

**Revised Working Group Recommendation**  
**re Conversion Clause Interim Opinion**

For September 15, 2023 Meeting

Based upon the California authorities cited in the draft Proposed Formal Opinion Interim No. 20-0005, "Conversion Clauses in Contingent Fee Agreements" and after consideration of public comments received in response to the Interim Opinion, the Working Group continues unanimously to recommend that the "bottom line" conclusion should be that such clauses which purport to entitle a discharged attorney to any fee calculated in any manner inconsistent with the California Supreme Court's holding in *Fracasse v. Brent* (1972) 6 Cal.3d 784, 791, are never ethically proper. Accordingly, submitted with this Recommendation is a revised "clean" draft of 20-0005 that the Working Group submits for consideration and hopefully adoption at the September 15, 2023 meeting.

In past meetings, some COPRAC members have been hesitant to accept this recommendation. The hesitancy apparently stems from two considerations. First, a minority of ethics opinions and some caselaw in other jurisdictions have concluded that a contract clause that converts a contingent fee to an hourly fee is not *per se* unethical. Second no California authority to date has expressly held that such a conversion clause is *per se* ethically improper.

The Working Group believes the first criticism is misplaced because California is unique among all jurisdictions in the Nation regarding the ethical standards by which fee contracts are evaluated. In all other jurisdictions, the ethical standard for the enforceability of a fee contract is that no fee agreement ethically may provide for the charging or collection of an "unreasonable" fee. Typically, this means subjecting the operation of the contract to a lodestar-type of analysis, taking into account all the usual factors that go into determining a reasonable fee. In other words, in all other jurisdictions, a fee agreement typically is ethical only where the resulting fee is not unreasonable.

Therefore, the difference between California and all other jurisdictions that have considered the enforceability of a conversion clause is that virtually all other jurisdictions to have done so have applied a "reasonableness" standard that is applicable not only to the fee agreement generally but also to the operation of any conversion clause. In our review of a substantial number of opinions and cases in such other jurisdictions, a conversion clause will be enforced where it's operation results in the overall charge of no more than a reasonable fee and a conversion clause will **not** be enforced where it results in the overall charge of an unreasonable fee. Such a clause also will not be enforced where it otherwise is tainted with some other violation of a statute or rule of professional conduct. Accordingly, with or without a conversion clause, all contracts in such non-California jurisdictions will be enforceable only to the extent that they provide for the charging of no more than a reasonable fee.

Noteworthy in these analyses in other jurisdictions is the recognition that, since in all circumstances no more than a reasonable fee permissibly can be charged, the conversion clause does not unduly burden the client's unfettered right to terminate the relationship "with or without cause or for no reason at all," which is the Rule in California. See, *CRPC Rule 3.16(a)(4)*; *Fracasse v. Brent*, *supra*, 6 Cal.3d, at 791.

California, on the other hand, permits an attorney and client to negotiate for a fee that is "north" of reasonable as otherwise might be determined under a lodestar-type analysis provided that the fee is not "unconscionable." See *Pech v. Morgan* (2021) 61 Cal.App.5th 841, 846. Notably, in *Pech*, the Court recognized that contracting for such a fee "north" of reasonable requires compliance with B&P Code section 6148, governing only the hourly fee portion of a fee contract. The contingent fee portion of any fee contract, on the other hand, is governed by section 6147 (see, *Arnall v. Superior Court* (2010) 190.Cal.App.4th 360).

Finally regarding the weight of authority in other jurisdictions, it also is noteworthy that in 64 Mercer L. Rev. 363 (2013), the authors review all of the then-existing case law and law review articles that consider conversion clauses and has reported that "Courts Invariably Find Efforts to Contract Around Common Law Protections to the Client as Unenforceable: Several courts and bar association have addressed the terms to contingent fee agreements that restrict the client's right to terminate the lawyer in ways inconsistent with state common law. *All have rejected them* [emphasis added]."

In addition, the article notes that, among other ethical constrictions, "[i]n addition to creating inherent and intractable conflicts of interest and undermining the policies furthered by contingent fee agreements, compensation-on-withdrawal provisions also violate state disciplinary rules regulating withdrawal as well as those prohibiting arranging for, charging, or collecting an unreasonable or unconscionable fee. Importantly, there is no provision in any of these rules for client consent, let alone 'prospective' consent to an unconscionable fee, to impinging upon the client's right to settle, or withdraw without complying with ethical rules. In addition, to the extent that these provisions create non-consentable conflicts of interest, they violate rules relating to conflicts between the lawyer's interests and those of the client."

Under such circumstances, although California is unique among all the other states, a conversion clause in a contingent fee contract could result in an overall charge that will be in excess of an otherwise reasonable fee. And, for this reason, cases such as *Fracasse* have held that, since the discharged attorney is permitted to recover under *quantum meruit* (absent some other violation of the CRPC or a termination for cause), a conversion clause that requires a fee in addition to *quantum meruit* recovery does place an undue burden on the client's unfettered right to terminate the relationship. Further, cases such as *In re: Scapa & Brown* (1993) 2 Cal. State Bar Ct. Rptr. 635, have held that an attorney's attempt to "contract around" *quantum meruit* to seek a fee higher than *quantum meruit* is a disciplinable offense.

93 In response to the second criticism – that there is no California “on all fours” with  
94 the Interim Opinion should it be published “without exceptions” – *Fracasse* and *Scapa*  
95 provide ample applicable authority. Specifically, in *Fracasse*, at 792 the Supreme Court  
96 answers the question directly: “Having held herein that an attorney henceforth will be  
97 entitled to recover only the reasonable value of his services to the time of discharge, the  
98 question arises whether his cause of action has accrued at that time. With respect to  
99 contingent fee contracts, we hold otherwise for two reasons. . . . First, [i]t is apparent that  
100 any determination of the ‘result obtained’ is impossible, and any determination of the  
101 ‘amount involved’ is, at best, highly speculative, . . . until the matter has finally been  
102 resolved. Second, and perhaps more significantly, we believe it would be improper to  
103 burden the client with an absolute obligation to pay his former attorney regardless of the  
104 outcome of the litigation.”

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106 In addition, other California authorities consistently have held contract provisions  
107 that violate the CRPC are either void or voidable or unenforceable, leaving the attorney  
108 to *quantum meruit* only, absent an “egregious” violation which could permit no recovery  
109 at all.

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111 Notable examples are the cases involving violations of old Rule 2-200 and now  
112 Rule 1.5.1. In *Chambers v. Kay* (2002) 29 Cal. 4<sup>th</sup> 152, 159, where the Supreme Court  
113 held that an agreement to divide a fee is void and unenforceable absent strict compliance  
114 with the rule’s requirement that the client consent in writing, even in the face of testimony  
115 that the client was fully aware of and orally had agreed to the fee split between her  
116 attorneys. *Chambers* left open the question of whether *quantum meruit* recovery may be  
117 had despite the violation. In the related case of *Huskinson & Brown v. Wolf* (2004) 32  
118 Cal.4<sup>th</sup> 113, 125, the Supreme Court concluded that *quantum meruit* recovery was  
119 appropriate but, significantly, it also held that such recovery must be determined by  
120 appropriate factors (such as the typical lodestar-type factors) *other than the contract*  
121 *amount*. The *Chambers* line of cases also begs the question: If an agreed upon fee split  
122 in a contingent fee matter cannot burden the client with anything more than the agreed  
123 upon overall contingent fee amount even if agreed upon in writing, how can it be ethically  
124 proper for one of the two attorneys sharing the ultimate fee to increase his or her  
125 compensation unilaterally solely because the client exercises his or her “unfettered” right  
126 to terminate the relationship?

127  
128 Following the holdings in *Chambers* and *Huskinson*, the Supreme Court next  
129 decided *Sheppard, Mullin, Richter & Hampton LLP v. J-M Mfg. Co.* (2018) 6 Cal.5<sup>th</sup> 59,  
130 81, holding that any fee agreement that fails to comply fully with the CRPC is “contrary to  
131 the public policy of the state” and “is for that reason unenforceable.” As in *Chambers* and  
132 *Wilkinson*, the Supreme Court in *Sheppard Mullin* allowed that *quantum meruit* was an  
133 adequate safeguard against any unfairness to the attorneys.

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135 And, in *Arnall, supra*, at 373, we find instructive reasoning being applied to the  
136 related issue of failure to comply with the strict language of B&P Code section 6147  
137 regulating contracts for charging a contingent fee. In *Arnall*, in a hybrid contingent fee  
138 contract regarding the recovery of a multi-million-dollar tax saving extensively negotiated

139 with an extremely sophisticated client, the omission in the written contract of the singular  
140 phrase about the negotiability of the amount was held to have made the contract voidable  
141 as to the contingent fee portion of the fee agreement. Explaining its rationale, the Court  
142 stated: “[W]hen a statute protects the public by denying compensation to parties who fail  
143 to meet regulatory demands, the statute constitutes a legislative determination that the  
144 need for compliance outweighs any resulting harshness . . . .”  
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146 Finally, one as yet untested proposition also militates against holding conversion  
147 clauses enforceable against the client. In *Fletcher v. Davis* (2004) 33 Cal.4<sup>th</sup> 61, 68-70,  
148 the Supreme Court discusses whether a “charging lien” that becomes actionable to  
149 recover an hourly fee must comply with then-rule 3-300 (i.e., fair and reasonable and  
150 consented to in writing by the client after the opportunity to consult with independent  
151 counsel) and concluded that although “a charging lien does not grant an attorney the  
152 attorney the power to summarily extinguish the client’s interest in any recovery, a charging  
153 lien could significantly *impair* the client’s interest by delaying payment of the recovery or  
154 settlement proceeds until any disputes over the lien can be resolved.” While the *Fletcher*  
155 Court did not decide whether a charging lien for a contingent fee need comply with then-  
156 rule 3-300, it concluded that a charging lien for an hourly fee must comply. Significantly,  
157 although in a conversion clause situation the fee starts out as a contingent fee, the  
158 operation of the conversion clause converts the lien into a charging lien for an hourly fee  
159 that *Fletcher* has held must comply with the rule.  
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161 Accordingly, the Drafting Group is persuaded that ample authority in California  
162 supports the proposition that any contract that violates the CRPC or other applicable  
163 statute is void or voidable as a matter of public policy and that *quantum meruit* is adequate  
164 compensation for any resulting unfairness to the attorney who engages in such a  
165 violation. We therefore renew our recommendation that the Interim Opinion be voted out  
166 favorably for publication without discussion of possible scenarios where a conversion  
167 clause in a contingency fee agreement would result in compensation above or beyond  
168 *quantum meruit* upon termination of the attorney-client relationship prior to the happening  
169 of the contingent event.  
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171 Finally, there is some sentiment among the Drafting Team that, should there  
172 continue to be significant opposition to voting out the Interim Opinion with no exception,  
173 the foregoing California authority at a minimum should be revisited by COPRAC to  
174 consider whether, rather than adopting a qualified opinion, we instead might withdraw the  
175 Interim Opinion altogether.

**THE STATE BAR OF CALIFORNIA  
STANDING COMMITTEE ON  
PROFESSIONAL RESPONSIBILITY AND CONDUCT  
FORMAL OPINION INTERIM NO. 20-0005**

**ISSUES:** Under what circumstances, if any, are “conversion clauses” in contingent fee agreements ethically permissible?

**DIGEST:** Conversion clauses in contingent fee agreements are ethically prohibited primarily because their use improperly interferes with important client rights and violate an attorney’s ethical duties, including the client’s right to discharge the lawyer or the client’s right to determine whether to settle, and where they constitute an agreement to charge an unconscionable fee.

**AUTHORITIES**

**INTERPRETED:** Rules 1.2, 1.5, and 1.16 of the Rules of Professional Conduct of the State Bar of California.<sup>1</sup>

**INTRODUCTION AND SCOPE**

This opinion addresses the ethical permissibility of conversion clauses in contingent fee agreements. For purposes of this opinion, a conversion clause is a contractual provision that, if triggered, converts the fee due to a lawyer from that contingent fee to an alternate fee arrangement which purports to entitle the attorney to a fee greater than the reasonable value of the attorney’s services up to the time of discharge not calculated against the recovery actually obtained or against the services of successor counsel in relation to the recovery actually obtained.<sup>2</sup>

It is the view of the Committee that such conversion clauses are ethically prohibited for two reasons. First, they impermissibly interfere with the client’s right to discharge the lawyer or the client’s right to determine whether to settle. Second, they can result in the charging of an amount in excess of the discharged attorney’s right to a “reasonable fee,” which is not permitted by California case law and thus would constitute an agreement to charge an unconscionable fee.

**DISCUSSION**

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<sup>1</sup> Unless otherwise indicated, all references to “rules” in this opinion will be to the Rules of Professional Conduct of the State Bar of California.

<sup>2</sup> This opinion is not intended to address the ethical validity or enforceability of hybrid fee agreements, which are distinct from conversation clauses and usually involve the payment of attorneys’ fees in some combination of an hourly rate, flat rate, or contingency fee. For some analysis on ethical issues related to hybrid fee agreements, see Bar Association of San Francisco Formal Ethics Opn. No. 1999-1 (opining that as long as the client enters into the fee agreement in an arm’s length transaction and agrees to the fee with informed consent, such arrangements would be permissible under rule 1.5 provided that the fee charged is not unconscionable).

**A. The Client's Right to Discharge Counsel.**

Both the rules and California decisional law confirm a client's absolute right to discharge his or her attorney. (Rule 1.16(a)(4); *Fracasse v. Brent* (1972) 6 Cal.3d 784 [100 Cal.Rptr. 385 ]; *Kroff v. Larson* (1985) 167 Cal.App.3d 857, 860 [213 Cal.Rptr. 526] [client has the absolute right at any time to discharge an attorney, with or without cause].) Conversion clauses which purport to entitle a lawyer in a contingent fee representation, if terminated, to an amount in excess of the quantum meruit value of the attorney's services up to the time of discharge (an amount that cannot be determined until if and when the contingency in fact occurs) is impermissible because it would interfere with the client's right to discharge counsel. (See *Fracasse v. Brent*, *supra*, 6 Cal.3d at p. 792 [improper to burden the client in contingency cases with an absolute obligation to pay the attorney regardless of outcome]; see also, Colorado State Bar Ethics Opinion 100 (1997); 64 Mercer L. Rev. 363 (2013); *Compton v. Killtelson* (2007) 171 P.3d 172 [contingent fee agreement retroactively converted to hourly fee upon discharge of attorney was unconscionable and a violation of Model Rule 1.2]; *U.S. Postal Service v. Haselrig Corp* (D. Md. 2004) 349 F.Supp.2d 955 [agreement that attempted to unlawfully penalize the client for discharge of the attorney by requiring payment of 40% contingency or flat \$35,000 was unreasonable at inception].)

An argument sometimes heard is that conversions clauses are necessary to "protect" contingent fee lawyers from perceived bad-faith termination by clients. However, established law already protects a contingent fee lawyer under the principles of *quantum meruit*,<sup>3</sup> which allow a terminated contingent attorney to receive a fee commensurate with the reasonable value<sup>4</sup> of the services provided up to the time of discharge. As the California Supreme Court in *Fracasse* noted (in a different but related context): "... we find no injustice in a rule awarding a discharged attorney the reasonable value of the services he has rendered up to the time of discharge," a rule which the court noted, "preserve[s] the client's right to discharge his attorney without undue restriction, and yet acknowledge[s] the attorney's right to fair compensation for work performed." (*Fracasse v. Brent*, *supra*, 6 Cal.3d. at p. 791.) Conversion clauses purporting to entitle a discharged attorney to a fee in excess of quantum meruit operate as improper penalties rather than ethically permissible attorney protections.

In addition, because the reasonable value of the discharged attorney's services cannot be calculated until the case terminates and the amount of recovery, if any, is known, the risk that some contractual formula may ultimately result in a fee greater than the reasonable value of the services or in a fee where

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<sup>3</sup> "Quantum meruit" refers to the principle that the law implies a promise to pay for services performed under circumstances disclosing that they were not gratuitously rendered. The doctrine of *quantum meruit*, where appropriate, allows attorneys to recover the reasonable value of their services even in the absence of a valid or enforceable contract. (See *Sheppard, Mullin, Richter & Hampton, LLP v J-M Manufacturing Co., Inc.* (2018) 6 Cal.5th 59, 88 [237 Cal.Rptr.3d 424].) Although beyond the scope of this opinion, California has a well-developed body of law concerning when a discharged lawyer's conduct entitles or disentitles the lawyer to a reasonable fee (i.e., a *quantum meruit* recovery) such as where a contingent fee attorney withdraws from the case without justifiable cause (see *Rus Miliband & Smith v. Conkle & Olesten* (2003) 113 Cal.App.4th 656 [6 Cal.Rptr.3d 612]; *Hensel v. Cohen* (1984) 155 Cal.App.3d 563 [202 Cal.Rptr. 85]; *Fracasse v. Brent*, *supra*, 6. Cal.3d. at p. 791) or certain ethical violations such as an egregious conflict of interest (see *Cal Pak Delivery, Inc. v. United Parcel Service Inc.* (1997) 52 Cal.App.4th 1 [60 Cal.Rptr.2d 207]).

<sup>4</sup> For further analysis on the factors involved in determination of a reasonable fee, see State Bar of California Arbitration Advisory 1998-03 (rev. 2016).

no recovery ultimately is retained is a further impermissible disincentive to the exercise of the client's right to discharge counsel.

For these reasons, it is the view of the Committee that any conversion clause which purports to entitle a discharged contingent-fee attorney to more than *quantum meruit* is ethically prohibited. Further, it is the view of the Committee that a conversion clause which seeks to entitle a contingent-fee lawyer to any fee in circumstances under which that contingent-fee lawyer would otherwise be legally disentitled to recover a fee in *quantum meruit*, is ethically prohibited. (See fn. 3, *supra*).

#### **B. The Client's Right to Decide Whether or Not to Settle**

A lawyer is ethically required to abide by a client's decision concerning the objectives of the representation. The rules expressly extend this precept to the decision to accept or reject a settlement offer. "[A] lawyer shall abide by a client's decision whether to settle a matter." (Rule 1.2(a).) Nonetheless, conversion clauses are often designed to "protect" an attorney against a client's unreasonable or even bad-faith decisions regarding whether to accept or reject settlement proposals contrary to the lawyer's recommendation.

Such conversion clauses often purport to entitle the lawyer to payment of the lawyer's contingent fee percentage calculated against any settlement offer that the lawyer recommends the client to accept, but which the client rejects. Alternatively, some clauses entitle a lawyer to the lawyer's hourly rates if the client accepts a settlement offer (or walk-away agreement) which the lawyer believes is insufficient.

While ethics committees of other states have approached such settlement-related conversion clauses from a variety of perspectives, all (save for one possible exception posed in a hypothetical comment from a Colorado opinion) have found conversion clauses to be ethically impermissible. By way of example only, see, 64 Mercer L. Rev. 363 (2013); Wisconsin State Bar Professional Ethics Committee Formal Opinion No. E-82-5 (1982) (a contingent fee agreement that permits charging hourly fees if attorney deems a settlement offer inadequate is overreaching and unethical); Philadelphia Bar Association Ethics Opinion No. 2001-1 (majority opinion would permit conversion where there is clear advanced agreement on the goals of representation and agreement as to alternate methods of compensation if the client's goals change; the minority opinion would permit conversion clauses for sophisticated clients, not unsophisticated clients); Nebraska Ethics Advisory Opinion No. 95-1 (a provision triggered by a client not following attorney's settlement advice, which allows the attorney to choose between the contingent percentage or full hourly fee, restricts the client's authority to settle a matter).

It is the view of the Committee that the requirement imposed by rule 1.2(a), that "a lawyer shall abide by a client's decision whether to settle a matter," is clear and unwaivable and its elimination by contract is simply not permitted under rule 1.2(b). (See, e.g., *Amjadi v. Brown* (2021) 68 Cal.App.5th 383 [283 Cal.Rptr.3d 448] [holding that a provision in a fee agreement purporting to grant the lawyer the right to accept a settlement offer on behalf of the client in the lawyer's "sole discretion" violates the rules and is

void];<sup>5</sup> *In the Matter of Guzman* (Review Dept. 2014) 5 Cal. State Bar Ct. Rptr. 308, 314–315 [the State Bar Court held that “[a]ttempts by an attorney to restrict a client’s right to control his or her case are invalid and evidence of overreaching”].) Conversion clauses keyed to the acceptance or rejection of settlement offers thus are ethically prohibited.

## CONCLUSION

It is the view of the Committee that conversion clauses are ethically prohibited because they impermissibly interfere with a client’s right to (1) terminate an attorney or (2) decide whether to settle and because they can result in an agreement to charge an unconscionable fee, either facially or as-applied.

This opinion is issued by the Standing Committee on Professional Responsibility and Conduct of the State Bar of California. It is advisory only. It is not binding upon the courts, the State Bar of California, its Board of Trustees, any persons, or tribunals charged with regulatory responsibilities, or any member of the State Bar.

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<sup>5</sup> *Amjadi* also held that attempts by lawyers to wrest control from clients as to settlement decisions not only violate rule 1.2, but also create a conflict of interest between the lawyer and client under rule 1.7(b) whenever the client and attorney disagree about settlement.