NYPRR | December 2002

Non-Refundable Fees: Pitfalls And Safe Harbors

BY SARAH DIANE MC SHEA

Eight years ago, the New York Court of Appeals affirmed a two-year suspension imposed on a lawyer who charged minimum, non-refundable fees to three clients, and then refused to refund any part of the fees, even though he was discharged before their matters were completed. *Matter of Cooperman,* 83 N.Y.2d 465 (1994). The Appellate Division was outraged at the minimum, non-refundable fees Cooperman charged to handle two criminal cases - $10,000 and $15,000, respectively - and found it "unconscionable" that a lawyer would claim that he had earned such large amounts merely for filing a notice of appearance. *Matter of Cooperman,* 187 A.D.2d 56 (2nd Dep't 1993). The Court of Appeals agreed and held that "non refundable" retainers were inherently unethical and improper. The Court distinguished general retainers, which secure a lawyer's appearance, but are not applied to any legal services which the lawyer might render.

According to the Court of Appeals, fees paid in advance for future legal services must be refundable, or the client's right to freely discharge the lawyer will be thwarted. Public policy, said the Court, favors a client's unimpeded right to counsel of the client's choosing. A non-refundable retainer inhibits a client's ability to fire one lawyer and hire another one and therefore cannot be permitted. The primary exception is when the retainer is paid not for services to be rendered, but rather for the lawyer's general availability. *Martin v. Camp,* 219 N.Y. 170 (1916). Retainers may also be non-refundable when the lawyer has incurred expenses or changed her position in reliance on the client's promise to use the lawyer's services. *Atkins & O'Brien LLP. v. ISS International Service System, Inc.,* 252 A.D.2d 446 (1st Dep't 1998).

All other advance retainer payments are said to be refundable, at least in principle, if the client discharges the lawyer before the representation is complete. However, it is clear from the steady stream of reported cases (criminal, civil and disciplinary) that lawyers continue to charge what are in essence "non-refundable" retainers. Sometimes these are upheld and, other times, they result in loss of fees or disciplinary sanctions. Notwithstanding the sweeping language in *Cooperman,* it seems clear that some non-refundable retainers are perfectly proper and ethical. While it is almost certainly inadvisable to include the words "non-refundable" in any retainer agreement, the use of that language does not seem to be a per se violation of the ethics rules or to result automatically in fee forfeiture.

In *Matter of Tate,* 258 A.D.2d 120, 691 N.Y.S.2d 477 (1st Dep't 1999), a disciplinary committee hearing panel held that what was characterized in the lawyer 's retainer agreements as a "non-refundable retainer" was actually an initial fee payment for "availability" that was "earned when paid" and, therefore, did not violate *Matter of Cooperman.* However, the Tate case is a cautionary tale, for Tate had been initially suspended on an interim basis, in part because she used "non-refundable" retainer agreements. (*Matter of Tate,* 233 A.D.2d 53, 662 N.Y.S.2d 482 (1st Dep't 1997)).

In *Landa v. Sullivan,* 255 A.D.2d 295, 679 N.Y.S.2d 323 (2nd Dep't 1998), the Appellate Division upheld a lawyer 's claim to fees on an account stated theory, although the original fee agreement with the client

called for a minimum non-refundable retainer. This is consistent with cases in the matrimonial field which award quantum meruit fees to lawyers whose retainer agreements are nonexistent, improper or unenforceable. *Markard v. Markard,* 263 A.D.2d 470 (2nd Dep't 1999); *Hom v. Hom,* 210 A.D.2d 296 (2nd Dep't 1994). It appears that the lawyer 's submission of regular billing statements in *Landa* helped him to preserve a fee that otherwise might have been lost.

Careful lawyers nonetheless will avoid using the term "non- refundable" in their retainer agreements. The term invites a level of scrutiny that may be avoided by better drafting and more careful articulation and explanation of the actual fee arrangements. However, as was evident in *Ramirez v. Aidala,* Sup.Ct, New York Cty. (September 2002) (*see* NYPRR, November 2002, page 4), merely avoiding use of the term "non-refundable" is not enough. With few exceptions, the fee charged must be reasonable, agreed to by the client and, if the services are not performed, refundable.

How To Assure Adequate Compensation?

Many lawyers are understandably reluctant to be retained on small cases or short representations and properly want the client's assurance that the representation will be worth the bother. Promises being what they are, these assurances are best secured financially. The lawyer's concern at the beginning of each new representation is to make sure that his efforts will be worth the attendant risks and burdens. The client's concern is to get zealous and devoted representation for a reasonable legal fee.

The gold standard for the courts has been hourly billing: you can count the hours spent by the lawyer, evaluate the reasonableness of the hourly rate and arrive at a total fee. The appeal of hourly billing is that it is an easy way to calculate the value of legal services and has the aura of objectivity. However, hourly billing arrangements are unsatisfactory in many types of legal matters and have come under considerable fire recently. (*See,* The New York Times, "Stop the Clock? Critics Call the Billable Hour a Legal Fiction" (10/29/02)). Many clients prefer flat fees, which have the benefit of predictability and do not reward lawyer inefficiency. Lawyers, also, are increasingly disenchanted with hourly fees, which often do not reflect the real value of the lawyer's services or provide sufficient incentive for the lawyer to take on the small matter or the new client.

While the benefits of taking on new clients seem obvious, experienced lawyers are well aware that the risks presented by new clients may often outweigh the benefits. The potential consequence to the lawyer of accepting a new client or matter is increased exposure to potential civil liability for errors and omissions, as well as the increased risk of discipline that comes with each new matter, not to mention the impact on the lawyer's ability to devote adequate time and attention to existing clients.

Each new representation also means that the lawyer may not be able to take on other clients in unrelated matters. This may be described as a "time and availability conflict." Each new representation also means that the lawyer may be barred by conflicts rules from representing other clients in the same matter. This may be described as an "interest conflict."

Reasonable fees that secure a lawyer's appearance (and compensate the lawyer for the loss of other or future business) are ethical and proper. Cooperman held that lawyers could not charge "non-refundable" retainers, but left intact retainer payments which are not meant to be applied to future legal services.

Thus, minimum fees and classic retainers, which secure the lawyer's appearance, were both proper, according to Cooperman.

Classic general retainers are of little help to lawyers who seek a client's assurance that the retention will not be a financial disaster for the lawyer. The classic general retainer is paid to secure a lawyer's availability to the client for a stated period of time. It is not applied to any actual legal services rendered by the lawyer - those are billed separately and in addition to the retainer. Of course, many clients are not willing to pay a general retainer and then pay additionally for specific legal services. Most frequently, the client retains the lawyer to handle a specific matter, not to be available for any legal representation which the client may need in the future. How, then, may the lawyer structure her fees to protect her interests?

Appearance Or "Conflict" Fee

Without running afoul of the rules, it seems clear that a lawyer may charge a fixed fee for undertaking to represent a client. A fixed fee may properly be characterized as a "minimum" fee and may include an "appearance" or "conflict" fee, as well as payment for actual legal services. The fee must be reasonable, in compliance with DR 2-106(b), and it should be accurately described in a retainer agreement. Often, it can be helpful to include the reasons why the fixed fee is being charged, and, what amount is solely for appearing in the matter.

An important element of an "appearance" or "conflict" retainer is that, like the general retainer, it secures the lawyer 's involvement on the client's behalf. It typically is not applied to work done by the lawyer, for its purpose is to compensate the lawyer reasonably if the client discharges the lawyer a day (or a week) later, but before the lawyer has rendered significant legal services. It is helpful, of course, if the lawyer makes clear to the client what her problems and concerns are, e.g., the client switching counsel and the lawyer being conflicted out of taking on other clients with differing interests in the same or substantially-related matters.

A lawyer may also charge a "minimum" fee for representing a client. A minimum fee is the lowest fee which the lawyer will charge the client for representation in a matter. A note of caution is warranted here, for a minimum fee is at least partially refundable if the lawyer does not complete the representation. Also, the minimum fee is subject to review for "reasonableness" under DR 2-106, which sets forth 8 factors to be considered in evaluating whether a lawyer's fees are reasonable. While a client may pay all or a part of the minimum fee in advance, the lawyer must be prepared to refund the "unearned" portion of the minimum fee if the representation is terminated, even if the relationship is precipitously, prematurely or unfairly terminated by the client.

Given the impossibility of making minimum fees non- refundable, it is generally beneficial to the lawyer to describe in the fee agreement how the fees will be calculated in the event the representation is terminated before the work is completed. It is also advisable to keep detailed and contemporaneous time records, since hourly billings remain the favorite method used by courts in calculating fees when disputes arise. Keeping good time records may be tedious and bothersome, but often it is ultimately worthwhile when disputes arise.

Reasonableness Is Key Element

Characterizing a client's payment as a "general" retainer or an "appearance" or "conflict" retainer will not be sufficient to avoid the refundability problem raised by Cooperman, unless the arrangement is both reasonable and agreed to by the client. This was evident in the recent *Ramirez case, supra,* in which the court rejected a lawyer 's characterization of the $75,000 advance payment made by the client as a "general retainer." Instead, the court found the payment to be an advance retainer for legal services to be rendered in a criminal matter. Although the lawyer's retainer agreement, which was never signed by the client, specified that the payment was a "general retainer" and a "fee for my availability" up to the point of trial, the court rejected this, concluding that Ramirez had *hired* Aidala to represent him in the criminal matter and directing Aidala to return the retainer, minus the value of the services actually rendered to Ramirez, who discharged Aidala two weeks after retaining him. It seems likely that Aidala would have retained a larger portion of the retainer, if his fee agreement had specified a more reasonable (and smaller) amount for his availability.

It ought to be clear by now - eight years after Cooperman - that non-refundable retainer agreements are prohibited and will not be enforced. Even if the advance fee payment is not described as non-refundable, if the net effect of the fee agreement is to prevent the client from discharging the lawyer and recovering the unearned portion of the advance fees, the fee agreement will be set aside and the lawyer will be left with quantum meruit fees only. It is also clear that courts are fairly astute at separating true "general" retainers from subterfuges in the guise of non-refundable fees. These are rarely effective in preserving the advance "retainer" payments when the lawyer is discharged prior to completion of the representation.

Lawyers may properly employ, however, a far broader array of ethical fee arrangements than simple hourly billing. Obviously, it is important to be accurate and precise in describing the fee arrangements in any retainer agreement. It is also important to be reasonable. Lawyers who overreach are not treated sympathetically by reviewing courts or disciplinary agencies. Sophisticated practitioners often find it useful to get independent professional advice and sometimes even independent counsel for the client, if there is any doubt about the propriety or enforceability of a proposed fee arrangement. This has been effective (and financially worth while) for lawyers who contemplate significant fees and are concerned about the possibility that a client will later renege on the fee agreement.

It is worth mentioning here that ethics experts and risk management analysts are nearly unanimous in their endorsement of written retainer agreements, which are now mandatory in New York for many types of representations. The consensus is that written agreements largely inure to the benefit of lawyers, although most of them have yet to realize the potential benefits. The model retainer agreement (letter of engagement) drafted by Professor Roy Simon (NYPRR, March 2002, page 9) is a "must have" for practicing lawyers.

In the words of Hill Street Blues' Sergeant Esterhaus, "be careful out there."

Sarah Diane McShea represents lawyers and law firms in ethics matters and disciplinary proceedings.

© Copyright 2008 −The New York Professional Responsibility Report (NYPRR)