Referral Fees
Practical Implications of Professional Rule of Conduct 1.5(f)

By the NHBA Ethics Committee
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I. INTRODUCTION

On May 16, 1996, the New Hampshire Bar Association Ethics Committee (“Ethics Committee”) issued a formal opinion addressing the question whether fees may be paid to an attorney solely for the act of referring a client matter to another attorney. EO 1995/96-12 (May 16, 1996). The Ethics Committee responded “no,” holding that an attorney may not pay another attorney a fee solely for that attorney’s referral of a client matter, but rather, in order to earn a fee, an attorney must have active and material involvement in the matter. The purpose of this article is to offer guidance to attorneys to comply with the Opinion and Rule of Professional Conduct 1.5(f).

The opinion is based on an analysis and interpretation of Rule 1.5(f), which states as follows:

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.

The Rule, as interpreted by the Ethics Committee, prohibits so-called referral fees, which are fees paid for the simple act of referring a client matter. Rather, fee splitting or fee division among lawyers who are not members of the same firm can occur only under the three following circumstances, subject to the requirement of proportionality:

(1) to the extent actual services are performed by each attorney or firm; or
(2) to the extent responsibilities are retained or assumed by each attorney or firm; or
(3) to the extent risks are retained or assumed by each attorney or firm.

The “risks” or “responsibilities” assumed must result from active and material participation in a client matter, either prior to or in concert with another attorney to whom the matter is referred. EO 1995/96-12, at 5. The division of fees must be made in reasonable proportion to the services performed or risks or responsibilities assumed. Rule 1.5(f)(2). Therefore, when the services performed or the risks or responsibilities assumed decline in proportion to the entire representation of the client matter, the division of fees must decline proportionally. EO 1995/96-12, at 5.

There has been little guidance to attorneys concerning the application of Rule 1.5(f). As stated in the Ethics Committee opinion, the New Hampshire version of Rule 1.5(f) is different from the ABA Model Rule, which does not permit splitting unless the referring attorney assumes joint responsibility for the representation or receives a fee in proportion to the services rendered. EO 1995/96-12, at 2 (citing ABA Model Rule 1.5(f)). The New Hampshire Rule 1.5(f) is also different from states which specifically allow “pure” referral fees. See, e.g., Moran v. Harris, 182 Cal. Rptr. 519 (Cal. App. 1982). (California Supreme Court approved 1979 amendment to rule deleting limitation of fee division to services performed or responsibilities assumed, thereby condoning pure referral or forwarding fee arrangements). New Hampshire Rule 1.5(f) permits a fee division in proportion to the services performed or the risk or responsibility an attorney assumes in the representation of the client.

II. RULE 1.5(f)(1).

First, there can be no question under Rule 1.5(f)(1) that a fee division among lawyers who are not members of the same firm must be disclosed fully to the client, and the client must consent to the employment of the other lawyer. While there is no discussion in Rule 1.5(f)(1) of the meaning of “full disclosure,” a review of Rule 1.7(b)(2) supports an interpretation that the disclosure include knowledge of the proportional distribution of the services performed or risks or responsibilities assumed as well as knowledge of the proportional fee distribution. Rule 1.7(b)(2) provides that a lawyer shall not represent a client if the representation may be materially limited by the lawyer’s own interests, unless the “client consents after consultation and with knowledge of the consequences . . . .”
This language indicates that mere disclosure of the fact that a fee division will occur is not sufficient. The client must have actual knowledge of the consequences of the shared fee and the shared tasks or shared risks or responsibilities of the attorneys. A lawyer who refers a client to another lawyer with the expectation of sharing in the fee, as well as the services or risks or responsibilities, has a financial interest in the representation. The New Hampshire Comments to Rule 1.7 explain that Rule 1.7(b)(2) was drafted so that the client will have actual knowledge of the consequences which will occur in a situation where a lawyer’s own interest is potentially adverse to that of his client. See New Hampshire Comments to Rule 1.7.

In addition, Rule 1.4(b) requires an attorney to inform a client of the legal and practical aspects of a matter, as well as the alternative courses of action, such that the client may make informed decisions regarding the representation. As such, a lawyer has a duty to keep his client fully informed of the proportional division of fees, and the proportional performance of services or shared risks or responsibilities, so that the client may make an informed decision whether to consent to the employment of another attorney and the fee division. See Schniederjon v. Krupa, 514 N.E.2d 1200, 1202 (Ill. App. 1987); cert. denied 520 N.E.2d 393 (Ill. 1988) (stating an attorney owes a fiduciary duty to a client to specifically disclose the fee division made with another attorney, and citing Corti v. Fleisher, 417 N.E.2d 764, 768 (Ill. App. 1981)).

Finally, Rule 1.5(f)(1) does not discuss the manner in which a full disclosure of the fee division should be made to the client. To help prevent any confusion or disputes concerning the fee division by the client, either attorney, or the Professional Conduct Committee, the Ethics Committee highly recommends that the fee disclosure be in writing.

III. RULE 1.5(f)(2)

Provided that full disclosure of a fee division is made to a client as addressed above, and the client consents to the employment of the other lawyer, the next issue to address is what services must be performed or what risks or responsibilities assumed to justify a fee division. Rule 1.5(f)(2) states that the division must be made in “reasonable proportion to the services performed or responsibilities or risks assumed by each.” (Emphasis added). Consequently, an attorney at the least must either perform services for the client, or assume risks or responsibilities in the representation, to satisfy the second prong of Rule 1.5.

A. Services Performed.

The services a lawyer can perform to meet Rule 1.5(f)(2) are not limited by the rule and assuredly include the wide variety of legal work a lawyer regularly provides a client. For instance, but not by way of exclusion, investigating the client matter by reviewing documents or interviewing witnesses, drafting a writ, preparing interrogatories or other legal documents, conducting depositions, researching legal issues and developing the strategy of a client’s case, would certainly qualify as “services performed.” See, e.g., Schniederjon v. Krupa, 474 N.E.2d 804, 809 (Ill. Ap. 1985).

An example of a fee division for services performed that would be acceptable under Rule 1.5(f)(2) is as follows. A general practitioner has an initial consultation with a client who has a potential medical malpractice claim. Beyond the initial consultation, the lawyer conducts a preliminary investigation and analysis of the facts and issues of the case and conducts some research into the law. The lawyer then concludes the client’s needs could be better met by a more experienced medical malpractice attorney, and after fully disclosing the benefits of the referral and the fee division in writing to the client, refers the matter to the other attorney. Because the referring lawyer performed services for the client, the lawyer may justify a fee division that is reasonably proportional to the services he performed under Rule 1.5(f)(2). This can be done either through straight billable time or a proportional contingency fee.

Another scenario in which two lawyers may justify splitting a fee under Rule 1.5(f)(2) is when one lawyer conducts the pretrial preparation of a case, and the second lawyer represents the client at trial. Because both attorneys have performed services for the client, a fee division that is reasonably proportional to the services rendered is justified under Rule 1.5(f)(2).

B. Responsibilities or Risks Assumed.

Rule 1.5(f)(2) does not explain the meaning of “responsibility or risks assumed” by each lawyer. In the opinion of the Ethics Committee, however, a “pure” referral does not give rise to the assumption, without more, of a compensable responsibility or risk. The Ethics Committee is aware that other jurisdictions have held a referring attorney liable for the legal malpractice of the attorney to whom the case was referred (“receiving attorney”). Tormo v. Yormack, 398 F.Supp. 1159 (D.N.J. 1975); NY County Lawyers’ Ass. Comm. on Prof. Ethics, Opinion 715 (1996). The Tormo case, however, involved egregious facts whereby the referring attorney did no investigation into the competence of out-of-state receiving counsel, who was at the time of the referral under indictment for insurance fraud, and who subsequently converted the client’s
settlement proceeds. Id. at 1166. More importantly, it is rather odd logic, and seemingly poor public policy, that an attorney can justify a “pure” referral fee on the premise that the attorney should be paid for taking the risk that the receiving attorney is incompetent to handle the client matter. The “risks” contemplated in Rule 1.5(f)(2) relate instead to the economic risk borne by the attorney (with respect to out-of-pocket expenses, unpaid legal fees, or the risks inherent in contingency fee cases) in the success of the case, and not the risk that the attorney will handle the client’s matter negligently.

A referring attorney who has performed services on a case prior to the referral, such as drafting a writ or developing a case strategy, also has assumed responsibility for the case, or assumed (at least partially) the risk of failure or success, even if another attorney takes over the representation of the client.

The key to the “responsibility or risks assumed” language is the interpretation by the Ethics Committee that Rule 1.5(f)(2) requires an attorney’s active participation in the representation of the client in order to justify a fee division. Moreover, the Ethics Committee is now of the opinion that the attorney must agree and disclose, preferably in writing, to participating counsel and the client those responsibilities and/or risks which the attorney is assuming. Such a disclosure is consistent with the principles in Rule 1.4 that “a client has a right to be informed in most cases of the nature of the legal problem, the consequences of choices to be made and legitimate alternatives available to address the client’s problem.” See New Hampshire Comments to Rule 1.4. As stated in the Ethics Committee Opinion, the “risk assumed” language was added to Rule 1.5(f)(2) “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.” EO 1995/96-12, at 5 (emphasis added). The Ethics Committee stated that if the referring attorney has limited active involvement in the case and bears no risk other than for the reasonableness of his referral, the reasonable fee would have to be limited to a nominal amount. Id. The Ethics Committee also set forth the requirement that “in order to earn any fee, the attorney must have conducted a thorough client interview, undertaken an evaluation of the nature and scope of the case and based on that evaluation, fully informed the client about the advantages of a referral to that client.” Id. at 6. In addition, “[t]he 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.” Id. Only when the attorney has conducted a client interview such as described above, along with an analysis of the case, can the attorney establish the “active or material involvement in the client matter” to justify a fee division under Rule 1.5(f)(2).

As such, at a minimum, to qualify under the “active participation” necessary for the “responsibility or risks assumed” language of 1.5(f)(2), a referring attorney must conduct the above referenced client interview evaluating the needs of the client and the potential issues raised in the case (see above description) and, after discussing the benefit of a referral with the client, must make a “thoughtful” referral of the case to another attorney or firm (see description above). Thereafter, if the referring attorney has no other active involvement in the client’s representation, the attorney must continue to assume responsibility for the case in order to justify a fee division. Because in such a “pure” referral matter, the referring attorney’s active involvement is minimal, the Ethics Committee has said the fee shared should be nominal.

On the other hand, if the referring attorney has drafted the writ, conducted an investigation of the case, developed a case strategy, or has performed some other work for which the attorney shares a risk of professional liability with the receiving attorney, Rule 1.5(f)(2) is satisfied and the proportional fee division may justifiably be higher.

Under the “active participation” rule, there may be no satisfaction of Rule 1.5(f)(2) in the scenario of one attorney performing pretrial work and a second attorney taking the case for trial purposes, if the case settles prior to trial as the result solely of the efforts of the first attorney and the trial attorney has performed no work. The second “trial” attorney will have to demonstrate some work performed for the client, or that the attorney actually assumed responsibility for the outcome of the matter before a fee division can be justified.

If the second “trial attorney’s” work is limited to reviewing and “signing off” on a settlement, her portion of the total fee would necessarily be lower than if she had actively participated in the settlement strategy and negotiations.

Similarly, an attorney who is approached by a client concerning, for example, a specialized tax matter, must conduct the above described client interview and case and referral analysis, and must assume responsibility for the case with the tax specialist to satisfy the minimal “active participation” and “responsibility assumed” requirements of Rule 1.5(f)(2). In such a fee division, the lawyer’s proportional share of the fee should reflect his minimal active involvement.

In addition to active participation, both participating counsel and the client should be advised of and agree upon the responsibilities or risks which the referring attorney is retaining, pursuant to a written agreement. An understanding and disclosure that the referring attorney is fully responsible for all aspects of the case, including the timely and proper filing of
pleadings or other documentary material, adequate preparation for a hearing, meeting or trial, and the like, justifies an equal division of the fee. Assumption and disclosure of more limited responsibility or risk in which, for example, the referring attorney only assumes responsibility for making a reasonable referral after active participation, but does not assume responsibility or risk that the performance of the receiving attorney in the referred case will be reasonable, justifies a smaller fee division. Similarly, an agreement to engage an attorney with whom fees will be divided to work on a particular time-consuming strategy or type of legal work for the client, coupled with an assumption of risk that the work will produce certain results or be outcome-determinative, may justify a more significant fee division. In short, Rule 1.5(f)(2) allows a referring attorney to earn a larger or smaller proportion of the fee for a referral depending upon (1) the referring attorney’s active participation in the case, and (2) his/her disclosed willingness to assume identified responsibility and/or risk beyond the referral itself.

IV. RULE 1.5(f)(3)

The final prong of Rule 1.5(f) is that the total fee charged to the client by the lawyers is reasonable. Rule 1.5(f)(3). The reasonableness of attorney’s fees is also address in Rule 1.5(a)-(e). In the context of a fee sharing agreement, the total fee charged to the client must be reasonable considering the services provided or the responsibility or risks assumed by each attorney. New Hampshire maintains a rule that prohibits clearly excessive fees. See New Hampshire Comments to Rule 1.5. Rule 1.5(f) does not specify that the client receive regular statements concerning the fees for the services performed, but such practice may help prevent fee disputes. In addition, full disclosure of the estimate of the fees, hourly rate, cost of the case and other expenses of both attorneys or firms is recommended prior to a referral of a client that will result in a fee division. As discussed above, such disclosure is also necessary under Rule 1.5(f)(1).

V. CONCLUSION

In summary, “pure” referral fees are not acceptable in New Hampshire, and all prongs of Rule 1.5(f) must be satisfied before a fee division is acceptable. Full disclosure of the fee division, including the proportional share of services performed or responsibility or risks assumed and the proportional fee, must be made to the client. After such full disclosure, the client must consent to the employment of the other attorney. Before any fee division can occur, both attorneys must have active participation in the case. The attorneys must each have performed services for the client, or in conjunction with active participation in the case, have assumed responsibility for or risks in the case. The fee division must be made in reasonable proportion to the services performed or the responsibility or risks assumed by each attorney. The ultimate fee to the client must be reasonable.

It is recommended that the full disclosure to the client be made in writing. A fee agreement setting forth the proportional responsibility or risks assumed in the case and the proportional fee divisions could dispel future questions or confusion concerning the relative roles and fees of the attorneys. Finally, full disclosure of the estimated cost of representation and the hourly fees of both attorneys or firms, as well as regular invoices to the client, may prevent any fee disputes or questions concerning whether full disclosure was made.1

1 This article has been reviewed and approved by a majority of the members of the Ethics Committee. However, as a Practical Ethics Article, it does not have the same weight of authority or precedential value as a Formal or Advisory Ethics Opinion. New Hampshire Bar Association Ethics Committee Procedural Rule