Legal Times

WEEK OF JUNE 30, 1997 • VOL. XX, NO. 7

How Should Contract Attorneys Be Billed?

By Mary Adelman

Use of contract attorneys by both corporations and law firms is clearly on the rise. Also on the rise are questions about how to bill out a contract attorney's time.

Most contract attorneys are found by corporations and law firms through an agency that specializes in identifying contract attorneys. The corporation or firm pays the agency an agreed-upon hourly rate for each of the attorneys the agency provides. The agency then pays the attorney.

The rates corporations and firms pay the agency for contract attorneys range between $30 and $125 per hour, typically one-third the billing rate of comparable associates. One of the first questions law firm attorneys ask when they are considering using a contract attorney is "How do I bill my client?"

Good question. There are essentially four ways law firms can handle the billing of contract attorneys:

• The rate the firm pays the agency for the contract attorney could be passed directly to the client.

• The amount paid to the agency could be marked up based on overhead incurred in using the contract attorney.

• Both overhead and a profit percentage could be added to the contract attorney's rate.

• The firm could bill the contract attorney at the rate it bills comparable attorneys associated with the firm.

Arguments can be made for employing any of these methods.

Should the law firm bill its client for the actual cost of the contract attorney, as a disbursement, in most instances the client would be very pleased with the savings, furthering a solid working relationship between the client and the firm.

Passing along the actual cost of contract attorneys is the method firms often choose when using numerous attorneys to review documents in major litigation.

The time that firm attorneys spend on supervising contract attorneys would normally be billed to the client.

Although the firm loses the opportunity to make a profit on much of the document production phase of the case, many firms view this loss as offset by the goodwill it engenders with the client and the fact that its fees in a major litigation will be nonetheless significant.

In other situations, such as a temporary increase in the workload, when a firm attorney takes a prolonged leave, or when none of the firm's attorneys possesses the particular expertise necessary to thoroughly evaluate or complete the project—passing on the actual cost of the contract attorney to the client may result in a loss to the firm.

If the contract attorney is working on the firm's premises, there may be overhead costs of office space, supplies, and possibly secretarial support. If the firm does not or is not allowed to pass overhead costs along to the client, so that it breaks even in the service it provides, the firm may not be motivated to use a billing method that can result in significant cost savings to the client. Accordingly, firms often include overhead costs in the fees charged to the client for the use of contract attorneys.

Whether law firms ethically can or should receive a profit on the hourly rate of contract attorneys has been the subject of debate in offices and conference rooms of corporations and law firms and in legal publications. This issue is also a concern of bar associations.

Obviously, if a contract attorney were not retained by the firm and an attorney in the firm performed the work, the law firm would receive a profit on the work. If firms did not use contract attorneys, the work would fall on firm attorneys whose billing rates are significantly higher.

If the costs for contract attorneys were required to be passed directly through to the client without the firm receiving a profit on the work, firms may be more inclined to stretch the usefulness of their own attorneys, on whom firms obviously profit, than to use contract attorneys.

Contract attorneys enable law firms to provide a valuable service to their clients without exhausting, and thereby decreasing the efficiencies of, their "permanent" attorneys.

Similarly, if firms were prohibited from making a profit on contract attorneys, it would make financial sense to bill clients for the time it would take one attorney to become proficient in a new area of law, rather than to retain a contract attorney who is expert in that particular area in which the firm lacks expertise.

None of the local bar associations in the District, Maryland, or Virginia, has issued any binding or mandatory guidance on whether clients should be informed if contract attorneys work on their matters or how clients should be billed for contract attorneys.

The D.C. Bar says it has received numerous inquiries on the subject, and anticipates issuing an opinion on the matter within the next several months.

The ABA Speaks

The American Bar Association's Standing Committee on Ethics and Professional Responsibility has issued a Formal Opinion that may shed light on the issue of whether it is ethically permissible for law firms to seek a profit on their use of contract attorneys.

In a 1993 opinion where the committee considered the manner in which law firms should handle in-house charges to clients for providing services such as photocopying, computer research, on-site meals, and deliveries, the committee wrote: "In the absence of an agreement to the contrary, it is impermissible 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 photocopying paper, tuna fish sandwiches, computer time or messenger services."

Since contract attorneys provide legal services through law firms, and the services they provide are not a newly created source of profit to firms, law firms should be able to realize a profit on the very service they were established to provide. By using contract attorneys, law firms are merely modifying the manner in which they have chosen to provide legal services.

Making this modification in the provision of legal services can be more efficient and economical than the traditional method of providing legal services—working attorneys until they are weary and no longer efficient, hiring new attorneys whose future at the firm is uncertain, or training attorneys in new areas of the law, which is often subsidized, if not paid for entirely, by the client.

In 1988, the ABA's Standing Committee on Ethics and Professional Responsibility issued a Formal Opinion on the subject of temporary, or contract, attorneys. In this opinion, the committee assumed that law firms may make a profit on their use of contract attorneys.

Disclosure Not Required

One focus of discussion in the opinion was whether the firm was even required to disclose to the client that it was using contract attorneys on client matters. The committee stated that "where the temporary lawyer is performing independent work for a client without the close supervision of a lawyer associated with the law firm, the client must be advised of the fact that the temporary lawyer will work on the client's matter and the consent of the client must be obtained."

The committee continued, however, that "where the temporary lawyer is working under the direct supervision of a lawyer associated with the firm, the fact that a temporary lawyer will work on the client's matter will not ordinarily have to be disclosed to the client."

Because firms are required to disclose their use of contract attorneys to their clients only under limited circumstances, the ABA reasoned that except in those circumstances, the firm would not have to reveal to the client the fees paid to the contract attorney or the agency.

The committee concluded that assuming that a law firm pays the temporary lawyer reasonable compensation for the services performed for the firm and does not charge the payments thereafter to the client as disbursement, the firm has no obligation to reveal to the client the compensation arrangement with the temporary lawyer.

Rule 1.5(e) of the Model Rules of Professional Conduct (1983, amended 1987), relating to division of a fee between lawyers, does not apply in this instance because the gross fee the client pays the firm is not shared with the temporary lawyer. The payments to the temporary lawyer are like compensation paid to non-lawyer employees for services and could also include a percentage of firm net profits without violation of the rules or the predecessor code.

The committee went on to state that if the firm and the temporary lawyer agree to a "direct division of the actual fee paid by the client," such as a percentage of a contingent fee, then Rule 1.5(e)(1) would require the client's consent to the arrangement.

In rejecting the notion that arrangements between law firms and agencies that specialize in the placement of contract attorneys involve a sharing of legal fees by a lawyer with a non-lawyer, in violation of Rule 5.4 or DR 3-102(A) of the code, the committee confirmed that law firms may recognize a profit on their use of contract attorneys.

"The fee paid by the client to the firm ordinarily would include the total paid the lawyer and the agency, and also may include charges for overhead and profit," the committee stated.

The committee also concluded that "the increasing use of placement agencies for temporary lawyers lends support to the view that this is an efficient and cost-effective way for law firms to manage their work flow and deployment of resources."

These ABA decisions leave little room for doubt that law firms may ethically obtain a profit on the use of contract attorneys in their provision of legal services.

Higher Rates

If, however, the law firm were to bill the contract attorney at the rate of a comparable associate in the firm, or approximately three times that which the firm is paying the agency, would this practice violate the rules of ethics?

In the committee's 1988 discussion of fee-sharing prohibitions, the only limitation the panel placed on the amount firms could bill clients for the use of contract attorneys was that firms must ensure that the total fee paid by the client is not unreasonably high.

The opinion would appear to permit the firm to bill the attorney at rates that are comparable to those of comparable attorneys associated with the firm. A law firm could take the position that if it did not use a contract attorney on the project, it would have used an

attorney in the firm, perhaps one who was distracted by other firm matters and therefore not as efficient, or an attorney who was not as experienced in the particular area as was the contract attorney.

Accordingly, even if the contract attorney is billed to the client at a rate similar to that for an attorney associated with the firm—even when that rate is triple what the firm paid the agency—the client is getting its money's worth.

Thus, the total fee charged the client would not be unreasonably high, and the ethical rules would not be violated.

Law firms will have to decide which policy they want to adopt with respect to billing clients for contract attorneys.

In-house counsel are aware that law firms in general are using contract attorneys, though many are not aware of whether their own outside counsel are using contract attorneys. Indeed, corporate counsel themselves are using contract attorneys in increasing numbers on in-house matters.

Based on the widespread use of contract attorneys, informing clients that the firm is using contract attorneys on a particular project should not be a risky venture. Clients may, in fact, be very pleased to learn that the firm is taking steps to increase the efficiency and effectiveness of their legal services.

Nonetheless, in deciding how to bill contract attorneys, firms should consider the potential ramifications if they are not forthright with their clients.

Not disclosing the use of contract attorneys may not only be risky to the relationship, it may violate the ethic rules of some state bars. In a 1996 Formal Opinion, the Committee on Professional and Judicial Ethics of the Association of the Bar of the City of New York stated that a firm may not refer to a contract attorney as an "associate" for billing, among other purposes.

Whether the contract attorney could be considered "of counsel" to the firm would depend on the nature of the relationship between the firm and the contract attorney. The New York bar did not state that firms were required affirmatively to inform clients that they were using contract attorneys, nor did it consider the rates at which law firms could or should bill contract attorneys. It merely stated that law firms could not refer to contract attorneys as "associates" and could refer to them as "of counsel" only in special circumstances.

With the increasing use of contract lawyers—and until there is further guidance from bar associations—law firms should establish a policy that they believe will be satisfactory to them as well as to their clients. ■

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