

NEW HAMPSHIRE BAR ASSOCIATION
Ethics Committee Formal Opinion #1994-95/2
Conflict of Interest: Personal Injury Settlements/Brokerage Referral
April 20, 1995

RULE REFERENCES:

*Rule 1.7
*Rule 1.8
*Rule 2.1
*Rule 5.4

SUBJECTS:

*Adverse effect on professional judgment.
*Conflict of interest.
*Division of fees.
*Fees.
*Independent judgment.

ANNOTATIONS:

QUESTION:

May an attorney refer a client to an investment broker in exchange for a referral fee from the broker if the referral fee is not paid from the client's funds, and if the lawyer discloses to the client the expectation of a referral fee?

FACTS:

The inquiring attorney seeks advice regarding the propriety of entering into an agreement with an investment counselor/broker whereby the attorney would refer clients to the broker in exchange for a referral fee paid by the broker to the attorney. The attorney would typically obtain a settlement or judgment on behalf of a client and would then advise the client of the availability of the broker's services. The client would be free to contact the broker independently. The attorney would advise the client of the attorney's interest in the referral and would disclose the attorney's expectation of a referral fee in the event the client decides to invest through the broker. The attorney would not share the client's name or any information regarding the client with the broker. The referral fee would be a portion of the commission earned by the broker, so the client's funds would not be further diminished by the payment of the referral fee.

RESPONSE:

The Committee was unable to agree on a majority opinion in this matter. We provide, therefore, the differing analyses of the issue.

Rule 1.7(b) provides that a lawyer shall not represent a client if the representation of that client may be materially limited by the lawyer's responsibilities to another client or to a third person, or by the lawyer's own interest, unless: (1) the lawyer reasonably believes the representation will not be adversely affected; and (2) the client consents after consultation and with knowledge of the consequences. Although Rule 1.7(b) focuses on whether the lawyer may represent a client under circumstances where a conflict of interest may exist, the principle underlying the rule is the importance of loyalty to the client; lawyers should not represent clients if the lawyer's own interest may have an adverse effect on representation of the client.

To determine whether representation is permissible in the face of a potential conflict of interest, the "disinterested lawyer" standard is applied. If a "disinterested lawyer" would conclude that the client should not agree to representation involving a potential conflict of interest, the lawyer may not ask for such an agreement or provide representation on the basis of a client consent. See Kelley's Case, 137 NH 314 (1993). If the test under Rule 1.7(b)(1) is met (the lawyer reasonably believes the representation will not be adversely affected), the client may "consent after consultation . . ."

In the present case, the inquiring attorney would be referring a client to an investment broker immediately following the completion of formal representation of the client. For the purposes of Rule 1.7(b), however, the Committee believes the referral by the inquiring attorney should be deemed to be "representation" and should be required to meet the requirements of Rule 1.7(b). We base this conclusion on the reasonable expectations of the client in this situation. A client who has vested his or her trust in an attorney throughout the case, and particularly one who has just received a disbursement from their lawyer, should be entitled to expect conduct consistent with the Rules for a reasonable period of time. The inquiring

attorney might be advised to disclose what information he has, if any, regarding the inquiring attorney's knowledge of the performance of the investment broker in order to allow the client to make a more fully informed choice.

A substantial difference of opinion exists within the Committee as to whether the Rule 1.7(b)(1) test is met - whether the potential conflict of interest is "waiveable" under the "disinterested lawyer" standard. Some Committee members believe that if the inquiring attorney fully discloses his expectation of a referral fee and merely provides the name of the broker to the client, the referral is not improper under Rule 1.7(b). They base this opinion, in part on the A.3.A. Model Rules comment. The A.B.A. Model Rules comments to Rule 1.7(b) state that "a lawyer may not allow related business interests to affect representation, for example, by referring clients to an enterprise in which the lawyer has an undisclosed interest." In such a case, it would appear that an adequate disclosure, coupled with the client's consent, would in some cases allow "representation" within the meaning of Rule 1.7(b). The client is free to accept or reject the lawyer's referral to the investment broker after disclosure of the lawyer's interest. These Committee members believe that before the lawyer makes the referral, the lawyer should be careful to disclose all information the lawyer has regarding the skill or record of the investment broker, should advise the client to seek independent advice regarding the investment, and should obtain the client's written consent.

A substantial number of Committee members believe this not to be a waivable conflict. These members acknowledge that as a general matter most conflicts should be waivable at the client's option, but believe this is a situation where a reasonable, disinterested lawyer would not proceed with the referral. See, *Fiandaca v. Cunningham*, 827 F. 2d 825 (1st Cir. 1987) and *Boyle's* case, 136 NH 21 (1992).

The essence of this position is that a lawyer confronted with some factor limiting his or her objectivity must evaluate the benefits and burden from the client's perspective. This evaluation must be done before the lawyer seeks client consent. For example, if the lawyer has a remote financial interest in the litigation, the lawyer must decide whether the client can evaluate whether the benefit of having this particular lawyer outweighs the possibility that the lawyer might not use full zeal due to the lawyer's own interest. In the normal course, this should be the client's decision.

These Committee members believe that here, however, there is really no benefit to the client. The client gets no independent advice. Also, the danger of client misunderstanding as to the limited nature of the information due to the lawyer's previous role as advocate for the client and the fact that the sole motivation here is a fee for the lawyer, makes it, in the opinion of many members, unreasonable conduct.

The same underlying debate exists when the fact pattern is analyzed under Rule 1.8. A portion of the Committee would permit the referral as long as the lawyer makes a full disclosure and advises the client as noted above. Those members who find the conflict unwaivable disagree.

The Committee also believes that Rule 2.1 is implicit here.

Rule 2.1 provides,

In representing a client, a lawyer shall exercise independent Professional judgment and render candid advice.

Rule 2.1 is not limited in its application to legal advice only. The A.B.A. model Code Comments state, "Where consultation with a professional in another field is itself something a competent lawyer would recommend, the lawyer should make such a recommendation."

The issue in the present case is whether the inquiring attorney is exercising his "independent professional judgment" in providing his client with the name of the investment broker, or whether the inquiring attorney's judgment is affected by his expectation of a referral fee. By advising the client of the lawyer's expectation of a referral fee and advising the client to seek independent advice, the lawyer is in essence advising the client that the advice is not purely "independent" and may be tainted by self-interest. The extent of the lawyer's disclosure will have a direct bearing on whether the client can receive "candid" advice from the lawyer. The Committee is split as to whether the lawyer making the referral to the broker can render "candid" advice and whether the lawyer is exercising 'independent professional judgment' in making the referral.

The Committee is in agreement on the issue of fee sharing. Rule 5.4 prohibits the sharing of legal fees with a non-lawyer, with certain exceptions, and prohibits forming a partnership with a non-lawyer for the practice of law. The purpose of Rule 5.4 is, as stated in the A.B.A. Model Code Comments, to "protect the lawyer's independence of professional judgment" and to recognize the lawyer's obligation to a client. This purpose similarly underlies Rules 1.7 1.8 and Rule 2.1.

The issue in the present case is whether the inquiring attorney intends to "share legal fees" within the meaning of Rule 1.5. Since the referral fee does not arise in connection with and is not compensation for legal advice, and since the referral does not constitute the practice of law, the referral fee can not be said to be a "legal fee" within the meaning of Rule 1.5. Rule 1.5 contemplates the payment by the lawyer of a fee earned in connection with rendering legal advice. The reverse is true in the present case, where the fee is being paid to the lawyer by a non-lawyer. For this reason, it appears that Rules 5.4 and 1.5 have no applicability in the present case.

An attorney who chooses to refer clients to an investment broker for a referral fee would be advised to be aware of the potential for the attorney's liability in the event that the investment broker commits fraud, violates Federal Securities laws, or if the investment turns out to be unwise or unprofitable.

CONCLUSION:

A substantial difference of opinion exists on the Committee as to whether an attorney may refer a client to an investment broker in exchange for a referral fee even if the attorney makes the proper disclosures.

¹ Rule 1.8 prohibits an attorney from entering into a business transaction with a client or acquiring a pecuniary interest adverse to a client unless the transaction is fair and reasonable to the client, the client agrees after consultation, the client is given an opportunity to obtain independent counsel and consents in writing. The term "business transaction within the meaning of Rule 1.8(a) implies a joint venture where the attorney and client share a pecuniary interest in the outcome. While the referral of a client to an investment broker may not be a Business transaction" because a referral fee is paid on the basis of the referral (and subsequent investment) by the client regardless of the outcome of the investment, the referral itself will result, presumably, in financial gain to both the client and to the referring attorney. In this sense, the attorney and the client may share a common benefit to the referral itself, and thus the referral may be considered a Business transaction" under Rule 1.8. The referral may also constitute a "pecuniary interest adverse to a clients under the second prong under Rule 1.8(a).