CONTINGENCY FEES

THE POSITION IN HONG KONG, THE ARGUMENTS, AND THE COMPARISON WITH ENGLAND

ANDREW JEFFRIES
ALLEN & OVERY
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1. Control of Solicitors' Remuneration in Hong Kong

Legal Practitioners Ordinance

1.1 Fees chargeable by solicitors in Hong Kong are subject to a number of controls. These come principally from Part VI of the Legal Practitioners Ordinance (Cap.159) (LPO), and the Hong Kong Solicitors' Guide to Professional Conduct, particularly Chapter 4. Other regulations in the Solicitors Practice Rules, or in relation to Legal Aid, may also apply.

1.2 The permissible arrangements for solicitors' costs differ between contentious and non-contentious business. There are also differences between what is permissible in civil contentious matters as against criminal contentious matters.

1.3 The principle controls relevant to this topic are as follows (this is not an exhaustive list of all controls):

1.4 Section 56 of the LPO sets out the scope for agreements for remuneration in non-contentious business. It is possible, by an agreement in writing, signed by the client, to agree to remuneration on any basis (subject to other overriding principles, such as solicitors must not overcharge their clients). This means that for non-contentious business, remuneration may be by way of fixed amount, commission or percentage, or time spent at hourly rates, or otherwise. Provided the agreement is in writing and signed, it may be sued on like any other contract (again subject to other overriding rules explained below). The client has the right to seek a taxation of the solicitors' costs, and if the client objects to the costs as unfair or unreasonable, and the Taxing Officer agrees, any order as to costs may be made, including overruling the agreement.

1.5 Sections 58-60 set out provisions in relation to remuneration of solicitors for contentious business. Section 58 permits the making of a written agreement with a client as to remuneration for contentious business, either on the basis of a gross sum or by salary - hourly rates. This may be at a greater or lesser rate than the solicitor would ordinarily charge. Section 58’s flexibility as to remuneration in contentious business is glaringly less than that in Section 56 for non-contentious business, and this forms the focus of the debate on contingency fees.

1.6 Suing on a contentious business fee agreement is also not as straight-forward as in the case of a non-contentious agreement: Section 60 provides that no action may be brought upon a Section 58 agreement, although the court has power to review, enforce or set aside the agreement on the application [of the solicitor]. The court may enforce the costs agreement if it is of the opinion that it is in all respects fair and reasonable. By Section 62, this court review supersedes the normal provision for taxation.

1.7 These sections deal with situations where there is an agreement with the respect to costs. Where there is no agreement at all, or any agreement does not fulfil the requirements for being in writing, then a solicitor will be entitled to reasonable remuneration. What is reasonable will depend on each case, and what, if anything, was discussed orally or in writing between the solicitor and the client. Nevertheless, the specific provisions above relating to costs agreements will not apply.

1.8 Sections 64-71 set out general provisions regarding remuneration of solicitors, of which most importantly Section 64(1)(b) provides for the invalidity of any agreement which stipulates that a solicitor retained or employed to prosecute any action, suit or other contentious proceeding will be paid only in the event of success in their action suit or proceeding.

1.9 By Section 66, an action on the solicitor's bill may not be commenced until one month after the bill has been delivered. Provision is set out for the formalities of signature and delivery of bills. Section 67 onwards deals with taxations.

Guide to Professional Conduct

1.10 Chapter 4 of the Hong Kong Solicitors' Guide to Professional Conduct deals with fees, covering such general matters as information to clients about costs, interim bills, payments on account and the form and contents of bills. Relevant to the present discussion are the following:

1.11 Principle 4.02 prescribes that when fees have been agreed with the client, the solicitor must promptly provide the client with a written record of the agreement. When no fee has been agreed or estimate given, a solicitor must still tell his client how his fees will be calculated (4.03) and must give on an appropriately regular basis, the approximate amount of costs to date (4.06). Special rules apply in criminal cases (see Solicitors Practice Rules 5D).

1.12 4.12 contains the overriding principle that a solicitor must not overcharge his client. This is also covered by Solicitors' Costs Rules 5. If an agreement is made between the solicitor and the client which is found to be wholly unreasonable, disciplinary action may be taken against the solicitor. This cannot be overridden by a Section 56 or 58 agreement. See also ***Stikeman Elliott -v- Wong Ming Yuen*** [1984] HKLR 191.

1.13 4.14 contains provisions in relation to a Hong Kong solicitor assuming liability for overseas lawyers instructed by him personally. However, a consequence of this is that a Hong Kong solicitor may agree the fees of an overseas lawyer to be on a contingent basis, even in circumstances where that would be unlawful in Hong Kong, provided it is permitted within the jurisdiction of that overseas lawyer. For example, therefore, a Hong Kong solicitor may engage US lawyers to pursue litigation in the US on any fee arrangement permissible in the US.

1.14 Finally, principle 4.16 expands the general ban on contingency fee arrangements:

A solicitor may not enter into a contingency fee arrangement for acting in contentious proceedings: see Section 64 of the LPO. A contingency fee arrangement is any arrangement whereby a solicitor is to be rewarded only in the event of success in litigation by the payment of any sum (whether fixed, or calculated either as a percentage of the proceeds or otherwise). This is so, even if the agreement further stipulates a minimum fee in any case, win or lose.

2. Contingency Fee Arrangements

2.1 Contingency fee arrangements are often treated generically as all one class, but the types of arrangement can be divided into three sub categories: A “speculative fee”, permitted in Scotland, where a solicitor does not charge, but receives his normal fee if the case is successful. This gives no incentive to the solicitors’ risk taking. A “contingency fee”, permitted in the US, where the lawyer takes a share of the compensation, although this may have no relationship to the risk taken or work done. A “conditional fee”, permitted in England and Australia, where the solicitor is paid an uplift or additional amount if the case is successful, usually as a percentage of normal fees, but sometimes a percentage of the compensation won.

2.2 In Hong Kong, contingency fee arrangements (i.e. covering all three types in 2.1 above) in contentious business are still prohibited. A contingency fee arrangement is said to be unlawful

on grounds of public policy. To enter into a contingency fee arrangement is also professionally improper. See for example *re A Solicitor* [1989] Civil Appeal 150 of 1988.

2.3 Section 64(1)(b) of the LPO sets out the general prohibition on contingency fees, but is amplified by principle 4.16 quoted above. The effect of this is not only to outlaw simple no win or no fee agreements, but also to outlaw arrangements whereby a solicitor's remuneration is dependent on success in the litigation, whether at trial or by settlement, and uplift agreements where there is some fixed or normal fee element, enhanced in the event of success.

2.4 Broadly the same principles also apply to counsel and their fees. See in particular paragraphs 124 and 60(A) of the Bar Code.

2.5 The prohibition is, however, relatively narrow and it should be observed that contingency or success related fees are permitted in non-contentious business. The prohibition only extends to fee agreements which involve proceedings. It is therefore lawful for a solicitor to enter into an agreement on a commission or success basis to recover sums due to a client, provided the costs agreement is clearly limited from the outset to debt recovery without involving the institution of proceedings. As noted above, conditional fee arrangements are permissible between a Hong Kong solicitor and an overseas lawyer, provided they are valid in the jurisdiction of that overseas lawyer.

2.6 It is finally interesting to note that a form of conditional fee is built into the Supplementary Legal Aid scheme. In claims falling within this scheme, a legally aided plaintiff who is successful, pays back a percentage of the compensation awarded into the Fund. Conversely, of course, if the case is lost, the Fund will pay all the legal costs.

2.7 Contingency fee arrangements were reviewed in the Consultation Paper on Legal Services in 1995. That paper was written in the context of reforms on conditional fees introduced at that time in England. The consultation paper rehearsed the fairly well worn arguments against contingency fees, a number of counter-arguments, and finally came down on the side of introducing reform to the restriction on contentious business contingency fees along the lines of those introduced in England. This has not been done, although the Law Society and others continue to look at the issue.

2.8 The arguments against centre on issues of solicitors losing their professional judgment and independence, or being over-compensated. Arguments may be summarised as follows:

(a) Lawyers may be tempted to advise a client to accept a lower amount than the client could get through the courts in order to avoid the risk of losing the case and the contingency fee. The lawyer takes a financial stake in the claim – a form of 'maintenance' which would otherwise be unlawful.

(b) Clients may be required to pay their lawyers a disproportionate amount of any sums recovered. The uplift to fees on success can swallow the damages. In some systems (e.g. England), losing parties are made to pay not only the winning party's ordinary costs, but also the uplift or contingency element. This can be seen as harsh to oppressive to losing/paying parties.

(c) Wholly unmeritorious actions, or "nuisance suits", may be brought by lawyers in the hope that defendants would settle them to avoid the trouble and expense of going to court.

(d) On the other hand, with a strong claim, the lawyer is motivated by success fees to fight on through trial rather than to settle for a reasonable sum which would satisfy the client.

(e) Lawyers may be tempted to try to enhance their clients' chances of success, perhaps by coaching witnesses or withholding inconvenient evidence or other misconduct.

(f) Lawyers start to judge whether a step in an action is appropriate or not by the fee economics rather than the legal issues or client's interests.

(g) The availability of contingency fees encourages pushy advertising and ambulance chasing.

2.9 Counter-arguments may be summarised thus:

(a) There will be no flood of speculative or unmeritorious claims. Lawyers only take the 'contingency risk' in strong cases. 'Try-on' claims will still be made from time to time regardless of the fee arrangement.

(b) The loser pays principle (generally absent in the U.S.) is a good deterrent to bringing bad claims.

(c) Lawyers already face and address these potential conflicts, although perhaps less so: with a strong case the lawyer wants to fight on for more fees and a profile winning reported decision, whilst the client wants a modest settlement?

(d) There is in fact no real evidence of conflict problems being more frequent because of contingency arrangements in countries which allow them. Rigorous conduct rules can be implemented.

(e) The exploitation issues are addressed by having full and proper information for the client, and capping the success element, together perhaps with the "checks and balances" to fees provided by the Court through taxation. Costs outweighing the amount at stake is of course not a new issue or one in any sense unique to contingency fee situations.

(f) Lawyers are motivated to spend costs wisely, and to be more dedicated to the matter.

(g) There is no real evidence of improper advertising or ambulance chasing. Again, conduct codes can deal with this.

(h) The English rules and Consultation Paper (and also the U.S. system) exclude criminal and matrimonial matters from contingency arrangements, where the risks of conflict are thought to be too great.

2.10 What are the motivations for change?:

(a) Increased access to justice for plaintiffs who are outside legal aid (financially or because of the nature of their claim), but would find it difficult to fund a claim. Better defence for defendants opposing a weak claim by a wealthy and oppressive plaintiff.

(b) Incentivisation for pro-bono cases.

(c) Save on the legal aid budget.

(d) Gives lawyers flexibility in fee arrangements and shares the risk burden.

(e) Gives work to lawyers they would not otherwise have.

(f) Competes with the debt collectors.

(g) Hong Kong stands largely alone against the contingency fee.

2.11 The real underlying issue here is the accessibility of the justice system to the public user – if the cost of litigation stifles claims and defences, the public is not being served by the system. That is a much wider issue than just contingency fees, but such fee arrangements are said to be one way to help correct the problem. There are, however, alternative or additional measures, each with their own pros and cons (the cons mostly relating to cost), which might be considered as part of the overall solution, since contingency fees alone will not cover all situations of inaccessibility. They include:

- Legal costs insurance
- Broader legal aid
- No fault systems of injury compensation
- Lawyers working pro-bono, free advice centres
- Controls on legal fees – scales and caps etc
- Reform of the court procedure and streamlining the litigation process

3. The Regime in England

3.1 The position now in Hong Kong is as England was before 1995. Section 58 of the Courts and Legal Services Act 1990 introduced a system of conditional fees in England. In summary, it is now permitted in England (subject to various criteria) for a solicitor act in contentious business on the basis that if the action is unsuccessful he receives no fee, but if successful he receives his normal fee, or his normal fee with an uplift. The system was brought into effect by the Conditional Fee Agreements Order 1995, and substantially overhauled in 2000.

Conditional fees are now generally permissible except in criminal and matrimonial proceedings.

3.2 Under the Access to Justice Act 1999 and the Conditional Fee Agreements Regulations 2000, a conditional fee arrangement (CFA) may now be entered into in four main ways:

- No win no fee, success fee if win
- No win reduced fee, success fee if win
- Normal fee if win, no fee if lose
- Normal fee if win, reduced fee if lose

3.3 Reference also needs to be made to the Civil Procedure Rules (Parts 43-48) and practice directions on CFAs. Information is available from the UK Law Society website, including a sample CFA (www.lawsociety.org.uk).

3.4 A detailed review of the Regulations is beyond this note, but suffice it to say they are complex and detailed, and must be rigorously followed. The essence is that full and frank information on all the terms and effects of the CFA must be explained to the client orally and largely also in writing. This must include the basis and calculation of any success fee, and when it is or is not payable. What happens if the case settles at what stage, and the effect of inter-parties taxation on liability for a success fee. When there is a liability for costs of any party or lawyer and how this is funded. Legal Aid options if any and insurance. The client must sign.

3.5 The amount of success fee uplift is capped by regulations at 100%, but such an uplift is the exception. On taxation after trial, the court looks at the success fee against the nature of the matter, the work done and the risk borne by the solicitor, and may reduce it. In that case, the client's liability is normally reduced correspondingly. If the case settles, the success fee is also limited to the costs deal done with the opponent, unless part of the settlement is a costs assessment by the Court. The basis for selecting a particular success uplift must be explained to the client.

3.6 Insurance by the CFA plaintiff is normal to cover the potential to have to pay the other side if the case is lost. Insurance can be taken out to cover both side's costs in the event the defendant wins and it is not a no win no fee deal, or the defendant loses but can't pay. Insurers normally demand a good counsel's opinion.

3.7 The other side must be told if a CFA is in place, and the success percentage, but not all the terms. The privilege waiver issue needs to be explained to the client. The 'success fee' should be divided where relevant into compensation for funding the case and only being paid at the end – the cashflow cost, not recoverable from the other side, and the pure success element – the reward for risk taking. That success fee is recoverable on taxation from a losing party, as is the insurance premium, together called an 'additional liability', subject to taxation.

4. Some Issues and Experience in England

4.1 The scheme initially applied only to a limited range of litigation – mainly personal injury and insolvency. It was soon extended, and now covers all claims except criminal and matrimonial. This is still early days – the scheme underwent a major overhaul only in 2001, and is still being fine-tuned. It has been used extensively for personal injury claims, and is almost the norm. Cut backs in the availability of Legal Aid, and lowering of the financial ineligibility threshold have certainly pushed this along. Boutique PI firms now advertise for claimants on a pay us nothing basis, and this has led to more claims being at least reviewed, but there does not seem to have been an explosion of ambulance chasing.

4.2 CFA's have also been used widely for libel claims, where there is no Legal aid. They are used in cases where the solicitor would otherwise have acted pro bono and recovered nothing, but can now effectively act without charge but recover costs from a losing party. Almost all CFAs are for poor plaintiffs, and are accompanied by insurance against having to pay the other side. CFAs are being used in relatively small strong and simple/easily assessed claims. They are not used in commercial actions, or much by commercial firms, nor in large or complex matters.

4.3 There has not, apparently, been much issue over the classic fears surrounding CFAs as set out above. There has apparently been little complaint that lawyers are suddenly less professional or acting on improper motives, nor of an explosion in speculative litigation. Some lawyers confess to being more cost conscious in pursuing claims, although this may also be a consequence of the wider shake up of costs in litigation and court procedure.

4.4 There has been much debate about the proper level of success fee, and some evidence of initial solicitor over-enthusiasm. The 100% success fee cap was the subject of fierce debate,

and only passed through Parliament by a narrow margin. Taxing Masters and courts have cut back the level of success fees put in place by solicitors. See for example *Callery –v- Gray (no. 1)* [2001] 1 WLR 2112 and *Halloran –v- Delaney* Unrep. 6.9.2002. It is now being suggested that the success fee should be staged normally, to be low in the event of an early settlement, but higher later on, better to reflect the risk taken by the solicitor.

4.5 The liability of defendants for success fees and insurance premiums was introduced in the 2000/2001 reform of the regulations. This has caused some complaint by defence lawyers and traditional defence clients such as insurers.

4.6 However, the real problem with the scheme has not been the ethical issues, but the complexity and intricate details of the regulations for CFAs, and the need to get every detail agreed properly with the client before the agreement is valid. See for example, *Woods –v- Chaleef* Unrep 2002. Failure can mean no recovery for the solicitor from either the losing opponent or the client. This is being used successfully and aggressively by defendants to avoid liability. The CFA itself can take up much time, and errors are disasterous.

4.7 There is evidence of teething problems with firm management and cashflow – disbursements and costs on account. Front-loading can be very high.

4.8 In this context, the changes can probably be judged a success: problems with the proper level of success fee can be ironed out with new regulations and judicial precedent, as can problems with the details of getting the CFA right. If there had been real signs of the feared ethical problems, that would have been much harder to resolve.

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