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Ethical, Legal and Practical Implications of Attorney Referral Fees

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Under what circumstances may an attorney ethically pay or receive a referral fee under the Code of Professional Responsibility? Moreover, is the penalty for non-compliance a disciplinary proceeding, an action for legal malpractice, forfeiture of the fee, or some combination of the above?

The Lawyers' Code of Professional Responsibility prohibits sharing fees with non-lawyers, and circumscribes the division of fees with an attorney who is not a partner or associate in the same firm.

According to DR 2-107 of the code:
A lawyer shall not divide a fee for legal services with another lawyer who is not a partner in or associate of the lawyer's law firm, unless:
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 in proportion to the services performed by each lawyer or, by a writing given the client, each lawyer assumes joint responsibility for the representation.
3. The total fee of the lawyers does not exceed reasonable compensation for all legal services they rendered the client.

The prohibition of a finder's fee was originally intended "to keep the profession of law from becoming an ordinary business." The rationale for the prohibition was pithily summarized in Nicholson v. Mason & Cohen: "The aims of the rule against fee splitting are to keep the profession of law, an element of which is the disinterested service of the administration of justice, from deteriorating into a money-grubbing trade, to prevent mercenary trafficking in lawsuits, to inhibit lawyers from dredging up meritless litigation and to protect clients against exploitation."

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Interviewing the client, discussing the matter with firm attorneys and attending a meeting with the client.

Inasmuch as the plaintiff attorney performed work on the case and served as liaison with the client, the Court of Appeals held he was entitled to his share of the fee as allocated in the parties' agreement, reasoning "The courts will not inquire into the precise worth of the services performed by the parties as long as each party actually contributed to the legal work and there is no claim that either refused to contribute more substantially."

The court in Krag v. Offerman, Fallon, Mahoney & Cassano, upheld an oral fee-splitting agreement in favor of an attorney who did no work on a personal injury action arising out of an automobile accident, but rather successfully obtained the dismissal of a workers' compensation action arising out of the same accident, thereby making the personal injury case possible by eliminating the workers' compensation defense. As a result, the plaintiff's attorney was entitled to a portion of the $600,000 contingent legal fee paid to the defendant's law firm for its work on the personal injury action.

Quantum Meruit Theory

Although most courts have refused to look behind the language of fee-splitting agreements to ascertain the precise amount of work performed by referring counsel, there is some authority to the contrary.

For example, the New York State Bar Association Committee on Professional Ethics has acknowledged that: "Although it is not unethical for the lawyers to agree in advance on a proposed fee split," at the conclusion of the matter, the relative proportions should be re-examined and adjusted in the event "the services actually performed and responsibility assumed by the forwarding attorney and the forwardee are grossly disproportionate to the division of fees agreed upon at the outset."

The Appellate Division recently refused to enforce a written agreement to divide fees between two attorneys because it would have been grossly disproportionate to their actual
work on the file. In Ford v. Albany Medical Center, the court found the conduct of the plaintiff's first attorney, who met repeatedly with his client, reviewed medical records and obtained an expert opinion that a viable medical malpractice case existed, was insufficient to enforce a written agreement pursuant to which that attorney would receive one-third of all attorneys' fees in the case.

Since enforcement of the agreement would have violated DR 2-107, the initial attorney's fee was reduced on a quantum meruit basis to 3 percent of the total fee. It remains to be seen whether Ford represents a mere aberration or the winds of change in the area of referral fees.

Disciplinary Proceedings

There has been a paucity of reported disciplinary proceedings for violations of DR 2-107. Even in those cases in which a court has found a violation, there has been, as a rule, no referral to the Grievance Committee, perhaps upon the unstated assumption that denial of the attorney's fee is punishment enough.

Among the few recent reported decisions of attorney discipline is a letter of admonition to an attorney who agreed to split a fee with another lawyer without the client's consent, and a private letter of caution issued to two attorneys who agreed to divide legal fees without regard to services performed or the level of responsibility assumed by each.

In 1997, an attorney was publicly censured by the Appellate Division for paying a referral fee to another attorney who did not work on a matter, but that was only one of several charges of misconduct in that case, including improper disbursement of escrow funds.

Other Pitfalls

In addition to the threat of disciplinary proceedings or forfeiture of the fee, a referring attorney should be mindful of the possibility of an action for legal malpractice in the event of alleged mishandling of the case.

Generally speaking, a lawyer who refers a case to another attorney is not responsible for the latter's malpractice, provided the referral itself was not negligent. The early case of Wildermann v. Wachtel, directed a verdict in a legal malpractice case in favor of a New York lawyer who had referred a collection matter to a Pennsylvania attorney. The latter negligently failed to file a lis pendens, resulting in an inability to collect on the client's claim. Since there was no claim that selection of the Pennsylvania lawyer had itself been negligent, the court rejected the malpractice claim against New York counsel, reasoning, "A lawyer should not be held to a stricter rule in foreign matters than the exercise of due care in recommending a foreign attorney."

Although Wildermann was a pre-code case, subsequent decisions have tended to tread lightly in the area of attorney liability for negligent referral or supervision. Moreover, those decisions have tended to equate referral to a specialist with referral to an out-of-state practitioner.

Joint Responsibility

In 1996, the New York County Lawyers' Association Committee on Professional Ethics interpreted DR 2-107 to imply financial responsibility on the part of referring counsel who participates in a referral fee. According to NYCLA Ethics Opinion 715, although referring counsel has no obligation to supervise the work of a specialist, she should be prepared to indemnify the client for the former's malpractice because, in the view of the committee, "Generally, an agreement among attorneys to divide fees will be honored, provided that referring counsel is able to establish he has done some work on the case ..."

"Joint responsibility is synonymous with joint and several liability."

Interestingly, NYCLA Ethics Opinion 715 suggests that referring counsel ethically may extract an indemnity agreement from receiving counsel.

While, as mentioned, the New York courts have been reluctant to impose liability on referring counsel for the malpractice of receiving counsel, an additional level of caution should be exercised when dealing with out-of-state referrals.

For example, a New York lawyer who referred a negligence case to a New Jersey practitioner who subsequently absconded with client funds was denied summary judgment in Tormo v. Vormark, a federal case applying New Jersey law. In that case, the New York attorney was unaware his New Jersey counterpart had been indicted for fraud. The former's representations to the client that his indicted colleague was "a good, well-qualified attorney," along with allegedly false representations about the status of the case in New Jersey, were sufficient to give rise to an action for professional liability, notwithstanding the fact he had not agreed to participate in the fee.

A 1997 Florida case, Norris v. Silver, upheld an action for legal malpractice against a Florida attorney who referred Illinois counsel a personal injury case arising out of an Illinois accident. Although there was no written agreement between the two attorneys dividing their fees or assuming joint responsibility for the representation, the Florida court held that an agreement to share fees could be inferred from the past course of dealing between them. The court concluded that an action for legal malpractice could arise from the Florida attorney's failure to enter into a written agreement accepting responsibility for the representation.

Conclusion

Generally, an agreement among attorneys to divide fees will be honored, provided that referring counsel is able to establish he has done some work on the case and he has not refused to contribute more significantly. However, a court may choose to look beneath the surface of a referral agreement and reduce the fees on a quantum meruit basis. The threat of a formal disciplinary proceeding is remote, at least absent other misconduct by the respondent attorney. Of course, the risk of professional liability should be kept in mind, particularly in the case of an out-of-state referral.

(1) DR 2-107, 21 N.Y.C.R.R. 1200:12[a].
(4) Simon's New York Code of Professional Responsibility Annotated (West 2002) p. 241. (The phrase "some work" was apparently coined by Professor Simon.)
(6) 85 N.Y.S.2d at 556, 626 N.Y.S.2d at 985 (citations omitted).
(7) 714 A.D.2d 889, 634 N.Y.S.2d 653 (3d Dep't 1995).
(9) 283 A.D.2d 843, 724 N.Y.S.2d 795 (3d Dep't 2001).
(12) In re Allan Kuklinski, 120 A.D.2d 104, 504 N.Y.S.2d 399 (2d Dep't 1989).
(14) 149 Misc. at 624-25, 267 N.Y.S. at 842.
(16) 67 Misc. 2d 248, 376 N.Y.S.2d 430 (1st Dep't 1972).
(18) 1596 WL 592658 at *3
(20) 398 F. Supp. at 1166.