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 contingency fee agreements ethically permissible?

DIGEST: A conversion clause—a provision in a contingent fee agreement that, upon a specified triggering event, converts the contingent fee to an alternate fee, such as an hourly rate, a lodestar amount, or a percentage of a settlement offer—is not prohibited per se under the Rules of Professional Conduct. However, such clauses warrant careful consideration, because they carry a heightened risk of resulting in an unconscionable fee or impairing rights the rules reserve to the client. A conversion clause is ethically impermissible where it burdens the client's absolute right to discharge counsel, where it interferes with the client's rights to control the objectives of the representation, or where the alternate fee is unconscionable. Whether a particular conversion clause crosses these lines depends on the facts and circumstances, including the sophistication of the client, the client's informed written consent, the nature and timing of the triggering event and alternate fee, and whether the alternate fee is unconscionable.

AUTHORITIES INTERPRETED: Rules 1.2, 1.5, and 1.16 of the Rules of Professional Conduct of the State Bar of California.[1]

INTRODUCTION

This opinion addresses the use of conversion clauses in contingent fee agreements.[2] In a traditional contingent fee arrangement, the lawyer receives no fee unless the client prevails. Contingent fee agreements are commonly used by lawyers representing plaintiffs in personal injury matters and function to shift the risks associated with the cost of litigation such that the lawyer receives no fee unless the client prevails and the lawyer receives a fee premium if the client prevails. (See Colorado Bar Association Ethics Committee Formal Ethics Opinion 100 (1997).) However, similar agreements are increasingly used in other types of representations, including with sophisticated clients in transactional matters. (See *Arnall v. Superior Court.*

---

1 Unless otherwise indicated, all references to "rules" in this opinion will be to the Rules of Professional Conduct of the State of California.

2 This opinion does not address whether or to what extent conversion clauses are legally enforceable, as that question requires an analysis of issues beyond the purview of this Committee. Additionally, this opinion does not address the enforceability of attorney liens.

(2010) 190 Cal.App.4th 360, 368 (a fee agreement entitling attorney to a "success fee" calculated as a percentage of client's tax savings or reduction in adverse tax impact was held to be a contingent or hybrid fee arrangement subject to Bus. & Prof. Code, § 6147.)).

For purposes of this opinion, a conversion clause is a provision that, if triggered, converts a contingent fee to an alternate fee (e.g., a fee based on lodestar calculations, a percentage of the most recent settlement offer, or a specific hourly rate). Some conversion clauses operate to reallocate risks by transferring certain risks back to the client. For example, a conversion clause in a contingency fee agreement might require the payment of an alternate fee if certain events occur before the contingency, such as a client deciding not to complete a transaction or settle a matter or choosing to terminate the lawyer or declining to follow the lawyer's advice concerning settlement. Such clauses pose the risk of interfering with a client's right to discharge counsel or control the objectives of the representation, including determining whether to settle and the terms of any settlement. These clauses also pose the risk of creating an unfair bargaining situation or an unconscionable fee.

However, starting from the basic premise that the negotiation of a fee agreement at the outset of a matter is an arm's-length transaction (see *Setzer v. Robinson* (1962) 57 Cal.2d 213, 217 [18 Cal.Rptr. 524]), the Committee recognizes that there is no prototypical client, lawyer, or risk allocation for all contingent fee arrangements. This opinion does not address all circumstances in which conversion clauses are prohibited by the rules, nor does it address all circumstances in which conversion clauses are ethically permissible. A lawyer must carefully consider the facts and circumstances in determining whether a conversion clause is ethically permissible under the circumstances and the relevant rules.

STATEMENT OF FACTS

Hypothetical 1

Corporate Client retains Lawyer to negotiate the acquisition of a target company. Because Corporate Client has limited liquidity, the parties agree in advance to a hybrid contingent fee. Lawyer will receive a reduced hourly rate plus a success fee calculated as a percentage of the amount paid for the acquired company.

The fee agreement includes a conversion clause that changes the fee arrangement if Corporate Client materially changes its objectives. Under the clause, if Corporate Client decides not to proceed with the acquisition for reasons unrelated to Lawyer's advice, Lawyer's compensation converts to a specific hourly rate for work performed to date. The hourly fee is subject to a cap, and payment is required only if Corporate Client abandons the transaction. Corporate Client understands the terms of the fee agreement and gives its informed written consent.

Midway through negotiations, Corporate Client reassesses the market and determines that the acquisition no longer aligns with its business strategy. Corporate Client instructs Lawyer to cease work. This decision triggers the conversion clause, entitling Lawyer to the specific hourly rate, subject to the agreed-upon cap.

Hypothetical 2

Plaintiff retains Lawyer under a standard contingent fee agreement in a personal injury lawsuit. The agreement contains a conversion clause requiring that, if Plaintiff discharges Lawyer before settlement or judgment, Lawyer becomes immediately entitled to the full contingent fee based on the most recent settlement offer. The fee is payable regardless of how much work Lawyer has completed.

After several months, Plaintiff becomes dissatisfied with Lawyer's communication. Plaintiff seeks new counsel. Several potential replacement attorneys decline representation because the conversion clause obligates Plaintiff to pay Lawyer a large fee upon discharge. That payment would leave insufficient recovery available to compensate successor counsel under a contingent fee arrangement.

Because of the financial consequences imposed by the conversion clause, Plaintiff faces significant difficulty finding replacement counsel.

DISCUSSION

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

Both the rules and California case law confirm a client's absolute right to discharge his or her attorney. (See 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 must be carefully reviewed to ensure that they do not impermissibly interfere with a client's absolute right to discharge counsel.

A conversion clause that renders it difficult or impossible for the client to secure replacement counsel is likely to place an impermissible burden on the client's right to discharge counsel.[3] This might happen, for example, if the alternate fee entitles the lawyer to more than the client

[3] In addition to impermissibly interfering with a client's right to discharge the lawyer, such a conversion clause may likely also be found to be an attempt to charge or collect an unconscionable fee. (See e.g., *In re Van Sickle* (Review Dept. 2006) 4 Cal. State Bar Ct. Rptr. 980, 987-988 ("our finding of unconscionability is based on the hearing judge's finding that respondent failed to disclose to [client] that he intended his 35 percent contingency fee to be in addition to the fee earned by [client's former counsel]"); see also Colorado Bar Association Ethics Committee Formal Ethics Opinion 100 (1997).)

will receive or otherwise leaves inadequate incentive for replacement counsel to accept the matter.[4]

The timing of the payment of the alternate fee may also create an impermissible burden on the client's right to discharge counsel. For example, if a conversion clause entitles a discharged lawyer to the alternate fee upon discharge, the resulting financial burden may cause the client to remain with the lawyer when they otherwise would have chosen to terminate the representation. This is true even if the alternate fee would otherwise be permissible if due upon the occurrence of the contingency because the *timing and fact* of the payment changes the nature of the risk. (See *Fracasse v. Brent* (1972) 6 Cal.3d 784; see also *Kroff v. Larson* (1985) 167 Cal.App.3d 857.) On the other hand, a conversion clause that permits recovery of an alternative fee for the attorney's hourly rate in the event a client backs out of a deal may not be impermissible, depending on the sophistication of the client, the extent to which the foreseeable risks were understood by the client, and whether the alternate fee creates an unconscionable fee.

B. The Client's Right to Control the Objectives of Representation

A lawyer is ethically required to abide by a client's decision concerning the objectives of the representation, including the decision to accept or reject a settlement offer. (See rule 1.2(a) ("[A] lawyer shall abide by a client's decision whether to settle a matter."). However, conversion clauses are sometimes structured to ensure a fee where a client accepts or rejects a settlement against the lawyer's recommendation. For example, in cases where a client rejects a settlement offer recommended by the lawyer, such conversion clauses may purport to entitle the lawyer to a percentage of the recommended settlement amount. In cases where a client accepts a settlement offer against the recommendation of the lawyer, such conversion clauses may purport to entitle the lawyer to hourly rates for work performed.

While ethics committees of other states have approached such settlement-related conversion clauses in different ways[5], such clauses deserve careful consideration. It is the view of the

---

[4] See *In re Van Sickle* (Review Dept. 2006) 4 Cal. State Bar Ct. Rptr. 980, 989 ("[T]he agreed upon contingent fee acts as an upper limit on the amount to be divided on a quantum meruit theory between the discharged and retained attorneys hired on a contingency basis in the same case (internal citation omitted)]. See also *In re Van Sickle*, *supra*, 4 Cal. State Bar Ct. Rptr. at page 988, footnote 11 ("Under *Fracasse v. Brent* (1972) 6 Cal.3d 784, 790–791, an attorney…who is discharged before the contingency occurs, and who was initially hired pursuant to a contingent fee contract, is entitled to be compensated on a quantum meruit basis for the reasonable value of his or her services, rather than at the contract price.").

[5] See, e.g., 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 Professional Guidance Committee Formal 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, but not for unsophisticated clients); Nebraska State Bar Association Ethics Advisory Opinion for Lawyers No. 95-1 (1995) (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, impermissibly restricts the client's authority to settle a matter).

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 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 granting 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]; *In the Matter of Guzman* (Review Dept. 2014) 5 Cal. State Bar Ct. Rptr. 308, 314 [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"].) However, the Committee can conceive of circumstances, however rare, where a conversion clause might ethically and reasonably account for a client's material change in objectives inconsistent with the advance agreement reached between the lawyer and client when the lawyer agreed to undertake a representation. (Cf. *Ramirez v. Sturdevant* (1994) 21 Cal.App.4th 904, 918 [in a matter not involving a conversion clause, lawyer conditioned continued representation on client's agreement to a minimum settlement]; *Little v. Amber Hotel Co.* (2011) 202 Cal.App.4th 280, 296 [in a matter not involving a conversion clause, court held that a provision requiring lawyer's consent to settle is void and against public policy, but held that "fee agreements containing reasonable limitations on the client's authority to settle an action are enforceable."]). For this reason, the Committee believes careful review is appropriate, rather than a per se prohibition.

C. The Attorney's Duty Not to Make an Agreement for, Charge, or Collect an Unconscionable Fee

Heightened caution is warranted where the fee agreement allows conversion to be susceptible to manipulation by the lawyer.[6] Conversion clauses triggered by the acceptance or rejection of settlement offers are ethically impermissible if they have the effect of restricting the client's right to determine the objectives of the representation, including whether or not to settle (or on what terms).

Rule 1.5 prohibits a lawyer from making an agreement for, charging, or collecting an unconscionable fee, and sets forth 13 factors to be considered (without limitation) in determining the unconscionability of a fee. Just as any contingent fee must comply with rule 1.5, so too must any alternate fee arising from a conversion clause. The determination of whether a conversion clause would result in an unconscionable alternative fee requires analysis of the terms of the clause and its application to the specific circumstances.

---

[6] See also Nebraska State Bar Association Ethics Advisory Opinion for Lawyers No. 95-1 (1995) (noting that conversion clauses tied to settlement are problematic because, among other things, "theoretically, once the lawyer has invested enough time in the matter that the contingent fee of any reasonable settlement will not be sufficient, the attorney could withhold approval and charge an hourly fee . . . Determining whether a lawyer is legitimately withholding approval of a settlement offer or wrongfully doing so would be extremely difficult . . . This difficult issue could be completely avoided by prohibiting the proposed contractual provision in the first place.").

A conversion clause that calls for payment of an alternate fee *prior* to the completion of the matter is likely to be unconscionable if it purports to entitle the lawyer to a risk premium[7] where no risk is present and there has been no change in the client's objectives. (See rule 1.5(b)(1)-(b)(2) [concerning overreach, fraud, and failure to disclose material facts]; see also *Fracasse v. Brent* (1972) 6 Cal.3d 784; *Kroff v. Larson* (1985) 167 Cal.App.3d 857.) Similarly, a conversion clause that requires payment of a predetermined contingent fee to a discharged lawyer, regardless of the work actually performed or the amount of work remaining in the matter, is unlikely to survive an unconscionability analysis.[8] (See rule 1.5(b)(3), (b)(7), & (b)(12); see also *In the Matter of Scapa and Brown* (Review Dept. 1993) 2 Cal. State Bar Ct. Rptr. 635.)[9]

Unconscionability of the alternative fee in the event of discharge would be determined on the basis of all facts and circumstances existing at the time of the termination because that would be the event triggering the fee. (See rule 1.5(b); *In the Matter of Yagman* (Review Dept. 1997) 3 Cal. State Bar Ct. Rptr. 788, 800.) Thus, the predetermined contingent fee or the hourly fees would need to be analyzed under the relevant factors, including proportionality between the amount of the fee and the value of the services performed by the attorney before termination, the sophistication of the client, novelty, difficulty and skill required by the legal services and the client's informed consent, among other factors.[10] In analyzing unconscionability, the sophistication of the client is a factor because contingent fee agreements can be complex in both construction and effect. (See, e.g., *Cotchett, Pitre & McCarthy v. Universal Paragon Group* (2010) 187 Cal.App.4th 1405 [114 Cal.Rptr.3d 781]; see also rule 1.5(b)(4), rule 1.4.) Similarly, in certain circumstances a lawyer's advertising may be a relevant factor for consideration.

D. Analysis of Hypothetical Scenarios

In Corporate Client's case, the conversion clause reflects an effort to address a material shift in the risk allocation underlying the hybrid fee arrangement and, in form, does not appear to restrict Corporate Client's authority to determine the objectives of the representation. However, the key issue is not just whether the client technically has the right to decide, but whether the fee arrangement might discourage the client from exercising that right. A provision reverting to a specific hourly fee for work performed may align with quantum meruit principles, particularly if the resulting fee reflects the reasonable value of services rendered. However, a

---

7 See Wisconsin State Bar Professional Ethics Committee Formal Opinion No. E-82-5 (1982) ("the large attorney's fees which are generated by the contingent fee can only be justified because of the risks the lawyers must bear of not making an adequate recovery to cover his or her time in certain cases. The client's desire to accept a less than satisfactory settlement offer is an inherent part of that risk. To suggest a lawyer can have it both ways with the use of the proposed clause is not acceptable to the committee.").

8 This opinion does not address fee-splitting agreements between attorneys, or between departing attorneys and their firms.

9 Established law already provides for payment to discharged contingent fee counsel on a *quantum meruit* basis where appropriate.

10 While rule 1.5 determines unconscionability for purposes of an attorney's ethical duties, California law requires that attorney fee agreements and billings "must be fair, reasonable and fully explained to the client." (See *Bird, Marella, Boxer & Wolpert v. Superior Court* (2003) 106 Cal.App.4th 419, 430–431 [130 Cal.Rptr.2d 782].)

clause conditioning payment solely on the client's decision to abandon the transaction presents a closer question, as it may create an economic consequence tied specifically to a change in Corporate Client's objectives. In other words, the Corporate Client agrees to pay a price for terminating the representation because it would be no longer necessary. Here, provided Corporate Client gives its informed written consent to the terms of the agreement, the hourly fee is reasonable, tied to the value of the work performed, and does not interfere with Corporate Client's right to discharge the attorney, the conversion clause may be ethically permissible.

In Plaintiff's case, the conversion clause may interfere with Plaintiff's right to discharge Lawyer because it imposes an immediate and significant financial burden that discourages Plaintiff from exercising the right to terminate representation. The clause requires payment of a predetermined contingent fee that does not reflect the value of the services performed and is triggered by discharge itself rather than the outcome of the matter, which makes it difficult for Plaintiff to secure alternate counsel. These factors create a barrier to Plaintiff's right to choice of counsel and risk producing an unconscionable fee, thereby making the alternate fee ethically impermissible.

CONCLUSION

While not all conversion clauses are prohibited by the rules, they do warrant caution. Conversion clauses that improperly interfere with a client's right to terminate an attorney, or with a client's right to control the objectives of the representation (including the right to decide whether to settle and on what terms) are ethically prohibited, as are conversion clauses that would result in an unconscionable fee.

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.