Risky Business: Attorney-Client Business Transactions

Overcoming the Presumption of Undue Influence is often difficult

By Edward J. Rolwes

Attorneys are required to exercise a higher level of good faith when they deal with a client than parties who simply deal with each other at arm's length. Lawyers who enter into business transactions with their clients bear a heavy burden of overcoming the presumption that the transaction stemmed from the lawyers exercise of undue influence and that they complied with specific ethics rules in this area. As a practical matter, although not required, no attorney should do business with their client unless the client has independent counsel.

Most of the case law regarding attorney-client transactions involve attorneys who drafted a will or other instrument, such as a deed, for the client which left some of the client's property to the attorney. These transactions are considered presumptively fraudulent and they are often attacked later on as having resulted from the attorney's exercise of undue influence. When challenged, the burden is on the attorney to prove by clear and convincing evidence that the gift or bequest was fair and equitable. Missouri cases dealing with this area of law include Cuthbert v. Heidsieck, 364 S.W.2d 583 (Mo. 1963), Flanagan v. DeLapp, 533 S.W.2d 592 (Mo.banc 1976), and, more recently, In Re Estate of Mapes, 738 S.W.2d 592 (Mo.banc 1987).

In Cuthbert the attorney was a long time "trusted lawyer, financial advisor and confidant" of Mabel Adams, an 80 year old widow. Mrs. Adams informed the lawyer that she wished to give him 200 shares of U. S. Steel Corporation. The attorney then assisted Mrs. Adams with the transaction and even accompanied her to the broker's office to complete the transfer. He also told her where to endorse the stock certificates, paid the charges for the transfer and picked up the new certificates at the broker's office. Later on the widow's guardian sued to set aside the gift, alleging the attorney exercised undue influence over Mrs. Adams in breach of their "fiduciary and confidential relationship." Even though independent witnesses testified Mrs. Adams had later informed them that she had transferred the stock to her attorney "for all the things he had done for her" over more than fifteen years without pay, the trial court set aside the gift and the appellate court affirmed.

In affirming the trial court ruling, the appellate court in Cuthbert emphasized that the attorney's active efforts to assist with the transfer raised a presumption that the gift stemmed from undue influence by the attorney over the client. Given this, the attorney had the burden of coming forward with evidence to show the gift was fair and equitable. The court specifically noted the record "did not establish that Mrs. Adams had independent and disinterested advice regarding the transfer of stock." The court concluded that the attorney's "position would be much improved had Mrs. Adams secured and acted upon the advice of some competent disinterested person who was cognizant of all of the circumstances connected with the transaction."

Today a Missouri court ruling on a similar case as Cuthbert would have an additional basis to set aside the gift; the transaction in Cuthbert would violate Rule 4-1.8(c) of the Missouri Rules of Professional Conduct. Rule 4-1.8(c) rule bars attorneys from preparing instruments that give the attorney or specified relatives of the lawyer any substantial gift from a client, including a testamentary gift. The only exceptions are gifts from an attorney's relative. Since the attorney in Cuthbert was not related to the widow the transaction would have violated Rule 4-1.8(c).

Rule 4-1.8(c) only applies to gifts, not to other transactions. There is no blanket rule in Missouri barring lawyers from entering into transactions with clients where some consideration is given by the attorney. There are however some specific safeguards that apply to these types of transactions.

Rule 4-1.8(a) governs business transactions between an attorney and a client. Rule 4-1.8(a) states that a "lawyer shall not enter in a business transaction with a client or knowingly acquire an ownership, possessory, security or other pecuniary interest adverse to a client" unless specific steps are taken.

To begin with, Rule 4-

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1.8(a)(1) requires that "the transaction and terms on which the lawyer acquires the interest" be (1) both fair and reasonable to the client, (2) fully disclosed to the client, and (3) transmitted in writing to the client in a manner which can be reasonably understood by the client." Note these are objective standards. The issue is what a reasonable attorney would have done under the circumstances. The attorney's good faith believe that he fully explained the transaction to the client ahead of time is irrelevant.

Second, Rule 4-1.8(a)(2) requires that the client be given a "reasonable opportunity to seek the advice of independent counsel in the transaction." Again, the "reasonable opportunity" test is not a subjective standard. Also, unlike in other states, there is no requirement in Missouri that the advice to seek independent counsel itself be in writing. (See, e.g.Hastings v. Twachtman, No. CV 95 57307 S (Jul. 23, 1997). Nonetheless, to protect against an undue influence charge the lawyer should always confirm in writing that the advice to seek separate counsel was given. As with any other factual dispute, a contemporaneous confirming letter will always carry more weight later on than after the fact testimony.

Finally, Rule 4-1.8(c) requires that the client's consent to the transaction be in writing. It is implied that the client's written consent must be signed before the transaction occurs, although this is not specifically required by the rule.

Rule 4-1.8(a) stems from the general rule that lawyers owe fiduciary duties to their clients which should trump any self interest the attorney may have in a business transactions. Lawyers who enter into business transactions with their clients are venturing into perilous waters and should carefully follow Rule 1.8(a) before the transaction is completed. Case law suggest this is not always the case. Too often, the rule is consulted after the fact in an effort to show compliance.

In addition to following Rule 4-1.8(a), as a practical matter, no lawyer should enter into a business relationship with a client unless the client actually obtains independent legal advice regarding the matter. Otherwise, there is a safe bet a court may later conclude the transaction violated Rule 1.8(a), subjecting the attorney to likely discipline. As in Cuthbert, courts tend to focus on whether the client had independent advise at the time of the transaction, even though no rule requires that this be done. Absent independent counsel, it is usually difficult for the attorney to overcome the presumption of undue influence that otherwise applies to these types of transactions.

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