Reconsideration of Ethics Arizona Ethics Opinion 09-01

Introduction

The Arizona Supreme Court's Attorney Ethics Advisory Committee (the Committee) has been asked to revisit Arizona Ethics Opinion 09-01, which concluded that a firm may not require, as a condition of employment, that an associate who departs from a firm pay a $3,500 fee for each former firm client that the associate continues to represent after departing. Arizona Ethics Opinion 09-01, issued by the State Bar of Arizona's Committee on Professional Responsibility (the State Bar Ethics Committee), did not address the 2006 Arizona Supreme Court opinion, *Fearnow v. Ridenour, Swenson, Cleer & Evans*, 213 Ariz. 24 (2006). The Committee has agreed review Ethics Opinion 09-01 to reconcile the two opinions.

This Committee concludes that requiring an associate who departs from a firm to pay a large fee[1] to continue to represent a client would violate the Arizona Rules of Professional Responsibility.

APPLICABLE ARIZONA RULES OF PROFESSIONAL CONDUCT ("ER __")

ER 1.5. FEES

(a) A lawyer shall not make an agreement for, charge, or collect an unreasonable fee or an unreasonable amount for expenses.

…

ER 1.7. CONFLICT OF INTEREST: CURRENT CLIENTS

(a) Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:

. . .

(2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.

. . . .

Comment

[10] . . . a lawyer may not allow related business interests to affect representation.

ER 1.16. DECLINING OR TERMINATING REPRESENTAION

. . .

b) Except as stated in paragraph (c), a lawyer may withdraw from representing a client if:

---

[1] The Committee is reluctant to determine what the exact fee is that is reasonable because of the varying nature of attorneys' practices. We do note that in most circumstances, a $3,500 fee per client would be unreasonable.

(1) withdrawal can be accomplished without material adverse effect on the interests of the client;

. . . .

ER 1.17. SALE OF LAW PRACTICE

A lawyer or a law firm may sell or purchase a law practice, or an area of law practice, including good will, if the following conditions are satisfied:

. . .

b) The entire practice, or the entire area of practice, is sold to one or more lawyers or law firms;

. . .

d) The fees charged clients shall not be increased by reason of the sale.

ER 5.6. RESTRICTIONS ON RIGHT TO PRACTICE

A lawyer shall not participate in offering or making:

(a) a partnership, shareholders, operating, employment, or other similar type of agreement that restricts the right of a lawyer to practice after termination of the relationship, except an agreement concerning benefits upon retirement;

. . . .

RELEVANT ARIZONA ETHICS OPINIONS

Ariz. Ethics Ops. 99-14, 01-01, 09-01

Background

The State Bar of Arizona Ethics Committee issued Ethics Opinion 09-01, which addressed the following question: "May Firm require, as a condition of employment, that in the event Associate departs from Firm, Associate must pay a $3,500 fee for each former Firm client that Associate continues to represent after departing?" The agreement provided that the fee would not be owed "where Associate can demonstrate that the client was not obtained through Firm marketing, where a court requires Associate to remain counsel of record, or where Firm elects to have the client continue with Associate."

Ethics Opinion 09-01 cited a line of cases that hold that "agreements that impose financial disincentives, as opposed to explicit restrictions, on a withdrawing partner's competition with the former firm" *Shuttleworth, Ruloff and Giordano, P.C. v. Nutter*, 493 S.E.2d 364, 367 (Va. 1997) (collecting cases) are prohibited under American Bar Association Model Rule 5.6, which is identical to Arizona's ER 5.6.

Ethics Opinion 09-01 concluded that the agreement at issue would violate ER 5.6 because it would, for four reasons, "improperly constrain a client's freedom to choose to continue

representation by the departing associate”: (1) it would discourage the departing lawyer from representing a client that might want to continue with the lawyer; (2) the set amount of the fee would have a disproportionate impact on continuing to represent clients in lower-value cases; (3) it would give the departing lawyer an incentive to charge the client more, in violation of the policy behind ER 1.17(d), which prohibits increasing a client’s fees when a practice is sold; and (4) it would create a conflict of interest in violation of ER 1.7(a)(2).

However, the Arizona Supreme Court addressed ER 5.6 in a 2006 opinion, *Fearnow v. Ridenour, Swenson, Cleer & Evans*, 213 Ariz. 24 (2006). The case arose from a dispute between a law firm and a lawyer who had left the firm to join another firm. Under the terms of the first firm’s shareholder agreement, the firm would repurchase the capital interest of a lawyer who chose to retire or was involuntarily expelled from the firm. But a lawyer who chose to leave the firm and continue practicing in the firm’s geographic area forfeited this right to repayment. When the firm refused to repurchase a voluntarily departing shareholder’s shares, the lawyer sued, arguing that the forfeiture provision violated ER 5.6 and was therefore unenforceable as against public policy.

The Arizona Supreme Court concluded that:

> Although the rule prohibits—and we will hold unenforceable—agreements that forbid a lawyer to represent certain clients or engage in practice in certain areas or at certain times, its language should not be stretched to condemn categorically all agreements imposing any disincentive upon lawyers from leaving law firm employment. Such agreements, as is the case with restrictive covenants between other professionals, should be examined under the reasonableness standard.

213 Ariz. at 30, ¶ 21. Thus, in drawing this conclusion, the Supreme Court acknowledged the line of cases cited by the State Bar Ethics Committee but declined to follow those. *Id*. at ¶ 20. Instead, the Court concluded that shareholder agreements are not per se unethical, but must be subject to a reasonableness standard. *Id*.

The Committee is issuing this opinion to address any apparent inconsistency between Ethics Opinion 09-01 and *Fearnow*.

Discussion

ER 5.6 has twin goals: lawyer autonomy and client choice. Both of these goals must be upheld for an agreement that restricts a lawyer’s right to practice to be ethical.

To preserve lawyer autonomy, the rule prohibits a lawyer from entering into an agreement that restricts the lawyer’s right to practice after leaving a firm or as part of a settlement agreement. Relying on a string of California cases, *Fearnow* added that a financial disincentive, as opposed to an outright restriction on a lawyer’s autonomy, does not violate ER 5.6. This is in contrast with Ethics Opinion 09-01, which relied on the line of cases which stood for the opposite premise—namely that disincentives are also prohibited.

Fearnow also requires that the restriction be reasonable. *Fearnow* at __. However, the *Fearnow* Court, while acknowledging that ER 5.6 is grounded in concerns about preserving both

"lawyer autonomy and client choice" (213 Ariz. at 27, ¶ 12), did not "condemn categorically all agreements imposing any disincentive upon lawyers from leaving law firm employment" (*id*. at 31, ¶ 21). Instead, "[s]uch agreements, as is the case with restrictive covenants between other professionals, should be examined under the reasonableness standard." *Id*. Thus, *Fearnow* also allows for prohibition of agreements imposing unreasonable financial disincentives.

The second goa of ER 5.6 is described in Comment 1—protecting individual clients and their right to the lawyer of their choice. Specifically, Rule 5.6 is intended to prevent limits on "the freedom of clients to choose a lawyer." *Id*.

The State Bar Ethics Committee also addressed the important issue of client choice in Ethics Opinion 09-01, saying:

> Based on such principles, this Committee has explained that "[w]here the departing lawyer has had significant personal contact with a client in connection with the provision of legal services to that client by the firm, . . . the client must be provided with the opportunity to choose between going with the departing lawyer or remaining with the firm." Ariz. Ethics Op. 99-14; see also Ariz. Ethics Op. 01-01 (opining that a lawyer cannot enter a contract that would preclude representing certain clients); ABA Formal Op. 99-414 ("[E]ach client has the right to choose the departing lawyer or the firm, or another lawyer to represent him."). We agree, therefore, that "[t]he commercial concerns of the firm and of the departing lawyer are secondary to the need to preserve client choice." Jacob, 607 A.2d at 151. *See also* Phil. Bar Assn. Op. 87-24 ("Although law firms have a right to protect their legitimate business interests, including their client base, they may not do so to the exclusion of the client's preference."). The need to preserve client choice is no less when the departing lawyer is an associate.

Fearnow also acknowledged that an agreement that limits client choice is unenforceable under ER 5.6. In a footnote, the Court stated, "it is difficult to see how client choice is significantly impacted by our reading of 5.6(a). The client is of course free to remain with the lawyer, whether or not the lawyer chooses to stay at his original firm or go elsewhere."

Synthesizing the two prongs of ER 5.6 and the holding in *Fearnow*, the Committee concludes that any agreement that restricts a lawyer's professional autonomy must be (1) reasonable and (2) protect client choice. Thus, the question becomes whether a large per client fee to be paid by a departing lawyer is reasonable and protects client choice.

As Opinion 09-01 explains, such a penalty has a direct impact on client choice and lawyer autonomy. A large per client fee acts as a substantial disincentive for the departing lawyer to agree to continue representing a client who wants to continue working with that lawyer. That is particularly true for clients with lower-value cases. More than the agreements at issue in *Fearnow* and the cases on which *Fearnow* relied, which can be characterized as protections for the capital structure of the law firms involved, the agreement here appears on its face to has much larger ramifications for client choice. In the opinion of the Committee, these are material differences.

Furthermore, the fees give the departing lawyer an incentive to charge larger fees to those clients from the former firm in violation of ER 1.17. *See e.g.,* Ethics Opinion 09-01, ER 1.17(d) (providing that "[t]he fees charged clients shall not be increased by reason of the sale [of a practice]"). If these fees are unreasonable, the attorney may also violate ER 1.5(a) ("[a] lawyer shall not make an agreement for, charge, or collect an unreasonable fee or an unreasonable amount for expenses.")

In addition, paying such a fee may give rise to a conflict of interest because of the difference in the interests between the attorney and the client. *See* ER 1.7(a)(2); *id*. at cmt [10] (explaining that "a lawyer may not allow related business interests to affect representation"). A lawyer cannot continue to represent a client if "there is a significant risk that the representation …will be materially limited by … a personal interest of the lawyer." ER 1.7(a)(2). Here, having to choose whether to retain a client and pay a large fee would mean that the lawyer has a personal interest in the client's matter, in violation of ER 1.7.

Conclusion

It is the determination of this Committee that the Arizona Rules of Professional Conduct prohibit a firm from requiring a departing attorney to pay an unreasonable fee for clients that opt to continue representation by the departing lawyer.