Applications of Ethics Rules to Attorney Fees in Probate, Trust & Conservatorships

or: How to Get Paid, and How Not to Violate the Rules When Getting Paid

In my view, ethics rules serve two main functions. The first is quite simple: to provide a legal basis to discipline attorneys for doing things that are obviously wrong (stealing money from clients, hitting clients, lying to courts, etc.). The second is more complex and, frankly, more useful to the average attorney: to advise and guide attorneys' actions when the intuitive response to a given situation is actually harmful to the client or to the profession, and that harm is either not obvious or is easily ignored or overlooked. Any attorney that needs to be told not to borrow money from the client trust account is already beyond my help. However, in the desire to help clients, it is easy for even a skilled attorney to miss certain issues or to fail to adequately position the client so that he or she may make an appropriately informed decision, and to proceed accordingly. The new rules appear to rely heavily on written waivers to call attention to these important issues. In the context of these materials, I shall be focusing on the second function of ethics rules, primarily in the context of one issue: getting paid.

A. *Background Fee Rules*

1. Applicable Rules – The Starting Point

Cal. Rule of Prof'l Conduct, Rule 1.5[1] is the centerpiece for what attorneys may charge in terms of fees. It starts by stating "A lawyer shall not make an agreement for, charge, or collect an unconscionable or illegal fee." (Rule 1.5(a).) I won't reproduce the entire rule here, but it was clearly modeled on Old Rule 4-200. Rule 1.5 does make a few important changes. First, it adds subsections (c), (d), and (e) that govern flat fees, true retains, and prohibitions on contingency fees for family law and criminal defense. More importantly, Rule 1.5 adds two key factors when evaluating whether a fee is "unconscionable" and it adds them *at the start of the list*. They are: "(1) whether the lawyer engaged in fraud* or overreaching in negotiating or setting the fee;" and "(2) whether the lawyer has failed to disclose material facts…"

This is important in the context of probate, trusts, and conservatorships because these cases often deal with clients with limited sophistication and education in relevant areas. The fear and desperation of our clients is certainly not unique to our niche in the law, but the wildly varying terms of payment across these cases, which may or may not be obviously applicable at the start of a given case, should give every person pause.

The new Rules did not change any of the Business and Professions Code sections on fees. (See, e.g. Bus. & Prof. Code §§ 6146 – 9149.5; see also Rule 1.5.) Your fees must still be reasonable, and you must have a written contract with your clients.

[1] For brevity, subsequent citations to the Rules of Professional Conduct shall be cited as "Rule" followed by the rule number. The now superseded rules are cited as "Old Rule."

Where the Rules have changed things are on the "flat fee" front. Most probate cases involve fees that need to be approved by the court before payment. However, if you represent a client in probate litigation, you may want to be paid as you go. You may charge for these services on a flat rate basis. However, you MUST NOT put the flat fee into your operating account unless you have actually earned it, unless the client waives this requirement in writing. That means waiting until you have done the corresponding work, or portion thereof, before taking your fee, or portion thereof, out of your client trust account. Rule 1.15 addresses the specifics of compliance.

2. Fee Division Among Attorneys

Another applicable Rule is 1.5.1. It sets forth the requirements when attorneys share a fee. It requires (1) a written agreement between the lawyers, (2) written consent from and written disclosure to client of the terms and identity of the fee splitters, and (3) the total fee being charged isn't increased just because more lawyers need to divvy up the pie.

Rule 1.5.1 restates Old Rule 2-200(a). The rest of Old Rule 2-200 ended up in Rule 7.2(b), which goes beyond the subject of these materials. Rule 1.5.1 does a better job than Old Rule 2-200 setting forth what actually has to be in the disclosure to the client, but the substance is essentially the same.

However, these rules get a bit of a twist when they come into our areas of practice.

B. *General Rules for Fees in Probates, Conservatorships, and Trust Matters*

1. There is Substantial Overlap Between the Categories

Much of the law governing fees in probate, trust, and conservatorships can be cited for one another. (*See, e.g., Conservatorship of Lefkowitz* (1996) 50 Cal.App.4th 1310 [a conservatorship in which a trustee's fees were considered] *cited in Estate of Moore* (2015) 240 Cal.App.4th 1101, 1106 [probate estate in which decedent's attorney, serving as temporary trustee, paid himself excessive amounts under authority as trustee].) Most questions about the reasonableness of a fee will apply similarly in conservatorship and trust proceedings, as well as extraordinary probate fees. This can present a challenge when researching specific issues that are addressed differently in different case types; for example, whereas an executor has a statutory duty to defend a will, a trustee does not. However, generally speaking, when it comes to the issues of "how much" and "who pays," most cases work well across all case types.

C. *Specific Application of Rule 1.5 to Probate, Conservatorships, and Trust Matters*

1. Core Rules

Just as before the new Rules were adopted, it is an ethical breach to take a fee in violation of an applicable statute. (Rule 1.5(a) [prohibiting an "illegal fee"].) Thus, some key sections to keep in mind are:

a. Probate Estates: *Calif. Prob. Code*[2] §§ 10810 et seq.
b. Conservatorships: §§ 2640 et seq.
c. Trusts: §§15684, 16243.

2. Key "Reasonableness" Question to Consider

When evaluating a fee application, a court must establish what compensation is "reasonable" under the circumstances. (§2640(c) ["…the court **shall** make an order allowing…any compensation…the court determines is **reasonable** to the attorney for services rendered…" emphasis added].) This requires the court to take into account, among other things, the size of the estate. (*See Guardianship of the Estate of Slakmon* (1978) 83 Cal.App.3d 224.) Thus, one would think that a court's award of fees would, *per se*, establish what a probate attorney can be paid from all sources. However, it is well established that trustees (and other fiduciaries) can pay out of pocket subject to later reimbursement from the subject estate. What happens when these don't line up?

First, consider *Reinstein, Land & Katz v. Clune* (1973) 30 Cal.App.3d 321. Prior to 1951, fees for a conservator's attorney were paid out of pocket then reimbursed. However, this changed when (then) section 1556.1 was passed. "Defendant contends that the effect of the foregoing statutory changes was to place attorneys for guardians in a position similar to that of attorneys for executors or administrators, and to relieve the guardian of personal liability for attorney's fees in guardianship matters in the absence of a contrary agreement. We agree." (*Id*. at 324.) The most relevant part of the holding in this case is the phrase: "**in the absence of a contrary agreement**." (*Id.*) In order for that language to have any meaning, it must be possible for a conservator, personal representative, or trustee to pay an attorney more than is allowed by the court for attorney fees. In essence, it becomes a question of contract interpretation.

Interestingly, Rule 1.5 does not once use the word "reasonable." Much like the statutes prohibiting payment without first getting a court order in probate and conservatorship cases, Rule 1.5(a) is written in the negative. This is why it is important to have in depth conversations with one's potential clients about how fees will be charged; the better that they understand, and the more informed they are *at the time the agreement is made*, the less likely one will be found to have sought an "unconscionable" fee.

3. Key Differences Between Case Types

The most obvious difference between the three categories is probably probate estates. These fees are separated into two categories: the regressive percentage of gross estate assets established by §10810 (often termed "ordinary" or "statutory" fees), and "extraordinary fees" permitted in the court's discretion by §10811. Only probates have a fixed fee calculation.

[2] Subsequent statutory references are to the *California Probate Code* unless otherwise indicated.

One of the most interesting aspects is that the relevant statutes for trusts, unlike estates and conservatorships, are written in the affirmative, not negative. This would lead one to think that fees in trust cases are, by their nature, more lenient. Given that not all trust attorney fees need to be reviewed by a court, that much is true. However, when a court does get ahold of a fee case, its analysis tends to be no more lenient than for a conservatorship or a probate.

D. *Deposit & Payment, From Whom?*

1. The "Illegal" Fee

As attorneys, we must be careful and read who issued the check. Taking fees from a conservatorship or probate estate without court authorization is, *per se*, illegal. (*Rossman v. State Bar* (1985) 39 Cal.3d 539, 545.) Attorney Rossman was paid $550 out of the conservatorship estate in 1980, roughly $1,800 today. He also delayed filing the bond and Letters for three years, and tried to cover up the fees that he had been paid. These actions got Mr. Rossman actually suspended for three months plus two years stayed suspension. That case went on to be cited in six other published discipline cases. Sadly, this case is far from unique. (*See, e.g. Alberton v. State Bar* (1987) 43 Cal.3d 638, 640.)

2. *People ex rel. Harris v. Shine*

It is well established that a trustee may pay attorney fees from a trust, but that the trustee may need to reimburse the trust in the event the fees were not properly for the benefit of the trust. (*See, e.g. Kasperbauer v. Fairfield* (2d Dist. 2009) 171 Cal.App.4th 229, 238.) Thus, when a trustee asks whether the trust covers your bill, you must counsel the trustee of this outcome as a possibility (or, in some cases, a probability), and to budget accordingly.

Practitioners up and down the state have spent decades complaining about the inherent tension of attorney fees when representing a trustee. When defending a personal representative, of course, no fees may be paid from the estate without prior court order and it is an ethical violation to accept payment from the estate. (§§ 10501(a)(2), 10830; *Alberton v. State Bar* (1987) 43 Cal.3d 638, 640 ["the failure to have obtained court approval rendered [the $1,800 fee] misappropriation."].)

But when defending a trustee, it is a different story. It is a hardship for an innocent trustee to come out of pocket for tens of thousands of dollars of litigation fees and costs. However, it also gives a bad actor a war chest to hold off the claims of legitimately wronged beneficiaries. Courts have the power to instruct trustees, and can enter orders upon petition instructing the trustee to post a bond (§15602(a)(2)) and to pay (or not pay) expenses including attorney fees, either by interpreting the trust document or otherwise, depending on the circumstances. (*See* §17200(b)(2), (6), (21).) In an oft-used litigation tactic, beneficiaries litigating with trustees seek to defer payment of attorney fees from the trust in order to weaken the trustee's footing. The applicable law established broad judicial discretion. (*See Kasperbauer, supra,* 171 Cal.App.4th 229, 233 – 34 [affirming as appropriate exercise of discretion a judicial award of interim attorney fees for

former trustee defending accounting and ordering beneficiaries to return distributed funds to the trust].) Enter into that scene *People ex re. Harris v. Shine* (1st Dist. 2017) 16 Cal.App.5th 524.

Shine was a trustee of a $40 million trust that created, among other things, a multi-million dollar foundation. The conservator for the demented surviving trustor objected to Shine's accounting a year into his tenure as sole trustee which resulted in a settlement that, among other things, required Shine to establish the foundation. However, Shine failed to properly perform on the settlement and in 2013 he caught the California Attorney General's attention who petitioned for removal, appointment of a receiver, and an accounting. (*Id*. at 529.)

Three years into the litigation, Shine petitioned for an order that the current trustee pay Shine's past and ongoing defense costs under the plain language of the trust's indemnity provision. (*Id*. at 530.) The Attorney General opposed, arguing among other things that the defense could not be to the benefit of the trust because Shine was such a bad actor.[3] (*Id*. at 531.) The trial court found that although "'the Attorney General has a strong case,'" the allegations "were still unproven and the alleged misconduct 'appear[s] to be encompassed by the plain language of the indemnity provisions'" and granted Shine's petition for payment of past and ongoing attorney fees. (*Id*. at 532.) The trial court included in its reasoning that Shine was defending "'against the unlimited resources of the Attorney General's office.'" (*Id*.) The Attorney General appealed the order and on review the Court of Appeals entered a very powerful, but vague, standard for "pendente lite" attorney fees.

First, let us focus on what *Shine* does <u>not</u> hold, but which some people think it does. It does not hold that advance court permission is necessary for fees, or that the promulgated standard applies to all trusts. The *Shine* court expressly established its standard "in an ordinary case, **where the trust instrument is silent on interim fees**, the *grant* of interim fees should be governed by the following…" (*Id*. at 539, bold added, italics in original.) Thus, the express compensation provisions of the trust instrument hold in the absence of good cause to deviate therefrom. (*See, Doolittle v. Exchange Bank* (2015) 241 Cal.App.4th 529, 533-34 [trust authorized trustee to defend contest at trust expense but court withheld interim fees due to factual showing that the challenge would likely succeed on the merits].)

Now, on to what *Shine* did hold. First, it held that the proper standard in the exercise of judicial discretion is to "first assess the probability that the trustee will ultimately be entitled to reimbursement of attorney fees and then balance the relative harms to all interests involved in the litigation…" (*Shine* at 539.) This assessment required "at least some inquiry" into the trustee's ability to satisfy an order to reimburse the trust should the fees not be entirely approved. (*Id*.)

[3] The Court of Appeals makes clear in the opinion that the Attorney General cited to substantial evidence supporting allegations of substantial misconduct and that Shine did not submit any contrary evidence. This was done perhaps to suggest that the trial court abused its discretion, but instead of basing the opinion on the evidence below, it established abuse of discretion by finding the trial court applied the incorrect legal standard, which the court then created. (*Shine* at 534.)

Very little direction was given on how to balance these harms, or whether an evidentiary hearing was necessary, or even proper, on the payment of fees. However, there was some guidance on how this scale should normally tip. In what is arguably dicta, the Court of Appeals stated quite clearly that "an award of pendente lite fees will seldom be justified where, as here, the trust is silent on interim fees and the trustee's misconduct is at issue." (*Id*. at 540.) Presumably this standard applies whether the trustee files an application for fees or if a beneficiary petitions for instructions that the trustee not pay pendente lite fees, but no published case expressly addresses this question. However, at least for this panel at least, that the unspoken burden is on the trustee to establish a favorable balancing of the equities in addition to providing evidence that the trustee properly discharged her duties.

Precious little help has come to clarify this First District case. Only two published cases cite *Shine*, and neither case involves attorney or trustee fees. Both citations are actually for the de novo standard of review. *Kasperbauer* isn't much better; it has five total published citations (including *Shine*), and at least those citing cases address attorney fees or collateral issues. However, there is very little guidance for how to apply this rather novel holding. This silence offers an opportunity for the drafter to potentially alter the outcome.

Please note that this is <u>not</u> a class in trust drafting, but rather collecting fees. The strategy and ethics applicable to how you wish to draft your own trusts will necessarily depend on your own style of practice, clients' objectives, and expected problems. However, if you want to give the court any guidance on how to allocate the risk between the trustee and beneficiaries, you must include explicit language in your trust instrument. What do you think is wise? Where will you allocate the most risk? Why?

3. <u>Contingent Fees</u>

Although not particularly common in an ordinary case, there is an additional layer of scrutiny whenever an attorney represents a personal representative or trustee as plaintiff. In that situation, the client (the fiduciary) and the beneficiaries – or, in the case of an accounting, a reviewing court. (*See Schultz v. Jeppesen Sanderson, Inc.* (2d Dist. 2018) 27 Cal.App.5th 1167, CRC 7.955.) In *Schultz*, an attorney agreed to represent a decedent's widow, two adult children, four minor children, and the decedent's company in connection with a Cessna crash in Germany. On the eve of trial, the defendant settled for over $18 million, and the trial court needed to hold a trial to determine the allocation of attorney fees and settlement proceeds to the minors.

The trial court rejected the proposed allocation among the parties. It also cut the attorney fees; the contingency agreement entitled the attorneys to 40%, and the attorneys asked for 31%, but the court awarded only 10%. The court of appeal reversed, reasoning that the trial court had severely underpaid the attorneys because it failed to consider the factors listed in CRC 7.955, and thus abused its discretion. (*Schultz*, *supra* at 1174.) CRC 7.955 is specific to minors and persons with a disability, but each of the seven elements in CRC 7.702 can be found in 7.955, albeit with

different wording. Thus, anyone familiar with an extraordinary fee application should be able to properly petition the court for approval of a contingency fee agreement.