

COMMISSION PROVISIONAL REPORT AND RECOMMENDATION: RULE 1.5 [4-200]

Commission Drafting Team Information

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I. CURRENT CALIFORNIA RULE

Rule 4-200 Fees for Legal Services

- (A) A member shall not enter into an agreement for, charge, or collect an illegal or unconscionable fee.
- (B) Unconscionability of a fee shall be determined on the basis of all the facts and circumstances existing at the time the agreement is entered into except where the parties contemplate that the fee will be affected by later events. Among the factors to be considered, where appropriate, in determining the conscionability of a fee are the following:
 - (1) The amount of the fee in proportion to the value of the services performed.
 - (2) The relative sophistication of the member and the client.
 - (3) The novelty and difficulty of the questions involved and the skill requisite to perform the legal service properly.
 - (4) The likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the member.
 - (5) The amount involved and the results obtained.
 - (6) The time limitations imposed by the client or by the circumstances.
 - (7) The nature and length of the professional relationship with the client.
 - (8) The experience, reputation, and ability of the member or members performing the services.
 - (9) Whether the fee is fixed or contingent.
 - (10) The time and labor required.
 - (11) The informed consent of the client to the fee.

II. FINAL VOTES BY THE COMMISSION AND THE BOARD

Commission:

Date of Vote: January 20 & 21, 2017

Action: Recommend Board Adoption of Proposed Rule 1.5 [4-200]

Vote: 14 (yes) – 0 (no) – 0 (abstain)

Board:

Date of Vote: March 10, 2017

Action: Board Adoption of Proposed Rule 1.5 [4-200]

Vote: X (yes) – X (no) – X (abstain)

III. COMMISSION'S PROPOSED RULE 1.5 [4-200] (CLEAN)

Rule 1.5 [4-200] Fees for Legal Services

- (a) A lawyer shall not make an agreement for, charge, or collect an unconscionable or illegal fee.
- (b) Unconscionability of a fee shall be determined on the basis of all the facts and circumstances existing at the time the agreement is entered into except where the parties contemplate that the fee will be affected by later events. The factors to be considered in determining the unconscionability of a fee include without limitation the following:
 - (1) whether the lawyer engaged in fraud* or overreaching in negotiating or setting the fee;
 - (2) whether the lawyer has failed to disclose material facts;
 - (3) the amount of the fee in proportion to the value of the services performed;
 - (4) the relative sophistication of the lawyer and the client;
 - (5) the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly;
 - (6) the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer;
 - (7) the amount involved and the results obtained;
 - (8) the time limitations imposed by the client or by the circumstances;
 - (9) the nature and length of the professional relationship with the client;

- (10) the experience, reputation, and ability of the lawyer or lawyers performing the services;
 - (11) whether the fee is fixed or contingent;
 - (12) the time and labor required;
 - (13) whether the client gave informed consent* to the fee.
- (c) A lawyer shall not make an agreement for, charge, or collect:
- (1) any fee in a family law matter, the payment or amount of which is contingent upon the securing of a dissolution or declaration of nullity of a marriage or upon the amount of spousal or child support, or property settlement in lieu thereof; or
 - (2) a contingent fee for representing a defendant in a criminal case.
- (d) A lawyer may make an agreement for, charge, or collect a fee that is denominated as “earned on receipt” or “non-refundable,” or in similar terms, only if the fee is a true retainer and the client agrees in writing* after disclosure that the client will not be entitled to a refund of all or part of the fee charged. A true retainer is a fee that a client pays to a lawyer to ensure the lawyer’s availability to the client during a specified period or on a specified matter, but not to any extent as compensation for legal services performed or to be performed.
- (e) A lawyer may make an agreement for, charge, or collect a flat fee for specified legal services. A flat fee is a fixed amount that constitutes complete payment for the performance of described services regardless of the amount of work ultimately involved, and which may be paid in whole or in part in advance of the lawyer providing those services.

Comment

Prohibited Contingent Fees

[1] Paragraph (c)(1) does not preclude a contract for a contingent fee for legal representation in connection with the recovery of post-judgment balances due under child or spousal support or other financial orders.

Payment of Fees in Advance of Services

[2] Rule 1.15(a) and (b) govern whether a lawyer must deposit in a trust account a fee paid in advance.

[3] When a lawyer-client relationship terminates, the lawyer must refund the unearned portion of a fee. See Rule 1.16(e)(2).

Division of Fee

[4] A division of fees among lawyers is governed by Rule 1.5.1.

Written Fee Agreements

[5] Some fee agreements must be in writing* to be enforceable. See, e.g., Business and Professions Code §§ 6147 and 6148.

IV. COMMISSION'S PROPOSED RULE 1.5 [4-200] (REDLINE TO CURRENT CALIFORNIA RULE 4-200)

Rule 1.5 [4-200] Fees for Legal Services

- (Aa) A ~~member~~lawyer shall not ~~enter into~~make an agreement for, charge, or collect an ~~illegal or~~ unconscionable or illegal fee.
- (Bb) Unconscionability of a fee shall be determined on the basis of all the facts and circumstances existing at the time the agreement is entered into except where the parties contemplate that the fee will be affected by later events. ~~Among the~~The factors to be considered, ~~where appropriate,~~ in determining the ~~conscionability~~unconscionability of a fee ~~are~~include without limitation the following:
- (1) whether the lawyer engaged in fraud* or overreaching in negotiating or setting the fee;
 - (2) whether the lawyer has failed to disclose material facts;
 - (13) ~~The~~the amount of the fee in proportion to the value of the services performed~~;~~;
 - (24) ~~The~~the relative sophistication of the ~~member~~lawyer and the client~~;~~;
 - (35) ~~The~~the novelty and difficulty of the questions involved~~,~~, and the skill requisite to perform the legal service properly~~;~~;
 - (46) ~~The~~the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the ~~member~~lawyer~~;~~;
 - (57) ~~The~~the amount involved and the results obtained~~;~~;
 - (68) ~~The~~the time limitations imposed by the client or by the circumstances~~;~~;
 - (79) ~~The~~the nature and length of the professional relationship with the client~~;~~;
 - (810) ~~The~~the experience, reputation, and ability of the ~~member or members~~lawyer or lawyers performing the services~~;~~;

(911) ~~Whether~~whether the fee is fixed or contingent-;

(4012) ~~The~~the time and labor required-;

(14) ~~The~~13) whether the client gave informed consent ~~of the client*~~ to the fee.

(c) A lawyer shall not make an agreement for, charge, or collect:

(1) any fee in a family law matter, the payment or amount of which is contingent upon the securing of a dissolution or declaration of nullity of a marriage or upon the amount of spousal or child support, or property settlement in lieu thereof; or

(2) a contingent fee for representing a defendant in a criminal case.

(d) A lawyer may make an agreement for, charge, or collect a fee that is denominated as "earned on receipt" or "non-refundable," or in similar terms, only if the fee is a true retainer and the client agrees in writing* after disclosure that the client will not be entitled to a refund of all or part of the fee charged. A true retainer is a fee that a client pays to a lawyer to ensure the lawyer's availability to the client during a specified period or on a specified matter, but not to any extent as compensation for legal services performed or to be performed.

(e) A lawyer may make an agreement for, charge, or collect a flat fee for specified legal services. A flat fee is a fixed amount that constitutes complete payment for the performance of described services regardless of the amount of work ultimately involved, and which may be paid in whole or in part in advance of the lawyer providing those services.

Comment

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[2] Rule 1.15(a) and (b) govern whether a lawyer must deposit in a trust account a fee paid in advance.

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Division of Fee

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Written Fee Agreements

[5] Some fee agreements must be in writing* to be enforceable. See, e.g., Business and Professions Code §§ 6147 and 6148.

V. RULE HISTORY

Current Rule 4-200 became operative on September 14, 1992. The Model Rule counterpart is ABA Model Rule 1.5. The rule regulates fee arrangements between lawyers and their clients.¹

The predecessor to current Rule 4-200, former Rule 2-107, was originally approved and became operative on January 1, 1975, under the same title “Fees for Legal Services.” That rule was based on Disciplinary Rule (DR) 2-106 of the ABA Model Code of Professional Responsibility. DR 2-106 had three subparagraphs. DR 2-106(A) prohibited a lawyer from entering into an agreement for, charging or collecting an “illegal” or “clearly excessive” fee. DR 2-106(B) stated a fee is “clearly excessive” when a lawyer of ordinary prudence had a “definite and firm conviction that the fee is ***in excess of a reasonable fee.***” (Emphasis added). DR 2-106(B) also provided eight factors to be considered in determining the “reasonableness” of a fee.² DR 2-106(C)

¹ Fee arrangements are also regulated by: rule 2-200 [1.5.1] concerning agreements to divide fees among lawyers who are not in the same law firm; rule 3-300 [1.8.1] concerning agreements between a lawyer and a client that confer on the lawyer an ownership, possessory, security, or other pecuniary interest adverse to a client; and Business and Professions Code §§ 6147 and 6148 concerning the minimum requirements necessary for a contingency fee or other fee contract (hourly, flat fee, etc.), respectively.

² The eight factors were:

- (1) The time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly.
- (2) The likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer.
- (3) The fee customarily charged in the locality for similar legal services.
- (4) The amount involved and the results obtained.
- (5) The time limitations imposed by the client or by the circumstances.
- (6) The nature and length of the professional relationship with the client.
- (7) The experience, reputation, and ability of the lawyer or lawyers performing the services.
- (8) Whether the fee is fixed or contingent.

prohibited a lawyer from entering into an agreement for, charging, or collecting a contingent fee for representing a defendant in a criminal case.

Although former Rule 2-107 was derived from the ABA Code, section (B) of the ABA Code provision was revised by the State Bar Special Committee to Study the ABA Code of Professional Responsibility to reflect California Supreme Court case law that had previously rejected a “reasonable fee” standard in discipline cases. In *Herrscher v. State Bar* (1934) 4 Cal.2d 399, a case seeking disbarment of an attorney for, in part, charging his client exorbitant fees, the California Supreme Court stated:

We think the proper rule in such cases is that the mere fact that a fee is charged in excess of the reasonable value of the services rendered will not of itself warrant discipline of the attorney involved. Ordinarily, the propriety of the fee charged should be left to the civil courts in a proper action.

4 Cal.2d at 402. The *Herrscher* court noted, however, that in some cases a gross overcharge may constitute an offense warranting discipline. In fact, an earlier California Supreme Court decision stated the rule as follows:

Although we are of the opinion that usually the fees charged for professional services may with propriety be left to the discretion and judgment of the attorney performing the services, we are of the opinion that if a fee is charged so exorbitant and wholly disproportionate to the services performed as to shock the conscience of those to whose attention it is called, such a case warrants disciplinary action by this court.

Goldstone v. State Bar (1931) 214 Cal. 490, 498.

In light of the foregoing Supreme Court precedent, the Special Committee substituted an unconscionability standard for the ABA Code’s “clearly excessive [of a reasonable fee]” standard. Paragraph (B) stated a fee “is unconscionable when it is so exorbitant and wholly disproportionate to the services performed as to shock the conscience of lawyers of ordinary prudence practicing in the same community.” Curiously, there was a disjunction between the first and the second and third sentences of paragraph (B), i.e., despite the substitution of the unconscionability standard, paragraph (B) also listed factors to be considered when determining the “reasonableness of a fee.”³

³ The second and third sentences of paragraph (B) provided:

Reasonableness shall be determined on the basis of circumstances existing at the time the agreement is entered into except where the parties contemplate that the fee will be affected by later events. Among the factors to be considered, where appropriate, in determining the *reasonableness* of a fee are the following:

(1) The novelty and difficulty of the questions involved and the skill requisite to perform the legal service properly.

(2) The likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer.

The Special Committee declined to recommend paragraph (C) of DR 2-107, which provided: “A lawyer shall not enter into, charge, or collect a contingent fee for representing a defendant in a criminal case.”

Former Rule 2-107 was amended in 1989 as part of the comprehensive study and revision of the Rules of Professional Conduct. The amendments included changing the numbering of the rule from 2-107 to 4-200 and deleting the references to “reasonableness” that had been retained in former Rule 2-107(B). The change was implemented because of Rule 2-107(B)’s aforementioned conflict in containing two inconsistent standards, unconscionability and unreasonableness:

1. The unconscionability standard reflects existing California Supreme Court decisions to the effect that the State Bar has no power to regulate the amount of the fees charged by its members unless such fees are so “outlandish” or the conduct of the attorney in negotiating for or attempting to collect a fee merit discipline. (See Code. Civ. Proc., § 1021.)
2. A fee structure based upon “reasonableness” necessarily implies both the existence and knowledge of an agreed upon standard against which particular fees can be judged. Such a standard could not be developed or communicated without violating federal antitrust laws.
3. At the present time, a client having a fee dispute with a member may require the member to submit the dispute to arbitration under California’s Fee Arbitration Program. (See Bus. & Prof. Code, § 6200 et seq.) The arbitration procedure does not, per se, involve a threat or risk of disciplinary proceedings. If clients were able to use the threat of disciplinary action simply by alleging that the member’s fees were “unreasonable,” members of the State Bar would be placed in an unwarranted disadvantage in fee dispute resolution.

(3) The amount involved and the results obtained.

(4) The time limitations imposed by the client or by the circumstances.

(5) The nature and length of the professional relationship with the client.

(6) The experience, reputation, and ability of the lawyer or lawyers performing the services.

(7) Whether the fee is fixed or contingent.

(8) The time and labor required.

(9) The informed consent of the client to the fee agreement. (Emphasis added).

The Special Committee did delete the ABA Code factor, “the fee customarily charged in the locality for similar legal services,” which traditionally is an indicator of whether a fee is *reasonable*, but it is not apparent why the “reasonableness” standard was retained in the second sentence of the rule 2-107(B).

(See Request that the Supreme Court of California Approve Amendments to the Rules of Professional Conduct of the State Bar of California, and Supplemental Memorandum and Supporting Documents in Explanation, Supreme Court Case No. Bar. Misc. 5626, pp. 43-44 (September 1988) (“1998 Report”)).

In addition to removing the word “reasonableness,” subparagraphs (B)(1) and (2) were added as factors because it was believed they were important factors to be considered in determining the conscionability of a fee.⁴

Rule 4-200 was amended again in 1992. The amendments included removing the word “agreement” from paragraph (B) and subparagraph (B)(11). These amendments were intended to: (1) clarify that paragraph (B) addressed the broad issue of the unconscionability of the fee obtained as opposed to the narrower issue of the unconscionability of the fee agreement itself; and (2) conform paragraph (B) and subparagraph (B)(11) to the text of paragraph (A) which refers to the amount of the fee, not the fee agreement. (Supreme Court Case No. SO24408 p. 18.)

VI. OCTC / STATE BAR COURT COMMENTS

- **Gregory Dresser, Office of Chief Trial Counsel, 9/27/2016**
(In response to 90-day public comment circulation):

1. Unconscionable Fees. OCTC finds the term “unconscionable fee” vague, difficult to understand, confusing, and very difficult to enforce. Moreover, there is no reason for California to use a different term than the rest of the country.
2. The term “unconscionable fees” is meant to refer to the common law doctrine of unconscionability of contracts. (See *Cotchett, Pitre & McCarthy v. Paragon Corp* (2010) 187 Cal.App.4th 1405, 1419.) It is often misinterpreted, however, to have a more generalized meaning and to create a much higher burden for the State Bar than is required.⁵ Consequently, OCTC has great difficulty in obtaining culpability under the current language, even in egregious cases.
3. The term “unconscionable fees” comes from a Supreme Court case finding that

⁴ The two added factors to be considered in determining whether a fee is “unconscionable” were:

- (1) The amount of the fee in proportion to the value of the services performed.
- (2) The relative sophistication of the member and the client.

⁵ The State Bar need not establish that the attorney acted “*knowingly*” or “*intentionally*” to establish a rule 4-200 violation. All that the State Bar must prove is that the attorney acted willfully — that the attorney acted or failed to act purposefully or, stated differently, that the attorney intended to commit the act or intended not to commit the act. (*In the Matter of Silverton* (Review Dept. 2004) 2004 WL 60709, reversed on other grounds, *In re Silverton* (2005) 36 Cal.4th 81.)

an attorney could in some situations be disciplined for excessive fees. (See *In re Goldstone* (1931) 214 Cal. 490, 498-499; *Bushman v. State Bar* (1974) 11 Cal.3d 558.) This was before there was a Rule of Professional Conduct addressing this type of conduct. It appears to be based on a violation of section 6106. But not every unconscionable fee constitutes an act of moral turpitude. (See *In re Silverton* (2005) 36 Cal.4th 81, 86 [rule 4-200 found but no moral turpitude found].) The ABA's term, which is followed by most other jurisdictions, is that the fee must not be unreasonable, using similar factors that are used in California's rule. The ABA's term is consistent with California law, which provides that "[a]ttorney fee agreements ... must be fair, reasonable and fully explained to the client." (*In the Matter of Kroff* (Review Dept. 1998) 3 Cal. State Bar Ct. Rptr. 838, 851. See also *In re Silverton* (2005) 36 Cal.4th 81, 86 ["Although Silverton was 'entitled to contract for, charge, and collect a reasonable fee for providing that service,' he 'did not do so.' He unequivocally contracted for a 100 percent contingency fee of any reduction he was able to negotiate. At least within the context of the present case, that fee is clearly unreasonable, unconscionable, and improper."]; and sections 6147 and 6148. Thus, this change is necessary to address developments in the law, and eliminate, where possible, any unnecessary differences between California's rules and those used by a preponderance of the states.

4. OCTC also urges the Commission to consider adding an additional factor to the list set forth in subsection (b): whether the services are legal in nature and whether the attorney charges the client for clerical or non-legal services at the same rate as legal services. Other states have disciplined attorneys for charging the same fee for these non-legal services at the legal services rate. (See e.g. *In re Green* (Co. 2000) 11 P.3d 1078 [charging lawyer's rate for faxing documents, etc.]; *Prof'l Ethics & Conduct of Iowa State Bar v. Zimmerman* (Iowa 1991) 465 N.W.2d 288 [lawyer charged full hourly rate for attending ward's birthday party and discussing toiletry needs]; *Cincinnati Bar Ass'n v. Alsfelder* (Ohio 2004) 816 N.E.2d 218 [charging for discussions and advice about boyfriends, vehicles, and restaurants].)
5. OCTC supports proposed subparagraphs (c), (d), and (e). It is well established that only a true retainer to secure an attorney's availability over time is non-refundable. This is because it is considered earned when paid. Advanced fees, however, no matter how the attorney characterizes them, must be refunded if not earned. A failure to do so is disciplinable. (See *In the Matter of Lais* (Review Dept. 1998) 3 Cal. State Bar Ct. Rptr. 907; *In the Matter of Phillips* (Review Dept. 2001) 4 Cal. State Bar Ct. Rptr. 315; *In the Matter of Fonte* (Review Dept. 1994) 2 Cal. State Bar Ct. Rptr. 752; *Matthew v. State Bar* (1989) 49 Cal.3d 984.) Flat fees also must be earned by performance of services. Any attempt to deal with the issue of creditor rights and government forfeiture rules, as proposed by some of the other commenters, is beyond the scope of the Rules of Professional Conduct.

6. OCTC recommends that the rule be amended to make the failure to have a written fee agreement disciplinable. Other jurisdictions discipline attorneys for failing to have a written fee agreement with the client. (See e.g. *In re Fink* (Vt. 2011) 22 A3d 461, 478-479.) Written fee agreements protect the public and are an integral part of an attorney's duty to communicate significant developments relating to his or her employment. (Rule 3-500; Business and Professions Code section 6068(m).) Disclosure of the terms of the agreement should be in writing, because it protects both the attorney and the client, and the client should not be expected to mentally retain such information throughout the pendency of the client's case. (See *Chambers v. Kay* (2002) 29 Cal.4th 142, 157.) Moreover, California law now requires that most fee agreements be in writing. (*Hawk v. State Bar* (1988) 45 Cal.3d 589, 606; Business and Professions Code sections 6147 and 6148.) In *In the Matter of Harney* (Review Dept. 1995) 3 Cal. State Bar Ct. Rptr. 266, 278-280, the Review Department found that failing to have a written agreement as required by sections 6147 and 6148 is not a disciplinable offense.⁶ Most clients will not be aware of their civil remedies when an attorney fails to provide a written fee agreement. (See Business and Professions Code sections 6147 and 6148.) Further, utilizing solely criminal and civil remedies to regulate attorney conduct is inadequate to protect the public from errant attorneys. (See *In Re Attorney Discipline* (1998) 19 Cal.4th 582, 608- 609.) Also, proposed rule 1.5.1 requires that fee sharing agreements between attorneys be in writing and the failure to do so constitutes a basis for discipline. The same should apply to fee agreements between attorneys and clients. There is no principled reason for this difference.
7. OCTC believes that Comment 1 should be in the rule, not a Comment.
8. Comments 2 and 3 seem unnecessary because these Comments are merely duplicative of the rule.

- **Gregory Dresser, Office of Chief Trial Counsel, 1/9/2017**
(In response to 45-day public comment circulation):

For the 45-day public comment version of the rule, OCTC re-submitted substantially the same comments as on the 90-day public comment version of the rule and the Commission's responses to OCTC remained the same. See 90-Day and 45-Day Public Comment Synopsis Tables, Attachments _____ and _____.

- **State Bar Court:** No comments were received from State Bar Court.

⁶ Although the Review Department decided in *Harney* that violations of section 6147 and 6148 were not a disciplinable offense, it found that this was a very close question. Moreover, the Review Department used Harney's failure to provide his clients with a written fee agreement as an aggravating circumstance showing harm and required Harney as a condition of probation to provide a certain class of his clients with written fee agreements.

VII. PUBLIC COMMENTS & PUBLIC HEARING TESTIMONY

Four comments, including the above comment from OCTC, were received. Two agreed with the proposed rule. One disagreed, and one agreed only if modified. A public comment synopsis table, with the Commission's responses to each comment, is provided at the end of this report.

One speaker appeared at the public hearing whose testimony was in support of the proposed rule if modified.

VIII. RELATED CALIFORNIA LAW AND ABA MODEL RULE ADOPTIONS

The ABA State Adoption Chart for the ABA Model Rule 1.5, which is the counterpart to current rule 4-200, is posted at:

- http://www.americanbar.org/content/dam/aba/administrative/professional_responsibility/mrpc_1_5.pdf
- Four states have adopted Model Rule 1.5 verbatim.⁷ Eighteen jurisdictions have adopted a slightly modified version of Model Rule 1.5.⁸ Twenty-nine states have adopted a version of the rule that is substantially different to Model Rule 1.5."⁹
- However, as discussed in Section IX.A.1, below, only four jurisdictions besides California have rejected the Model Rule's "unreasonable" standard.

IX. CONCEPTS ACCEPTED/REJECTED; CHANGES IN DUTIES; NON-SUBSTANTIVE CHANGES; ALTERNATIVES CONSIDERED

A. Concepts Accepted (Pros and Cons):

1. Retain the standard in current rule 4-200, i.e., unconscionability as opposed to Model Rule 1.5's "unreasonable" standard.
 - Pros: First, retaining the unconscionability standard will carry forward the public policy rationale stated over 80 years ago by the Supreme Court in *Herrscher v. State Bar* (1934) 4 Cal.2d 399, 402-403 [49 P.2d 832]:

⁷ The four states are: New Mexico, Rhode Island, South Dakota, and Utah.

⁸ The eighteen jurisdictions are: Delaware, District of Columbia, Hawaii, Idaho, Illinois, Indiana, Iowa, Maryland, Mississippi, Missouri, Montana, Nebraska, New Jersey, Oklahoma, Tennessee, Vermont, West Virginia, and Wyoming.

⁹ The twenty-nine states are: Alabama, Alaska, Arizona, Arkansas, California, Colorado, Connecticut, Florida, Georgia, Kansas, Kentucky, Louisiana, Maine, Massachusetts, Michigan, Minnesota, Nevada, New Hampshire, New York, North Carolina, North Dakota, Ohio, Oregon, Pennsylvania, South Carolina, Texas, Virginia, Washington, and Wisconsin.

“In the few cases where discipline has been enforced against an attorney for charging excessive fees, there has usually been present some element of fraud or overreaching on the attorney's part, or failure on the attorney's part to disclose the true facts, so that the fee charged, under the circumstances, constituted a practical appropriation of the client's funds under the guise of retaining them as fees.

Generally speaking, neither the Board of Governors nor this court can, or should, attempt to evaluate an attorney's services in a quasi-criminal proceeding such as this, where there has been no failure to disclose to the client the true facts or no overreaching or fraud on the part of the attorney. *It is our opinion that the disciplinary machinery of the bar should not be put into operation merely on the complaint of a client that a fee charged is excessive, unless the other elements above mentioned are present.*” (Emphasis added) (Citations omitted).

Second, the public is provided sufficient protection against avaricious lawyers who charge “unreasonable” fees through the civil court system and California’s unique system of mandatory fee arbitration. (See Bus. & Prof. Code § 6200 et seq. Put another way, rather than bog down the discipline system with ordinary fee disputes, the law provides a client with other forums, in particular mandatory fee arbitration, to contest an unreasonable fee. In any event, in extreme cases such as those described above, the public is further protected through imposing discipline on lawyers who charge, contract for or collect an unconscionable fee.

Third, this is a disciplinary rule and lawyers should not be disciplined for charging what can be determined in hindsight to have been an “unreasonable” fee. The unconscionable standard provides a clearer disciplinary standard, consistent with the Commission’s charge to draft articulable standards of discipline.

- Cons: The reasonableness standard has been adopted in nearly every jurisdiction.¹⁰ Rejecting an unreasonable standard, which has been adopted in every jurisdiction except California, Massachusetts and Texas, and retaining an unconscionability standard falls short of the Commission’s charge to protect the public and promote confidence in the legal profession and administration. It sends a message that the profession tolerates its members charging an unreasonable fee. This is an area where the Commission should reassess the continued viability of *Herrscher*. The concerns the Supreme Court expressed 75 years ago about the efficacy of inquiring into the reasonableness of fees should not control the debate for a self-regulating

¹⁰ Only California, Massachusetts, New York, North Carolina and Texas have not adopted the Model Rules’ standard, the latter four having adopted (or more accurately continued from the ABA Code of Professional Responsibility) an “excessive” or “clearly excessive” standard. Michigan, Ohio and Oregon have also carried forward the “excessive” standard but define “excessive” as in excess of reasonable, so they effectively have adopted a reasonable standard.

profession in this sensitive area of lawyer-client relations.

2. In paragraph (b), retain the 11 factors that are found in current rule 4-200(B) and include two other factors, derived from case law, for determining unconscionability and include in the introduction of paragraph (c) an express statement that the factors are to be considered without limitation. There are 13 factors in the current rule draft and there is a statement that they are to be considered without limitation.
 - Pros: There is no evidence that the factors, which have been included in the rule since 1975, have created a problem or confusion in determining the unconscionability of a fee. The statement that the factors to be considered are without limitation conforms to an OCTC comment received earlier in the Commission's deliberative process. With respect to the similarity of the factors to those used in the Model Rule for determining the reasonableness of a fee, the additional three factors unique to the California rule all relate to unconscionability, (see "Cons"). Further, the consideration of the two additional factors will further distinguish the provision from the Model Rule.
 - Cons: There is some confusion whether the factors can be used to determine unconscionability as they are nearly identical to those stated in Model Rule 1.5 for determining the reasonableness of the fee. The only different factors are: (1) the amount of the fee in proportion to the value of the services performed; (2) the relative sophistication of the client; and (3) the informed consent of the client to the fee.
3. Add new paragraph (c), derived from Model Rule 1.5(d), which identifies two types of contingent fee arrangements that are prohibited: certain family law matters and criminal matters. Drafting team consensus.
 - Pros: Although there are other kinds of contingent fee cases that might be prohibited, the two kinds of cases regulated under Model Rule 1.5(d) have traditionally been viewed as implicating important Constitutional rights or public policy. See, e.g., Restatement (3d) Law of Lawyers § 35, comments f.(i), f.(ii) and g.

In the family law matters, California has a strong public policy of promoting reconciliation and maintaining the family unit. Because a lawyer who is being paid on a contingent basis would recover a fee only if the marriage is dissolved and property apportioned, permitting contingent fees in these cases would undermine the California policy.

In criminal cases, a lawyer who is being paid on a contingent basis would recover a fee only if the client is found not guilty. That would create a conflict for a lawyer if the best interests of the client, in light of the evidence, warrant the client entering a plea.

Focusing on these two types of cases where public policy strongly opposes contingent fees should not lead to an inference that any other kind of contingent fee matter is permitted.

- Cons: Limiting the prohibition on contingent fees to two kinds of legal matters implies that contingent fees are permitted in any other kind of legal matter, which may not be true.
4. Add new paragraph (d), which prohibits denominating a fee as “earned on receipt” or “nonrefundable” except in the case of a true retainer, i.e., where the fee is paid to assure the availability of the lawyer. Drafting team consensus.
- Pros: Paragraph (d) is an attempt to balance a number of competing interests: a lawyer’s interest, on the one hand, of being assured of payment when relinquishing an opportunity for other employment and a client’s interest in not forfeiting a flat fee in the event the client changes his or her mind and wants to discharge the lawyer. At bottom, paragraph (e) recognizes that except under specific circumstances, a flat fee is not earned until services have been provided. Paragraph (e) states the nonrefundable/ earned on receipt fee arrangement that traditionally has been recognized in the profession and is already found in current rule 3-700(D)(2). Paragraph (e) also includes a description of what constitutes a “true retainer” that is more accurate than the language used in current Rule 3-700(D)(2), which simply states that a true retainer is a “fee paid solely for the purpose of ensuring the availability of the member for the matter.”
 - Cons: The proposed new description of “true retainer” differs from the longstanding language used in Rule 3-700(D)(2). There does not appear to be any disciplinary data indicating that this language should be changed.
5. Add new paragraph (e) that expressly provides that a flat fee is permissible only if the lawyer provides the agreed upon services. Drafting team consensus.
- Pros: Expressly states a basic concept in contract law: except for true retainers, an advance fee is not earned unless the lawyer provides the services for which he or she was retained.
 - Cons: Many lawyers, e.g., those in criminal law practice, typically have fee arrangements with clients that are denominated as non-refundable or earned-on-receipt. Their view is that the fee can be placed in the lawyer’s operating account and be protected from forfeiture proceedings. This issue is addressed in proposed Rule 1.15(b).
6. Add new Comment [1], derived from Model Rule 1.5, Cmt. [6], which explains that some contingent fee arrangements related to family law are permitted. Drafting team consensus.

- Pros: Recognizes certain post-judgment contingent fee arrangements in family law that permitted because they do not implicate the policies underlying the prohibition. RRC1 made a similar recommendation.
 - Cons: None identified.
7. Add new Comment [2] which provides a cross-reference to the rule governing a lawyer's duties with respect to handling client funds and property, particularly with respect to advance fees.
- Pros: The cross-references provides important information on the rule that would govern in the event there are unearned fees upon termination or there is a fee dispute, common occurrences in practice.
 - Cons: None identified.
8. Add new Comment [3] which provides a cross-reference to the rule governing a lawyer's duties concerning fees upon termination of the lawyer-client relationship.
- Pros: The cross-reference provides important information on the rule that would govern in the event there are unearned fees upon termination, a common occurrence in practice.
 - Cons: None identified.
9. Add new Comment [4] which provides a cross-reference to the fee splitting rule. Drafting team consensus.
- Pros: In nearly every other jurisdiction, the provision that governs fee divisions among lawyers is in the jurisdiction's counterpart to Model Rule 1.5. In California, the fee division provision is a separate rule. Providing a cross-reference to California's separate rule is appropriate.
 - Cons: None identified.
10. Add new Comment [5], which cross-references Bus. & Prof. Code §§ 6147 and 6148. Drafting team consensus. This concept has been incorporated in Comment [5].
- Pros: In Model Rule 1.5, paragraphs (b) and (c) set forth the requirements for written fee arrangements in general and contingent fee arrangements, respectively. In California, those requirements are addressed in §§ 6148 and 6147, respectively. Under those statutes, the client already has a remedy for a lawyer's violation of the statute: having the contract voided. Sections 6147(b), 6148(c). The drafting team has placed the reference in a comment; it does not believe that a violation of either section should subject a lawyer to discipline under this Rule in addition to the remedy provided in the statute. RRC1 made a similar recommendation.

- Cons: See discussion below in Section IX.B.1 of a concept rejected relating to OCTC's September 2, 2015 memorandum in which OCTC states: "OCTC is not in favor of cross-referencing Business and Professions Code, sections 6147 and 6148. Instead, rule 4-200 should state that a lawyer may be disciplined for failing to have a written fee agreement with the client. Written fee agreements protect the public and are part of a lawyer's duty to communicate significant developments relating to his or her employment."

B. Concepts Rejected (Pros and Cons):

1. Include a prohibition on charging an unconscionable "internal expense".

- Pros: The amount of expenses charged a client can constitute a large part of the client's total monetary obligations to a lawyer. A prohibition on charging an unconscionable expense adds language that clarifies the lawyer's obligation. It should both educate lawyers as to their duties and facilitate the imposition of discipline, where applicable. RRC1 recommended adding a similar prohibition.

The concept of expenses was added to the Model Rules as part of the Ethics 2000 revisions. Only Kansas and Texas do not include an express prohibition on charging unreasonable or excessive expenses.

- Cons: The concept of an unconscionable internal expense would be new and potentially confusing. Conceptually, if a lawyer's internal expense effectively functions as a hidden profit center, then that conduct would fit the existing rubric of an unconscionable fee charged without the client's consent. Compare the existing State Bar Court approach in *In the Matter of Kroff* (Review Dept. 1998) 3 Cal. State Bar Ct. Rptr. 838, at pp. 851-852 [finding that a lawyer's practice of charging a flat periodic fee or lump sum to cover disbursements is not a violation of Rule 4-200 or an act of moral turpitude provided the client consents and the amount at issue is not unconscionable].

2. Include an express definition of "unconscionable fee" in the rule.

- Pros: Presumably, such a definition would provide a succinct explanation of what is meant by the term "unconscionable fee." The language of the definition would be taken from California decisional law, including two Supreme Court cases. See *Herrscher v. State Bar* (1934) 4 Cal.2d 399, 402 [49 P.2d 832]; *Goldstone v. State Bar* (1931) 214 Cal. 490 [6 P.2d 513]. The definition could be used in conjunction with the factors set forth in paragraph (b) as an analytical framework for determining whether a fee is unconscionable.
- A definition of "unconscionable fee" is unnecessary and, in any event, a precise definition of the term is not possible. The phrase "unconscionable fee" is sufficiently defined by case law and has been found not to be unconstitutionally vague. Further, the non-exclusive factors set forth in paragraph (b) provide a sufficient framework for determining the

unconscionability of a fee in the discipline context.

3. Include a provision that addresses modification of fee agreements.

- Pros: A rule that governs fee arrangements is the logical place for such a provision. In fact, RRC1 drafted such a provision at the request of the Board and included it in its proposed Rule 1.5.¹¹ In addition, in OCTC's September

¹¹ RRC1's proposed rule paragraph provided:

(g) A lawyer shall not make a material modification to an agreement by which the lawyer is retained by the client that is adverse to the client's interests unless the client is either represented with respect to the modification by an independent lawyer or is advised in writing by the lawyer to seek the advice of an independent lawyer of the client's choice and is given a reasonable opportunity to seek that advice.

The rule paragraph was accompanied by several comments:

[3] Paragraph (g) imposes a specific requirement with respect to modifications of agreements by which a lawyer is retained by a client, when the amendment is material and is adverse to the client's interests. A material modification is one that substantially changes a significant term of the agreement, such as the lawyer's billing rate or manner in which fees or costs are determined or charged. A material modification is adverse to a client's interests when the modification benefits the lawyer in a manner that is contrary to the client's interest. Increases of a fee, cost, or expense pursuant to a provision in a pre-existing agreement that permits such increases are not modifications of the agreement for purposes of paragraph (g). However, such increases may be subject to other paragraphs of this Rule, or other Rules or statutes.

[3A] Whether a particular modification is material and adverse to the interest of the client depends on the circumstances. For example a modification that increases a lawyer's hourly billing rate or the amount of a lawyer's contingency fee ordinarily is material and adverse to a client's interest under paragraph (g). On the other hand, a modification that reduces a lawyer's fee ordinarily is not material and adverse to a client's interest under paragraph (g). A modification that extends the time within which a client is obligated to pay a fee ordinarily is not material and adverse to a client's interests, particularly when the modification is made in response to a client's adverse financial circumstances.

[3B] In general, the negotiation of an agreement by which a lawyer is retained by a client is an arms-length transaction. *Setzer v. Robinson* (1962) 57 Cal.2d 213 [18 Cal.Rptr. 524]. Once a lawyer-client relationship has been established, the lawyer owes fiduciary duties to the client that apply to the modification of the agreement that are in addition to the requirements in Paragraph (g). Lawyers should consult case law and ethics opinions to ascertain their professional responsibilities with respect to modifications to an agreement by which a client retains a lawyer's services. See, e.g., *Ramirez v. Sturdevant* (1994) 21 Cal.App.4th 904, 913 [26 Cal.Rptr.2d 554]; *Berk v. Twentynine Palms Ranchos, Inc.* (1962) 201 Cal.App.2d 625 [20 Cal.Rptr. 144]; *Carlson, Collins, Gordon & Bold v. Banducci* (1967) 257 Cal.App.2d 212 [64 Cal.Rptr.915]. Depending on the circumstances, other rules and statutes also may apply to the modification of an agreement by which a lawyer is retained by a client, including, without limitation, Rule 1.4 (Communication), Rule 1.7 (Conflicts of Interest), and Business and Professions Code section 6106.

2, 2015 memorandum providing comments on Rule 4-200, OCTC states: “Modification of fee agreements should require compliance with rule 3-300 regarding adverse interests. A lawyer holds a position of trust and has a fiduciary duty vis-a-vis his or her client. Compliance with rule 3-300 will help prevent lawyers from abusing their position and overreaching when renegotiating a fee agreement.”

- Cons: The negotiations by which a lawyer and client enter a fee agreement is an arms-length transaction. Current rule 3-300, Discussion ¶. 1, provides that rule 3-300 “is not intended to apply to the agreement by which the member is retained by the client, unless the agreement confers on the member an ownership, possessory, security, or other pecuniary interest adverse to the client.” Only under the latter described circumstances should special conditions be imposed on a fee modification. Those conditions are already provided in rule 3-300, which is the appropriate place to address the issue.
4. Include in the rule the general analytical framework for determining the unconscionability of a contract, an inquiry into the procedural and substantive unconscionability of a contract. (See, e.g., *Armendariz v. Foundation Health Psychcare Services, Inc.* (2000) 24 Cal.4th 83 [99 Cal.Rptr.2d 745]; *Cotchett, Pitre & McCarthy v. Universal Paragon Corp.* (2010) 187 Cal.App.4th 1405, 114 Cal.Rptr.3d 781.)
- Pros: Would bring the unconscionability inquiry in lawyer fee contracts in line with general contract law.
 - Cons: Including such a framework is unnecessary as there is no indication that the current analytical framework involving the consideration of a number of non-exclusive factors, does not provide an effective means for determining unconscionability of a fee.
5. Include a provision in the rule that would subject a lawyer to discipline for failure to comply with the writing and other requirements in Bus. & Prof. Code §§ 6147 and 6148.
- Pros: Written fee agreements protect the public and are part of a lawyer’s duty to communicate significant developments relating to his or her employment. A lawyer should be subject to discipline for failing to comply with those duties.
 - Cons: There is no reason to add a discipline element to the sanctions for noncompliance provided under §§ 6147 and 6148. Voiding the agreement and limiting the lawyer to recovery of the reasonable value of his or her

[3C] A modification is subject to the requirements of Rule 1.8.1 when the modification confers on the lawyer an ownership, possessory, security or other pecuniary interest adverse to the client, such as when the lawyer obtains an interest in the client’s property to secure the amount of the lawyer’s past due or future fees.

services is a sufficient disincentive to a lawyer's noncompliance with the statutes' written and other requirements, so the public should be protected.

6. Include a comment that would recognize that a lawyer may not be able to comply with paragraph (e)'s writing requirement in an emergency. Drafting team consensus.
 - Pros: This is an important qualification on the writing requirement for flat fee arrangements. These arrangements are often used in a criminal law practice, where lawyers are often retained on short notice, making the execution of a written agreement impracticable initially.
 - Cons: This comment arguably authorizes an oral contract that would create a lawyer-client relationship, at least until such time that a subsequent written agreement is entered into by the parties. Technically, the State Bar Act's requirement for a written fee agreement (for services where the total expense to a client will exceed \$1,000) has no comparable exception. Can a Rule of Professional Conduct establish an exception to a public protection statutory scheme governing contracts for legal services?

This section identifies concepts the Commission considered before the rule was circulated for public comment. Other concepts considered by the Commission, together with the Commission's reasons for not recommending their inclusion in the rule, can be found in the Public Comment Synopsis Tables.

C. Changes in Duties/Substantive Changes to the Current Rule:

1. Adding an express prohibition in paragraph (d) of certain types of contingent fee agreements.
2. In paragraph (d), expressly permitting a lawyer to denominate a fee as "earned-on-receipt" or "nonrefundable" only if it is a true retainer.
3. In paragraph (e), expressly permitting a lawyer to contract for, charge or collect a flat fee, which is paid in advance, only so long as the lawyer provides the agreed upon services.

D. Non-Substantive Changes to the Current Rule:

1. Change the rule number to correspond to the ABA Model Rules numbering and formatting (e.g., lower case letters)
 - Pros: It will facilitate the ability of lawyers from other jurisdictions who are authorized to practice in California, (see current rule 1-100(D)(1), which recognizes that reality, and rules such as the rule for *pro hac vice* admission, Rule of Court 9.40) to find the California rule corresponding to their jurisdiction's rule, thus permitting ease of determining whether California imposes different duties. It will also facilitate the ability of California lawyers

to research case law and ethics opinions that address corresponding rules in other jurisdictions, which would be of assistance in complying with duties, particularly when California does not have such authority interpreting the California rule. As to the “Con” that there is a large body of case law that cites to the current rule numbers, the rule numbering was drastically changed in 1989 and there has been no apparent adverse effect. A similar change in rule numbering of the Rules of Court was implemented in 2007, also with no apparent adverse effect.

- Cons: There is a large body of case law that cites to the current rule numbers and California lawyers are presumed to be familiar with that numbering system.

2. Substitute the term “lawyer” for “member”.

- Pros: The current Rules’ use of “member” departs from the approach taken in the rules in every other jurisdiction, all of which use the term lawyer. The Rules apply to all non-members practicing law in the State of California by virtue of a special or temporary admission. For example, those eligible to practice *pro hac vice* or as military counsel. (See e.g. rules 9.40, 9.41, 9.42, 9.43, 9.44, 9.45, 9.46, 9.47, and 9.48 of the California Rules of Court.)
- Cons: Retaining “member” would carry forward a term that has been in use in the California Rules for decades.

E. Alternatives Considered:

1. Instead of recommending proposed paragraphs (e) and (f) concerning true retainers and flat fees, respectively, take the same approach recommended by RRC1 (but which was ultimately rejected by the Board).¹²

¹² The first Commission addressed true retainers and flat fees in two separate paragraphs, which provided:

(e) When permitted by paragraph (f), a lawyer may make an agreement for, charge, or collect a fee that is denominated as “earned on receipt” or “non-refundable,” or in similar terms, but only if the client is advised in writing that the client nevertheless may discharge the lawyer at any time and may or may not be entitled to a refund of all or part of the fees charged, and the client agrees to the arrangement in a writing signed by the client.

(f) A lawyer is permitted to denominate a fee as “earned on receipt” or “nonrefundable” only in making an agreement for the following types of fee arrangements:

(1) a true retainer, which is a fee that a client pays to a lawyer to ensure the lawyer’s availability to the client during a specified period or on a specified matter, but not as compensation for legal services performed or to be performed.

(2) a flat fee for specified legal services, which constitutes complete payment for those services and may be paid in whole or in part in advance of the lawyer providing the services.

The provisions were accompanied by several comments:

[6A] Paragraph (e) prohibits the designation of a fee as “earned on receipt,” or as “nonrefundable,” or in similar terms unless the required disclosures concerning the client’s right to discharge the lawyer and the potential for a refund are made. The unconscionability requirement of paragraph (a) and the application of the factors in paragraph (c) may mean that a client is entitled to a refund of an advance fee payment even though it might have been denominated as “nonrefundable,” “earned upon receipt” or in similar terms that imply the client would never become entitled to a refund. So that a client is not misled by the use of such terms, paragraph (e) requires certain minimum disclosures that must be included in the written fee agreement. This does not mean the client will always be entitled to a refund, nor does it determine how any refund should be calculated, but merely requires that the client be advised of the possibility of the entitlement to a refund. In addition to a determination that a fee is unconscionable, a client’s entitlement to a refund might be based upon: (1) a determination that all or a portion of the fees paid have not been earned; or (2) some other failure of consideration, such as a natural disaster that destroys the lawyer’s law office making it impossible for the lawyer to render the agreed upon legal services. The foregoing examples are not intended to be a comprehensive statement of all possible bases for a client’s entitlement to a refund. Although there is always a potential for a refund because of subsequent events, paragraph (e) does not prohibit a lawyer from making an agreement for a fee which is earned upon receipt so long as the required disclosures are made in a writing signed by the client. As indicated by case law, however, a client may be entitled to a refund notwithstanding how the fees paid might have been characterized. See, e.g., *Matthew v. State Bar* (1989) 49 Cal.3d 784 [263 Cal.Rptr. 660]; *In re Matter of Lais* (Rev. Dept. 1998) 3 Cal. State Bar Ct. Rptr. 907. While discipline may result from a failure to refund fees, a primary forum for the resolution of fee dispute issues is mandatory fee arbitration under the State Bar Act. See Business and Professions Code sections 6200 et. seq. Nothing in this Rule is intended to prejudice the outcome of fee arbitration proceedings as this Rule, like any law, must be applied to the facts of a particular matter.

* * *

[7] Every fee agreed to, charged, or collected, including a fee under paragraph (f)(1) or (f)(2), is subject to paragraph (a) and may not be unconscionable.

[8] Paragraph (f)(1) describes a true retainer, which is sometimes known as a “general retainer,” or “classic retainer.” A true retainer secures availability alone, that is, it presumes that the lawyer is to be additionally compensated for any actual work performed. Therefore, a payment purportedly made to secure a lawyer’s availability, but that will be applied to the client’s account as the lawyer renders services, is not a true retainer under paragraph (f)(1). In addition to the statements required under paragraph (e), the written true retainer agreement should specify the time period or purpose of the lawyer’s availability and that the client will be separately charged for any services provided. Concerning the lawyer’s obligations with respect to the deposit of a true retainer in a trust account, see Rule 1.15, Comments [8] and [9].

[9] Paragraph (f)(2) describes a fee structure that is known as a “flat fee”. A flat fee constitutes complete payment for specified legal services, and does not vary with the amount of time or effort the lawyer expends to perform or complete the specified services.

X. COMMISSION RECOMMENDATION FOR BOARD ACTION

RECOMMENDATION:

That the Board of Trustees of the State Bar of California adopt proposed Rule 1.5 [4-200] in the form attached to this Report and Recommendation.

PROPOSED RESOLUTION:

RESOLVED: That the Board of Trustees adopts proposed Rule 1.5 [4-200] in the form attached to this Report and Recommendation.