TAKING A CHANCE: A PROPOSAL FOR CONTINGENCY FEES

Kate Tokeley[*]

Contingency fees are a regular feature of litigation in some jurisdictions and with the increasing cost of litigating there is pressure for their acceptance in New Zealand. In this article Kate Tokeley concludes that contingency fees are an effective and ethical way to increase access to justice, particularly for indigent plaintiffs. She argues that, provided comprehensive guidelines are established, then the social advantage of using contingency fees outweighs any potential dangers. An outline of the rules and guidelines are proposed, as are enforcement mechanisms.

I INTRODUCTION

A contingency fee arrangement operates by allowing lawyers to be paid on the basis of the outcome of a legal action. If the outcome of the case is successful, then the client will be charged a fee. If the case is lost, then the lawyer forgoes payment altogether. Sometimes a lawyer will take only his or her usual fee in the event that the litigation is successful. This form of contingency fee arrangement is often called a speculative fee agreement.[1] It is, however, more usual for the lawyer to charge a fee higher than normal if the case is successful. This increased fee is often calculated as a percentage of the amount recovered.

Although contingency fee arrangements are at times used by New Zealand lawyers, the legality of such fees is unclear.[2] The Auckland District Law Society has set up a specialist committee to examine the whole issue of contingency fees. The issue of whether such fees should be legal is, of course, related to the issue of whether or not these fees are ethical.

This article argues that contingency fees themselves are not unethical - it is their abuse which is unethical. For example, some lawyers who use contingency fees might abuse such

* Lecturer in Law, Victoria University of Wellington.

1 G E Dal Pont *Lawyers' Professional Responsibility in Australia and New Zealand* (LBC Information Services, Wellington, 1996) 307.

2 See part II of this article for a more detailed discussion of the New Zealand position.

an arrangement by charging excessive fees or suppressing evidence in their zeal to win the case. If, on the other hand, contingency fee arrangements are used responsibly they are of great benefit to society. They enable people who would otherwise be unable to afford a lawyer, to gain access to the legal system. The key to the successful use of contingency fees is to regulate their use in order to protect clients and promote the proper administration of justice. With appropriate regulation, the social advantage of contingency fees outweighs any potential dangers.

The article begins with an overview of the New Zealand position on contingency fee arrangements and then discusses the various arguments commonly made for and against contingency fees. This is followed by an examination of whether contingency fees should be legitimised in New Zealand. It is argued that contingency fee arrangements should be legitimised and that rules should be established to ensure that these fees are used ethically. Suggestions are then given for possible rules and guidelines for the use of contingency fees. Finally, the last part of the article considers the issue of who should enforce these rules.

II THE NEW ZEALAND POSITION

Rule 3.01 of the *New Zealand Law Society Rules of Professional Conduct for Barristers and Solicitors* states that "[a] practitioner shall charge a client no more than a fee which is fair and reasonable for the work done, having regard to the interests of both client and practitioner".[3] Paragraph 4 of the official commentary to this rule goes on to say:[4]

> The rule is drafted in terms which contemplate the possibility of charging a contingency fee. The following points should, however, be noted in that regard:
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> (i) It may be that, in some circumstances at least, the common law rules against maintenance and champerty may still apply, so as to invalidate an agreement for a contingency fee. In the absence of clear and current authority on the point, the Society draws the possibility of invalidity to the attention of practitioners.
>
> (ii) ...

In effect, the Law Society does not give its approval to the use of contingency fees but neither does it disallow their use. Perhaps partly as a consequence of the Law Society's cautious approach, lawyers in New Zealand do not use the contingency fee to the same extent as do lawyers in the United States.[5] This uncertainty is highly unsatisfactory for

3 *New Zealand Law Society Rules of Professional Conduct for Barristers and Solicitors* (4th ed, New Zealand Law Society, Wellington, 1996) 29.

4 Above n 3, 30.

5 Contingency fees are allowed in the United States and are widely used. They are, however, subject to certain restrictions set out in The American Bar Association Model

lawyers and their clients who are unable to confidently enter into contingency fee arrangements without fear that these arrangements may be illegal.

The Law Society's cautious approach is based, at least in part, on the concern that the common law rules against maintenance and champerty may in some circumstances invalidate a contingency fee arrangement. Maintenance occurs where a person supports litigation in which he or she has no legitimate concern without lawful justification.[6] Champerty is a form of maintenance where assistance is given in return for a share in the proceeds of litigation in the event of success. A contingency fee arrangement is therefore a form of champerty and until recently the United Kingdom treated all such arrangements as illegal under the common law.[7] Since 1967 both criminal and tortious liability for champerty have been abolished in the United Kingdom,[8] and since 1995, UK legislation has allowed a limited use of contingency fee agreements in specified proceedings such as personal injury cases.[9] New Zealand has never had criminal statutes prohibiting champerty, and comments in New Zealand case law that suggest that contingency fee agreements are illegal have only ever been in the form of obiter.[10] There is, therefore, no binding New Zealand authority stating that contingency fees are illegal.

Code and Model Rules. For example, the fee must be reasonable and a contingency fee cannot be charged in criminal cases or in cases involving matters of domestic relations; ABA Model Rule 1.5 (a) - (d).

6 *Hill v Archibold* [1968] 1 QB 686.

7 See, for example, *In re Trepca Mines Ltd (No.2)* [1963] 1 Ch 199; *Trendtex Trading Corporation v Credit Suisse* [1982] AC 679; and *Aratra Potato Co v Taylor, Johnson Garrett (a firm)* [1995] 4 All ER 695.

8 Criminal Law Act 1967 sections 13 and 14(1).

9 Section 58 of the Courts and Legal Services Act 1990 (UK) authorises contingency fee arrangements in certain specified proceedings to be designated by the Lord Chancellor. However, it was not until June of 1995 that the Lord Chancellor actually specified any such proceedings. At this time he allowed lawyers to charge a contingency fee in personal injury cases, insolvency claims, and cases before the European Court of Human Rights and set a maximum increase of 100% on a lawyer's normal hourly rate; see R Painter "Litigating on a Contingency: A Monopoly of Champions or a Market for Champerty?" (1995) 71 Chicago-Kent Law Rev 625, 627, n 10. This means lawyers can claim up to twice their usual hourly rate in a contingency case but that they cannot claim more than this by claiming a percentage of the client's recovery. This fee limit and the subject matter limit, mean that the use of contingency fees in the United Kingdom is far more restricted than it is in the United States.

10 *Mills v Roger* (1899) 18 NZLR 291; *Seivwright v Ward* [1935] NZLR 43. See J McDermott "Contingency Fees and the Law of Champerty" (1993) NZLJ 253.

The following part of this article examines the common concerns about contingency fees and the justifications often given for the use of such fees. This is a logical starting point for resolving the question of whether contingency fees should be legitimised and if so in what form.

III CONCERNS ABOUT CONTINGENCY FEES

A Floodgates

One fear about contingency fees is that removing the financial barrier to litigation will create a flood of unreasonable, "nuisance" litigation.[11] United States lawyers use contingency fee arrangements far more often than New Zealand lawyers and the United States has become renowned as a highly litigious society. This, however, is unlikely to be due solely to the use of contingency fees. The United States does not have an accident compensation scheme and so a lot of the litigation there is based on claims for damages for personal injury. Most of these claims would be barred in New Zealand by the Accident Rehabilitation Compensation and Insurance Act 1992, so the fear of a flood of litigation is probably exaggerated. Moreover, the contingency fee arrangement itself provides the lawyer with an incentive to decline to litigate unmeritorious claims and only agree to litigate those claims which have some chance of success.

B Unethical Behaviour

Critics of contingency fees also argue that contingency fees are dangerous because they tempt lawyers to act unethically in their zeal to ensure the client recovers a sum from which the lawyer will obtain a fee.[12] Lord Denning has said that a lawyer using contingency fees "might be tempted, for his own personal gain, to inflame the damages, to suppress evidence, or even to suborn witnesses".[13] A lawyer who has a financial interest in recovery might also be tempted to act in disregard of the client's interests by, for example, persuading the client to accept an early settlement offer rather than committing the extra time necessary to take the case to trial.

It might be said that lawyers have a strong personal desire to win cases regardless of whether they charge by contingency fee or any other type of fee, and so they already have a temptation to act unethically in order to obtain this goal. Nevertheless the added pressure of receiving no fee unless the case is successful will significantly add to this temptation.

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11 This fear is discussed and ultimately dismissed by R Birnholz "The Validity and Propriety of Contingent Fee Controls" (1990) 37 UCLA Law Rev 949, 953-954.

12 See, for example, Morgan "The Evolving Concept of Professional Responsibility" (1977) 90 Harv LR 702, 732.

13 See *Re Trepca Mines*, above n7, 219.

C Excessive Fees

Critics of contingency fees also express concern about the danger that the fee will be excessively high. This danger is seen as particularly acute if the fee is calculated as a percentage of the client's recovery because the fee may result in compensation which is far in excess of the time and effort the lawyer has invested in the case. In some cases in the United States, lawyers are collecting multi-million dollar fees essentially for performing para-legal work and contingency fee rates have become virtually standardised.[14] It is only rarely that less than 30% of the recovery amount is charged if the case is settled without trial, 40% if the case goes to trail and 50% if appeals are necessary to confirm the judgment.[15] Some proponents of contingency fees would argue that such high fees are justified because the lawyer must be compensated for the risk which they undertake when accepting a contingency fee case. The problem with this argument is that these standardised percentage fees are being charged regardless of the degree of risk involved in the particular case.

IV JUSTIFICATIONS FOR CONTINGENCY FEES

A Access To Justice

The most important advantage of contingency fees is that they improve access to the courts to those who would otherwise be unable to, or find it difficult to afford a lawyer. The contingency fee allows even the poorest of litigants the ability to afford a lawyer because they will pay no fee unless their litigation is successful. In the words of one legal commentator: "The contingency fee makes it possible for anyone in our society to get the best lawyer. The client need not be a rich man. He need only have a good cause."[16]

A good example of the type of dispute in which contingency fees would increase access to justice is a consumer dispute involving large numbers of consumers who have suffered economic loss due to the failure of a particular good or service.[17] Although each consumer

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14 See L Brickman "Contingency Fee Abuses, Ethical Mandates and the Disciplinary System: The Case Against Case - by - Case Enforcement" (1996) 53 Wash & Lee Law Rev 1339, 1340.

15 Above n 14.

16 Kriendler "The Contingent Fee, Whose Interests are Actually Being Served?" (1979) 14 Forum 406, 406.

17 If the loss suffered is less than $3,000 (or $5,000 with the consent of the defendant) a claimant can probably take their complaint to the Disputes Tribunal. This will only cost them $10-$20 and they will not need a lawyer. The Disputes Tribunal significantly increases access to justice for claimants of these low amounts. However, if the amount of loss is higher, then the Disputes Tribunal is no longer an option and without a contingency fee arrangement many of the consumers may lack the finances to be able to litigate the issue. Moreover, even if the amounts involved are low enough to qualify for a hearing in the Disputes Tribunal, the claimant may prefer to litigate their claim in the

may have only lost a relatively small amount of money, the manufacturer of the goods or provider of the services may have caused millions of dollars worth of harm in total. In these situations contingency fees would be a particularly effective "access to justice" mechanism when used in conjunction with the class action.[18] Class actions provide an opportunity for a class of people to litigate an issue in a situation where each person's loss is so small that it would not be economically viable for each person in the class to litigate in individual actions. As Chief Justice Bird explained in a Californian class action case:[19]

> ...without such actions defendants may be permitted to retain ill gotten gains simply because their conduct harmed large numbers of people in small amounts instead of small numbers of people in large amounts.

Currently in New Zealand the representative plaintiff in a class action is liable for the costs of litigation unless the other class members agree to pay a share in those costs. This financial burden placed on the representative plaintiff can act as an economic barrier to the use of the class action procedure. A contingency fee arrangement would avoid the problem of class members being "free-riders" in litigation and would make the class action procedure a more economically attractive option for claimants. This would significantly increase access to justice in situations where many people are affected and the total amount of a claim is large, yet the individual person's loss is small.

B Incentive For Lawyers To Work Harder and More Efficiently

A further justification sometimes cited in favour of contingency fees is that they provide a direct incentive for lawyers to work hard to obtain the best result for their client.[20] A lawyer who will receive no fee unless his or her client's litigation is successful, has good reason to work diligently in pursuit of a good result for the client. In addition, it is in the interests of the lawyer to work as quickly and incur as few expenses as possible in order to obtain the desired result. The contingency fee, it is argued, creates an alignment of interest between the client and the lawyer.

This justification for contingency fees is not as persuasive as the "access to justice" argument. With or without a contingency fee a lawyer owes a fiduciary obligation to the

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courts and may only be able to do so if a contingency fee is available to reduce the financial risk of the litigation.

18 For a full discussion of the advantages of combining contingency fees with class actions see V Morabito "Federal Class Actions, Contingency Fees and the Rules Governing Litigation Costs" (1995) 21 Monash University Law Review 231.

19 *State v Levi Strauss & Co.* (1986) 224 Cal Rpt 605, 612.

20 For example, R Birnholz has made this comment, see above n 14, 954. See also Kreindler, above n 16.

client to act in the client's best interests in so far as this duty does not conflict with the lawyer's duty to the court and the public.[21] In addition to the lawyer's awareness of their fiduciary obligation, it is the lawyer's personal interest in improving their career prospects by obtaining a better than expected result. In the absence of empirical data on lawyer's conduct when operating on a contingency fee basis, it is difficult to be certain that contingency fees do result in lawyers working harder and more efficiently.

C Freedom Of Contract

Another argument sometimes raised in favour of contingency fees is that they affirm freedom of contract between client and lawyer.[22] In other words if the client is fully informed of all the fee options and agrees to a contingency fee, then the lawyer and client should be free to voluntarily enter into a contingency fee agreement. In some situations this may be true, however, the difficulty with this argument as a justification for the *unregulated* use of contingency fees, is that it fails to recognise that the principle of freedom to contract cannot be absolute. It is a principle which is and should be modified in situations where it conflicts with other significant ethical considerations. There are ethical concerns arising from the use of contingency fees which suggest that in some situations there is justification for overriding or modifying the principle of freedom of contract.

In addition, the notion of freedom of contract rests on the assumption that the two contracting parties have equal bargaining power. This is a justifiable assumption in regard to most commercial contracts, however fee arrangements between a lawyer and client are not ordinary commercial contracts. The lawyer has far more legal knowledge than the client. Moreover, the nature of the lawyer-client relationship, especially in relation to contingency fees, is such that unfettered freedom to contract is inappropriate. In a contingency fee contract, the client is likely to have even less bargaining power than usual because they may be unable to afford the fee if it is charged in a non-contingent way.

V SHOULD CONTINGENCY FEE ARRANGEMENTS BE LEGITIMISED IN NEW ZEALAND?

A Are Contingency Fees Necessary in New Zealand?

It might be argued that the question of whether or not contingency fees are ethical or not is irrelevant in New Zealand because the nature of our legal system is such that New Zealanders simply have no need for contingency fees. There are three reasons why

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21 See generally chapter one of *New Zealand Law Society Rules of Professional Conduct for Barristers and Solicitors*, above n 4. See also *Sims v Craig Bell and Bond* [1991] 3 NZLR 535.

22 See, for example, T Swanson "The Importance of Contingency Fee Agreements" (1991) 11 Oxford Journal of Legal Studies 193, 195.

contingency fees may be perceived as unnecessary. First is the fact that unlike the United States, New Zealand has a government-funded accident compensation scheme. The Accident Rehabilitation Compensation and Insurance Act 1992 (ARCIA) bars claims for damages arising out of a personal injury by accident[23] and instead provides compensation to those who suffer such injuries. This scheme significantly reduces the amount of civil litigation in New Zealand, and it is in this area of civil claims for personal injury, that contingency fees are most frequently used in the United States.

There are, however, still significant areas of civil litigation not affected by ARCIA in which the use of contingency fees could effectively be used to increase access to justice. For example, exemplary damages are not barred by ARCIA[24] and with the demise of the lump sum payment under the accident compensation scheme there is likely to be an increase in the number of exemplary damages cases in New Zealand. In addition, civil litigation for damages unrelated to any personal injury is another area in which contingency fees might be a useful fee option. For example, shareholder derivative actions or claims for economic loss caused by defective consumer products are not claims related to personal injuries and so are not barred by ARCIA. As has been stated earlier in this article, contingency fees in these types of cases may be particularly useful when used in conjunction with a class action mechanism.

The second reason why contingency fees may be perceived as unnecessary in New Zealand is that we have a civil legal aid scheme.[25] It might be argued that this scheme will assist those people who are unable to pay for their own lawyer and so there is no need for a contingency fee system to be introduced in order to give these people access to the courts. Unfortunately, however, the current New Zealand civil legal aid scheme offers assistance to only the very poorest of litigants and even then it requires many litigants to pay back the amount of civil legal aid that they have received.[26] Contingency fees, therefore, have the potential to increase access to justice for those people who are unable to afford a lawyer on an hourly-rate fee and yet are not poor enough to qualify for legal aid.

The third reason why contingency fees may be perceived as unnecessary in New Zealand is that the fees may fail to improve access to justice because of New Zealand's rules as to

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23 Section 14(1) of the Accident Rehabilitation Compensation and Insurance Act 1992 bars claims for damages arising directly or indirectly out of personal injury covered by the Act, or personal injury by accident covered by the 1972 and 1982 Accident Compensation Acts.

24 *Donselaar v Donselaar* [1982] 1 NZLR 97.

25 See the Legal Services Act 1991, Part II.

26 Above n 25, ss 37 and 38.

costs. Although a claimant paying on a contingency fee basis will not have to pay his or her own legal expenses if their litigation is unsuccessful, they will nevertheless generally be ordered to pay a significant portion of the winning side's costs.[27] The fact that a claimant will incur expenses even if they lose, may significantly reduce the attractiveness of the contingency fee arrangement.

This argument does have some merit. Nevertheless, the fact remains that even with the current rules as to costs, the contingency fee arrangement will significantly reduce the financial risk of litigation for the client and will therefore increase access to justice. In addition it may be possible to expand the contingency fee arrangement so that lawyers also agree to assume the risk of paying for the opponent's costs if the litigation is unsuccessful.[28]

If contingency fees were officially legitimised in New Zealand, it is probably true that they may not in fact be used as prevalently as they are in the United States. This does not, however, mean that contingency fees are unnecessary in New Zealand. If the charging of these fees is ethical and can increase access to justice then they should be adopted in New Zealand. The fact that they may not be widely used, in fact, adds support to legitimising their use since a flood of litigation is unlikely.

B Are Contingency Fees Ethical?

Contingency fees are not unethical per se, indeed they have the potential to significantly increase access to justice. It is the abuse of contingency fees which is unethical and therefore creates the fears and concerns discussed in part III of this article.

If a lawyer charges a speculative contingency fee to a poor litigant and acts ethically throughout the case, then no-one could criticise the contingency fee as being unethical. The lawyer in this case has helped a client to gain access to justice, has not succumbed to pressures to act unethically in the running of the case and if the case is successful, he or she will receive a normal hourly-rate fee which cannot in any way be termed an excessive fee.

Many lawyers using a contingency fee arrangement would, however, be more likely to charge an amount higher than their normal fee payable only in the event of a successful outcome. Let us assume that a lawyer charging this higher rate is helping a client to gain access to justice and that they act ethically throughout the case. Let us also assume that the amount charged above the lawyer's normal hourly-rate fee adequately represents a reasonable degree of risk calculated by the lawyer in accepting a contingency fee arrangement in this particular case. In this situation there is nothing unethical about the

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27 See, rule 46 of the High Court Rules and *Morton v Douglas Homes Ltd (No. 2)* [1984] 2 NZLR 620.

28 See R Painter, above n 9, 630.

contingency fee arrangement. The client benefits from being able to afford a lawyer. The lawyer has not taken advantage of the client by charging an excessive fee. It is fair for a lawyer to be compensated for the risk they assumed on undertaking a case in which they may have received no fee at all. In addition, the justice system has not suffered from any unethical practices.

These two examples show that contingency fees can be used ethically and responsibly and benefit society by increasing access to justice. Having identified the abuse of contingency fees as the problem rather than the contingency fee itself, the challenge is to determine whether guidelines can be developed which will ensure that contingency fees are used in an ethical way. If this is possible, then the desirable option for New Zealand is for the use of contingency fees to be clearly legitimised and a detailed set of rules to be drafted either into legislation or as part of the Law Society's Rules of Professional Conduct.

A starting point to establishing a set of ethical rules is to analyse each of the concerns about contingency fees to determine if each concern is legitimate and if so whether guidelines and limits on the use of contingency fees could address these concerns. The three concerns about contingency fee arrangements identified in part III of the article were the fear of a flood of litigation, the danger of the fees tempting lawyers into unethical behaviour, and the concern that excessive fees might be charged.

As has already been argued, the floodgates fear is exaggerated. The problem of a flood of litigation is more perceived than real. The latter two concerns, however, are important but they are not enough to justify the banning of contingency fees altogether. The danger of contingency fees tempting lawyers into unethical behaviour needs to be balanced against the significant increase in access to justice that the use of such fees can bring. This might suggest that the use of contingency fees should only be sanctioned in cases where a client has an access to justice problem. It also needs to be remembered that only a small proportion of lawyers may be tempted into unethical behaviour and that temptation to act unethically is already a possibility in the legal profession as it is in any other profession. The third concern regarding the charging of excessive fees is something that can be controlled by guidelines and rules about what a reasonable fee is in a contingency fee arrangement.

Other options for controlling the use of contingency fees include rules which require informed consent from the client and rules limiting the use of contingency fees to particular types of litigation. The following section of this article analyses some possible rules and guidelines which could be established to ensure the ethical use of contingency fees.

VI SUGGESTED RULES AND GUIDELINES FOR ENSURING THE ETHICAL USE OF CONTINGENCY FEES

A Deserving Cases

In light of the dangers of using contingency fees it would seem desirable to limit their use to situations where the social advantage of increased access to justice, outweighs the potential dangers of these fees. In other words, contingency fees should only be used in situations where the client would not be able to afford the lawyer or would not consider taking the litigation if they had to pay an hourly-rate fee because of the financial burden it would impose on them. The cost of litigation is so high these days that for most individual clients a contingency fee will increase their access to justice. However, in the case of a large multi-million dollar corporate considering litigation, the option of a contingency fee is unlikely to dictate whether or not the corporate proceeds with the litigation. Without the benefit of increasing access to justice, the scales tip in favour of disallowing a contingency fee in this case. The danger of excessive fees and unethical behaviour are still present and yet there is no corresponding advantage of increased access to justice.

The guidelines for the use of contingency fees should therefore limit their use to deserving cases. The rule would have to be drafted in fairly broad terms because it will not necessarily always be possible for the lawyer to assess the financial position of their client. Nevertheless the rule could make it clear that contingency fees are not to be charged in cases where the lawyer knows or should know that the client clearly does not need a contingency fee arrangement in order for them to access the justice system.

Of course, one could argue that there are very few people in New Zealand who actually *need* a contingency fee to access the justice system. Most people could use up their savings, sell their car or house or take out a loan in order to afford a lawyer. In other words it is only those with no savings, no assets and a very low income who need a contingency fee. However, this is a harsh approach to take. People are unlikely to make such burdensome choices as those suggested above in order to access the justice system and nor should they have to, the justice system should be more readily accessible than this. A contingency fee system should be available to anyone for whom paying a lawyer on a non-contingent fee basis is an unrealistic choice. Although a rule drafted on this basis may be open to different interpretations by different lawyers, it at least provides lawyers with a general guideline and ensures that contingency fees are not used for those clients who clearly do not need a contingency fee to access the justice system.

B Subject Matter of the Case

Any rules about contingency fees also need to address the question of whether there are any types of litigation in which it would be unethical or inappropriate to use a contingency

fee. The two types of case which are not generally deemed suitable for contingency fees are criminal cases[29] and divorce and matrimonial proceedings.[30]

1 *Criminal cases*

There are several reasons against the use of contingency fees in criminal cases. First, as in any contingency fee arrangement, the lawyer may be tempted to act unethically in order to win the case. They may for example, suppress evidence or encourage their client to lie in court. The danger of a lawyer's behaviour being tainted by their financial interest in the outcome of the case is arguably a more serious wrong in a criminal case than it is in a civil case. This is because the lawyer's unethical behaviour in a criminal case could result in a guilty and possibly dangerous person being acquitted and potentially committing further crimes.

Charging contingency fees in a criminal case may also be unethical due to the fact that the client in a criminal case has far less bargaining power than a client in a civil case. Deciding whether or not to invoke the law in a civil matter is always a matter of choice. If a fee arrangement appears unfair, the civil client can decide not to take legal action or at least he or she has the time to ask another lawyer for their prices (although shopping around for legal services is not common it is at least a more realistic option in civil litigation). On the other hand, the client in a criminal case has no choice about whether or not to be involved in the litigation. They have been charged with an offence and need a lawyer immediately. They therefore have little bargaining power when it comes to fee arrangements and may be persuaded to enter into a contingency fee agreement against their own interests.

A further reason to prohibit the use of contingency fees in criminal cases is the existence of criminal legal aid. The most persuasive argument in favour of contingency fees is their ability to increase access to justice. However, in the case of criminal litigation there is no need to use contingency fees to increase access to justice because New Zealand has an

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29 See F B McKinnon *Contingent Fees for Legal Services* 52 (1964) (A report of the American Bar Association), Gillers *Regulation of Lawyers: Problems of Law and Ethics* (4th ed, Little, Brown & Co, New York, 1995), 144. See also disciplinary rule DR 2-105 (C) of The Code of Professional Responsibility of the American Bar Association which prohibits a lawyer from charging a contingency fee for representing a defendant in a criminal case. See also P Lushing "The Fall and Rise of the Criminal Contingency Fee" (1991) 82 The Journal of Criminal Law and Criminology, 498. Lushing argues that contingency fees should be permitted in criminal cases.

30 See, for example, *Levine v Levine* (1954) 206 Misc, 884, 135 N.Y.S.2d 304 (Sup. Ct. Queens Co. 1954).

effective criminal legal aid system which ensures that all criminal litigants have access to a lawyer regardless of their financial position.[31]

Finally, there is a practical reason why charging a contingency fee in a criminal case is inappropriate: there is no recovery in a criminal case from which to draw the lawyer's fee. It is possible that a contingency fee might still be an attractive fee option to a client facing the possibility of a prison sentence, because they at least have the possibility of earning an income if they are acquitted. Nevertheless, winning a criminal case does not increase a client's assets so it is not as suited to a contingency fee arrangement as a civil case.

For the above reasons a set of rules about contingency fees should include a prohibition on the use of contingency fees in criminal cases.

2 *Matrimonial proceedings*

A fee arrangement where the payment of fees is contingent upon a certain amount of money being secured for the client in the divorce settlement is unethical because it is against public policy. This is because such a fee arrangement gives a lawyer a financial incentive to discourage reconciliation. Not only is promoting reconciliation and conciliation a lawyer's ethical duty, it is also a legal duty under section 8 of the Family Proceedings Act 1980. Charging contingency fees in divorce proceedings should therefore be prohibited under the rules established to regulate the use of contingency fees.

C Guidelines for What Amounts to a Reasonable Fee

One of the chief concerns about the contingency fee system is the potential for lawyers to charge excessive fees. To avoid the abuse of contingency fees in this way, it is essential to develop rules regulating the quantum of fees. Some lawyers may regard specific and strict controls on the fee they charge as an unjustified intervention into the legal marketplace.[32] They may argue that fees will not become excessive in a free market, because clients will shop around for the most reasonable fee and therefore the economics of competition will control the fee levels.

Unfortunately the free market mechanism of competition does not operate effectively in the legal market-place.[33] Unlike other consumer products, the prices of comparable legal

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31 Legal Services Act 1991, Part I.

32 This is the view of T Swanson, above n 22, 195.

33 See L Brickman, "Contingent Fees Without Contingencies: *Hamlet* Without the Prince of Denmark?" (1989) 37 UCLA Law Review 29, 102; see also part 3.2 of the E-DEC Report, *Purposes, Functions and Structure of Law Societies in New Zealand* (independent internal report to the New Zealand Law Society, Wellington, September 1997) 5-6. The E-DEC report is available on the internet at [http://www.nz-lawsoc.org.nz/general/report.htm].

services are not readily available or easy to discover. Further, the ability of lawyers to advertise is strictly limited by rules of professional conduct.[34] Discovering and comparing the prices of the services offered by various lawyers is not as easy as comparing the quality and price of loaves of bread in the supermarket. Without full information about the options available, a customer of legal services is unable to register their preference by making an informed choice. For this reason, the free market mechanism of price control is not particularly effective in the legal market-place.

The law already recognises that a free legal market will not necessarily result in a fair and reasonable fee. This is the reason for the cost revision procedures set out in Part VIII of the Law Practitioners Act 1982. These provisions allow the District Council of the appropriate District Law Society to revise a practitioner's bill of costs, either of it's own motion, or by order of a Court, or when a client refers a bill to the District Law Society in order for the bill to be revised.[35] If either the lawyer or the client is dissatisfied with the decision of the District Council they can appeal to a Registrar of the High Court and if either party is dissatisfied with the Registrar's decision they may apply to the High Court for a review of the decision.[36]

When a District Council revises a bill it is concerned with whether the fee charged is fair and reasonable. Rule 3.01 of the *New Zealand Law Society Rules of Professional Conduct* requires a practitioner to charge "no more than a fee which is fair and reasonable for the work done, having regard to the interests of both the client and the practitioner."[37] The commentary to the rule refers lawyers to the Society's *Costing and Conveyancing Practice Manual* which requires lawyers to take into account all relevant factors when calculating a fair and reasonable fee. It lists particular factors to be taken into account including the skill and knowledge required, the time and labour expended and the complexity of the matter.[38] The list does not mention particular factors to be taken into account when calculating a contingency fee. However, part 4 of the commentary to rule 3.01 points out that the rule applies to contingency fees and that the quantum of a contingency fee would be subject to

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34 See chapter 4 of the *New Zealand Law Society Rules of Professional Conduct for Barristers and Solicitors*, above n 3.

35 Section 143 Law Practitioners Act 1982.

36 Above n 35, sections 148 and 149.

37 Above n 3, 29.

38 Other factors to be taken into account are the responsibility required, the value or amount of any property or money involved, the importance of the matter to the client and the results achieved, the difficulty or novelty of the questions involved, the urgency and the circumstances in which the business is transacted and the reasonable costs of running a practice.

revision under Part VIII of the Law Practitioners Act 1982. The Rules then quote Rule 18 of the International Code of Ethics which provides:

> A contract for a contingency fee, where sanctioned by the law or by professional rules of practice, should be reasonable under all the circumstances of the case, including the risk and uncertainty of the compensation, and subject to supervision of a Court as to its reasonableness.

Although this gives some guidance for a lawyer charging a contingency fee, it is desirable to establish clearer, more detailed directives on setting contingency fees.

It is probably impossible to state in any rules on contingency fees, exactly how much above a normal hourly-rate fee will fairly represent the particular risks of a specific case. Just as no single, fixed, hourly rate can be said to represent a fair and reasonable rate in a non-contingency fee arrangement. The concepts of fair and reasonable are relatively subjective. In an English case on cost revisions, Donaldson J made the following comment about the calculation of a fair and reasonable fee:[39]

> The object of the exercise...is to arrive at a sum which is fair and reasonable having regard to all the circumstances... It is an exercise in assessment, an exercise in balanced judgement - not an arithmetical calculation. It follows that different people may reach different conclusions as to what is fair and reasonable, although all should fall within a bracket which, in the vast majority of cases, will be narrow.

Similarly, it is likely that a band of contingency fee levels can be considered fair and reasonable in any given case. For example, let us assume that a lawyer estimates that a case will take a week of work with a fee of $6000 calculated on the basis of a normal hourly-rate, and that there is a 75% chance that the case will succeed. A fair and reasonable rate might be calculated on the basis that the lawyer should receive $10,000 or $15,000 or maybe even $20,000 if the case succeeds. However, if the lawyer charges out a contingency fee on the basis that he or she should receive $150,000 if the case is won, then this is outside the band of fair and reasonable fees, and is clearly excessive.

Although the envisaged rules may not be able to give exact figures or percentages for particular levels of risk, the rules should emphasise the importance of the relationship between the quantum of the fee and the risks undertaken. The contingency fee must be proportionate to the anticipated effort and the magnitude of these risks. Each case needs to be decided on its individual facts because the degree of risk will be different from case to case. For this reason it is inappropriate to have a standard contingency fee rate. The

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39 *Property and Reversionary Investment Corporation Ltd v Secretary of State for the Environment* [1975] 2 All ER 436, 441. Although the case is not about a contingency fee, the comment is relevant to any type of fee. The case was approved in *Gallagher v Dobson* [1993] NZLR 611, 620.

standard contingency rates charged in the United States are unethical because they do not adequately represent the varying degrees of risk undertaken in each case.

The notion of risk is essential to the calculation of a contingency fee. As Justice Wiener said "the raison d' etre for the contingent fee...[is] the contingency".[40] It would therefore be unethical to charge a contingency fee in cases which involve minimal work on the part of the lawyer and no realistic risk of non-recovery. There are, however, very few cases in which from the outset it can be said that there is no risk at all and that the client will certainly recover. It is also unethical to charge a disproportionately high contingency fee in cases where there are risks involved, but those risks are small. An example of this type of abuse would be where a lawyer charges a contingency fee of a standard hourly rate plus 60% of the recovery in a case where there is very little chance of non-recovery.

The fact that a contingency fee is ethical only when it is charged in relation to a risk, also has implications for cases in which a certain amount of a claim is undisputed. For example, if a defendant has already made an admission of liability of a certain sum to a client before they come to the lawyer to discuss legal action, then the lawyer cannot charge a contingency fee based on a percentage of the admitted sum. This is because there is nothing contingent about recovering this sum, the defendant is only disputing paying a higher amount. The lawyer may, however, charge a contingency fee on the amount recovered above the admitted sum.

The calculation of a fee to represent the effort and risk undertaken in a contingency fee arrangement could be charged in several different ways. The following part of this article examines some of the ways in which a contingency fee can be charged. The conclusion to this section summarises some possible rules or guidelines that could be used to promote the charging of fair and reasonable contingency fees.

1 *The contingency fee calculated as a percentage of the recovery*

The usual way to charge a contingency fee is to calculate the fee as a percentage of the recovery. In this type of fee arrangement the nature of the risk undertaken by the lawyer is threefold. First, the lawyer is assuming the risk that he or she will receive no fee at all if the case is unsuccessful. Secondly, the lawyer is assuming the risk that the effort expended is greater than anticipated and that therefore the percentage fee does not represent the actual effort put into the case by the lawyer. Finally, the lawyer takes the risk that the recovery is smaller than expected and therefore the percentage fee does not represent the effort put into the case. All these risks can be taken into account when estimating a fair and reasonable fee for the case.

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40 *Cazares v Saenz* (1989) 208 Cal. App. 3d 279, 288, 256 Cal. Rptr. 209, 214.

The advantage to the client of this type of fee calculation is that since the fee is expressed as a percentage of the recovery, the client can be sure that they will retain a portion of the winnings. The disadvantage of this method of calculation is that it may be difficult to accurately translate a fair monetary value for the effort and risk, into a percentage of an estimated recovery. The size of the potential recovery and the number of hours that the lawyer will need to work are both merely estimations. It is therefore possible that the ultimate fee may either result in a shortfall or a windfall for the lawyer.

In order for this type of fee to be fair and reasonable, the lawyer must make a proper estimation of the recovery and then calculate a percentage of this amount which fairly represents the estimated effort required to take the case and the degree of risk undertaken by using this type of contingency fee in this particular case. The lawyer will then charge this percentage figure from the actual amount recovered.

If the ultimate fee charged does result in some windfall for the lawyer, this does not mean that the fee is unfair or unreasonable. Part of the fee arrangement agreed to by the client, involved the possibility that the lawyer may receive a somewhat higher fee than expected. In return for this, the client was able to gain access to justice and also gained the certainty of knowing from the outset that they would receive a particular percentage of the recovery. In addition there was a chance that the client might have paid less than an amount which represented the actual effort and risk undertaken by the lawyer.

What happens, however, if the actual fee charged is far in excess of any amount anticipated by either the lawyer or client? For example, let us assume that a lawyer estimates that an amount of $50,000 is a fair fee for compensating her or him for the estimated hours of work and risks involved in the case. The lawyer estimates the likely recovery at around $200,000, and so charges a contingency fee of 25% of the recovery. Much to everyone's surprise the recovery is in fact $4,000,000, and so the lawyer's fee is $1,000,000. Is the lawyer's fee still fair and reasonable? In this situation the fee is not fair and reasonable. When a fee is grossly larger than expected, it may indicate one of three things. First it is possible that the lawyer was aware of the chances of receiving such a high fee, and was therefore dishonest in his or her calculation of the fee. It might alternatively be that the lawyer was negligent in his or her original assessment of the case and failed to properly evaluate the estimated recovery. In either of these two cases, it can be said that the fee is unfair and unreasonable.[41] Finally it is possible that although the lawyer calculated a

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41 It is also likely that in this situation the lawyer will be liable for misrepresentation under the Contractual Remedies Act 1979 or the Fair Trading Act 1986 . In addition the lawyer may be liable under the Consumer Guarantees Act 1993 for breach of the guarantee as to reasonable care and skill. See part VI, D of this article for a discussion of the application of the Contractual Remedies Act, Fair Trading Act and the Consumer Guarantees Act to contingency fee contracts.

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fee with reasonable care and good faith, the completely unpredictable occurred and a huge windfall was bestowed upon the lawyer. In this situation the ethical thing for the lawyer to do would be to make some reduction to the fee charged to the client so that it more accurately reflects the actual effort and risks involved in the case.

The above situation is, however, unlikely to occur in New Zealand in light of the near absence of jury awarded damages. Assuming that the lawyer has made sufficient inquiries to properly evaluate the case, then the chances of the actual fee being a significant shortfall or windfall are not great, particularly if the damages sought are compensatory rather than punitive. The chances of the actual fee charged being grossly more than expected is more likely to happen in the United States where damages are more often set by juries.[42]

The reverse situation is where the recovery is much smaller than the lawyer or client could have anticipated and therefore the actual fee does not compensate the lawyer for the work and risks involved. Is this fee fair and reasonable and should the lawyer be able to demand a surcharge from the client to boost the fee so it more closely represents the actual effort and risks? In these circumstances the fee is probably still fair and reasonable and it would be unfair to demand further payment from the client. The situation is certainly closer to what the contracting parties anticipated than the above situation where the lawyer received $1,000,000. The lawyer may have received less than expected, but it was always possible that the action would be unsuccessful and the lawyer would have received nothing. In addition, the lawyer is better able to avoid this kind of loss than the client because they are more likely to have the skill and knowledge to be able to competently and accurately evaluate the likely amount of recovery. Even if the lawyer does make a reasonable evaluation of the likely amount of recovery and an unpredictably low amount is recovered, the lawyer is still, more often than not, in a better financial position to bear this loss than is the client.

2 *The contingency fee calculated on the basis of an increased hourly-rate for the estimated hours to be worked*

An alternative method of fee calculation is to estimate the hours likely to be spent on the case and charge an hourly-rate fee which is boosted by a percentage which represents the degree of risk undertaken by the lawyer in taking this particular case on a contingency fee basis. So, for example, a lawyer may estimate that a case will take 100 hours and normally charges out at $200 an hour (ie $20 000 total). Because of the risks involved in doing this case for a contingency fee, the lawyer increases the hourly-rate by 50%, and so charges

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42 For a discussion about the power of the American jury see D Bedingfield "The Contingency Fee System in America" (1991) NLJ Nov 26, 1670.

$30,000 for the case. The consequence being that the lawyer receives the first $30,000 of the recovery and the client receives the rest.

There are two risks for the lawyer in this type of fee arrangement. First there is the risk of non-recovery and therefore no fee being collected at all. Secondly there is the risk that the lawyer will in fact spend longer on the case than anticipated and so will receive a lower hourly rate than will fairly compensate the lawyer for the actual effort and risk involved in the case. The advantage of this type of arrangement, however, is that the fee is more likely to represent the actual effort and risks involved in the case than a calculation based on a bare percentage of the recovery. This is because the calculation of the fee is no longer based on an estimation of an uncertain amount of recovery. The only uncertainty in the fee calculation is the danger that the lawyer might over or underestimate the number of hours to be spent on the case.

The disadvantage of this method of contingency fee calculation for the client is that the lawyer's fee might in some cases consume the entire recovery. The client cannot be certain when agreeing to the contingency fee that the litigation will be financially worthwhile for them. In order for this type of fee to be procedurally fair and reasonable, it is essential that the client be given full information about the fee arrangement. They should be told the amount of the fee, the estimated risk of non recovery in terms of a percentage, and the estimated size of the recovery. In addition, the lawyer should clearly explain to the client the risk of the recovery being totally consumed by the fee. With this information the client can assess the risks of the fee arrangement and decide whether they are prepared to assume these risks.

3 *The contingency fee calculated on the basis of an increased hourly-rate for the actual hours worked*

A variation on the above fee calculation method, is to increase the hourly fee rate by a percentage which represents the degree of risk undertaken by the lawyer and charge this increased hourly fee rate for the *actual* hours spent on the case.[43] The advantage of this method of calculation for both the client and the lawyer, is that the fee will represent a fair and reasonable price for the actual effort and risks involved in the case.

The lawyer in this situation is only undertaking one risk and that is the risk of non-recovery. The flip side of this low risk for the lawyer is that he or she has no chance of receiving a windfall. The risk to the client of this type of fee arrangement is again that the fee will consume the entire recovery. This risk is harder for the client to assess in this type of fee arrangement than it is in the calculation based on an inflated hourly rate for *estimated*

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43 This kind of approach to calculating a contingency fee is advocated by H See in "An Alternative to the Contingent Fee" (1984) 3 Utah L Rev 485.

hours worked. This is because at the outset it is uncertain how many hours will actually be spent on the case.

This type of fee arrangement can be ethical but only if the client is given full information in order to make a meaningful assessment of the risks involved. This requires a lawyer to give the client an estimate of the hours to be spent on the case, even though the fee calculation will be based on the actual hours spent on the case. Without this information the client will be unable to compare the likely fee with the likely recovery in order to assess the chances of the fee consuming the recovery.

4 *The contingency fee calculated on the basis of the actual or estimated hours plus a percentage of the recovery*

A final method of contingency fee calculation is a hybrid of the above methods. It involves charging the client a normal hourly rate for either the actual or estimated hours worked and then adding on a percentage of the recovery to represent the risks to the lawyer of undertaking the case on a contingency fee basis. The advantage of this method for the lawyer is that, unlike the straight percentage fee, there is less danger that the lawyer will be under paid for the reason that the fee recovered is much less than anticipated. The risks that the lawyer is undertaking in this fee arrangement are first, that the case will be unsuccessful and secondly, if the calculation is based on estimated hours of work, there is the added risk that the lawyer might underestimate the hours of work actually needed. Lastly, there is a risk for the lawyer that the recovery will be less than expected and therefore the percentage of the fee taken as a bonus will not adequately reflect the risks undertaken by the lawyer. This risk is, however, likely to be of far less concern to the lawyer than the situation where the fee is based entirely on a percentage of recovery so that if the recovery is much smaller than expected the lawyer might not even receive enough to compensate them for the actual hours that they have worked.

There are several disadvantages of this type of fee arrangement to the client. Because the fee is based in part on a percentage of the recovery, there is a chance that the recovery will be larger than anticipated and the lawyer will therefore receive a windfall amount of money. Unlike the fee based entirely on a percentage of the recovery, the client no longer has the corresponding advantage of being certain that they will retain a particular portion of the recovery. The part of the fee which represents the actual or estimated hours worked may, in fact, consume the entire recovery. Despite these dangers, a client may still be willing to take these risks. So long as the client is given full information about the fee calculation and the risks involved, and the fee is properly calculated according to effort and risk, then the fee will usually be fair and reasonable. The only time it may not be fair and reasonable is in the unlikely event that the recovery is grossly larger than expected, resulting in a fee which gives the lawyer an unreasonable windfall for the work done and risks undertaken. In this

case the lawyer should reduce the fee so that it more accurately reflects the effort and risks involved in the case.

5 *Effect of Statutory Obligations*

It should be noted that in all of the above contingency fee methods the lawyer must be careful to make a proper assessment of the risk of non-recovery, the hours likely to be spent on the case and the likely amount of the recovery. If the lawyer fails to make a competent assessment of any of these factors then not only is the fee likely to be unfair and unreasonable, but in addition the client may be entitled to damages under the Fair Trading Act 1986 or may be entitled to cancel the contract or receive damages under the Contractual Remedies Act 1979. In addition the lawyer may be liable for a breaching the Consumer Guarantees Act 1993.

(a) The Contractual Remedies Act 1979

Section 6 of the Contractual Remedies Act allows a party to a contract to claim damages from the other party if he or she has been induced to enter the contract by a misrepresentation. Section 7 provides that the contract may be cancelled if the misrepresentation is in respect of a serious matter or has serious consequences for the innocent party.

A misrepresentation is a false statement of fact. Statements about the chances of non-recovery, the estimated hours of work or the likely amount that might be recovered, are all statements of opinions relating to future events. Usually a statement of opinion about a future event does not contain a statement of fact beyond the fact that the person expressing the opinion does actually hold that opinion. However, where the speaker is in a better position to know the facts than the person spoken to, an expression of opinion about a future event will also imply to the addressee, a statement about a present fact beyond the mere fact that the person honestly holds the opinion.[44] So for example, when a lawyer tells a client that he or she thinks that the case will take three days of work, he or she is implying that the case is of a nature that a competent lawyer could reasonably hold the opinion that the case will take three days. If it subsequently turns out that the case actually takes three months and a competent lawyer could not reasonably have held the opinion that the particular case would take only three days work, then there has been a misrepresentation.

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44 For an example of a case where an expression of opinion was treated by the court as a representation that there were facts which justified that opinion, see *Root v Badley* [1960] NZLR 756. For examples of cases where a statement which is seemingly about the future may also contain a statement about a present fact, and might therefore be a misrepresentation, see *Ware v Johnson* [1984] 2 NZLR 518; and *New Zealand Motor Bodies Ltd v Emslie* [1985] 2 NZLR 569.

For the client to be entitled to damages under the Contractual Remedies Act, it must also be shown that the misrepresentation induced the client to enter into the contract. Statements about the likelihood of successful litigation and the size of the recovery are likely to be a relevant considerations for a client in deciding whether or not to enter into a contingency fee contract. If a client is told by the lawyer that there is an excellent chance of recovery and that the likely amount of recovery is very high, then these representations are likely be part of the reasons which induce the client to enter into the contingency fee agreement.

Misrepresentations about the estimated hours of work are also likely to have induced a client into entering into a contingency fee agreement. If the lawyer calculates the contingency fee on the basis of payment for the *actual* hours worked then the lawyer must be careful to not give the client an estimation of hours which is unreasonably low. This low estimation may form part of the inducement for the client to enter the contingency fee agreement. If the lawyer in fact works far more hours than estimated, the client will have to pay far more than they had anticipated. If the estimation of hours was a misrepresentation then the client will be entitled to damages under the Contractual Remedies Act. If the fee is calculated on the basis that payment will be made for an *estimated* number of hours work then the lawyer needs to be careful not to calculate the fee on the basis of an unreasonably high estimation of hours to be worked. This high estimation may have formed part of the reason why the client feels it is reasonable to expect to pay the quoted fee and this may form part of the inducement for them to enter into the contract. If the lawyer actually works far less hours than was estimated and the high estimation was a misrepresentation, then the client is entitled to damages and possibly to cancel under the Contractual Remedies Act.

(b) The Fair Trading Act 1986

Failure to make a proper assessment of the factors relevant to the setting of a contingency fee could also result in liability under the Fair Trading Act 1986. Section 9 of the Fair Trading Act prohibits a person from engaging in conduct that is misleading or deceptive or is likely to mislead or deceive. It is misleading for a lawyer to base fee calculations on incompetent or deceptive assessments of the chances of non-recovery, the estimated hours of work or the likely amount of the recovery. Section 13(g) of the Fair Trading Act may also be relevant. It provides that no person in trade, in connection with the supply or possible supply or promotion of goods or services, shall make a false or misleading representation with respect to the price of any goods or services. A lawyer who has based a fee calculation on misleading information given to the client, has in a sense made a misleading representation in respect of the price of the legal service.

If the court finds that the client has suffered loss because of the misleading conduct or misleading representation it has the power to make various orders under section 43. These include orders to vary the contract or orders directing the person who engaged in the conduct to refund money or pay damages for the amount of the loss.

(c) The Consumer Guarantees Act 1993.

Section 28 of the Consumer Guarantees Act 1993 implies into the lawyer/client contract a guarantee that the service will be carried out with reasonable care and skill. Part of the service the lawyer performs is to provide the client with information regarding the setting of the fee. In a contingency fee arrangement this information will include statements about the chances of non-recovery, the estimated hours of work and the likely amount of the recovery. If the lawyer fails to take reasonable care in assessing these various factors then they have breached the guarantee as to reasonable care and skill.

6 Summary of the Rules on Setting a Fair and Reasonable Fee.

All of the methods of fee calculation discussed above are valid and can lead to fair and reasonable fees. The essential aspects of any rules on setting fair and reasonable contingency fees are that:

- the calculation of the fee must be related to the effort and risks involved in the particular case;
- a contingency fee is unethical if used in a case involving no realistic risk that the action will be unsuccessful or that the lawyer will not be fully compensated;
- it is unethical to charge a contingency fee on an amount of a claim which is undisputed;
- the lawyer must competently evaluate the risk of non-recovery, the hours likely to be spent on the case and likely amount of the recovery;
- the client should be fully informed of the details of the fee arrangement and the risks that they are undertaking with the particular fee arrangement; and
- if the fee is based either in whole or in part on a percentage of the recovery, then if the amount of the recovery is far in excess of any amount anticipated by the lawyer, then the lawyer has a duty to reduce the fee payable by the client so that it more accurately reflects the effort and risks involved in the case.

Another issue to consider when establishing rules about the quantum of contingency fees, is whether or not there should be a cap on the percentage of the recovery which can be charged.[45] The purpose of a fee cap is to prevent lawyers charging excessive contingency

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45 Fee caps are provided for in legislation in the United States, especially in relation to medical malpractice suits. See Birnholz, above n 11 , 950 at n 6 for a list of States which have imposed

fees. This article does not, however, recommend the setting of a fee cap. This is because there is a danger that a fee charged at a rate less than the cap might automatically be regarded as ethical. As the above discussion shows, this fee will not, in fact, always be ethical. If a lawyer charges an amount just short of the fee cap in a case where there is little or no chance of non-recovery, then this would be an unethical practice.

Charging a reasonable and fair contingency fee is not a science. It will inevitably involve some guess work. What is important in any rules and guidelines about contingency fees is that lawyers are made aware of the principles which are relevant to setting a fair and reasonable contingency fee. It might also be useful for the guidelines to outline the various methods of contingency fee calculation and the advantages and disadvantages of each method.

D *Informed consent*

As has already been noted, it is important that the client is fully informed about the details and risks of the particular contingency fee arrangement which he or she is contemplating. There are also other aspects of the contingency fee arrangement which should be discussed with the client prior to the client agreeing to this type of fee option. The agreement will not be ethical if it is imposed on a client without the client's full and informed consent.

There is already a general duty at common law to disclose all material information to a client.[46] Nevertheless, it would be desirable to have a more detailed directive to lawyers to disclose the nature and details of a contingency fee arrangement to the client before any final agreement is made.[47] A rule could be drafted which requires a lawyer to discuss such matters as:

- the availability of non-contingency fee options;
- the availability of alternative dispute resolution processes;
- the ability of the client to pay on a non-contingent basis;
- the likely cost if the case is charged on a non-contingent fee basis;
- the likelihood of success expressed as a percentage;

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medical malpractice fee caps.

46 See *McKaskell v Benseman* [1989] 3 NZLR 75 and Rule 1.09 of the *New Zealand Law Society Rules on Professional Conduct*, above n 3, 15.

47 The American Bar Association (Formal Opinion 94-389) are of the opinion that lawyers have a duty to discuss all the factors relevant to a client who is considering entering a contingency fee agreement.

- the amount or percentage to be charged if a contingency fee is used;
- the likely amount of the recovery if the case is successful;
- the amount of hours' work which the case is likely to require; and
- the risks that the client is assuming with the particular method of contingency fee calculation offered.

Introducing these kind of directives helps to ensure that clients are fully informed about what their options are. This enables clients to make an informed choice about whether or not entering into the particular contingency fee arrangement is in their best interests.

E *Writing*

It is advisable to require that a contingency fee agreement be in writing. This would help to ensure that the client has given informed consent. Perhaps the best way to do this is to require a standard form to be filled out which includes details of all the relevant matters in the agreement including the lawyer's usual hourly rate, the number of hours the lawyer estimates will be spent on the case, the likelihood of success and the anticipated amount of recovery.

It should also be a requirement that a written copy of the agreement be given to the client along with advice that the client has the right to have the fairness and reasonableness of the fee reviewed. A further option to protect clients from being pressured into a contingency fee agreement, would be to require the written contract to include a provision that the client has a "cooling off" period of a specified number of days. During the cooling off period the client would be able to cancel the contract by notice in writing to the lawyer.[48]

VII *WHO SHOULD ENFORCE THE GUIDELINES/RULES?*

Having decided that the use of contingency fees should be regulated, the next question is who should regulate their use. One option is for the rules and guidelines for the use of contingency fees to be incorporated into the *New Zealand Law Society's Rules of Professional Conduct*. The Rules would then be enforced by the Law Society under the complaints procedure and cost revision procedures set up under the Law Practitioners Act 1982.[49] The current functions of the Law Society include promoting the proper conduct of lawyers and

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48 In South Australia a client has a five day cooling off period after signing a contingency fee agreement, see *South Australia Professional Conduct Rules*, r 8.10 and the Legal Practitioners Act 1981 (SA) s 42(6)(c).

49 See sections 98 to 155 of the Law Practitioners Act 1982. Decisions of the New Zealand Disciplinary Tribunal and revisions of bills of cost made by the District Councils of the Law Society may be appealed in the High Court, see sections 118 and 149.

suppressing dishonourable and improper practices of the legal profession.[50] Controlling contingency fees is a role which would fit neatly under this general function.

The problem with allowing the Law Society to regulate contingency fees is that this role potentially conflicts with another role of the Society; that of promoting the interests of lawyers.[51] The difficulty arising from this conflict of interest between regulating the profession and promoting the interests of the profession has been expressed in a recent report on the functions of New Zealand Law Societies conducted by an independent research organisation:[52]

> ...the present system has evolved over time reflecting, if anything, the interests of lawyers rather than the interests of clients and the public... In fact, the present system has no certainty as to what it is to be promot(ing), the public interest or lawyers' interests, quite apart from which aspects of public interest or lawyers' interest are to be pursued.

The report recommends that a New Zealand Council be established to deal with the regulation and education functions of the New Zealand Law Society, in other words, the Council would promote client interests. The functions of the New Zealand Law Society would then simply revolve around promoting the interests of lawyers. Redesigning the New Zealand Law Society in this way would certainly reduce the conflict of interests facing the regulatory body. Nevertheless, it is anticipated that the New Zealand Law Council would consist of 30 members elected by all practising lawyers and the funding for the Council would come from a levy paid by all practising lawyers.[53] The Council, therefore, would still not be independent from the legal profession. Human nature would tend to suggest that such a self-regulatory body is unlikely to be a completely impartial judge of client complaints.

In the United States, studies have shown that complaints made to self regulatory disciplinary agencies about contingency fees, almost never result in disciplinary action against the lawyers.[54] Self regulation is a process which seems to afford clients little consumer protection. An alternative to self regulation would be to draft the contingency fee rules into legislation and allow clients to complain directly to the courts. The judges who preside over the courts are of course ex lawyers, but they no longer have a direct self interest in the promotion of lawyers' interests so are more independent than a body funded by and made up of lawyers. The disadvantage of handing the task of enforcement solely to

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50 section 4(1)(b) and (c).

51 section 4(1)(a)

52 See E-DEC report, above n 33, 29.

53 See E-DEC report, above n 33, 25.

54 Above n 14, 1354 and 1359.

the courts, is that the courts would act only on complaints made by clients who are prepared to take legal action. Many clients who are dissatisfied with a contingency fee arrangement are unlikely to want to spend the time and the money required to resolve the complaint within the justice system. In addition, clients will only bring complaints about instances of excessive fees or lack of informed consent. Breaches of the rules about subject matter or the prohibition on charging contingency fees when there is no access to justice issue, are not going to come to the attention of the court by virtue of a client complaint. A more informal complaints procedure and a body with powers to investigate complaints made by any persons would be an improvement on relying solely on the courts.

Ideally this complaints procedure and investigation would be carried out by an independent organisation. Any person, including other lawyers, should be able to make a complaint to the organisation about a lawyer's contingency fee arrangements. The organisation could set up a disciplinary procedure and appeals could be heard in the High Court. Alternatively, the organisation could take the complaints to court and allow the court to enforce the contingency fee rules. In this way the organisation would be playing a role similar to the role the Commerce Commission plays in respect of the Fair Trading Act 1986.

The organisation could be either a government-funded body or alternatively a scheme similar to the Legal Services Ombudsman scheme in The United Kingdom could be established. An industry-funded ombudsman scheme is, however, less ideal than a government-funded scheme because the funding in an ombudsman scheme would come from the lawyers themselves and therefore jeopardise the independence of the organisation. However, in the present political climate it may simply be unrealistic to expect a government-funded body to be established. An industry-funded ombudsman scheme may be a more realistic option. Nevertheless either option would probably only be efficient if it was responsible for all facets of legal services complaints and lawyers' ethics, rather than being limited to contingency fees issues.

Consideration also needs to be given to the appropriate disciplinary action for breaches of the various rules on contingency fees. A lawyer who inadvertently breaches the rules in a minor way may need no more than a warning. On the other hand a lawyer who is found to have repeatedly and deliberately charged excessive fees and or engaged in unethical practices in the running of cases in order to win them, should be subject to more severe disciplinary action. Disciplinary action for more serious breaches of the rules could range from imposing fines to suspending the lawyer from practice or striking the lawyer off the roll.

In addition to establishing a disciplinary procedure, there should also be appropriate remedies available for clients who suffer harm from a breach of the rules. If the client is charged an unfair and unreasonable fee there is already provision under Part VIII of the

Law Practitioners Act 1982 to have the costs reviewed. In some situations, however, a client may be charged a quite fair and reasonable fee but still suffer harm because of a lawyer's breach of the contingency fee rules. For example, the client may have been given insufficient or incorrect information and so did not give their informed consent to the contingency fee arrangement or perhaps they were advised incorrectly by their lawyer that an early settlement would be in their best interests. In these situations the lawyer should be required to compensate the client for their loss.

VIII CONCLUSION

This article has concluded that contingency fees are ethical and that it is only the abuse of these fees which is unethical. Because contingency fees can result in the important social advantage of increasing access to justice, they should be legitimised, so long as rules are devised to promote their ethical use. These rules should limit the use of contingency fees to situations where the fee arrangement increases the client's access to justice. The rules should also include guidelines as to what amounts to a fair and reasonable fee, limits on the type of cases in which contingency fees can be used, a requirement that a contingency fee agreement is entered into only with the full and informed consent of the client and a requirement that the agreement be in writing. This type of approach allows society to gain the benefits of contingency fees and yet limits the possibility that these fees will be used in an unethical manner.