LOS ANGELES COUNTY BAR ASSOCIATION
PROFESSIONAL RESPONSIBILITY AND ETHICS COMMITTEE

FORMAL OPINION NO. 480: March 7, 1995

SUMMARY

RESTRICTION ON LAWYER COMPETITION -- A law partnership agreement may impose a reasonable cost on departing partners who compete with the law firm in a limited geographical area, and this does not violate Rule 1-500 of the Rules of Professional Conduct.

AUTHORITIES CITED:

Howard v. Babcock, 6 Cal.4th 409 (1993)
Haight, Brown & Bonesteel v. Superior Court, 234 Cal.App.2d 963 (1991)
Champion v. Superior Court, 201 Cal.App.3d 777 (1988)
Fox v. Abrams, 163 Cal.App.3d 610 (1985)
Jewel v. Boxer, 156 Cal.App.3d 171 (1984)
Fracasse v. Brent, 6 Cal.3d 784 (1972)
Rules of Professional Conduct 1-500, 2-200, and 4-200
Business & Professions Code §§16600, *et seq.*

A law partnership has asked for our opinion on the following provision from their partnership agreement:

> "If any Partner withdraws from the Partnership and is thereafter engaged to render legal services for any individual or entity which has received legal services from the Partnership within the twelve months immediately preceding said withdrawal, said Partner shall pay to the Partnership a consulting fee in a sum which is equal to twenty-five percent (25%) of the total of all legal fees collected from that individual or entity for services rendered during the twelve (12) months immediately following that Partner's withdrawal from the Partnership."

This provision appears modeled on the partnership provision ruled upon in Champion v. Superior Court, 201 Cal.App.3d 777 (1988). Although this issue now is controlled by Howard v. Babcock, 6 Cal.4th 409 (1993) and Haight, Brown & Bonesteel v. Superior Court, 234 Cal.App.2d 963 (1991), we begin our analysis with Champion.

The court in Champion pointed to three different rules that might be violated by a provision of the kind we face. These are Rules 2-107 (now Rule 4-200) which prohibit members from entering into agreements for, charging, or collecting any illegal or unconscionable fee; Rule 2-108 (now Rule 2-200) which restricts fee splitting between lawyers; and Rule 2-109 (now Rule 1-500) which prohibits agreements restricting the right of an attorney to practice law. The Champion court found that the unconscionability rule was dispositive of the provision before the Court, so it did not reach the issues of fee splitting and restriction of an attorney's right to practice law.

The Champion court pointed out the client's absolute power to discharge an attorney, with or without cause, and the closely related client's right to retain counsel of choice. The provision in question in this Opinion would permit the client to elect representation by a withdrawing partner but effectively restricts that right by the burden placed on the withdrawing partner; this provision requires the 25% consulting fee without regard to the amount of work, if any, performed by the firm.

The fee is not intended as compensation for services rendered. The nature of the consulting fee and the inquiry show that the consulting fee is designed to satisfy the partnership's desire to protect its expected profits, based on the assumption that the client relationship is an asset of the firm. However, the consulting fee applies without regard to the partnership's, or the withdrawing partner's, relationship with the client. For example, it might provide compensation to the partnership even if the client previously had terminated its attorney-client relationship with the partnership because of dissatisfaction with the work of the remaining partners. Similarly, it would apply to fees collected from clients whose relationship with the withdrawing partner preceded his or her relationship to the firm. Saying that it was motivated ". . . by public policy, which urges us to protect the interests of the partnership's former clients." (201 Cal.App.3d at 783), the Champion court invalidated the 25% consulting fee.

The court in Champion pointed out that the partnership is put to an election by the decision of a partner to withdraw. A withdrawing partner may represent a former client under the same terms as would an attorney who had never been a partner, controlled only by the *quantum meruit* requirement of Fracasse v. Brent, 6 Cal.3d 784 (1972), that he or she reimburse the partnership for its contribution to the case. If a partner leaves with less than his or her share of the lucrative cases, this approach is better for the partnership than a dissolution and still protects the clients' interests. If a partner withdraws taking more than his or her share of the lucrative cases, the partnership can achieve a more

favorable result by electing to dissolve and wind up its financial affairs under the principles of Fox v. Abrams, 163 Cal.App.3d 610 (1985) and Jewel v. Boxer, 156 Cal.App.3d 171 (1984). These cases apply a principle of partnership law that, absent an agreement to the contrary, no partner is entitled to extra compensation for services rendered in completing unfinished business of the partnership:

> "The former partners will receive, in addition to their partnership portion of such income, their partnership share of income generated by the work of the other former partners, without performing any post dissolution work on those cases. On balance, the allocation of fees according to each partner's interest in the former partnership should not work an undue hardship as to any partner where each partner completes work on the partnership's cases which are active upon its dissolution." Jewel, supra, 156 Cal.App.3d at 179.

The court in Jewel noted two basic fiduciary obligations of former partners, the duty to wind up and complete the unfinished business of the dissolved partnership, and the principle that no former partner may take any action with respect to unfinished business which leads to purely personal gain (Ibid.). Under these principles, the former partners are obligated to insure that a disproportionate burden of completing unfinished business does not fall on one former partner or one group of former partners (Ibid.). Thus, the partnership controls the decision whether to permit the withdrawing partner to represent the clients as would a stranger to the partnership or to wind up the partnership with a sharing of the fees and of the work on the unfinished cases. The recent opinion of the California Supreme Court in the Howard case takes a completely different approach. Without citing the Champion case, the court concludes that there is no reason to distinguish the legal profession from all other professions, which already are subject to the general rule that a partnership agreement may provide against competition by withdrawing partners in a limited geographical area. See Business & Professions Code §§16600, *et seq.* The court cites with approval the analysis of the Haight case that the validity of the non-competition agreement depends on whether it "amounts to an agreement for liquidated damages or an agreement resulting in a forfeiture." Haight, supra, at 972.

The Court stated: "We hold that an agreement among partners imposing a reasonable cost on departing partners who compete with the law firm in a limited geographical area is not inconsistent with rule 1-500 and is not void on its face as against public policy." Howard, supra, at 425.

The Court goes on to explain that an absolute ban on competition with the partnership would be *per se* unreasonable and inconsistent with the legitimate concerns of assuring client choice of counsel and assuring attorneys of the right to practice their profession. This results in an analysis comparable to a traditional liquidated damage analysis in which trial courts will be required to distinguish between a reasonable cost, that would be enforceable, and an excessive cost, that would be categorized as an unenforceable penalty.

The partnership agreement in Howard provided for a forfeiture of all withdrawal benefits, other than the right to a return of capital, if more than one partner or associate withdrew from the firm before the age of 65 and within one year thereafter engaged in the practice of law within Los Angeles or Orange Counties in the firm's specialty of liability insurance defense work.[1] This was a forfeiture only, and did not involve any payments from the former partners to the firm, so the court therefore was not required to deal with Rule 2-200 or Rule 4-200.

If the partnership imposes only reasonable costs on the departing partner the agreement will be enforceable under B&P C. §§16600, *et seq.* If so, it appears from the opinion in Howard that the agreement is not subject to analysis under concepts of fee splitting or of unconscionable fees (but we cannot conclude this with certainty from the opinion in Howard because it deals only with a limited forfeiture of economic rights). If the partnership agreement does not survive analysis under B&P C. §§16600 *et seq.,* then the attorneys involved may face Rules 1-500, 2-200, and 4-200.

We finally conclude that in the absence of a partnership agreement that imposes only reasonable costs on former partners who compete with the partnership, the relationship between the partnership and its former partners will continue to be governed by the traditional partnership analysis of Fracasse v. Brent, supra, Fox v. Abrams, supra, and Jewel v. Boxer, supra.

This opinion is advisory only. The Committee acts on specific questions submitted *ex parte* and its opinion is based on such facts only as are set forth in the inquiry submitted.

[1] The Haight opinion, which was approved in Howard, validated a partnership provision under which the departing partner also forfeited his capital in the partnership.