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Billing practices, problems can create costly liability

Lawyers and law firms are potentially liable not only for the services they render but also for the bills they send.

Improper billing may expose a lawyer to civil liability. For example, in *Coughlin v. SeRine,* 154 Ill.App.3d 510 (1st Dist. 1987), the Illinois Appellate Court held that lawyers could be liable — on theories of legal malpractice and breach of fiduciary duty — for charging clients excessive fees. In *Coughlin,* the quality of the legal services was never in dispute.

More recently, the Illinois Appellate Court held that improper billing may expose lawyers to claims of common-law fraud or violations of the Illinois Consumer Fraud Act. *Cripe v. Leiter,* 291 Ill.App.3d 155 (3d Dist. 1997)(*Cripe I*), *Cripe v. Leiter,* 291 Ill.App.3d 161 (3d Dist. 1997)(*Cripe II*).

In *Cripe I,* the 3d District Appellate Court held that the statutory prohibition against punitive damages in legal malpractice claims was inapplicable where there were allegations that the law firm had falsified bills. (The Illinois Supreme Court last week denied leave to appeal in *Cripe I* but granted leave to appeal in *Cripe II.*)

As punitive damages and fee disgorgement claims typically are not covered by lawyers' professional liability policies, law firms cannot count on their carriers to absorb such losses.

While most clients who seek redress for overbilling rely on civil grounds, such as breach of contract, breach of fiduciary duty and misrepresentation, others cooperate with prosecutors in bringing criminal charges. See D. Ricker, "Greed, Ignorance and Overbilling," ABA Journal (August 1994).

According to the August 1994 ABA article, a San Francisco law firm was prosecuted on federal mail fraud charges for allegedly padding billable hours and charging 15 percent of each bill for direct costs. The firm pleaded guilty to 12 counts of felony mail fraud and paid $25,000 in fines and $125,000 in restitution, according to the report.

Improper billing also has subjected a surprising number of Illinois lawyers to discipline. The Attorney Registration and Disciplinary Commission reported in its 1996 annual report that it logged more than 500 charges of excessive fees that year. In addition, the ARDC said, 14 percent of the complaints filed before its Hearing Board in 1996 alleged excessive or unauthorized fees. Of the 44 lawyers disbarred in Illinois that year, seven of them, or 16 percent, were found guilty of fee violations. During the same period, 60 lawyers were suspended. Fourteen of those, or 23 percent, were suspended for fee violations.

Rule 1.5 of the Illinois Rules of Professional Conduct requires a lawyer's fee to be reasonable. Some of the factors used in determining whether a fee is reasonable are the time and labor required, the novelty and difficulty of the questions involved, and the skill required to perform the legal service properly. Rule 1.5(a)(1). Rules 1.5(a)(2) through 1.5(a)(6) set forth additional factors.

However, even a reasonable fee may subject a lawyer to discipline or civil liability. Assume that a client agrees to pay a lawyer by the hour. Under the rules, that agreement is proper, even though the time required is only one of many factors that may be used in determining whether a fee is reasonable. However, unless the lawyer's client has been informed that other factors will be considered in determining the fee, the lawyer may not ethically take those factors into account in billing.

Legal Malpractice

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"It goes without saying that a lawyer who has undertaken to bill on an hourly basis is never justified in charging a client for hours not actually expended," states ABA Formal Opinion 93-379, "Billing for Professional Fees, Disbursements and Other Expenses" (Dec. 6, 1993). "If a lawyer has agreed to charge the client on this basis and it turns out that the lawyer is particularly efficient in accomplishing a given result, it nonetheless will not be permissible to charge the client for more hours than were actually expended on the matter."

The ABA opinion includes several examples of improper billing by a lawyer who agrees to work on an hourly basis.

One example is the lawyer who spends four hours of time on behalf of three clients and bills each of them four hours. Another example is the lawyer who bills two clients for the same four-hour flight, one for the travel time and the other for work performed during the flight. Yet another example is the lawyer who recycles old work product, spends virtually no time redoing the recycled work for a new client, and charges the new client for the hours previously billed to another client.

"[T]he lawyer who has agreed to bill solely on the basis of time spent is obligated to pass the benefits of these economies on to the client," the ABA opinion declares.

Since the 1980s, lawyers who bill their clients by the hour have been under increasing pressures to maximize their production. As Chief Justice William H. Rehnquist observed in the Indiana Law Journal, "If one is expected to bill more than 2,000 hours per year, there are bound to be temptations to exaggerate the hours actually put in."

According to ABA Formal Opinion 93-379, "It is a common perception that pressure on lawyers to bill a minimum number of hours and on law firms to maintain or improve profits may have led some lawyers to engage in problematic billing practices." The pressure stems from the reality that billable hours are frequently taken into account in determining associate and partner

compensation.

We are reminded of an anecdote by the management expert W. Edwards Deming, who recounted the story of a federal mediator who was rated on the number of meetings he attended during the year. The mediator confessed to Deming that he improved his ratings by stretching out to three meetings labor negotiations that he easily could have concluded in one. There is no reason to believe that this dynamic does not also apply to the practice of law. See W. Deming, "Out of the Crisis" (Massachusetts Institute of Technology Center for Advanced Engineering Study 1986).

Law firms can take specific steps to reduce the risk of civil liability and disciplinary charges relating to their billing practices.

Internal educational efforts are critical, as firms cannot assume that their lawyers know and understand the ethical rules or how to apply them.

Firms also should establish policies and procedures relating to billing. For example, firms may require that no new matter may be opened without an engagement letter setting forth the basis of the fee.

Firms also may want to consider whether hidden incentives relating to compensation systems encourage problematic billing practices. See M. Flaherty and R. Jacobson, "Striking Out Free Agents," ABA Journal, (July 1997).

Are minimum billable-hour requirements creating more problems than they solve? Are billing attorneys punished or otherwise discouraged from writing off time that they believe inappropriate to bill? Such operational self-analysis is difficult and sometimes painful, but helpful in reducing risk.

In their risk-management efforts, some law firms designate one or more partners to serve as internal ethics counsel. Others retain outside counsel to address these issues in an effort to cloak risk-management advice with privilege. Many such firms believe that outside risk-management counsel may provide more candid assessments of law firm operations, as inside lawyers may be reluctant to criticize existing business practices.

While either approach has its costs, in the end these costs may be justified by the protections afforded to the law firm's bottom line.

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