New York State Bar Association

Committee on Professional Ethics

Opinion 753 – 2/26/02

Topic: Ancillary business organizations; mortgage brokerage; title abstract company; conflict of interest

Digest: Where a client is represented by a lawyer and uses an ancillary business owned by the lawyer, the rules applicable to personal conflicts of interest and transactions between clients and lawyers continue to apply after promulgation of DR 1-106. Under those rules, a lawyer owning mortgage brokerage and title abstract businesses may not, even with informed consent, represent buyer or seller and act as mortgage broker in the same transaction or act as title abstract company with respect to non-ministerial tasks, but may, where the client consents after full disclosure, act as abstract company with respect to purely ministerial abstract work. The lawyer may, with informed consent, represent the lender in the same transaction in which the lawyer's company acts as mortgage broker, but may not represent the lender in transactions in which the lawyer's title abstract company acts in other than a ministerial capacity. The lawyer may in certain circumstances, with informed consent, represent both the buyer's lender and the seller in the same transaction or, where not required to negotiate terms, the buyer's lender and the buyer in the same transaction.

Code: DR 1-106; DR 1-107; DR 5-101(A); DR 5-105; EC 1-14.

QUESTIONS

A lawyer is the sole shareholder of a licensed New York mortgage brokerage corporation and a separate title abstract company. Where the attorney informs the client of the attorney's other business relationships and discloses same to the client in a Statement of Client's Rights in Cooperative Business Arrangements, and where the client gives informed written consent, may the attorney and/or the attorney's companies:

1. Represent the selling client in a real estate transaction and (a) broker the mortgage for the buyer, (b) act as the lender's attorney at closing, and (c) act as the abstract company for the transaction?

2. Represent the buying client in a real estate transaction and (a) broker the mortgage for the buyer, (b) act as the lender's attorney at closing, and (c) act as the abstract company for the transaction?

OPINION

On July 23, 2001, the Appellate Divisions adopted new rules on multidisciplinary practice, effective November 1, 2001. One of those rules, DR 1-106 (22 NYCRR §1200.5-b), addresses the responsibilities of lawyers or law firms providing nonlegal services to clients or other persons, including lawyers or law firms that own or control or are otherwise affiliated with an entity providing nonlegal services to clients of the lawyer or law firm. That rule provides, in pertinent part, that where an entity controlled by a lawyer or law firm provides nonlegal services to a person, the lawyer or law firm is subject to the disciplinary rules with respect to the nonlegal services if the person receiving the services could reasonably believe that the nonlegal services are the subject of an attorney-client relationship. DR 1-106(A)(3). The rule goes on to state that

> it will be presumed that the person receiving nonlegal services believes the services to be the subject of an attorney-client relationship unless the lawyer or law firm has advised the person receiving the services in writing that the services are not legal services and that the protection of an attorney-client relationship does not exist with respect to the nonlegal services, or if the interest of the lawyer or law firm in the entity providing nonlegal services is de minimis.

DR 1-106(A)(4).

In opinions issued prior to the new rules, this Committee held that in certain circumstances a lawyer also engaged in a nonlegal business could not

provide both legal and nonlegal services in the same transaction even with the consent of the client. In particular, with respect to brokers, we held in N.Y. State 208 (1971), N.Y. State 291 (1973), N.Y. State 340 (1974), and N.Y. State 493 (1978), that a lawyer could not act as a lawyer in the same transaction in which the lawyer or his or her spouse acted as a real estate broker "because of the possible conflict between his client's and his own personal interest." N.Y. State 208 (1971). *Accord* N.Y. County 685 (1991); *see also* N.Y. State 694 (1997) (impermissible to participate in broker-run home buyer's program because of resulting strong interest in broker's success). We do not appear to have addressed mortgage brokers, but have reached similar conclusions with respect to insurance brokers and securities brokers. N.Y. State 536 (1981); N.Y. State 619 (1991). We have also suggested, though, that a lawyer-broker can sell insurance to a client where advice about the purchase of insurance products is "merely tangential" to the legal representation. N.Y. State 687 (1997); N.Y. State 711 (1998).

With respect to abstract title companies, in N.Y. State 595 (1988), N.Y. State 621 (1991), and N.Y. State 738 (2001), we held that a lawyer could, with consent after disclosure, refer real estate clients to a title abstract company in which the lawyer or his or her spouse had an ownership interest "for purely ministerial abstract work," but not where the abstract company provided the additional service of preparing a title report or serving as an agent for the title underwriter. The central rationale was that if the abstract company prepared a report showing exceptions in title and recommending whether a title insurance policy should be issued, the law firm for the party would be required "to negotiate these issues . . . with itself." N.Y. State 738 (2001). *See also* N.Y. State 731 (2000) (lawyer cannot pay employees to refer clients to lawyer-owned title company for non-ministerial tasks).

In N.Y. State 752 (2002), we concluded that these decisions, and similar opinions limiting or barring lawyers from performing dual roles, survive the promulgation of DR 1-106. This is because the decisions were based on the application of DR 5-101(A) to the *legal* services, not the nonlegal services. That rule bars a lawyer from accepting legal employment if the exercise of professional judgment might be affected by the lawyer's own "financial, business, property or personal interests." The pursuit of the nonlegal business activities in the same transaction in which the lawyer was representing a client created an irreconcilable conflict for the lawyer.

We turn now to the particular dual employments suggested by the inquirer.

Representing Buyer or Seller and Acting as Lender's Attorney.

This part of the inquiry does not involve ancillary businesses at all. The inquirer proposes to represent as a lawyer, in the first question, both the selling

client and the lender and, in the second, both the buying client and the lender. These questions are governed by DR 5-105, which regulates conflicts of interest in simultaneous representations.

Taking the second question first, the proposal to represent both the buying client and the lender in the same transaction creates the potential for a clear conflict. The role of the lender's attorney can be, in part, to protect the interests of the bank in negotiating the loan agreement with the borrower and obtaining the necessary security on the borrower's property. The role of the buyer's attorney can be, in part, to protect the borrower's interests in those same matters. In situations in which the lawyer for the buyer could be called upon to negotiate with the lawyer for the lender, it would not be possible for one lawyer to play both roles, even with consent, because that would put the lawyer in the position of negotiating with him or herself. The lawyer could not zealously represent both parties. *See* DR 5-105(C); N.Y. City 2001-2 ("Situations in which a lawyer or members of a single law firm would be required to negotiate directly with herself or each other on behalf of multiple clients in a transaction ... will rarely be consentable").

This committee has recognized, however, that in some circumstances there is no negotiation or assertion of rights between the lender and buyer in which a lawyer has any role. As long as full disclosure of the risks of dual representation has been made and knowing consent obtained, we have held such dual representation can be permissible. N.Y. State 8 (1965); N.Y. State 199 (1971); N.Y. State 438 (1976); N.Y. State 694 (1997); *see also* ABA Inf. 643 (1963) (same); ABA Inf. 837 (1965) (same). *But see* Nassau County 98-10 (lawyer may not represent buyer and lender in same residential purchase and mortgage transaction).

This committee has likewise recognized that representation of a seller and a lender, which commonly do not directly negotiate with each other at all, can be permissible with consent after disclosure. N.Y. State 611 (1990). Even here, we have cautioned that there may be circumstances when the dual representation would be barred:

> If, for example, issues arise concerning the acceptability of title, or environmental conditions, or some other condition of closing, the seller may desire to close while the lender may decide it has no obligation to make the loan. ... Where in a particular matter it is not unlikely that such differing interests may arise, the multiple representation should be declined.

Id.

Representing Buyer, Seller or Lender and Acting as Mortgage Broker.

The inquirer also asks whether the brokerage company can act as the buyer's mortgage broker in the same transaction in which the inquirer represents as counsel either the seller or the buyer, and the lender. As noted, this committee has held in a number of opinions that a lawyer cannot act as a real estate broker and as counsel to a party in the same transaction. N.Y. State 208, 291, 340, 493. The rationale for these opinions is that a lawyer should not have a personal stake in the advice rendered, and a broker who is paid only if the transaction closes cannot be fully independent in advising the client as a lawyer.

With respect to the buyer or seller, we see nothing in the nature of the mortgage brokerage business that calls for a different result. The inquirer advises that a mortgage broker is paid a percentage of the money borrowed and only when the loan closes. While the amount of the fee varies widely, the gross mortgage broker fee (before subtraction of the individual salesperson's fee) almost always exceeds the legal fee a lawyer receives for representing a buyer or seller in a typical, uncomplicated purchase or sale in the inquirer's area. Under these circumstances, the rationale of our prior opinions with respect to real estate brokers applies with full force. *See also* Nassau County 89-33 ("By acting as an associate of the mortgage broker for a commission, the attorney would then have a divided loyalty between the obligations to his client and the desire to see the transaction close."); Nassau County 41/87 (similar); N.C. 248 (1997) (attorney may not "certify title or act as settlement agent because [attorney's] personal interest in seeing that [mortgage brokerage corporation] receives its fee or commission for placing the loan could conflict with the client-borrower's desire to close only when it is in his or her best interest to do so"). *But see* S.C. 96-04 (permitting dual role, but cautioning, "An attorney must determine that his conflicting role as a mortgage broker will not affect the attorney's ability to judge independently and render candid advice").

The opinions in which we have suggested that a lawyer-broker might sell insurance to a client if the purchase was "merely tangential" to the advice are different, for there the lawyer was not engaged for estate planning or for similar advice that could be influenced by a desire to ensure that the insurance purchase would close. As we said in N.Y. State 711, "[I]f there is a reasonable probability (viewed objectively) that the lawyer's professional judgment will be adversely affected by the lawyer's business interests, then the lawyer must not offer to sell insurance to client." In the case of the mortgage broker, whose interest is in seeing the transaction close, there is such a reasonable probability.

Our opinions do not address at any length whether the prohibition on brokers acting as lawyers extends to lawyers for lenders.[1] Whatever may be the

[1] N.Y. State 694 (1997) noted in passing that a lawyer could not participate in a real estate broker's program to provide a single, lower-cost attorney to represent the lender and the buyer:

situation with real estate brokers, the lender is in quite a different position in relation to the mortgage broker than the buyer or seller. The mortgage broker is frequently simply a distribution channel for the lender, who sets the terms of the products that will be offered and pays the mortgage broker's compensation. The lender is typically a sophisticated commercial entity. If it is not happy with the relative incentives provided by the amounts it pays for brokerage and legal services, it can decline to consent to the dual representation. If it wishes to have the greater set of "checks and balances" provided by separating the mortgage broker and legal functions, it can do so. Further, the lender will frequently have an ongoing relationship with the mortgage broker/lawyer, thus tempering any impulse by the broker/lawyer to "close at any cost." Finally, there is rarely substantial negotiation of the terms of a residential mortgage, and the lawyer's range of discretion is correspondingly narrower, so any less-than-vigorous representation of the lender will be easier to detect. In short, we do not believe that the dual status of mortgage broker and lender's attorney creates "'such delicate conflicting relationships and inescapable divided loyalties that the likelihood of improper conduct or motivation, without any showing of harm and regardless of disclosure and consent, may give rise to professional misconduct.'" N.Y. State 516 (1980) (*quoting Matter of Kelly*, 23 N.Y.2d 368, 378, 296 N.Y.S.2d 937, 945-46 [1968]). With full disclosure and consent, we conclude there are transactions in which a lawyer may act as counsel to an institutional lender and as a mortgage broker for that lender.

We are aware that in some circumstances mortgage brokers receive cash compensation from the buyer or undertake, or otherwise have, duties to the buyer to find the best possible mortgage for the buyer. It is possible that in such circumstances the broker's duties to the buyer would raise an insurmountable conflict for the lender's lawyer; however, we do not believe that should call for a per se rule. If, for example, the lender's lawyer was retained only after the loan had been placed with a particular lender, the mortgage broker's duties to the buyer may have been discharged before the lawyer's duties to the lender begin. In addition, we do not deal here with any disclosure obligations the mortgage broker may have to the buyer, as that is not a question of legal ethics.

Representing Buyer, Seller or Lender and Acting as Abstract Company.

As noted, in N.Y. State 595, 621 and 738 we found that a lawyer could not refer real estate clients to a title abstract company in which the lawyer had an ownership interest and that would be hired to provide insurance or perform other than ministerial tasks. That conclusion was based on DR 5-101(A). *See, e.g.,* N.Y. State 738 (2001). As set forth above, those rules continue to apply after the

---

"We believe the personal financial incentive for the attorney to use his or her influence over the Purchaser to secure an enforceable contract of sale and to close the transaction is sufficiently great that it is not at all obvious that the Attorney can adequately represent the interests of the Purchaser *and Lender* as well." (Emphasis added.)

promulgation of DR 1-106. Our opinion in N.Y. State 595 expressly extended this prohibition to counsel for the lender. The lender's interests in marketable, insured title at the lowest price are little different from the buyer's.

The inquirer reports that in the inquirer's geographic region, abstract companies "do the research, work the file and present the package to the Title Insurance Companies who provide the Title Insurance to the buyer." This appears to go beyond the purely ministerial abstract searching contemplated by our earlier opinions. To the extent that the abstract company examines the title and makes recommendations on insurability or exceptions, it would appear to have an irreconcilable conflict with its attorney-owner's duty to provide independent advice and negotiate title problems, if necessary.

We note one further matter. The inquirer intends to provide clients with a "Statement of Client's Rights in Cooperative Business Arrangements," in order to inform the clients that the services performed by the inquirer through the title abstract company are not legal services and that the protection of an attorney-client relationship does not exist with respect to the nonlegal services. The Statement of Client's Rights in Cooperative Business Arrangements is a statement prescribed by 22 NYCRR §1205.4 for use in alerting clients to the existence of contractual relationships between lawyers and nonlegal professionals commonly involving the reciprocal referral of clients and, to a certain extent, the sharing of premises, overhead and professional fees. *See* DR 1-107; EC 1-14. It is not clear that this Statement is appropriate in these circumstances. The inquirer does not refer to any agreements or understandings for the reciprocal referral of clients between the law firm and the ancillary businesses, which is the focus of the Statement; the Statement does not disclose the fact that the lawyer owns the mortgage brokerage and abstract title companies, which is highly material; and the Statement does not expressly state that the protections of the attorney-client relationship do not exist with regard to the nonlegal services, as required by DR 1-106(A)(4). We advise the inquirer to use in place of the Statement of Client's Rights in Cooperative Business Arrangements, or to supplement it with, a statement more tailored to the requirements of DR 1-106(A)(4) and DR 5-101(A).

CONCLUSION

A lawyer who owns a title abstract company and a mortgage brokerage is barred from acting as a lawyer in a transaction in which one or both of those companies is also acting in a variety of situations in which the lawyer's personal interest in a fee (or dividend) from the ancillary businesses compromises the independence of the lawyer's legal advice. Our conclusions on this are summarized in the following chart, in which "Y" means that the lawyer can act in the dual capacity in certain circumstances, with informed consent and under the conditions set forth above and in our prior opinions, and "N" means the lawyer cannot act in the dual capacity at all:

CAN LAWYER ACT IN DUAL ROLE WITH INFORMED CONSENT?			
	Buyer's Lawyer	Seller's Lawyer	Lender's Lawyer
Mortgage Brokerage	N	N	Y
Title Abstract Co. providing insurance or making insurance recommendation	N	N	N
Title Abstract Co. performing only "ministerial tasks"	Y	Y	Y

(43-01)