UNDERSTANDING CONTINGENCY FEE AGREEMENTS

By Franci Leppan

The subject of contingency fee agreements often elicits a negative response from both the public and media. In the past few years, a number of controversial matters have received significant attention in the press, probing the purpose, basis and ethics pertaining to contingency fee agreements. The mis-conception that members of the public are "ripped off" by attorneys with questionable ethics practices are often the premise of these controversial reports.

AN OVERVIEW OF CONTINGENCY FEE AGREEMENTS

Contingency fee agreements are regulated by the Contingency Fees Act 66 of 1997 (the Act). In terms of the Act, "normal fees" are those fees normally charged by the attorney to provide legal services and contingency fees are fixed fees charged by the attorney for legal services provided to a client. In terms of common law, contingency fee agreements are held to be unlawful. However, the Act allows for the legitimising of such agreements, subject to strict controls and clearly set out criteria.

Contingency fee agreements allow individuals without the necessary financial means to self-fund certain types of complicated and specialised litigation by entering into litigation on an outcome basis. The agreement entered into entitles the attorney to a portion of the capital amount awarded to the client, contingent upon the outcome of the case only – "no win, no fees". For this reason, these agreements are often referred to as outcome-based agreements.

A number of highly specialised attorneys, particularly in the fields of personal injury and medical malpractice, regularly enter into these types of agreements. The expertise of the attorney, coupled with the inherent risk of litigation makes this a potentially high-risk endeavour. Such specialist attorneys often engage with highly qualified experts such as specialist doctors and fund these experts' costs at their own risk in furtherance of the client's claim.

FORMAL REQUIREMENTS FOR COMPLIANCE

Section 3 of the Act sets out the formal criteria to be fulfilled when entering into a valid and enforceable contingence fee agreement and requires that such agreement:

- always be in writing[1] ; and
- be signed by both the attorney and its client[2]

Section 3(3) sets out the proceedings to which the agreement relates, as well as the necessary legal averments pertaining to the rights of the client, the definition of success in the circumstances (including partial success), calculation of amounts payable and the client's right to cancel the agreement.

Section 4 of the Act deals with settlement offers and the requirements to be met in these circumstances. This section requires that if a client accepts a settlement proposal, an affidavit has to be filed with the court. If the matter is not presented before a court, such affidavit is to be filed with the Law Society or relevant regulatory body.

Strict compliance with the Act is essential and an agreement which falls foul of such compliance will be held to be invalid.

[1] Section 3(1) of the Act
[2] Section 3 (2) of the Act

A MYTH – DEBUNKED

A number of attorneys operate under the misapprehension that an attorney is automatically entitled to 25% of the client's capital claim. This could not be further from the truth.

An attorney who enters into a contingency fee agreement needs to fulfil not only all the criteria as set out above, but also comply with the Act when calculating the fees that they are entitled to. An incentive fee, or a so-called "success fee" to compensate the attorney for the risk involved in taking on the matter contingent upon its outcome and concluding it successfully, is condoned by the Act.

An attorney has to draft a detailed bill of costs at the conclusion of a matter, setting out all relevant fees claimed. Such fees, duly quantified, may then be doubled (normal fee plus 100%) to provide for the "success fee".

It is imperative to note that an attorney would only be entitled to claim EITHER 25% of the claim amount received, OR its normal fees plus 100%, whichever is the LESSER. An automatic entitlement to 25% of the claim amount is prohibited by the Act and can't be enforced.

AUDITING CONSIDERATIONS

Attorneys may not simply agree with clients to charge contingency fees. There are strict requirements set out in the Act that must be followed before an attorney can charge contingency fees. The existence of contingency fee agreements may give rise to specific fraud risk factors that the auditor should be alert to, including attorneys charging fees in excess of what is permitted in terms of the Act.

When dealing with audits of attorney trust accounts which include matters involving contingency fee agreements, a close scrutiny of any purported agreement is vital and ensuring that the calculation of fees is in strict compliance with the Act is essential.

It is common practice for an attorney to charge an hourly fee rate. The fee is often negotiated with the client and agreed upon upfront in an engagement letter. However, many small practitioners do not have engagement letters and negotiate the fee after the matter has been settled. In line with the requirement of the Act, which allows the attorney to charge the lower of double the normal fee or the 25% of the capital award, the auditor may encounter practical issues in auditing contingency fee arrangements where the attorney has not kept time records of the hours spent on the case.

An affidavit, setting out the exact calculation of fees debited, to be deposed by an attorney, should be required in circumstances where there appears to be non-compliance with the Act. The Act prohibits entering into contingency fee agreements at the conclusion of a successful matter in an attempt to justify higher fees.

IN CONCLUSION

Contingency fee agreements are prevalent in Road Accident Fund cases as well as medical negligent claims. Contingency fee agreements are tightly regulated agreements and the audit of attorney trust accounts that include matters involving such agreements requires specialised knowledge. Auditors are cautioned to exercise the appropriate level of professional scepticism and approach the audit of legal cases involving contingency fees with the necessary competence and due care.