Ethics Watch

Enforcing Fee Splitting Rules: Equity Rather Than Strict Compliance

By Nathan M. Crystal

Relationships among lawyers who are not members of a firm are commonplace in modern law practice, particularly litigation matters. Broadly speaking, such relationships can take two forms: referral or cocounsel. In both situations it is common for lawyers to split or divide fees. A recent decision from the Illinois Court of Appeals shows the risks when lawyers fail to comply with the ethical rules regarding fee splitting. *Fohrman v. Alberts*, 2014 Ill. App. Lexis 152 (2014), dealt with a referral agreement between Fohrman, who specialized in workers' compensation cases, and Alberts, who handled personal injury and medical malpractice cases. Fohrman and Alberts entered into an oral agreement in which Fohrman agreed to refer clients who had personal injury cases to Alberts in exchange for Alberts's agreement to pay Fohrman 50 percent of the fees he received from such cases. Fohrman alleged that the agreement called for Alberts to disclose properly the cocounsel relationship to the clients in conformity with ethics rules. In most of the fee agreements Fohrman and Alberts were both listed as counsel with a fee of 33 1/3 percent. However, the fee agreement did not specify the portions that each of the lawyers was to receive, although Fohrman argued that it was presumptive that the fee would be split 50-50. He also argued that the dual listing showed that he was equally responsible with Alberts for the handling of the cases and subject to liability if either attorney committed malpractice. It appears that Fohrman did not do any work on the referred cases.

Alberts paid Fohrman more than $700,000 in referred cases, but at a certain point he stopped paying. Fohrman sued for damages on numerous theories, including breach of contract, breach of fiduciary duty, fraud, unjust enrichment, promissory estoppel, and others. Alberts moved to dismiss the complaint on the ground that the fee splitting agreement violated Illinois Rule of Professional Conduct 1.5(e) and was therefore unenforceable as a matter of public policy. The Illinois version of 1.5(e) is substantially the same as the ABA Model Rule and the South Carolina rule. Alberts also raised a variety of defenses, including the claim that Fohrman was fully aware that the agreements with the clients did not comply with the ethics rules, but he nonetheless failed to inform his clients of the referral agreements and obtain their informed consent. The lower court dismissed some of Fohrman's claims and granted summary judgment for Alberts on others.

The Court of Appeals affirmed the lower court's judgment for Alberts. The opinion is significant with regard to fee splitting agreements in a number of respects. First, the court recognized that the fee splitting rule reflects a strong public policy; that "strict compliance" with Rule 1.5(e) was necessary; and that in the absence of such compliance, any fee division agreement was unenforceable. To comply with the rule in Illinois, the writing must disclose "the respective responsibility to be assumed and economic benefit to be received by the other lawyer." The Court of Appeals held that the fee agreements did not comply with Rule 1.5(e) because they did not set forth the division of fees and they did not specify the responsibility assumed by Fohrman. Second, the court understood that its decision allowed Alberts to keep fees that he had agreed to pay to Fohrman; however, the court reasoned that Rule 1.5(e) is based on the policy of protecting clients and overrides any claims of unfairness on the part of one of the lawyers to the fee splitting agreement: "[W]e do not condone any alleged misconduct or encourage unfairness in relationships between attorneys. We uphold the Rules' interest in protecting clients above the interests of attorneys in recovering fees." Id. at *36-37. Third, the court ruled that the duty to comply with Rule 1.5(e) applied to both the referring and the performing lawyer. That was especially true on the facts of the case because Fohrman and Alberts were both named as counsel in the engagement agreement, Fohrman had received copies of Alberts's engagement agreements for a number of years, and he should have been aware that they did not comply with Rule 1.5(e). Fourth, the court rejected Fohrman's "substantial compliance" argument. He claimed that because the fee agreements with the clients listed him as counsel it was "presumptive" that the fees would be divided 50-50 and that he was equally responsible for the cases with Alberts. The court held that such a presumption would be inconsistent with the basis of the rule—client protection—and with the requirement that the rule be complied with strictly. Id. at *41. Finally, the court concluded that the rule of unenforceability applied not only to claims for breach of contract between the lawyers but also to all other claims that were based on fee splitting, including breach of fiduciary duty and quantum meruit.

The strict compliance approach followed by the court in *Fohrman* appears to be the majority rule. See

Special Report, 30 Laws. Man. Prof. Cond. (ABA/BNA) 218 (2014). However, some courts have adopted an equitable approach. For example, the court in *Post v. Bregman*, 707 A.2d 806 (Md. 1998), ruled that the defense of violation of Rule 1.5(e) was equitable in nature. The court stated that the following factors were relevant to determining whether the fee splitting agreement should be enforced even if the agreement violated Rule 1.5(e): (1) the nature of the violation, (2) how the violation occurred, (3) the extent to which the parties acted in good faith, (4) whether the lawyer raising the defense was equally culpable and was raising the defense to avoid paying an otherwise valid obligation, (5) whether the violation had particular public importance, (6) whether the client would be harmed by enforcement of the agreement, and (7) other relevant considerations.

Although I know that controversies on fee splitting are common, I am unaware of any South Carolina cases dealing with the issue of enforceability of fee division agreements that fail to comply with Rule 1.5(e). When the issue arises in this state, in my opinion for a number of reasons discussed below, the S.C. Supreme Court should adopt the equitable approach of *Post v. Bregman* rather than the strict compliance rule that is apparently followed by a majority of courts. However, because the S.C. Supreme Court may adopt the majority view, lawyers are advised to comply strictly with all of the requirements SCRPC 1.5(e).

The equitable approach is more consistent with principles of general contract law and the rules governing forfeiture of attorney fees than the strict compliance view. Under general contract law, when a statute or regulation does not specifically declare that a contract in violation of the statute or regulation is unenforceable, courts do not apply a per se rule of invalidity; instead, they balance a number of factors to determine whether the contract should be enforced. See Restatement (Second) of Contracts §178. Rule 1.5(e) does not specifically state that a contract in violation of the rule is unenforceable. Application of the equitable approach would, therefore, be more consistent with the balancing approach of general contract law.

The equitable approach is also more consistent with the rules governing forfeiture of attorney fees than the strict compliance standard. The general rule is that a violation of a rule of ethics does not necessarily make the fee agreement unenforceable. Only if the lawyer engages in a clear and serious violation of the rules will a court order a lawyer to forfeit all or a portion of the lawyer's compensation. Restatement (Third) of the Law Governing Lawyers §37. Under this section the court should consider a number of factors to determine the extent of forfeiture. The equitable approach to enforcement of fee splitting agreements that violate Rule 1.5(e) is more consistent with the general rule governing fee forfeitures than the strict compliance approach.

Courts following the strict compliance approach usually state that the rule is designed for client protection. However, many of the rules of ethics—confidentiality, conflicts of interest, reasonableness of fees—are designed for client protection. Indeed, many of these rules rest on client interests that are at least as significant as the client interest in the fee splitting rules, yet a violation of these other rules does not necessarily result in fee forfeiture.

It could be argued that a rule of strict compliance is necessary because otherwise lawyers will cut corners and ignore the mandates of Rule 1.5(e). This argument is unconvincing, however, because intentional efforts to avoid Rule 1.5(e) would not fare well under the equitable approach. Further, even if a lawyer does not forfeit fees for violation of Rule 1.5(e), the lawyer could still face disciplinary action.

Several other reasons support the equitable approach. Ambiguities exist in the application of Rule 1.5(e). Must the disclosure of the amount of the fee split and the identity of the lawyers with whom fees will be split be made at the inception of the attorney-client relationship or can it be made later? What exactly is meant by "joint responsibility" and is it necessary for the written disclosure of the terms of the fee split to include a statement about the joint responsibility of the referring lawyer? In cocounseling cases, when is the fee division in proportion to services performed by the lawyers? Given these uncertainties—and others—is a rule of strict compliance either reasonable or fair?

More fundamentally, the rule of strict compliance gives performing lawyers an incentive to seek reasons to refuse to honor agreements that they have in fact made with referring lawyers. Instead, rules of law should promote trust and fair dealing among lawyers, rather than encouraging lawyers to avoid commitments they have made to fellow members of the bar. ■