

Outside Counsel

Expert Analysis

Retaining Lien: a Useful Tool In Uncertain Economic Times

In past economic downturns, law firms have typically been immune and held their own from a financial perspective. The recent recession, however, has had a devastating effect on the business aspect of the legal profession. In the past, many firms leaned on shareholder disputes, general litigation, and bankruptcy filings to get them through the tough times. Today, many firms are finding that business people are less inclined to incur the costs and expenses of litigation, and even angry shareholders are thinking twice before incurring the high costs of litigation.

In the bankruptcy arena, cases that used to linger for months—or even years—are quickly turning into sales of substantially all of the debtor's assets or straightforward liquidations. As a result, thousands of attorneys have been laid off by some of the biggest and most profitable firms in the country. In addition, firms have de-equitized partners, laid off contract partners, cut salaries, downsized support staff, and cancelled on-campus interviews. Many law firms are rethinking their business models altogether. Some legal analysts are predicting that the legal market will not pick up until 2011, at the earliest.

It is extremely important, therefore, for firms to maximize collections from current clients. In the past, law firms used to be in a position to demand retainers sufficient to cover any deficiency if the client either



By
**Leo V.
Leyva**



And
**Jed M.
Weiss**

refused or was unable to pay. The current financial crisis has negatively impacted many clients' ability to provide a sufficient retainer at the outset of the litigation. Firms that used to turn away business because of an insufficient retainer are finding that they have no choice but to accept the business in hopes that the client can pay the bills as the services are provided.

Courts will take it upon themselves to ensure the reasonableness of fees when fixating retaining liens.

This article discusses the rights and remedies available to law firms when a client does not pay for services rendered, specifically, the availability of retaining liens, and the effect of the recent Southern District of New York court decision in *Katz v. Image Innovations Holdings Inc.*, 06CV3707 (S.D.N.Y. May 27, 2009) (Koeltl J.).

Retaining Liens

A retaining lien is a remedy available to an attorney or firm that has not been paid for services rendered and has not been discharged for cause.¹ The

lien permits the firm, in the absence of exigent circumstances, to secure a client's documents, materials, securities, and even funds that were acquired by the firm during the course of the litigation until all its reasonable charges are paid in full. Only "exigent circumstances," such as a pending criminal matter, uncontroverted allegations of indigency, or the nature of the case (i.e., matrimonial) will serve to defeat a firm's request for a retaining lien.

"Exigent circumstances" is determined on a case-by-case basis and, importantly, does not include an incoming counsel's need to have access to the client's files in order to continue to litigate on the client's behalf. Indeed, the courts have held that it is an abuse of discretion if the withdrawing counsel is forced to turn over the client's files, even during a pending litigation, despite the imposition of a retaining lien because doing so renders the lien ineffective. If, however, the court does determine that exigent circumstances are present, the firm's request for a retaining lien will simply be converted into one for a "charging lien," which gives the firm the right to any judgment or verdict in the client's favor.

The retaining lien is advantageous to firms because it permits them to seek a more efficient resolution to the dispute with the non-paying client rather than resorting to a separate, and more costly, litigation against the client. To secure a retaining lien, a relieved attorney or firm makes an application to the court presiding over the dispute in which the firm was previously representing the client.

The court will determine the amount of the retaining lien, keeping in mind that the purpose of the lien is to inconvenience the

LEO V. LEYVA is a member, and JED M. WEISS is an associate, in the New York office of Cole, Schotz, Meisel, Forman & Leonard. They can be reached at lleyva@coleschotz.com and jweiss@coleschotz.com, respectively.

client to compel payment. The retaining lien will remain in effect until the firm's balance due for professional services is paid and is not limited to payment relating to the papers or property in the firm's possession. Importantly, the attorney cannot, *sua sponte*, resort to self-help; that is, an attorney cannot maintain control over a client's case files or materials without a court order, lest the attorney be in violation of R.P.C. 1.15(c)(4).²

Importance of Records

In *Katz*, the issue of retaining liens was raised by the firm McCarter & English (McCarter), which represented four individual defendants in the primary litigation matter and two related matters. McCarter was ultimately successful in obtaining dismissal of the majority of the claims against its clients. McCarter accrued a total of \$412,996.47 in attorney's fees and disbursements, of which the clients paid only \$25,000, leaving \$387,996.47 outstanding. In light of the defendants' refusal to pay their legal bills, the court granted McCarter's motion to withdraw as counsel. McCarter promptly filed a motion for the fixation of a retaining lien, a motion that was unopposed by the defendants.

In connection with the retaining lien motion, the court ordered McCarter to produce time records reflecting the time spent by lawyers and their billing rates, so that the court could determine whether the firm's application was reasonable. The court held that in determining what is reasonable, it reviewed several factors, including: 1) the difficulty of the matter; 2) the nature of the services rendered; 3) the time reasonably expended on those services; 4) the quality of performance by counsel; 5) the qualifications of counsel; 6) the amount at issue; and 7) the results obtained. Based on these factors, the court held that McCarter's submission was "generally reasonable" in that McCarter provided "excellent" representation in several difficult matters and obtained a favorable outcome. Notwithstanding this finding, the court nevertheless reduced McCarter's fees.

The court, which clearly scrutinized McCarter's submission, found duplication

in McCarter's billing entries "caused by McCarter's employment of 14 attorneys in this matter, and its billing for internal conferences." As a result of this duplication, the court reduced McCarter's fees by five percent and ultimately fixed the amount of the retaining lien at \$369,169.72 (the court deducted disbursements from its five percent discount). Even with the deduction, the imposition of the retaining lien clearly afforded McCarter leverage in its attempt to secure the remaining amount due from the former clients.

While the fixation of the retaining lien is clearly a useful device for the firm to employ in the event that a client refuses to pay for services rendered, to obtain the maximum benefit of the retaining lien, it is important for the practitioner or firm to keep a scrupulous account of the time expended and costs incurred in connection with the matter. For example, even though McCarter's fees were only reduced by 5 percent, it is clear that courts will take it upon themselves to ensure the reasonableness of fees when fixating retaining liens.

The benefit of keeping meticulous billing entries is not limited to securing a retaining lien, as evidenced by Magistrate Judge Andrew J. Peck's recent decision in *VFS Financing Inc. v. Pioneer Aviation, LLC*, 08CV7655 (S.D.N.Y. Aug. 18, 2009) (Peck J.). The plaintiff in *VFS* sued for non-payment of a promissory note and was granted summary judgment. The contract provided for attorney's fees to the prevailing party; therefore, the plaintiff sought \$133,727.86 in attorneys' fees and costs.

The court, after reviewing the plaintiff's application, agreed with the defendants, who argued that a percentage fee reduction was appropriate because a number of plaintiffs' attorneys' billing entries were overly vague or duplicative. Defendants argued, and the court agreed, that as a result of the vagueness of the entries, it was virtually impossible to determine the nature of the work done, the need for it, and the amount of time reasonably required. Accordingly, the court reduced plaintiff's recovery by 10 percent.

While the retaining lien is a useful device for firms to realize their maximum earning

potential, these two cases highlight the importance of keeping meticulous and justifiable billing entries. Clearly, the requirement for thorough billing entries is extremely important, not only to secure the maximum benefit of a retaining lien, but also to realize the practitioner's or firm's full potential at a time when every dollar counts. Using retaining liens, and maintaining accurate and easily explainable billing entries, is not only good practice; it is good business.

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1. When a court grants a firm's motion to withdraw as counsel, by definition the discharge is not "for cause," even in the instance where the law firm withdrew because the client did not pay its bills.

2. R.P.C. 1.15(c)(4) states, "A lawyer shall...promptly... deliver to the client or third person as requested by the client...the properties in possession of the lawyer..."