Opinion No. 577
March 2007
The Professional Ethics Committee
For the State Bar of Texas

QUESTION PRESENTED

May a law firm hire a lawyer who is not an associate, partner, or shareholder of the law firm to provide legal services for a client of the firm and then bill the client a higher fee for the work done by that lawyer than the amount paid to the lawyer by the firm?

STATEMENT OF FACTS

A law firm enters into an arrangement with a lawyer who is not an associate, partner or shareholder of the law firm to work on a matter for a client. The law firm will pay the lawyer an agreed-upon amount for his work on the matter, but the lawyer will not assume joint responsibility with the law firm for the representation. The law firm intends to charge the client an hourly fee established by the law firm for the lawyer's work as well as for the work of the partners, shareholders and associates of the law firm. The result is that the law firm will charge the client more for the lawyer's work than the law firm is paying the lawyer for that work. The lawyer will be identified on the law firm's bills along with a description of the work done and the hours spent doing that work, but the amount paid by the law firm to the lawyer will not be disclosed to the client.

DISCUSSION

Rule 7.01(a) of the Texas Disciplinary Rules of Professional Conduct refers to lawyers practicing under a firm name, and Rule 7.01(d) provides that "[a] lawyer shall not hold himself or herself out as being a partner, shareholder, or associate with one or more other lawyers unless they are in fact partners, shareholders, or associates." Rule 1.04(f) deals with a division of fees between "lawyers who are not in the same firm . . . ." The Terminology Section of the Texas Disciplinary Rules provides that "'Firm' or 'Law firm' denotes a lawyer or lawyers in a private firm; or a lawyer or lawyers employed in the legal department of a corporation, legal services organization, or other organization, or in a unit of government" and that "'Partner' denotes an individual or corporate member of a partnership or a shareholder in a law firm organized as a professional corporation."

Rule 1.04(f) requires that, when a law firm and a lawyer who is not "in" the firm divide legal fees or agree to do so, the division must meet several requirements: (1) either the billing is in proportion to services performed or the lawyers involved assume joint responsibility for the matter, (2) the client consents in writing to the terms of the fee division arrangement, and (3) the total fee complies with the requirement of Rule 1.04(a) that a fee for legal services not be unconscionable.

If a lawyer is "in" the law firm that is billing for the lawyer's work, such billing will not involve a division of fees and the requirements of Rule 1.04(f) will not apply. To determine whether a lawyer is or is not "in" a law firm, the relationship between the lawyer and the law firm must be considered in more detail. A lawyer will either be in the law firm and referred to in this opinion as a "firm lawyer" or not in the law firm and referred to in this opinion as a "non-firm lawyer." The Texas Disciplinary Rules do not provide guidance on when a lawyer is in a law firm for purposes of the Rules. That may be in part because traditionally law firms consisted basically of partners or shareholders and "associates," who were

any lawyers employed by the law firm who were not partners or shareholders. Today the legal services landscape is more varied.

In the case of a firm lawyer, his relationship with the firm may be as a shareholder, partner, or associate or he may have some other type of relationship with the firm. For the purposes of this opinion, firm lawyers who are not shareholders, partners, or associates will be referred to "other firm lawyers." Other firm lawyers are lawyers that are reasonably considered to be "in" the law firm. Such a determination can be based on various objective factors, including but not limited to the receipt of firm communications, inclusion in firm events, work location, length and history of association with the firm, whether the firm and the lawyer identify or hold the lawyer out as being in the firm to clients and to the public, and the lawyer's access to firm resources including computer data and applications, client files and confidential information. Examples of other firm lawyers include lawyers referred to as of counsel, senior attorneys, contract lawyers and part-time lawyers.

Just as with partners, shareholders and associates, a firm may establish an hourly rate for other firm lawyers that results in the firm charging the client more for the work of the other firm lawyers than the law firm is paying those lawyers for that work. Doing so does not mislead or deceive the client because other firm lawyers are understood to be "in" the firm, as are partners, shareholders and associates. For the same reasons, the law firm may identify other firm lawyers on the firm's bills with a description of the work, the hours expended, and the lawyer's hourly rate. Doing so does not violate either Rule 1.04(f) or Rule 7.01.

For the purposes of this opinion, the term "non-firm lawyer" as applied to a particular lawyer's relationship to a law firm means a lawyer who is not "in" the law firm and instead practices separately from the law firm even when working with the firm on a particular client's matter. The determination as to whether a particular lawyer is or is not "in" a particular law firm can be based on the various objective factors discussed above. Examples of non-firm lawyers can include outside patent counsel, local counsel, counsel with expertise dealing with a particular government agency, counsel in another state hired to advise regarding the application of that state's laws, and lawyers hired individually or through another organization that provides temporary additional staffing or capabilities such as document review or research for a particular matter. In many cases, a non-firm lawyer is in fact a member of another law firm.

In the case of non-firm lawyers, it is the opinion of the Committee that a division of fees subject to Rule 1.04(f) is not involved if the law firm bills the client as an expense, and without markup, the non-firm lawyer's fees which have been billed to the law firm by the non-firm lawyer. Billing for a non-firm lawyer's services as an expense should not be considered a division of fees implicating Rule 1.04(f) because there is in fact no division of fees taking place – the law firm is billing and collecting for the law firm the fees due for the law firm's services and the law firm is billing, collecting and paying over the fees charged by the non-firm lawyer for that lawyer's services. Although treating a non-firm lawyer's bills as an itemized expense without markup would be the most usual arrangement in such cases, the law firm could also avoid a division of fees while including the non-firm lawyer's work in hourly billing provided that there was a clear presentation in the bill of the non-firm lawyer's billed time and resulting bill amount without markup or markdown. In this latter billing arrangement, the law firm would also be required to indicate clearly in the bill that the non-firm lawyer was not a lawyer in the firm.

Under Rule 1.04(f), a division of fees will exist when a law firm includes in its bills fees for work done by a non-firm lawyer and the amounts billed to the client for the non-firm lawyer's work differ from the amounts billed by the non-firm lawyer to the law firm for such work. In that situation, either the non-firm lawyer is sharing fees for his services with the law firm or the law firm is sharing a portion of its fees with the non-firm lawyer. For example, consider the situation in which a law firm is handling a lawsuit

for a client and then brings in a non-firm bankruptcy lawyer for advice on a particular issue. In one month the bankruptcy lawyer bills the firm $500 for five hours of work on the case billed at the bankruptcy lawyer's standard billing rate of $100 per hour. The law firm may, without engaging in a division of fees subject to Rule 1.04(f), bill to the client the $500 billed by the bankruptcy lawyer either as an expense or as hourly work for which exactly $500 is included in the law firm's fee. However, if the firm bills the client more than $500 (say, $600) for the bankruptcy lawyer's work, there will be a division of fees between the firm and the bankruptcy lawyer because the law firm rather than the bankruptcy lawyer will receive the excess (in this example $100) over the $500 billed by the bankruptcy lawyer for his 5 hours of work. There would also be a division of fees if the law firm chose to bill the client less than $500 (say $450) for the bankruptcy lawyer's work because in that case the law firm would be sharing with the bankruptcy lawyer the law firm's fees to the extent the amount collected for the bankruptcy lawyer's work itself was insufficient to cover the full $500 due to the bankruptcy lawyer – in this example $50 of the law firm's fees would be shared with the non-firm lawyer.

Thus, in the case of non-firm lawyers, when a law firm bills a client for the work of the firm's lawyers and for the work of a non-firm lawyer, there will be a division of fees under Rule 1.04(f) unless the law firm bills the non-firm lawyer's fee to the client in the same amount as billed to the law firm by the non-firm lawyer. If there is a difference between the amount billed by the non-firm lawyer and the amount charged by the law firm to the client with respect to this work, such billing will not be permissible unless all the requirements of Rule 1.04(f) are met – proportionality of fees to services performed or joint responsibility for the representation, written client consent to the terms of the fee division, and a total fee that is not unconscionable under Rule 1.04(a). In addition, Rule 7.01(d) will prohibit the law firm from incorporating the non-firm lawyer's name, work and time into its own bill unless the law firm does so in a way that identifies the non-firm lawyer as a lawyer who is not in the firm.

The Committee notes that the conclusions reached in this opinion differ substantially from the conclusions reached in American Bar Association Standing Committee on Ethics and Professional Responsibility Formal Opinion 00-420 (November 29, 2000) (the "ABA Opinion"). The ABA Opinion concluded, interpreting rules similar to the applicable provisions of the Texas Disciplinary Rules, that if the costs associated with a contract lawyer's services are billed as an expense they should not be greater than the actual cost incurred by the billing lawyer (including expenses of the billing lawyer in obtaining and providing to the client the services of the contract lawyer) but that a billing lawyer may add a surcharge for the services of a contract lawyer when the services are billed to the client as a fee for legal services provided that the total charge is reasonable. However, for the reasons set forth above, this Committee believes that the conclusions reached in the present opinion correctly interpret the provisions of the Texas Disciplinary Rules of Professional Conduct applicable to Texas lawyers with respect to the issues addressed in this opinion.

CONCLUSION

Under the Texas Disciplinary Rules of Professional Conduct, a law firm may establish an hourly rate for a lawyer who is not a shareholder, partner or associate but is otherwise "in" the firm, the law firm may use that hourly rate in billing clients for such lawyer's work at a rate that is more than the law firm is paying the lawyer for that work, and the law firm may identify such lawyer on the firm's bills with a description of the work performed, the hours expended, and the lawyer's hourly rate without distinguishing such lawyer from other lawyers in the firm and without disclosing the amount paid by the firm to such lawyer. However, when a law firm bills a client for legal services provided by a lawyer that is not "in" the law firm, there will be a division of fees between the law firm and the lawyer unless the law firm bills the client precisely the amount that has been billed to the law firm by such lawyer. Any arrangement for division of fees between a law firm and a non-firm lawyer would be required to meet all

the requirements of Rule 1.04(f) - proportionality of fees to services performed or joint responsibility for the representation, written client consent to the terms of the fee division, and a total fee that is not unconscionable under Rule 1.04(a). In addition, the law firm would be prohibited from incorporating a non-firm lawyer's name, work and time into its own bill unless it did so in a way that showed that the non-firm lawyer was not in the firm.