STATE BAR OF NEVADA
STANDING COMMITTEE ON ETHICS AND PROFESSIONAL RESPONSIBILITY

Formal Opinion No. 24
June 18, 1987

QUESTION - May a lawyer accept an ongoing referral fee from an investment advisor/broker where the fee payments are disclosed in advance to an existing client and the lawyer monitors the account, but the investment advisor/broker has exclusive responsibility for managing the account?1

ANSWER - The conflict of interest inherent in the situation is not waivable as the lawyer cannot continue to act as the client's lawyer once he assumes the role and responsibilities of a broker. If an investment is made through the lawyer/broker, the client must first obtain independent legal advice and it must be objectively clear that the lawyer/broker is acting only as a broker.

AUTHORITIES RELIED ON
Nevada Rules of Professional Conduct (Supreme Court Rule) 157.2, 158.6, 167 and 188; Annotated Rules of Professional Conduct, American Bar Association, 1992; New Hampshire Bar Ethics Committee Opinion #1994/95-2 ABA Informal Op. 1482 (1982); In re Singer, 109 Nev. 1117, 865 P.2d 315 (1993); Louisiana State Bar Assn.. v. Drury, 455 So. 2d 1387 (La 1984) cert denied, 470 U.S. 1004 (1985); Attorneys' Conflicts of Interest in the Investment Company Industry, 6 U. Mich. J.L Ref. 58.

DISCUSSION
The New Hampshire Bar Ethics Committee wrestled with a nearly identical question in its Opinion #1994/95-2 and was unable to agree on a majority opinion. Some New Hampshire committee members believed that the lawyer could not give truly

1 The question as presented to the committee points out that Nevada law requires the referring lawyer to be licensed as an investment advisor in order to receive a portion of the management fee.

Independent advice--the motivation being a fee for the lawyer-and therefore there was no real benefit from the advice to the client and the conduct was unreasonable. But other New Hampshire committee members were concerned that a fully informed client is free to reject the referral after disclosure of the lawyer's interest, and the comments to A.B.A. Model Rule 1.7(b) imply that a lawyer may allow such a referral given full written disclosure. (The

A.B.A. comments to Rule 1.7(b) state that, "a lawyer may not allow related business interests to affect representation, for example, by referring clients to an enterprise in which the lawyer has an undisclosed interest.")

SRC 158.6 precludes a lawyer from taking compensation from one other than his client if there is any interference with the lawyer's "independence of professional judgment". An application of that concept to the present issue is critical. In making that analysis , this committee notes that while a lawyer can have business interests which may be affected by representing a client, and such a conflict may be remedied by full disclosure and a valid waiver, we do not believe that any such conflict should involve the actual payment of a legal fee to that lawyer by the differing interest for the same subject matter upon which the lawyer is rendering advice, and in fact the case law on that subject consistently upholds that interpretation. See Annotated Rules of Professional Conduct, American Bar Association, 1992, pg. 146. See also In re Singer, 109 Nev. 1117, 865 P.2d 315 (1993),(There is a presumption of impropriety in any business transaction between lawyer and client which benefits the lawyer.)

The situation posited, upon close examination, is far more complex than a run-of-the-mill third party payment situation, such as an insurance company paying a lawyer for representing an insured. In the

instant matter, the client of the lawyer is likely asking investment advice based upon the receipt of a settlement or inheritance acquired through the lawyer's services. More likely than not, there will not be a direct billing to the client by the lawyer for the investment advice, and more likely than not the subject matter for which the lawyer was hired is essentially over. The person paying for the lawyer" services is actually the investment advisor. Yet, unlike an insurance carrier paying for an insured, the investment advisor does not expect any significant services to be rendered to the client by the lawyer, and certainly does not expect to pay for any such services, as the fee paid to the lawyer is a fixed percentage of a management fee, not an hourly rate.

This committee is particularly troubled by that portion of the question which would have the referring lawyer monitor the client's investments without the ability to affect the investment decisions. SCR 188.3 precludes a lawyer from permitting one who pays him to render legal services for another to direct or regulate the lawyer's professional judgment in rendering those services. How can a lawyer possibly act as an independent monitoring agent if he not permitted to affect the investment decisions? How can the lawyer realistically be expected to suggest to the client that the investment strategy is unsound when the lawyer is being paid by the investment company on a continuing basis? What exactly is the lawyer expected to do for the fee being paid to him by the investment advisor? To whom does the lawyer owe a duty of loyalty? When looked at in this context, the lawyer has taken off his lawyer that when asked by the client about where to place the funds, and has put on his broker/investor hat. A written disclosure agreement is meaningless and may even be misleading since the lawyer is not acting in the client's interest, but in his own interest and that of the investment advisor. The client is being denied "independence of professional judgment".

In Louisiana State Bar Assn. V. Drury, 455 So. 2d 1387 (La 1984) cert denied,470 U.S. 1004 (1985), a lawyer was suspended for taking a referral fee from a doctor in a personal injury case. Although the lawyer failed to disclose the "kick-backs", the court noted the following:

" . . . Drury had a substantial interest in the doctor's medical fees which might tempt him to overlook overcharges, excessive treatment or poor medicine, should any occur. He clearly was not insulated from the desires of others or pressures that might influence his free professional judgment. The primary object of DR 5-107 if to prevent an attorney from becoming involved in conflicts of interests which may lead to the harm of his clients, the bar or the public. The harm does not have to occur in order for a prohibited conflict to exist."

Analogizing the client and his invested and managed resources to a fund such as a mutual fund (investment company), the inherent nature of the conflict becomes readily apparent:

"The Code implies that an attorney can continue to represent differing interests so long as there is full disclosure to all clients and their consent to such representation is obtained. In the investment company industry, however, dual representation should not be permissible. The attorney for the fund is usually retained by the management company, which pays his salary and to which he is ultimately responsible. Counsel's loyalty, whether consciously or unconsciously, is directed primarily toward the management company and not toward the fund. . . . Judge McGowan feels that disclosure of conflicts to the client simply shifts the burden of avoiding or approving the conflict to the client. He suggests that this is unrealistic, because "it is [not' the client who can best make the decision as to whether there is a harmful conflict, even though he knows all the facts."" Attorneys' Conflicts of Interest in the Investment Company Industry, 6 U. Mich. J.L. Ref. 58, 67-68 (1972).

When a client asks a lawyer for investment advice, a number of obligations come into question. Has the lawyer made an independent assessment of the skill and advantages or disadvantages of all of the investment advisors in the area? What is the lawyer's knowledge and understanding in the investment field? Does the referral fee increase the management fee to the client? Could the lawyer negotiate for the client a reduced management fee with or without the referral fee included in the equation? What is the lawyer's liability to the client for a mismanaged account?

Clients take recommendations of lawyers as advice to be trusted. It is one thing for a knowledgeable client to sign off on a written disclosure of the lawyer's interest, including an understanding of the necessity to seek independent legal advice. It is quite another thing for this committee to presume that the lawyers making such referrals would not be affected in making the suggestion by the lure of a continuing fee, magnified over time by the many fees that might be forthcoming based upon the referral of many clients.

CONCLUSION

A lawyer is not precluded from acting as a broker, so long as it is clear that the person being provided brokerage service is not a client of the lawyer's firm and cannot be confused as such. If the funds in question were obtained for the person seeking investment advice by the broker's law firm, the committee believes that circumstance would constitute prima facie evidence of a conflict which would require that the person seeking investment advice first obtain independent legal counsel before the investment can be made through the lawyer/broker.

This opinion is issued by the Standing Committee on Ethics and Professional Responsibility of the State Bar of Nevada, pursuant to SCR 225. It is advisory only. It is not binding upon the courts, the State Bar of Nevada, its Board of Governors, any person or tribunal charged with regulatory responsibilities, or any member of the State Bar.