NEW HAMPSHIRE BAR ASSOCIATION
Ethics Committee Formal Opinion #1995/96-12
Referral Fees: When May They Be Paid and How May They Be Advertised
May 8, 1996

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RULE REFERENCES:
* 1.5(f)
* 7.2(c)
* 1.7(b)

SUBJECTS:
* Advertising and Solicitation
* Conflict of Interest
* Fees
* Referrals

ANNOTATIONS:

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QUESTIONS PRESENTED

May fees be paid to an attorney solely for the act of referring a client matter to another attorney?

Are advertisements by law firms stating that "Referral Fees Honored" unethical?

BRIEF ANSWER

An attorney may not pay another attorney a fee solely for that attorney's referral of a client matter. The rule requires that in order to earn a fee, an attorney must have active and material involvement in the client matter.

Under the circumstances, advertisements directed to other attorneys stating that referral fees are "honored" are not unethical. The preferred practice is to advertise that fee divisions or fee splitting may be considered.

DISCUSSION

The New Hampshire Supreme Court Professional Conduct Committee (PCC) has expressed concern over the practice of referral fees, particularly if the fee is paid solely for the act of one lawyer referring a client matter to another. Citing to Rule 1.5(f) governing the division of fees between lawyers and Rule 7.2(c) which prohibits a lawyer from giving anything of value to a person for recommending a lawyer's services, the PCC has asked the Bar Association's Ethics Committee whether fees for "pure referrals"; that is, fees paid solely for a referral and the rendering of no other services is prohibited. Moreover, to the extent that a referral under the conditions of Rule 1.5(f) occurs, the PCC has asked whether advertisements containing the language "Referral Fees Honored" is misleading, and therefore, barred.

BACKGROUND AND RULES

In 1993, this Committee examined the law surrounding referral fees. In an article by Peter C. Scott, Esquire, entitled "Fee Splitting Between Referring and Receiving Attorneys" (New Hampshire Law Weekly, July 9, 1993, Page 9), the Committee discussed the history and the rules involving fee divisions. First, the article examined the New Hampshire rule on the division of fees - which differs from the Model Rules of Professional Conduct. The New Hampshire rule (Rule 1.5(f)) provides that:

"A division of fee between lawyers who are not in the same firm may be made only if:

(1) the client consents to employment of the other lawyer after a full disclosure that a division of fees will be made;

(2) the division is made in reasonable proportion to the services performed or responsibility or risks assumed by each; and

(3) the total fee of the lawyers is reasonable.

New Hampshire Rule 1.5(f) (Emphasis supplied).

The Rule replaces the language used in the ABA Model Rule.

The Model Rule, in pertinent part, states that:

"A division of fee between lawyers who are not in the same firm may be made only if: (1) the division is in proportion to the services performed by each lawyer or, by written agreement with the client, each lawyer assumes joint responsibility for the representation ...."

Courts have stated that the ABA rule is clear - the rule does not countenance straightforward or "pure" referral fees, using the term from the Scott article. In Re Berl, 540 A.2d. 410, 413 (Del.Sup.Ct. 1988); see also Annotation, Validity and Enforceability of Referral Fee Agreements Between Attorneys, 28 ALR4th 665 (1984). The referring attorney must assume joint responsibility for the representation if the division of fees is not based upon the allocation of services rendered. ABA/BNA Lawyer's Manual on Professional Conduct, 41:709.

However, the Committee noted that the New Hampshire rule - which underwent changes before its final promulgation - is not so clear. The initial version of Rule 1.5(f)(2) stated that:

"A division of fee between lawyers who are not in the same firm may be made if:

(1) ...

(2) The division is made in proportion to the services performed or responsibility assumed by each;"

See Proposed Rule 1.5(f), 26 NHBJ 61, 78 (Winter 1985) (Emphasis added).

During the deliberative process, the term "reasonable" was inserted before "proportion" and the phrase "or risk" was added by the Supreme Court following the word "responsibility". While seemingly innocuous, the changes engendered such debate on the Committee that in 1993, no consensus could be reached over the propriety of "pure" referrals. At the time, some members argued that because the referring lawyer assumes the risk that the receiving attorney will negligently handle the referral, leaving the referring lawyer subject to a claim for negligent referral, then the mere referral without more may be compensated. Indeed, such claims have been recognized in other jurisdictions. Tormo v. Yormack, 398 F.Supp. 1159 (D.N.J. 1975) See also Malpractice Dangers in Tort Case Referrals, 24 Trial 62 (1988); ABA/BNA Lawyer's Manual on Professional Conduct, Section 301:1008. Other members, however, claimed that because the referring attorney would likely have an action against the receiving attorney if the referring attorney was found secondarily liable for the receiving attorney's negligence, then the referring attorney's risk is minimal, if not non-existent.

Because the Committee could not reach a consensus on the propriety of a "pure" referral fee, it opted to recommend only that the language of Rule 1.5(f) be modified to clear up the ambiguity. The Committee did, however, agree on other conclusions. Specifically, it agreed:

1. A lawyer should not receive a referral fee when the sole involvement of that lawyer in the case is the referral of the case to another lawyer due to the referring lawyer's conflict of interest.

2. A lawyer may divide fees with a disbarred or suspended attorney in proportion to the work performed by each attorney. The share of the disciplined attorney is limited to those services which he or she provided prior to the imposition of discipline.

3. A question exists as to whether a lawyer may share fees with an out-of-state lawyer not admitted to practice in New Hampshire on a pro hac vice or any other basis, to the extent that the out-of-state lawyer is considered a non-lawyer under the Rules.

ANALYSIS

As put by one treatise:

"Depending on one's philosophy of lawyering, payment of referral fees may be thought of either as an old and honorable tradition that helps bring about the best representation for the client, or as a chronic scourge of the profession that enriches lawyers for doing nothing." ABA/BNA Lawyer's Manual on Professional Conduct, Section 41:708.

The latter view has been summarized in the oft-cited case of Corti v. Fleisher, 93 Ill.App.3d. 517, 417 N.E.2d. 764 (Ill. App.Ct. 1981). In that case, the court stated:

"It is evident from this review that attorneys have long been ethically and legally prohibited from sharing with other members of the profession fees generated from the disposal of a legal matter when the only 'service' rendered by the claimant attorney is the referral of the case. Profiting from the solicitation of professional employment is injurious to the legal profession and to the public. As the various authorities reveal, this practice is injurious to the legal profession since the public loses confidence in those who treat clients as merchandise in a market place rather than the recipients of the attorney's skills and abilities. More importantly, the best interest of the clients are (sic) jeopardized by the arrangements when it becomes more profitable for attorneys to sell clients than to give them a legal service."
Corti v. Fleisher, 417 N.E.2d. at 775.

On the other hand, a California appeals court stated:

"The practice of forwarding fees among lawyers, part of our legal culture ..., remains with us even though the detrimental effect upon the client appears obvious .... The honoring of a referral fee is even more puzzling where the referring attorney is merely heeding the Rules of Professional Conduct in rejecting a case which he does not have the requisite skill or experience to handle competently .... Regardless of the logic of this argument, there is another point of view. If the ultimate goal is to assure the best possible representation for a client, a forwarding fee is an economic incentive for less capable lawyers to seek out experienced specialists to handle a case. Thus, with marketplace forces at work, the specialist develops a continuing source of business, the client is benefited and the conscientious, but less experienced lawyer is subsidized to competently handle the cases he retains and to assure his continued search for referral of complex cases to the best lawyers in particular fields."

Moran v. Harris, 130 Cal.App.3d. 872, 182 Cal.Rptr. 519 (Cal.App. 1982). See also Justice Richard Neely's arguments in a concurring opinion in the matter of Watson v. Pietranton, 364 S.E.2d. 812, 816-818 (W.Va.Sup.Ct.App. 1987).

In New Hampshire, a third view about "pure" referrals has arisen, having to do with the evolution of the language in the rule. Due to the lack of legislative history, no record or explanation exists for the change to the rule which permitted fee splitting based on "risks assumed". Stephen L. Tober, Esquire, who chaired the committee charged with reviewing and adapting the ABA Model Rules to New Hampshire practice, and several fellow committee members have expressed the belief that at no time were "pure" referral fees ever contemplated. Instead, they believe that the "risks assumed" language was added to ensure that fees need not be divided based on the proportionality of work by attorneys, so long as each attorney continued to remain responsible for the case. It was also added, they claim, to reflect situations where one attorney replaces another attorney in ongoing litigation, yet risks for the first attorney remain because that attorney sculpted and designed the strategy and claims in the case. In such an instance, they argue, there ought to be some freedom between past and present counsel to divide fees reasonably and equitably. On the other hand, former Supreme Court Associate Justice Charles

Douglas submitted a letter dated December 11, 1995, urging the Court to permit "pure" referral fees "so long as the fee is not greater than it otherwise would be, and is reasonable in terms of its arrangement". To that end, he urged deletion of NHRPC 1.5(f)(2) altogether. Thus, there is unpersuasive, if not conflicting evidence in the Court's file as to its intent.

After reviewing the soundness of all arguments, the Committee is of the opinion that "pure" referral fees are prohibited under the New Hampshire Rules of Professional Conduct. To that end, the Committee believes that the term "risks assumed" was added to allow fees to be divided based on the responsibility and risk assumed by each attorney resulting from active participation, either prior to or in concert with another attorney, in a client matter. We believe the Supreme Court was trying to protect several important interests. First, the Committee is in agreement with the court's logic in the Corti v. Fleisher case, cited above. Clients should not be treated as merchandise nor should a client's call for advice be treated as an economic commodity to be traded to the most financially remunerative referral attorney. This interest is protected by another of our rules prohibiting the giving of "anything of value" for recommending a lawyer's services. See NHRPC 7.2(c). Although concerns over champerty, barratry and maintenance - old English terms describing case brokering and lawsuit promotion - may seem arcane, in fact, case brokering for profit damages the image of the profession.

More importantly, the practice is beset by conflict of interest problems. The attorney in whom a client places ultimate trust may be sorely tempted to refer that client to the referral attorney who pays the highest referral fee, even if the referring attorney is not the best attorney for that client's case. Attorneys should choose competent referral counsel without interference that might result due to the attorney's own financial interests. Referrals motivated by profit, rather than careful evaluation of the referring attorney's experience, knowledge, temperament, competence and other important factors is violative of NHRPC 1.7(b).

Finally, it does not take a great deal of imagination to posit that without the obligation to pay a "pure" referral fee, an attorney may deliver legal services on a basis where the client is able to retain more of his or her recovery. While it is true that NHRPC 1.5(f)(3) requires that the total fee of the lawyers must be reasonable, if "pure" referral fees are eliminated as an institutional expense that the referring lawyer must cover in calculating a fee agreement, the fees charged to a client may diminish. Put differently, a prohibition against such fees eliminates another cost of business which the client ultimately pays. See Krajewski v. Klawon, 84 Mich.App. 532, 270 NW.2d. 9 (1978).

The Committee is well aware of the trend among some states to permit "pure" referrals. See Protection of the Public Through Amendment of the Rule on Referral Fees, 36 NHBJ 55 (1995). It is also aware from the contacts by bar members regarding this opinion, that the practice exists among New Hampshire lawyers. Nevertheless, given concerns about the impact of such fees upon the image of the profession, the dangerous conflicts of interest that are created and the effect on the cost of the delivery of legal services, the Committee believes that the rule prohibits the practice unless and until the New Hampshire Supreme Court allows the same.

Fee division or fee splitting remains permissible, subject to a "proportionality" rule, in three situations: where there are (i) services performed by each attorney or firm, (ii) responsibilities retained or assumed by each attorney or firm, or (iii) risks retained or assumed by each attorney or firm. As previously stated, the concept of risk retention or assumption means the risk assumed by an attorney resulting from active and material participation in a client matter, either prior to or in concert with another attorney to whom the matter is referred. This rule means that as services, responsibilities or risks performed or retained by the referring attorney decline on a relative basis, the amount or percentage of the fee that may be permissibly divided or split and given to the referring attorney must also decline.

This analytical model logically gives rise to a sliding scale of divisible fees, depending on the degree to which the referring attorney is involved in the case, either at the outset or throughout the matter. It is straight forward to justify a precisely equal division of a fee where each lawyer performs fifty percent of the work. Even where the referring attorney does not expect to perform 50% of the work, appropriate fee allocations could be agreed to in advance based on his/her expected percentage of the total work performed. In the alternative, a referring attorney may negotiate for a proportionate fee based on the "responsibility prong" of Rule 1.5(f)(2), even if he or she performs only a small percentage of the trial preparation and in-court work. It may be appropriate for him or her to receive a fee division that is more than nominal, if for example, he or she has performed case evaluation work at the outset and remains jointly responsible for strategic and tactical decisions and for settlement evaluation and recommendations.

On the other hand, if the referring attorney does not have such an active and material involvement with the case and bears no risk other than the reasonableness of his or her referral, a reasonable fee would have to be limited to a much more

nominal amount. Even under this example, in order to earn any fee, the attorney must have conducted a thorough client intake interview, undertaken an evaluation of the nature and scope of the case and based on the evaluation, fully informed the client about the advantages of a referral to that client. The attorney must make a thoughtful referral of the client to another attorney or firm based on the nature of the case, the issues raised by the case, the receiving attorney's or firm's experience, skills, reputation and ability, the goals and personality of the client, the circumstances and limitations faced by the client and other issues. In this way, it may be said that there was some active or material involvement in the client matter.

ADVERTISING

The second issue presented to the Committee is whether advertisements proclaiming that referral fees are honored are violative of the Rules of Professional Conduct. NHRPC 7.2(c) provides that "a lawyer shall not give anything of value to a person for recommending the lawyer's services ...." It may be argued that fee divisions or fee splitting between attorneys based on one attorney's referral and subsequent participation in a case is, in part, a form of compensation for recommending a fellow attorney. However, Rule 7.2(c) is not intended to supplant legitimate fee sharing under Rule 1.5(f), and thus, we do not interpret the rule to prohibit the advertisement of fee divisions. Indeed, an attorney who divides fees with another attorney based on the "reasonable proportion of services performed or responsibility or risks assumed" is not receiving a fee simply for a referral. The primary reason for the payment of a fee is to compensate fairly an attorney for his or her participation in the case.

This leads to a second advertising concern: Whether it is ethical to identify fees as "referral fees", when a more accurate description might be "fee splitting" or "fee division". NHRPC 7.1(a) states that:

"A lawyer shall not make a false or misleading communication about the lawyer or the lawyer's services. A communication is false or misleading if it ... contains a material misrepresentation of fact or law, or omits a fact necessary to make the statement, considered in light of all circumstances, not materially misleading ...."

At best, the label "referral fees" is potentially misleading. Yet, as noted by several attorneys providing responses to this Committee's solicitation, the advertisements are directed to other attorneys, and not the public at large. There is, in fact, authority for the proposition that solicitation letters between lawyers are not scrutinized with the same rigor as solicitations to a potential client. See e.g. ABA Committee on Ethics and Professional Responsibility Informal Op. 84-1504 (1984) and citations therein. See also Wehringer's Case, 130 NH 707, 720 (1988). Some firms stated that they require that the referring attorney remain involved in the case and assume some agreed-upon responsibility for representation, in order for fees to be divided. All respondents implied or stated that the fee arrangements were reduced to writing. Thus, it will become clear as the fee agreement is negotiated that the fees are not "pure" referral fees, paid solely for the purpose of referral, but true fee splitting and fee division anticipated under Rule 1.5(f). In turn, this must be disclosed to and approved by the client. NHRPC 1.5(f)(1). Therefore, while the term "referral fee" may be potentially misleading to a layperson, under the circumstances described above, the advertising is not inherently misleading. It is also noted that potentially misleading advertisements may not be constitutionally banned. In Re RMJ, 455 U.S. 191 (1982). The better practice, however, is to refer to such fees as "fee divisions" or "fee splitting".

CONCLUSION

In conclusion, this Committee finds that "pure" referral fees - fees paid solely for the act of one lawyer referring the case to another - are prohibited under the New Hampshire Rules of Professional Conduct. This Committee also finds that advertisements proclaiming that referral fees are honored are not violative of the advertising prohibitions in the Rules, assuming that the referral fees in question are fees paid in conformance with this Committee's interpretation of Rule 1.5(f).