

## Rule 1.8: Conflict of Interest: Current Clients: Specific Rules

### 1. Current Kentucky Rule with Official Comments:

#### SCR 3.130(1.8) Conflict of interest: prohibited transactions

(a) 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 on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing to the client in a manner which can be reasonably understood by the client;

(2) The client is given a reasonable opportunity to seek the advice of independent counsel in the transaction; and

(3) The client consents in writing thereto.

(b) A lawyer shall not use information relating to representation of a client to the disadvantage of the client unless the client consents after consultation.

(c) A lawyer shall not prepare an instrument giving the lawyer or a person related to the lawyer as parent, child, sibling, or spouse any substantial gift from a client, including a testamentary gift, except where the client is related to the donee.

(d) Prior 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.

(e) A lawyer shall not provide financial assistance to a client in connection with pending or contemplated litigation, except that:

(1) A lawyer may advance court costs and expenses of litigation, the repayment of which may be contingent on the outcome of the matter; and

(2) A lawyer representing an indigent client may pay court costs and expenses of litigation on behalf of the client.

(f) A lawyer shall not accept compensation for representing a client from one other than the client unless:

(1) Such compensation is in accordance with an agreement between the client and the third party or the client consents after consultation;

(2) There is no interference with the lawyer's independence of professional judgment or with the client-lawyer relationship; and

(3) Information relating to representation of a client is protected as required by Rule 1.6.

(g) A lawyer who represents two or more clients shall not participate in making an aggregate settlement of the claims of or against the clients, or in a criminal case an aggregated agreement as to guilty or nolo contendere pleas, unless each client consents after consultation, including disclosure of the existence and nature of all the claims or pleas involved and of the participation of each person in the settlement.

(h) A lawyer shall not make an agreement prospectively limiting the lawyer's liability to a client for malpractice unless permitted by law and the client is independently represented in making the agreement, or settle a claim for such liability with an unrepresented client or former client without first advising that person in writing that independent representation is appropriate in connection therewith.

(i) A lawyer related to another lawyer as parent, child, sibling or spouse shall not represent a client in a representation directly adverse to a person who the lawyer knows is represented by the other lawyer except upon consent by the client after consultation regarding the relationship.

(j) 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.

## Supreme Court Commentary

### Transactions Between Client and Lawyer

[1] As a general principle, all transactions between client and lawyer should be fair and reasonable to the client. In such transactions a review by independent counsel on behalf of the client is often advisable. Furthermore, a lawyer may not exploit information relating to the representation to the client's disadvantage. For example, a lawyer who has learned that the client is investing in specific real estate may not, without the client's consent, seek to acquire nearby property where doing so would adversely affect the client's plan for investment. Paragraph (a) does not, however, apply to standard commercial transactions between the lawyer and the client for products or services that the client generally markets to others, for example, banking or brokerage services, medical services, products manufactured or distributed by the client, and utilities' services. In such transactions, the lawyer has no advantage in dealing with the client, and the restrictions in paragraph (a) are unnecessary and impracticable.

[2] A lawyer may accept a gift from a client, if the transaction meets general standards of fairness. For example, a simple gift such as a present given at a holiday or as a token of appreciation is permitted. If effectuation of a substantial gift requires preparing a legal instrument such as a will or conveyance, however, the client should have the detached advice that another lawyer can provide. Paragraph (c) recognizes an exception where the client is a relative of the donee or the gift is not substantial.

### Literary Rights

[3] An agreement by which a lawyer acquires literary or media rights concerning the conduct of the representation creates a conflict between the interests of the client and the personal interests of the lawyer. Measures suitable in the representation of the client may detract from the publication value of an account of the representation. Paragraph (d) does not prohibit a lawyer representing a client in a transaction concerning literary property from agreeing that the lawyer's fee shall consist of a share in ownership in the property, if the arrangement conforms to Rule 1.5 and paragraph (j).

### Person Paying for Lawyer's Services

[4] Paragraph (f) requires disclosure of the fact that the lawyer's services are being paid for by a third party unless such payment is provided for in an agreement between the client and the third party. Such an arrangement must also conform to the requirements of Rule 1.6 concerning confidentiality and Rule 1.7 concerning conflict of interest. Where the client is a class, consent may be obtained on behalf of the class by court-supervised procedure.

#### Limiting Liability

[5] Paragraph (h) is not intended to apply to customary qualifications and limitations in legal opinions and memoranda.

#### Family Relationships Between Lawyers

[6] Paragraph (i) applies to related lawyers who are in different firms. Related lawyers in the same firm are governed by Rules 1.7, 1.9, and 1.10. The disqualification stated in paragraph (i) is personal and is not imputed to members of firms with whom the lawyers are associated.

#### Acquisition of Interest in Litigation

[7] Paragraph (j) states the traditional general rule that lawyers are prohibited from acquiring a proprietary interest in litigation. This general rule, which has its basis in common-law champerty and maintenance, is subject to specific exceptions developed in decisional law and continued in these Rules, such as the exception for reasonable contingent fees set forth in Rule 1.5 and the exception for certain advances of the costs of litigation set forth in paragraph (e).

## 2. Proposed Kentucky Rule with Official Comments:

### SCR 3.130(1.8) Conflict of interest: ~~prohibited transactions~~ current clients: specific rules

(a) 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~~ the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted

in writing ~~to the client~~ in a manner ~~which~~ that can be reasonably understood by the client;

(2) ~~The~~ the client is advised in writing of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent legal counsel in on the transaction; and

(3) ~~The~~ the client ~~consents~~ gives informed consent, in a writing ~~thereto~~ signed by the client, to the essential terms of the transaction and the lawyer's role in the transaction, including whether the lawyer is representing the client in the transaction.

(b) A lawyer shall not use information relating to representation of a client to the disadvantage of the client unless the client ~~consents after consultation~~ gives informed consent, except as permitted or required by ~~Rule 1.6 or Rule 3.3~~ these Rules.

(c) A lawyer shall not solicit any substantial gift from a client, including a testamentary gift, or prepare on behalf of a client an instrument giving the lawyer or a person related to the lawyer as ~~parent, child, sibling, or spouse~~ any substantial gift from a client, including a testamentary unless the lawyer or other recipient of the gift, except where the client is related to the donee client. For purposes of this paragraph, related persons include a spouse, child, grandchild, parent, grandparent or other relative or individual with whom the lawyer or the client maintains a close, familial relationship.

(d) Prior 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.

(e) A lawyer shall not provide financial assistance to a client in connection with pending or contemplated litigation, except that:

(1) A a lawyer may advance court costs and expenses of litigation, the repayment of which may be contingent on the outcome of the matter; and

(2) A a lawyer representing an indigent client may pay court costs and expenses of litigation on behalf of the client.

(f) A lawyer shall not accept compensation for representing a client from one

other than the client unless:

(1) ~~Such compensation is in accordance with an agreement between the client and the third party or the client consents after consultation~~ gives informed consent;

(2) ~~There~~ there is no interference with the lawyer's independence of professional judgment or with the client-lawyer relationship; and

(3) ~~Information~~ information relating to representation of a client is protected as required by Rule 1.6.

(g) A lawyer who represents two or more clients shall not participate in making an aggregate settlement of the claims of or against the clients, or in a criminal case an aggregated agreement as to guilty or nolo contendere pleas, unless each client ~~consents after consultation, including~~ gives informed consent, in a writing signed by the client. The lawyer's disclosure of shall include the existence and nature of all the claims or pleas involved and of the participation of each person in the settlement.

(h) A lawyer shall not:

(1) make an agreement prospectively limiting the lawyer's liability to a client for malpractice unless permitted by law and the client is independently represented in making the agreement;<sup>2</sup> or

(2) settle a claim or potential claim for such liability with an unrepresented client or former client without first advising unless that person is advised in writing that of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent representation is appropriate legal counsel in connection therewith.

(i) ~~A lawyer related to another lawyer as parent, child, sibling or spouse shall not represent a client in a representation directly adverse to a person whom the lawyer knows is represented by the other lawyer except upon consent by the client after consultation regarding the relationship.~~

~~(j)~~ (i) 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~~ acquire a lien ~~granted~~ authorized by law to secure the lawyer's fee or expenses; and

(2) ~~Contract~~ contract with a client for a reasonable contingent fee in a civil case.

(j) A lawyer shall not have sexual relations with a client unless a consensual sexual relationship existed between them when the client-lawyer relationship commenced.

(k) While lawyers are associated in a firm, a prohibition in the foregoing paragraphs (a) through (i) that applies to any one of them shall apply to all of them.

### Supreme Court Commentary Comment

#### Business Transactions Between Client and Lawyer

[1] ~~As a general principle, all transactions between client and lawyer should be fair and reasonable to the client. In such transactions a review by independent counsel on behalf of the client is often advisable. Furthermore, a lawyer may not exploit information relating to the representation to the client's disadvantage. For example, a lawyer who has learned that the client is investing in specific real estate may not, without the client's consent, seek to acquire nearby property where doing so would adversely affect the client's plan for investment. Paragraph (a) A lawyer's legal skill and training, together with the relationship of trust and confidence between lawyer and client, create the possibility of overreaching when the lawyer participates in a business, property or financial transaction with a client, for example, a loan or sales transaction or a lawyer investment on behalf of a client. The requirements of paragraph (a) must be met even when the transaction is not closely related to the subject matter of the representation, as when a lawyer drafting a will for a client learns that the client needs money for unrelated expenses and offers to make a loan to the client. It also applies to lawyers purchasing property from estates they represent. It does not apply to ordinary fee arrangements between client and lawyer, which are governed by Rule 1.5, although its requirements must be met when the lawyer accepts an interest in the client's business or other nonmonetary property as payment of all or part of a fee. In addition, the Rule does not, however, apply to standard commercial transactions between the lawyer and the client for products or services that the client generally markets to others, for example, banking or brokerage services, medical services,~~

products manufactured or distributed by the client, and utilities' services. In such transactions, the lawyer has no advantage in dealing with the client, and the restrictions in paragraph (a) are unnecessary and impracticable.

[2] Paragraph (a)(1) requires that the transaction itself be fair to the client and that its essential terms be communicated to the client, in writing, in a manner that can be reasonably understood. Paragraph (a)(2) requires that the client also be advised, in writing, of the desirability of seeking the advice of independent legal counsel. It also requires that the client be given a reasonable opportunity to obtain such advice. Paragraph (a)(3) requires that the lawyer obtain the client's informed consent, in a writing signed by the client, both to the essential terms of the transaction and to the lawyer's role. When necessary, the lawyer should discuss both the material risks of the proposed transaction, including any risk presented by the lawyer's involvement, and the existence of reasonably available alternatives and should explain why the advice of independent legal counsel is desirable. See Rule 1.0(e) (definition of informed consent).

[3] The risk to a client is greatest when the client expects the lawyer to represent the client in the transaction itself or when the lawyer's financial interest otherwise poses a significant risk that the lawyer's representation of the client will be materially limited by the lawyer's financial interest in the transaction. Here the lawyer's role requires that the lawyer must comply, not only with the requirements of paragraph (a), but also with the requirements of Rule 1.7. Under that Rule, the lawyer must disclose the risks associated with the lawyer's dual role as both legal adviser and participant in the transaction, such as the risk that the lawyer will structure the transaction or give legal advice in a way that favors the lawyer's interests at the expense of the client. Moreover, the lawyer must obtain the client's informed consent. In some cases, the lawyer's interest may be such that Rule 1.7 will preclude the lawyer from seeking the client's consent to the transaction.

[4] If the client is independently represented in the transaction, paragraph (a)(2) of this Rule is inapplicable, and the paragraph (a)(1) requirement for full disclosure is satisfied either by a written disclosure by the lawyer involved in the transaction or by the client's independent counsel. The fact that the client was independently represented in the

transaction is relevant in determining whether the agreement was fair and reasonable to the client as paragraph (a)(1) further requires.

### Use of Information Related to Representation

[5] Use of information relating to the representation to the disadvantage of the client violates the lawyer's duty of loyalty. Paragraph (b) applies when the information is used to benefit either the lawyer or a third person, such as another client or business associate of the lawyer. For example, if a lawyer learns that a client intends to purchase and develop several parcels of land, the lawyer may not use that information to purchase one of the parcels in competition with the client or to recommend that another client make such a purchase. The Rule does not prohibit uses that do not disadvantage the client. For example, a lawyer who learns a government agency's interpretation of trade legislation during the representation of one client may properly use that information to benefit other clients. Paragraph (b) prohibits disadvantageous use of client information unless the client gives informed consent, except as permitted or required by these Rules. See Rules 1.2(d), 1.6, 1.9(c), 3.3, 4.1(b), 8.1 and 8.3.

### Gifts to Lawyers

~~[2]~~ [6] A lawyer may accept a gift from a client, if the transaction meets general standards of fairness. For example, a simple gift such as a present given at a holiday or as a token of appreciation is permitted. If a client offers the lawyer a more substantial gift, paragraph (c) does not prohibit the lawyer from accepting it, although such a gift may be voidable by the client under the doctrine of undue influence, which treats client gifts as presumptively fraudulent. In any event, due to concerns about overreaching and imposition on clients, a lawyer may not suggest that a substantial gift be made to the lawyer or for the lawyer's benefit, except where the lawyer is related to the client as set forth in paragraph (c).

~~[2]~~[7] If effectuation of a substantial gift requires preparing a legal instrument such as a will or conveyance, however, the client should have the detached advice that another lawyer can provide. Paragraph (c) recognizes an The sole exception to this Rule is where the client is a relative of the donee or the gift is not substantial.

[8] This Rule does not prohibit a lawyer from seeking to have the lawyer or a

partner or associate of the lawyer named as executor of the client's estate or to another potentially lucrative fiduciary position. Nevertheless, such appointments will be subject to the general conflict of interest provision in Rule 1.7 when there is a significant risk that the lawyer's interest in obtaining the appointment will materially limit the lawyer's independent professional judgment in advising the client concerning the choice of an executor or other fiduciary. In obtaining the client's informed consent to the conflict, the lawyer should advise the client concerning the nature and extent of the lawyer's financial interest in the appointment, as well as the availability of alternative candidates for the position.

### **Literary Rights**

~~[3]~~ [9] An agreement by which a lawyer acquires literary or media rights concerning the conduct of the representation creates a conflict between the interests of the client and the personal interests of the lawyer. Measures suitable in the representation of the client may detract from the publication value of an account of the representation. Paragraph (d) does not prohibit a lawyer representing a client in a transaction concerning literary property from agreeing that the lawyer's fee shall consist of a share in ownership in the property, if the arrangement conforms to Rule 1.5 and ~~paragraph (j)~~ paragraphs (a) and (i).

### **Financial Assistance**

[10] Lawyers may not subsidize lawsuits or administrative proceedings brought on behalf of their clients, including making or guaranteeing loans to their clients for living expenses, because to do so would encourage clients to pursue lawsuits that might not otherwise be brought and because such assistance gives lawyers too great a financial stake in the litigation. These dangers do not warrant a prohibition on a lawyer lending a client court costs and litigation expenses, including the expenses of medical examination and the costs of obtaining and presenting evidence, because these advances are virtually indistinguishable from contingent fees and help ensure access to the courts. Similarly, an exception allowing lawyers representing indigent clients to pay court costs and litigation expenses regardless of whether these funds will be repaid is warranted.

### **Person Paying for a Lawyer's Services**

~~[4] Paragraph (f) requires disclosure of the fact that the lawyer's services are being paid for by a third party. Such an arrangement must also conform to the requirements of Rule 1.6 concerning confidentiality and Rule 1.7 concerning conflict of interest. Where the client is a class, consent may be obtained on behalf of the class by court-supervised procedure.~~

[11] Lawyers are frequently asked to represent a client under circumstances in which a third person will compensate the lawyer, in whole or in part. The third person might be a relative or friend, an indemnitor (such as a liability insurance company) or a co-client (such as a corporation sued along with one or more of its employees). Because third-party payers frequently have interests that differ from those of the client, including interests in minimizing the amount spent on the representation and in learning how the representation is progressing, lawyers are prohibited from accepting or continuing such representations unless the lawyer determines that there will be no interference with the lawyer's independent professional judgment and there is informed consent from the client. See also Rule 5.4(c) (prohibiting interference with a lawyer's professional judgment by one who recommends, employs or pays the lawyer to render legal services for another).

[12] Sometimes, it will be sufficient for the lawyer to obtain the client's informed consent regarding the fact of the payment and the identity of the third-party payer. If, however, the fee arrangement creates a conflict of interest for the lawyer, then the lawyer must comply with Rule 1.7. The lawyer must also conform to the requirements of Rule 1.6 concerning confidentiality. Under Rule 1.7(a), a conflict of interest exists if there is significant risk that the lawyer's representation of the client will be materially limited by the lawyer's own interest in the fee arrangement or by the lawyer's responsibilities to the third-party payer (for example, when the third-party payer is a co-client). Under Rule 1.7(b), the lawyer may accept or continue the representation with the informed consent of each affected client, unless the conflict is nonconsentable under that paragraph. Under Rule 1.7(b), the informed consent must be confirmed in writing.

### Aggregate Settlements

[13] Differences in willingness to make or accept an offer of settlement are among the risks of common representation of multiple clients by a single lawyer. Under Rule 1.7, this

is one of the risks that should be discussed before undertaking the representation, as part of the process of obtaining the clients' informed consent. In addition, Rule 1.2(a) protects each client's right to have the final say in deciding whether to accept or reject an offer of settlement and in deciding whether to enter a guilty or nolo contendere plea in a criminal case. The Rule stated in this paragraph is a corollary of both these Rules and provides that, before any settlement offer or plea bargain is made or accepted on behalf of multiple clients, the lawyer must inform each of them about all the material terms of the settlement, including what the other clients will receive or pay if the settlement or plea offer is accepted. See also Rule 1.0(e) (definition of informed consent). Lawyers representing a class of plaintiffs or defendants, or those proceeding derivatively, may not have a full client-lawyer relationship with each member of the class; nevertheless, such lawyers must comply with applicable rules regulating notification of class members and other procedural requirements designed to ensure adequate protection of the entire class.

#### Limiting Liability and Settling Malpractice Claims

~~[5] Paragraph (h) is not intended to apply to customary qualifications and limitations in legal opinions and memoranda.~~

[14] Agreements prospectively limiting a lawyer's liability for malpractice are prohibited unless the client is independently represented in making the agreement because they are likely to undermine competent and diligent representation. Also, many clients are unable to evaluate the desirability of making such an agreement before a dispute has arisen, particularly if they are then represented by the lawyer seeking the agreement. This paragraph does not, however, prohibit a lawyer from entering into an agreement with the client to arbitrate legal malpractice claims, provided such agreements are enforceable and the client is fully informed of the scope and effect of the agreement. Nor does this paragraph limit the ability of lawyers to practice in the form of a limited-liability entity, where permitted by law, provided that each lawyer remains personally liable to the client for his or her own conduct and the firm complies with any conditions required by law, such as provisions requiring client notification or maintenance of adequate liability insurance. Nor does it prohibit an agreement in accordance with Rule 1.2 that defines the scope of the representation, although a definition of scope that makes the obligations of representation

illusory will amount to an attempt to limit liability.

[15] Agreements settling a claim or a potential claim for malpractice are not prohibited by this Rule. Nevertheless, in view of the danger that a lawyer will take unfair advantage of an unrepresented client or former client, the lawyer must first advise such a person in writing of the appropriateness of independent representation in connection with such a settlement. In addition, the lawyer must give the client or former client a reasonable opportunity to find and consult independent counsel.

#### **Family Relationships Between Lawyers**

~~[6] Paragraph (i) applies to related lawyers who are in different firms. Related lawyers in the same firm are governed by Rules 1.7, 1.9, and 1.10. The disqualification stated in paragraph (i) is personal and is not imputed to members of firms with whom the lawyers are associated.~~

#### **Acquisition of Acquiring Proprietary Interest in Litigation**

~~[7] [16] Paragraph (j) (i) states the traditional general rule that lawyers are prohibited from acquiring a proprietary interest in litigation. This Like paragraph (e), the general rule, which has its basis in common law champerty and maintenance, and is designed to avoid giving the lawyer too great an interest in the representation. In addition, when the lawyer acquires an ownership interest in the subject of the representation, it will be more difficult for a client to discharge the lawyer if the client so desires. The Rule is subject to specific exceptions developed in decisional law and continued in these Rules, such as the exception for reasonable contingent fees set forth in Rule 1.5 and the exception for certain advances of the costs of litigation set forth in paragraph (e). The exception for certain advances of the costs of litigation is set forth in paragraph (e). In addition, paragraph (i) sets forth exceptions for liens authorized by law to secure the lawyer's fees or expenses and contracts for reasonable contingent fees. The law of each jurisdiction determines which liens are authorized by law. These may include liens granted by statute, liens originating in common law and liens acquired by contract with the client. When a lawyer acquires by contract a security interest in property other than that recovered through the lawyer's efforts in the litigation, such an acquisition is a business or financial transaction with a client and is governed by the requirements of paragraph (a).~~

Contracts for contingent fees in civil cases are governed by Rule 1.5.

### Client-Lawyer Sexual Relationships

[17] The relationship between lawyer and client is a fiduciary one in which the lawyer occupies the highest position of trust and confidence. The relationship is almost always unequal; thus, a sexual relationship between lawyer and client can involve unfair exploitation of the lawyer's fiduciary role, in violation of the lawyer's basic ethical obligation not to use the trust of the client to the client's disadvantage. In addition, such a relationship presents a significant danger that, because of the lawyer's emotional involvement, the lawyer will be unable to represent the client without impairment of the exercise of independent professional judgment. Moreover, a blurred line between the professional and personal relationships may make it difficult to predict to what extent client confidences will be protected by the attorney-client evidentiary privilege, since client confidences are protected by privilege only when they are imparted in the context of the client-lawyer relationship. Because of the significant danger of harm to client interests and because the client's own emotional involvement renders it unlikely that the client could give adequate informed consent, this Rule prohibits the lawyer from having sexual relations with a client regardless of whether the relationship is consensual and regardless of the absence of prejudice to the client.

[18] Sexual relationships that predate the client-lawyer relationship are not prohibited. Issues relating to the exploitation of the fiduciary relationship and client dependency are diminished when the sexual relationship existed prior to the commencement of the client-lawyer relationship. However, before proceeding with the representation in these circumstances, the lawyer should consider whether the lawyer's ability to represent the client will be materially limited by the relationship. See Rule 1.7(a)(2).

[19] When the client is an organization, paragraph (j) of this Rule prohibits a lawyer for the organization (whether inside counsel or outside counsel) from having a sexual relationship with a constituent of the organization who supervises, directs or regularly consults with that lawyer concerning the organization's legal matters.

### Imputation of Prohibitions

[20] Under paragraph (k), a prohibition on conduct by an individual lawyer in paragraphs (a) through (i) also applies to all lawyers associated in a firm with the personally prohibited lawyer. For example, one lawyer in a firm may not enter into a business transaction with a client of another member of the firm without complying with paragraph (a), even if the first lawyer is not personally involved in the representation of the client. The prohibition set forth in paragraph (j) is personal and is not applied to associated lawyers.

### 3. Discussion and Explanation of Recommendation:

#### a. Comparison of proposed Kentucky Rule with its counterpart ABA Model Rule.

The ABA Reporter's Explanation of Changes to MR 1.8 expresses the Committee's view. It is adopted by the Committee for purposes of explaining in detail recommended changes and is quoted below. Note that paragraph (j) and Comments [17], [18] and [19] on client-lawyer sexual relationships are new with no counterpart Rule or Comments in the current KRPC 1.8.

- ABA Reporter's Explanation of Changes -- Model Rule 1.8

Caption: Change to "Conflict of Interest: Current Clients: Specific Rules."

The caption has been changed to parallel the change in Rule 1.7 and to more accurately reflect the scope of the Rule.

Rule 1.8(a): Business Transactions between Client and Lawyer

TEXT:

#### 1. Paragraph (a)(1): Stylistic changes

The changes to this paragraph are grammatical and stylistic. No change in substance is intended.

#### 2. Paragraph (a)(2): Client to be advised in writing of desirability of seeking counsel

The Commission recommends adding a requirement that the client be advised in writing of the desirability of seeking the advice of independent legal counsel, in addition to affording the client a reasonable opportunity to seek such counsel. A number of jurisdictions have adopted such a requirement. The Commission believes these additional requirements are

necessary for the protection of clients; moreover, some are already imposed by common law decisions providing for the voidability of such transactions by clients.

### 3. Paragraph (a)(3): Informed consent to essential terms of transaction and lawyer's role

The Commission recommends clarifying the nature of the consent to be given by the client under this paragraph. Lawyers have reported considerable confusion regarding its meaning. Several states have specified that the consent refers to the essential terms of the transaction. Case law in some jurisdictions goes further and requires disclosure regarding the risks of the transaction. The Commission recommends informed consent to both the terms of the transaction and the lawyer's role, including whether the lawyer is representing the client in the transaction.

### 4. Paragraph (a)(3): Informed consent in writing signed by client

The Commission is proposing a number of revisions to the Rules that would require the lawyer to document certain communications or agreements in writing. The Commission believes that it should be clear in all instances what type of writing is required, particularly whether the writing needs to be signed by the client. Certain terms are defined in Rule 1.0, including the term "writing." Because there are only a few instances in which a client's signature is required, the Commission is recommending that those instances be clearly stated in the text of the Rule. The Commission believes that, because of the risk of overreaching in business transactions between lawyers and clients, the client's informed consent to both the essential terms of the transaction and the lawyer's role should be obtained in a writing signed by the client.

COMMENT:

Caption: "Business" was added to the caption to clarify its meaning.

[1] This Comment was revised to state the rationale for the Rule and to clarify which transactions are covered.

[2] This new Comment emphasizes that the lawyer must comply with the requirements of all three subparagraphs. It also elaborates on the nature of the disclosure the lawyer must make under paragraph (a)(3), including a cross reference to Rule 1.0(e), which gives the general definition of informed consent.

[3] This new Comment clarifies the relationship between Rules 1.8(a) and 1.7, which has not been well understood by lawyers. Both Rules apply whenever the client reasonably expects that the lawyer is representing the client in the transaction itself or when the lawyer's financial interest in the transaction otherwise creates a significant risk to the lawyer's representation of the client in another matter. Thus, Rule 1.8(a) focuses on the risks of the transaction itself, whereas Rule 1.7 focuses on the risks of the representation.

[4] This new Comment clarifies how paragraph (a) applies when the client is represented by independent counsel in the transaction.

#### Rule 1.8(b): Use of Information Related to Representation

TEXT:

1. Replace "consent after consultation" with "gives informed consent"

The Commission is recommending that throughout the Rules the phrase "consent after consultation" be replaced with "gives informed consent," as defined in Rule 1.0(e). No change in substance is intended.

2. Replace "Rule 1.6 or Rule 3.3" with "these Rules"

The Commission recommends that the enumeration of applicable Rules should be in Commentary rather than in text. No change in substance is intended.

COMMENTARY:

Caption: The caption was added to set off new Comment [5].

[5] This new Comment states the rationale for the Rule and gives examples of both prohibited and permissible uses of information relating to the representation.

#### Rule 1.8(c): Gifts to Lawyers

TEXT:

1. Add prohibition on lawyer solicitation of substantial gifts:

The Commission recommends adding a prohibition on a lawyer soliciting a substantial gift from a client, in order to avoid the danger of overreaching. The current Rule has been criticized for regulating gifts made by instrument but not those made in other ways.

2. Change in definition of relationships that fall within the exception for lawyers related to client or donee

The Commission has retained the exception for related lawyers. It is recommending changes to clarify that the same degree of relatedness applies in determining whether the donee is related to both the lawyer and the client and to adopt the more expansive and flexible definition of the ABA Model Code of Judicial Conduct (defining "member of the judge's family").

COMMENTARY:

Caption: The caption has been added to set off the following Comments.

[6] Current Comment [2] has been revised to reflect the Commission's decision to prohibit lawyer solicitation of nontestamentary gifts, except when such gifts are insubstantial. It also reminds lawyers that, while the Rule does not prohibit lawyers from accepting substantial gifts not solicited by the lawyer, such gifts may be voidable by the client under the doctrine of undue influence.

[7] This Comment is also based on current Comment [2]. The changes are stylistic. No change in substance is intended.

[8] This new Comment clarifies a present ambiguity by addressing the question of whether appointment of the lawyer or the lawyer's firm as executor constitutes a "substantial gift" within the meaning of this Rule. The Commission believes that such appointments are not "gifts" but that they may create a conflict of interest between the client and the lawyer that would be governed by Rule 1.7.

Rule 1.8(d): Literary Rights

TEXT:

No change recommended.

COMMENTARY:

[9] The sole revision to current Comment [3] adds an additional cross reference to Rule 1.8(a).

Proposed Rule 1.8(e): Financial Assistance

TEXT:

No change recommended.

COMMENTARY:

Caption: The caption has been added to set off the new Comment [10]. This new Comment states the rationale for the Rule, explains that it covers both making and guaranteeing loans and indicates more specifically the kind of expenses that lawyers are permitted to advance. No change in substance is intended.

Rule 1.8(f): Person Paying for Lawyer's Services

TEXT:

Change "consents after consultation" to "gives informed consent"

The Commission is recommending that throughout the Rules the phrase "consent after consultation" be replaced with "gives informed consent," as defined in Rule 1.0(e). No change in substance is intended.

COMMENTARY:

[11] This new Comment replaces current Comment [4]. It presents a more detailed explanation of the rationale for and requirements of the Rule. It also clarifies that a client who pays for the representation of a co client is governed by this Rule. Finally, it adds a cross reference to Rule 5.4(c).

[12] This new Comment explains the relationship between this Rule and Rule 1.7.

Rule 1.8(g): Aggregate Settlements

TEXT:

1. Replace "consents after consultation" with "gives informed consent"

The Commission is recommending that throughout the Rules the phrase "consent after consultation" be replaced with "gives informed consent," as defined in Rule 1.0(e). No change in substance is intended.

2. Client consent required to be "in a writing signed by the client"

The Commission is proposing a number of revisions to the Rules that would require the

lawyer to document certain communications or agreements in writing. The Commission believes that it should be clear in all instances what type of writing is required, particularly, whether the writing needs to be signed by the client. Certain terms are defined in Rule 1.0, including the term "writing." Because there are only a few instances in which a client's signature is required, the Commission is recommending that those instances be clearly stated in the text of the Rule. The Commission believes that because aggregate settlements entail settlement offers posing potentially serious conflicts of interest between the clients, each client's informed consent should be obtained in a writing signed by the client.

COMMENTARY:

Caption: The caption has been added to set off the new Comment.

[13] This new Comment states the rationale for the Rule, which is an application of Rules 1.7 and 1.2. In addition, it reminds lawyers involved in class actions that, while this Rule does not apply, lawyers must comply with procedural requirements regarding notification of the class.

Rule 1.8(h): Limiting Liability and Settling Malpractice Claims

TEXT:

1. Break Rule into two paragraphs

The purpose of this change is to clarify the two separate obligations under this Rule. No change in substance is intended.

2. Paragraph (h)(1): Delete "unless permitted by law"

The Commission is unaware of any statute or case law that addresses the question of whether such agreements should be permitted. Given that the phrase "unless permitted by law" appears to play no significant role in addressing these conflicts, the Commission is recommending that such agreements be permitted when the client is independently represented. The Commission believes that there may be good reasons to permit a lawyer to limit liability prospectively and that the client is adequately protected when represented by independent counsel.

### 3. Paragraph (h)(2): Add "potential claim"

The purpose of this change is to clarify that the Rule applies even when the client has not actually asserted a claim, for example, when the lawyer asks the client to sign a release as part of settling a dispute over legal fees.

### 4. Paragraph (h)(2): Reword advice to obtain independent counsel

The purpose of this change is to conform the language to that used in Rule 1.8(a). No change in substance is intended.

#### COMMENTARY:

Caption: The caption has been changed to better reflect the two separate obligations in the Rule.

[14] This new Comment states the rationale for paragraph (h)(1). It also addresses three questions that frequently arise concerning the application of the Rule whether the Rule prohibits agreements requiring arbitration of a legal malpractice claim, whether the Rule applies to lawyers practicing in limited liability entities and whether the Rule prohibits agreements limiting the scope of the representation.

[15] This new Comment states the rationale for paragraph (h)(2).

#### Deletion of Current Rule 1.8(i): Family Relationships between Lawyers

#### TEXT:

At the time this Rule was first enacted, there was concern that lawyer spouses would be unable to find employment in different firms in the same city because of the fear that one spouse's conflicts would result in the disqualification of the other spouse's law firm. Thus, the primary purpose for treating such conflicts under Rule 1.8 rather than Rule 1.7 was to avoid the imputation of the conflict under Rule 1.10. The Rule, however, is both under and over inclusive. It is underinclusive because it does not address personal interest conflicts arising from close family or family like relationships other than those enumerated in the Rule, such as couples who live together in a relationship approximating marriage. Moreover, it is limited to directly adverse conflicts and does not include material limitation conflicts, for example when lawyer spouses represent coplaintiffs or codefendants with

significantly different positions in the litigation. The Rule is overinclusive because it permits the representation with the consent of the client, regardless of whether the conflict would otherwise be deemed nonconsentable under Rule 1.7. Moreover, while imputation is unnecessary in most cases, in some instances it may be indicated. Under the changes proposed for Rule 1.10, personal interest conflicts are not imputed unless they present a significant risk of materially limiting the representation of the client by the remaining lawyers in the firm. As a result of these changes, the Commission is recommending deletion of this Rule and the addition of a Comment to Rule 1.7 addressing conflicts of interest arising from a lawyer's family relationships. See Rule 1.7, Comment [11].

COMMENTARY:

[6] The Commission is proposing deleting this Comment and the associated caption along with the text.

#### Rule 1.8(i): Acquiring Proprietary Interest in Litigation

TEXT:

Substitute "authorized by law" for "granted by law"

The purpose of this change is to clarify that the exemption applies to all liens authorized by substantive law, including those liens that are contractual in nature.

COMMENTARY:

Caption: The caption has been changed to better reflect the meaning of the Rule.

[16] This expanded Comment further explains the rationale for the Rule and adds a cross reference to Rule 1.8(a), which will apply when a lawyer acquires by contract a security interest in property other than that recovered through the lawyer's effort in the litigation.

#### Rule 1.8(j): Client Lawyer Sexual Relationships

TEXT:

Adopt new per se Rule prohibiting most client lawyer sexual relationships

The Commission recommends following the lead of a number of jurisdictions that have adopted Rules explicitly regulating client lawyer sexual conduct. Although recognizing that most egregious behavior of lawyers can be addressed through other Rules, the

Commission believes that such Rules may not be sufficient. Given the number of complaints of lawyer sexual misconduct that have been filed, the Commission believes that having a specific Rule has the advantage not only of alerting lawyers more effectively to the dangers of sexual relationships with clients but also of alerting clients that the lawyer may have violated ethical obligations in engaging in such conduct.

The Commission further recommends a total, rather than a partial, ban on client lawyer relationships, except for those pre-dating the formation of the client lawyer relationship. Partial bans, i.e., those that prohibit relationships only when they involve coercion or cause the lawyer to act incompetently, do not effectively address the problem of conflicts of interest, particularly the difficulty of obtaining an adequately informed consent from the client. Moreover, they do little to prevent problems from arising in the first place.

COMMENTARY:

Caption: The caption has been added to set off the new Comments.

[17] This new Comment states the rationale for the Rule.

[18] This new Comment states the rationale for the Rule's exception for pre existing relationships, noting that even though the Rule does not apply, such relationships may give rise to conflicts of interest under Rule 1.7.

[19] This new Comment was added to explain how the Rule is applied in the case of an organizational client.

Paragraph (k): Imputation of Prohibitions

TEXT:

1. Treat imputation under Rule 1.8 rather than 1.10

The Commission is recommending that imputation of the prohibitions in Rule 1.8 be addressed by Rule 1.8 rather than by Rule 1.10. Under paragraph (k), an associated lawyer may not necessarily proceed with the informed consent of the client (as the lawyer could under Rule 1.10); moreover, there is no exception here (as there is in Rule 1.10) for personal interest conflicts of the individually disqualified lawyer.

## 2. Impute all prohibitions except paragraph (j)

Under current Rule 1.10, only the prohibition of paragraph (c) (gifts to lawyers) is imputed to other lawyers in a firm. The Commission recommends that the prohibition of all paragraphs except (j) be so imputed.

COMMENTARY:

Caption: The caption has been added to set off the new Comment.

[20] This new Comment explains the rationale for paragraph (k).

### b. Detailed discussion of reason for variance from ABA Model Rule (if any).

There is no variance in proposed KRPC 1.8 from MR 1.8.

#### Dissent and Committee Response

Committee member Peter L. Ostermiller dissents from the Committee Rule 1.8(e) recommendation. His dissenting opinion is inserted here for consideration by the reviewing authorities. The results of the Committee's consideration of this dissent follow the opinion.

Rule 1.8(e) addresses the issue of a lawyer's financial assistance to a client in connection with pending or contemplated litigation.

The current Rule in Kentucky, and the recommendation of the majority of the Committee, is to continue the prohibition against any financial assistance to a client except for the lawyer's payment of court costs and expenses, the repayment of which may be contingent upon the outcome of the litigation.

The alternate proposal, which is the subject of this Dissent, would provide a limited lifting of the prohibition against a lawyer providing financial assistance to a client. The alternate proposal would incorporate language adopted in Alabama, Minnesota and Texas. The alternate proposal would authorize, with limitations, emergency financial assistance, in addition to advancing court costs and expenses in litigation.

Model Rule 1.8(e), as does Kentucky's existing SCR 3.130(1.8(e)), continues the prohibition of a lawyer providing financial assistance to a client regarding a pending or contemplated lawsuit except as to advancing "court costs and expenses in litigation."

“Expenses of litigation” may include expenses advanced by the lawyer without any expectation of repayment by the client in the event the lawsuit is unsuccessful. Such amounts may run into the thousands, tens of thousands and, in some litigation, i.e., medical malpractice or products liability cases, into the hundreds of thousands of dollars of money paid by the attorney. For all practical purposes, unless there is a recovery in the litigation, the attorney will be out those costs.

Logically, and as a matter of common sense, if, for example, an attorney may advance \$50,000.00 in litigation expenses, (which will only be recovered if the lawsuit is successful), by a parity of reasoning, the attorney should also be able to advance reasonable and necessary living expenses to a client, or, at the very least, advance emergency expenses.

Defendants in personal injury litigation, including products liability litigation, medical malpractice, complex tort litigation, etc., are typically either corporate or organizational defendants or are parties whose defense is funded by an insurance company. Correspondingly, plaintiffs in such litigation are typically individuals with limited financial resources. But for the availability of contingent fee arrangements, the injured person would not be able to pursue litigation against the potential tortfeasors.

The existing language in Rule 1.8(e) is illogical and anti-consumer. An attorney’s payment of emergency living expenses will not, in any material manner, put any pressure on an attorney to resolve particular litigation. Under the current mechanism authorized under Rule 1.8(e), an attorney may incur hundreds of thousands of dollars of expenses in litigation. If the policy consideration behind prohibiting an attorney from advancing living expenses to a client is to avoid having the lawyer be under pressure to settle a case to recover the expenses advanced, that is a problem that currently exists, if it is a problem, under the current version of Rule 1.8(e). The ultimate proposal set forth in this Dissent merely seeks to place all parties in such litigation on an equal footing.

This Dissent recognizes the policy considerations against permitting an attorney to provide general and non-emergency financial assistance to a client concerning a potential or pending lawsuit. However, there are emergency and non-reoccurring instances where such financial assistance would be in the best interest of the client and would preclude a

client from being put in the position of having to settle litigation for an unreasonably low amount in order to avoid a current financial emergency. The alternate proposal set out in this Dissent seeks to pull the best language from those States which have adopted similar provisions in order to address legitimate policy concerns.

Several States, i.e., Texas, Minnesota and Alabama, have adopted provisions authorizing financial assistance to clients otherwise prohibited by the existing Rule 1.8(e). The text of those Rules, and the Commentary, if any, is set out below.

## ALABAMA

### Alabama Rule of Professional Conduct 1.8(e)(3)

#### Emergency Financial Assistance:

A lawyer may advance or guarantee emergency financial assistance to the client, the repayment of which may not be contingent on the outcome of the matter, provided that no promise or assurance of financial assistance was made to the client by the lawyer, or on the lawyer's behalf, prior to the employment of the lawyer.

#### Commentary

On occasion, a client of a lawyer may suffer a financial emergency. The client may be totally unable to turn to traditional sources of emergency financial assistance such as banks, families, or neighbors to obtain necessary assistance in meeting such a financial emergency. While the client may have an expectation that a recovery in a pending lawsuit would provide ample funds from which to repay a loan, the collateralization of a loan with the anticipated proceeds of litigation is not generally accepted as a good business practice. In these circumstances, the only alternative to whom the client may realistically be able to turn is the lawyer handling the lawsuit. For true financial emergencies, arising from circumstances beyond the control of the client, the Rule permits the lawyer either to advance a loan to the client or to guarantee the repayment of a loan by a third party to the client.

A lawyer departs from the role of advocate when the lawyer becomes a lender to the client. The lawyer as lender is placed in a position adverse to the client, particularly if the client refuses to repay. Since the repayment by the client may not be contingent on the

outcome of a matter, the client is always responsible for repayment of any loan, whether the client wins or loses the pending lawsuit.

Rule 1.8(e)(3) permits the lawyer to act as both advocate for and lender to the client under only the narrowest and most compelling of circumstances. The lawyer must not, prior to employment, directly or indirectly have assured the client of the availability of emergency financial assistance. The assistance must meet a true emergency. Emergency financial assistance does not include the regular provision of income and support to a client. Rather, the Rule is intended to permit the lawyer to help in those few cases which rise to the level of an emergency. The lawyer is never obligated to provide such assistance, and he is obligated to attempt collection from the client regardless of the outcome of the matter.

## MINNESOTA

### Minnesota Rule of Professional Conduct 1.8(8)

#### Loan Guarantee:

A lawyer may guarantee a loan reasonably needed to enable the client to withstand delay in litigation that would otherwise put substantial pressure on the client to settle a case because of financial hardship rather than on the merits, provided the client remains ultimately liable for repayment of the loan without regard to the outcome of the litigation and, further provided, that no promise of such financial assistance was made to the client by the lawyer, or by another in the lawyer's behalf, prior to the employment of that lawyer by that client.

## TEXAS

### Texas Disciplinary Rules of Professional Conduct 1.08(d)(1)

#### Advance or Guarantee Medical and Living Expenses:

A lawyer may advance or guarantee court costs, expenses of litigation or administrative proceedings, and reasonably necessary medical and living expenses, the repayment of which may be contingent on the outcome of the matter.

## ALTERNATE PROPOSAL TO SCR 3.130-1.8(e)

The following alternate proposal seeks to pull the most appropriate language from the above-mentioned jurisdictions which have adopted similar language, while at the same time, providing that such emergency assistance will be the exception and not the rule. The alternate proposal also contains language to preclude any reasonable potential for abuse by lawyers and clients.

The following alternate proposal would add a new subsection (3) to SCR 3.130-1.8(e), which would read as follows:

“(3) Emergency Financial Assistance:

A. A lawyer may advance or guarantee emergency financial assistance to, or on behalf of, the client reasonably needed to enable the client to withstand delay in litigation that would otherwise put substantial pressure on the client to settle a case because of financial hardship rather than on the merits.

B. The client remains ultimately liable for repayment of any such assistance, without regard to the outcome of the litigation. The lawyer shall not waive, directly or indirectly, nor may the lawyer excuse, directly or indirectly, the client from the repayment of any such assistance.

C. No promise or assurance of such assistance shall be made to the client by the lawyer, or on the lawyer’s behalf, before the employment of the lawyer.

D. Any such extension of assistance by the lawyer to, or on behalf of, the client shall be reflected to writing and signed by the lawyer and the client before any such assistance is provided.”

Committee Consideration of the Dissent to its Recommendation: The dissent presents the argument for extending emergency financial assistance that has been the subject of considerable discussion in professional responsibility circles for some time and has been implemented in some jurisdictions. It is a serious matter and warrants consideration for inclusion in the KRPC as recommended in the dissent. The majority of the Committee, however, agreed with the MR position that “emergency financial assistance” carries too much risk of encouraging frivolous law suits and giving lawyers too much of a financial stake in the litigation. This policy is expressed in proposed Comment [10] above and

repeated here for convenience:

[10] Lawyers may not subsidize lawsuits or administrative proceedings brought on behalf of their clients, including making or guaranteeing loans to their clients for living expenses, because to do so would encourage clients to pursue lawsuits that might not otherwise be brought and because such assistance gives lawyers too great a financial stake in the litigation. These dangers do not warrant a prohibition on a lawyer lending a client court costs and litigation expenses, including the expenses of medical examination and the costs of obtaining and presenting evidence, because these advances are virtually indistinguishable from contingent fees and help ensure access to the courts. Similarly, an exception allowing lawyers representing indigent clients to pay court costs and litigation expenses regardless of whether these funds will be repaid is warranted.

It is noteworthy that in response to this issue some lending institutions have programs to assist persons requiring living expenses pending litigation. While such programs are subject to abuse, they show that there are reasonable alternative ways for an indigent with a meritorious claim to acquire living expenses without entangling a lawyer in problematic financial arrangements.

**Committee proposal adopted without change. Order 2009-05, eff 7-15-09.**