FEE SHARING AND THE CHANGING LEGAL LANDSCAPE

What is fee sharing? The answer seems fairly obvious – you cannot share a legal fee with someone who is not a lawyer. While that sounds straightforward, it is not always straightforward or clear in practice. In the continually emerging and disruptive world of legal tech, for example, the lines are being blurred in ways that are not so obvious. The pitfalls are real and we will examine them alongside the more traditional cases of fee sharing that violate ethics rules.

Rule 5.4 of the Rules of Professional Conduct states:

RULE 5.4. Professional Independence of a Lawyer

(a) A lawyer or law firm shall not share legal fees with a nonlawyer, except that:

(1) an agreement by a lawyer with the lawyer's firm, partner, or associate may provide for the payment of money, over a reasonable period of time after the lawyer's death, to the lawyer's estate or to one or more specified persons;

(2) a lawyer who undertakes to complete unfinished legal business of a deceased lawyer may pay to the estate of the deceased lawyer that proportion of the total compensation which fairly represents the services rendered by the deceased lawyer;

(3) a lawyer or law firm may include nonlawyer employees in a compensation or retirement plan, even though the plan is based in whole or in part on a profit-sharing arrangement;

(4) a lawyer who purchases the practice of a deceased, disabled, or disappeared lawyer may, pursuant to the provisions of Rule 1.17, pay to the estate or other representative of that lawyer the agreed-upon purchase price; and

(5) a lawyer may share legal fees as otherwise provided in Rule 7.2(c)(13).

(b) A lawyer shall not form a partnership with a nonlawyer if any of the activities of the partnership consist of the practice of law.

(c) A lawyer shall not permit a person who recommends, employs, or pays the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal services.

(d) A lawyer shall not practice with or in the form of a professional corporation or association authorized to practice law for profit, if:

(1) a nonlawyer owns any interest therein, except that a fiduciary representative of the estate of a lawyer may hold the stock or interest of the lawyer for a reasonable time during administration;

(2) a nonlawyer is a corporate director or officer thereof or occupies the position of similar responsibility in any form of association other than a corporation; or

(3) a nonlawyer has the right to direct or control the professional judgment of a lawyer.

FEE SHARING CASES AND SANCTIONS

In re Billy Gene Watley and Amy E. Watley, 2001-B-1775, La. 12/7/01, 802 So. 2d 593, involved a father and daughter attorney team that entered into a written agreement with "We the People" Paralegal Services, LLC ("WTP"), in which WTP would provide paralegal and secretarial services to the Watleys' law firm. In exchange, the Watleys agreed in writing to pay WTP forty percent (40%) of the attorney's fees earned on each personal injury case and sixty percent (60%) of attorney's fees for cases WTP referred to them. The Watleys also agreed to pay WTP $10 per hour for the time WTP's staff worked on any case that was not a personal injury case.

The Watleys paid a 40% fee to WTP in two cases but did not pay the fee in 17 other cases. Not surprisingly, WTP filed suit against the Watleys for breach of contract. The Office of Disciplinary Counsel ("ODC") learned of the lawsuit and investigated to determine if the Watleys were engaged in a fee sharing arrangement with nonlawyers. The Watleys were charged with numerous violations of the Rules of Professional Conduct, including Rule 5.4(a) (fee sharing with a nonlawyer).

The case proceeded to a hearing before a hearing committee, but the Watleys did not appear. The ODC presented documentary evidence, live testimony, and a hearing transcript from the civil case filed by WTP. At the hearing, a representative of WTP testified she was present at the meeting where the Watleys proposed the fee sharing agreement to WTP. She stated WTP accepted the terms of the agreement and performed services pursuant to it.

Next, ODC's expert audit consultant testified he examined two checks which proved fee-sharing between the Watleys and WTP. The two checks established that in accordance with the Watleys' agreement with WTP that WTP had been paid exactly 40% of the fee received by the Watleys in connection with two personal injury matters. As to the second check examined, the expert compared the notations on the checks to the invoice numbers and found the invoice numbers did not match up to the checks. This in his expert opinion signified an effort by the respondents to "throw anyone who was examining [the checks] off."

The hearing committee found, based upon the evidence presented, that the testimony and documentary evidence submitted by the ODC proved by clear and convincing evidence that the Watleys violated Rule 5.4 by sharing fees with a nonlawyer. It determined that the Watleys intentionally violated their duties to the profession, thereby causing actual or potential injury to

the profession. It further determined the fact that Watleys did not admit to their misconduct was indicative of the potential for additional misconduct.

Given these conclusions, the hearing committee determined sanctions. First, the committee identified both mitigating and aggravating factors. The committee found no mitigating factors but found the following aggravating factors: a pattern of misconduct, dishonest or selfish motive (attempt to hide the misconduct by referencing invoice numbers on their checks), failure to admit to wrongful nature of conduct, and bad faith obstruction of disciplinary proceeding by intentionally failing to comply with the order of the disciplinary agency to appear before the committee. Additionally, the committee found that Billy Gene Watley had a prior disciplinary record consisting of an admonition.

The hearing committee recommended the Watleys be suspended from the practice of law for a period of six months, followed by a one year period of probation. The ODC filed an objection to the leniency of the committee's recommendation. The ODC recommended an eighteen month suspension, with six months deferred, followed by a one year period of probation.

The Supreme Court addressed applicable sanctions. The Court agreed the Watleys had engaged in fee sharing with nonlawyers and that these actions were intentional. The Court found several aggravating factors, including dishonest or selfish motive, failure to admit the wrongful nature of the conduct and bad faith obstruction of the disciplinary proceedings. The only mitigating factor present the Court identified was inexperience in the practice of law. The Court imposed a one-year and one-day suspension upon the Watleys, which necessitated an application for reinstatement.

In re Butler, 18-1812 (La. 5/8/19), 283 So. 3d 455, involved scenarios similar to *In re Billy Gene Watley* and *Billy Gene Watley and Amy E. Watley,* both *supra.* There, Butler entered into an arrangement with Knowledge Center Temple (KCT), which was a business of "pro se paralegals" who assisted incarcerated individuals with their post-conviction relief proceedings. Butler agreed to proofread KCT's legal work done on behalf of KCT clients. Butler knew the KCT principals were not attorneys and that they, KCT, were drafting legal pleadings. None of the arrangement was reduced to writing nor was a fee agreement, which varied with KCT's client and the type of work performed.

Butler was charged with violating Rule 5.4 (fee sharing). He was also charged with violations of Rule 5.5(a) (a lawyer shall not practice law in violation of the regulation of the legal profession in that jurisdiction, or assist another in doing so), and Rule 8.4(a) (violation of the Rules of Professional Conduct). Butler denied the charge of fee sharing and suggested that "his misconduct, if any, was committed negligently."

The hearing committee found violations of all Rules charged and recommended sanctions of a three-year suspension from the practice of law, with an order of restitution and the assessment of with costs and expenses. Butler filed an objection to the severity of the sanctions.

The ODC conceded that the hearing committee's factual findings were not manifestly erroneous but recommended the less stringent sanctions of a suspension from the practice of law

of six months, fully deferred, subject to a one-year period of probation and attendance at Ethics School. The ODC also recommended that respondent be assessed with the costs and expenses of the proceeding.

After reviewing the record, the Supreme Court stated:

> There is clear and convincing evidence in the record that respondent improperly shared legal fees with Mr. Taylor and Ms. Terrell [KCT] and assisted them in practicing law. Respondent knew that Mr. Taylor and Ms. Terrell were not lawyers, yet he willingly assisted them in the preparation of legal pleadings and shared in fees for those services. Based on these facts, respondent has violated the Rules of Professional Conduct as charged by the ODC.
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> Having found evidence of professional misconduct, we now turn to a determination of the appropriate sanction for respondent's actions. In determining a sanction, we are mindful that disciplinary proceedings are designed to maintain high standards of conduct, protect the public, preserve the integrity of the profession, and deter future misconduct. *Louisiana State Bar Ass'n v. Reis*, 513 So. 2d 1173 (La. 1987). The discipline to be imposed depends upon the facts of each case and the seriousness of the offenses involved considered in light of any aggravating and mitigating circumstances. *Louisiana State Bar Ass'n v. Whittington*, 459 So. 2d 520 (La. 1984).
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> Respondent's conduct was knowing. He violated duties owed to his clients, the public, and the legal profession, causing actual harm to Mr. Casaday and Mr. Daigre. Considering the ABA's Standards for Imposing Lawyer Sanctions, the baseline sanction in this matter is suspension.
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> The record supports the aggravating factor of vulnerability of the victims. The record supports the following mitigating factors: absence of a prior disciplinary record, full and free disclosure to the disciplinary board and a cooperative attitude toward the proceedings, inexperience in the practice of law (admitted 2011), and character or reputation.

The sanctions were imposed in part based upon the Supreme Court's reliance on *In re Watley, supra:*

> While we do not find respondent's conduct warrants disbarment, it is important to note that in cases involving fee sharing with a nonlawyer, "we have imposed a suspension of one year and one day." *In re Watley*, 01-1775 (La. 12/7/01), 802 So. 2d 593. Furthermore, in *In re Mopsik*, 04-2395 (La. 5/24/05), 902 So. 2d 991, we imposed an actual period of suspension for the negligent facilitation of the unauthorized practice of law, suggesting that where, as here, knowing misconduct is at issue, an actual period of suspension would certainly be warranted.

> Based on this jurisprudence, we will reject the recommendation of the majority of the disciplinary board that respondent receive a fully deferred suspension. Rather, respondent shall be suspended from the practice of law for eighteen months, with all but one year deferred, subject to a one-year period of unsupervised probation. Respondent shall also be required to attend Ethics School.

Justice Crichton dissented in part, disagreeing with the severity of the sanction, specifically finding the sanction too harsh under the circumstances:

> I find the majority failed to adequately consider the mitigating factor of respondent's inexperience in the practice of law at the time this arrangement began. Specifically, respondent was admitted in 2011, and in 2014, he entered into this particular fee arrangement with the nonlawyers. In my view, a mere three years into the practice of law at the time respondent's misconduct began is a significant mitigating factor in this matter. See generally, *In Re Abdalla*, 17-453 (La. 10/18/17), 236 So. 3d 1223 .. and [I] would order respondent to be suspended for one year, with all but six months deferred, followed by a one year period of probation with conditions (including attendance and successful completion of a session of the Louisiana State Bar Association's Ethics School).

It should be noted that Butler was charged in another disciplinary proceeding, *In re Butler,* 19-1199 (La. 9/24/19), 279 So. 3d 886. The charges did not involve fee sharing and Butler entered into a Petition for Consent Discipline prior to disciplinary charges being filed. The Supreme Court imposed sanctions of suspension from the practice of law for a period of eighteen months with all but one year and one day deferred and the imposition of all fees and expenses incurred in the proceeding. This suspension was made retroactive to May 8, 2019, the date of respondent's prior suspension imposed in *In re Butler, supra*.

Another similar fee sharing case is *In re Stacy L. Morris*, 2014-1067 (La. 10/15/14), 149 So. 3d 229. There, Morris was formally charged with four client matters then subsequently Morris was charged in another client matter. The charges involved violations of several rules including fee sharing. All formal charges proceeded to hearing.

In each client matter, Morris was providing legal services to individuals hired by non-attorney entities. For example, Morris contracted with the entity Citizens Against Legal Abuse (CALA), a non-licensed domestic corporation that provided legal services to clients in the New Orleans area. CALA aggressively advertised its services to the New Orleans minority community as a "non-profit" legal representation resource. During 2004, CALA and Morris maintained adjacent addresses in a duplex on Banks Street in New Orleans. Morris was advertised as available to represent clients referred by CALA. To facilitate this arrangement, copies of printed attorney-client contracts with the heading "Citizens Against Legal Abuse, Inc., Stacy L. Morris Attorney and Counselor at Law," were given to prospective clients. CALA retained primary responsibility for setting, quoting, and collecting legal fees (usually a fixed fee) from prospective clients.

After concluding contractual terms with the client, a CALA employee contacted Morris to advise she had been retained and to provide details of the legal matter. In exchange for a referral,

Morris typically remitted to CALA a percentage or portion of the fee paid by the client, characterizing such payments as "donations." In her sworn statement, Morris indicated that she shared as much as fifty (50%) of her retainer fees with CALA. Neither the founder/owner of CALA nor several CALA employees identified by Morris were attorneys. Printouts from CALA's website indicated that CALA was not a recognized law firm authorized to practice law.

Morris was charged with multiple counts and violations of 5.4(a) (a lawyer shall not share legal fees with a nonlawyer); 5.5(b) (facilitating the unauthorized practice of law by a nonlawyer); and 7.2(b) (sharing fees with a corporation not licensed to practice law) for her relationship with CALA. Morris was found to have violated these Rules.

As to sanctions, the Supreme Court considered the charges involved in two consolidated cases. Given this, the other acts of misconduct, particularly Morris' conversion of the funds of two clients (who had no association with CALA), the Court imposed a sanction of a three-year suspension, along with payment of restitution to the affected clients.

The Rule prohibits a lawyer from sharing with a paralegal firm a percentage of the legal fees earned in a personal injury matter. See *In re Watley*, 802 So. 2d 593 (La. 2001) (*supra)*; *In re Garrett*, 12 So. 3d 332 (La. 2009) (sharing fees with an unlicensed law school graduate); *In re Jackson*, 1 So. 3d 454 (La. 2009) (suspended attorney sharing fees with a licensed attorney); *In re Guirard & Pittinger*, 11 So. 3d 1017, 1026 (La. 2009) (paying employee "case managers" a percentage of personal injury recovery).

The Legal Tech Landscape Is Changing: Will the Lawyers Change?

What are the reasons for the prohibition on fee sharing? First, the limitations are in place to protect the lawyer's professional independence of judgment, as stated in section (c) of the Rule. When someone other than the client pays the lawyer's fee, there is always the possibility the third party will try to influence the lawyer's independence and judgment. This simply cannot happen. The lawyer's duty and obligations are to the client, period, regardless of who pays the legal fees.

The Rule also expresses the traditional limitations on permitting a third party to direct or regulate the lawyer's professional judgment in rendering legal services to another. See also Rule 1.8(f) (lawyer may accept compensation from a third party as long as there is no interference with the lawyer's independent professional judgment and the client gives informed consent).

Both of these situations call into question the legal debate over maintaining versus relaxing these rules in light of the legal and successful "matchmaking" services such as Avvo, LegalZoom, and RocketLawyer. Essentially, these online services claim to "match" [refer] lawyers and clients in exchange for a fee [fee sharing]. The arrangements also raise concerns over the unauthorized practice of law and in some instances, advertising.

The legal landscape is being inundated with legal tech online startups and disrupters that cut across all areas of practice. These newer entities and legal matchmakers typically violate ethics rules concerning fee sharing, referral fees, the unauthorized practice of law, and the impairment of

a lawyer's impartial judgment. These can also blur traditional lines of what is considered to be lawyer advertising.

Legal writers and business bloggers are discussing the need to relax current ethics rules under the guise of "delivery of legal services". These writers and bloggers insist that the legal profession and its disciplinary rules and regulations are hampering business' ability to generate income, restricting consumers' access to legal services, and are adversely impacting the economics of the profession; *i.e.,* lawyers are earning less income than their professional counterparts in the larger economy. They urge the situation will only become worse, thus change is necessary.

"Change" as the writers see it is a wholesale relaxing of the rules, regulations, and restrictions on practicing law. Such proposed changes would for example, allow lawyers to create partnerships and other business associations with nonlawyers while practicing law. The changes seem counterintuitive in light of most states' limited resources and continuing efforts to root out unethical lawyers in the practice.

A July 2018 report commissioned by the State Bar of California, the Legal Market Landscape Report, asserted:

> Throughout the United States, legal regulators face a challenging environment ... The primary mechanism for regulating this market is lawyer ethics, including the historical prohibition on nonlawyer ownership of businesses engaged in the practice of law. However, private investors are increasingly pushing the boundaries of these rules by funding new technologies and service delivery models designed to solve many of the legal market's most vexing problems.
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> ... Solving the problem of lagging legal productivity requires lawyers to work closely with professionals from other disciplines. Unfortunately, the ethics rules hinder this type of collaboration ... Modifying the ethics rules to facilitate greater collaboration across law and other disciplines will (1) drive down costs; (2) improve access; (3) increase predictability and transparency of legal services; (4) aid the growth of new businesses; and (5) elevate the reputation of the legal profession. Some U.S. jurisdiction needs to go first. Based on historical precedent, the most likely jurisdiction is California.

Many of these conclusions seem suspect on their face, particularly elevating the reputation of the legal profession. To most lawyers, the radical changes would seem to accomplish just the opposite. It is clear the urgent push to enact significant changes is coming from Silicon Valley, the heart of the legal tech revolution. While the tech revolution in general has created many innovations that enhance daily lives, slow and steady may be the best approach when it comes to legal ethics.

In response to the July 2018 report, the California Bar's Board of Trustees formed a Task Force on Access through Innovation of Legal Services (ATILS). The Task Force in July 2019

delivered sweeping recommendations to the California Bar and opened the period for public comment. The Board focused on two main ethics areas: the unauthorized practice of law and fee sharing. The report recommends drastic changes to both rules. In addition to declining legal income, a key driver for the proposed changes is the new legal tech disrupters or legal matchmakers which "match" lawyers to clients for a fee.

Included in the recommendations as to fee sharing are:

- Largely eliminating the longstanding general prohibition and substitute a permissive rule broadly permitting fee sharing with a nonlawyer provided that the lawyer or law firm complies with requirements intended to ensure that a client provides informed written consent to the lawyer's fee sharing arrangement with a nonlawyer; and

- Adoption of a version of the ABA Model Rule that foster investment in, and development of, technology-driven delivery systems including associations with nonlawyers and nonlawyer entities.

Following a public comment period, it is anticipated there will be meetings and discussions for the report's recommendations at the annual American Bar Association convention in San Francisco in August 2020.

These changes are far ranging and would significantly alter the legal landscape. Critics of the report claim the changes would result in a near annihilation of current ethics rules concerning fee sharing. Critics point out that the rules are in place *because* the practice of law is a profession, and the people who engage in the profession are professionals. Thus, to remove the safeguards designed to protect the integrity of the profession makes no sense.

A more balanced view is seen in the November 2019 American Bar Association's journal article "When the Rules Stagnate Innovation, Change the Rules". The article addresses the California report and discusses the blurring of boundaries between the licensed and regulated "practice of law" and other business services, and the ethics issues they present such as fee sharing. Both make for interesting reading.

This is just the first shot in what will likely be hard fought challenges to existing ethics rules and regulations. Over the last year, several states have established task forces to re-think these rules particularly the restrictions concerning fee sharing and the unauthorized practice of law. Only time will tell what changes to ethics rules will be made.

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