305 (N.C.App.1978); Comment on Model Rule 1.16(a)(3) ("a client has a right to discharge a lawyer at any time, with or without cause"); DR 2-110(B)(4), or that the client will insist on proceeding with the litigation through appeals or otherwise longer than the lawyer would proceed, if it were the lawyer's, rather than the client's decision.<sup>19</sup> See Model Rule 1.2. Additionally, the lawyer is being compensated for the often lengthy delay between the time work is performed and the time a fee is received.

**G. There Is No Ethical Requirement for a Plaintiff's Lawyer Whose Compensation Agreement Is Contingent on the Recovery to Solicit an Early Settlement Offer from the Defendant**

An inquirer has asked whether, as an ethical matter, the plaintiff's lawyer must solicit an early offer of settlement. The Committee concludes that there is no such ethical requirement. First, neither the Model Rules nor the Model Code require any such solicitation. Second, the suggestion seems inequitable as no reciprocal requirement for the defendant to make an early settlement offer is imposed. Any requirement to seek an early settlement offer would raise fundamental problems. Plaintiff's counsel, whether proceeding on a contingent fee basis or not, must be free (with appropriate consultation with the client) to select her own strategy. It may be that at the outset of the litigation, she doesn't have enough information about the defendant's conduct to make an intelligent evaluation of a settlement offer. For example, she may not know whether liability is clear or uncertain or whether exemplary damages may be available. Additionally, the plaintiff's damages at that juncture may still be a matter of significant uncertainty, with respect to either extent, per-

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19. "The ordinary rule of construction of contingent fee contracts is that, absent an express provision otherwise, services rendered by the attorney in upholding a judgment on appeal are within the underlying contract." *Attorney Grievance Commission v. Korotki*, 569 A.2d 1224 (Md.1990). See also *New York City Ethics Opinion 1986-6*; *Michigan State Bar Committee on Professional & Judicial Ethics Formal Opinion R-11* (1991). Conversely, if the client decides to voluntarily dismiss a case that the lawyer considers meritorious and likely to succeed, the lawyer cannot recover on a contingent fee contract.

manence, or both. Finally, the plaintiff may have decided that he does not, under any circumstances, wish to settle or enter into settlement negotiations.

As an ethical matter, these are all matters to be decided between lawyer and client; there is no ground in the Model Rules for suggesting that the lawyer who is retained on a contingent basis and the plaintiff who retained her should be any less free than a lawyer who is compensated on some other basis to decide with her client whether and when to solicit or make a settlement offer. While the ethical rules require that any strategy pursued by the lawyer be directed to the client's best interests, it is not the role of the ethical rules to force lawyers to follow any specific litigation strategy or approach. Additionally, any proposed rule that seeks to dictate a particular strategy in all cases would be in conflict with Model Rule 2.1 which requires a lawyer to exercise her independent professional judgment on behalf of her client.

#### H. The Contingent Fee Arrangement Must Be Reasonable

In addition to the requirement that a fee be appropriate, Model Rule 1.5 requires that the fee, whether based on an hourly rate, a contingent percentage or some other basis, "shall be reasonable." Similarly, DR 2-106 prohibits a "clearly excessive fee," which is in turn defined as a "fee ... in excess of a reasonable fee."<sup>20</sup>

In deciding whether a contingent fee arrangement is reasonable the lawyer must consider the following factors set forth in Model Rule 1.5(a):

- (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.

Additionally, the lawyer must look again at, and discuss with the client, the factors that were considered in reviewing the appropriateness of the fee, discussed in Section C above.

We stress that the lawyer should take all these factors into account in evaluating every case. See ABA Formal Opinion 329 (1972). For this reason, a lawyer who always charges the same percentage of recovery regardless of the particulars of a case should consider whether he is charging a fee that is, in an ethical context, a reasonable one. One standard fee for all cases may have the

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20. DR 2-106 provides that "[a] lawyer shall not enter into an agreement for, charge, or collect an illegal or clearly excessive fee." A fee is "clearly excessive" under DR 2-106 "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."

effect, given the difference among cases, of both over- and under-compensating the lawyer. Cf. *In re Recorder's Court Bar Association v. Wayne Circuit Court*, 503 N.W.2d 885 (Mich.1993) (finding that a fixed fee system for compensating attorneys who represented indigent defendants that did not take into account the particulars of the case was unreasonable).

As with the question of appropriateness, the mere fact that liability may be clear and that some recovery is likely does not per se make any given contingent fee unreasonable. It is important to keep in mind that the reasonableness as well as the appropriateness of a fee arrangement necessarily must be judged at the time it is entered into. All contingent fee agreements carry certain risks: the risk that the case will require substantially more work than the lawyer anticipated; the risk that there will be no judgment, or only an unenforceable one; the risk of changes in the law; the risk that the client will dismiss the lawyer, and the risk that the client will require the lawyer to reject what the lawyer considers a good settlement or otherwise to continue the proceedings much further than in the lawyer's judgment they should be pursued. If a lawyer accepts a given risk--for example, the risk posed by the fact that the opposing party has a reputation for being intransigent in its approach to settlement--and offers a fee contract reflecting that risk, which is accepted by a fully informed client, the lawyer should not be required as a matter of ethics to give up the benefit of the agreement because the opposing party, to everyone's surprise, offers an early settlement that is acceptable to the client.<sup>21</sup> By the same token, a later development that increases the risk to the lawyer--for example, a statutorily imposed cap on liability, the loss of a summary judgment motion everyone expected to win, or the need to take three times the number of depositions originally anticipated--should not permit the lawyer to demand a new, more generous fee arrangement.<sup>22</sup>

### **I. The Percentage of a Contingent Fee May as an Ethical Matter Be Increased On the Basis of How Far the Lawyer Must Proceed in Prosecuting the Case**

The Committee has also been asked whether it is ethical for a lawyer and

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21. Brickman, *supra* note 4, at 87 ("It is not the actual effort expended by the attorney that is determinative of the legitimacy of the fee, but what a good faith, professionally informed estimate of anticipated effort and risk of non-recovery would have been prior to the commencement of representation"). (Emphasis added.)

22. See, e.g., *Chase v. Gilbert*, 499 A.2d 1203 (D.C.1985) (A lawyer cannot modify a fee agreement even if he ends up performing significantly more services than were contemplated when agreement was entered into). Because reasonableness is judged at the time the contract is entered into, there is nothing necessarily unethical about charging a contingent fee on the portion of any recovery that is equal to an early settlement offer. See ABA Formal Opinion 329 ("[n]o reasonable method of fixing fees which takes into account the factors of DR 2-106(B) is proscribed by the Code of Professional Responsibility"). It should be noted, however, that extreme changes in circumstances occurring after negotiation of the fee agreement may lead a reviewing court to decide, *ex post facto*, that payment of the fee is unreasonable. See, e.g., *Mckenzie Construction Inc. v. Maynard*, 758 F.2d 97 (3d Cir.1985).

client to enter into a fee agreement that provides for higher contingent fees after specific benchmarks, for example, 25% if the case settles within six months and 33% after trial. The higher contingent fee at advanced stages of the matter is meant to compensate the lawyer for the additional time and labor necessary in the case. As demonstrated in the factors set forth in Model Rule 1.5(a) set out above, the time and labor involved in a matter are among the reasonable bases for setting a fee. Therefore, it is the Committee's opinion that such a fee agreement is ethical as long as the overall fee is appropriate and reasonable. See, e.g., Phila.Bar Assoc.Ethics Op. 93-11 (approving such a fee arrangement).

### **J. The Percentage of a Contingent Fee May Increase with the Amount of the Recovery**

Finally, the Committee has been asked whether it is ethical for a lawyer to enter into a fee agreement that provides for a higher percentage fee as the amount of the recovery goes up or the amount of the savings increases: for example, 15% on the first \$100,000 recovered or saved, 20% on the next hundred thousand, and 25% on everything thereafter. Such an arrangement on its face runs contrary to what several states have mandated in terms of reducing the percentage recovery as the amount recovered rises.<sup>23</sup> Nonetheless, as a matter of ethics, the Committee is of the view that a percentage that increases with the amount of the recovery can be permissible. Model Rule 1.5(a) refers, in connection with the reasonableness of a fee, to "results obtained," and the "ability of the lawyer or lawyers performing the services" as factors that may be considered. Since a higher recovery would, by definition, reflect the first of these factors and, in all likelihood, reflect the other as well, the Committee is of the view that such a fee agreement is ethical, so long as the matter for which the fee is charged is appropriate and the amount of the fee is reasonable. Indeed, many would say that this form of contingent fee agreement more closely rewards the effort and ability the lawyer brings to the engagement than does a straight percentage fee arrangement, since everyone would agree that it is the last dollars, not the first dollars, of recovery that require the greatest effort and/or ability on the part of the lawyer. It may be that any lawyer would have been able to achieve a \$100,000 verdict for a given plaintiff's injuries, but that only the most skilled would have been able to secure a \$500,000 award plus an additional sum for exemplary damages.

### **K. Conclusion**

A lawyer entering into a contingent fee arrangement complies with the ethical standards set forth in both the Model Rules of Professional Conduct and the Model Code of Professional Responsibility if the fee is both appropriate and reasonable and if the client has been fully informed of all appropriate alternative billing arrangements and their implications. Contingent fee arrangements are appropriate for both the affluent and those who cannot otherwise afford the lawyer's services. It is not necessarily unethical to charge a

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23. See, Calif.Bus. & Prof.Code § 6146 (West 1990); see also note 16, supra.

contingent fee when liability is clear and some recovery is anticipated. A lawyer compensated on a contingent basis has no obligation to solicit on behalf of the client an early settlement offer; further, she may collect a contingent fee on the total recovery, including any amount that was the subject of an early settlement offer. Finally, a lawyer may charge a different contingent fee at different stages of a matter, and may increase the percentage taken as a fee as the amount of the recovery or savings to the client increases.

is permissible as long as the attendant ethical obligations are met. These include the obligation to assure that any representations that have been made regarding the relationship are clear and not misleading, and the obligations to avoid conflicts and preserve confidences as may be entailed by the actual circumstances of the relationship. Related firms should also see to it their fee and referral arrangements do not conflict with applicable ethical rules.