

## Opinion No. 642, May 2014

### QUESTIONS PRESENTED

1. May a Texas law firm include the terms “officer” or “principal” in the job titles of the firm’s non-lawyer employees?
2. May a Texas law firm pay or agree to pay specified bonuses to non-lawyer employees contingent upon the firm’s achieving a specified amount of revenue or profit?

### Statement of Facts

A Texas law firm employs non-lawyer professionals to manage the firm’s business, including its marketing, advertising, IT services, and search-engine optimization. The firm plans to give these employees the titles “chief executive officer” and “chief technology officer” and to identify them as “principals” in the law firm. In addition to paying salaries to these employees, the firm intends to pay them specified bonuses if the firm achieves a designated amount of revenue or profit.

### Discussion

The term “officer” in titles such as “chief executive officer” or “chief technology officer” indicates that the person holding the title has the power to control either the entire law firm (in the case of “chief executive officer”) or significant areas of the firm’s operations (in the case of “chief technology officer”). Use of the term “principal” for non-lawyer employees implies that the employees have an interest in the firm involving control, ownership, or both.

The Texas Disciplinary Rules of Professional Conduct generally do not permit Texas lawyers to allow non-lawyers to have controlling or ownership interests in their law firms. Rule 5.04(a) provides that “[a] lawyer or law firm shall not share or promise to share legal fees with a non-lawyer,” subject only to limited exceptions not applicable here. In the case of a law firm organized as a for-profit professional corporation or association, Rule 5.04(d)(2) prohibits lawyers from

practicing law with such an organization if “a nonlawyer is a corporate director or officer thereof[.]” Moreover, Rule 5.04(d)(3) prohibits a lawyer from practicing law in the form of a for-profit professional corporation or association if “a nonlawyer has the right to direct or control the professional judgment of a lawyer.” In the case of a law firm organized as a partnership, the conclusion is the same: A non-lawyer may not control a partnership’s provision of legal services. Rule 5.04(b) prohibits a lawyer from forming a partnership with a non-lawyer if any of the activities of the partnership consist of the practice of law.

If the non-lawyer employees will not, in fact, control operations of the law firm nor own an interest in the firm, then designating these employees as “officers” or “principals” would be misleading and thus violate Rule 7.02(a), which states: “A lawyer shall not make or sponsor a false or misleading communication about the qualifications or the services of any lawyer or firm.” Identifying a person as an “officer” or a “principal” in a law firm when the person does not, in fact, have a controlling or ownership interest in the firm would be a false or misleading communication about the firm. Furthermore, using the title “officer” or “principal” for a non-lawyer employee who does not act as an “officer” or “principal” of the firm would violate Rule 8.04(a)(3), which prohibits a lawyer from engaging in “conduct involving dishonesty, fraud, deceit or misrepresentation[.]”

The law firm’s plan to pay specified bonuses to non-lawyer employees contingent upon the firm’s achieving a specified amount of revenue or profit requires consideration of Rule 5.04(a), which prohibits a lawyer or law firm from sharing or promising to share legal fees with a non-lawyer, except in instances not applicable here.

Comment 1 recognizes that Rule 5.04(a)’s purpose is to deter lawyers from providing an incentive for non-lawyers to practice law or to solicit clients for the lawyers. The law firm’s proposed plan for paying bonuses is the type of plan that Rule 5.04(a) forbids: one that is tied to achieving a specified level of revenue or profit. Such a plan would provide an incentive for the firm’s non-lawyer employees to increase revenues, which could be accomplished through soliciting clients, or to reduce expenses, which could be accomplished by interfering with a lawyer’s independent judgment in practicing law. Furthermore, tying a bonus to achieving a specified level of profit is similar to tying a bonus to achieving a specified level of revenue because profit is a function of revenue and expenses.

Of course, a law firm’s willingness and ability to pay bonuses will depend upon the firm’s profitability. As a practical matter, a law firm may consider its revenue, expenses, and profit in determining whether to pay bonuses and, if so, how much. In the Committee’s opinion, Rule 5.04(a) does not preclude a law firm from taking

such considerations into account when paying or promising to pay bonuses. Rule 5.04(a) does, however, prohibit a law firm from agreeing to pay a non-lawyer employee a specified bonus that is tied to specified revenues or profits, such as: “We will pay you a bonus of \$10,000 if the firm’s revenue (or profit) for the year is at or above \$1 million.”

### Conclusion

Under the Texas Disciplinary Rules

of Professional Conduct, a Texas law firm may not use “officer” or “principal” in the job titles for non-lawyer employees of the firm.

The Texas Disciplinary Rules of Professional Conduct also prohibit a Texas law firm from paying or agreeing to pay specified bonuses to non-lawyer employees contingent upon the firm’s achieving a specified level of revenue or profit. A Texas law firm may, however, consider its revenue,

expenses, and profit in determining whether to pay bonuses to non-lawyer employees and the amount of such bonuses. **TBJ**

*The Supreme Court of Texas appoints the nine members of the Professional Ethics Committee from members of the bar and the judiciary. The court also appoints the committee’s chair. According to Section 81.092(c) of the Texas Government Code, “Committee opinions are not binding on the supreme court.”*



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- Conduct and procedural rules
- Information about the attorney grievance system
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The webpage will be updated regularly to ensure it remains current.

## Opinion No. 643, May 2014

### QUESTION PRESENTED

*Under the Texas Disciplinary Rules of Professional Conduct, is it permissible for a lawyer to arrange for a debt management services company owned by the lawyer to refer customers of the company to the lawyer's law firm for legal services?*

### Statement of Facts

A lawyer, who practices law in a law firm owned and controlled by the lawyer, creates a debt management services company in accordance with chapter 394 of the Texas Finance Code to assist customers in settling their debts. The debt management services company is separate from the law firm and does not provide legal services. The lawyer wishes to arrange for the debt management services company to refer its customers who are in need of legal services to the law firm.

### Discussion

Debt settlement companies provide advice to customers about strategies related to their finances and they seek to negotiate the reduction or settlement of their customers' debts. In many cases, advice on a customer's debt situation would include consideration of existing or potential legal claims against the customer and possible legal actions that might be taken by the customer with respect to these claims. For these legal matters the customer would need legal advice and representation and the customer would frequently be open to recommendations as to a lawyer or law firm to provide such legal services.

Under the Texas Disciplinary Rules of Professional Conduct, "a lawyer should act with competence, commitment and dedication to the interest of the client and with zeal in advocacy on the client's behalf." Comment 6 to Rule 1.01. Rule 2.01 requires that a lawyer "exercise inde-

pendent professional judgment and render candid advice."

The Disciplinary Rules prohibit a lawyer from representing a client in a matter where the lawyer's interests conflict with the interests of the client except in situations where a client may appropriately consent to the representation after being fully informed concerning the conflict. Rule 1.06(b) provides in pertinent part as follows:

"... except to the extent permitted by paragraph (c), a lawyer shall not represent a person if the representation of that person:

...

(2) reasonably appears to be or become adversely limited by the lawyer's or law firm's responsibilities . . . to a third person or by the lawyer's or law firm's own interests."

Loyalty and zealousness on behalf of a client are impaired when a lawyer's own interests foreclose alternative courses of action that should be considered for a client. See Comment 4 to Rule 1.06. Comment 5 to Rule 1.06 cautions that "[a] lawyer should not allow related business interests to affect representation . . . ."

Thus the lawyer and his law firm must address the question of whether representation of customers of the company will involve impermissible conflicts of interest. When the lawyer's law firm has accepted a referral from the debt management services company of a legal matter involved in the

customer's debt situation, the law firm will necessarily be advising the company's customer concerning matters on which the debt management services company has also given advice. The law firm is required by the Texas Disciplinary Rules to provide legal advice based solely on the best interest of the law firm's client, but the law firm will in these circumstances almost certainly be limited in its ability to provide independent advice concerning courses of action that have been recommended or rejected by the debt management services company. Thus there will inevitably arise a conflict of interest under Rule 1.06(b)(2)—the representation of the company's customer by the law firm will reasonably appear to be limited by the lawyer's interests as owner of the debt management services company.

Even in the presence of a conflict of interest under Rule 1.06(b)(2), a lawyer may continue to represent a client if the requirements of Rule 1.06(c) are met:

"A lawyer may represent a client in the circumstances described in (b) if:

(1) the lawyer reasonably believes the representation of each client will not be materially affected; and

(2) each affected or potentially affected client consents to such representation after full disclosure of the existence, nature, implications, and possible adverse consequences of the common representation and the advantages involved, if any."

Applying the provisions of Rule 1.06(c), the lawyer must first reasonably determine whether his ownership of the debt management services company will materially affect his law firm's legal representation of the client. The lawyer, as owner of the company, would have a strong interest in the well-being of the debt management services company and, at the same time, would as a lawyer owe undivided loyalty to the client. This is exactly the type of situation that the provisions of Rule 1.06(b) and (c) are intended to prevent. In the opinion of the Committee, the lawyer could not reasonably believe that, if the interests of the debt management services company and the client came into conflict, the lawyer and his law firm could act with commitment and dedication to the client or that he could exercise independent professional judgment and render candid and critical advice concerning the client's debt situation and lawsuits or claims that might arise from that debt. In all cases where the law firm proposes to provide legal representation to a customer of the company on matters relating to the customer's debt situation, the Committee believes that the lawyer and his law firm could not reasonably determine, as required by Rule 1.06(c)(1), that representation of the client would not be materially affected by the lawyer's ownership of the debt management services company. Accordingly it is the opinion of the Committee that the law firm could not accept referrals of customers of the debt management services company as to matters on which the debt management services company has provided any type of services. Only where there was a referral to the law firm of legal matters wholly unrelated to the matters for which the debt management services company provided advice would the law

firm be able to accept the referral without violation of the conflict of interest rules.

In other similar circumstances, this Committee has determined that a lawyer would be unable to comply with the requirements of Rule 1.06(c)(1). In Professional Ethics Committee Opinion 543 (April 2002), the Committee determined that the requirements of Rule 1.06(c)(1) could not be met where a health care provider referred patients with personal injury claims to a lawyer who was also the health care provider's in-house counsel. Similarly, in Opinion 555 (December 2004), the Committee determined that a lawyer's ownership interest in a chiropractic practice to which the lawyer would refer his clients for treatment would create a conflict of interest under Rule 1.06(b) that could not be cured by client consent under Rule 1.06(c). Finally, in Opinion 641 (May 2014), the Committee determined that the conflict of interest inherent in the situation where a financial planning services company refers customers to a lawyer who is regularly engaged by the financial planning services company cannot normally be cured under Rule 1.06(c) even with consent of the clients concerned except in the case of legal matters unrelated to the customer's relationship with the company.

In the case of legal matters referred by the debt management services company to the lawyer's law firm that do not involve prohibited conflicts of interest, the lawyer, in his role as owner and controlling person of the debt management services company and in his role as owner of his law firm, will be required to act honestly and avoid actions that would constitute dishonesty or misrepresentation prohibited by Rule 8.04(a)(3). The

lawyer, as the person owning and controlling the debt management services company, would not be permitted to cause or permit the company to recommend the lawyer's law firm to a customer of the company unless the law firm was appropriate for the provision of legal services in the particular case. Moreover, in these circumstances, any recommendation of the lawyer's law firm would have to be accompanied by disclosure of the common ownership and control of the debt management services company and the law firm. Finally, the lawyer could not through his debt management services company provide below cost services or other benefits to customers as a means of soliciting business for the lawyer's law firm in violation of Rule 7.03(c).

### Conclusion

Under the Texas Disciplinary Rules of Professional Conduct, it is not permissible for a lawyer to arrange for a debt management services company owned by the lawyer to refer customers of the company to the lawyer's law firm for legal services except as to matters unrelated to matters for which the company has provided services to the customer. A referral in such an unrelated matter would be permitted if the lawyer's law firm was an appropriate provider of services in the matter, the fact of the common ownership of the company and the law firm was disclosed to the customer of the company, and the debt management services company did not provide benefits to the customer to promote business for the lawyer's law firm. **TBJ**

*The Supreme Court of Texas appoints the nine members of the Professional Ethics Committee from members of the bar and the judiciary. The court also appoints the committee's chair. According to Section 81.092(c) of the Texas Government Code, "Committee opinions are not binding on the supreme court."*