BILLING IN A PARETO OPTIMAL WORLD: CREATIVE PRACTICE MANAGEMENT TECHNIQUES TO MATCH EXCELLENT ESTATE PLANNING WITH THE CLIENT'S WILLINGNESS TO PAY FOR SERVICES

presented at the

31st Annual Kansas City Estate Planning Symposium
Kansas City, MO

April 27, 2012

Louis S. Harrison, Esq.
Harrison Held Carroll & Wall, LLP
333 W. Wacker Drive, Suite 1700
Chicago, IL 60606
lharrison@harrisonheld.com

TABLE OF CONTENTS

Introductory Remarks: Why This Topic and Why Now?

We practice law because it is interesting, challenging, we are good at it, and we are professionals. We also practice law because it is our business. As our business, we should rightly expect that fees charged should equal fees collected. And a certain amount of indignancy should accompany those fees that go uncollected. But also a certain amount of blame must remain with the practitioner as to uncollected fees. Did the practitioner follow a Best Practice approach in the fee presentation and collection process?

Minimal useful information has been written in this area as it pertains to estate planning. This paper is intended to be a starting point as to a Best Practices primer on the fee area as it relates to estate planning.

We will consider one of the most important topics, rarely discussed, that of best practices that should be considered by estate planners in their management of client's estate planning expectations and billing. The resulting white paper on recommended strategies is a result of ten years of analysis and research, and reliance on the principles of behavioral finance to explain irrational client behavior (and translating this understanding into action steps). Areas to be discussed will include discussing fees and structuring fee arrangements with clients, understanding and developing bill formats and protocols, and re-tooling practice styles to match client expectations when it comes to billing. Specific items include the importance of demonstrating value to clients relative to the expected fees and tolerance for fees; how to manage client's expectations as to the range of projects undertaken; the advantages and disadvantages of hourly rates versus fixed fees for estate planning work; how to improve on client's perceptions as to the hourly fee; how to increase collections upon billing; setting flat fees and the types of projects for which they are acceptable, as well as the process by which the planner should discuss this alternative with the client and also set the fee; taking into account client behavior as to their estate planning and the payment of fees and focusing on client behavior in developing the estate planning project, expectations, timetable, and billing structure; and structuring estate planning work so that it is done both economically and effectively. We will focus on steps to enhance the profitability of an estate planning and administration practice, while reducing risk, by focusing more on the importance of the billing process and integrating effectively that process into the overall estate planning project. Sample forms and formats are provided.

The presentation discusses billing methodology and practice styles in an effort to solve the following equation -- Imagine a good you purchased - car, TV, hockey stick, fishing pole, boat, plane -- that was so outstanding <u>that after the purchase</u>, you felt good about buying it, regardless of its cost. If we want a longstanding relationship with a client, we want the client to view payment for our services along these same lines. This segment focuses on how our billing protocols can be improved to achieve this level of satisfaction and appreciation.

These materials are divided into three parts. Part One is a written summary of practical concerns with our billing practices and how to address those. Part Two focuses on Value Billing. Part Three is a summary of Best Practices in the Billing Area. Appendices one through four contain useful ancillary material relevant to assessing risk and providing a backdrop for developing billing protocol.

Part One: Improvements to Billing Protocol

A. Understanding What is Needed to Improve Billing

Pre mortem estate planning refers to tax planning, Wills, living trusts, GRATs, education trusts, and all other matters that we do for clients while they are living. Bills are sent directly to those individuals who have requested our services, to deal with a topic that is very painful, albeit important -- Where does the Property that I have worked Hard for During My Life go when I Die?

It's not hard to understand why clients are reluctant to engage in estate planning. It is not a fun topic. Re-read the prior underlined sentence and ponder it a bit.

Therefore, even when we add significant value, say, saving $5 million in future estate taxes, a bill currently of $25,000 may seem repugnant. A bill currently for $10 may also seem repugnant. It's the process of what they are doing, which has no relevance to the tax savings, that is painful for clients to accept.

With that understanding in mind, what are the best billing practices? To understand the answer, one has to begin thinking out of the box as to practices. We should recognize (or agree) that current billing practices are subpar and done because (of what is known, as will be discussed in great detail below, as a status quo bias) they were done before.

Hypothesis 1: There is nothing rational about consumer behavior. As practitioners, we are often not thinking about our billing practices in the most strategic way.

Hypothesis 2: Practitioners spend about 10 % of the amount they should on billing, and disregard its importance to clients' happiness.

Hypothesis 3: Practitioners delay in billing because they know that clients will often perceive their charges as unpleasant and will be unhappy. Delay hurts further.

Hypothesis 4: The following paradigm is the fault of the practitioner, not the client:

Example 1: Practitioner does an A-B estate plan for a client, and quotes the client an hourly billing rate of $250. The project is done efficiently and within the client's time expectations. The hours spent are less than the practitioner anticipated. The hourly rate is less than others in the area. And the overall bill seems less than what it has been in the past. The clients are still surprised at the amount and unhappy.

Hypothesis 5: Which billing format, attachment 1-a or attachment 2, is preferable from a client happiness perspective. Would it shock you if we said that in the vast majority of cases, attachment 2 would be preferable?

Hypothesis 6: Technology has increased the quality, efficiency, and lowered the cost of producing estate planning work product. But this is not reflected in the billable hour concept,

nor accepted by clients as an item to bill for. As practitioners, we have not developed a way to charge for technology.

B. Rationality in Consumer Perception of Our Billing

1. Behavioral Finance

Traditional economics teaches and the logical way lawyers think is that we are all rational actors who make decisions in ways that maximize our financial well being.

An alternative – behavioral economics – relies on cognitive-psychology research to relax those assumptions, teaching us that humans are capable of only so much "rationality," and sometimes make biased decisions that run counter to their objective best interests. We need to understand this in the context of billing.

2. Example as it Relates to Legal Services

Are good results the #1 variable in a client's satisfaction with their legal services?

3. Guiding Principle in All Billing Related Aspects

Expand one's current focus and rely on scientific studies – behavioral finance studies – as to how clients really perceive our services. To do so, eliminate any subjective beliefs as to what billing should be, and rely on the objective.

For example, we fail to understand that consumers are not rational when it comes to hourly billing for estate planning matters. Many of us think that if hours are correctly reported, the hourly rate is reasonable, and the project is done timely, the clients will accept the bill as "reasonable" or as "good value." But fundamentally we are missing a tenet of finance law: that the rational consumer does not always make rational choices, but is influenced by his or her own mental accounting,[1] which often changes rational consumers into irrational ones. Later on, we explore how to fix problems with the hourly charge.

C. Digging Down: The Overriding Principle: Fairness

1. Fairness: Value, Value, Value

Consumers like to perceive themselves as being treated fairly, even when the end result or product or cost is the exact same whether they are being treated fairly or unfairly. Think about an IRS examiner who has two identical cases, both capable of yielding either $300,000 or $500,000 for the government, depending on the level of effort the examiner puts in.

---

[1] In "Mental Accounting Matters," 12 J. Behav. Dec. Making 183-206 (1999), Richard Thaler, one of the leading behavioral economists in the Country, explores the concept of mental accounting. Unlike financial accounting, which consists of numerous rules and conventions that can be explored in a textbook, mental accounting rules – a description of the ways consumers perceive their economic choices—can only be observed by behavior and inferring the rules.

To the extent one taxpayer is perceived as "trying to pull a fast one" on the agent, and the other taxpayer is acting reasonably and perceived to be a straight up kind of person, the agent is more likely to audit the Fast Eddie-prepared return more ferociously than the other. Why? Perceptions of fairness. Here's another:

Example 2: You're sitting on the Beach at La Semana in St. Marteen's, hot as the dickens. And thirsty. You're buddy says he is going to buy a beer at the hotel and asks if you want one. You say yes; he asks if you care how much it costs, even if it costs $15? You say no because you know it will cost a lot. The place you are staying is expensive, and you expect that they will charge a lot for their stuff. Your buddy decides not to go. Instead, a bum on a push cart comes buy and asks if you would like ice cold Heinekan's…you think yes…until the bum says, "$15." Why should that guy make so much money from me?[2]

2. Exploring Fairness in an Arbitrary and Capricious World

The ultimatum game – illustrates why a person may punish herself to punish a third party she perceives as acting unfair? (To be illustrated during the oral presentation).

A sale to a grantor trust strategy can be very effective. It is a complicated transaction with many moving parts. Should, objectively, cost ever really be a determinant for a client in going forward with this strategy? The ultimatum game illustrates why sometimes it is. If it is, would there have been a different way to have framed the cost to have made the issue more palatable, and less concerning, to a client?

3. Two End Results that are the Same Can Still Lead to Different Actions by an Individual as a Result of Perceptions of Fairness

Example 3: You go to the store to buy your favorite movie on a DVD. It is priced at $14.99. While at the store, your best friend mentions that the same DVD is available for $4.99 at the Walgreen's about 15 minutes away. Will you go to the Walgreen's? Compare this to the situation where you are at the Stereo store and the salesperson says the stereo costs $499. Your best friend says the same stereo is available at $489 at the store 15 minutes away. Will you go to the other store? There's no difference financially, but the results have empirically been shown to be different. The consumer's perceptions are different in both situations, reflecting fairness issues. Conclusion: we cannot assume economic rationality —- that clients will consistently act in a way that maximizes their financial interests — for our client's economic decisions.

[2] Example adapted from *Thaler*, *infra*.

D. Fairness as it Translates to the Hourly Rate

1. Problems with Hourly.

A client may perceive an hourly rate of $350 to be "way too expensive" for someone spending an hour thinking about something. Is that rational (probably not, *see* below). In contrast, the client may perceive a bill for $5,000 for estate planning documents that achieve estate tax savings, creditor protection trusts, management of assets in the event of disability, and so on, as being reasonable.[3]

Meaning, in estate planning (not estate administration or contested litigation), disabuse yourself that hourly billing, without more, is satisfactory. You must do more than just emphasize hourly billing as being the measure. For example, practice the concept of either doing or demonstrating project/value billing as much as possible.

> *Example 4: It's not rational: Attorney X recently spent about an hour coming up with an estate planning wrinkle for a client that saved him about $500,000 on a strategy. If the Attorney quoted him an hourly rate of $2,000, and then sent him a bill for $2,000, the client would be upset. If the Attorney quoted him a flat fee of $5,000 to try to implement a strategy that would save $500,000, he may have been absolutely fine with this, depending on the framing of the project and resolution.*

How much are hourly rates despised by clients? In a Wall Street Journal article in August of this year, the author cited a few developments by public companies with regard to the hourly rate:

"Cisco Systems Inc. has notified its stable of outside law firms that it is vital for the company to move away from the hourly billing structure. Cisco now uses fixed fees or other alternatives to the billable hour for about 80 % of its legal work."

In the same article, the author points out the (irrational) distrust by clients of the hourly rate:

"Companies have long complained that legal fees are inflated by a business model in which law firms have high priced junior lawyers who must be kept busy billing for work that could be handled more efficiently." Id.

And companies are reacting to this perception:

"Pfizer used to have a rule that no lawyer with an hourly rate higher than a second year attorney could bill the drug company for legal research." Id.

[3] Assume the plan took five total hours to prepare, but that total hours is not reported on the bill.

And shifting from hourly does not mean a reduction in revenue or profitability:

"Orrick, Herrington & Sutcliffe LLP…has tripled the revenue it generates from alternative billing arrangements in the past year, but maintained profitability through efficiencies." Id.

2. The Six Point Process to Make the Hourly Rate Fair:

The following principles will all be explored during the oral presentation. The techniques:

(a) Project Fees (*See also*, discussion on the consumer value function)

(b) Quoting Ranges

(c) Self Affirmation

Referencing at the first meeting the lawyer's professional affiliations, speeches, articles, reputation, other clients as references (careful to preserve confidentiality, very important for estate planners), and the substantial level of a typical client.

And, though price should never be a factor in trying to convince a client to use us – "we're cheaper" sounds bad as a marketing technique (ouch!) – letting a client know that the costs for your services will be in the range of what others at your level costs, will add to the client's perception of fairness.

(d) Anchoring

(e) Relativity

(f) Ambience

Example 5: I am a casual guy, but could never understand (and think lawyers are short sighted when it comes to trends) why our profession would want to be casual. A lawyer in a nice suit connotes value, thereby connoting a certain professionalism that carries with it the expectation that the charge for services will be great. Well groomed, manicured, well spoken; all go hand in hand. Cf. La Semana versus the bum example above.

Offices and how they look are another aspect of perceived value.

7. And Formatting, a topic in and of itself.

E. Formatting the Bill

Fairness dictates that the bill must connote value. Another principle that is relevant to how we bill and charge clients is how we all "feel pain."

1. Understanding The Consumer's Value Function: One Big Hurt Is Better Than A Series Of Small Hurts

The loss function is convex, meaning that the marginal pain felt by incremental losses is greater than the pain felt by a larger loss. Specifically, as to the losses, the pain associated with the sum of the parts is greater than the pain associated with the whole. For example, if you lose $5 daily on an investment over nine days, for a total $45, this will be more painful to you than if you lose $50 in one day during this nine-day period.

Ponder how this applies to a bill:

1. Every day entry associated with a time is translated into an hourly charge, a loss.

2. A bill with 20 daily time entries results in 20 losses. "Death by a 1,000 Cuts." It is more painful to review than a bill with one entry. Other businesses recognize this.

> *Example 6: "Consider the case of the pricing policies of the Club Med resorts. At these vacation spots consumers pay a fixed fee for a vacation that includes meals, lodging and recreation. This plan has two advantages. First, the extra cost of including the meals and reaction in the price will look relatively small when combined with the other cost of the vacation. Second, under the alternative plan each of the small expenditures looks large by itself, and is likely to be accompanied by a substantial dose of negative transaction utility given the prices found at most resorts."* Thaler*, infra, at 192.*

What does this mean for our billing? Flat fees are much more preferable because a consumer may get greater transaction utility out of powers of attorney than out of drafting a complicated trust, but when each are broken out, the consumer evaluates each action separately and determines whether each action translates into value equivalent to the cost. Further, flat fees avoid the marginal pain associated with each hourly "loss." Clients would much prefer fixed fees, for a variety of reasons.

Thaler notes, **not** in the context of law billing (interestingly):

> *"[C]onsumers don't like the experience of 'having the meter running'. This contributes to what has been called the 'flat rate bias' in telecommunications. Most telephone customers elect a flat rate service even though paying the call would cost them less."*

2. Mechanically How to Write Bills

A. Two aspects: narrative and the structure. First the narrative. Understand the concept of framing. Consider framing in the context of attachments 1-a and 1-b.

Because people are loss adverse, ponder whether we can achieve better fees by framing fees in the positive, e.g., contingent fees if there are tax savings. For example, if our billing practices were set up so that clients merely had to pay us if they succeeded in achieving tax savings, that would be easier to bill and many of us would now be retired.

Example 5: in 1984, for A-B plans, we would describe to clients that if we were able to achieve a tax savings greater than without estate plan, we would be paid 20 % of the tax savings, but only at that point. Most clients would be delighted with this option. Sound bad to you? It should not. Consider the average time to payoff for a client age 65 would be less than 20 years. What's the current value in 1984 of tax savings in 2004? In 2004, the credit was, say, 1.5 million. So the savings with an A-B plan could be $750,000. 20 % of this amount would be $150,000. Ignoring the friction associated with transaction costs to collect this amount, the discounted present value in 1984 of $150,000 to be received in 2004 at a 5 % discount rate is $56,533 ($150,000/(1+.05)^20). Yes, we would all be done at this point in our practice. Not only that, but those of us who are older could have monetized our practices and sold these fee arrangements in 2004, without having to work another day. (Importantly, now we have circular 230 constraints.)

But returning to reality, and recognizing that we do not bill on "tax savings," then to the extent bills are detailed in their descriptions, or projects summarized in cover letters, we should not be afraid to frame in the positive versus the negative. E.g., which sounds better: "Draft of trusts to address estate tax issues;" or "Incorporation of estate tax savings trusts." Or, "Draft of generation skipping trusts" versus "structure of trusts to prevent the payment of estate tax as assets move from generation to generation."

B. Format of the Bill (ignoring the narrative): how do we get a bill so that the consumer feels one large loss, not a series of small losses that objectively add up to less than the large loss, but subjectively are much greater pain than the large loss? Ponder the $10 additional charge for internet in your $400 hotel room, versus all inclusive in your $450 hotel room (e.g., same hotel room). Ponder, further, charges of $5 for a copy job and a $5,000 bill. Why is the $5 an irritation, and not the $5,000?

Attachments 1-3 provide sample billing formats, which all correctly report the time and effort on a matter. Attachment 3 is the most detailed, but also the least friendly and most offensive to most estate planning clients. In determining which format to use for individual clients, the question should be asked: which one provides the kind of information that would be useful to the client in addressing the value provided, and therefore the amount of the bill?

Attachment 1 provides an evolving format of what could be useful to the client. Attachment 1-a is an unedited day by day description of the work done, without too much thought of its impact on a client reading it. Attachment 1-b creates a better picture of what was done. Attachment 1-c is a narrative summary of the actions taken. Commentators believe that 1-c is preferable to 1-b, but it should be considered and tried only on a case by case basis.

F. Get Rid of the Bogus Plaintiff Case: I Need a New Car but Cannot Afford It

Clients that should do sophisticated estate planning, such as GRATs, QPRTs, and other advanced techniques, often hesitate to complete such projects for two primary reasons: first, the

clients may feel that their own wealth cannot be jeopardized by a current transfer; or second, clients may not want to incur the costs. There are myriad other reasons, some subtle, some not so, such as not wanting kids to have immediate access to funds, not wanting to deal with one's mortality and focus on such advanced estate planning items, desiring to simplify, not complicate, one's life; or feeling good about one's wealth and defining oneself by it.

Practitioners should certainly docket a client's decision for inaction, that is, the client's decision not to proceed with a strategy. But the practitioner should also realize that inaction can be ameliorated, to an extent, by the principles discussed here with regard to billing.

Consider the following. First, for a client that is on the border as to whether to proceed with an advanced planning strategy, or even basic estate planning, a restructuring of the billing protocol can push that client to action. From the principles discussed in this article, we know that there are two basic principles that make billing more palatable to the client: (1) fairness and (2) one large loss is easier to handle than a series of smaller ones that do not add up the large one. In other words, eliminate the hourly rate in the fee quote, which satisfies neither the fairness equation, nor (the behavior finance principle to) aggregate losses. Hourly rates are perceived as unfair, and each hourly entry inflicts pain. Further, a client does not know the extent of his potential losses with an hourly bill concept, and the client's loss aversion tells her not to go ahead. As a result, instead of the hourly quote, quote the client on a flat fee basis.

Second, break the overall estate planning project into smaller projects, and quote a fee for each project, thereby allowing the client to proceed on a landscaping sort of basis, doing the front estate planning yard this year, the side planning yard next year, and so forth.

Third, make sure you demonstrate to the client the tax and non tax value that will be obtained by the client by completing these projects (*e.g.*, dollars potentially saved, spousal protection for kids, family harmony, or philanthropic desires). As an iteration on the fairness concept, a client that perceives value to the end result of the planning will also perceive the bill as fair. As we will discuss during the oral presentation, a client's acceptance of the fairness of the price is also based on their perception of your high quality as a practitioner.

G. Macro Takeaway

How interesting behavioral finance is to what we do on a day to day basis. We would theorize that focus on this area could be the single greatest untapped value to us as practitioners. But it does require thought and focus, and effort for which no hourly payment is immediately made. Creativity on bonus structures is perhaps our greatest missed opportunity. As the tired metaphor goes, "we can't catch any fish if our pole is not in the billing lake to begin with." We sometimes become so focused on short term results associated with hourly billing that we miss the retirement forest for the billing trees.

Attachment 1-a

Day & Night, 333 Aurora Borealis Way, Chicago, IL 60606-1218 www.dayandnight.com

Invoice submitted to:

Marc and Cleo Antony
Estate Planning
One Mag Mile
Chicago, IL 60610

Invoice Number: 4950

July 01, 2007

Professional Services

Amount		
5/12/2006	CGW	Draft new wills, powers of attorney for property and health care and living trusts for Marc and Cleo Antony.
5/15/2006	CGW	Continue to draft new living trusts for Marc and Cleo Antony (dispositive provisions including subtrusts for children; tax and trustee provisions); draft letter to Marc and Cleo summarizing key terms of their new estate planning documents, tax consequences thereunder and asset reallocation issues.
5/10/2007	CGW	Review summary of proposed estate planning documents for Marc and Cleo Antony; work with Lou Harrison on fine tuning the Antonys' new plan.
5/30/2007	LSH	Review and analysis of drafts of documents; update to fiduciary provisions; update to generation skipping provisions; transmittal for review.
6/26/2007	CGW	Review file in preparation for meeting with the Antonys; meeting with Marc and Cleo to discuss drafts of their new estate planning documents and proposed revisions to documents. Begin revisions.
6/27/2007	CGW	Revising and finalizing living trusts and wills for Marc and Cleo; conference with Cleo regarding fiduciary backups; having documents prepared for execution.
6/28/2007	CGW	Meeting with Marc and Cleo to execute estate planning documents; prepare for meeting; post-meeting notes regarding issues for follow up.

6/29/2007 CGW Draft letters to the Antonys and J. Caesar and send them booklets of the Antonys' new estate planning documents.

Subtotal of charges	$3,682.50
Courtesy Discount	($182.50)
For professional services rendered	$3,500.00

Timekeeper Summary

Name	Hours	Rate
Constance G. Work (CGW)	10.40	325.00
Len S. Happenstance (LSH)	0.92	330.00

Attachment 1-b

Day & Night, 333 Aurora Borealis Way, Chicago, IL 60606-1218 www.dayandnight.com

Invoice submitted to:

Marc and Cleo Antony
Estate Planning
One Mag Mile
Chicago, IL 60610

July 01, 2007 Invoice Number: 4950

Professional Services

		Amount
5/12/2006	CGW	Initial outline of distribution provisions to be included in estate planning documents, and outlining terms of tax beneficial credit shelter and marital trusts, for Marc and Cleo Antony. Determination to use Will/living trust format for the estate plan.
5/14/2007	CGW	Draft trusts for children, including spousal and creditor protection features; work on trustee provisions in documents, including successor trustees, and means to appoint successors when none are named; consideration of distributions to grandchildren and draft of provision. Draft letter to Marc and Cleo summarizing key terms of their new estate planning documents, tax consequences thereunder and asset reallocation issues.
5/15/2006	CGW	Draft distribution provisions for credit shelter and marital trust, to incorporate tax and creditor planning. Work on drafting terms consistent with decisions at meeting.
5/30/2007	LSH	Review and analysis of tax and fiduciary provisions in the drafts of documents to make sure they comply with most recent provisions in the law. Update to fiduciary provisions. Update to generation skipping provisions. Transmittal to the Antonys for their review.
6/26/2007	CGW	Meeting with Marc and Cleo to review and discuss drafts of their new estate planning documents and proposed revisions to documents.

6/27/2007 CGW Following meeting, update and finalize living trusts and wills for Marc and Cleo to incorporate different distribution provisions, protective tax and creditor provisions for children. Follow up phone conference with Cleo regarding fiduciary backups; preparation of documents in final form.

6/28/2007 CGW Prepare items needed to implement estate planning documents prior to meeting. Meeting with Marc and Cleo to execute estate planning documents. Post-meeting notes regarding issues for follow up.

6/29/2007 CGW Calendaring key dates for review plan documents, to finish on funding and beneficiary designation update; Work and review of closing book to make sure no additional items needed. Work on document book to Cleo and Antony.

Subtotal of charges	3,682.50
Courtesy Discount	(182.50)
For professional services rendered	$3,500.00

Timekeeper Summary

Name	Hours	Rate
Constance G. Work (CGW)	10.40	325.00
Len S. Happenstance (LSH)	0.92	330.00

Attachment 1-c

Day & Night, 333 Aurora Borealis Way, Chicago, IL 60606-1218 www.dayandnight.com

Invoice submitted to:

Marc and Cleo Antony
Estate Planning
One Mag Mile

Invoice Number: 4950

July 01, 2007

Professional Services

Amount

5/12/2006 CGW Initial outline of distribution provisions to be included in estate planning documents, and outlining terms of credit shelter and marital trusts, for Marc and Cleo Antony. Determination to use Will/living trust format for the estates plan; 5/15/2006 CGW Draft distribution provisions for credit shelter and marital trust, to incorporate tax and creditor planning; work on terms consistent with meeting; 5/10/2007 CGW Draft trusts for children, including spousal and creditor protection features; work on trustee provisions in documents, including successor trustees, and means to appoint successors when none are named. including subtrusts for children; tax and trustee provisions). Draft letter to Marc and Cleo summarizing key terms of their new estate planning documents, tax consequences thereunder and asset reallocation issues; 5/30/2007 LSH Review and analysis of drafts of documents; update to fiduciary provisions; update to generation skipping provisions; transmittal for review; 6/26/2007 CGW Meeting with Marc and Cleo to discuss drafts of their new estate planning documents and proposed revisions to documents; 6/27/2007 CGW Following meeting, update and finalize living trusts and wills for Marc and Cleo to incorporate different distribution provisions, protective tax and creditor provisions for children. Follow up phone conference with Cleo regarding fiduciary backups; preparation of documents in final form; 6/28/2007 CGW Meeting with Marc and Cleo to execute estate planning documents; prepare for meeting; post-meeting notes regarding issues for follow up; 6/29/2007 CGW Calendaring key dates for review plan documents, to finish on funding and beneficiary designation update; Work and review of closing book to make sure no additional items needed. Work on document book to Cleo and Antony.

Subtotal of charges	$3,682.50
Courtesy Discount	($182.50)

For professional services rendered $3,500.00

Timekeeper Summary

Name	Hours	Rate
Constance G. Work (CGW)	10.40	325.00
Len S. Happenstance (LSH)	0.92	330.00

Attachment 2

Day & Night, 333 Aurora Borealis Way, Chicago, IL 60606-1218 www.dayandnight.com

Invoice submitted to:

Marc and Cleo Antony
Estate Planning
One Mag Mile
Chicago, IL 60610

Tax ID

April 28,2008

For professional services rendered $3,500.00

Timekeeper Summary

Name	Hours	Rate
Constance G. Work (CGW)	10.40	325.00
Len S. Happenstance (LSH)	0.92	330.00

Attachment 3: Illustration of a Not so Good Bill and Consideration of Its Impact on Client

(10 pages of following bill intentionally omitted)

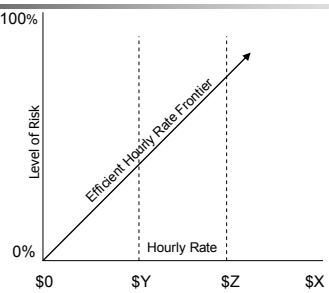
Client_name	Folder_name	Initials	Effective Date	Hours	Rate	Dollars	Comments
Estate of Josey Smith	Tax Compliance	M. Stennett	09/19/2007 00:00:00	5.9	$ 255.00	$ 1,504.50	Estate Planning - Section 6161 Analysis v Strangi Note, Cash Flow Projections
Estate of Josey Smith	Tax Compliance	M. Stennett	01/15/2008 00:00:00	0.5	$ 268.00	$ 134.00	Estate Form 706
Estate of Josey Smith	Tax Compliance	M. Stennett	01/11/2008 00:00:00	1.2	$ 268.00	$ 321.60	Form 706
Estate of Josey Smith	Tax Compliance	M. Stennett	09/21/2007 00:00:00	2.2	$ 255.00	$ 561.00	Estate planning Analysis, prep for next weeks meeting
Estate of Josey Smith	Tax Compliance	M. Stennett	09/20/2007 00:00:00	1.9	$ 255.00	$ 484.50	6161 Analysis - meeting with Joe
Estate of Josey Smith	Tax Compliance	M. Stennett	12/24/2007 00:00:00	0.5	$ 255.00	$ 127.50	Form 706 and valuation communications
Estate of Josey Smith	Tax Compliance	M. Stennett	09/28/2007 00:00:00	0.7	$ 255.00	$ 178.50	Client communications
Estate of Josey Smith	Tax Compliance	M. Stennett	11/20/2007 00:00:00	0.3	$ 255.00	$ 76.50	Estate Form 706

Estate of Josey Smith	Tax Compliance	M. Stennett	09/24/2007 00:00:00	7	$	255.00	$ 1,785.00	Estate Cash Flow Projections
Estate of Josey Smith	Tax Compliance	M. Stennett	09/26/2007 00:00:00	6.6	$	255.00	$ 1,683.00	Cash Flow Projections and preparation and attendance of meeting
Estate of Josey Smith	Tax Compliance	M. Stennett	07/27/2007 00:00:00	4.9	$	230.00	$ 1,127.00	Preparation for, attendance, and recap of Estate of AJ Smith meeting
Estate of Josey Smith	Tax Compliance	M. Stennett	09/27/2007 00:00:00	1.1	$	255.00	$ 280.50	Cash Flow Projections and T/C with Harvey
Estate of Josey Smith	Tax Compliance	M. Stennett	01/09/2008 00:00:00	0.8	$	268.00	$ 214.40	Form 706
			J. Koney Total	17.4			$ 2,674.00	
			Grand Total	132.9			$ 45,196.40	
Estate of Josey Smith	Tax Compliance	E. Tarzan	11/23/2007	0	$	-	$ 7,700.00	Progress Bill
Estate of Josey Smith	Tax Compliance	E. Tarzan	10/3/2007	0	$	-	$ 14,630.00	Progress Bill
Estate of Josey Smith	Tax Compliance	E. Tarzan	9/11/2007	0	$	-	$ 13,265.00	Progress Bill
Estate of Josey Smith	Tax Compliance	E. Tarzan	1/22/2008	0	$	-	$ 9,620.00	Progress Bill
							$ 62,312.00	

Part Two: Premium Billing

A. Is the Billing Method Fair to the Practitioner?

The Hypothetical Hourly Rate in the Context of RISK;
Why the Hourly Rate can be Fatal to One's Practice



Note: $Y and $Z are stable rates independent of risk

(1) What action items does a practitioner take based on this knowledge? (Pricing should be along diagonal line based on risk)
(2) If practitioners take such action, what happens in the long run to vertical $Y and $Z lines? (They become diagonal)
(3) Will not happen in practice because risk is not built into the hourly structure.
(4) Note: Risk is not necessarily tied to complexity; *e.g.*, difficulty of client, sensitivity of matter, time urgencies, level of inattention, fee constraints can all add to level of risk. Reviewing another firm's estate planning documents for a "second opinion" is fraught with risk.
(5) If pricing cannot take into account risk, what actions should we take? (focus on not taking matter, or know that you are getting paid less than risk you are taking, or increase effort to decrease risk)

145855 7-72 PPT

B. The Premium Method Illustrated

Generally, the hourly rate is an accepted – albeit not appreciated by the practitioner or client –method for billing by an attorney. Interestingly, hourly rates have not been called into question under ethical rules, but fees are always subject to a reasonableness structure.

In this section, we examine how and when a practitioner can impose a bonus or premium concept because the results obtained are so GOOD in light of expected outcomes due to the practitioner's unique solution to a difficult issue.

As with billing practices generally, there is a methodology as to how this is to be done.

> *Example of premium concept. The practitioner develops a financial model for pricing a stream of earnings on lottery winnings, to justify a liquidity discount based on lack of marketability and a synthetically arrived at comparable asset. The practitioner develops this methodology based on substantial capital investment into financial instruments over a period of months, and develops a strategy around certain Tax Court cases holding to the contrary. The practitioner indicates that the set fee for the strategy is $X, independent of the hourly effort and independent of the result achieved.*

The steps to impose such a premium or bonus payment is constrained by each state's ethical constraints and federally mandated guidelines under Circular 230.

C. Ethical and Regulatory Considerations in Billing Practices

1. **Generally**

MRPC 1.5(a) provides that a lawyer's fee must be reasonable considering an enumerated list of factors.

Reg. §10.27(a) of Circular 230 provides that a practitioner may not charge an unconscionable fee.

Reg. §10.30(b)(2) of Circular 230 provides that if a practitioner publishes a written fee schedule, then the practitioner may not charge more than the published rates for the 30 day period after the publication.

2. **As Applied to Bonus or Contingent Fees**

MRPC 1.5(c) provides that all contingent fee arrangements must be agreed to in a writing signed by the client.

For fee arrangements entered into after March 26, 2008, Reg. §10.27(b)[4] of Circular 230 provides that a practitioner may charge a contingent fee in any "matter before the IRS" *only in connection with*:

- The Service's examination of or challenge to: i) an original tax return; or ii) an amended tax return or claim for refund filed before the taxpayer received written notice of an examination of or challenge to the original return, or an amended return or claim for refund filed no later than 120 days after the taxpayer received written notice of an examination of or challenge to the taxpayer's original return.

- A claim for credit or refund filed solely to determine statutory interest or penalties assessed by the Service.

- A claim under IRC §7623 (the whistleblower statute).

- Any judicial proceeding arising under the Internal Revenue Code.

All other contingent fees for "matters before the IRS" are prohibited under §10.27(b)(1) of Circular 230.

Reg. §10.27(c)(1) defines a contingent fee as:

[4]As amended by Notice 2008-43, 2008-15 IRB 748.

> "[A]ny fee that is based, in whole or in part, on whether or not a position taken on a tax return or other filing avoids challenge by the Internal Revenue Service or is sustained either by the Internal Revenue Service or in litigation. A contingent fee includes a fee that is based on a percentage of the refund reported on a return, that is based on a percentage of the taxes saved, or that otherwise depends on the specific result attained. A contingent fee also includes any fee arrangement in which the practitioner will reimburse the client for all or a portion of the client's fee in the event that a position taken on a tax return or other filing is challenged by the Internal Revenue Service or is not sustained, whether pursuant to an indemnity agreement, a guarantee, rescission rights, or any other arrangement with a similar effect."

As a result, any fee based on a specific tax result, regardless of how the fee is calculated, is included in the definition of "contingent fees." For example, the definition seems to include not only percentage based fees but also success premiums and bonuses for certain results.

Reg. §10.27(c)(2) provides that a "matter before the IRS" includes:

> "tax planning and advice, preparing or filing or assisting in preparing or filing returns or claims for refund or credit, and all matters connected with a presentation to the Internal Revenue Service or any of its officers or employees relating to a taxpayer's rights, privileges, or liabilities under laws or regulations administered by the Internal Revenue Service. Such presentations include, but are not limited to, preparing and filing documents, corresponding and communicating with the Internal Revenue Service, rendering written advice with respect to any entity, transaction, plan or arrangement, and representing a client at conferences, hearings, and meetings."

Apparently, the policy behind the Circular 230 rules is that contingent fees should not be allowed in cases in which the audit lottery is played and won. Rather, contingent fees will be permitted only in those cases in which the government is directly involved.

3. **Sanctions for Willful Violation of Circular 230 Regulations**

After notice and an opportunity for a hearing, the Secretary of the Treasury may censure, suspend, or disbar a practitioner from practice before the IRS if the practitioner willfully violates the Circular 230 Regulations (Reg. §10.50(a) and Reg. §10.52(a)(1)).

In addition to the censure, suspension, or disbarment, after notice and an opportunity for a hearing, the Secretary of the Treasury may impose a monetary penalty on the practitioner or on his or her firm, if the firm knew or should have known about the conduct (Reg. §10.50(c)(1)(i) and Reg. §10.50(c)(1)(ii)). The amount of the penalty is limited to the gross income derived (or to be derived) from the prohibited conduct (Reg. §10.50(c)(2)).

Ironically, the impermissible contingent fee is not refunded to the taxpayer. The Service gets to recover a portion of the taxpayer's tax savings through the Treasury's imposition of a monetary penalty.

Example of a monetary penalty. Assume an attorney enters into an agreement with the Personal Representative of the Estate that the attorney will receive 1/3 of any tax savings associated with an FLLC discount. Assume the FLLC discount results in $1 million in tax savings and the Estate is not selected for audit. The attorney is paid $333,333 as her fee. The Secretary of the Treasury gives the attorney notice and an opportunity for a hearing. After the administrative proceeding occurs, the Secretary disbars the attorney from practice before the IRS and imposes a monetary penalty of $333,333.

The bottom line result is that the IRS recovered $333,333 of the tax it lost in this Estate. And since this is a before tax amount, the practitioner is substantially disadvantaged monetarily.

D. Planning Examples of the Bonus Fee as Impacted by Circular 230 Prohibitions on Contingent Fees

1. Client engages estate planning attorney to create an FLLC. The fee agreement is entered into in April, 2008, is in writing, and provides that the attorney will receive a fee of $x for the project. The FLLC is implemented and client dies in March, 2009. The PRs of the estate engage the same attorney to handle tax matters for the estate. The fee agreement is in writing and provides that for all services, except handling an estate tax audit or tax litigation, the lawyer will be paid on an hourly basis. The 706 is filed in December, 2009 and reflects a valuation discount on the FLLC units. The 706 is selected for audit. The PRs and the attorney enter into a separate written fee agreement whereby the attorney agrees to handle the estate tax audit on a contingent fee basis. Is the attorney in compliance with the MRPC and Circular 230?

2. Client engages an attorney to obtain a private letter ruling with respect to a transfer tax issue. May the attorney undertake the representation on a contingent fee basis?

3. The PRs of an estate engage an attorney to handle the estate. May the attorney structure his or her fee as a combination of hourly rates with a "success premium" for success in connection with the estate tax?

    a. Why would a client hire an attorney on this basis post mortem, versus the pre mortem structuring?

    b. 230 constraints?

4. Attorney has an estate planning strategy that he has developed, or a wrinkle to an existing strategy that he believes works in the current setting. The attorney is not willing to be engaged in the project on an hourly basis for the following reasons:

    a. The risk to the practitioner of the strategy not succeeding far outweighs the compensation to be attained on an hourly basis;

b. The practitioner has spent substantial time developing the concept for which he was not compensated;

c. The practitioner has a strategy not in the common domain for which she expects a premium for under the principles of supply and demand; and

d. The practitioner believes that the strategy will save substantial taxes not otherwise obtainable via any other strategy.

The attorney is cognizant of the following prohibition: "A contingent fee includes a fee that is based on a … percentage of the taxes saved, or that otherwise depends on the specific result attained." Accordingly, the practitioner indicates that the strategy could save up to $5,000,000, and offers to provide the strategy for a flat $Y, independent of whether the strategy is successful or not.

a. Is this a fee based on a percentage of the taxes saved, or that otherwise depends on the specific result attained.

b. Can the practitioner market the strategy to a client?

c. Is the fee reasonable?

d. What happens if the strategy is not successful? Clearly, a refund is prohibited by Circular 230, and practitioner knows that even permissible estate tax strategies are sometimes not allowed by the Service (to our dismay, but to one's hourly advantage sometimes).

E. Construct Premium Billing Arrangements

First, the concept must be agreed to by the client at the beginning of the representation; e.g., merely asking for a bonus at the end because the result obtained was so good is not a prudent approach.

Second, the objective must be defined, but more importantly, what unique talent or recommendation is the practitioner bringing to the equation that justifies the bonus fee.

Example: Structuring a 5 year GRAT transaction, for a 75 year old, with a 5 year SCIN hedge, structured along the same economic lines, and assuming reasonable rate of return objectives (are there any these days?) for the GRAT, can result in a risk free estate tax arbitrage. Structuring a SCIN, taking into account both section 2036 and income tax results, is not generic and can be quite difficult. Achieving the arbitrage, and structuring the actuarial risk premium internally, require unique practitioner skills. This kind of transaction is one justifying a bonus fee.

Third, the prohibitions in Circular 230 must be avoided. Merely describing the fee as a percentage of projected tax savings is now not allowed under C 230. A bonus of $Z dollars, independent of whether the strategy is successful, is one way to consider the bonus.

Fourth, the client needs to be satisfied with the arrangement. Creative structuring of the payment of the bill is one way to achieve client satisfaction. E.g., with the $Z dollar bonus, can it be structured so that the client's children pay it at the time of the filing of the estate tax return? Or from the property transferred during life if the strategy relates to a lifetime transfer?

Fifth, the bonus should be in writing, in an engagement letter signed by the client. However, is the language in the letter sufficient to justify the premium while at the same time not sabotaging the strategy if produced in audit on examination?

The above constraints and steps are important, and to the practitioner engaging in bonus billing for the first time, somewhat daunting. On the other hand, as practitioners we do not shy away from engagements just because they are difficult. Likewise, we should provide the same respect to the business side of our practices, and not shy away from the premium billing concept merely because it is difficult to implement.

The premise and answer must remain the same: if a practitioner is providing a unique strategy to solve a difficult legal equation, that practitioner should be rewarded on more than an hourly basis. Keep in mind that the hourly billing method assumes excellent work for every minute committed to a problem. It does not guarantee success, nor does it pay for work that is beyond excellence – that is, the unique solution to a difficult quandary.

Part Three: The White Paper Techniques For Preferable Billing

The Best Practice Summation (discussed in outline and oral presentation)

1. Discuss fees during the initial meeting
2. Time that discussion for the tail end of the meeting
3. Determine a fee quote at the first meeting
4. Deliver fee quote in a thought out manner and make sure you believe in and deliver the quote in a way conveying fairness
5. Have client provide down payment or retainer before engagement begins
6. Understand that Fairness matters to clients – clients want to pay for services that they perceive as Fair
7. Many estate planning projects will be perceived as Fair if quoted as a Flat Fee
8. To demonstrate Fairness, make sure that all the component parts, and accomplishments, with the estate planning project are demonstrated throughout the project; also, deliver excellent service; also, de-cliché clichés
9. Divide estate planning BIG PROJECT into sub projects so that value and accomplishments can be more easily understood
10. Value added billing can be considered but must be addressed in the engagement letter (see below)
11. Send bills frequently and timely
12. On a bill, do not exceed a quoted fee unless explained and discussed with the client during the project
13. Connote value in the bill itself and descriptions; spend time with each individual bill
14. Make sure to consider the format of the bill that will most easily connote value and which will avoid the Client's Loss Aversion function
15. Decouple Having to Have the Consumer Assign a 'Value' to Each Hourly Charge

A decoupling device noted by Thaler is the credit card:

"We know that credit cards facilitate spending simply by the fact that stores are willing to pay 3 % or more of their revenues to the card companies…A credit card decouples the purchase from the payment in several ways. First, it postpones the payment by a few weeks. This delay creates two distinct effects: (a) the payment is later than the purchase; (b) the payment is separate from the purchase. A second factor contributing to the attractiveness of credit card spending is that once the bill arrives, the purchase is mixed in with many others," Thaler, infra (emphasis added).

Takeaways for us: credit cards can be used for a service business. If we decide to go this route, do we pass the cost along to our clients? If we take credit cards, beware of credit card fraud, of which there may be no insurance.

How else can we decouple our services? To the extent we can get clients on a flat retainer, or an annual charge, and include as many services as possible, this will decouple (as will a "project" fee). Payment for services out of a trust or closely held company can also decouple the benefits associated with the services from the pain of payment.

Decoupling could also apply to the services provided. Instead of bundling services, break them into distinct projects so that each project can have a positive marginal utility associated with it. As a mental exercise, can you decouple one estate planning project into 20 distinct services provided by the documents? Transfer Tax planning, Income tax planning, Creditor protection, Funeral plans, Protecting assets if child is a spendthrift, Planning for the children's education, Protecting assets in the event of disability, Planning for a child with a disability, Providing health care alternatives, Organ donation options, Guardians for the children, Planning for long term care, Planning for liquidity at a person's passing., Doing beneficiary designations correctly, Reallocating assets, Planning for college funding, Preserving tax-free nature of retirement planning, Assessing insurance needs, and Assistance in a plan to get rid of household stuff, Preserving peace in the barnyard

16. Discounting is appreciated by clients, in many situations. In addition to discounts, another item that is effective, and a bit more subtle than discounting, is that "luxurious gifts can be better than cash," which according to Thaler, is "well known to those who design sales compensation schemes." What are we doing for clients above and beyond providing them services? We will be discussing this in some detail during the oral presentation.
17. Demonstrate client care throughout the process by prompt service, attention, and non work communications
18. Know when you are proposing unique solutions to an estate planning or transfer tax issue that justifies a bonus or premium arrangement
19. Consider for unique solutions to difficult projects structuring the engagement as a combination hourly, accompanied with a bonus payment because of the uniqueness of the solution
20. Make sure the bonus avoids Circular 230 prohibitions
21. Determine how to properly discuss and market the bonus structure to a client

Appendix One: Relevant Provisions of Circular 230:

§ 10.27 Fees.

"(a) *In general.* A practitioner may not charge an unconscionable fee in connection with any matter before the Internal Revenue Service."

> "(b) *Contingent fees* — (1) Except as provided in paragraphs (b)(2), (3), and (4) of this section, a practitioner may not charge contingent fee for services rendered in connection with any matter before the Internal Revenue Service.(2) A practitioner may charge a contingent fee for services rendered in connection with the Service's examination of, or challenge to — (i) An original tax return; or (ii) An amended return or claim for refund or credit where the amended return or claim for refund or credit was filed within 120 days of the taxpayer receiving a written notice of the examination of, or a written challenge to the original tax return. (3) A practitioner may charge a contingent fee for services rendered in connection with a claim for credit or refund filed solely in connection with the determination of statutory interest or penalties assessed by the Internal Revenue Service. (4) A practitioner may charge a contingent fee for services rendered in connection with any judicial proceeding arising under the Internal Revenue Code. (c) *Definitions.* For purposes of this section — (1) *Contingent fee* is any fee that is based, in whole or in part, on whether or not a position taken on a tax return or other filing avoids challenge by the Internal Revenue Service or is sustained either by the Internal Revenue Service or in litigation. A contingent fee includes a fee that is based on a percentage of the refund reported on a return, that is based on a percentage of the taxes saved, or that otherwise depends on the specific result attained. A contingent fee also includes any fee arrangement in which the practitioner will reimburse the client for all or a portion of the client's fee in the event that a position taken on a tax return or other filing is challenged by the Internal Revenue Service or is not sustained, whether pursuant to an indemnity agreement, a guarantee, rescission rights, or any other arrangement with a similar effect. (2) *Matter before the Internal Revenue Service* includes tax planning and advice, preparing or filing or assisting in preparing or filing returns or claims for refund or credit, and all matters connected with a presentation to the Internal Revenue Service or any of its officers or employees relating to a taxpayer's rights, privileges, or liabilities under laws or regulations administered by the Internal Revenue Service. Such presentations include, but are not limited to, preparing and filing documents, corresponding and communicating with the Internal Revenue Service, rendering written advice with respect to any entity, transaction, plan or arrangement, and representing a client at conferences, hearings, and meetings. (d) *Effective/applicability date.* This section is applicable for fee arrangements entered into after March 26, 2008."

Appendix Two: ACTEC COMMENTARIES ON THE MODEL RULES OF PROFESSIONAL CONDUCT

MRPC 1.5: FEES

(a) A lawyer shall not make an agreement for, charge, or collect an unreasonable fee or an unreasonable amount for expenses. The factors to be considered in determining the reasonableness of a fee include the following:

(1) the time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly;

(2) the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer;

(3) the fee customarily charged in the locality for similar legal services;

(4) the amount involved and the results obtained;

(5) the time limitations imposed by the client or by the circumstances;

(6) the nature and length of the professional relationship with the client;

(7) the experience, reputation, and ability of the lawyer or lawyers performing the services; and

(8) whether the fee is fixed or contingent.

(b) The scope of the representation and the basis or rate of the fee and expenses for which the client will be responsible shall be communicated to the client, preferably in writing, before or within a reasonable time after commencing the representation, except when the lawyer will charge a regularly represented client on the same basis or rate. Any changes in the basis or rate of the fee or expenses shall also be communicated to the client.

(c) A fee may be contingent on the outcome of the matter for which the service is rendered, except in a matter in which a contingent fee is prohibited by paragraph (d) or other law. A contingent fee agreement shall be in a writing signed by the client and shall state the method by which the fee is to be determined, including the percentage or percentages that shall accrue to the lawyer in the event of settlement, trial or appeal; litigation and other expenses to be deducted from the recovery; and whether such expenses are to be deducted before or after the contingent fee is calculated. The agreement must clearly notify the client of any expenses for which the client will be liable whether or not the client is the prevailing party. Upon conclusion of a contingent fee matter, the lawyer shall provide the client with a written statement stating the outcome of the matter and,

if there is a recovery, showing the remittance to the client and the method of its determination.

(d) A lawyer shall not enter into an arrangement for, charge, or collect:

(1) any fee in a domestic relations matter, the payment or amount of which is contingent upon the securing of a divorce or upon the amount of alimony or support, or property settlement in lieu thereof; or

(2) a contingent fee for representing a defendant in a criminal case.

(e) A division of a fee between lawyers who are not in the same firm may be made only if:

(1) the division is in proportion to the services performed by each lawyer or each lawyer assumes joint responsibility for the representation;

(2) the client agrees to the arrangement, including the share each lawyer will receive, and the agreement is confirmed in writing; and

(3) the total fee is reasonable.

* * * * * * * * * * * * * *

ACTEC COMMENTARY ON MRPC 1.5

Basis of Fees for Trusts and Estates Services. Fees for legal services in trusts and estates matters may be established in a variety of ways provided that the fee ultimately charged is a reasonable one taking into account the factors described in MRPC 1.5(a). Fees in such matters frequently are primarily based on the hourly rates charged by the attorneys and legal assistants rendering the legal services or upon a mutually agreed upon fee determined in advance. Based on the revisions to MRPC 1.5 in 2002, unless the lawyer has regularly represented the client on the same basis or rate, the lawyer must advise the client of the basis upon which the legal fees will be charged and obtain the client's consent to the fee arrangement. As revised in 2002, the rule also requires a lawyer to inform the client, preferably in writing, before or within a reasonable time after commencing the representation, of the extent to which the client will be charged for other items, including duplicating expenses and the time of secretarial or clerical personnel. Any changes in the basis or rate of the fee or expenses shall be communicated to the client. Basing a fee for legal services solely on any single factor set forth in MRPC 1.5 is generally inappropriate unless required or allowed by the law of the applicable jurisdiction. In recent years courts in several states have, in effect, prohibited or seriously limited the use of fees based upon a percentage of the value of the estate.

Most states allow a lawyer who serves as a fiduciary and as the lawyer for the fiduciary to be compensated for work done in both capacities. However, it is inappropriate for the lawyer to receive double compensation for the same work.

Fee Paid by Person Other than Client. One person, perhaps an employer, insurer, relative, or friend, may pay the cost of providing legal services to another person. Notwithstanding the source of payment of the fee, the person for whom the services are performed is the client, whose confidences must be safeguarded and whose directions must prevail. Under MRPC 1.8(f) (Conflict of Interest: Prohibited Transactions) the lawyer may accept compensation from a person other than a client only if the client consents after consultation, there is no interference with the lawyer's independence of judgment or with the lawyer-client relationship, and the client's confidences are maintained. See ACTEC Commentary on MRPC 1.8 (Conflict of Interest: Prohibited Transactions).

No Rebates, Discounts, Commissions or Referral Fees. The lawyer should not accept any rebate, discount, commission or referral fee from a non-lawyer or a lawyer not acting in a legal capacity in connection with the representation of a client. Even with full disclosure to and consent by the client, such an arrangement involves too great a risk of overreaching by the lawyer and the potential for actual or apparent abuse. The client is generally entitled to the benefit of any economies that are achieved by the lawyer in connection with the representation. The acceptance by the lawyer of a referral fee from a non-lawyer may involve an improper conflict of interest. See MRPC 1.7 (Conflict of Interest: General Rule) and MRPC 1.8 (Conflict of Interest: Current Clients: Specific Rules). In those jurisdictions that permit referral fees between lawyers, the lawyer should comply with the requirements of local law governing such matters, including full disclosure to the client. A lawyer is generally prohibited from sharing legal fees with non-lawyers. See MRPC 5.4 (Professional Independence).

ANNOTATIONS
See Caveat to Annotations
(Limiting the Scope and Purpose of the Annotations)

Percentage, Excessive and Reasonable Fees

Statute

Florida:

Florida has enacted a comprehensive statute governing compensation of the attorney for a personal representative. Attorneys for personal representatives are entitled to “reasonable compensation” without court order. If the compensation is calculated pursuant to a statutory percentage fee schedule set forth in the statute, it is presumed to be “reasonable.” Provision is made for payment for certain “extraordinary services,” examples of which are included in the statute. Upon the

petition of any interested person the court may increase or decrease the compensation for ordinary services or award compensation for extraordinary services (if the facts and circumstances of the particular administration warrant.) The statute also includes a list of factors for the court to use in determining what is "reasonable" and gives the court discretion to give such weight to each such factor as the court determines to be appropriate. Fla. Stats. § 733.6171 (eff. July 1, 1995).

Cases

California:

Estate of Trynin, 264 Cal. Rptr. 93 (1989). The Supreme Court of California, construing California's statute governing extraordinary compensation for attorneys, here held that in an appropriate case attorneys may be compensated for legal services rendered in preparing and prosecuting a claim for prior extraordinary legal services (so-called "fees on fees"). The Court observed that the trial court retains the discretion to reduce or deny additional compensation for fee-related services if the court finds that the fees otherwise awarded the attorneys for both ordinary and extraordinary services are adequate, given the value of the estate and the nature of its assets, to fully compensate the attorneys for all services rendered.

Colorado:

Estate of Painter, 567 P.2d 820 (Colo. Ct. App. 1977), appeal after remand, 628 P.2d 124 (Colo. App. 1980), appeal after remand, 671 P.2d 1331 (Colo. Ct. App. 1983). Fee awards for personal representative and counsel based on expert testimony applying percentage method of determining fees were reversed. The Colorado legislature had repealed authorization for percentage fees and adopted a reasonable fee standard.

People v. Woodford, 81 P.3d 370 (Colo. 2003). This case is discussed in the Annotations following the ACTEC Commentary on MRPC 1.1.

Florida:

Florida Bar v. DellaDonna, 583 So. 2d 307 (Fla. 1991). A lawyer acting as personal representative was disbarred for five years for gross mismanagement of estate, conflicts of interest, and excessive fees. The court rejected the argument that discipline could not be imposed on the lawyer since the lawyer was not acting as a lawyer.

In re Estate of Platt, 586 So. 2d 328 (Fla. 1991). The court here held that it was inappropriate to determine the fees of a fiduciary and the fiduciary's lawyer solely according to a percentage of the value of the estate when governing statutes

provide a number of factors to be considered in determining fees. (See discussion of Florida statute below.)

Teague v. Estate of Hoskins, 709 So. 2d 1373 (Fla. 1998). In this case of first impression, the Supreme Court of Florida held that the attorneys' fees awarded to a widow's guardian against an estate's personal representative in the guardian's successful litigation with the personal representative over the widow's homestead, and elective share rights constituted a claim of the highest priority against the estate's assets. Two dissenting judges argued that the majority's opinion "exacts no toll from the personal representative for initiating and pursuing a fruitless claim."

Illinois:

Cripe v. Leiter, 703 N.E.2d 100 (Ill. 1998). The court here concluded that the Illinois Consumer Fraud Act did not apply to regulate the conduct of lawyers in representing clients. The matter involved a fee dispute brought on behalf of a trust beneficiary challenging the fees of the lawyer for the trustee.

In re Estate of Pfoertner, 700 N.E.2d 438 (Ill. App. 1998). An attorney filed a successful will contest on behalf of some, but not all, of the intestate heirs of a decedent. The attorney moved for an order assessing his fees and costs against each heir's intestate share of the estate to the extent such heir's interest exceeded what the heir would have received under the challenged will. The appellate court affirmed the trial court's authority and broad discretion to award fees and costs pursuant to the common fund doctrine (described as an equitable exception to the "American Rule" that each party to litigation must bear its own attorneys' fees). The appellate court nevertheless remanded the case to the trial court to make a quantum meruit award.

Indiana:

In re Matter of Gerard, 634 N.E.2d 51 (Ind. 1994). A lawyer was here suspended for one year for enforcing contingent fee agreement under which the lawyer received over $150,000 with respect to largely administrative work in locating certificates of deposit that belonged to an elderly hospitalized client. The lawyer's conduct involved fraud and charging a clearly excessive fee.

Maine:

In re Estate of Davis, 509 A.2d 1175 (Me. 1986). The practice of basing a lawyer's fee on a percentage of the estate being handled should carry little or no weight in determining a reasonable fee.

Massachusetts:

In re Matter of Tobin, 628 N.E.2d 1273 (Mass. 1994). A lawyer was suspended for 18 months for fraudulently inducing a client unnecessarily to probate an estate, all of the assets of which passed to her as surviving joint tenant, for charging excessive fees based on bar association's former fee schedule, and misrepresenting facts to probate court.

Missouri:

Estate of Perry, 978 S.W.2d 28 (Mo. Ct. App. 1998). This was an action brought by the decedent's son by a prior marriage to remove the decedent's surviving husband as personal representative and for an accounting. The trial court declined to remove the husband as personal representative but entered a money judgment against him for certain claims made on jointly secured obligations. The court also adjudicated the husband's request for an allowance of exempt property. The appellate court, reversing the trial court on the issue of attorneys' fees, held that the son was entitled to a fee award since the estate had benefited from the judgment against the husband and the fact that the son was not successful in his removal action was not determinative on the attorneys' fees issue.

Montana:

Hauck v. Seright, 964 P.2d 749 (Mont. 1998). In this will contest action where the decedent had executed two wills within four days, counsel for the personal representative was unsuccessful in defending the validity of the second will. Nevertheless, in admitting the first will to probate, the trial court awarded attorneys' fees to the personal representative under the second will. On appeal by the contestant, the Supreme Court of Montana, construing Montana's statute, held that a personal representative is entitled to recover fees from an estate when he defends or prosecutes a proceeding in good faith, whether successful or not.

New York:

In re Estate of Freeman, 311 N.E.2d 480 (N.Y. 1974). This case lists the factors to be taken into account by a surrogate judge in determining the fees of counsel in estate matters, which include the amount involved, results obtained and the skill and time required.

North Carolina:

Estate of Smith v. Underwood, 487 S.E.2d 807 (N.C. Ct. App. 1997). The appellate court here upheld a trial court's award in favor of the beneficiaries of a trust who had sued the attorney/trustee (together with an accountant and the accountant's firm) for breach of fiduciary duty and professional negligence. The attorney had filed an initial trust accounting and obtained approval of his fees and commissions in 1955, the year after the decedent died, but from 1956 until 1991 filed no annual accountings and did not obtain the probate court's approval of the

fees and commissions that he collected. The award against the attorney included statutory double damages allowed under state law when an attorney has committed a fraudulent practice.

Ohio:

Estate of Haller, 689 N.E.2d 612 (Ohio Ct. App. 1996). An attorney/administrator sought fees for his firm's representation of himself in an estate administration. Introducing no expert testimony, the attorney did support his application with a 67-page itemization of his services. In affirming the trial court's approval of the entire fee requested (approximately $39,000), the court observed that, "[w]hile the better practice may be to introduce expert testimony as to the reasonableness of the fees, a probate court judge is nevertheless qualified to make a determination, upon evidence, of the reasonable attorney fees to be paid from the estate without the necessity of expert testimony." 689 N.E.2d at 615.

Oregon:

In re Stauffer, 956 P.2d 967 (Or. 1998). While representing the personal representative of an estate, lawyer took action to recover assets for the estate in order to collect an attorney fee the lawyer claimed was owed to him by the decedent, to the detriment of the personal representative (title to the asset was in the name of the personal representative). The lawyer failed to apprise the personal representative client of his conflict of interest and failed to obtain consent. The lawyer was suspended from practice for two years.

Pennsylvania:

In re Trust Estate of LaRocca, 246 A.2d 337 (Pa. 1968). Estate and trust counsel are provided guidance with respect to the setting of fees for their services. Factors include the amount of work, difficulty of the problems involved, amount of money or value of the property in question and degree of responsibility incurred.

In re Estate of Preston, 560 A.2d 160, 165 (Pa. Super. 1989). The compensation allowed by the lower court was reduced: "The lower court's use of the Attorney General's [percentage] schedule for calculating fees is clearly improper and must cease."

In re Estate of Sonovick, 541 A.2d 374, 376 (Pa. Super. 1988). In this case the compensation of the lawyer and the fiduciary were reduced. The court stated that: "Thus, the fiduciary's entitlement to compensation should be based upon actual services rendered and not upon some arbitrary formula."

South Dakota:

Estate of O'Keefe, 583 N.W.2d 138 (S.D. 1998). In this action decedent's two nephews, who had acted as fiduciaries in taking care of his property, were found liable for both compensatory and punitive damages for breach of their fiduciary duties, conversion, fraud and deceit. The plaintiff, who, with the nephews, was the only other beneficiary of the estate, sought an order to prevent the two nephews from receiving any part of the punitive damages as estate beneficiaries and requested the court to assess the estate's attorneys' fees incurred in the prior litigation against the nephews' distributive shares. After the trial court so ruled, the Supreme Court of South Dakota, interpreting that state's version of the Uniform Probate Code, upheld the trial court's order regarding the punitive damages but reversed the award of attorneys' fees, finding that such fees could only be awarded by contract or when explicitly authorized by statute.

Washington:

Bennett v. Ruegg, 949 P.2d 810 (Wash. Ct. App. 1999). In this case the court, interpreting statutory law, found that the state's broadly drawn statute permitting attorneys' fees to be awarded in a probate proceeding "as justice may require" applies to permit the personal representative's recovery of attorneys' fees from a beneficiary who has unsuccessfully sought removal of the personal representative.

Estate of Morris, 949 P.2d 401 (Wash. Ct. App. 1998). A corporate personal representative personally incurred attorneys' fees in successfully defending a suit for removal brought by the beneficiaries of two estates. Its request for reimbursement from the estates was disallowed. The appellate court affirmed the trial court's decision denying any fees on the grounds that the bank's conduct had conferred no "substantial benefit" on the estate as required by the applicable Washington statute.

Ethics Opinions

ABA:

ABA Formal Op. 93-379 (1993). This opinion articulates more particularly the duties of a lawyer to disclose the basis of fees and charges as provided in MRPC 1.5. In addition, in matters where the client has agreed to have the fee determined with reference to the time expended by the lawyer, a lawyer may not bill more time than she actually spends on a matter, except to the extent that she rounds up to minimum time periods (such as one-quarter or one-tenth of an hour). A lawyer may not charge a client for overhead expenses generally associated with properly maintaining, staffing and equipping an office; however, the lawyer may recoup expenses reasonably incurred in connection with the client's matter for services provided in house, such as photocopying, long distance telephone calls, computer research, special deliveries, secretarial overtime, and other similar services, so long as the charge reasonably reflects the lawyer's actual cost for the services rendered. A lawyer may not charge a client more than her disbursements for

services provided by third parties like court reporters, travel agents or expert witnesses, except to the extent that the lawyer incurs costs additional to the direct costs of the third-party services.

Arizona:

Ariz. Op. No. 94-09 (1994). (For a more detailed summary see the Annotations following the ACTEC Commentary on MRPC 1.6.) A lawyer who believes that the fees charged by another lawyer in connection with the administration of an estate are clearly excessive has a duty to report the other lawyer's violation of the rules to the state bar.

Connecticut:

Op. 00-22 (2000). Attorney had previously represented a corporate fiduciary on unrelated estate matters. No written fee agreement is required for lawyer's representation of same corporate executor of a new estate.

Oregon:

Op. No. 2003-177 (2003). A lawyer does not charge or collect an illegal fee in a probate case if the lawyer requests and receives an initial payment or interim payments from the personal representative's own funds. The personal representative client may later seek court approval for reimbursement from the estate assets of some or all of the money advanced for legal fees. Lawyer who is serving as a personal representative of an estate must obtain court approval before withdrawing any compensation for services.

Contingent Fee Agreements

Cases

Indiana:

In re Matter of Gerard, 634 N.E.2d 51 (Ind. 1994). This case, summarized above, involved a contingent fee agreement that resulted in an excessive fee. The "enormity of Respondent's fee in relation to the amount of service rendered is fraudulent." 634 N.E.2d at 53.

Oklahoma:

Estate of Hughes, 90 P.3d 1000 (Ok. 2004). The court has authority to examine a written contract between attorney and personal representative before approving attorney's fee as an expense. The contract here was found ambiguous because it was unclear what portion of a contingent fee was for representation of the

personal representative in estate matters and what portion was for representing her individually.

Ethics Opinions

Missouri:

Informal Advisory Op. 20000090 (2000). Attorney who represents the children of a decedent on a contingent fee basis in an attempt to secure their portion of an intestate estate may later represent them in a suit involving other family members under a representation contract with terms providing for a small retainer up front and a later contingency fee basis. The fee assessed at the conclusion of the representation must be assessed for its reasonableness.

New York:

New York City Bar Formal Op. 1993-2 (1993). This opinion concludes that a lawyer may enter into a contingent fee contract with a client in connection with a dispute involving a will. The lawyer may not enter into a joint fee agreement among the lawyer, clients and a private investigator under which the investigator would receive a contingent fee.

Payment of Fee by Person Other than Client

Ethics Opinion

ABA:

ABA Inf. Op. 86-1517 (1986). A lawyer may bill a corporation for personal services provided to the corporation's shareholder, director, officer or employee, if the corporation and the attorney's personal client agree and the bill identifies the services as personal services and the amount of the charge for the services.

Reduced Rates for Employees of Corporate Client

Ethics Opinion

Illinois:

Ill. Op. 92-8 (1993). This opinion approved an arrangement under which a law firm that represents a corporation would represent corporate employees at reduced rates in return for the corporate president's recommendation that the employees use the law firm's services. However, the opinion observes that the promise of "reduced" rates may be misleading unless the fees charged are less than the firm's normal and customary fees. The same may be true unless the fees charged are less than the fees generally charged in the locality for similar legal services. There is

also a substantial risk of a conflict of interest between the employees and the employer.

Rebates, Discounts, Commissions or Referral Fees

Cases

Kansas:

In re Matter of Farmer, 747 P.2d 97 (Kan. 1987). It is improper for a lawyer to negotiate discounts on a client's medical expenses that were payable from personal injury settlement, charge the client for the full amount of the claims without disclosure, and retain the difference as an additional fee.

New York:

In re Estate of Clarke, 188 N.E.2d 128 (N.Y. 1962). The lawyer for a personal representative who entered into an agreement with a real estate broker to split the broker's fee on the sale of real property belonging to the estate had a conflict of interest that required denial of all of the lawyer's fees.

Ethics Opinions

ABA:

ABA Formal Op. 93-379 (1993). This opinion covers a number of subjects relating to attorneys' fees and disbursements. It states, in part, that, "if a lawyer receives a discounted rate from a third-party provider, it would be improper if she did not pass along the benefit of the discount to her client rather than charge the client the full rate and reserve the profit to herself. Clients quite properly could view these practices as an attempt to create additional undisclosed profit centers when the client had been told he would be billed for disbursements."

California:

L.A. County Op. 443 (1987). A lawyer may not accept payments from a physician to whom the lawyer refers clients for medical treatment.

San Diego Op. 1989-2 (1989). A lawyer for the executor of a decedent's estate may not ethically demand payment of a referral fee by a real estate broker as a condition to retention of the broker. "Disclosure and consent by the client (per Rule 3-300) does not cure the abuse."

New Jersey:

N.J. Op. 514 (1983). This opinion is summarized in the Annotations following the ACTEC Commentary on MRPC 1.7.

New York:

N.Y. Formal Op. 610 (1990). This opinion is summarized in the Annotations following the ACTEC Commentary on MRPC 1.7.

North Carolina:

99 Formal Ethics Opinion 1 (1999). A lawyer may not accept a referral fee or solicitor's fee for referring a client to an investment advisor.

Pennsylvania:

Op. 2003-16 (2003). Although it is conceivable that an estate planning attorney could be ethically permitted to sell life insurance, securities, or other financial products to his or her client as part of the estate planning process, it is highly unlikely that the lawyer could satisfy MRPCs 1.7(b), 1.8(a) and 1.8(f).

Op. 2000-100 (2000). Lawyers may accept referral fees from insurance agents, investment advisors, or other persons who provide products or services to the lawyer's client subject to MRPCs 1.7(b) and 1.8(f).

Texas:

Op. 536 (2001). A lawyer may not receive referral or solicitation fees for referring a client to an investment adviser while the lawyer's client continues to receive services from the investment adviser because the client would be adversely affected by the lawyer's own financial interests and his obligations to the investment adviser.

Utah:

Op. No. 01-04 (2001). Charging an annual fee for estate planning or asset protection services based on a percentage of the value of the client's assets would be ethical "only in extraordinary circumstances." The opinion does not suggest any circumstances where the arrangement would be appropriate.

Op. No. 99-07 (1999). It was not "per se unethical" for a lawyer to refer a client to a financial advisor and to receive a referral fee, but the lawyer "has a heavy burden to insure compliance with applicable ethical rules." The opinion noted that several states hold, as do the Commentaries, that the practice is "per se unethical."

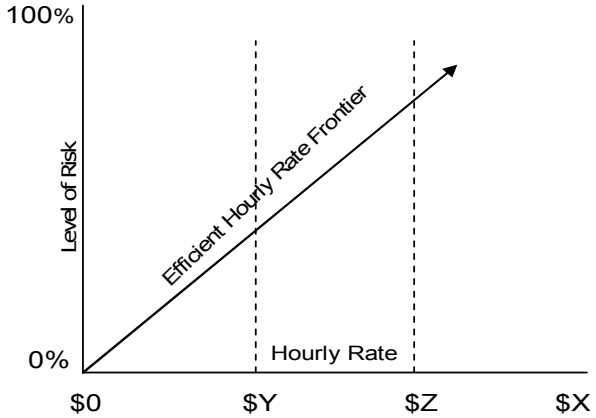
Op. No. 146A (1995). This opinion held that a lawyer may sell life insurance products to an existing client if the lawyer complies with MRPC 1.8(a).

Virginia:

Op. 1754 (2001). It is not unethical for an attorney and an insurance agent to share the commission generated by the purchase of a survivorship life insurance policy to fund client's irrevocable life insurance trust provided full and adequate disclosure is made to the client.

Selected Power Point Slides

The Hypothetical Hourly Rate in the Context of RISK; Why the Hourly Rate can be Fatal to One's Practice



Note: $Y and $Z are stable rates independent of risk

(1) What action items does a practitioner take based on this knowledge? (Pricing should be along diagonal line based on risk)
(2) If practitioners take such action, what happens in the long run to vertical $Y and $Z lines? (They become diagonal)
(3) Will not happen in practice because risk is not built into the hourly structure.
(4) Note: Risk is not necessarily tied to complexity; *e.g.,* difficulty of client, sensitivity of matter, time urgencies, level of inattention, fee constraints can all add to level of risk. Reviewing another firm's estate planning documents for a "second opinion" is fraught with risk.
(5) If pricing cannot take into account risk, what actions should we take? (focus on not taking matter, or know that you are getting paid less than risk you are taking, or increase effort to decrease risk)

130586

7-31 PPT

Morgan/Foonberg

Survey of legal clients:

A. Only 6 % listed "results achieved by the lawyer" as most important element.

B. 47 % listed "effort" as most important element in accepting a fee

Source: "How to draft bill clients rush to pay" ABA Law Practice Management Section

→what we learn from this exercise

130586 7-5 PPT