CASH CONFLICTS: RECONCILING CONFLICTS OF INTEREST BETWEEN ATTORNEYS' FEES AND THE NEEDS OF THE CLIENT

I. INTRODUCTION

A direct conflict of interest exists between attorneys' desires to make money and clients' interests in receiving quality legal work at the lowest possible cost. Although attorneys' fees must be "reasonable," considerable debate (and tort reform efforts) exist over the meaning of "reasonable." Regardless of whether or not an attorney's fee is reasonable, this article addresses the question of when an attorney's fee violates the rules of ethics. Specifically, this Article first addresses when an attorney violates the rules of ethics by improperly participating in a business partnership with its clients. The Article next examines other miscellaneous methods of payment that may also violate the rules of ethics, including: contingency fees (in some cases), certain fees in bankruptcy cases, media rights as a method of payment, and payment of fees by a third party.

II. BUSINESS PARTNERSHIPS

A lawyer should be cautious when engaging in a business transaction with a client if the client expects the lawyer to simultaneously perform the duties of a partner and attorney. Rule 1.8(a) of the Model Rules of Professional Conduct (Model Rules) provides:

A lawyer shall not enter into a business transaction with a client or knowingly acquire an ownership, possessory, security, or other pecuniary interest adverse to a client unless:
(1) the transaction and terms . . . are fair and reasonable . . . and are fully disclosed and transmitted in writing to the client . . .
(2) the client is given a reasonable opportunity to seek the advice of independent counsel in the transaction; and

2. Model Rules of Professional Conduct Rule 1.7(b) (1997) (An attorney's fee violates the Model Rules of Conduct when the fee causes the lawyer's own interests or the interests of a third party to materially limit the representation of a client).
(3) the client consents in writing thereto.\textsuperscript{4}

Cases from different jurisdictions explain each relevant phrase of the rule.

A. "Enter Into a Business Transaction"

Attorneys have sometimes violated Model Rule 1.8(a) because they were not aware that the transaction was "business." In several cases, attorneys violated the rules of ethics by treating personal loans between a client and the attorney as personal dealings instead of business transactions.\textsuperscript{5} In \textit{In re Coxeter},\textsuperscript{6} two New York attorneys (Daniel and Susan Coxeter) accepted a loan from a client.\textsuperscript{7} The Coxeters, as borrowers, prepared the loan documents for the client.\textsuperscript{8} The New York court held that the attorneys violated the rules of ethics, even though it was a personal loan, because the client expected the attorneys to represent their interests when drafting the loan.\textsuperscript{9}

B. A Lawyer Shall Not Enter Into a Business Transaction With a Client

Absent an attorney-client relationship, an attorney cannot violate the rules of ethics by improperly engaging in a business relationship.\textsuperscript{10} Courts differ on how to define the "client" under Rule 1.8(a). Specifically, some courts apply Rule 1.8(a) to every client of a law firm, while others define a client as only those persons for whom a lawyer personally performs legal services.\textsuperscript{11} In Arizona, an attorney’s business activities

\begin{itemize}
\item\textsuperscript{4} \textit{Id.}
\item\textsuperscript{5} \textit{In re Coxeter}, 620 N.Y.S.2d 501 (N.Y. App. Div. 1994); \textit{In re Drake}, 642 P.2d 296 (Or. 1982) (Attorney suspended for three years for reasons including failing to refuse employment when client’s needs in making a loan to the lawyer were adverse to that of the lawyer’s needs); \textit{In re McClain}, 671 A.2d 951 (D.C. 1996) (attorney suspended for 90 days for borrowing money from clients); \textit{In re Gillingham}, 896 P.2d 656 (Wash. 1995).
\item\textsuperscript{7} \textit{Id.} at 502.
\item\textsuperscript{8} \textit{Id.}
\item\textsuperscript{9} \textit{Id.}
\item\textsuperscript{10} \textbf{MODEL RULES OF PROFESSIONAL CONDUCT} Rule 1.8(a) (1997).
\item\textsuperscript{11} \textit{See In re Murphy}, 936 P.2d 1272 (Ariz. 1997); \textit{In re Manns}, 685 N.E.2d 1071, 1079 (Ind. 1997).
\end{itemize}
are restricted by Rule 1.8(a) with all clients of the law firm.\footnote{12} In \textit{In re Murphy}, the court held that whether the attorney “actually performed legal services for [the client] . . . is of no consequence since [the attorney] was a partner in the firm whose members did.”\footnote{13} In contrast, Indiana does not restrict the business activities of the attorney simply because the business partner is a client of another lawyer in the firm.\footnote{14} In \textit{In re Manns}, the court held that “[p]rofessional Conduct Rule 1.8(a) is not expressly incorporated into that ‘imputed disqualification’ rule. We therefore find no violation of Prof. Cond. R. 1.8(a) because there was insufficient evidence to find that the investor [a client of the respondent’s law firm] was the respondent’s client.”\footnote{15}

\textbf{C. (1) The Terms . . . Are Fair and Reasonable . . . and Fully Disclosed}

Attorneys are permitted to engage in business relationships with clients if certain criteria are met. The first criterion is that the business relationship must be fair and reasonable.\footnote{16} However, even when lawyers are fair and reasonable when engaging in business relationships with their clients, the lawyer may still violate the rules of ethics.\footnote{17} In \textit{In re Gillingham},\footnote{18} an attorney drafted and obtained a loan from the client without meeting the proper safeguards.\footnote{19} The attorney eventually repaid the loan with interest to the client.\footnote{20} The court held that the attorney “did not fully disclose and transmit in writing . . . the terms of the loan. Therefore, the transaction at least technically violate[d] [Rule] 1.8(a).”\footnote{21} The court concluded that this small infraction deserved admonition.\footnote{22}

\begin{itemize}
\item \footnote{12}{\textit{Murphy}, 936 P.2d at 1273.}
\item \footnote{13}{\textit{Id.}}
\item \footnote{14}{\textit{Manns}, 685 N.E.2d at 1074.}
\item \footnote{15}{\textit{Id.}}
\item \footnote{16}{\textit{Model Rules of Professional Conduct} Rule 1.8(a) (1997).}
\item \footnote{17}{\textit{See In re Gillingham, 896 P.2d 656, 658 (Wash. 1995); Weiss v. Statewide Grievance Committee, 633 A.2d 282, 288 (Conn. 1993).}}
\item \footnote{18}{896 P.2d 656 (Wash. 1995).}
\item \footnote{19}{\textit{Id.} at 658.}
\item \footnote{20}{\textit{Id.} at 659.}
\item \footnote{21}{\textit{Id.} at 661.}
\item \footnote{22}{\textit{See also In re Guidone, 653 A.2d 1127, 1129 (N.J. 1994) (“[i]n cases involving a conflict of interest, absent egregious circumstances or serious economic injury to the clients involved, a public reprimand constitutes appropriate discipline.”}}
\end{itemize}
even though the client entered into the loan voluntarily and was in no way injured by the business relationship. 23

Similarly, an attorney may have a conflict of interest with the needs of a client if the lawyer's fee is paid by a share of the client's business, even though the fee is fair and reasonable. In addition to violating the rules of ethics, a lawyer might also subject himself to a malpractice action if that attorney engages in a business transaction with a client. For example, in Bell v. Clark, 24 the attorney was a partner in, and a counsel- or for a real estate partnership. 25 The Indiana Court of Appeals upheld the decision to find the lawyer guilty of malpractice. 26

In Weiss v. Statewide Grievance Committee, 27 a Connecticut lawyer rendered legal services in connection with a project to develop a full service hotel. 28 When the legal fees came due, the clients were unable to pay for Weiss' legal services. 29 The parties then agreed that Weiss should receive an 18% interest in the hotel project as fair compensation in lieu of cash payment. 30 The State Grievance Committee reprimanded Weiss because a conflict of interest arose when Weiss received the 18% interest. 31 On appeal, the Supreme Court of Connecticut affirmed the reprimand of Weiss because it was reasonable to conclude that Weiss

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25. Id.
   (“A lawyer’s representation of an interest adverse to his client can constitute malpractice because such action taken against the client’s interests constitutes the failure to exercise the knowledge, skill, and ability ordinarily possessed and exercised by lawyers.”).
27. 633 A.2d 282 (Conn. 1993).
28. Id. at 284; see also Rule 1.8(j) (1990):
   A lawyer shall not acquire a proprietary interest in the cause of action or subject matter of litigation the lawyer is conducting for a client, except that the lawyer may: (1) acquire a lien granted by law to secure the lawyer's fee or expenses; and (2) contract with a client for a reasonable contingent fee in a civil case.
29. Weiss, 633 A.2d at 284.
30. Id. at 284.
31. Id. at 285-86.
“had ‘adversely affected [his] judgment or loyalty to [the client],’ thereby causing him to ‘[overreach] his client to pursue his own self-interest.’”  

D. (2) The Client Is Given a Reasonable Opportunity to Seek the Advice of Independent Counsel

An attorney should not use contract language alone to inform his other client of the opportunity to seek the advice of independent counsel. In *In re Singer*, the attorney included language in a loan contract and letter that the client should seek the advice of another attorney. However, the attorney did not inform the client of his conflict of interest nor did he explain why the client should seek the advice of another attorney. The court noted that “Singer clearly placed himself in a position wherein the exercise of his professional judgment on behalf of his clients could be affected by his own financial interests.” The court held that although the attorney technically informed the client of the opportunity to seek counsel, the notice was insufficient to make the client fully aware of the need for independent counsel. Therefore, the court reprimanded the attorney for his failure to properly encourage his client to seek the advice of another attorney.

In *Committee on Professional Ethics and Conduct of the Iowa State Bar Association v. Carty*, the Iowa Supreme Court reprimanded an attorney who procured independent counsel for his clients. In *Carty,*

32. *Id.* at 288 (quoting Statewide Grievance Committee v. Rozbicki, 595 A.2d 819 (Conn. 1991)).
34. *Id.*
35. *Id.* at 317.
36. *Id.*
37. *Id.*
39. *Id.* It is important to note, however, that Nevada has an unusual burden of proof for ethics violations. In Nevada, “[i]n any transaction in which an attorney is charged with obtaining a business advantage from a client, there is a presumption of impropriety which may be overcome only by clear and satisfactory evidence that the transaction was fundamentally fair, free of professional overreaching, and fully disclosed.” *Id.*
40. 515 N.W.2d 32 (Iowa 1994).
41. *Id.* at 35.
the attorney and his clients were business partners in a farming operation.\textsuperscript{42} Carty orally instructed his clients to seek independent counsel and then had a fellow lawyer attend a reassignment closing on behalf of the clients.\textsuperscript{43} The court held:

>[the client’s] employment of Jones [the independent counsel] and his meeting with him and Carty did not meet the standard of independent counsel. This was the only meeting [the client] had with Jones regarding the reassignment. Carty sat in on the entire meeting and expressed his opinions along with those expressed by Jones. Carty should have insisted that [the client] secure independent counsel to advise them upon the legal consequences of the reassignment.\textsuperscript{44}

Due to Carty’s failure to properly instruct his clients to seek independent advice, the Iowa Supreme Court affirmed the Ethics Committee’s public reprimand.\textsuperscript{45}

\textit{E. In Writing}

The writing requirement applies to both the attorney’s duty to disclose the terms of the policy in writing and the duty to obtain the client’s consent in writing.\textsuperscript{46} Although all attorneys’ business transactions should be in writing, cases exist where a lawyer failed to comply with the writing requirement. In \textit{In re Gillingham},\textsuperscript{47} an attorney drafted and obtained a loan from the client without fully transmitting the terms of the loan to the client in writing.\textsuperscript{48} Although the terms of the loan were fair and reasonable, the court concluded that this small infraction deserved admonition,\textsuperscript{49} even though the client entered into the loan voluntarily and was in no way injured by the business relationship.\textsuperscript{50}

\begin{itemize}
\item \textsuperscript{42} \textit{Id.}
\item \textsuperscript{43} \textit{Id.}
\item \textsuperscript{44} \textit{Id.} at 36.
\item \textsuperscript{45} \textit{Carty}, 515 N.W.2d at 36.
\item \textsuperscript{46} \textit{Model Rules of Professional Conduct Rule 1.8(a)(1) & (3)} (1997).
\item \textsuperscript{47} 896 P.2d 656 (Wash. 1995).
\item \textsuperscript{48} \textit{Id.} at 661.
\item \textsuperscript{49} \textit{Id.; see also In re Guidone, 653 A.2d 1127, 1129 (N.J. 1994) ("[I]n cases involving a conflict of interest, absent egregious circumstances or serious economic injury to the clients involved, a public reprimand constitutes appropriate discipline.")}
\item \textsuperscript{50} \textit{Gillingham}, 896 P.2d at 662.
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III. OTHER FEE ARRANGEMENTS THAT HAVE ETHICAL IMPLICATIONS

There are other fee arrangements which may violate the rules of ethics because the fee itself creates a conflict of interest. Some fees where ethics are at issue include: contingency fees in divorce and criminal cases, media rights as a method of payment, payment of fees by a third party, and fees in bankruptcy reorganization cases.

A. Contingency Fees

Considerable debate exists over the amount of fees lawyers can and should charge in contingency fee arrangements. Except in certain circumstances, a "fee may be contingent on the outcome of the matter for which the service is rendered," as long as the fee is reasonable. Two circumstances in which a contingent fee can never be charged are divorce proceedings and criminal proceedings.

Contingent fee arrangements in a criminal case violate the rules of ethics because "such an arrangement can create a conflict between the interests of the client and those of the attorney." The rationale for the rule is that lawyers could risk the welfare of their clients by forgoing settlement and pursuing acquittal in order to receive a greater fee. For example, in State v. Labonville, the attorney was to receive almost three times more per hour if there was an acquittal for the defendant. The New Hampshire Supreme Court explained the problem:

Where an attorney is to be paid only if his client is acquitted, the attorney may be tempted to seek a full trial of the case, even though acceptance of a plea bargain or other relief would better serve the client. For this reason, professional ethics prohibit such arrangements

53. Model Rules of Professional Conduct Rule 1.5(d) (1997); see Model Code of Professional Responsibility Rule DR 2-106(C) (1997) (citing Peyton v. Margiotti, 156 A.2d 865, 867 (Pa. 1959) ("In criminal cases, the rule is stricter because of the danger of corrupting justice."); cf. Model Code of Professional Responsibility Rule EC 2-20 (1997) (Contingency fees in divorce proceedings are "rarely justified.").
and attorneys who violate professional standards are subject to discipline.\textsuperscript{56}

Similarly, a lawyer cannot enter into a contingent fee arrangement in matters relating to the dissolution of a marriage.\textsuperscript{57} According to the California Bar, "[t]he rationale of holding such agreements void [is] that an attorney acquire(s) a personal, pecuniary interest in preventing a reconciliation between husband and wife."\textsuperscript{58} In addition, the lawyer might also have a conflict of interest with the client by seeking greater monetary awards in lieu of intangible interests such as child custody.\textsuperscript{59}

\textbf{B. Media Rights}

As a general rule, a lawyer cannot initially contract for media rights when representing a client.\textsuperscript{60} Model Rule 1.8(d) provides that "[p]rior to the conclusion of representation of a client, a lawyer shall not make or negotiate an agreement giving the lawyer literary or media rights to a portrayal or account based in substantial part on information relating to the representation."\textsuperscript{61} A conflict of interest between the attorney and client is created in such a fee arrangement because "[m]easures suitable in the representation of the client may detract from the publication value of an account of the representation."\textsuperscript{62}

In \textit{United States v. Hearst},\textsuperscript{63} the defendant alleged that her lawyer, F. Lee Bailey, was being compensated for his services through a book contract.\textsuperscript{64} Although the court examined whether Hearst was entitled to a new trial, the Ninth Circuit noted that "[t]he allegations and admissions in the record of the present case raise serious questions as to whether Bailey

\begin{thebibliography}{99}
\item 56. \textit{Id.} at 1379.
\item 59. \textit{But see} California State Bar Standing Comm. on Professional Responsibility and Conduct, Formal Op. 1983-72 (1983); \textit{Model Code of Professional Responsibility} EC 2-20 (1981) (Contingent fees in divorce proceedings have not always been barred outright, traditionally they were "rarely justified.").
\item 60. \textit{Model Code of Professional Conduct} Rule 1.8(d) (1997).
\item 61. \textit{Id.}
\item 62. \textit{Id.} at cmt. 3.
\item 63. 638 F.2d 1190 (9th Cir. 1980).
\item 64. \textit{Id.} at 1192-93.
\end{thebibliography}
and, to the extent of his participation, Johnson have been guilty of conduct unbecoming of members of the bar."65 Because of the book contract, "Bailey may have violated ABA CPR Disciplinary Rule 5-101(A) . . . "66 Disciplinary Rule 5-101(A) provides that a lawyer shall not accept employment when his professional judgment may be impaired by his own interests.

The mention of F. Lee Bailey in this context immediately brings to mind the multiple book deals in the O.J. Simpson case. Under an initial reading of the rules of ethics, the book deals in the O.J. case should not have been part of the lawyers' salary. However, a lawyer's fees may be paid by literary rights once the proceedings have finished.67 Therefore, as long as the legal fees in the O.J. case were supplemented with media revenue after the proceedings had finished, the lawyers technically did not violate the rules of ethics.

C. Payment of Fees By a Third Party

There is no absolute prohibition against a third party paying fees for a client. In fact, it is common for an insurance company, a business,68 or a parent69 to make payments to a lawyer for services rendered to a non-paying client. However, to prevent a conflict of interest between the lawyer, client, and the third party, Model Rule 1.8(f) provides that the lawyer must: 1) have the client consent, 2) maintain independent professional judgment, and 3) maintain client confidentiality.70

65. Id. at 1197; see also Beets v. Scott, 65 F.3d 1258, 1273 (5th Cir. 1995) ("[A] media rights contract is offensive because it may encourage counsel to misuse the judicial process for the sake of his enrichment and publicity-seeking, and it necessarily trades on the misery of the victim and his family.").
66. Hearst, 638 F.2d at 1197.
67. MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.8(d) (1997).
68. See MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.7 cmt. 10 (1997); see also Ingersoll-Rand Equipment v. Transportation Insurance, 963 F. Supp. 452, 454-55 (M.D. Penn. 1997).
69. See MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.7 cmt. 10 (1997); see also Ingersoll-Rand Equipment v. Transportation Insurance, 963 F. Supp. 452, 454-55 (M.D. Penn. 1997). It is important to note that although a parent or friend paying for a client's fees rarely raises a conflict of interest, the lawyer's duty of confidentiality to the client (under Rule 1.6) is an area that can cause a lawyer to violate the rules of ethics.
70. MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.8(f) (1997).
In *Miami County Bar Association v. Thompson,* the attorney represented a lender in a series of small loans. The attorney received his fee from the borrower for each small loan. The borrower became financially unstable during the series of loans. However, the attorney failed to fully inform the lender of the borrower's financial instability. The court found that the attorney did not maintain his professional judgment because the attorney benefitted in the transaction by not informing the lender of the borrower’s instability.

The State of Kentucky examined Rule 1.8(f) in the context of insurance companies which provided representation to their insureds on a set fee arrangement. In *American Insurance Association v. Kentucky Bar Association,* the Kentucky Supreme Court held that an insurance company could not contract with a lawyer for a set fee arrangement, nor could the insurance company provide in-house counsel to represent the client. In explaining why this fee arrangement might impair an attorney’s professional judgment, the court held that “a set fee arrangement enables the insurer to constrain counsel for the insured by, in effect, limiting the defense budget . . . .”

**D. Bankruptcy**

Bankruptcy reorganization cases are one instance in the law where a client’s interests are inherently in conflict with the attorney’s fee. Bankruptcy attorneys do not violate the rules of ethics in these cases even though their fee is in direct conflict with the interest of the client. In reorganization cases, a debtor/client is trying to retain enough assets to “stay afloat.” A lawyer’s fee charged to the client directly reduces the available pool of scarce resources needed to ensure the feasibility of the reorganization. Furthermore, if a lawyer takes a lien on the assets held

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71. 676 N.E.2d 879 (Ohio 1997).
72. *Id.* at 880.
73. *Id.* at 881.
74. *Id.*
75. *Id.*
76. See *American Insurance Ass’n v. Kentucky Bar Ass’n,* 917 S.W.2d 568, 569 (Ky. 1996).
77. 917 S.W.2d 568 (Ky. 1996).
78. *Id.*
79. *Id.* at 572.
80. See Jay Lawrence Westbrook, *Paying the Piper: Rethinking Professional*
in bankruptcy, his position becomes that of a creditor which is directly in conflict with the client/debtor.\textsuperscript{81} The lawyer in this situation is placed in an unavoidable, inherent "conflict between the lawyer's need to assure compensation and the client's interest in applying scarce resources in other ways."\textsuperscript{82} To avoid abuse, some courts require judicial approval of any fee arrangement in bankruptcy reorganizations to ensure the reasonableness of fees.\textsuperscript{83} However, to ensure that the attorneys are paid in these cases, all courts must accept this unavoidable conflict of interest. Therefore, bankruptcy attorneys do not violate the rules of ethics in their fee arrangements even though there is a conflict of interest.

\textbf{IV. CONCLUSION}

Except in pro bono cases, a lawyer will always have some level of cash conflict with the client (or third party payor) when the lawyer charges a fee. Such a conflict does not violate the rules of ethics as long as the fee is reasonable. However, certain billing arrangements create unethical conflicts of interest. Aside from contingent fee arrangements,\textsuperscript{84} if an attorney has a personal pecuniary interest in a certain outcome in a case, a lawyer may face an ethical dilemma or violation.

An attorney should be particularly cautious when engaging in a business partnership with a client due to his dual role as attorney and business partner. It is irrelevant whether the lawyer acts in good faith and in fairness toward the client if the attorney has not actively encouraged the client to seek independent counsel, and put all the terms of the business deal in writing. When an attorney obtains media rights as a pecuniary interest in lieu of cash payments, he or she must be certain that such a payment is not agreed upon until the resolution of all legal proceedings. Similarly, to meet the spirit of the rule, attorneys must not change trial tactics to increase media exposure when the attorney expects that future media/book rights will ultimately be the method of payment. In divorce

\textit{Compensation In Bankruptcy,} 1 AM. BANKR. INST. L. REV. 287, 297 (1993) ("The key point is that the conflict is inherent and unavoidable.").

81. \textit{Id.} at 299.
82. \textit{Id.} at 297.
84. MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.5(c) (1997); \textit{but see} Model Rule 1.5(d) (forbidding contingent fee arrangements in criminal and divorce proceedings).
and criminal proceedings, contingency fees are forbidden to prevent the method of payment from affecting the attorney’s settlement tactics. Finally, the inevitable conflict in bankruptcy cases is worthy of academic note because it represents an area where the law must accept the conflict of interest in the attorneys’ fees to ensure that attorneys are paid in reorganization proceedings.

Clients directly benefit if their lawyers do not have a pecuniary conflict of interest in their fees. Such a conflict of interest also brings ill repute to individual lawyers, the bar, and the law. Therefore, it ultimately is the good name of the legal profession that benefits from avoiding conflicts of interest when charging fees.

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