March 3, 2023

The State Bar Standing Committee on Professional Responsibility and Conduct (COPRAC)

Re: Comments from California Employment Lawyers Association, Economic Security Project Action, National Consumer Law Center, National Employment Law Project, Open Markets Institute, People's Parity Project, Public Good Law Center, Public Justice, Student Borrower Protection Center, and Towards Justice in Support of Draft Formal Opinion No. 19-0003

VIA Email

Dear Committee on Professional Responsibility and Conduct (COPRAC),

As organizations that advocate for workers and consumers, we write to urge COPRAC to finally adopt Draft Formal Opinion No. 19-0003, which describes a lawyer's ethical duties when advising a client regarding a provision that is unlawful in a contract presented to a third party, including a worker or consumer.

This is an urgent matter calling for prompt action from legal ethics authorities. Recently, federal and state policymakers have taken bold action to regulate the terms of fine print contracts that harm workers and consumers. This includes the Federal Trade Commission's recent proposal to prohibit non-compete clauses. Unlawful contract provisions are, nonetheless, abundant in the marketplace, and they cause real harm whether or not a court would ever enforce them because workers and consumers assume that those provisions have the force of law. Unlawful non-compete agreements, for example, keep thousands of workers trapped in jobs that provide inadequate pay and may also involve unsafe and unfair working conditions. Prohibiting attorneys from *knowingly* advising a client to present an unenforceable or illegal contractual provision to a third party would protect millions of non-lawyers and help to restore faith in the legal profession. It would also do nothing to inhibit attorneys from zealously representing their clients.

Regulating attorney conduct in this context finds clear support in legal ethics rules, and California is not the only jurisdiction considering how it should address the problem. The Washington D.C. Attorney General recently called on the D.C. Bar Ethics Committee to issue an opinion clarifying that it is unethical for a lawyer to counsel a client to present a worker with an illegal or unenforceable contractual term. As the D.C. Attorney General explained, "It should be uncontroversial that a lawyer may not advise a client to use a provision in its contracts that is illegal and unenforceable. Despite this, clauses that are harmful to workers remain pervasive in employment contracts even where they are illegal and unenforceable." We have attached that letter for your consideration as Exhibit A.

While the Formal Opinion is an important step in the right direction, and we appreciate the Committee's attention to this important issue, COPRAC should not adopt the Opinion in its current form. In particular, we urge the Committee to clarify that, at least with respect to contracts of adhesion drafted by corporations for workers, consumers, and others there is no meaningful difference between a contractual term a lawyer knows to be *illegal* and a term the lawyer knows to be *unenforceable*.

The Formal Opinion Addresses an Urgent and Critical Problem

Millions of people in this country most frequently interact with the legal profession through the lawyer-drafted fine-print in the terms and conditions they're forced to enter into as a condition of getting a job, taking out a loan, getting medical treatment, renting a home, or obtaining so many other basic necessities. These contracts can have exceptionally harsh consequences. They can keep people trapped in low-paying jobs, strip them of their right to go to court, or require them to stay silent about unsafe or abusive working conditions.

Policymakers around the country are working to protect workers and consumers from the abuses of coercive contracting. For example, the Federal Trade Commission's new proposed rule prohibiting non-compete agreements with workers would help millions of workers trapped in their jobs,[1] and the Consumer Financial Protection Bureau's new rule requiring supervised nonbanks to provide transparency into their fine-print terms would help police some of the worst abuses.[2]

The vast majority of fine-print contracts, however, will never be scrutinized by a regulatory agency or court. They are drafted by a lawyer and presented to a person who is likely unrepresented and who doesn't have the bargaining power to get a better deal or the familiarity with complex legal questions to understand whether the contract they are forced to sign would ever be enforced by a court. They assume the contract has the force of law.

This means that unlawful contractual terms, which are abundant across the marketplace, can have devastating consequences. The FTC observed in its notice of proposed rulemaking regarding non-compete agreements, for example, that the "available evidence indicates that, in states where non-compete clause are void, workers are subject to non-compete clauses at approximately the same rate as workers in other states, suggesting that employers may believe workers are unaware of their legal rights."[3] As scholars have recognized for decades, "[f]or every covenant [not to compete] that

[1] Fed. Trade Comm'n, Notice of Proposed Rulemaking, *Non-compete Clause Rule*, 16 CFR Part 910 (July 19, 2023); *see also* Workforce Mobility Act of 2021, S.483, 117th Cong. (2021).
[2] Consumer Fin. Prot. Bureau, Proposed Rule, *Registry of Supervised Nonbanks that Use Form Contracts to Impose Terms and Conditions that Seek to Waive or Limit Consumer Legal Protections*, 16 CFR Part 1092.
[3] Fed. Trade Comm'n, Notice of Proposed Rulemaking, *Non-compete Clause Rule*, 16 CFR Part 910 (July 19, 2023); *see also* J.J. Prescott, Evan Starr & Norman D. Bishara, *The Behavioral Effects of (Unenforceable) Contracts*, 36 J.L. ECON. & ORG. 633 (2020).

finds its way to court, there are thousands which exercise an *in terrorem* effect on employees who respect their contractual obligations. …Thus, the mobility of untold numbers of employees is restricted by the intimidation of restrictions whose severity no court would sanction." Harlan M. Blake, *Employee Agreements Not to Compete*, 73 Harv. L. Rev. 625, 682-83 (1960).

The problem is not confined to non-compete agreements. Unconscionable terms in arbitration agreements can chill people from vindicating their rights in any forum. *See, e.g.*, *Hale v. Brinker Int'l*, Inc., No. 21-CV-09978-VC, 2022 WL 2187397, at *1 (N.D. Cal. June 17, 2022) (describing how contract drafters may have an "incentive" to include unenforceable terms in arbitration contracts for the purpose of "chill[ing] claims"). And unenforceable confidentiality provisions can chill people reports of abuse. *See, e.g.*, Marissa Ditkowsky, *#ustoo: The Disparate Impact of and Ineffective Response to Sexual Harassment of Low-Wage Workers*, 26 UCLA Women's L.J. 69, 103 (2019) (describing how non-disclosure agreements may chill workers from reporting abuse to public enforcement agencies, even though such a prohibition is unlawful). Countless other types of unenforceable contract provisions chill people from exercising their rights in any number of ways.

The Formal Opinion Should Be Uncontroversial and Finds Clear Support in Legal Ethics Rules

Unlawful contracts that exert coercive pressure on workers and consumers are often drafted by lawyers and presented to people who don't have lawyers. Especially in these contexts, there is no legitimate justification for counseling a client to present a contract to a non-drafting party that includes an unambiguously illegal term. The only reason to include such a term would be to gain the benefit of the chilling effect that term may have on the non-drafting party, including workers who will have less bargaining power because of an illegal non-compete agreement.

Counseling a client to deceive others in this manner is plainly inconsistent with a lawyer's professional obligations. See Bus. & Prof. Code § 6068(d); 4.1(a) & 8.4(c). Professional bodies regulating attorney conduct have relied on the prohibitions against deceptive conduct to conclude that lawyers may not help clients draft fraudulent documents, ABA Model Rule 1.2, cmt. 10; may not make material misrepresentations during contract negotiations, Cal. Formal Opn. 2015-194; and may not misrepresent to another party their obligations under an order or decree, S.C. Ethics Op. 05-03 (2005). It is similarly unethical to encourage a client to present an unenforceable contractual provision to a worker or consumer who is likely to think the provision has the force of law.

The proposed opinion also recognizes the disparities in bargaining power between the counseled parties that draft contracts and the people without lawyers who are required to sign them. "[A] lawyer may be in a superior negotiating position when dealing with an unrepresented nonclient, who therefore should be given legal protection against overreaching by a lawyer." Restatement (Third) of the Law Governing Lawyers § 103, cmt. b. In particular, the Committee should be concerned about conduct that is likely to mislead an unrepresented nonclient about their rights in a

negotiation. *Id.* When a lawyer presents an illegal contractual term to an unrepresented party, the attorney incorrectly suggests that the nonclient will be bound by such a term if they enter into it. This misstates the nonclient's rights "to the prejudice of the nonclient." Restatement (Third) of the Law Governing Lawyers § 103(1).

COPRAC Should Remove Any Distinction between Illegal and Unenforceable Contractual Terms

We appreciate the Committee's attention to this matter and its recognition that non-compete agreements in California are not only *unenforceable* but also *illegal*.[4] If this opinion is adopted it will mean that it is unethical for a California lawyer to encourage an employer to present a non-compete agreement to a California worker. That's a critical clarification of attorneys' ethical obligations.

The Opinion, however, also introduces a distinction between illegal and unenforceable contractual terms and suggests that it may not be unethical for an attorney to encourage a client to present an unenforceable contractual term to a third party so long as the term is not illegal. Formal Opinion No. 2022-208 at 3 (explaining that the opinion "is not intended to address provisions that are legal, but against public policy, unenforceable, voidable, or subject to some other prohibition."). Prior drafts of the opinion had removed this language, but it has been reintroduced into the current draft. It should be removed.

First, drawing a distinction between illegal and unenforceable terms is out of step with the prevailing views of the legal profession. Notably, the Washington D.C. Attorney General recently called on the D.C. Bar Ethics Committee to issue an opinion clarifying that it is unethical for a lawyer to counsel a client to present a worker with an unenforceable contractual term. The D.C. Attorney General letter recognizes that there is no difference between illegal and unenforceable contractual terms. *See* D.C. Att'y Gen. Letter at 1 (Attached).

Second, nothing in the Rules of Professional Conduct suggests a meaningful distinction between "illegal" and "unenforceable" contractual terms. Rule 1.2.1, for example, covers terms that are "in violation of any law, rule, or ruling of a tribunal." Even if a term were merely "unenforceable" and not "illegal," it would be in violation of the law or rule that proscribes its enforceability.

Furthermore, counseling a client to draft and present to a third party an unenforceable contractual term involves deceptive conduct that is unethical even if it does not involve encouraging a client to engage conduct in "in violation of any law" under Rule 1.2.1. It is unclear what the

[4] Formal Opinion No. 2022-208 at 3 ("For example, provisions in employment contracts that impair the ability of employees to compete against their employers following termination of employment have been found to be illegal and unenforceable, and the use of these provisions violates California law, subject to specific, limited exceptions.").

purpose could be of advising a client to use a term the attorney *knows* to be unenforceable except to deceive the non-drafting counterparty. Courts in California and elsewhere have recognized that unambiguously unenforceable contractual terms are likely to deceive non-drafting parties about their rights. *Leardi v. Brown*, 474 N.E.2d 1094, 1100 (Mass. 1985); *People v. McKale*, 25 Cal. 3d 626, 635 (1979). And the Consumer Financial Protection Bureau has concluded that "including an unenforceable material term in a consumer contract is deceptive, because it misleads consumers into believing the contract term is enforceable." Bureau of Consumer Financial Protection, Compliance Bulletin, 87 Fed. Reg. 17,143, 17,144 (Mar. 28, 2022). Therefore, counseling a client to use a term that is clearly unenforceable is unethical under Rule 1.2.1's prohibition against counseling a client to engage in "fraudulent" conduct, whether or not it is also deemed to be "in violation of any law."

Third, there is no risk that clearly bringing unenforceable terms within the Formal Opinion would render the Opinion ambiguous or difficult to apply in practice. It is true that unenforceability often raises fact-specific questions, especially in the unconscionability context, but the Formal Opinion's repeated clarification that it only reaches contractual terms that the attorney knows are in violation of law provides broad protection for attorneys operating in good faith. For example, even with the expanded language we propose here, there is no threat that an attorney would be found to fall within the language of the Opinion merely by drafting a term that substantially benefits the drafting party and that could be unenforceable depending on how it is presented to the non-drafting party. The attorney in such a case would not know that such term would be unenforceable.

Fourth, if the Committee has any concern that there may be non-deceptive reasons to enter into a clearly unenforceable contractual term with a counterparty bargaining at arm's length, the Committee could limit the application of the Formal Opinion to unenforceable terms in "standard form contracts." There is substantial case law in California regarding "standard form contracts," *see, e.g., People ex rel. Bill Lockyer v. Fremont Life Ins. Co.*, 104 Cal. App. 4th 508, 516, 128 (2002), as modified on denial of reh'g (Jan. 16, 2003) (". . . unfair business practices include unconscionable provisions in standardized agreements"); *Baker v. Sadick*, 162 Cal. App. 3d 618, 625 (1984), and in practice, the question whether any particular contract is a standard form contract is likely to be substantially less difficult to resolve than the question of whether a particular clearly "unenforceable" contractual term is also "illegal."

The Formal Opinion is an important step in the right direction, but the distinction it draws between illegal and unenforceable terms will cause confusion and hurt unrepresented parties required to enter into standard form contracts who reasonably assume that the provisions of those contracts would be enforceable in court.

* * *

For every harsh and unenforceable contract that intimidates someone from exercising an important right, like the right to quit a job or speak out publicly about mistreatment, there's a lawyer who drafted it. The legal profession must act.

We appreciate the Committee's continued attention to this issue.

Thank you,

California Employment Lawyers Association
Economic Security Project Acton
National Consumer Law Center
National Employment Law Project
Open Markets Institute
People's Parity Project
Public Good Law Center
Public Justice
Student Borrower Protection Center
Towards Justice

Exhibit A

GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE ATTORNEY GENERAL

Karl A. Racine
Attorney General

Public Advocacy Division
Workers' Rights and Antifraud Section

December 16, 2022

By U.S. Mail & E-mail
Legal Ethics Committee
District of Columbia Bar
901 4th Street, NW
Washington, DC 20001
ethics@dcbar.org

RE: Proposal for Formal Opinion on Advising Clients on Illegal Contract Provisions

Dear Members of the D.C. Bar Legal Ethics Committee:

On behalf of the Workers' Rights and Antifraud Section of the Office of the Attorney General for the District of Columbia, we write to request a formal ethics opinion on a topic of importance to District workers and the Bar's missions of improving the legal system and enhancing access to justice. Specifically, we seek an opinion on whether an attorney's participation in the drafting, review without objection, approval, or execution of contractual language in an employment contract that is unambiguously illegal or unenforceable is a violation of Rule 1.2, Rule 3.1, Rule 8.4, or any other rules of the D.C. Bar Rules of Professional Conduct.

It should be uncontroversial that a lawyer may not advise a client to use a provision in its contracts that is illegal and unenforceable. Despite this, clauses that are harmful to workers remain pervasive in employment contracts even where they are illegal and unenforceable.

Consider noncompete clauses, which the D.C. Council recently banned for most District workers.[1] Noncompete clauses prohibit workers from pursuing employment similar to their current role, working for another employer who competes against their current employer, or operating their own business. While noncompete clauses vary in terms of time period and geographic scope, all noncompetes limit employees' job opportunities. Empirical research has repeatedly borne this out:

[1] On October 1, 2022, the District's Non-Compete Clarification Amendment Act of 2022 took effect, banning the use of noncompete clauses for most D.C. workers. *See* D.C. Code § 32-581, *et seq*. While noncompete clauses are sometimes referred to as noncompete "agreements," we avoid that terminology in recognition of the reality that many workers lack meaningful power and opportunity to bargain over the terms of their employment.

noncompetes depress the mobility and wages of all types and wage-levels of workers,[2] but noncompetes are especially harmful to middle- and low-wage workers, who lack the bargaining power to negotiate the terms of their employment. Despite these documented harms, the use of noncompete clauses is growing in virtually every industry.[3] Almost 20% of American workers are subject to noncompetes, 12% of whom are in low-skill and low-wage jobs.[4]

The District's ban on noncompetes is a positive step but it is not sufficient to end the harm to District workers. Research shows that contract provisions like noncompetes not only continue to exist, but proliferate, even in jurisdictions where they are illegal and unenforceable.[5] For example, the U.S. Department of Treasury's Office of Economic Policy has reported that approximately 19% of California workers are required to enter a noncompete by their employer–a percent even higher than the national average–despite the fact that noncompete contracts are unenforceable there.[6] One recent study found almost no difference in the incidence of noncompetes between states that will and will not enforce noncompetes, and this phenomenon was consistent across all employers, including those with both local and national workforces.[7] The same study found that the use of noncompetes was only slightly higher in states that enforce noncompete contracts most zealously, by a difference of 2%.[8]

The proliferation of noncompetes, even where they are legally prohibited, has significant consequences for workers. One study, aptly titled "The Behavioral Effects of (Unenforceable) Contracts," found that noncompetes reduce employee mobility significantly in both states that do and do not enforce noncompetes.[9] Relatedly, even in states that do not enforce noncompetes,

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[2] *See, e.g.*, Matt Marx & Lee Fleming, *Non-Compete Agreements: Barriers to Entry . . . and Exit?*, *in* 12 INNOVATION POL'Y & ECON. (2012), https://www.journals.uchicago.edu/doi/full/10.1086/663155; Natarajan Balasubramanian et al., *Locked In? The Enforceability of Covenants Not to Compete and the Careers of High-Tech Workers*, U.S. CENSUS BUREAU CTR. FOR ECON. STUD. (2019), https://www2.census.gov/ces/wp/2017/CES-WP-17-09.pdf.

[3] Alexander J.S. Colvin & Heidi Shierholz, *Noncompete Agreements*, ECON. POL'Y INST. (Dec. 10, 2019), https://www.epi.org/publication/noncompete-agreements; *also see* Statement of Randolph Chen before the Committee on Labor and Workforce Development, Public Hearing on Bill 23-0494, the "Ban on Non-Compete Agreements Amendment Act of 2019," https://oag.dc.gov/release/testimony-ban-non-compete-agreements-amendment-act.

[4] Evan Starr, J.J. Prescott & Norman Bishara, *Noncompetes in the U.S. Labor Force*, 64 J.L. & ECON. 53, 58-59 (2021).

[5] *Id*.

[6] U.S. DEP'T TREASURY OFF. ECON. POL'Y, *Non-compete Contracts: Economic Effects and Policy Implications*, 4 (March 2016) https://home.treasury.gov/system/files/226/Non_Compete_Contracts_Econimic_Effects_and_Policy_Implications_MAR2016.pdf.

[7] *Supra* note 5, at 61.

[8] *Id*.

[9] J.J. Prescott, Evan Starr & Norman D. Bishara, *The Behavioral Effects of (Unenforceable) Contracts*, 36 J.L. ECON. & ORG. 633 (2020).

workers frequently point to their noncompete as an important reason for declining offers from competitors.[10]

Illegal and unenforceable contracts like noncompetes remain pervasive because employers know that many workers are poorly informed about the existence or enforceability of these terms, and many workers lack the ability to meaningfully bargain with their employer. In other words, employers can reap many of the benefits of noncompetes even where they are not enforceable. These "in terorrem" effects of illegal and unenforceable contracts on workers are well documented and studied.[11] And these results are supported by findings that many workers sign employment contracts without researching their legality: one study found that when presented with a noncompete, most workers simply read and sign it (88%), some workers do not even read it (6.7%), and a mere 17% actually consult with friends, family, or a lawyer before signing.[12] A similar study concluded that 88% of workers do not even attempt to negotiate over noncompete provisions included in their employment contracts.[13]

This research all suggests that it is not enough to render noncompete contracts illegal or unenforceable. Rather, truly protecting workers from the harms of noncompetes and other illegal or unenforceable contract terms requires eliminating these clauses from employment contracts altogether. To achieve that goal, we urge you to hold responsible the lawyers who draft these terms in employment contacts.

The requested opinion is vital to ensure that attorneys uphold their ethical obligations and do not contribute to the proliferation of unlawful provisions. Specifically, we request an opinion stating that it is misconduct for an attorney to participate in the drafting, review without objection, approval, or execution of contractual language in an employment contract that is unambiguously illegal or unenforceable. Rule 1.2, Rule 3.1, Rule 8.4, and potentially other rules of the D.C. Bar Rules of Professional Conduct provide a basis for issuing such an opinion. Rule 1.2 states that a "lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent." Rule 3.1 further states that a lawyer "shall not bring or defend a proceeding, or assert or controvert an issue therein, unless there is a basis in law and fact for doing so that is not frivolous, which includes a good-faith argument for an extension, modification, or reversal of existing law." Further, Rule 8.4 states that it is professional misconduct for an attorney to, "[e]ngage in conduct involving dishonesty, fraud, deceit, or misrepresentation." Any of these Rules could serve as a basis for the requested opinion.[14]

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[10] *Id.*

[11] Charles A. Sullivan*, The Puzzling Persistence of Unenforceable Contract Terms*, 70 OHIO ST. L.J. 1127 (2009); *supra* note 5.

[12] *Supra* note 5, at 61.

[13] *Id*.

[14] Beyond existing legal rules of ethics, other areas of District law reflect a public policy in favor of protecting the District residents from deceptive contracts. For example, the D.C. Consumer Protection Procedures Act states that it is an unfair or deceptive trade practice to "[r]epresent that a transaction confers or involves rights, remedies, or obligations which it does not have or involve, or which are prohibited by law." D.C. Code § 28–3904(e-1).

In order to be effective, we request that any ethics rule to this effect be accompanied by concrete examples of misleading contracts. For example, the rule should illustrate that it is misleading, and therefore misconduct, for an attorney to draft a contract with an illegal or unenforceable term, even where the contract utilizes disclaimer language that purports to comply with all relevant laws. For example, such a rule should illustrate that an attorney may not draft a contract that includes a noncompete or other illegal term and then merely state that "nothing in this contract should be construed to conflict with District law," or any other boilerplate legal disclaimer. Permitting contracts like this would be misleading to workers who are in a worse position to know the law than the attorneys who draft employment contracts.

Finally, we note that the problem of illegal or unenforceable contract provisions exists outside of the employment context. For example, one recent study found that as many as 73% of rental leases contain unenforceable clauses.[15] We encourage the Committee to solicit input from advocates in other areas of law regarding whether such an opinion is necessary in other contexts.

We are grateful for the work of the Legal Ethics Committee and hope that you will consider this important request.

Sincerely,

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[15] Meirav Furth-Matzkin, *On the Surprising Use of Unenforceable and Misleading Clauses in Consumer Contracts: Evidence from the Residential Rental Market*, 9 J. LEGAL ANALYSIS 1 (2016).

* Admitted to practice only in New Jersey. Practicing in the District of Columbia under the direct supervision of Graham Lake, a member of the D.C. Bar, pursuant to D.C. Court of Appeals Rule 49(c)(8).