Employment Agreements Regarding Division of Fees Earned Post-Separation

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QUESTION PRESENTED:

May a law firm require associates to sign an employment agreement, upon initial employment, that contains a separation provision requiring a departing associate to pay the firm a percentage of fees earned thereafter from clients who have elected to remain clients of the departing associate?

The proposed separation provision in the employment agreement requires that: 1) when an associate decides to depart, the clients' files would be interim billed; 2) the associate could then leave with the files of the clients who choose to depart with the associate; 3) if the departing client was generated by the departing attorney, then no follow-up payment to the law firm is required; 4) if the departing client was not generated by the departing associate, then the departing attorney is required to pay the firm a percentage of fees generated thereafter for the next two years.

APPLICABLE RULES: Prof.Cond.R. 1.5 and 5.6.
OPINION:

Restriction on right to practice

Lawyers are prohibited from offering or entering into an employment agreement that restricts the right of a lawyer to practice after termination of the relationship, except when incident to retirement benefits or upon sale of a law practice. Prof.Cond.R. 5.6, cmt. [1], [3]. The rationale behind the rule is that restrictive covenants can limit a lawyer’s professional autonomy and a client’s freedom to choose a lawyer. Id. at cmt. [1]; Adv. Op. 90-14. The Court has recognized there is a strong public policy interest in permitting a party’s continued representation by counsel of his or her choice. Kala v. Aluminum Smelting & Refining Co., 81 Ohio St.3d 1, 688 N.E.2d 258 (1997). Furthermore, a client does not belong to a lawyer or a law firm, but rather the client has the power to choose counsel of his or her choice. Ohio Bd. of Prof. Cond., Switching Firms, Ohio Ethics Guide (2017).

In a prior advisory opinion, the Board addressed Prof.Cond.R. 5.6 in the context of settlement provisions. Adv. Op. 2019-04. The Board noted that while a proposed provision in an agreement may not directly bar future representation by a lawyer, it may have the practical effect of limiting the lawyer’s right to practice. Id. The Board further reasoned, “[a]n analysis of less obvious restrictions under Prof.Cond.R. 5.6 requires a determination of whether the lawyer is given significantly less discretion in pursuing future claims than a lawyer not subject to the agreement. In those instances, the provision constitutes an impermissible restriction on the practice of the lawyer.” Id.

In Cincinnati Bar Assn. v. Hackett, 129 Ohio St.3d 186, 2011-Ohio-3096, the Court addressed a similar employment agreement wherein the departing associate was required to pay the firm 95 percent of the attorney fees generated on cases in which the clients followed the departing lawyer, regardless of the proportion of work each attorney performed. The Court observed that a client’s absolute right to discharge a lawyer, at any time with or without cause, subject to compensation for services rendered, would be hollow if the discharged attorney could prevent other attorneys from representing the client. Id. at ¶8. The Court concluded that if the employment agreement were enforced, it would create an “economic deterrent for the departing attorney that would adversely affect the clients’ right to retain an attorney of their own choosing.” Id. at ¶9.
In the Board’s view, financial disincentives in an employment agreement, such as requiring a departing attorney to pay a percentage of fees generated from work occurring subsequent to departure, places both a burden on the departing attorney and impairs a client’s right to choose counsel. The economic deterrent for the departing attorney may discourage or prevent the departing associate from agreeing to continue to represent the client, despite the client’s wishes. The purpose of the provision in the employment agreement is to discourage competition. Moreover, as a result of the agreement, the departing lawyer has significantly less discretion in agreeing to continue to represent the client than a lawyer not subject to the agreement.

*Fee Splitting*

The proposed employment agreement also implicates Prof.Cond.R. 1.5(e), which provides that lawyers not in the same firm may only divide fees if: 1) the fees are divided in proportion to the services performed or both lawyers agree to be jointly responsible for the representation; 2) the client gives written consent to the division of fees; 3) in the event the fee agreement is contingent, both lawyers and the client sign the closing statement; and 4) the total fees are reasonable. Comment [8] to the rule indicates that it does not prohibit or regulate the division of fees to be received in the future for work done when lawyers were previously associated in a law firm. The rule and comments are silent as to fees related to work occurring by a lawyer subsequent to departure from a firm. If the employment agreement were enforced, it would operate to impose the division of fees paid by the client without input from the client. The client would not be required to consent to the disposition of his or her fees and the law firm would not be required to maintain joint responsibility for a matter which was ongoing and from which the firm may ultimately benefit financially.

The Board advises against the use of employment agreements with a pre-arranged separation provision requiring a departing associate to pay the firm a percentage of fees earned thereafter from clients who have elected to remain clients of departing associate.