



The Law Society

Questions and answers on referral fees

Guidance issued by Rules & Ethics Committee

Last updated: 21st December 2005

In March 2004 the provisions on the payment by solicitors of referral fees were liberalised subject to various conditions and safeguards. The Society reviewed the operation of the modified provisions after these had been in force for 12 months. This review included a number of research projects, including interviews with firms which had made referral fee arrangements. The research indicated that a number of practitioners were not familiar with, or did not fully understand, the current provisions. The Standards Board has, therefore, requested that further guidance be published to increase awareness of and promote compliance with these provisions.

This further guidance is issued by the Society's Rules & Ethics Committee on 21 December 2005. This guidance does not form part of the rules and is not mandatory, but the Law Society may have regard to it when exercising its regulatory functions. Solicitors may need to be able to demonstrate how they have complied with the rules if they have not followed this guidance.

Question 1: Do all referral agreements have to be in writing?

The Solicitors' Introduction and Referral Code (the Code) does not specifically require referral agreements under section 2A (i.e. those involving referral fees) to be in writing. However, the Code does require you to keep a written record of all referral agreements (whether or not there is any payment involved). Also, you are required to have an undertaking from the introducer that the introducer will comply with the terms of the Code. If you have an arrangement under section 3 or 3A of the Code (i.e. an agreement under which you will be paid by the introducer to do work for the introducer's customers) this has to be in writing.

Question 2: What do I have to tell clients about my referral fee arrangements?

Section 2A(3) requires you to provide the client with "all relevant information concerning the referral and, in particular, the amount of any payment." Where a payment is made to an introducer in relation to each client referred by the introducer, either as a fixed amount or as a proportion of the fee charged to the client, the amount of the payment must be disclosed to each client. Where the payment is more general in nature (for example a fixed annual or monthly payment) clients should be informed that you are making a payment (or providing other consideration), but the actual amount need not be disclosed. If the client asks for more information about the overall amount of any payment made, you should supply such information as you can. If you cannot give the client all information about the arrangement with the introducer, you should make sure that the information you do give does not give the client a misleading picture. When making any disclosure about the arrangement you also need to have regard to your general fiduciary duties.

Question 3: How can I be sure that the introducer is complying with the requirements of the Code?

Section 2A(4) requires you to be satisfied that the introducer is complying with the requirements of the Code, in relation to the information the introducer gives to referred clients about the referral arrangement, and the way in which the introducer obtains clients. You might do this in a number of ways. The first step is probably to agree with the introducer, when you enter into the agreement, the nature of the information to be given to the client, and to keep a record of what you agree. You should also discuss how the introducer markets its services, as you cannot have a referral fee arrangement with a referrer which obtains clients using marketing or other activities which (if done by a solicitor) would breach any of the practice rules, in particular by "cold calling". You may wish to carry out random checks, by asking clients what information the introducer has given them and whether they have been "cold called" by the introducer, and keep a record of these checks. If you are unsure, you may also wish to insist that introducers confirm in writing to the client and to you details of matters they have disclosed to your clients.

Question 4: Can I pass on the cost of the referral to my client?

Referral fees are simply part of the cost of running your practice, in the same way as other marketing costs. They may be taken into account in calculating the fees to be charged, either generally or in respect of particular clients, but they may not be charged directly to the client. You may, for example, charge a higher fee for clients referred by a particular source, to take into account any referral fees payable; or you may choose to spread the cost of referrals across all of your clients. Either way, all referred clients must be informed that a referral fee is being paid and, where appropriate, the amount of the payment.

A referral fee is not a disbursement and may not be charged to the client as such, nor treated as such for accounting purposes. It is not a liability that you have incurred on the client's behalf in the course of acting for the client. It is your liability, incurred by you before the client instructed you. By including the referral fee as a separate item on the client's bill or in a quotation (whether or not it is described as a disbursement) you would be suggesting that the client is responsible for paying the referral fee, when this is in fact your liability under whatever agreement you have entered into with the introducer.

The client will probably have no idea that this is an unusual charge, and something their solicitor would be expected to fund. You could be said to be taking advantage of the ignorance of the client, even if you tell the client that you intend to charge for it and the client agrees. This could amount to a breach of Principle 12.09 which states that solicitors must not "abuse the solicitor/client fiduciary relationship by taking advantage of the client." It could also be damaging to the reputation of the profession, in breach of Practice Rule 1.

Question 5: I am not passing on the cost of the referral to the client so I do not consider it to be relevant to the client. Do I still have to disclose it?

Yes. The disclosure requirements apply regardless of whether clients in respect of whom referral fees are paid are charged more than other clients.

Question 6: Can I comply with the disclosure requirements by putting the information in my “client care” letter?

The answer depends on when you send out your client care letter to referred clients. Section 2A(3) requires you to provide the necessary disclosure “immediately upon receiving the referral and before accepting instructions to act”. Client care letters are normally sent following an initial discussion with the client, in order to confirm the client’s instructions, and the information you have given to the client about the retainer, such as costs and who will be dealing with the matter. It is, therefore, advisable that you notify clients, either orally or in writing, about the arrangement as soon as you are asked to act for them. You may then wish to confirm this information in your client care letter. If the information is initially given orally, you should make a file note to show that the information has been given at the appropriate time.

Question 7: I have had an arrangement for several years with a marketing company that refers clients to me. The payments I make are for marketing and undertaking initial investigations into potential claims, rather than for referrals, so I don’t have to comply with the Code, do I?

Section 2A of the Code applies to “any payment to a third party in relation to the introduction of clients to the solicitor”. It applies whenever a solicitor makes a payment, or gives other consideration to a third party who refers clients to the solicitor, unless the solicitor can show that the payment is wholly unconnected with the referral of any client to the solicitor. The conditions apply regardless of how the payment is described. For example, the conditions apply to the payment of administrative fees or marketing fees; payments described as “disbursements” which are not proper disbursements; panel membership fees; and fees for training provided by an introducer. Many arrangements which solicitors or introducers may have considered were not in breach of the previous (pre-March 2004) provisions are nevertheless now subject to the provisions in section 2A of the amended Code.

Question 8: The arrangement I have with a claims management company requires me to use medical experts specified by the company and to obtain counsel’s opinion in every case. Is this a problem?

If you are making payments to the claims management company in respect of the referral of clients, you will need to consider section 2A(4)(c) of the Code. This requires you to be satisfied that the introducer does not, under the arrangement, influence or constrain your professional judgement in relation to the advice given to the client. The question of whether, and if so which, counsel to instruct, or whether, and if so which expert to instruct, is the client’s decision, based on the solicitor’s advice. That advice must be given on professional grounds, not on the basis of a commercial contract which precludes a free exercise of the solicitor’s professional judgement. It is recognised, however, that certain third parties, such as a funder, may have a legitimate interest in this decision and may need to be consulted and/or give approval before instructions are given.

Question 9: I am thinking of setting up a joint marketing company with a number of other local firms of solicitors. This will involve referrals to the member firms which will all contribute to the costs of running the scheme. Will this be subject to the Code?

The Code does not apply to referrals between lawyers. However, where a marketing scheme is conducted through a separate company, rather than as part of a solicitors' practice, the company will not be a "lawyer" for the purpose of the Code. The provisions of the Code will apply as they would in relation to any scheme operated by a third party.

You should also be aware that Practice Rule 5 and the Solicitors' Separate Business Code 1994 prohibit practising solicitors from having any active involvement in a business which provides certain services, unless the business is a practice regulated by the Law Society. The services in question are listed in section 3 of the Separate Business Code, and include:

- the conduct of any matter which could proceed before any court, tribunal or inquiry, whether or not proceedings are commenced; and
- giving legal advice.

"Any active involvement" includes actively participating in the business or in the provision of its services to customers, and having any substantial ownership in or control over the non-solicitor business, including indirect control through another person, such as a spouse or civil partner.

Question 10: Can I pay, or offer to pay, referral fees to doctors or other medical professionals?

The Code does not specify categories of persons or businesses to whom or to which referral fees may be paid or offered. However, all referral arrangements (whether or not there is any payment involved) are subject to the general provisions of the Code, which requires compliance with all of the Practice Rules, in particular Practice Rule 1. This prohibits solicitors doing anything which compromises or impairs, or is likely to compromise or impair, the good repute of the solicitor or the solicitor's profession. Similarly, you should consider whether any publicity or marketing for your firm, whether carried out by your firm or by a third party on behalf of your firm, breaches this rule.

Question 11: Can I make payments to an introducer which are calculated as a proportion of my fees? Isn't this fee sharing?

Yes, this will be fee sharing, but the rule on fee sharing (Practice Rule 7) has also been relaxed. You can share your fees with a third party provided that "the purpose of the fee sharing arrangement is solely to facilitate the introduction of capital and/or the provision of services to the practice." There are other conditions, in particular that neither the arrangement, nor the extent of the fees shared, permits any fee sharer to influence or constrain the solicitor's professional judgement in relation to the advice given to any client.

In general the referral of clients will be a service to the firm. However, if the extent of the fee sharing is disproportionate to the value of the referrals, this may suggest that there is some other purpose to the arrangement.

Question 12: My client has agreed to pay a “case management fee” to a company that refers clients to my firm. As part of the agreement between my firm and the introducer, I am required to deduct that sum at the conclusion of the matter from money I hold on behalf of the client. Does this amount to “other consideration” under section 2A?

Yes, if this is a condition of referrals being made to your firm. You are providing a benefit to the introducer (the guarantee of having the money sent to them at the end of the matter) in return for the referral. Therefore both you and the introducer will need to disclose to the client that this is what has been agreed. You should bear in mind, however, that the client may be entitled to withhold or withdraw his or her authority for you to make this payment.

Where a client has agreed to make such payments you should also consider whether your duties to your client include advising them whether this is a properly justifiable payment, in view of the services being provided by the introducer.

For further help...

Please contact the Professional Ethics Helpline on 0870 606 2577. Please also refer to the guidance issued by the Society’s Standards Board in March 2004 entitled *Disclosure of funding, fee sharing and referral arrangements*. This is available on the Law Society’s website at the following link:

http://www.lawsociety.org.uk/documents/downloads/Profethics_Fund_Fee_Refer.pdf