

Collecting Your Fee

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- I. Overview §3.1
 - II. The Billing System §3.2
 - III. The Collection System
 - A. In General §3.3
 - B. Steps for Effective Collecting §3.4
 - C. New Clients §3.5
 - IV. Liens and Lawsuits
 - A. In General §3.6
 - B. Retaining Liens §3.7
 - C. Charging Liens §3.8
 - D. Security Interests §3.9
 - E. Judgment Liens and Lawsuits §3.10
 - F. Equitable Liens §3.11
- Exhibit
- 3.1 Lien Quick-Reference Chart

I. Overview

§3.1 Attorneys and law firms need to keep a careful eye on the aging of accounts receivable. After all, cash flow within the firm is the result of clients paying their bills. The timely payment of invoices is the focus of this chapter. Failure to adequately control and monitor the collection cycle can and will put a firm into a financial tailspin.

Attorneys should take note that improvements in the collection of accounts receivable, or outstanding billings, often result in a higher margin of profit without the attorney having to increase rates or work more hours. This fact alone will hopefully inspire the implementation of more efficient collection techniques. The discussion that follows presents practical tips on improving collections and cash flow.

Whether they work in a large or small law firm, most attorneys feel that the collection of accounts receivable is an administrative matter. The task is assigned, in many instances, to a paralegal, secretary, or clerk who bears the weight of many responsibilities within the firm but is still expected to make collection calls “when time permits.” This indifferent attitude is ironic given that the Michigan Attorney Grievance Commission has informally estimated that about 80 percent of the grievance complaints filed in Michigan relate to fee disputes. Marcia L. Proctor, *When the Client Doesn’t Pay the Bill*, 68 Mich B J 856 (1989).

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The best protection against delinquent accounts receivable is attorney responsibility, or “ownership,” over accounts receivable. Commissioned salespeople in many companies are back-charged on commissions if their customers fail to pay. Attorneys should likewise be financially accountable if their billings do not turn into cash. Goals should be set for percentages of collection of accounts receivable. The attorney, not the paralegal, should be the one to decide how much pressure to put on a particular client and whether to compromise the receivable. Attorneys often fail to consider making a deal on a delinquent account because of pride or ego (“I performed detailed work for this client and I expect my client to pay it in full, immediately, in cash”).

It is too easy to fall into the mind-set that the client cannot be actively pursued until after the statute of limitations for malpractice expires. For example, if the statute of limitations for malpractice is two years and is six years for a suit on a contract for providing legal services, the mind-set would be to not pursue the claim until the two years have run. This is a mistake. Polite yet very persuasive collection proceedings can and definitely should be pursued.

II. The Billing System

§3.2 Effective billing procedures are incredibly important and are easy to set up and follow, particularly with today’s high-speed computers and printers. Attorneys who fail to bill quickly are really missing the boat. Billings should be issued frequently and regularly as the case progresses, not at the end of the case. In addition to individual billings for services rendered, the attorney should issue statements every month, without exception. (A statement is a summary of the amount currently owing, sometimes broken down by “aging,” e.g., \$100: 30 days overdue; \$250: 60 days overdue; \$300: 90 days or more overdue.) There is no reason why monthly statements should not be sent to clients as constant reminders that current bills are due and past due bills are long since due. See §2.9–§2.12 for additional discussion of billing practices. Word processing, spreadsheet, and legal accounting programs are available at reasonable prices to facilitate these tasks considerably.

Bill terms are almost always net 30 days. Some attorneys offer a 3–5 percent discount for early payment just like many companies do. (Large companies often offer a 3–5 percent discount for prompt payment of the bill within the first 10–30 days, with the full bill due and no discount offered after 30 days.) Attorneys may also charge interest or a time-price differential on unpaid bills. See §2.12.

III. The Collection System

A. In General

§3.3 If a client does not pay a bill in a timely fashion (within 30 days), it is important to treat the bill as an overdue debt and begin collection efforts promptly. Perhaps the most important rule to remember in collections is that the reason the systems are in place is to constantly remind people that they owe money. In this day and age, you can safely figure that your client owes money to at least 10, and probably 20 or 30, other creditors. The creditors who are the squeaky wheels get paid. Consider your own experience where you perhaps missed a payment on a credit card. Suddenly you would start receiving a barrage of letters, telegrams, and maybe even a phone call, all threatening that your card would be suspended, your credit would be ruined, and life as you know it would cease to exist unless you paid immediately. Compare this system of collection with that of a doctor or other professional (professionals are the worst) who sends out a bill once every 60 days and charges no interest. The financially successful professional needs to find a middle ground. Many clients/debtors react positively to fairly aggressive collections as long as these tactics are

professional. Many clients are even apologetic about their inability to pay and appreciate firm but polite reminders.

Because so many people are delinquent in paying their bills, in addition to the billing system, you need to have in place a collection system permitting follow-up by both telephone and letter. To follow up, you should do the following:

1. Issue monthly statements summarizing the balance currently owed, the terms, and an address where the money should be sent.
2. Enclose a self-addressed, stamped envelope to encourage recalcitrant clients to send in the money.
3. Add interest to the bill to create some sense of urgency (it is important to include a provision in your fee agreement stating that you will charge either interest or a time-price differential on unpaid bills. See §2.12).
4. Begin a formal collection process if no payment is made within 45 days.

B. Steps for Effective Collecting

§3.4 Typically, the weakest link in the law office collection system is the failure to begin following up when the account is more than about 45 days delinquent. Once the law firm allows the client to go 60–90 days without paying the bill, the client begins to feel that the bill is not urgent and moves on to other priorities. Payments on the mortgage and credit cards are made, and the law firm bill is ignored. Therefore, follow-up with the client must be fairly firm at this juncture, and someone should be assigned to systematically pursue payment.

The first step in collecting an overdue bill is for the office manager to notify the billing attorney that the account is delinquent. The billing attorney can then decide whether to call the client or take some other form of action. The recommended course is for the billing attorney to make the telephone call personally. If a paralegal or a member of the support staff is assigned the task of making the telephone call, that person must be familiar with the bill and have the proper documents and the billing history. The call should be placed to accomplish the following goals: (1) to determine whether the client has been receiving the billings; (2) to determine whether the client admits that the billings are accurate and the money is due; (3) to determine exactly when (not “in about two weeks,” but by a specific date) payment will be made; and (4) to set up a payment plan (but only if the client cannot pay in full).

Take notes during the call. Does the client admit that he or she owes the money? (This can become extremely significant if litigation is brought.) What is the date by which the money is to be paid in full? What is the date by which the first installment is to be paid?

If you find during the call that the client disputes the bill, take steps to resolve the dispute. The billing attorney is probably the best person to contact the client to resolve the issues. For a slight reduction in the bill, the client may come around. A few kind words may help. (Let’s face it, a lot of people don’t like to pay attorney fees.) You might offer to do a simple follow-up task to induce the client to pay. However, keep in mind that you may not want to do any more work on the case if there is a statute of limitations or malpractice concern, as this may toll the statute.

Take a tip from an experienced bill collector: Telephone calls are much more effective than demand letters, particularly if the letters sound like demand letters. Whoever is making the calls should place a series of them so that they get on a “roll.” The collector must be given a telephone, time to make the calls, copies of the statements, and some authority to make payment arrangements. A calm approach usually works better than threats. Sometimes during the call, the client wants to vent his or her frustration. It is OK for the conversation to get off track for a few minutes

as long as the collector brings the conversation back to its focus before the client hangs up. You can count the call a success if the client has promised a sum certain by a specific date.

Once the bill becomes substantially delinquent (more than 120 days past due without a significant interim partial payment), it should be referred to a committee or the supervising partner in charge of accounts receivable. This is particularly true if the bill is disputed. When there is a dispute, something needs to be done to correct any mistakes or to improve the relationship with the client if the client's feelings have been hurt. Law firm pride should not prevent correction of an error.

Finally, if the debtor/client avoids telephone calls and fails to respond to letters, statements, and billings, a decision has to be made about whether to sue, write the account off, or use a collection agency or other outside party to collect the bill. There are advantages and disadvantages of using in-house counsel versus outside assistants such as collection agencies or collection attorneys. An advantage of using in-house counsel is that it will save the firm money because the firm will not have to retain counsel or pay contingent fees. Another potential advantage is that in-house attorneys often respond more quickly to the problem than do outside counsel. Potential disadvantages to using in-house counsel are that an in-house attorney may be defensive about client criticism or may become too personally involved.

Attorneys collecting their own accounts are not subject to the federal Fair Debt Collection Practices Act (FDCPA), 15 USC 1692 et seq. However, two state statutes are applicable. The first, MCL 445.251 et seq., prohibits a "regulated person" (attorneys are regulated, even for collection of their own debts; *see* MCL 445.251(g)(xi)) from harassing or making misleading and deceptive communications to debtors. MCL 445.252. In a civil claim, the court may assess a \$50 damages award or actual damages, whichever is greater. MCL 445.257. The Michigan Consumer Protection Act (MCPA) also protects consumers regarding personal and household-related debts for such things as personal wills, home sales, and family law matters, and prohibits similar infractions. MCL 445.901 et seq. In any event, common sense should prevail: Don't use profanity, always make the calls during normal business hours, and limit calls to the actual client—don't call third parties.

C. New Clients

§3.5 The collection system in your office ought to be comprehensive enough to allow not only for the collection of due and past-due bills but also for the review of new clients' creditworthiness. Keep in mind that most businesses have professional credit managers who evaluate the creditworthiness of new customers and set credit limits. You might consider setting credit limits, requiring a client to keep the account within a certain dollar amount. Law firms typically do not do this because services, once started, are generally forced to continue by the nature of the legal problem. However, an attorney may stress to a nonpaying client the importance of the client's keeping his or her part of the agreement by paying the bill. The issue of keeping current with payments can also be addressed in the fee agreement. *See*, for example, form 8.1.

Lawyers may also reduce the chances for delinquent accounts receivable by adopting the three rules known so well to criminal attorneys: Get paid up front, get paid up front, and get paid up front. Obviously, this is not always possible. Be aware that a client who is unwilling or unable to pay you a reasonable retainer will probably be unwilling or unable to pay you later. *See* also §2.3.

IV. Liens and Lawsuits

A. In General

§3.6 In some instances, you may wish to assert a lien in an attempt to collect your fee. There are essentially five types of liens that you may use, depending on the situation: the retaining lien (see §3.7), the charging lien (see §3.8), the security interest (see §3.9), the judgment lien (see §3.10), and the equitable lien (see §3.11).

A *retaining lien* is the right to retain possession of a file or documents relating to the case where the fee is owed, while a *charging lien* is the right to retain a portion of the proceeds or funds resulting from litigation on the case where the fee is owed. You can assert these liens only against files or funds relating to the case on which the fee is due; you cannot assert them against some other case on which you are working for the same client where the fee is not past due. Because retaining and charging liens arise as a matter of law and fit within the most common fee dispute scenario (client owes attorney fees), these are the two liens most often used. The restrictions on retaining liens (see §3.7) make the charging lien the most popular.

A *security interest*, unlike the other types of liens, arises as a matter of contract. Under MRPC 1.8(j), a lawyer is prohibited from acquiring a security interest against property that is the subject of the litigation.

An *equitable lien* arises by agreement and protects an attorney in a situation where someone who is not a client of the attorney is being enriched as a result of the attorney's efforts.

Judgment liens are the least used type of lien because the assets must be levied on or seized for the lien to become operative. This necessitates the attorney suing the client for the fee. That is seldom done for many reasons, not the least of which is that under the ethics rules an attorney may not sue his or her client while representing the client on any matter, even if that matter is unrelated to the matter at issue.

The discussion below summarizes the main features of liens in Michigan. For further information, see the excellent article by Marcia L. Proctor, *Clarifying Liens*, 73 Mich B J 690 (1994). See also exhibit 3.1, Lien Quick-Reference Chart, from page 695 of that article.

B. Retaining Liens

§3.7 In some cases, a lawyer may withhold from a client the client's file or other property, following reasonable notice. The lawyer's right to withhold the file or property, called a *retaining lien*, automatically arises when the attorney has billed the client for a fee and the client has not paid. The attorney does not have to take further action to perfect the lien. There are, however, limited circumstances under which this lien ethically may be asserted against a client. See MRPC 1.15(b), 1.16(d). One of the leading cases in the area, *Kysor Indus Corp v DM Liquidating Co*, 11 Mich App 438, 161 NW2d 452 (1968), allows for a retaining lien until the client pays the attorney the balance due. Note that the lawyer's voluntary withdrawal from representation terminates the retaining lien.

The retaining lien arises only against property the lawyer possesses as a result of the representation on which the bill was incurred. A lawyer may not assert a retaining lien on other property coming into the lawyer's possession. Such an action violates MRPC 1.15(b). *Freyer v Mutual Benefit Health & Accident Ass'n*, 45 Wis 2d 106, 172 NW2d 338 (1969). A lawyer has a retaining lien only as long as the money is owed, and the lien terminates when the fee is paid. *White v Zeff*, 107 Mich App 520, 309 NW2d 650 (1981). A retaining lien is not available in a criminal representation. *Marsh, Day & Calhoun v Solomon*, 204 Conn 639, 529 A2d 702 (1987). A retaining lien also may not be available when the client needs the file to pursue legal rights, such as an appeal. *Vogelhut v Kandel*, 66 Md App 170, 502 A2d 1120 (1986). It has been held that assertion of a retaining lien is reserved for those situations where the client refuses to pay as opposed to those situations

where the client is unable to pay. *McGrath v State Bar of California*, 21 Cal 2d 737, 135 P2d 1 (1943).

C. Charging Liens

§3.8 Michigan acknowledges a common-law charging lien. The charging lien is the most common form of lien used by courts and practitioners. It is equitable in nature and is under the court's discretion and control. The charging lien is a "charge," or lien, created on any money that may come into the attorney's hands as a result of a judgment that the attorney has obtained for his or her client. Essentially, it is a charge in the same respect as a security interest formed under the Uniform Commercial Code (UCC) for the attorney's benefit on specific litigation proceeds. *Aetna Cas & Sur Co v Starkey*, 116 Mich App 640, 645, 323 NW2d 325 (1982). The lien applies only to judgment proceeds resulting from work the lawyer has done for the client. *Wipfler v Warren*, 163 Mich 189, 128 NW 178 (1910).

Where a lawyer was hired on a one-third contingent fee and obtained a default judgment for \$25,000 (entitling the lawyer to a contingent fee of slightly more than \$8,000), the court set aside a satisfaction of judgment where the client, without the lawyer's knowledge or consent, settled the case directly with defaulted defendant for \$1,500. The court acknowledged the existence of the attorney's charging lien and pointed out that plaintiff and defendant could not discharge the underlying debt in prejudice of the charging lien without the attorney's consent. *Doxtader v Sivertsen*, 183 Mich App 812, 455 NW2d 437 (1990).

A lawyer who withdraws without cause loses the charging lien. *Ambrose v Detroit Edison Co*, 65 Mich App 484, 237 NW2d 520 (1975). The *Ambrose* case also stands for the proposition that the court will calculate the amount of the charging lien in a contingent fee case on the basis of quantum meruit.

Charging liens do not attach to files or documents, only to money or proceeds that result from the lawyer's efforts on behalf of the client. *Rubel v Brimacombe & Schlechte, PC*, 86 BR 81 (ED Mich 1988). A lawyer who wishes to formalize a charging lien into a UCC lien must first meet the UCC requirements, including filing a financing statement and showing that a security agreement exists. *George v Sandor M Gelman, PC*, 201 Mich App 474, 506 NW2d 583 (1993).

D. Security Interests

§3.9 Security interests, unlike retaining and charging liens, are created by contract. A security interest can therefore be created before the existence of the money or fund resulting from the attorney's action on behalf of the client. For example, an attorney might take a case on a contingent fee basis and assert a security lien on any *potential* recovery. Because security liens are contracts, they must comply with UCC Article 9 requirements for security agreements and financing statements and agree with the terms of MRPC 1.8(a). It should be noted that the UCC relates only to liens on personal property and not to liens on real estate. To establish a lien as a matter of contract on real estate, the lien must be recorded in the register of deeds office. Again, you must adhere to the requirements of MRPC 1.8(a).

You might create a security lien at the beginning of a transaction, at the same time that you formulate the retainer agreement. Security liens are particularly useful in situations where you are taking a case on a contingent fee basis and are concerned that the liened property may flow directly to the client, bypassing you and thus making it difficult for you to claim a charging lien. In other words, the security interest is a good lien to use if you suspect that the client may attempt to avoid paying legitimate attorney fees.

E. Judgment Liens and Lawsuits

§3.10 In many states, such as Ohio and other sister states in the Midwest, a judgment may become a lien on all of the defendant's assets by filing the judgment in the register of deeds office. This is not the case in Michigan. As Detroit College of Law Professor Clark Johnson has stated, "Michigan is not a judgment lien state, it is a race-to-the-assets state." In Michigan, you cannot automatically obtain a lien on a defendant's property where you have a judgment against that defendant. You must first sue the client and obtain a judgment on the debt for fees. Then you must execute the judgment. Note that in order to have standing to sue in the first place, you must have a valid contract for fees—i.e., a fee agreement, preferably written. See §2.21.

F. Equitable Liens

§3.11 An equitable lien arises from a written agreement between lawyer and client that certain specified property being held by a third party may be used to secure the lawyer's fee. Under very limited circumstances, where a lawyer and client verbally agree to a lien on certain personal property and do not put that agreement in writing, the court may impose an equitable lien. *Warren Tool Co v Stephenson*, 11 Mich App 274, 161 NW2d 133 (1968); *see also Cheff v Haan*, 269 Mich 593, 257 NW 894 (1934); *Kelly v Kelly*, 54 Mich 30, 19 NW 580 (1884).

Nonclients must have notice that the lawyer's services are being rendered to their benefit for the lawyer to obtain an equitable lien. If the fee itself is based on a contingent fee, a writing is required under MCR 8.121(F) and MRPC 1.5(c).

Exhibit 3.1
Lien Quick-Reference Chart

LIEN QUICK-REFERENCE CHART					
	Judgment Lien	Retaining Lien	Charging Lien	Security Interest	Equitable Liens
DESCRIPTION	Lien arising from judgment obtained by lawyer against client.	Lawyer has right to retain possession of client property coming into lawyer's hands during the course of professional employment until the bill is paid.	Lawyer has right to be paid from the money proceeds of the case in which the lawyer's services were rendered.	Lawyer has lien against real or personal property of client to secure payment of lawyer's fee.	Lawyer has a lien for payment of fees from non-client who is enriched by the services performed by the lawyer.
AUTHORITY: HOW ARISES	Lawyer must sue and obtain judgment on the debt, then execute on the judgment before lien arises.	Lien arises automatically when lawyer bills client for amount owed and client fails to pay.	Lien arises automatically when client's obligation to pay has accrued and client fails to pay; cannot be created by contract.	Lien arises under written agreement with client.	Lien arises from written or verbal agreement that both identifies the property and evidences an intention that such property serve as security for the lawyer's fee.
OTHER REQUIREMENTS	To have standing to sue, must have valid underlying contract.	Lien may only be exercised over property coming into lawyer's possession for the representation in which fee is due; does not transfer to other representations. Lien is waived if lawyer discloses or provides copies of material over which lien is exercised.	Lien may only be exercised against money proceeds in case in which lawyer's services were rendered; does not transfer to other property or to other representations. Persons who hold funds against which lien is claimed must have notice of lien prior to conclusion of case. No lien arises if lawyer wrongfully withdraws from representation. In case of dispute, disbursement must be determined by court.	Written agreement must comport with MRPC 1.8(a) and provisions of the Uniform Commercial Code.	Non-clients must have notice that the lawyer's services are being rendered to their benefit; if based on contingent fee contract, a written agreement is required by MCR 8.121 and MRPC 1.5(c).
ETHICAL CONSIDERATIONS	Suit for nonpayment of fees should be a last resort. A lawyer may not sue a client for collection of fees while still representing the client on unrelated matters, nor may a lawyer assign the lawyer's rights under the fee contract to another person for legal action while the lawyer continues to represent the client.	Not ethical to exercise lien when the client or successor counsel needs the property to pursue the client's legal rights, or if the client is unable to pay, as opposed to refuses to pay.	Not ethical to exercise if the lawyer withdraws without cause.	Not ethical to obtain lien against property which is the subject matter of litigation in which the lawyer's services are to be used, unless authorized by law.	

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