

**Pennsylvania Bar Association Committee
on Legal Ethics and Professional Responsibility**

**REFERRAL FEES AND FEE SPLITTING UNDER RULE 1.5
OF THE RULES OF PROFESSIONAL CONDUCT**

Formal Opinion Number 96-176

Dated: March 14, 1997

The Committee on Legal Ethics and Professional Responsibility of the Pennsylvania Bar Association is frequently questioned by member attorneys on various ethical considerations presented by referral fees and so-called "fee splitting" agreements between attorneys. In an effort to provide general guidance on these questions, the Committee has compiled this Formal Opinion, which should be reviewed for guidance by Pennsylvania lawyers when they are confronted with issues of this kind.

I. Fee Splitting Under Rule 1.5

Rule 1.5(e) governs fee splitting with lawyers from different firms. That Rule provides as follows:

- (e) A lawyer shall not divide a fee for legal services with another lawyer who is not in the same firm unless:
- (1) the client is advised of and does not object to the participation of all the lawyers involved, and
 - (2) the total fee of the lawyers is not illegal or clearly excessive for all legal services they rendered the client.

The Comment to Rule 1.5(e) notes that a fee split "most often is used when the fee is contingent and the division is between a referring lawyer and a trial specialist," and the Committee's record of inquiries supports this conclusion. While the Rule permits non-affiliated lawyers to divide a fee if the total fee is not "illegal or excessive," and the client is advised and does not object, the Comment expressly notes that the Rule "does not require disclosure to the client of the share that each lawyer is to receive." Thus, the disclosure requirement is satisfied so long as the client is advised of the identity of the attorneys' law firms participating in the gross fee that is paid. [FN1]

Under the former Code of Professional Responsibility, both the disclosure and the "total fee" provisions were more restrictive. For example, DR 2-107(A) allowed a fee split only if the client consented "to employment of the other lawyer" after being apprised that the fee would be split. The use of the term "employment," with its implication that the second lawyer would actually have to play some active role in the case in order to be entitled to fee, is not present in Rule 1.5(e); rather, the Rule uses the term "participation." Similarly, former Rule DR 2-107(A)(2) required that the total fee "not clearly exceed reasonable compensation." The current standard, of permitting all gross fees that do not rise to the level of "illegal or clearly excessive," removes the "reasonableness" element from the analysis and arguably permits attorneys a freer hand to structure compensation agreements to a greater variety of situations. The precise language of Rule 1.5(e) has given rise to Committee inquiries in three general areas: (1) The client's right to approve or disapprove of a fee split agreement between the referring

attorney and the principal attorney; (2) the client's right to accept or reject the specific terms of such an arrangement, specifically the percentage amount of the referral fee to be paid to a referring attorney; and (3) whether any particular percentage amount, paid as a referral fee, risks being considered per se "unethical". This Formal Opinion sets forth the Committee's position on these three questions.

II. The "Unethical" Referral Fee

The Committee's research reveals that Rule 1.5(e)(2) is the subject of relatively little commentary and analysis. This subsection provides that an otherwise permissible fee-split will not be rendered impermissible unless the total, or gross, fee taken by all participating lawyers is "illegal or clearly excessive". Neither of these terms is defined with precision in either the Rule or the companion comment, and the determination of what constitutes an "illegal" or "clearly excessive" fee is a question that may be highly fact-sensitive. The eight factors to be considered in determining the propriety of a fee are set out under Rule 1.5(a). However, there is no one bright-line test for when a proposed fee becomes clearly excessive. It is likely that the most comprehensive answer to this question can be found in the current custom and usage of the trial bar and in fee petitions approved by the courts in an inquirer's geographic area. The Committee notes that cases of varying complexity or duration may be the subject of fees that are significantly higher than a more traditional one third contingent fee for mainstream personal injury matters. Such situations are, by their nature, fact-specific, and the Committee does not intend in this Formal Opinion to provide guidance as to the precise borderline between an "ethical" and "unethical" referral fee in a given case.

III. Client Controls on the Existence of a Referral Fee Agreement

Rule 1.5 gives the client ultimate control over the existence of a split-fee agreement between a referring and principal attorney. Rule 1.5(e)(1) only permits such split fees if "the client is advised of and does not object to the participation" of all such lawyers in the fee. It is important to note what is and what is not said in the above-quoted portion of Rule 1.5(e)(1). First, as noted above, the Rule permits several lawyers (and presumably law firms) to "participate" in the fee without mandating that they all be specifically employed by the client to perform services. In this way, the current Rule departs from the prior DR 2-107(A) which, by its terms, permitted fee sharing only where all compensated lawyers were actually employed to perform services for the client. With this change, Rule 1.5 made expressly permissible the long recognized practice of paying referral fees in contingent fee cases where the referring attorney did little or no work on the file before referring the client to what the Rule's comment calls a "trial specialist." [FN2]

Second, Rule 1.5(e)(1) carefully words its "client approval" language. Unlike many other Rules, which require a client's express consent after full disclosure of a particular aspect of representation, this Rule only requires that, after being apprised that more than one lawyer will participate in the fee, the client "does not object." Presumably, by use of this passive, rather than active, voice the Rule places the burden on the client to speak up if, after being advised of the proposed fee-splitting arrangement, she does not wish to give her consent. In the absence of such an affirmative statement by the client, the principal attorney and referring attorney may both participate in the fee on whatever terms they choose, so long as the arrangement otherwise complies with Rule 1.5(e). Thus, the Committee concludes that an attorney seeking to pay a referral fee has complied with the provisions of Rule 1.5(e)(1) once he advises the client that a referral fee will be paid, and the client consents or does not affirmatively object.

IV. Client's Input Into Specific Referral Terms

As stated above, Rule 1.5(e)(1) permits the client to prohibit payment of the referral fee or other fee split by stating an objection thereto. However, the client's input apparently stops at the "yes" or "no" option, and Rule 1.5(e) does not require that the attorney permit the client any input into the specific details of the referral relationship. The express language of Rule 1.5(e)(1) mandates only that the client be advised of the multi-lawyer participation and that there be an absence of an objection. In another departure from other Rules, Rule 1.5(e)(1) does not require typical "full disclosure," but rather requires only that the client be advised that a fee-sharing arrangement is in place. The Rule's express language does not require that the attorney go into any degree of detail concerning the referral relationship, its terms, or the precise division of the fees at issue. [FN3] The companion comment makes it clear that such full disclosure is not required:

Paragraph (e) permits the lawyers to divide a fee if the total fee is not illegal or excessive and the client is advised and does not object. It does not require disclosure to the client of the share that each lawyer is to receive. (emphasis added)

Because there is no requirement that the client be told anything more than the fact that a fee will be split, the Committee concludes that Rule 1.5(e)(1) does not convey to the client the authority to manipulate or veto the specific terms of the referral or split fee relationship. As a practical matter, a client may inquire as to those details in deciding whether or not to object to the referral relationship, and the attorney who refuses to provide that information may do so at the peril of the client's objection to any referral at all. However, the Rule imposes no obligation to disclose to the client the specific terms of the referral relationship.

One problem that is not addressed by the Rule or companion comment is that of a potential conflict between the ethical mandate of Rule 1.5 and a contractual relationship that may exist between a referring and principal lawyer. If the two attorneys have an agreement that a referral fee be paid, and the client subsequently objects to that payment, the principal attorney is in a quandary: paying the fee over the client's objection risks ethical violations, while withholding the payment at the client's direction will likely be treated as a breach of contract by the referring attorney. Unfortunately, Rule 1.5 offers no guidance on this dilemma, nor do other rules. It is apparent that substantive contract law will shed light on the question, an area on which the Committee cannot opine. In such situations, the Committee generally recommends that the referral fee, or whatever portion of such fee is in dispute, not be disbursed pending resolution of the dispute. Since the principal lawyer may simply become a "stakeholder" in such a dispute, it may be preferable for the referral fee to be deposited by agreement in an escrow account maintained by the referring lawyer, with the written understanding that the funds will not be drawn down or removed absent court order or the client's consent.

V. Conclusion

Rule 1.5 brings the ethical and disciplinary treatment of referral fees into compliance with modern practice, but continues to leave certain frequently recurring questions unanswered. The lawyer's general obligations to communicate with the client require adequate disclosure at the outset of the existence of the referral fee arrangement. While client consent (or lack of objection) to the referral arrangement should be secured when the referral fee agreement is made, the lawyer is not required

under Rule 1.5 to secure an additional consent to the payment of the referral fee upon the conclusion of the matter and distribution of the proceeds, assuming the referral fee is entirely drawn from the previously agreed upon contingent fee. The payment of the referral fee, absent some agreement to the contrary, is not contingent on the effort expended by the referring lawyer in achieving the result. Where a client objects to the payment of a previously agreed referral fee, the preferred practice is to place in escrow the portion of the referral fee as to which there is an objection pending resolution of the dispute, with prompt advice to the referring lawyer and the client.

Committee on Legal Ethics and Professional Responsibility of the Pennsylvania Bar Association

Thomas G. Wilkinson, Chair

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FN1. Rule 1.5(c) provides that all contingent fee arrangements must be in writing, and further provides that, if there is a recovery, the lawyer must provide the client with a written statement showing the remittance to the client and the method of its determination.

FN2. There may be certain circumstances where, due to a disabling conflict of interest or otherwise, it will be impermissible for the lawyer to request or accept a referral fee. This opinion does not address that issue.

FN3. The Committee has and continues to emphasize the importance of complete client communication on matters material to the representation. See Pa.RPC 1.4. For example, in a recent formal opinion, the Committee emphasized the need for explicit advice and consent of clients when attorneys propose to employ various forms of fee retainer arrangements. Formal Opinion 95-100: Ethical Considerations in Connection With Retainers Paid on Account of Legal Services (Aug. 1, 1995).