

The Supreme Court of Ohio

BOARD OF COMMISSIONERS ON GRIEVANCES AND DISCIPLINE

41 SOUTH HIGH STREET-SUITE 3370, COLUMBUS, OH 43215-6105
(614) 644-5800 FAX: (614) 644-5804

OFFICE OF SECRETARY

OPINION 2000-1

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Withdrawn by Adv. Op. 2019-10

[CPR Opinion-provides advice under the Ohio Code of Professional Responsibility which is superseded by the Ohio Rules of Professional Conduct, eff. 2/1/2007.]

SYLLABUS: It is ethically improper for a lawyer to accept a fee from a financial services group for referring clients in need of financial services. The referral fee agreement involves an improper business relationship with clients and non-lawyers under DR 3-103(A) and DR 5-104(A). The referral fee agreement creates a financial interest that will affect or reasonably may affect the professional judgment of a lawyer under DR 5-101(A)(1) and DR 5-107(A)(1) and (2). Full disclosure and consent do not resolve the conflict. While DR 5-101(A)(1), DR 5-104(A), and DR 5-107(A)(1) and (2) provide a full disclosure and consent exception, DR 3-103(A) does not. Because of the joint application of these rules, the full disclosure and consent exception does not apply.

OPINION: This opinion addresses whether it is ethically proper for a lawyer to accept a referral fee from a financial services group.

Is it ethically proper for a lawyer to accept a fee from a financial services group for referring clients in need of financial services?

Ohio lawyers are being asked to enter into a business arrangement with a financial services group. The group offers financial services through its investment planners, investment advisors, and money managers. The group offers insurance services through independent insurance specialists and offers accounting services through several local accounting firms. The group proposes paying lawyers a fee for referring clients in need of financial services. Upon referral, the financial services group meets with the client at the lawyer's office. The lawyer is to be present at the initial meeting. The lawyer approves the plan or product before it is offered to the client. The lawyer receives a fee for each client referred. The financial services group and the lawyer negotiate the fee in advance of the referral.

The opinion addresses whether the proposed activity is ethical. The opinion does not address whether a referral fee from a financial/investment advisor is unlawful for that is beyond the advisory authority of the Board of Commissioners on Grievances and Discipline.

Several rules within the Ohio Code of Professional Responsibility are applicable to the question raised, DR 3-103(A), DR 5-101(A)(1), DR 5-104(A), and DR 5-107(A)(1) and (2). These rules govern two ethical concerns relevant to this opinion: (1) Improper

business relationships with clients and other non-lawyers and (2) Interference with the professional judgment of a lawyer.

Improper business relationships with clients and other non-lawyers

DR 3-103(A) A lawyer shall not form a partnership with a non-lawyer if any of the activities of the partnership consist of the practice of law.

DR 5-104(A) A lawyer shall not enter into a business transaction with a client if they have differing interests therein and if the client expects the lawyer to exercise his [her] professional judgment therein for the protection of the client, unless the client has consented after full disclosure.

DR 3-103(A) prohibits the formation of partnerships between lawyers and non-lawyers when any of the activities include the practice of law. DR 3-103(A) has been construed as applying to the formation of business relationships and associations, not just true partnerships formed under state law. *See*, Ohio Sup Ct, Bd Comm'rs on Griev & Disc, Op. 92-15 (1992) advising that a law firm retained by a business corporation to perform services related to the corporation's marketing of wills, durable powers of attorney, and living wills gives the appearance of a business relationship, possibly running afoul of DR 3-103(A); and Ohio Sup Ct, Bd Comm'rs on Griev & Disc, Op. 97-1 (1997) advising that "[a] lawyer who enters a franchise agreement with a non-lawyer would be involved in a business relationship with a non-lawyer where the activities consist of the practice of law in violation of DR 3-103(A)."

The financial services group, while not asking lawyers to form partnerships as defined under state law, is asking for ongoing business associations or relationships with the law firms. As explained below, the proposed business relationships involve activities that consist of the practice of law and therefore violate DR 3-103.

Clients expect lawyers to make appropriate referrals to other individuals or groups when the need becomes apparent during the legal representation. If during the legal representation, a lawyer ascertains that a client needs financial services, the lawyer has a fiduciary duty to refer a client to appropriate resources. These referrals are part of the attorney's practice of law. The lawyer's duty of loyalty demands that the referral be made in the client's best interest, free of compromise and conflict. A lawyer should not make these referral decisions based upon financial incentives that a particular company may offer the lawyer.

DR 5-104 prohibits a lawyer from entering a business relationship with a client when there are differing interests therein. For the reasons stated below, the proposed business relationship involves the lawyer in a business relationship with the client and with the financial services group in which there are differing (and/or the potential for differing) interests that would violate DR 5-104(A) in the absence of informed client consent.

The lawyer appears to be entering a business relationship with only the financial services group and not with the client, but upon closer examination, the business relationship is a

triumvirate. The financial services group receives clients and earns money from the sale of its plans and products. The client receives plans and products from the financial services group and receives legal advice about the plans and products from the attorney. The attorney refers the client, provides office space for the meetings between the financial group and the client, attends the initial meeting, and approves the financial plans and products being offered. The attorney and the financial group might negotiate the referral fee in a variety of ways and as a consequence the interests would vary. For example, the fee might be negotiated as a one-time fee per referral. The fee might be negotiated as a one-time fee based upon how much of the product the client buys. Or, the fee might be negotiated as an ongoing fee throughout the life of the product, such as a negotiated portion of the asset management fee. Regardless, of how the fee is negotiated, there exists a business relationship among the lawyer, client, and the financial services group.

Interference with the professional judgment of a lawyer

DR 5-101(A)(1) Except with the consent of the client after full disclosure, a lawyer shall not accept employment if the exercise of professional judgment on behalf of the client will be or reasonably may be affected by the lawyer's financial, business, property, or personal interests.

DR 5-107(A) Except with the consent of his [her] client after full disclosure, a lawyer shall not:

- (1) Accept compensation for his [her] legal services from one other than his [her] client.
- (2) Accept from one other than his [her] client any thing of value related to his [her] representation of or his [her] employment by his [her] client.

DR 5-101(A)(1) prohibits a lawyer's acceptance of employment when the lawyer has financial, business, property, or personal interests that will affect or reasonably may affect the exercise of a lawyer's professional judgment on behalf of the client. By logical extension, the rule also prohibits a lawyer's continued employment when there are such interests. A referral fee is a financial interest that will or reasonably may affect a lawyer's professional judgment under DR 5-101(A). The more referrals, the more money made.

DR 5-107(A)(1) prohibits a lawyer from accepting compensation for legal services from one other than the client. As already stated, making an appropriate referral of represented clients in need of financial services is a legal service expected of a lawyer in fulfilling his or her fiduciary duties to a client. A referral fee paid by a financial services group to a lawyer falls within the ambit of this rule because the fee indirectly provides compensation to a lawyer for expected legal services.

DR 5-107(A)(2) prohibits a lawyer from accepting any thing of value related to his or her representation or employment of the client. A fee paid by a financial services group to a lawyer for referring a client to the group is a thing of value related to a lawyer's representation or employment of the client and is restricted by this rule.

These rules provide that consent of a client after full disclosure obviates the restrictions of the rules. Nevertheless, whether a referral fee paid to a lawyer is appropriate upon client consent is subject to interpretation and is an area of disagreement among ethics committees interpreting the rules of professional conduct.

One view is that disclosure and consent cure such conflict.

Connecticut Bar Ass'n, Informal Op. 97-16 (1997). An attorney may accept a referral fee from a network of associated investment advisor representatives if the referring attorneys abide by certain requirements including disclosure and consent.

Missouri SupCt, Chief Disciplinary Counsel, Op. 960124 (undated). An attorney's participation in a program involving payment of an ongoing fee to an attorney by an investment advisor and securities broker-dealer for referring a client who opens an account will violate Rule 4-1.7(b), unless the attorney fully discloses the relationship and the potential for the attorney to receive a financial benefit as a result of the referral.

Rhode Island SupCt, Ethics Advisory Panel, Op. 99-08 (1999). A lawyer may accept a referral fee from a business associate for referring a client in need of investment services, if permitted by the rules and law governing the other business, but pursuant to Rule 1.8(a) must disclose that fact to the client.

Another view is that disclosure and consent do not cure the conflict.

Kentucky Bar Ass'n, Op. E-390 (1996). A lawyer may not receive compensation structured as a percentage share of a recurring account management fee for the lawyer's referral of a client to an investment advisor, even after disclosure to and consent by the client.

Maryland State Bar Ass'n, Op. 96-17 (1995). A lawyer may not ethically participate in a proposed business arrangement with a financial planning organization pursuant to which the lawyer, following settlement, having previously entered the relationship with the organization, refers a client for financial planning services and receives a commission if the client purchases any financial service. The committee noted in footnote 2 of the opinion that "even with full disclosure to the client, this Committee most probably would not condone the marketing arrangement."

New York State Bar Ass'n, Op. 682 (1996). An attorney may not accept a referral fee from an investment advisor. Disclosure and consent would not cure the conflict.

Vermont Bar Ass'n Op. 98-8 (undated). A lawyer may not accept a referral fee from an investment advisory service even with prior disclosure and consent by the client.

This Board agrees that clients expect appropriate referrals by their lawyers during the course of representation and that such referrals should be made free of financial incentive to the lawyers. *See, e.g.*, Vermont Bar Ass'n, Op. 98-8 (undated) advising that "[c]lients view recommendations to other professionals as part of their representation by their lawyers and expect their lawyers to act independently of any underlying financial interest in such referral; New York State Bar Ass'n Op. 682 (1996) advising that "disclosure and consent would not cure the direct and substantial conflict between the client's and lawyer's interests inherent in accepting a referral fee from the investment advisor, even where the client is offered the choice to claim the referral fee and the attorney purports to exercise independent judgment in framing his or her initial recommendation to consult an investment advisor. Clients view recommendations of other professionals as part of their representation by their lawyers, and expect that lawyers will act as trusted fiduciaries in such matters."

This board also agrees that full disclosure and consent do not resolve the conflict. Under the Ohio Code of Professional Responsibility, DR 5-101(A)(1), DR 5-104(A), and DR 5-107(A)(1) and (2) provide a full disclosure and consent exception, but DR 3-103(A) does not. Because of the joint application of these rules to the issue raised, the full disclosure and consent exception does not apply.

In *Cincinnati Bar Ass'n v. Bertsche*, 84 Ohio St. 3d 170, 174 (1998), the Supreme Court of Ohio imposed an indefinite suspension on an attorney who, along with committing other misconduct, assisted bankruptcy clients in obtaining loans from a company to pay off their Chapter 13 balances and received \$1200 to \$1900 in fees from the company on each loan. According to the court,

[r]espondent neither advised his clients in advance of his fees for loan refinancing nor filed the required applications to inform the court of those fees. As a consequence, respondent set his fee unilaterally with no input from his clients or the court. Thus, if respondent represented his clients in the loan transactions, he failed to adhere to our Ethical Considerations and failed to comply with the federal bankruptcy rules.

The record indicates that at least two of respondent's clients believed that the \$1500 added to their loans was a fee that Associates [the company] paid to respondent for referring the clients to it. If such was the case, respondent was in a conflict-of-interest situation. In either this situation or the unilateral-fee-setting situation, respondent was in violation of our disciplinary standards.

Id. at 173-74.

In conclusion, this Board advises that it is ethically improper for a lawyer to accept a fee from a financial services group for referring clients in need of financial services. The referral fee agreement involves an improper business relationship with clients and non-lawyers under DR 3-103(A) and DR 5-104(A). The referral fee agreement creates a financial interest that will affect or reasonably may affect the professional judgment of a lawyer under DR 5-101(A)(1) and DR 5-107(A)(1) and (2). Full disclosure and consent do not resolve the conflict. While DR 5-101(A)(1), DR 5-104(A), and DR 5-107(A)(1)

and (2) provide a full disclosure and consent exception, DR 3-103(A) does not. Because of the joint application of these rules, the full disclosure and consent exception does not apply.

Advisory Opinions of the Board of Commissioners on Grievances and Discipline are informal, nonbinding opinions in response to prospective or hypothetical questions regarding the application of the Supreme Court Rules for the Government of the Bar of Ohio, the Supreme Court Rules for the Government of the Judiciary, the Code of Professional Responsibility, the Code of Judicial Conduct, and the Attorney's Oath of Office.