L.E.O. 2006-01[1]

IS IT PROPER FOR A LAWYER TO ACCEPT A REFERRAL FEE FROM A FINANCIAL SERVICES PROVIDER?

Introduction

The Lawyer Disciplinary Board has received a request to review a proposal from a financial investment advisor concerning a program entitled the LPL Partners Program. The proposal detailed in the literature submitted to the Lawyer Disciplinary Board suggests that lawyers could enter into a "strategic relationship" with the financial advisor "to offer fee-based investment solutions" to their clients. For each client referral that results in an investment advisory account with the financial services provider, the lawyer would then receive "an on-going percentage of the advisory fee as compensation."[2] The literature further cautions that the lawyer should refer clients to the financial investment advisor only after "obtaining appropriate state investment advisory representative licensing and providing written disclosure of their relationship with the . . . financial advisor." While the instant request is specific to the LPL Partners Program, the Board recognizes that there may be other financial services groups with programs such as this one which involve lawyers receiving a referral fee for referral of the lawyer's clients to the financial services group.[3] Thus, the

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[1] At its December 9, 2005 meeting, the West Virginia Lawyer Disciplinary Board voted to change the title of its Formal Opinions from Legal Ethics Inquiries (L.E.I.) to Legal Ethics Opinions (L.E.O.).

[2] In the cover letter attached to the literature, the financial investment advisor stated that "[a]ttorneys involved would be paid as 'solicitors' and not Investment Advisors." For the reasons stated below, the Board is of the opinion that this distinction is irrelevant.

[3] The Board believes that this L.E.O. can also offer general guidance to lawyers with regard to other instances in which a lawyer may have an ownership or other pecuniary interest adverse to his or her client, including but not limited to ownership interest in a real estate company or other business. However, lawyers are cautioned to also review any *West Virginia Rules of Professional Conduct* or other L.E.I. that may more specifically relate to his or her particular situation.

Board issues this opinion to offer guidance to lawyers regarding the potential ethical problems associated with such programs and whether it is ethically proper for a lawyer to accept a referral fee from a financial services provider or investment advisor.

Discussion

The referral fee arrangement raises concerns under several of the *West Virginia Rules of Professional Conduct*, including Rule 2.1 (professional independence of attorney); Rule 1.7(b) (prohibition of representation that may be materially limited by the lawyer's own interests); and Rules 1.8(a) and (f) (prohibition of business transactions with the client and prohibition from accepting compensation for representing a client from one other than the client).

First, it is the opinion of the Board that a referral fee creates a financial interest that may affect a lawyer's professional independence in representing his or her client, *i.e.*, the more referrals made to the specific financial services group, the more money the lawyer makes. As was recently stated in L.E.I. 2005-02 (Legal Funding Plans), "[i]f an attorney allows anything, including his or her self-interest, or the interest of a third party to interfere with his [or her] 'independent professional judgment', the lawyer is in violation of Rule 2.1." Rule 2.1 of the *West Virginia Rules of Professional Conduct* provides that "[i]n representing a client, a lawyer shall exercise independent professional judgment and render candid advice." In the instant situation, the lawyer would appear to be promoting his or her own self-interest by referring a client to a specific financial services provider so that the lawyer will receive the referral fee. This would be a violation of Rule 2.1.

In addition, this scenario also implicates Rule 1.7(b), which provides in pertinent part, that "[a] lawyer shall not represent a client if the representation of that client may be materially limited by the lawyer's responsibilities to another client or to a third person, or by the lawyer's own interests, unless (1) the lawyer reasonably believes the representation will not be adversely affected; and (2) the client consents after consultation . . . ." As was stated above, the lawyer's own interests are involved because he or she is receiving a fee to refer a client to a specific financial services provider. Furthermore, if the lawyer has entered into an agreement with the financial services provider, then the lawyer may feel that he or she is under an obligation to refer all such clients in need of financial services to that one financial services provider, regardless of the client's specific needs. The Board does not believe that a lawyer could be seen to objectively evaluate the situation when the lawyer's own financial interests are involved pursuant to his or her own agreement with a financial services provider for referrals in exchange for a fee. While the Board recognizes that Rule 1.7(b)(2) provides that the lawyer could continue with representation should the client consent after consultation, the lawyer should remember that both sections of 1.7(b) need to be met. This Board believes that in this situation, the lawyer cannot be seen to reasonably and objectively evaluate the situation when his or her own self-interest and/or financial interests are involved. Thus, even if all other conditions were met, the arrangement still has an appearance of impropriety.

Second, it is also the opinion of the Board that an agreement between a lawyer and a financial services provider for referrals in exchange for a referral fee paid to the lawyer

implicates Rules 1.8(a) and 1.8(f). Rule 1.8 (Conflict of interest: Prohibited transactions.) of the *West Virginia Rules of Professional Conduct* provides, in pertinent part, as follows:

> (a) A lawyer shall not enter into a business transaction with a client or knowingly acquire an ownership, possessory, security or other pecuniary interest adverse to a client unless:
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> (1) the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing to the client in a manner which can be reasonably understood by the client;
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> (2) the client is given a reasonable opportunity to seek the advice of independent counsel in the transaction; and
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> (3) the client consents in writing thereto.
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> (f) A lawyer shall not accept compensation for representing a client from one other than the client unless:
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> (1) the client consents after consultation;
>
> (2) there is no interference with the lawyer's independence of professional judgment or with the client-lawyer relationship; and
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> (3) information relating to representation of a client is protected as required by Rule 1.6.

As a general principal, all transactions between client and lawyer should be fair and reasonable to the client. In transactions wherein the lawyer knowingly has an ownership or other pecuniary interest adverse to the client, at a minimum, the same should be disclosed to the client, review by independent counsel should be conducted and the client should consent to the same in writing. Receipt of a referral fee or acquisition of a financial interest in a transaction involving the client, based upon an agreement with a financial services provider by a lawyer, is clearly adverse to the client's interest because there is the potential that the lawyer might not provide the client with meaningful and appropriate advice due to the

lawyer's own financial interest in the referral.[4] Furthermore, the conflict of interest is such that the Board believes it cannot be cured by full disclosure to the client, or by the client's consent to the arrangement.[5] Referral fees, whether they are called referral fees or "solicitor" fees, paid by a financial services provider to a lawyer can be regarded as payments to a lawyer for allowing that person or organization to make a profit from his or her client.[6]

The instant request contemplates that the lawyer and the financial services provider would enter into an agreement for the lawyer to provide a referral of his or her clients to a particular financial services provider in exchange for a referral fee. It is the opinion of the Board that this arrangement also runs afoul of Rule 1.8(f), as stated above. In referring clients to financial services providers, the Board considers the lawyer to be providing a legal service that may be expected by the client as part of the attorney-client relationship. Furthermore, the Board makes the assumption that clients view recommendations to other professionals by the lawyer as part of the representation being provided, and they expect that lawyers will act as fiduciaries in such matters.[7] Therefore, should the lawyer receive a referral fee from the financial services provider, then it is the opinion of this Board that the referral fee is indirectly providing compensation by one other than the client to the lawyer for his or her legal services.

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[4] *See*, New York State Ethics Opinion 682.

[5] "Moreover, in many instances the lawyer's affiliation with the investment advisor and the resultant client referrals could involve the lawyer in matters beyond his [or her] professional competence, and, indeed raises difficult questions regarding state and federal investment advisor registration and examination requirements .... Consequently, it would be difficult, if not impossible, for the lawyer to fully and fairly disclose to the client the consequences of pursuing the recommended course instead of other alternatives that the lawyer is unlikely to have evaluated or considered." Kentucky Ethics Opinion E-390 (1996).

[6] *Id.*

[7] *See*, New York State Ethics Opinion 682.

Conclusion

The Board agrees with the Professional Ethics Commission of the Maine Board of Overseers of the Bar, which stated:

> The Commission finds that the referral fee at issue here is inherently unfair and unreasonable to the client. [Footnote omitted.] The singular purpose and desire of this arrangement is to influence the lawyer to make recommendations to the lawyer's client for the benefit of an investment advisor who is paying the lawyer to do so, in stark contrast to the lawyer's being motivated by the best interests of the client. This arrangement is so adverse to the fiduciary relationship that is the foundation of the lawyer's responsibility to the client, that the Commission finds it to be fundamentally and objectively unfair and unreasonable to the client, ...

Maine Ethics Opinion No. 184 (2004).

Accordingly, the Board finds that it is ethically improper for a lawyer to accept a referral fee from a financial services provider. The referral fee creates a financial interest by the lawyer in the representation that affects a lawyer's professional independence in representing his or her client. Furthermore, the type of arrangement proposed in this request also requires an improper business relationship involving clients and non-lawyers that even full disclosure and consent from the client cannot cure.

APPROVED by the Lawyer Disciplinary Board on the17th day of November, 2006 and **ENTERED** this 29 day of December, 2006.

David A. Jividen, Chairperson
Lawyer Disciplinary Board