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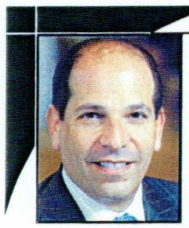
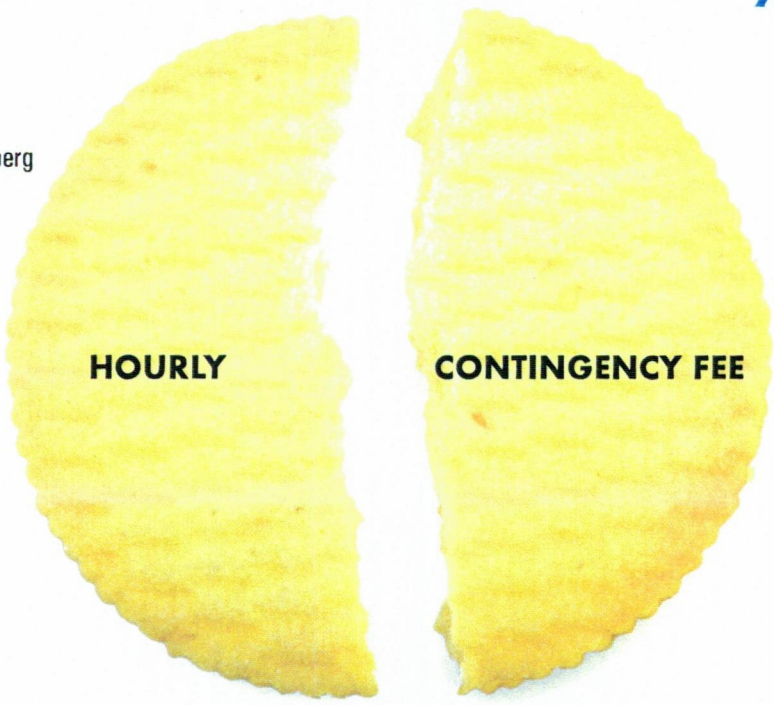


Barry P. Goldberg



"Hybrid" fee agreements work for business litigation cases

A combination of hourly and contingency fee contract may be the way to take your case the extra miles it needs for a great result in a business case

More contingency fee lawyers are being asked to prosecute business-litigation cases. More hourly-based business-litigation lawyers are being asked to prosecute cases on a contingency fee. A straight contingency-fee agreement is not well suited for business litigation because a business client may not see a case through to its conclusion, may opt for a settlement which does not include cash, or may change lawyers right when the case appears more valuable. A reasonable alternative is to insist on a "hybrid" fee agreement wherein the attorney is paid a reduced hourly rate, but accepts an "upside" on contingency.

The "hybrid" has several advantages. It is cost-effective for the client and provides the attorney with a regular cash flow within which to prosecute the case. As with any contingency agreement, the attorney has an incentive, not just to litigate the case, but to successfully conclude the case for the maximum amount possible whether by trial or settlement. Moreover, many business-litigation cases simply stall as the pre-trial hourly attorney fees escalate beyond the client's ability to pay. With a hybrid, the client's resources can be extended.

Legally defining the "hybrid" arrangement is not that easy – but, it can be done. Subject to some exceptions, "the negotiation of a fee agreement is an arm's-length transaction." (See *Ramirez v. Strurdevant* (1994) 21 Cal.App.4th 904, 913, citing *Seltzer v. Robinson* (1962) 57 Cal.2d 213, 217.) Under Rules of Professional conduct 4-200 (A), a lawyer may not enter into an "agreement for or charge or collect an illegal or unconscionable fee." The term "unconscionable" is unique to California law and has been defined, with respect to attorney fees, as "so exorbitant and wholly disproportionate to the services performed as to shock the conscience." (See, *Bushman v, State Bar of Cal.* (1974) 11 Cal.3d 558, 563; see, also, *Tarver v. State Bar of Cal.* (1984) 37 Cal.3d 122, 134.)

As long as the hybrid arrangement does not constitute a "double fee," it should be permissible. Therefore, it is recommended that the fee agreement set forth specifically the attorney's regular "customary hourly rate" for cases of like complexity and that such rate is being reduced in favor of a contingency.

In order for the hybrid relationship to work for the attorney, the attorney must be able to protect himself against the client eliminating the benefit of the upside contingency for his own business reasons. A clause in a retainer agreement prohibiting the client from settling or dismissing his lawsuit without the consent of his attorney is void as against public policy. (*Hall v. Orloff* (1920) 49 Cal.App. 745.) Therefore, the client may unilaterally decide to settle or dismiss the suit regardless of how the attorney feels about it and irrespective of whether it would destroy a valuable contingent fee. Moreover, it is not uncommon in the business context for litigation to be used as a "bargaining tool" for the next deal; i.e., a lease extension, a more favorable new contract or a million other legitimate reasons. All of these "non-cash" resolutions create problems for the prosecuting attorney to actually get paid.

Accordingly, the centerpiece of any hybrid fee agreement should be an enforceable lien and an upward readjustment of the attorney's hourly rate to compensate for the loss of the contingency. The agreement should state that the attorney will be retroactively paid his "customary hourly rate" should the client

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pull the plug on the case. For example, an experienced trial attorney may command $500 per hour or more. However, in the hybrid, he may charge a reduced rate of $150 per hour and accept a 20 percent contingency on the total of the outcome of the case. The hybrid fee agreement should state that if the client either resolves the case without the payment of a full cash value, or if the client discharges the attorney before the conclusion of the case, then the reduced rate is converted to the stated "customary hourly rate" and the balance becomes immediately due and payable. Such a provision may encourage a client to more fully consider the attorney's interest when deciding whether to resolve or dismiss the case.

Compliance with Rule 3-300

Of great importance is that an attorney's lien against a client's future recovery to secure hourly legal fees is considered a "charging lien." Fee agreements by which the attorney obtains an "ownership, possessory, security or other pecuniary interest adverse to the client" must comply with California Rules of Professional Conduct 3-300. A charging lien in this circumstance is considered an "adverse interest" requiring compliance with that rule. That rule requires "fair and reasonable" terms, full disclosure in writing, written advice to consult independent counsel (and a reasonable opportunity for the client to do so), and the client's written consent. Violation of that rule renders the lien unenforceable. However, it does not invalidate the underlying fee agreement or preclude the attorney from otherwise recovering the agreed-upon contractual fee. (See, *Shopoff & Cabvallo, LLP v. Hyon* (2008) 167 Cal.App.4th 1489, 1522-25.)

It strains reality to think that when a lawyer sits down to negotiate at arm's-length with a prospective client, as part of that negotiation, he must recommend to that the client in writing that he consult with a different lawyer before agreeing to such a charging lien. But, that is exactly what he must do according to Rule 3-300. In practical terms, such an acknowledgement can be inserted into the agreement along with a place for the client to initial that he read and understood his right to consult with another lawyer and, nonetheless, has agreed to the charging lien.

A hybrid is a contingency fee agreement with all its requirements

There is a recent case where the court determined, as a matter of first impression, that a hybrid fee agreement was a "contingency fee agreement" subject to all the statutory requirements. (*Arnall v. Superior Court* (2010) 190 Cal.App.4th 360, 369.) In *Arnall, supra*, the court found that the term "contingency fee contract" is ordinarily understood to encompass any arrangement that ties the attorney's fee to successful performance, including those which incorporate a non-contingent fee based upon the rate of payment. (*Id.* at 370.) The Court concluded that the statutory requirements on contingency fee contracts in Business and Professions Code section 6147 apply to hybrid agreements. If the requirements are not followed, the fee agreement is void. (*Ibid.*)

Section 6147 provides, in pertinent part: (a) an attorney who contracts to represent a client on a contingency fee basis shall, at the time the contract is entered into, provide a duplicate copy of the contract, signed by both the attorney and the client, or the client's guardian or representative, to the plaintiff, or to the client's guardian or representative. The contract shall be in writing and shall include, but is not limited to, all of the following:

(1) A statement of the contingency fee rate that the client and attorney have agreed upon.

(2) A statement as to how disbursements and costs incurred in connection with the prosecution or settlement of the claim will affect the contingency fee and the client's recovery.

(3) A statement as to what extent, if any, the client could be required to pay any compensation to the attorney for related matters that arise out of their relationship not covered by their contingency fee contract. This may include any amounts collected for the plaintiff by the attorney.

(4) Unless the claim is subject to the provisions of Section 6146[MICRA], a statement that the fee is not set by law but is negotiable between attorney and client. . . ."

If the attorney fails to comply with any of the section 6147 requirements, it renders the agreement "voidable at the option of the plaintiff, and the attorney shall thereupon be entitled to collect a reasonable fee." (§ 6147(b))

Handling the award of attorney fees

Because many business litigation cases involve contracts which provide an award of attorney fees and costs to the prevailing party, it is absolutely essential that the handling of those awards is spelled out clearly in the fee agreement. Where the contract is silent on the handling of attorney fee awards, the award probably will go directly to the client and would not be considered a "recovery" out of which the attorney thought he would be receiving a percentage. "In the absence of a contract expressly providing that he (attorney) may receive those fees *in addition* to his compensation under the contract; those fees must be credited to the amount payable under the contract." (*Mahoney v. Sharff* (1961) 191 Cal.App.2d 191, 195, (emphasis in original; parentheses added)

Court-ordered fees are designed to relieve the prevailing party of a fee obligation. The award cannot be considered part of the "recovery" obtained by the attorney because that would simply add to the prevailing party's contract fee obligation: "In other words, it would be paying (the attorney) attorney's fees for getting attorney's fees." (*Mahoney v. Sharff, supra*, 191 CA2d at 197 (parentheses added))

The fee agreement can designate at least three alternative arrangements for handling court-awarded fees:

(a) The fee agreement may provide that the percentage of the contingent fee will be reduced by the amount of any court awarded fee. (See, *Denton v. Smith* (1951) 101 CA2d 841, 844);

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(b) The fee agreement may provide that any court-awarded fees will be included in the total recovery for purposes of calculating the attorney's percentage fee. (See Los Angeles Bar Ass'n Form.Opn. 523 (2009) – including court-awarded attorney fees in total recovery for purpose of percentage fee calculation does not violate CRPC 1–320(A) prohibition on fee-splitting with nonlawyer);

(c) The fee agreement may provide that any court-awarded attorney fees belong to the attorney, not the client. (*Matter of Yagman* (Rev.Dept. 1997) 3 Cal. State Bar Ct.Rptr. 788, 799 – "We reject the argument that a retainer agreement violates Rule 4-200 solely because it provides that an attorney may receive both a contingent fee and a statutory fee") In such event, the attorney may be entitled to both the contract percentage fee and the fee awarded by the court.

In conclusion, a mutually beneficial agreement can be reached if counsel pays close attention to the applicable Rules of Professional Conduct concerning charging liens and contingency fees. In addition, because many business cases potentially involve the award of attorney fees, how those awards will be handled are of critical importance. The end result will be a hybrid that will allow the client to go those extra miles to obtain a great result in a business case.

Barry P. Goldberg is the principal of Barry P. Goldberg, A Professional Law Corporation, *located in Woodland Hills. Goldberg has been in practice since 1984 and attended the University of California, Los Angeles undergraduate and obtained his law degree from Loyola Law School, Los Angeles. He is an experienced trial attorney and has extensive insurance coverage experience. He has written and lectured extensively about UM/UIM Arbitrations and is a member of CAALA and the San Fernando Valley Bar Association.*