Lawyer Conundrum – Non-Compete

Friends,

I'd appreciate any input on this issue. A friend of mine is a relatively
new attorney. Her first job was as an associate in a satellite office of a
law firm.

Under the terms of the employment agreement, if she leaves the firm and
works with any of her former clients, she is required to pay to the old
firm an amount equal to 75% of what the old firm would have charged for the
work.

So, for example, suppose a former client - "Bob" - contacts her to form a
corporation. If the old firm would have charged $1,000 for the
incorporation, she would have to pay them $750, no matter how much she
actually charges the client.

I believe this has three problems:

1) California generally disfavors non-competes. This is not technically a
non-compete, but it has that effect, to be sure.

2) The Rules of Professional Responsibility say that an attorney cannot
share any portion of a fee with another attorney, unless the client
consents in writing and the total fee is not increased as a result of the
fee-sharing. This agreement violates the first, and probably the second,
prong of that rule.

3) It effectively creates a price-fixing scheme. It makes it functionally
impossible for the departing attorney to ever charge less than the original
firm. It pretty much forces the attorney to charge MORE than the former
firm would. (Who can live on 25% of the reasonable fee?)

I figured I'd put this to the firm for feedback. Thanks!

Bigger issue

Client gets to choose their attorney and this clause works against that

Erin M. Schmidt, Ohio

David, I'd take a look at rule 1.500, particularly the last sentence of the discussion section; "free to practice without any contractural restriction" is pretty clear; and any cases/bar opinions dealing with it.

(A) A member shall not be a party to or participate in offering or making an agreement, whether in connection with the settlement of a lawsuit or otherwise, if the agreement restricts the right of a member to practice law, except that this rule shall not prohibit such an agreement which:
(1) Is a part of an employment, shareholders', or partnership agreement among members provided the restrictive agreement does not survive the termination of the employment, shareholder, or partnership relationship; or
(2) Requires payments to a member upon the member's retirement from the practice of law; or
(3) Is authorized by Business and professions Code sections 6092.5 subdivision (i), or 6093.

(B) A member shall not be a party to or participate in offering or making an agreement which precludes the reporting of a violation of these rules.
Discussion:
Paragraph (A) makes it clear that the practice, in connection with settlement agreements, of proposing that a member refrain from representing other clients in similar litigation, is prohibited. Neither counsel may demand or suggest such provisions nor may opposing counsel accede or agree to such provisions.
Paragraph (A) permits a restrictive covenant in a law corporation, partnership, or employment agreement. *The law corporation shareholder, partner, or associate may agree not to have a separate practice during the existence of the relationship; however, upon termination of the relationship (whether voluntary or involuntary), the member is free to practice law without any contractual restriction except in the case of retirement from the active practice of law.* (Amended by order of Supreme Court, operative September 14, 1992.)

Ronald Jones, Florida

I had a friend some years ago who got into a fee dispute with her old law firm. She lost the case (wish I could find the cite). I'm sure this varies by state, and CA would probably be harder on attorney fee agreements than VA, but the gist of the case was that although the firm couldn't prevent my friend from taking clients with her, the old firm *was* entitled to some compensation from fees realized after she left the firm if work was done on the case before she left. In my friend's case, the fee in the agreement was a sliding scale based on how far the case had advanced by the time she left. The court was basically permitting a quantum meruit claim by the former firm. Not sure how a fixed 75% of fee would hold up though.

Kevin Grierson, Virginia

This is an impermissible restrictive covenant and would be against public policy in most (if not all) states. If the law firm is an international one, then it is possible the agreement just included their standard language (for example, British law firms put in non-competes for their associates around the world).

There is a bigger issue that your friend may have broken the ethical rules by signing the agreement in the first place, so she should tread carefully.

Cannot believe a law firm would do something like this - how sleazy!

Regards,

Murtaza Sutarwalla, Texas

I think a distinction needs to be made between new matters that begin after an attorney leaves a firm, and matters that are opened while at the old firm, particularly if significant work is done. Two examples:

1. Lawyer brings client with her to new firm after matter concluded. Client calls lawyer up for new matter not handled by old firm (say, a will). I don't think the old firm can collect here.

2. Lawyer begins work on PI case at old firm. Takes matter through filing suit, and discovery. Lawyer leaves firm, client comes with her, and a week later the case settles. In this case, I think a contractual provision indicating that some portion of the attorneys fee must be paid to the old firm would be upheld in most states.

Regarding the second example, I think a contrary holding would encourage lawyers to pick up and leave a firm if they pick up a really big case so they don't have to share the proceeds.

kwg

Kevin W. Grierson

I think many states have a prohibition on non-competes by attorneys and this seems to be a way to avoid. I see a large issue with client consent and getting around that issue.

If friend is planning to leave, or has, may want to point out the problems and ask that they rescind it as to her. If not, she may need to file a declaratory judgment action to determine the enforceability of the agreement. If she can find anyone that left and paid over fees, they may prove to be an ally if it means they can claw back some of what was paid.

A strong demand up front may be enough for the firm to rescind the agreement as to her in order to save face and prevent the agreement becoming a nullity for all time. The firm would need to weigh the likelihood of her taking clients from them.

Phil A. Taylor, Massachusetts

David, this does not seem like a non-compete per say (as everyone noted, generally speaking, attorneys are not subject to non-competes).

However, I believe point 2, about sharing fees, is valid. Maybe an exception could exist where the departed attorney used work product it created during her time at the firm to service the client in the attorney's new position. Though, the agreement should have to spell this out.

My sense is that this would be invalidated, but the existence of such an agreement gives the old firm a ticket to go to court and drag the attorney through distracting litigation. If your friend does not mind rocking the boat a bit, she could ask for an advisory ethics opinion from the bar association on this (maybe even anonymously).

Roman R. Fichman

Here in Indiana we had an interesting (unpublished) opinion on a similar issue just last week.

http://www.in.gov/judiciary/opinions/pdf/08271402jgb.pdf

In short, it appears the law firm lost its case to take fees from the leaving attorney because the trial judge found they weren't unjustly enriched where they made (literally) millions more off of the attorney's work and cases than they paid him (4X more in one year than they paid him in the whole 3 years).

Kind of an interesting read, I thought.

Also, there was a recent disciplinary case in Indiana on similar facts - lawyer requiring the agreement was given a public reprimand for using it.

http://www.in.gov/judiciary/opinions/pdf/04291401per.pdf

Sincerely,

Aaron M. Cook, Indiana

I don't think it would fly here at all, based on 1) the bar on non-competes for lawyers, and 2) the restrictions on fee sharing; the fee goes to whomever actually worked the matter for the client and assumed professional liability (which is almost exclusively personal, and not imputed to the firm unless there's evidence of cultural or managerial inducement to the malpractice).

-Rick

Richard J. Rutledge, Jr., North Carolina

Have you looked lately at Edwards v Arthur Andersen, LLP (2008) 44 Cal4th
937?

In that case, the Supreme Court got very upset with a non-solicitation
agreement required of an accountant (which the Court characterized as a
non-compete). The Court also stated that "partial restraints" we're not
permissible in California in light of the prohibition on non-competes.

While your friend's situation is not identical, I suspect a court (and
quite probably the Bar) would see it as analogous. In practical effect, it
is a non-compete coupled with a liquidated damages clause for violation.

Brian Cole, California

Thanks everyone! This is solid gold. I will forward the responses to my
friend. She's still very early in her career and was worried. I think your
responses will set her mind at ease quite a bit.

Cheers,

David Allen Hiersekorn, California

Stephanie Hill can weigh in - she's got way more experience here than I do - but I don't think this would fly in MN. Its EFFECT is to deny clients the right to choose their attorney (down it goes) and it is in effect a noncompete.

Her best bet, though, is to file an ethics complaint with the state. She can't fight the big firm. State ethics can and probably will.

Larry Frost, Minnesota

I should not have said file a complaint with State Ethics; file the facts and ask for a determination letter, Q: Is this employment agreement in violation of (inster number of CA ethics rule against denying clients free choice of attorney) or is this a noncompete in violation of any state ethics rule.

This avoids her having to 'complain' about her company (she can even file it w/o old firm name) but if the results are as we expect, she can proceed with or witout notifying old firm in some confidence she will win if they come after her.

Larry Frost

Great idea, Larry. If she can get an opinion it's a great solution.

Kevin W. Grierson