

# P E N N S Y L V A N I A LAW WEEKLY

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## **A SLIPPERY SLOPE**

*Lawyers must tread carefully if they accept referral fees from investment advisors*

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Can a domestic relations attorney accept a referral fee from an investment advisor who provides a service to a client referred by the attorney, when the lawyer is engaged in a continuing relationship with that client? The answer is yes.

Two influential bar associations have addressed this question culminating in a Joint Ethics Opinion from the Pennsylvania Bar Association and Philadelphia Bar Association known as Joint Ethics Opinion 2000-100. The domestic relations attorney must proceed, however, as if a porcupine were crossing his or her path - very, very carefully.

Joint Ethics Opinion 2000-100 permits an attorney who is part of an ongoing lawyer-client relationship to receive a referral fee for referring a client to a service provider such as an investment advisor. The umbrella over an attorney's ability to accept such a referral fee is that the lawyer must be scrupulous in determining that the acceptance of such a fee would not impact negatively on the lawyer-client relationship or on the lawyer's ability to exercise independent judgment for the benefit of the client. The attorney must also secure the client's consent and must make full disclosure to the client.

Pennsylvania Rule of Professional Conduct 1.5(d)(1) provides that a lawyer cannot enter into an arrangement to charge or collect any fee in a domestic relations matter for which the payment is contingent upon the securing of a divorce or upon the amount of alimony or support. (Emphasis added.) If a domestic relations attorney represents a client who cannot afford to pay counsel fees which are due and owing and if that attorney can secure a referral fee from an investment advisor, after the divorce, when the funds will be available for investment and then apply the referral fee to the client's outstanding legal fees, is that acceptance of the referral fee tantamount to a contingency fee? On the one hand, one could argue that but for the referral fee from the investment company, received post-divorce, the client would not have been able to secure truly competent representation. One could also argue that many domestic relations attorneys find that the dependent spouse runs out of monies and they must wait for payment until equitable distribution is made to be paid the balance of legal fees due. The attorney, by making an agreement with the investment company to refer the client there with the client's funds realized post-divorce has been able to continue to represent that client, knowing that the referral fee from the investment company would pay the client's outstanding balance. The client, of course, is only

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too happy to consent to this arrangement because her attorney continued to represent her and her fees were paid by a third party. Does this arrangement pass the smell test? When in doubt, rule it out.

Consider the following language, from Joint Opinion 2000-100, May 2000: "As a preliminary matter, frequently the preferred practice for a lawyer who is offered a referral fee will be for the lawyer, rather than accepting the referral fee, to negotiate a reduction in the fee that the client will pay the service provider. In other situations, such as if the service provider is willing to pay a referral fee but not to reduce the service provider's charge to the client, the preferred practice for a lawyer offered a referral fee may be for the lawyer to accept the referral fee and then to remit that fee to the client, either directly or as a credit against the lawyer's fee. In the latter case, the lawyer's bill should clearly show the lawyer's fee before the credit, the amount and source of the credit, and the lawyer's fee after the credit."

## **Is It Contingent?**

Even if the referral fee received by the attorney is applied as a credit to the client, does it constitute a contingent fee because the receipt of the referral fee is contingent upon securing the divorce in order to secure the monies to set up the investment account from which the referral fee flows? It could be argued that this credit back to the client so that legal fees for representation are paid would not fall into the contingent fee prohibition because the lawyer is working for the best interests of the client. The argument contra is that the lawyer hastens the divorce in order to get paid, thereby serving the attorney's best interests rather than those of the client. What if the fee agreement letter specifically states that the fee is based on an hourly rate? Does that fee agreement put to rest whether the referral fee from the investment advisor constitutes a contingent fee upon divorce? No, it does not. As Juliet said, "A rose by any other name would smell as sweet." An admonition against a family lawyer using a contingent fee is just that and a prudent domestic relations attorney should avoid any indicia of impropriety.

The Joint Ethics Opinion admonishes that if the attorney wishes to remit or credit the referral fee to the client, the lawyer must comply with Rule 1.7(b) and Rule 1.8(f), dealing with conflicts of interest that a lawyer may face in accepting a referral fee from a service provider. Assume a situation where the client opens an investment account with an investment firm that pays a referral fee to the attorney. Assume the client becomes unhappy after being with the investment firm for a period of time and decides to leave. The investment firm, of course, stops any referral fee because the attorney's client is no longer their client. The attorney's bill for that client is unpaid. The attorney has entered into an agreement with the client that the satisfaction of the outstanding balance will come from the referral fees paid by the investment firm. Does the client still owe the firm money? The client is now unhappy with the investment firm and faults the lawyer for recommending the firm in order to benefit financially from the recommendation. The attorney is now facing a potential malpractice suit for referring the client to the investment firm. This writer cannot see a good ending here. If the attorney referred the client to an investment firm that was to pay a referral fee to be credited to payment of the client's legal fee account and

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the client is unhappy with the service provider and leaves, the finger can only point to the attorney.

At all times, regarding the representation of the client and thereafter, the attorney's first obligation is to the client. A review of the various Rules of Professional Conduct evidence an obligation to the client during the course of representation and thereafter. The lawyer must always be prudent and cautious that the lawyer is exercising independence of professional judgment and is acting in the best interest of the client. Query the situation where there is an annuitized referral fee to the attorney from the investment firm that will ultimately total in excess of \$100,000 from the client's accounts having remained with that investment firm over the years. At the time the referral is made, the client owes the lawyer \$20,000. When the lawyer makes disclosure to the client, the lawyer must disclose that it is possible that the lawyer will realize an amount in excess of the amount that the client owes him. The reasonableness of the fee is a compelling issue in light of the dictates of Rule 1.5(a), which provides, "A lawyer shall not enter into an agreement for, charge, or collect an illegal or clearly excessive fee". An annuitized fee to the lawyer after conclusion of the attorney's representation of a client, can be a violation of rule 1.5(a). The potential for ethics violations in an attorney's receiving an annuitized fee seems endless, much less when the fee exceeds the amount owed by the client.

## **What the Neighbors Do**

Pennsylvania's sister states of New Jersey and New York prohibit referral fees from service providers as do Arizona and Ohio. Connecticut, Michigan and Utah do permit an attorney to accept such referral fees. The referral of a client to an investment firm would appear to benefit a client in a situation where the attorney does not accept referral fees but instead is able to negotiate a better rate charged by the investment firm to the client. However, what if the client becomes unhappy and blames the referral of the investment advisor on the attorney, stating, "But for Attorney Jones, I would have gone to a different investment firm." Again, the potential for problems rears its ugly head.

In light of the prohibition against domestic relations attorneys accepting contingent fees which are specifically contingent upon divorce, this writer cannot imagine what family law attorney would take the risk of accepting a referral fee from an investment advisor, even with the client's consent, given the potential for a malpractice suit and/or disciplinary action. Although the Joint Ethics Opinion, with caution, permits attorneys to accept referral fees from an investment advisor, "Within the context of an ongoing lawyer-client relationship . . .", the very definition of what constitutes an ongoing lawyer-client relationship is elusive. In a domestic relations case, if a divorce is "final", and if certain financial obligations, pursuant to court order or agreement are to take place over the next five years subsequent to divorce, does that continuing nexus provide for an "ongoing lawyer-client relationship?" Presently, there is no clear definition of "ongoing lawyer-client relationship."

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In light of the various potential violations that have been explored, the domestic relations attorney is well advised to avoid any scintilla of conflict of interest. In short, the family law attorney must be like Caesar's wife – beyond reproach. If an issue impacting the lawyer-client relationship doesn't pass the smell test, don't do it. The potential repercussions cannot justify a domestic relations attorney accepting a referral fee from an investment advisor, notwithstanding Joint Ethics Opinion 2000-100. •

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