ATTORNEY ETHICS ADVISORY COMMITTEE

Thursday January 30, 2020

No. 5 Update and possible action regarding Ethics Opinion draft

o EO-19-0006

Committee member Hon. John Napper will present information at the meeting.

ETHICS OPINION REQUEST

Sent: Tuesday, March 28, 2017 9:12 AM
To: Patricia Seguin <patricia.seguin@staff.azbar.org>
Subject: Reconsideration of Ethics Op. 09-01

Hi Patricia,

I am just following up on our telephone conversation early last month regarding reconsideration of Ethics Op. 09-01, in light of the Supreme Court case, *Fearnow v. Ridenour, Swenson, Cleere & Evans, P.C.*, 213 Ariz. 24, 138 P.3d 723 (2006). As I mentioned during our call, *Fearnow* held that provisions like the one at issue in the ethics opinion must be reviewed under a reasonableness standard. The Ethics Op. makes no mention of *Fearnow* and does not analyze the provision under that standard, and thus, in my opinion, its reasoning is flawed.

I am not certain if the Ethics Committee is still on "hiatus." I would appreciate if you could pass my concerns about Ethics Op. 09-01 to Becky Albrecht, Lisa Panahi and Ann Ching (if you did not do so after we spoke). If there is anything else that I might need to do regarding this issue, please let me know.

Thanks!

State Bar of Arizona Ethics Opinions

09-01: Restrictions on Right to Practice; Departing Lawyer 5/2009

A law firm may not employ associate lawyers using a contract that requires a departing associate to pay $3,500 to the law firm for each instance in which the departing associate continued to represent a law firm client. This requirement would violate the policy underlying ER 5.6 that puts the commercial interests of law firms secondary to the need to preserve client choice.

FACTS

A law firm (Firm) is contemplating using an employment contract that requires an associate lawyer (Associate) to pay Firm $3,500 for each client or prospective client for whom Associate provides legal representation after departing Firm. The contract characterizes this as a "Firm Reimbursement Fee" and explains that it compensates Firm for marketing expenses. Such fees would not be owed, however, 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.

QUESTION PRESENTED

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?

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

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:
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> > . . .
> >
> > (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.
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> . . . .

Comment

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

ER 1.16. Declining or Terminating Representation

> . . .
>
> b) Except as stated in paragraph (c), a lawyer may withdraw from representing a client if:
>
> > (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;
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> . . .
>
> d) The fees charged clients shall not be increased by reason of the sale.

Comment

[1] The practice of law is a profession, not merely a business. Clients are not commodities that can be purchased and sold at will. Pursuant to this Rule, when a lawyer or an entire firm ceases to practice, or ceases to practice in an area of law, and other lawyers or firms take over the representation, the selling lawyer or firm may obtain compensation for the reasonable value of the practice as may withdrawing partners of law firms. See ERs 5.4 and 5.6.

[6] The Rule requires that the seller's entire practice, or an entire area of practice, be sold. The prohibition against sale of less than an entire practice area protects those clients whose matters are less lucrative and who might find it difficult to secure other counsel if a sale could be limited to substantial fee-generating matters. The purchasers are required to undertake all client matters in the practice or practice area, subject to client consent. This requirement is satisfied, however, even if a purchaser is unable to undertake a particular client matter because of a conflict of interest.

[15] This Rule does not apply to the transfers of legal representation between lawyers when such transfers are unrelated to the sale of a practice or an area of practice.

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

OTHER RELEVANT ETHICS OPINIONS

ABA Formal Op. 99-414

OPINION

With few exceptions, courts have consistently recognized that American Bar Association Model Rule 5.6 [1] "prohibit[s] 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). For example, in *Jacob v. Norris, McLaughlin & Marcus*, 607 A.2d 142 (N.J. 1992), the court explained the purpose of Model Rule 5.6:

> The history behind the [rule] and its precursors reveals that the [rule's] underlying purpose is to ensure the freedom of clients to select counsel of their choice, despite its wording in terms of the lawyer's right to practice. The [rule] is thus designed to serve the public interest in maximum access to lawyers and to preclude commercial arrangements that interfere with that goal.

Id. at 146. The same court identified the underlying policy that controls the resolution of this inquiry, as follows: "[T]he practice of law must be carefully governed by ethical considerations rather than by the economic concerns that guide strictly commercial enterprises." *Id*. at 147.

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.

The primary question raised here, therefore, is whether Associate's obligation to pay a $3,500 fee would improperly constrain a client's freedom to choose to continue representation by the departing associate. *See* ER 5.6 & cmt [1]. We conclude, that it does.

There are four related reasons why the fee would improperly constrain a client's freedom to choose to continue representation by the departing associate.

First, the fee "acts as a disincentive to representing the client" and, thereby, "limits the client's ability to retain counsel of choice." Phil. Bar Assn. Op. 89-3. [2] *Cf. Stevens v. Rooks Pitts & Poust*, 682 N.E.2d 1125, 1132 (Ill. App. 1997) (holding that "no law partnership agreement should restrict a departing partner's ability to practice law"). "Financial disincentives may involve either forfeiting compensation that is due to the departing lawyer or requiring that the departing lawyer remit to the firm a part of profits earned from representing former clients of the firm." *Legal Ethics, Law. Deskbk. Prof. Resp*. § 5.6-1 (2008-09 ed.) See *ABA/BNA Lawyer's Manual on Professional Conduct* 51:1205 (2004) (examining financial disincentives involved in Rule 5.6). The fee here surely has such an effect because it must be paid each time that the departing associate continues the representation of a Firm client.

Second, because the fee is fixed at $3,500, it places a disproportionate disincentive on continuing the representation of less lucrative matters. [3] Although ER 1.17 itself only applies to the sale of a law practice, *id*. at cmt [15], it recognizes a more general policy concern that "protects those clients whose matters are less lucrative and who might find it difficult to secure other counsel." *Id*. at cmt [6]. The proposed contract here would improperly place a heightened disincentive on a departing associate continuing the representation of such clients. It would appear decidedly improper if clients whose matters are less lucrative had any additional barriers to securing representation of their choice. [4]

Third, the fee improperly gives a departing associate incentive to charge larger fees to clients represented at the former firm. This is contrary to the policy disfavoring arrangements that create an incentive to charge clients greater fees. *See, e.g.*, ER 1.17(d) (providing that "[t]he fees charged clients shall not be increased by reason of the sale [of a practice]").

Fourth, the fee creates a conflict of interest. The Ethical Rules proscribe conflicts between the lawyer's personal interests and those of 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"). Formation and termination of the lawyer-client relationship is part of representation. The fee creates a conflict to the extent that it deters the associate from taking the representation.

In closing, because in matters of professional responsibility, "justice and the law must rest upon the complete confidence of the public and to do so they must avoid even the appearance of impropriety," *State v. Hursey*, 176 Ariz. 330, 334, 861 P.2d 615, 619 (1993) (alteration and quotation marks omitted), we note that we would evaluate the fee no differently in the context of a law firm that had unusually high marketing expenses.

CONCLUSION

A client's right to choose counsel must have precedence over the lawyer's commercial interests. The fee proposed here improperly violates that policy because it puts the firm's commercial interests ahead of the client's right to choose. Given the substantial amount of this fee, that it would directly discourage a departing associate from agreeing to continue the representation of clients, and that it would encourage the associate to charge former firm clients higher fees, the proposed fee is unethical and cannot be part of an employment agreement.

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[1] Model Rule 5.6(a) is identical to our Ethical Rule (ER) 5.6(a).

[2] In this opinion, the Philadelphia Bar Association addressed a contract provision that required a departing lawyer to pay all sums due on the account of a departing client. The opinion recognized that "to the extent that the required personal liability of the attorney acts as a disincentive to representing the client, the proposed clause limits the client's ability to retain counsel of choice." *Id*. The Philadelphia Bar Association held that such agreements were unethical because "[i]n view of the possible magnitude of post-termination payments, the proposed contract clause operates as a restriction on the right to practice." We agree and disapprove as well for the other reasons offered in this opinion.

[3] The $3,500 per matter fee is a very substantial disincentive for any size matter. Assuming the associate is starting a new practice, he or she might only earn about $60,000 the first year. *Natl. Assoc. for Law Placement* http://www.nalp.org/ (last visited May 2009, reporting that the mean income for new lawyers is $60,000 per year).

[4] *But see* Phil. Bar Assoc. Op. 87-24 ("liquidated damages" clause not necessarily unethical that required payment of a set percent of fees earned during first year from clients taken by departing associate). We disagree with this opinion. A liquidated damages provision defined as a percentage of fees earned would either require the associate to share responsibility with the former law firm or would allow a division of fees without sharing of responsibility. We disapprove of the former because it would compel the client to continue representation by Firm as a condition of going with Associate. We disapprove of the latter because our ER 1.5(e)(1) requires that "each lawyer receiving any portion of the fee assumes joint responsibility for the representation." The Pennsylvania rule 1.5(e) did not (and does not) have this requirement.