NEW YORK STATE BAR ASSOCIATION
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New York State Bar Association
Committee on Professional Ethics

Opinion 1256 (05/26/2023)

Topic: Lawyer purchasing claims from clients of his law firm through a company he owns and then prosecuting those claims by retaining the law firm, or by retaining another law firm with which the lawyer has no affiliation.

Digest: A lawyer may not purchase claims through a company he owns from clients of a law firm where the lawyer is employed and then prosecute those claims by retaining the law firm. Whether a lawyer can purchase claims through a company he owns from clients of a law firm where the lawyer is employed, and then prosecute those claims by retaining another law firm with which the lawyer has no affiliation is not expressly governed by the New York Rules of Professional Conduct. Assuming such conduct is not illegal under Judiciary Law section 488, it is subject to the provisions of Rule 1.8(a), which govern business transactions with clients.

Rules: 1.8(a), 1.8(i), 8.4(a).

FACTS:

1. The inquirer is employed by a law firm in which he has no ownership interest. The firm's practice includes litigation against insurance companies that have denied or disclaimed insurance coverage. Rather than engage the firm to pursue such coverage claims on behalf of the insureds, some clients would prefer to sell and assign their claims outright to the law firm for an agreed price.

QUESTIONS:

2. The inquirer asks if a company he owns can purchase denied insurance claims from clients of the law firm where he is employed and then retain that law firm to litigate those claims?

3. If not, may a company that the inquirer owns purchase the denied insurance claims and retain another law firm with which the inquirer has no employment affiliation to litigate on behalf of the company?

OPINION:

4. Rule 1.8(i) of the New York Rules of Professional Conduct provides that "[a] lawyer shall not acquire a proprietary interest in the cause of action or subject matter of litigation the lawyer is conducting for a client." That provision prevents the inquirer from purchasing, on behalf of a corporation he owns, the denied insurance claims of clients of the law firm where he works, and then retaining that law firm to litigate those claims. See also Restatement Third, The Law Governing Lawyers § 36 ("Forbidden Client–Lawyer Financial Arrangements")(discussing the prohibition in Rule 1.8(i)).

5. While it is a question of law beyond the scope of our jurisdiction, the inquirer should also consider whether the proposed conduct violates the prohibitions in Judiciary Law section 488, entitled "Buying demands on which to bring an action." See Judiciary Law § 488(1) ("An attorney or counselor shall not…[d]irectly or indirectly, buy, take an assignment of or be in any manner interested in buying or taking an assignment of a bond, promissory note, bill of exchange, book debt, or other thing in action, with the intent and for the purpose of bringing an action thereon.").

6. The inquirer's second question is whether a company he owns can purchase the denied insurance claims and retain another law firm with which the inquirer has no employment affiliation to litigate the claims on behalf of the company. While this conduct is not expressly governed by Rule 1.8(i), we note that "[a] lawyer or law firm shall not…violate or attempt to violate the Rules of Professional Conduct…through the acts of another." Rule 8.4(a).

7. Assuming that the purchase of a client's denied insurance claim, with the intent to prosecute that claim through another law firm, is not illegal under the provisions of the Judiciary Law and other substantive law, it would be subject to Rule 1.8(a), which governs business transactions with clients. See N.Y. State 1231 (2021) (an estate-planning lawyer who has an interest in a nonlegal financial management company that the lawyer hopes to recommend to estate-planning clients must comply with Rule 1.8(a)). Rule 1.8(a)(1) requires that the terms of the transaction be "fair and reasonable to the client." Furthermore, "the terms of the transaction [must be] fully disclosed and transmitted in writing in a manner that can be reasonably understood by the client." Rule 1.8(a)(1). Rule 1.8(a)(2) requires that the client be advised in writing of the desirability of seeking the advice of independent legal counsel on the transaction and be provided with a reasonable opportunity to seek independent counsel. See Rule 1.8(a), Comment [2] ("When necessary, the lawyer should discuss both the material risks of the proposed transaction, including any risk presented by the lawyer's involvement and the existence of reasonably available alternatives, and should explain why the advice of independent legal counsel is desirable."). Finally, Rule 1.8(a)(3) requires that the client give an "informed consent, in a writing signed by the client, to the essential terms of the transaction and the lawyer's role in the transaction, including whether the lawyer is representing the client in the transaction."

8. While a client need not be independently represented when consummating a business transaction with her lawyer, certain requirements in Rule 1.8(a) are deemed satisfied if independent representation exists. As Comment [4] to Rule 1.8 states:

> If the client is independently represented in the transaction, paragraph (a)(2) is inapplicable, and the requirement of full disclosure in paragraph (a)(1) is satisfied by a written disclosure by either the lawyer involved in the transaction or the client's independent counsel. The fact that the client was independently represented in the transaction is relevant in determining whether the agreement was fair and reasonable to the client, as paragraph (a)(1) further requires.

CONCLUSION:

9. A lawyer may not purchase claims through a company he owns from clients of a law firm where the lawyer is employed and then prosecute those claims by retaining the law firm. The question of whether a lawyer can purchase claims through a company he owns from clients of a law firm where the lawyer is employed, and then prosecute those claims by retaining another law

firm with whom the lawyer has no affiliation, is not expressly governed by the New York Rules of Professional Conduct. Assuming such conduct is not illegal under Judiciary Law section 488, it is subject to the provisions in Rule 1.8(a), which govern business transactions with clients.

(06-23)