

REASONABLE FEES AND COSTS IN THE AGE OF COMPUTERS:
AN ETHICAL DILEMMA

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By
Gary L. Stuart
JENNINGS, STROUSS & SALMON, P.L.C.
One Renaissance Square
Two North Central
Phoenix, Arizona 85004-2393
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Preface

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American Lawyers have seen a dramatic change in the practice of law in the last few years. The first significant change is the advent of electronic databases and the ability to access and manipulate information. The second significant change is the wake up call to our clients regarding our fees and costs.

The ability of a transactional lawyer to create legal documents on a computer now allows you to do in one day what it took you several days to accomplish just a few years ago. Of course, you have to invest a great deal of money and a fair amount of time in upgrading yourself and your office to computer literacy. While you are making this concerted effort to be more efficient, your clients have been busy analyzing your bills and discovering "fee abuse" all over the country.

The old English custom of slipping money into the barrister's robe was an acceptable method of compensating lawyers a century ago. Now, lawyers seem determined to dig the grave of the profession even deeper by the insistence on exorbitant hourly rates for fees whose only measurement is "by the hour".

Thus, I see the paradox in our practice along the following lines. If computers allow us to do our work in half the time, are we going to cut our fees in half? If not, are we going to do twice as much work and thus try to serve twice as many clients? Does serving twice as many clients really benefit any of them? Even if it did, does it say anything about the principled and honorable profession that we thought we joined years ago?

The Fee Contract

The fee arrangement between a lawyer and the client is contractual in nature. The ethical issues regarding fees start with the lawyer's duty of communication under ER 1.4. The rule requires the lawyer to explain all matters to the extent reasonably necessary to permit the client to make informed decisions regarding the representation. The essence of the fee arrangement must be clearly communicated to the client so that the client can make an informed decision about the fee.

ER 1.5 (b) specifically requires the lawyer to communicate the "basis or rate of the fee" to the client either before or within a reasonable time after commencing the representation. With respect to any fee that is "non-contingent" the communication regarding the fee should, but not must, be in writing. Contingent fees must be in writing pursuant to ER 1.5(c).

The standing committee on Ethics and Professional Responsibility of the ABA rendered an important opinion regarding billing for professional fees, disbursements, and other expenses on December 6, 1993, in its Formal Opinion 93-379. The thrust of the opinion is the ethical requirement for full disclosure of the basis for billings and the nature of disbursements. In summary, the ABA concludes that, absent a contrary understanding, any invoice for professional services should fairly reflect the basis on which the client's charges have been determined.^{1/}

In what appears to be a matter of first impression for the ABA, the Committee makes three categorical statements:

(i) A lawyer may not bill more time than he or she actually spends on a matter, except to the extent that the lawyer rounds up to minimum time periods.

(ii) A lawyer may not charge a client for overhead expenses generally associated with properly maintaining, staffing, and equipping an office; however, the lawyer may recoup expenses reasonably incurred in connection with the client's matter for services performed in-house, such as photocopying, long distance telephone calls, computer research, special deliveries, secretarial overtime, and other similar services, so long as the charge reasonably reflects the lawyer's actual cost for the services rendered.

(iii) A lawyer may not charge a client more than his or her disbursements for services provided by third parties such as court reporters, travel agents, or expert witnesses, except to the extent that the lawyer incurs costs additional to the direct cost of the third-party services.

The ABA cites, as the basis for its opinion on billing standards, Model Ethical Rule 1.5, and, as its moral force, the "common perception that pressure on lawyers to bill a minimum number of hours and on law firms to maintain or improve profits."

In its opinion, the ABA comments on the necessity for identical treatment of prospective clients sought by "advertising" and actual clients already acquired:

It is clear under Model Rule 7.1 that in offering to perform services for prospective clients it is critical that

^{1/}ABA Comm. on Ethics and Professional Responsibility, Formal Op. 93-379 (1993).

lawyers avoid making any statements about fees that are not complete. If it is true that a lawyer when advertising for new clients must disclose, for example, that costs are the responsibility of the client, *Zauderer v. Office of Disciplinary Counsel*, 471 U.S. 626 (1985), it necessarily follows that in entering an actual client relationship a lawyer must make fair disclosure of the basis on which fees will be assessed.^{1/}

The ABA also took the opportunity in its Formal Opinion 93-379 to chastise zealous billers with the following blunt language:

A lawyer who spends four hours of time on behalf of three clients has not earned twelve billable hours. A lawyer who flies for six hours for one client, while working for five hours on behalf of another, has not earned eleven billable hours. A lawyer who is able to reuse old work product has not re-earned the hours previously billed and compensated when the work product was first generated.^{1/}

. . . it is impossible for a lawyer to create an additional source of profit for the law firm beyond that which is contained in the provision of professional services themselves. The lawyer's stock in trade is the sale of legal services, not photocopy paper, tuna fish sandwiches, computer

^{2/}*Id.* at 7.

^{3/}*Id.* at 11.

time or messenger services.^{1/}

The use of a "nonrefundable fee" retainer has been held to be unethical and described as "unconscionable in spite of the inherent right of attorneys to enter into contracts for their services."^{1/}

The *Cooperman* court said that the use of nonrefundable fee arrangements violated the lawyer's obligation to refund unearned fees upon termination of the lawyer-client relationship. The court also noted that nonrefundable fees differed from minimum fee agreements in that the latter was a forecast of the minimum amount the client can expect to pay. Under minimum fee agreements the lawyer is paid under a quantum meruit basis if discharged by the client before termination of the case.

Amount of the Fee

In the United States, the lawyer has always been regarded as having a legally enforceable right to compensation for professional services, whether by virtue of special agreement or on a quantum meruit basis.^{1/} A client is not bound to accept advice given in error; however, where the client has requested advice, he or she must pay for it, even though declining to follow it.^{1/}

Prior to the adoption of ABA Model Rules in the early 1980's, the test regarding the amount of a lawyer's fee was whether it was "excessive." With the adoption of the Model Rules, the test has become one of "reasonableness." ER 1.5 mandates that fees shall be reasonable and details eight separate factors to be considered in ER 1.5(a).

The historic decision by the Supreme Court regarding attorneys' fees is *Goldfarb v. Virginia State Bar*.^{1/} *Goldfarb* considered a fixed fee schedule for Virginia lawyers, which recommended minimum prices for common legal services. The Court

^{4/}*Id.* at 17.

^{5/}*In re Cooperman*, 591 N.Y.S.2d 855, 857 (1993).

^{6/}*See* 172 AM. ST. REP. 841 (1908); *History of Right to Sue for Fees*, Adams v. Stevens, 26 WEND. 451 (1841).

^{7/}HENRY S. DRINKER, LEGAL ETHICS (1953).

^{8/}421 U.S. 773 (1975).

held that the fee schedules represented anti-competitive conduct by lawyers within the reach of the Sherman Act. The Court commented that the interest of the states in regulating lawyers is especially great because lawyers are essential to administering justice as "officers of the courts."^{9/}

In the Comment to ER 1.5, the ABA reminds lawyers that it is not necessary to recite all the factors that underlie the basis of the fee, only those that are directly involved in its computation. It is sufficient, for example, to state that the basic rate is an hourly charge, or a fixed amount, or an estimated amount, or to identify the factors that may be considered in finally fixing the fee.

Costs and Expenses

Under ER 1.8(e), lawyers may advance court costs and expenses of litigation provided the client remains ultimately liable for such costs and expenses. Pursuant to ER 1.8(j), lawyers may acquire liens to secure either fees or expenses. The advancement of costs and expenses in personal injury cases has triggered numerous legal and ethical opinions.

In ABA Opinion 246,^{10/} the Committee held:

A contract for a reasonable contingent fee where sanctioned by law is permitted by Canon 13, but the client must remain responsible to the lawyer for expenses advanced by the latter. There is to be no barter of the privilege of prosecuting a cause for gain in exchange for the promise of the attorney to prosecute at his own expense.^{11/}

Fees by the Hour

^{9/}*Id.* at 792.

^{10/}ABA Comm. on Professional Ethics and Grievances, Formal Op. 246 (1942).

^{11/}*Id.* at 7 (citing *In re Gilman*, 251 N.Y. 265, 270-71 (1929)).

As our profession became more "businesslike", we discovered that lawyers who kept accurate track of their time seemed to make more money than those who did not. Logging time on an hourly basis during the course of the workday became the standard by which lawyers sought to justify fees charged to clients.^{12/}

Of course, in the pre-computer days, lawyers largely believed that an hour of time in the library or at your desk with a dictating machine or in your client's office at a meeting all had the same common denominator: an hour of time is an hour of time. Now we have a different dilemma: an hour of time on a computer may be "worth" more than an hour of time.

Fixed fees were the norm before they were deposed by the hourly rate obsession. However, with the advent of word processors, routine legal services became standardized. Consequently, things like simple Wills, real estate conveyances and debt collection matters are, once again, being billed on a fixed fee basis. Where the lawyer's effort is inadequately defined by the amount of time the lawyer will have to expend to accomplish the client's objective; fixed fees are satisfactory remedies. The client gets a definite and limited cost and the lawyer secures the client's future business for routine and repetitive legal tasks. The fixed fee was informally approved by the ABA in 1977.^{13/}

Alternative Fees

There are many forces at work in changing the way that lawyers charge for their services. Increased competition due to increased numbers of lawyers, the ability to advertise, the real estate slump of the 80's, the S&L crisis and a nationwide recession are only the beginning of the list. If one adds to this list the fact that technology will make lawyers much more efficient, it is easy to conclude that the pressure on hourly billings will become even more intense in the near term.

Innovation in lawyer compensation and billing systems has been the subject of many conferences and articles. The ABA Section of Economics of Law Practice published an excellent compilation of articles on the subject in 1989.^{14/} At its

^{12/}Smith, *Toward Value Billing: An Artificial Intelligence Approach*, 15 Legal Econ. 23 (Nov. /Dec. 1989); Ross, *The Ethics of Hourly Billing by Attorneys*, 44 Rutgers L. Rev. 1, 11-12 (1991).

^{13/}ABA Informal Opinion 1389 (1977).

^{14/}*Beyond the Billable Hour; an Anthology of Alternative Billing Methods* (R. Reed Ed. 1989).

1992 Annual Meeting, the ABA Section of Litigation published another interesting collection of studies and essays along with a bibliography.^{15/}

Reasonableness

Whether one charges by the hour, the legal project or some combination thereof, the ethical standard against which fees are measured is reasonableness. This single guideline governs all fees and costs. Reasonableness is much more than an ethical issue. It is also an economic issue, a practical issue and an important factor in lawyer-client relationships.

It is an ethics issue because ABA Model Rule 1.5 categorically states that a lawyer's fee shall be reasonable. The Rule allows eight separate factors to be considered in determining the reasonableness of a fee. The first factor identified in E.R. 1.5 is time. I submit that it is less important than the other factors that make up "reasonableness", particularly within the context of practicing law by, for and with computers. The other factors that lawyers are allowed to use in determining the reasonableness of a fee include the novelty and difficulty of the issue, the skill needed to represent the client, the likelihood that the work will preclude other employment, customary fees, results, time limitations, and, the amount involved. Even without considering the computer connection, I believe that the other factors ought to be more important in determining the reasonableness of your fee for any legal service. Indeed, an argument can easily be made to demote time to the bottom of the list of factors.

Internal expenses incurred on behalf of a client were largely absorbed by lawyers 25 or so years ago. As we became more "businesslike", we began to collect and organize our disbursements for the purpose of seeking reimbursement and thus improving the cash flow of our "business". Costs, like fees, are subject to the ethical test of reasonableness. We can charge our clients only what we ourselves pay for the item or service we designate as a "cost". We cannot add a surcharge to the cost of a particular product or service that we incur "unless the lawyer herself incurred additional expenses beyond the actual cost of the disbursement item".^{16/} We cannot profit by charging our clients more than we actually pay for in-house services. As previously noted by the ABA, our stock in trade is the sale of legal services, not "tuna fish sandwiches, computer time

^{15/}Value billing in gaining a competitive advantage in the legal marketplace (8 Lawyers Manual on Professional Conduct 286 (1992)).

^{16/}ABA Formal Opinion 93-379 (1993).

or messenger services".^{17/}

The other way that the test of reasonableness applies to costs is in the context of fees charged to the client. When costs are added to fees, the total charged to the client must still be reasonable.^{18/} It is in this context that the issue of the cost of computer assisted research initially became an ethical issue. Illinois addressed the question in 1986 when it approved the practice of a lawyer passing on to clients the cost of computer assisted research.^{19/} The Philadelphia Bar approved the practice of billing the on-line costs of computer research in 1987.^{20/} Maryland also approved the practice of billing clients for legal research services in 1991.^{21/} It is believed that these three states are the only ones to have officially addressed the issue of billing the costs of computer-assisted research or on-line services.

Unfortunately, neither the ABA nor any particular state has yet addressed the more difficult question of establishing a reasonable fee for the legal document prepared by a transactional lawyer largely on the basis of a computer data base and a software program that literally "creates" the legal product.

Legal Bureaucracies

The business clients served by transactional lawyers went from good business to big business to multinational to conglomerates between World War I and the Vietnam War. While traditional beliefs in individual enterprise survived, a new ideology emphasizing efficiency and specialized expertise emerged in the business world during this period of time. The parallel only became true within the American legal profession following the Vietnam War.

The legal profession went from full service firms in regional financial centers to giant firms with branch offices everywhere and specialized expertise so narrow as to be undefinable. It may not be a mere coincidence that the expansion of law firms

^{17/}IBID.

^{18/}ABA Model Ethical Rule 1.5.

^{19/} Illinois Ethics Opinion 85-9 (1986).

^{20/}Philadelphia Ethics Opinion 87-23 (1987).

^{21/}Maryland Ethics Opinion 92-19 (1991).

into branches occurred, about the same time that we got into the business of advertising, firm brochures and beauty contests for new clients. The "image" of the profession became inseparable from our normal "business" practices. The most striking social change in the legal profession was bureaucratization. This was not limited to private practice because corporate entities dramatically increased in-house legal staffs, and mid-sized companies brought in salaried lawyers. Part of this was undoubtedly due to the economic pressure on business managers to reduce their legal costs. That pressure came full circle by causing lawyers to increase hourly rates in an effort to stay even in an ever increasingly competitive market.

Now, we seem to be facing a new challenge whereby there are more lawyers with less work to do, complicated by the technological fact that the work can be done in less time via computers.

The Computer Problem

Computers allow law firms who routinely charge "high hourly rates" to compete effectively with smaller firms that offer lower rates. This happens because lower rate firms that handle routine transactions cannot compete on price with a high-rate firm that uses a modern document assembly program. Electronic document assembly is the process of having a computer put together what has been written before to create the document needed now. This helps lower the firm's "cost" by allowing junior lawyers and nonlawyer personnel to enhance the effectiveness of senior lawyers.

The question that inherently flows from this phenomenon is how to reasonably charge the client for the increased effectiveness. This is not to say that the single most important element in lawyering will be replaced by computer technology. Personal service and the quality of legal advice will continue to be the bedrock on which the lawyer-client relationship stands. Personal contacts and dedication are still vital parts of the profession. However, even these concepts will change as law firms invest wisely in computer technology. E-mail connections with clients are possible with good computer systems. Law firms that offer their clients' in-house lawyers the opportunity to search and browse electronically among the law firm's own materials secure and cement their relationships with their clients.

The computer industry envisions a world of electronic data where videotapes, graphics and information of all kinds will flow to lawyers through computers in the office, your car, your home and even your briefcase. Those who adapt quickly and efficiently as the technology expands will have a personal and professional advantage. Again, the questions that naturally follows are how will you establish a reasonable fee

for your firm's increased level of service and your own increased efficiency and availability (via modem of course).

Back when lawyers created their own documents, they often charged a fixed fee based on the value of the service. Profit was connected to productivity and the practice of law was both professionally rewarding and profitable. Then, we computerized and automated our billing systems. Those systems emphasized fees charged by the hour (or perhaps by the minute). It seemed to make sense but it became obvious that it limited annual income to the number of hours that you worked during the course of the year. Your income was now tied to how many minutes you billed rather than on how efficiently you worked. Hourly billings also focused clients on ever increasing hourly rates rather than on value and that, in turn, caused major resistance to legal fees.

While all of this was going on, we continued to create documents inefficiently, we charged high rates for lots of hours and we limited the legal options for our clients. Even the slowest clients began to realize that if our fees are based primarily on how much time it takes to do the work, we have no incentive to be more efficient. To make it worse, we either have to work longer or charge more by the hour to increase our income. If we raise the rates, we risk losing the client, and if you spend too much time on the project, you risk more than simply losing the client.

The Computer Solution

At the outset, the "solution" I am about to suggest is limited to the problem of billing the client for the document created by the computer with the assistance of the lawyer. This is not a prophylactic solution for the more serious problem, which is the dramatic increase in our level of efficiency by the intelligent use of computers.

In my opinion, the solution is to establish fee arrangements with our clients on a "value" basis that both encourages and rewards the efficiency acquired by the intelligent use of computer technology.

To test my thesis, imagine the transactional lawyer of ten years ago preparing a mortgage (or like instrument) for an important client involving a substantial piece of property for a considerable sum of money. The lawyer most likely gathered the facts, organized them and decided which particular document was needed for the transaction. The lawyer then performed whatever research was necessary to determine the essential contents of the document. This included a search for needed phrases and paragraph precedents from form books, reference books, statutes and closed files. The lawyer then continued the process until the necessary precedents were found to cover all

items to be included. This usually resulted in a process of cutting, pasting, copying and marking up old documents and forms, along with marginal notes and instructions. Often, portions of the document were handwritten or dictated. This process resulted in giving the marked up forms, word processing sections, handwritten notes and other instructions to a secretary to cut, paste and type draft. When the draft was returned, it was marked up, returned to the secretary for revisions, followed by re-markups and more revisions. Eventually, the process was terminated and the document was declared to be "in final form".

The transactional lawyer who is computer literate and who has invested wisely in both hardware and software would undoubtedly have a modern document assembly program. He or she might go about the process of preparing the document for the same client something like this: the document would be selected by screening the program menu; the text would be selected from the menu of choices; the client specific details not already included in the data base would be entered; the lawyer would then have to find something else to do while the software program assembled the document in final form.

Estimates vary widely, but the ABA's Section of Law Practice Management notes that document assembly programs result in the preparation of documents in one-tenth to one-half of the time they formerly took, both in elapsed time and real time. The ABA notes that secretaries are thus free to do more challenging and rewarding tasks and that everyone in the office is more efficient. More transactions can be documented and clients are impressed by streamlined operations.^{1/}

The End

The preface to this monograph notes the Old English custom of slipping money into a barrister's robe as an acceptable method of compensating lawyers a century ago. Actually, Professor Henry S. Drinker notes a much earlier basis for establishing fees in England in the 13th century.^{1/} Professor Drinker notes that an ordinance of the City of London of 1280 established four points in the matter of fixing the amount of compensation of a lawyer: "the amount of the matter in dispute, the labour (travail) of the sergeant, his value as a pleader (contour) in respect of his learning, eloquence

^{22/}*Winning With Computers, Trial Practice in the 21st Century, Part 2*, American Bar Association Section of Law Practice Management (1993).

^{23/}Henry S. Drinker, *Legal Ethics*, p. 173 (Columbia University Press 1953).

(facunde) and repute (donur) and the usage of the court."

I am not a transactional lawyer and really have no business advising any of you how to establish a reasonable fee for the documents you prepare or the services you render for your clients. However, having been asked to do so, I respectfully suggest the following: If your level of skill and integrity has been recognized by election to fellowship in the American College of Mortgage Attorneys, you ought to charge your client a fee based on the value of the product or service to the client. Consider the amount at risk or in issue, your effort, learning, eloquence and repute and forget (or at least minimize) how long it took you to do the job.

Gary L. Stuart
Phoenix, Arizona