

# NYSBA OK's Reciprocal Referral Arrangements with Brokers

BY LAZAR EMANUEL

In Opinion 765 (7/22/03), the Committee on Professional Ethics of the State Bar considered in detail the application of DR 1-107(C), adopted by the Appellate Divisions on July 23, 2001. The Committee considered the following two questions:

1. May a lawyer enter into a contractual relationship with an insurance or securities agent or broker which involves reciprocal referrals?
2. Would the answer be the same if the parties entered into a reciprocal referral agreement instead of a contractual relationship?

Both questions require interpretation of DR 1-107. The Committee acknowledged that this was its first effort to deal at length with the new rule. The Committee's analysis required focus on two provisions of DR 1-107. DR 1-107(A) permits a lawyer to enter into and maintain "a contractual relationship with a non-legal professional or non-legal professional services firm for the purpose of offering to the public, on a systematic and continuing basis, legal services...as well as other non-legal professional services."

The contractual relationships contemplated by DR 1-107(A) - usually referred to as multi-disciplinary practice - bear a number of conditions and restrictions. As described by the Committee:

Among other things, the rule requires a lawyer to make certain specified disclosures to clients (including a prescribed "Statement of Client's Rights in Cooperative Business Arrangements") and limits the professions with which lawyers can so contract to those professions on a list designated by the Appellate Divisions. The rule also sets forth in DR 1-107(B), the requirements for a profession to be included on the Appellate Division list (i.e., Bachelor's Degree, licensing, and a comparable ethical code). As of now the list includes only (1) architects, (2) certified public accountants, (3) professional engineers, (4) land surveyors, and (5) certified social workers.

Under DR 1-107(D), a contractual relationship between lawyer and nonlawyer satisfying the requirements of DR 1-107(A) permits the parties to the relationship to allocate costs and expenses between themselves, provided the allocation reasonably reflects their pro-rata share of costs.

DR 1-107(C) carves out an exception to the requirements of DR 1-107(A). The exception is described as "relationships consisting solely of nonexclusive reciprocal referral agreements or understandings" between a lawyer and a nonlegal professional. Relationships under DR 1-107(C) are not limited to professions on the Appellate Division approved list. But they may not be exclusive and they may not involve any sharing of costs or expenses.

### **Prohibited Referral Fees & DR 1-107(C) Arrangements**

Non-exclusive relationships under DR 1-107(C) must be construed under the provisions of DR 2-103(B), which prohibits compensation, or exchange of anything of value, for a lawyer referral. The Committee noted that DR 2-203(B) excepts from its application contractual relationships under DR 1-107(A), providing for legal and other services "on a systematic and continuing basis," provided, however, that referrals under these relationships "shall not otherwise include any monetary or other tangible consideration or reward for such, or the sharing of legal fees..."

The Committee acknowledged that the State Bar had never met squarely the question whether the very nature of an informal non-exclusive reciprocal referral relationship between lawyer and non-lawyer constitutes "compensation" or the "giving of value." The Committee noted that a Nassau County ethics opinion issued prior to the adoption of DR 1-107 had concluded that reciprocal referral arrangements were prohibited. But the Committee rejected the reasoning of that opinion, especially when viewed under the language of DR 1-107. For example, if DR 2-203(B) were applied strictly, "a nonexclusive agreement with an accountant to provide mutual referrals would be barred as the giving of value, but if the arrangement included some other element - such as shared expenses or joint advertising - it would be permitted."

Further, the language and history of DR 1-107 do not suggest that informal non-exclusive reciprocal referral arrangements violate the spirit or intent of DR 2-203(B). The distinction between the terms "contractual relationships" under DR 1-107(A) and "agreements or understandings" under DR 1-107(C) suggests that the drafters considered

DR 1-107(C) "agreements or understandings" of limited value to the parties. The special committee of the State Bar which recommended the adoption of DR 1-107 found that nonexclusive reciprocal referral arrangements were not in themselves particularly dangerous.

While some might argue that such arrangements fall within the letter of the ethical prohibitions, they are not pernicious in nature because of the responsibility of each of the allies to utilize its best judgment for its clients in selecting the most appropriate 'referee.'

Both the MacCrate Report and recent changes in the ABA Model Rules confirm the low level of professional concern about nonexclusive reciprocal referral arrangements. Thus, ABA Model Rule 7.2(b)(4) now provides:

A lawyer shall not give anything of value to a person for recommending the lawyer's services except that a lawyer may

(4) refer clients to another lawyer or a nonlawyer professional pursuant to an agreement not

otherwise prohibited under these Rules that provides for the other person to refer clients or customers to the lawyer, if

(i) the reciprocal referral agreement is not exclusive, and

(ii) (ii) the client is informed of the existence and nature of the agreement.

The Committee concluded that it would be inconsistent with the purposes and intent of DR 1-107 to prohibit nonexclusive reciprocal referral agreements on the theory that they constituted an impermissible exchange of compensation or benefits, especially as applied to the five professions on the approved Appellate Division list.

### **Not Limited To Professions On List**

The Committee recognized that securities and insurance brokers and agents are not on the approved list required for DR 1-107(A) "contractual" relationships. "There is, however, no textual basis for restricting nonexclusive reciprocal referral arrangements to the listed professions." On the contrary, the concept of a restricted list occurs only in DR 1-107(A), which concerns and anticipates more complicated and involved relationships than "naked" mutual referral arrangements. Nor does sound policy require limiting DR 1-107(C) arrangements to specified professions.

Persons seeking legal help commonly need assistance from a far broader set of service providers in resolving their problem: estate planning clients frequently need insurance and investment advice; real estate clients often need real estate and mortgage brokers and title services. If lawyers at least in some circumstances may refer clients to entities providing these services that are affiliated with the lawyer, and vice versa, as we opined in N.Y. State 753, it is difficult to see why other lawyers cannot likewise choose a reputable provider with which they can exchange referrals. This is not the joint provision of services under common advertising or a common roof, which implicates the concerns of confidentiality, improper influence and conflicts that motivated the restrictions in DR 1-107(A) and (B).

The Committee concluded that nonexclusive mutual referral arrangements between a lawyer and an insurance agent or broker or a securities broker are permitted under DR 1-107(C) and DR 2-103(B)(1). Both securities brokers and insurance agents are educated services often relied upon by lawyers. However, the relationship must be maintained as a "relatively loose reciprocal referral arrangement" and may not include joint advertising or the sharing of costs. These are reserved to the professions on the Appellate Division list.

Further, the lawyer must verify the competence of the non-legal service provider to render the services needed by the client. And a referral should be made by the lawyer only when the client requests it or when the lawyer deems it necessary in the interests of the client. For this and other reasons, the arrangement between lawyer and nonlawyer may not require referrals on an exclusive basis.

The Committee considered next whether the lawyer in a nonexclusive mutual referral arrangement has an obligation to disclose the relationship to the client. The Committee said:

...although the specified disclosures set forth in DR 1-107(A)(3) are not required...a reciprocal referral arrangement would generally constitute a conflict of interest under DR 5-101(A), such that the relationship would need to be disclosed and consent obtained before the lawyer made the referral.

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