

OPINION 531

December 1999

Question

May a corporation charge wholly-owned or partially-owned subsidiaries "market-based" fees for legal services rendered by the corporate legal staff? If not, may a corporation initially charge its subsidiaries "market-based" fees for legal services if the amounts of fees in excess of "costs" to the corporation are annually rebated to the subsidiaries?

Statement of Facts

A Texas-based, multi-national corporation with a large legal staff wishes to provide legal services to its wholly-owned and partially-owned subsidiaries. Instead of charging the subsidiaries for the "costs" of legal services, the legal staff would like to charge "market-based" fees. Unlike "costs", which encompass overhead such as salaries of lawyers and support staff, and rent, "market-based" fees would be comparable to fees charged by lawyers in private practice for rendering the same services. The legal staff *may* annually rebate the subsidiaries those amounts charged which are in excess of "costs."

Discussion

The fact scenario set forth above raises issues governed by Texas Disciplinary [Rule 5.04](#), Professional Independence of a Lawyer, and Texas Disciplinary [Rule 5.05](#), Unauthorized Practice of Law. Each rule will be considered separately, for purposes of responding to the questions set forth above, as will Texas Professional Ethics Committee Opinions and pertinent case law.

[DR 5.04](#) - Professional Independence of a Lawyer

Texas Disciplinary [Rule 5.04](#) provides, in pertinent part, that:

(a) A lawyer or law firm shall not share or promise to share legal fees with a non-lawyer, except ...

[where fees or other sums are paid to the estate of a deceased lawyer, or non-lawyer employees are included in a law firm's retirement plan].

(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 lawyers 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 a profit, if:

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- (1) a non-lawyer 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 non-lawyer is a corporate director or officer thereof; or

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

Tex. Disciplinary R. Prof. Conduct [5.04](#)(a), (c) and (d) (1)-(3), reprinted in, Tex. Gov't Code Ann., tit. 2, subtit. G, app. A (Vernon Supp. 1997).

[DR 5.04](#)(a) clearly prohibits the sharing of legal fees with non-lawyers. [DR 5.04](#)(d) also prohibits practicing law for a profit where non-lawyers either own an interest in the practice, are corporate officers and directors, or have the ability to direct or control the lawyer's professional judgment. Under the facts set forth above, therefore the corporation's legal staff would violate [DR 5.04](#)(a) and (d) were charged *market-based fees* (or fees in excess of costs) for legal services rendered.

Additionally, since a "lawyer's professional judgment should be exercised [only] for the benefit of the client, free of compromising influences and loyalties...under [Rule 5.04](#)(c) a person who recommends, employs, or pays the lawyer to render legal services for another cannot be permitted to interfere with the lawyer's professional relationship with that client." ([DR 5.04](#), Comment 4. *See also* DR1.08(e)(2), Conflict of Interest: Prohibited Transactions "A lawyer shall not accept compensation for representing a client from one other than the client unless [inter alia] there is no interference with the lawyer's independence of professional judgment...").

DR 5.05 - Unauthorized Practice of Law

Texas Disciplinary [Rule 5.05](#) provides, in pertinent part, that a lawyer shall not:

(b) assist a person who is not a member of the bar in the performance of activity that constitutes the unauthorized practice of law. (Tex. Disciplinary R. Prof. Conduct [5.05](#)(b), *reprinted in*, Tex. Gov't Code Ann., tit. 2, subtit. G, app. A (Vernon Supp. 1997).)

The primary intent of [Rule 5.05](#) appears to be that of protecting individuals and the public from the mistakes of "untrained," and the schemes of the unscrupulous. ([DR 5.05](#), Comment 1.) This is clearly *not* a consideration in the fact scenario set forth above, since the legal services to be provided would be rendered by the corporation's legal staff.

"Neither statutory nor judicial definitions [however] offer clear guidelines as to what constitutes the practice of law or the unauthorized practice of law." ([DR 5.05](#), Comment 2.) It is for this reason that the parent corporation could potentially engage in the unauthorized practice of law where *market-based fees* (or fees in excess of costs) are charged for legal services provided to subsidiaries.

Many authoritative sources emphasize the fact that when a non-lawyer corporation profits from the services of its legal staff, the corporation engages in the unauthorized practice of law. In *Stewart Abstract Co. v. Judicial Comm'n of Jefferson County*, 131 S.W.2d 686 (Tex. Civ. App. - Beaumont 1939, no writ), for example, the court directly addressed whether corporations could profit from their in-house attorneys' services:

A corporation has a legal right to employ an attorney or maintain a legal department to handle its own legal business, furnish its opinions, legal counsel or advice for its own benefit in connection with the performance of its lawful duties... But a corporation may not furnish legal services to others and collect fees or profits therefore, directly or indirectly,

and it may be enjoined from doing so. (*Id.* at 690.)

In handling FHA loans, Stewart Abstract Company and Stewart Title Guarantee Company employed attorneys who prepared mortgages, mechanics' liens, and notes for execution by customers, the charge for their services being included in the fee collected for title insurance. (*Id.* at 688-689.) The companies also advertised services regarding examining title to real estate and rendering title opinions, receiving payment therefore as part of a flat fee. (*Id.*) Finding that these actions constituted the unauthorized practice of law, the court affirmed an order granting injunctive relief. (*Id.* at 690.)

In line with *Stewart Abstract*, the Texas Committee on Professional Ethics determined, in Opinion 498, that salaried corporate attorneys could not prepare estate planning documents for customers of a corporation if that corporation received payments for the lawyer's services. In reaching this decision, the committee reasoned that, were the corporation to receive payment, the arrangement would amount to an agreement by the lawyer to share legal fees with a non-lawyer (the corporation) in violation of [Rule 5.04](#) (a). The committee therefore determined that an attorney could not enter an agreement with a corporation that is not a professional corporation owned solely by licensed attorneys under which the attorney is employed on a salaried basis and regularly provides legal services to customers of the corporation, if the corporation receives fees, commissions, or profits there to any extent compensation for the attorney's legal services to the customers.

In Opinion 417, the Texas Professional Ethics Committee further examined this issue in considering whether an attorney could accept employment with a collection agency, sharing in the fees paid to the agency by creditors for legal services. In this regard, the committee opined that an attorney could accept employment from a collection agency provided: (i) the attorney received *all* fees paid to the agency by the creditor for legal services rendered; (ii) the attorney did not permit the agency to direct or interfere with his representation of the creditor; and (iii) the attorney acted as an attorney for the creditor, rather than the agency. The committee found that, otherwise, the attorney would be assisting the non-lawyer agency to engage in the unauthorized practice of law.

Unlike the previous authorities, however, the present situation involves a relationship between a parent corporation and its subsidiaries. The committee has already determined that parent corporations may charge controlled companies the its "costs" for legal services without violating the Texas Disciplinary Rules of Professional Conduct. In Opinion 343, the Professional Ethics Committee considered whether a corporation could charge subsidiaries the "actual costs" of performing legal services without violating the former Texas Canons 32 and 43, and ABA Canons 35 and 47 (regarding intermediaries and the unauthorized practice of law).

In examining this questions, the committee determined that the corporate attorney *could* ethically render legal services for other, related corporations, provided certain safeguards were maintained, *i.e.*, that the employer (unless its interests in a particular matter are identical) not direct or control the manner in which attorney renders legal services, or be allowed to dictate advice given to the subsidiary corporation.

[The attorney] must be sure that it is clear and agreeable to both the employer and the other corporation that, having undertaken to perform legal services for the other corporation...his client in the matter is the corporation for whom the services are to be performed and that in such matter his undivided fidelity is owed to that corporation He must be certain that his services and advice to such corporation are in its interest and he must preserve its confidences inviolate. If there is a conflict of interest between his general corporate employer and the other corporation, then he must, of course, disqualify [himself] unless the

conflict is fully disclosed and expressed consent for representation is given by all concerned.

In Opinion 512, the Professional Ethics Committee considered whether an in-house lawyer of a corporation could represent a joint venture when the employing corporation was party to the venture. The employing corporation wished to provide legal services to the joint venture, provided the joint venture reimbursed the corporation for its legal costs. After considering the issue, the committee determined that the corporation would not be engaging in the unauthorized practice of law so long as: (i) the joint venture *does not reimburse the corporation for more than the full "costs"* of the legal services; and (ii) the corporation does not direct the lawyer in the performance of legal services for the joint venture.

Conclusion

Under the present fact scenario, therefore, the corporation may *not* charge wholly-owned subsidiaries "*market-based fees*" for the legal services rendered by the corporation's in-house counsel. To permit the corporation to recover anything other than its "costs" (even if those costs were later reimbursed to the subsidiary by means of a *rebate*) would permit corporation to profit financially from the legal services provided by its in-house counsel and thereby engage in the unauthorized practice of law.