



**New York State Bar Association
Committee on Professional Ethics**

Opinion 1086 (3/7/2016)

Topic: Referral fee from investment advisor

Digest: An attorney may not accept a fee or commission from an investment firm for referring the client to such firm where the money to be invested arises from an engagement in which the lawyer represented the client because the fee creates a non-consentable conflict.

Rules: 1.7(a)(2), 1.7(b), 1.8(f)

FACTS

1. The inquiring attorney represents clients in workers' compensation and personal injury matters. Some of the attorney's clients receive large sums of money as a result of their cases, and when that happens, clients commonly ask the attorney for advice regarding how to manage the settlement funds.
2. When clients ask about managing their settlement funds, the inquiring attorney would like to refer them to a licensed investment professional with whom he has a relationship and receive a fee or commission from the investment firm. The inquirer represents that he may receive such a fee or commission because he holds a number of securities and insurance licenses.
3. The inquirer states he would make the referral only after all legal work has concluded, the client's case has closed and the inquirer has fully disclosed to the client that the inquirer will financially benefit from the referral.

QUESTION

4. May an attorney refer clients to an investment firm with whom the attorney has a professional relationship and receive a fee or commission from the investment firm for the referral?

OPINION

5. We note at the outset that the Committee does not opine on questions of law, and thus, does not opine on whether the proposed fee or commission violates any statute or regulation. In the event the proposed fee or commission is illegal and reflects adversely on the lawyer's honesty, trustworthiness or fitness as a lawyer, it would violate Rule 8.4(b). *See also* N.Y. State 845 (2010); N.Y. State 667 (1994); N.Y. State 595 (1988); N.Y. State 576 (1986); N.Y. State 461 (1977). For purposes of the following analysis, we assume that the investment firm may

legally pay the attorney a fee or commission and that such payment is not otherwise illegal.

Applicable Rules Provisions

6. Whether a lawyer may accept a referral fee from a third party service provider generally involves analysis of New York Rules of Professional Conduct (the "Rules") 1.7(a)(2) and 1.8(f).

7. Rule 1.7(a)(2) governs conflicts involving a lawyer's personal interests and generally prohibits a representation in which there is a significant risk that the lawyer's personal interests would have an adverse effect on the lawyer's exercise of professional judgment, unless the conflict can be and is waived under Rule 1.7(b).

8. Rule 1.8(f) provides that "a lawyer shall not accept compensation for representing a client, or anything of value related to the lawyer's representation of the client, from one other than the client unless: (1) the client gives informed consent; (2) there is no interference with the lawyer's independent professional judgment or with the client-lawyer relationship; and (3) the client's confidential information is protected as required by Rule 1.6."

9. A number of our prior opinions have permitted a lawyer to accept a referral fee or commission from a third-party service provider for referring a client to the service provider under very limited circumstances. *See, e.g.*, N.Y. State 981 (2013) (referral fee not prohibited by Rule 1.7 where the service is not related to the lawyer's legal services and the lawyer makes no recommendation to use the service); N.Y. State 667 (1994) (lawyer may accept referral fee from mortgage broker notwithstanding predecessors to Rules 1.7(a) and 1.8(f) as long as client consents and all proceeds are credited to client if client so requests); N.Y. State 626 (1992) (lawyer for lender may retain fees from a title insurance company as long as client consents and amount of the fee is disclosed to the borrower who will pay the cost of the insurance and the total amount of the lawyer's fee is not excessive); N.Y. State 576 (1986) (lawyer may act as agent for title insurance company and also represent the buyer, seller or mortgagee in a real estate transaction consistent with the predecessors to Rules 1.7(a) and 1.8(f) as long as lawyer credits client with amount received from title insurer or the client expressly consents to the lawyer retaining the fee paid by the insurer); N.Y. State 461 (1977) (lawyer may accept part of a fire adjuster's commission consistent with predecessor to Rule 1.7(a) if client consents and all proceeds thereof are credited to client); and N.Y. State 107 (1969) and N.Y. State 107(a) (1970) (both permitting lawyer to accept a referral fee from a financial company where the lawyer invests the client's funds in certificates of deposit, if client consents after disclosure and lawyer remits the fee to client if client so requests).

10. On the other hand, a number of our prior opinions have prohibited a lawyer from accepting a referral fee or commission from a third-party service provider for referring a client to the service provider. Where our opinions have held that a lawyer may not accept a fee from a third-party service provider, we often have found that the lawyer's personal conflict of interest is so great that disclosure to and consent from the client will not cure the conflict. *See, e.g.*, N.Y.

State 682 (1996) (lawyer may not accept a fee from an investment adviser for referring a client under predecessor to Rule 1.7 because disclosure and consent would not cure the lawyer's direct and substantial conflict); N.Y. State 671 (1994) (lawyer engaged in estate planning may not accept referral fee from insurance company for referring client under predecessor to Rule 1.7 because disclosure and consent could not cure the direct and substantial conflict between the client's and the lawyer's interests); N.Y. State 619 (1991) (where estate planning lawyer's remuneration from the third party would vary with the quantity of the product or services recommended, receipt of the referral fee was impermissible under predecessors to Rules 1.7 and 1.8(a) [business transaction with client] because the lawyer's substantial financial interest conflict could not be cured by disclosure and consent).

11. N.Y. State 682 identifies two factors that determine whether the lawyer's financial interest in a referral fee¹ is so great that disclosure and client consent will be ineffective. A client may give informed consent for a referral fee when (1) the transaction at issue concerns a product or service that is fairly uniform among providers and is required in an objectively determinable quantity or (2) when the product or service is fairly uniform among providers and is unconnected to any particular legal services.

Application to the Inquirer's Proposal

12. The first questions under our prior opinions are (i) whether the products or services that are the subject of the referral are fungible in nature, (ii) whether the required amount is objectively determinable, and (iii) whether the product or service is unconnected to the legal services provided by the lawyer.

13. In N.Y. State 682 (1996) we determined that an attorney may not accept a fee from an investment advisor for referring a client to the advisor, because the services of advisors vary substantially among different providers and the amount of funds that should ideally be entrusted to any particular advisor is not objectively determinable. Consequently, we said, the potential exists that "the attorney might increase the referral fee by recommending that more of the client's funds be entrusted to the advisor without appropriate regard to the client's interests." Accordingly, we found that meaningful consent was not possible, even where the client is offered the choice to claim the referral fee and the attorney purports to exercise independent judgment in framing the initial recommendation to consult an advisor.

14. Similarly, in N.Y. State 1043 (2015), we opined that a lawyer representing a client in a real estate transaction could not ethically accept a referral fee from the real estate broker in lieu of charging legal fees. Opinion 1043 followed from our prior opinions generally holding that a

¹ We see no distinction between the fee or commission proposed here and a "referral fee". The proposed fee or commission would result from the attorney recommending that the client consult with an investment professional with whom the lawyer has a professional relationship.

lawyer may not act as a lawyer and a broker in the same real estate transaction because the “lawyer’s pecuniary interest in the broker’s success and attendant commission ... irredeemably interferes with the lawyer’s distinct obligation to exercise independent professional judgment on the client’s behalf.”

15. Here, as in N.Y. State 682, the services of the investment advisors are not uniform nor is the amount of funds that should ideally be entrusted to any particular adviser objectively determinable. The lawyer here, when asked by the client to recommend an investment advisor, should be making that recommendation based on the needs of the client. That means recommending an advisor based on the services the advisor provides or even recommending more than one advisor in order to meet the client’s needs. However, under these circumstances, we do not believe that the lawyer will be able to exercise independent judgment in making a recommendation given the prospect of receiving a referral fee based on recommending a particular advisor. Further, under these circumstances, our prior opinions provide that disclosure to and consent of the client is impermissible because the interests of the client and attorney are in such direct conflict that the client cannot give meaningful consent.

16. Thus, a non-waivable conflict under Rule 1.7(b) exists here. Accordingly, we need not reach the issue of whether the lawyer could meet the requirements of Rule 1.8(f), which include both informed consent and the absence of interference with the lawyer’s independent professional judgment, in order to accept a payment in connection with representing a client from one other than the client.

17. Additional facts present under the circumstances here also support our conclusion that a non-waivable conflict exists. For example, in the course of the representation, the attorney might decide to recommend a settlement rather than risk going to trial because a settlement will not only produce a definite legal fee, but also is likely to produce a referral fee from the investment advisor. Conversely, if the attorney sees the possibility of a large jury verdict but the client prefers the "bird in the hand" of a settlement, the attorney might steer the client toward trial in hopes of generating a larger pool of funds on which to collect a commission from the investment advisor. Thus, where the lawyer is counseling (or should be counseling) a client on whether the client should settle or proceed to trial, the prospect of a larger referral fee from an investment advisor produces exactly the kind of conflict that we have said is non-consentable in other contexts.

18. Similarly, when counseling a client about the payment options for a potential settlement, the attorney may be likely to steer the client toward a lump sum payment rather than another option, such as a structured settlement, in order to maximize the opportunity for a referral fee. Again, the lawyer’s advice to a client would be affected by the prospect of a referral fee, rather than the course that is in the best interest of the client.

19. We recognize that the inquiring attorney has stated that the referral to the investment firm would only be made after the representation of the client concluded. However, if clients frequently ask the lawyer to recommend an investment adviser, the lawyer’s judgment in

structuring a settlement may be affected even if the recommendation is not made until after the settlement has been agreed upon. Moreover, in some instances, particularly, as we understand it, in workers' compensation matters, the client's case remains subject to review at future proceedings, and the client therefore may require representation on an ongoing basis over an extended period of time. Under these circumstances, it would be difficult to identify a particular moment when the representation concludes. Thus, our holding in N.Y. State 1043, that a conflict exists regardless of whether the referral fee is offered before or after the representation concludes, also applies to the facts here.

CONCLUSION

20. An attorney may not accept a fee or commission from an investment firm for referring the client to such firm where the money to be invested arises from an engagement in which the lawyer represented the client because the fee creates a non-consentable conflict.

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