

# LAWYERS AND OTHER PEOPLE'S MONEY

*Fifth Edition*

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**Contents**

ABOUT THE AUTHORS ..... i

INTRODUCTION ..... 5

SECTION 1: FUNDS AND OTHER PROPERTY OF CLIENTS..... 7

    1.1 In General ..... 7

    1.2 Rule 1.15..... 8

    1.3 Scope..... 10

    1.4 Other Property ..... 10

    1.5 Types of Trust Accounts..... 11

    1.6 Interest and Other Investments ..... 12

    1.7 Recordkeeping and Accounting..... 13

    1.8 Deposits into Trust Accounts—Commingling ..... 17

    1.9 Withdrawals from the Trust Account—Conversion ..... 19

    1.10 Mitigating Circumstances—Vicarious Responsibility ..... 24

SECTION 2: BUSINESS TRANSACTIONS WITH CLIENTS..... 26

    2.1 In General ..... 26

    2.2 Activities and Relationships ..... 27

    2.3 Prohibited Economic Relationships ..... 29

    2.4 Full and Adequate Disclosure; Independent Counsel ..... 31

    2.5 Ancillary Businesses ..... 33

    2.6 Lawyer as a Fiduciary ..... 37

SECTION 3: FEES..... 40

    3.1 In General ..... 40

    3.2 Contingent Fees ..... 43

3.3 Percentage Fees .....	45
3.4 Hourly Rates .....	46
3.5 Hybrid and Other Fees .....	47
3.6 Fee Agreements.....	48
3.7 Division of Fees .....	52
3.8 Collection and Termination of Employment .....	53
CONCLUSION.....	57
APPENDIX 1: SELECTED VIRGINIA RULES OF PROFESSIONAL CONDUCT AND COMMENTARY .....	58
APPENDIX 2: PART 6, SECTION IV, PARAGRAPH 20, RULES OF THE SUPREME COURT OF VIRGINIA.....	81
APPENDIX 3: ESCROW ACCOUNT RECORD-KEEPING AND ACCOUNTING FORMS .....	87
APPENDIX 4: SUMMARIES OF CITED LEGAL ETHICS OPINIONS.....	93
INDEX.....	129

## INTRODUCTION

Concerns about the honesty and integrity of lawyers predate formal codes of legal ethics and disciplinary proceedings. An early English statute provides:

That if any Serjeant, Pleader or other do any Manner of Deceit or Collusion in the King's Court, or consent unto it, in Deceit of the Court, or to beguile the Court, or the Party, and thereof be attainted, he shall be imprisoned for a Year and a Day and from thereafter shall not be heard to plead in that Court for any Man.<sup>1</sup>

A nineteenth-century treatise on lawyers finds the law to require the highest degree of fairness and good faith of a lawyer in dealings with clients.<sup>2</sup> The treatise declares that lawyers are liable to their clients for any sums belonging to the clients that are not paid over when received or which are commingled with the lawyer's funds.<sup>3</sup>

Nowhere does the concern about lawyer honesty and integrity become more intense than in the case of lawyers dealing with their clients' money. A lawyer's responsibility for a client's money is now largely defined by ethical codes that in turn draw heavily on the laws of agency and trusts. A lawyer occupies the dual role of an agent and a trustee in dealings with clients<sup>4</sup> and is held to the high standards of accountability one would normally expect from such fiduciaries.

A lawyer is more than just a fiduciary; he or she is an officer of the court. Errors or misdeeds by the lawyer reflect poorly not only on the legal profession, but on the system of the administration of justice as well.<sup>5</sup> It is no wonder that courts appear to be willing to mete out the stiff disciplinary punishments of disbarment and suspension with little hesitation when addressing a lawyer who has improperly handled a client's funds.

While a simple entrustment of funds to a lawyer on behalf of a client is the clearest form of a lawyer's involvement with a client's money, there are other methods of involvement as well. Lawyers may get involved in the businesses of their clients or may seek to involve a client in a business of the lawyer or another client. A client may become a customer of an ancillary business of the lawyer, such as a title insurance agency, arising out of the lawyer's representation of the client.

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<sup>1</sup> Statute of Westminster the First, 3 Edw., c. 29 (1275), *quoted in* Carol A. Turner, Comment, *Attorney May Be Punished for Charging Excessive Fee Absent Aggravating Circumstances, Fraud, or Dishonesty*, 4 Fla. St. U. L. Rev. 126, 127 n.13 (1976).

<sup>2</sup> Edward P. Weeks, *A Treatise on Attorneys and Counsellors at Law* § 258 (2d ed. 1892).

<sup>3</sup> *Id.* § 272.

<sup>4</sup> Charles W. Wolfram, *Modern Legal Ethics* 175 (1986) [hereinafter Wolfram]; *Restatement (Second) of Agency* § 13 (1958).

<sup>5</sup> *In re Wilson*, 409 A.2d 1153 (N.J. 1979); *see also Barrett v. Virginia State Bar*, 269 Va. 583, 611 S.E.2d 375 (2005) ("An attorney who exhibits a lack of civility, sound manners, and common courtesy tarnishes the entire image of what the bar stands for.").

Perhaps the most direct involvement of a lawyer with a client's money is in the fee charged by the lawyer for his or her work. Not only do most trust account violation cases have some issue about fees alleged or owed, but there is also the more fundamental question of just how much the lawyer may charge for services. A lawyer's status as a fiduciary and an officer of the court imposes duties with respect to the fee contract that exceed those normally found in contractual dealings between nonlawyers.

This monograph will focus on a lawyer's responsibility for other people's money in the three areas described above: holding funds and other property entrusted to the lawyer, business relations with clients, and fees. It is intended to be a practical guide for the Virginia lawyer who must deal with these subjects. While sources other than Virginia law have been used frequently, they have been chosen because of the guidance they provide. This monograph is not intended as a comprehensive treatise on lawyer discipline.

The Virginia Rules of Professional Conduct<sup>6</sup> (the Rules) are the principal basis for evaluating the conduct of a Virginia lawyer. The Rules are based on the 1983 Model Rules of Professional Conduct (Model Rules) adopted by the American Bar Association. The Rules follow the "black letter rule followed by commentary" format used by the Model Rules.

The Standing Committee on Legal Ethics of the Virginia State Bar has issued a number of legal ethics opinions (LEOs) interpreting applicable ethical guidelines. While LEOs are nonbinding, informal statements of opinion unless formally adopted by the Virginia Supreme Court,<sup>7</sup> they provide needed guidance in many areas.<sup>8</sup>

Before the adoption of the Rules, ethical standards for Virginia lawyers were found in the Virginia Code of Professional Responsibility (CPR).<sup>9</sup> The CPR consisted of three parts: Canons, Disciplinary Rules, and Ethical Considerations. The CPR was based on the 1969 Model Code of Professional Responsibility of the American Bar Association (Model Code).

While much has been made of differences of wording, authority interpreting the CPR and other similar codes tends to follow the concepts of the Model Rules closely.<sup>10</sup> There does not appear to be a significant divergence between jurisdictions using CPR-type codes and Model Rules jurisdictions in evaluating the liability of a lawyer to a client outside the ethical codes. Even though the issues in these cases are not ethical code issues, the courts tend to adopt concepts found in the Model Rules and Code of Professional Responsibility in evaluating the liability of the lawyer to the

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<sup>6</sup> Rules of the Supreme Court of Virginia [hereinafter Va. R.] pt. 6, § II. The Rules were adopted on January 25, 1999 and became effective January 1, 2000.

<sup>7</sup> Rules for the Organization and Government of the Virginia State Bar Rules 10-2(C); Va. R. 6:IV.

<sup>8</sup> It is the understanding of the author that LEOs issued under the Virginia Code of Professional Responsibility (CPR) were reviewed to determine their continuing applicability under the Rules. Some of the LEOs cited in this monograph were issued under the CPR and their citation reflects the author's judgment about the continuing applicability of the principles they set forth under the Rules.

<sup>9</sup> The CPR was found in the prior provisions of part 6, section II of the Rules of the Supreme Court of Virginia.

<sup>10</sup> See, e.g., ABA/BNA, *Lawyers' Manual on Professional Conduct* (1984) [hereinafter *Lawyers' Manual*].



client.<sup>11</sup> For these reasons, this monograph will draw on the Model Rules and authority from Model Rules jurisdictions as well as on authority from CPR jurisdictions.

## SECTION 1: FUNDS AND OTHER PROPERTY OF CLIENTS

### 1.1 IN GENERAL

A lawyer who receives funds and other property of a client has a fiduciary duty to keep the client's funds and property separate from his or her own and to preserve and safeguard them for the benefit of the client.<sup>12</sup> The dual goal of this rule is to avoid the appearance of impropriety by the lawyer and to eliminate the possibility that the lawyer may inadvertently use the funds for his or her own purposes or otherwise expose the funds to loss.<sup>13</sup> The standard of care for the lawyer is no less than would be expected of a bank or other financial institution acting as a fiduciary.<sup>14</sup>

The fiduciary obligation of a lawyer to preserve and keep separate the property of a client finds its expression in Rule 1.15 of the Virginia Rules of Professional Conduct.<sup>15</sup> Related rules include part 6, section IV, paragraph 20 of the Rules of the Supreme Court of Virginia and the provisions of Title 55, Chapter 27.3 of the Code of Virginia (formerly known as CRESPA).<sup>16</sup>

Rule 1.15 mandates the maintenance of a trust account unless the lawyer's practice is such that the lawyer will never have client funds in his or her possession.<sup>17</sup> The prevailing view holds that the requirements regarding trust accounts may not be waived by clients or avoided by the consent of clients.<sup>18</sup> A lawyer is strictly accountable for compliance with the trust account rules without regard to the lawyer's evil or fraudulent intent.<sup>19</sup>

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<sup>11</sup> ABA Standing Comm. on Lawyers' Prof'l Liab., *The Lawyer's Desk Guide to Legal Malpractice* 8 (1992) [hereinafter *Malpractice Desk Guide*].

<sup>12</sup> *Amsler v. American Home Assurance Co.*, 348 So. 2d 68 (Fla. Dist. Ct. App. 4th Dist. 1977); *Restatement (Second) of Agency* § 398 (1958).

<sup>13</sup> *See also* Wolfram, *supra* note 4, at 177.

<sup>14</sup> Geoffrey C. Hazard, Jr. & W. William Hodes, *The Law of Lawyering* § 19.4 (3d ed. 2000) [hereinafter Hazard & Hodes].

<sup>15</sup> This rule is reproduced at Appendix 1.

<sup>16</sup> Va. Code § 55-525.16 *et seq.*

<sup>17</sup> ABA Informal Op. 621; LEO 1372.

<sup>18</sup> *Gay v. Virginia State Bar ex rel. Second Dist. Comm.*, 239 Va. 401, 380 S.E.2d 470 (1990); *Archer v. State*, 548 S.W.2d 71 (Tex. Civ. App. 1977); ABA Informal Op. 621; LEO 1617. Wisconsin may allow its counterpart of the rule to be waived with the consent of the client in writing. *See* John B. McCarthy, *The Attorney's Trust Account Obligation*, 61 Wis. B. Bull. 16 (Mar. 1988).

<sup>19</sup> *Archer v. State*, 548 S.W.2d 71 (Tex. Civ. App. 1977).

## 1.2 RULE 1.15

Rule 1.15(a) requires that all funds received or held on behalf of a client,<sup>20</sup> other than reimbursements for advances or expenses, be deposited in one or more identified trust accounts maintained at a financial institution in the state in which the lawyer's office is located.<sup>21</sup> The rule applies both to funds received from a client and to funds received from a third party.<sup>22</sup> The exception for advances or expenses applies to those already incurred, not to expected future expenses. Funds received from a client for expenses that have not yet been billed to the lawyer must be deposited in the lawyer's trust account.<sup>23</sup>

The Virginia trust account for clients of a multi-jurisdictional firm does not have to be physically located in Virginia as long as it is with a qualifying financial institution authorized to do business in Virginia.<sup>24</sup> A trust account may have a non-Virginia lawyer as a signatory as long as proper supervision of the account is maintained by a Virginia lawyer.<sup>25</sup>

In certain circumstances it may be appropriate to have more than one trust account.<sup>26</sup>

Lawyers acting as settlement agents in transactions subject to the statutes governing real estate settlement agents (hereinafter "RESA statutes"; formerly CRESA) are required to have a separate fiduciary account for those transactions.<sup>27</sup> A transaction is subject to the RESA statutes if it involves the purchase of, or lending on the security of, not more than four residential dwelling units located in Virginia.<sup>28</sup> A settlement agent is a person who provides escrow, closing, or settlement services in connection with a transaction subject to the RESA statutes, who is not a party to the transaction, and who is listed as a settlement agent on the settlement statement for the transaction.<sup>29</sup> Any person other than a party to the transaction who conducts a settlement conference and receives or handles money is deemed to be a settlement agent.<sup>30</sup>

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<sup>20</sup> The comparable provision of the Model Rules parallels Rule 1.15(a), with the significant exception that the Model Rules also apply to funds and property of third parties.

<sup>21</sup> The term "financial institution" is defined to include regulated state or federally chartered banks, savings institutions, and credit unions that have signed a Trust Account Notification Agreement with the Virginia State Bar and are licensed and authorized by federal and state law to do business in which deposits are insured by an agency of the federal government.

<sup>22</sup> *In re Cutrone*, 492 N.E.2d 1297 (Ill. 1986).

<sup>23</sup> LEO 1636.

<sup>24</sup> LEO 1238.

<sup>25</sup> LEO 724.

<sup>26</sup> See generally ABA Ctr. for Professional Responsibility, *Annotated Model Rules of Professional Conduct* Rule 1.15, comment [1] (5th ed. 2003) [hereinafter *Annotated Model Rules*]; Frederick G. Miller, *A Practical Guide to Attorney Trust Accounts and Record Keeping*, 64 N.Y. St. B. J. 34 (Mar./Apr. 1992).

<sup>27</sup> Va. Code § 55-525.24(A).

<sup>28</sup> Va. Code § 55-525.18(A).

<sup>29</sup> Va. Code § 55-525.16.

<sup>30</sup> *Id.*

No funds belonging to the lawyer or his or her firm may be deposited into the lawyer's escrow account except funds reasonably necessary to pay service charges or to maintain a required minimum balance to avoid the imposition of service fees; or funds in which two or more persons claim an interest.<sup>31</sup> The portion of joint funds belonging to the lawyer must be withdrawn promptly after it is due unless the lawyer's right to the funds is disputed by the client, in which case the funds may not be withdrawn until the dispute is resolved.<sup>32</sup>

A lawyer must promptly notify a client of receipt of the client's funds, securities, or other property<sup>33</sup> and label and identify securities and property and place them in a safe deposit box or other place of safekeeping as soon as practicable.<sup>34</sup> A lawyer must maintain complete records of all funds, securities, and other property of clients coming into his or her possession and render appropriate accounts regarding them.<sup>35</sup> A lawyer must promptly deliver or pay to the client or another as requested by such person funds, securities, and other property that the person is entitled to receive.<sup>36</sup>

A lawyer should be aware of applicable insurance limits and the stability of the institution holding clients' funds when depositing them into trust accounts. LEO 1417 indicates there is no affirmative ethical duty on a lawyer to make sure all clients' funds are deposited in accounts within applicable insurance limits but requires that the lawyer's status as a director and stockholder of the depository bank be disclosed. If the lawyer/director knows the financial institution is in a precarious situation, the lawyer may not deposit funds in the account without specific authorization from the client.

While federal insurance limits apply separately to each individual with funds in an insured trust account, a Connecticut opinion indicates that a lawyer has a duty to determine whether a client has sufficient funds in the account to cause insurance limits to be exceeded. If so, the lawyer must consult with the client as to the proper course of action.<sup>37</sup> Given a lawyer's potential liability to the client for loss of funds, it would appear prudent for a lawyer to either get the client's consent to exceed the insurance limits or to divide funds among multiple institutions to maximize available insurance if the lawyer is likely to hold substantial sums of money for the client over more than the brief interval required to complete a real estate closing or similar transaction.

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<sup>31</sup> Rule 1.15(a)(3).

<sup>32</sup> Rule 1.15(a)(3)(ii), (d)(2).

<sup>33</sup> Rule 1.15(b)(1).

<sup>34</sup> Rule 1.15(a)(1), (b)(2).

<sup>35</sup> Rule 1.15(b)(3).

<sup>36</sup> Rule 1.15(b)(4).

<sup>37</sup> Connecticut Bar Comm. on Professional Ethics, Ops. 92-8, 91-2.

### 1.3 SCOPE

Rule 1.15 by its terms applies to all funds held by a lawyer on behalf of a client or a third party or by a lawyer acting as a fiduciary.<sup>38</sup> Commentators and courts have broadly interpreted the scope of the trust account rules, at least as far as their implicit prohibitions against conversion or commingling are concerned. In addition to the categories explicitly recognized by the text of the Virginia rule, the requirements of comparable rules have been extended to lawyers serving as real estate agents and corporate officers.<sup>39</sup> The *Restatement of the Law Governing Lawyers* provides that the safeguarding and anti-conversion/commingling provisions of the escrow account rules apply to all property that comes into the possession of a lawyer during a representation, including that of third parties.<sup>40</sup> In instances when a lawyer serves in a dual capacity, such as lawyer and corporate officer, courts are particularly reluctant to accept the argument that an alleged defalcation or other violation occurred while the individual was acting in a nonlawyer capacity.<sup>41</sup>

### 1.4 OTHER PROPERTY

While a lawyer's obligations with respect to funds of the client are the principal focus of the authority interpreting and applying the concepts of Rule 1.15, the duties of segregation, safeguarding, and delivery of client property extend to both tangible and intangible property of the client as well.<sup>42</sup> Segregation and safeguarding are accomplished by labeling the property in question as belonging to the client and placing it in a safe-deposit box or other place of safekeeping.<sup>43</sup>

The courts have not hesitated to impose discipline on lawyers who have dealt with their clients' property improperly. *Florida Bar v. Carlton*<sup>44</sup> upheld discipline imposed on a lawyer who, among other things, was unable to return a client's insurance policies and other personal property entrusted to him. *In re Grubb*<sup>45</sup> concerned a lawyer who took an impressive ring from a client as security for a fee in a criminal case. While the lawyer initially put the ring in a locked box, he subsequently took it home with him and carried it about. The lawyer was censured when he lost the ring and was unable to return it to his client.

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<sup>38</sup> Note that the RESA statutes apply rules comparable to those of Rule 1.15 to persons acting as settlement agents regardless of whether all the parties to the transaction are the lawyer's clients. See, e.g., Va. Code § 55-525.24.

<sup>39</sup> Wolfram, *supra* note **Error! Bookmark not defined.**, at 178.

<sup>40</sup> *Restatement of the Law Governing Lawyers* § 44 cmt. b (2000); see also Philadelphia Bar Ass'n Professional Guidance Comm., Op. 89-4.

<sup>41</sup> See *In re Lurie*, 546 P.2d 1126 (Ariz. 1976); *Black v. State Bar*, 368 P.2d 118 (Cal. 1962); *People v. Vernon*, 660 P.2d 879 (Colo. 1982). But see Michigan Formal Ethics Op. R-7.

<sup>42</sup> Rule 1.15(a), (b). See generally *El-Amin v. Virginia State Bar*, 257 Va. 608, 514 S.E.2d 163 (1999) (attorney agreed to sell client's car and hold the net proceeds as his retainer but instead traded the car for a newer model; the court held that the "credit" the attorney received over and above the value of the client's car became "funds" within the meaning of the rule).

<sup>43</sup> Rule 1.15(b)(2); Wolfram, *supra* note **Error! Bookmark not defined.**, at 180.

<sup>44</sup> 366 So. 2d 406 (Fla. 1978).

<sup>45</sup> 663 P.2d 1346 (Wash. 1983).

LEO 330 indicates that more than safekeeping may be appropriate in some circumstances. This opinion concerns a lawyer who received a redeemable airline ticket that was about to expire on behalf of a client who had been committed to a mental institution. The opinion holds that the lawyer should redeem the ticket, deposit the funds in his or her trust account, and advise the court of the receipt of the funds.<sup>46</sup> This opinion serves as a reminder of the duty of a lawyer to both safeguard and preserve the property of the client.<sup>47</sup>

## 1.5 TYPES OF TRUST ACCOUNTS

Part 6, section IV, paragraph 20 of the Rules of the Supreme Court of Virginia establishes three permissible types of lawyer trust accounts:<sup>48</sup>

1. A pooled interest-bearing trust account for multiple clients if the account has an accounting system that provides for an allocation of interest among the various clients with funds in the account and pays or credits the interest to the applicable clients less fees and expenses charged by the lawyer for administering the account at least quarterly.
2. An IOLTA account. An IOLTA account is an interest-bearing account for pooled client funds that does not have procedures for computing and paying to clients their share of the interest earned on the account. The expenses of allocating and paying the interest on the IOLTA account must be reasonably expected to exceed the interest that would be earned on this account. Interest on the IOLTA account must be remitted periodically to the Legal Services Corporation of Virginia by the bank in which the account is maintained. Other than a remittance fee for computing the interest and remitting it to the Legal Services Corporation, the bank may not charge fees against an IOLTA account that it would not charge nonlawyer depositors. No fees may be charged against the principal of the account. The bank has periodic reporting responsibilities both to the Legal Services Corporation and to the lawyer with respect to its remittances.
3. A non-interest-bearing trust account. The lawyer or law firm may not receive any consideration or benefit from the bank for opening a non-interest-bearing trust account or for converting from an IOLTA account to a non-interest-bearing trust account.

Lawyers have no obligation to obtain their clients' consent for depositing funds in an IOLTA account or to report to the client the interest earned on that account.

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<sup>46</sup> With regard to closed files, LEO 1664 holds that even under circumstances where files being stored by an attorney may have historical significance, absent client consent the files must be safeguarded and may not be reviewed to determine their potential historical contributions.

<sup>47</sup> See generally *Restatement (Second) of Agency* § 69 (1958).

<sup>48</sup> Part 6, section IV, paragraph 20, of the Rules of the Supreme Court of Virginia is reproduced at Appendix 2. Lawyers who never receive client funds that require a trust account are exempt from the rules if they file a certificate with the Legal Services Corporation of Virginia.

A lawyer may elect not to maintain an IOLTA account. The election is made on a form provided by the Legal Services Corporation. A lawyer may elect not to maintain an IOLTA account at any time by submitting a notice of election during the month preceding the month in which participation is to be terminated. In addition, the Legal Services Corporation may permit a lawyer to withdraw from the IOLTA program at any time.

An election not to have an IOLTA account effectively requires a lawyer to either credit and pay interest earned on the trust account to the clients whose funds are in the account or to maintain a non-interest-bearing trust account. The lawyer may not receive interest earned on clients' funds in the trust account.<sup>49</sup>

LEO 1170 indicates that a lawyer could not avoid the prior disciplinary rule provisions regarding interest on client funds merely by establishing a separate real estate settlement subsidiary that would handle real estate closings for his clients. However, the opinion finds that interest on escrow funds held by the settlement subsidiary could accrue to the benefit of the lawyer in the case of persons using the service who were not clients of the lawyer. It also allows the subsidiary to earn interest on the client's funds if the lawyer provided the client with referrals to other similar entities in addition to the one in which he had an interest. Even in the latter instance, the ruling confirms that the requirements of DR 5-104(A) regarding business relations with clients must be satisfied.<sup>50</sup> Thus, the attorney must obtain the client's consent after full and adequate disclosure of the attorney's differing interests. LEO 1469 would allow a lawyer who operates a closing service but who does not engage in the practice of law to avoid application of the requirements of the prior disciplinary rule provisions regarding interest on accounts. Any activity by the lawyer constituting the practice of law, however, would trigger application of the disciplinary rules.

## 1.6 INTEREST AND OTHER INVESTMENTS

One overlooked result of the rules regarding permissible trust accounts is the duty the rules impose on a lawyer who chooses to keep separate accounts for separate client matters to use accounts that produce interest for the benefit of the client. The duty to deposit client funds in an interest-bearing account is in accordance with the lawyer's duty to make funds held for the client productive.<sup>51</sup>

Read in conjunction with part 6, section IV, paragraph 20 of the Rules of the Supreme Court of Virginia, Rule 1.15(a) generally requires an interest-bearing account in an insured financial institution as the only permissible investment vehicle for client funds. LEO 1265 disapproves the investment of escrow funds held in a lawyer's trust account in repurchase agreements fully collateralized by United States

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<sup>49</sup> See, e.g., LEOs 831, 392, 280. The RESA statutes impose a similar requirement on settlement agents but provide that IOLTA accounts are acceptable. Va. Code § 55-525.24(C).

<sup>50</sup> The counterpart of DR 5-104(A) under the Rules of Professional Conduct is Rule 1.8(a).

<sup>51</sup> *Annotated Model Rules*, supra note **Error! Bookmark not defined.**, at 252; *Restatement (Second) of Agency* § 70 (1958); *Lawyers' Manual*, supra note **Error! Bookmark not defined.**, at 45:109; Miller, supra note **Error! Bookmark not defined.**, at 35; Roy Conn, III, Comment, *Attorney Misappropriation of Client Funds*, 27 How. L.J. 1597, 1608 (1984).

government and United States agency securities through an automatic investment management service offered by a bank.<sup>52</sup> The opinion reasons that as the funds would not have been deposited in a bank or banking institution with insured deposits, the investment violated the rules of DR 9-102, the antecedent of Rule 1.15(a).<sup>53</sup>

## 1.7 RECORDKEEPING AND ACCOUNTING

Implicit in the obligations of a lawyer as a fiduciary of his or her client's property are the duties to account to the client for that property and to keep proper records of the client's property.<sup>54</sup> The duty to keep proper records and accounts is recognized in Rule 1.15(b)(3). These rules are amplified by Rule 1.15(c), which establishes specific recordkeeping requirements.<sup>55</sup> The importance of the recordkeeping requirements cannot be overstated. It has been suggested that most cases of lawyer defalcation begin with negligent recordkeeping, which leads to the slippery slope of client losses and the use of one client's funds to make up deficiencies in another client's account.<sup>56</sup> The recordkeeping rules address the enforcement objective of determining whether a lawyer is satisfying his or her obligations under Rule 1.15. A lawyer who scrupulously complies with the requirements of Rule 1.15(c) will go a long way toward satisfying the lawyer's obligations under Rule 1.15 generally. It should be emphasized that the recordkeeping rules are not limited to escrow accounts in the usual sense but apply to all accounts in which client funds are held.

At the same time, however, bookkeeping techniques alone do not satisfy the accounting requirements of Rule 1.15. A Wisconsin ethics opinion emphasizes that DR 9-102 (the CPR counterpart of Rule 1.15(a)) requires actual separate accounts, not just separate accountings for portions of a commingled account.<sup>57</sup>

Courts view the recordkeeping requirements for trust accounts to be sufficiently important that they have not hesitated to impose discipline in cases involving only violations of recordkeeping requirements.<sup>58</sup>

Rule 1.15(c) requires as a minimum that a lawyer maintain the following books and records for each escrow account:

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<sup>52</sup> All funds deposited with an approved banking institution need not be insured. The bank need only participate in the federal insurance program. LEO 1417.

<sup>53</sup> Minnesota and North Dakota allow investment of client funds in federally regulated investment companies, and New Jersey allows the investment of client funds in repurchase agreements. *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 45:108.

<sup>54</sup> *Restatement (Second) of Agency* §§ 381, 382 (1958); Wolfram, *supra* note **Error! Bookmark not defined.**, at 181.

<sup>55</sup> See Appendix 3 for sample journals and other forms that reflect the various records required by Rule 1.15(c).

<sup>56</sup> Edmund N. Carpenter, II, *The Negligent Attorney Embezzler: Delaware's Solution*, 61 A.B.A. J. 338 (1975); David R. Rosenfeld & Michael J. Rost, *Lawyer Trust Accounts*, 42 Va. Law. 43 (1993).

<sup>57</sup> Wisconsin State Bar Standing Comm. on Professional Ethics, Op. E-81-4.

<sup>58</sup> *Motley v. Virginia State Bar*, 260 Va. 251, 536 S.E.2d 101 (2000); *Delk v. Virginia State Bar*, 233 Va. 187, 355 S.E.2d 558 (1987) (loss of money by client is not a prerequisite to imposition of discipline); *Wright v. Virginia State Bar*, 233 Va. 491, 357 S.E.2d 518 (1987) ("Neither loss of money by a client nor proof of a lawyer's moral turpitude is a prerequisite to a finding that a lawyer has mismanaged his financial records and client's funds."); *In re Hollendonner*, 504 A.2d 1174 (N.J. 1985); *Annotated Model Rules*, *supra* note **Error! Bookmark not defined.**, at 253-54.

1. A cash receipts journal listing all funds received, the source of receipts, and date of receipts;<sup>59</sup>
2. A cash disbursements journal listing and identifying all disbursements from the escrow account;<sup>60</sup> and
3. A subsidiary ledger containing a separate account for each client and for every other person or entity from whom money has been received in escrow. By separate columns or otherwise, the ledger must clearly identify escrow funds disbursed and the escrow funds balance on hand. All fees paid from trust accounts must be clearly indicated.<sup>61</sup>

Monthly reconciliations are required at month's end of the cash balances derived from the receipts and disbursements journals, the escrow account checkbook balance, and the escrow account bank statement balance. The subsidiary ledger must have a periodic trial balance at least quarterly within 30 days of the end of the quarter. This balance must show the balance of each client at the end of the period. The trial balance for the subsidiary ledger must agree with the control figure, which is the beginning balance, increased by receipts and decreased by disbursements. At least quarterly and within 30 days of the end of the quarter, the cash balances must be reconciled to the subsidiary ledger trial balance. All balances and reconciliations must identify the preparer and be approved by a lawyer.<sup>62</sup> Duplicate deposit slips or other records that are sufficiently detailed to identify each item must be maintained.<sup>63</sup>

Each trust account must be clearly identified as such.<sup>64</sup> The Virginia State Bar must approve each financial institution that maintains lawyer trust accounts.<sup>65</sup> As a condition of approval, each such institution must agree to notify the State Bar if any otherwise proper instrument is presented against an escrow account containing insufficient funds,<sup>66</sup> regardless of whether the instrument is honored.<sup>67</sup> If the financial institution does not honor the instrument, the notification of overdraft must be identical to the overdraft notice provided to customers and should include a copy of

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<sup>59</sup> Checkbook entries of receipts and deposits, if adequately detailed and bound, may suffice. If separate cash receipts journals are not maintained for fiduciary and nonfiduciary funds, the consolidated journal must have separate columns for fiduciary and nonfiduciary receipts.

<sup>60</sup> Checkbook entries of disbursements, if adequately detailed and bound, may constitute a journal. If separate cash disbursement journals are not maintained for fiduciary and nonfiduciary funds, the consolidated journal must have separate columns for fiduciary and nonfiduciary disbursements.

<sup>61</sup> The purpose of all receipts and disbursements must be fully explained and supported by adequate records. Rule 1.15(f)(6).

<sup>62</sup> Rule 1.15(d)(3).

<sup>63</sup> Rule 1.15(d)(2).

<sup>64</sup> Rule 1.15(a)(1).

<sup>65</sup> *Id.* The notification agreement that an approved depository must execute with the Virginia State Bar requires that the institution notify Bar Counsel if the institution changes its name, corporate form, or ownership or affiliation. The successor institution must inform Bar Counsel whether it wishes to continue serving as an approved depository. See the Trust Account Notification Agreement in Appendix 3.

<sup>66</sup> Paragraph 20. "Insufficient funds" refers to an overdraft in the commonly accepted sense, namely, based on the bank's accounting records. For this purpose, the balance does not include funds on deposit that have not been collected. Rule 1.15(f)(1)(vi).

<sup>67</sup> Appendix 3 contains a copy of the applicable form.



the dishonored instrument if normally provided. The notice must be given simultaneously with the notice to the customer and within the time period provided by law for notice of dishonor. If the instrument is honored, the report of overdraft must contain the identifying information specified in Paragraph 20 as well as the amount of the overdraft, and it must be made within five banking days of the instrument's presentation for payment.<sup>68</sup>

The ABA Model Recordkeeping Rules are considerably more detailed than the minimum requirements of Rule 1.15. In addition to the rules set forth above, the ABA rules require that each deposit be identified in the cash receipts journal by date, source, and description and that each payment be identified in the cash disbursements journal by date, payee, and description. The client subsidiary ledger must contain a separate page for each client. Each client's ledger should clearly identify all funds received and disbursed with the same specificity as is required for the cash receipts and disbursement journals. In addition to the basic books required by Rule 1.15, the ABA also recommends retaining the following: all retainer and compensation agreements; all bills to clients; all statements to clients showing the disbursement of funds on their behalf; information regarding payments to third parties on behalf of the client; checkbooks, stubs, bank statements, and related documents; copies of monthly trial balances and quarterly reconciliations of the lawyer's trust accounts; and such portions of client files as are necessary to understand the financial records.<sup>69</sup>

A lawyer serving as a fiduciary is required to complete an annual summary of receipts, disbursements, and changes in assets comparable to an accounting that would be required of a court-supervised fiduciary in similar circumstances. The summary must be in sufficient detail to allow a reasonable person to determine whether the lawyer is properly discharging the obligations of the fiduciary relationship.<sup>70</sup> The lawyer fiduciary must maintain original source documents sufficient to substantiate, and where necessary, explain the required annual summary.<sup>71</sup> The records are required to be kept for at least five years following the termination of the fiduciary relationship.<sup>72</sup>

The provisions of Rule 1.15 applying to lawyers as fiduciaries are substantially similar to those of LEO 1617, which was issued under the Code of Professional Responsibility. LEO 1617, however, indicates that a lawyer fiduciary has to account to particular persons, a subject that is not addressed by Rule 1.15. In the case of a lawyer fiduciary subject to the provisions of section 26-8 *et seq.* of the Virginia Code,<sup>73</sup> the final duty of accounting is satisfied by an annual accounting to the court. For

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<sup>68</sup> Paragraph 20. *See also* Appendix 3.

<sup>69</sup> *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 45:1005.

<sup>70</sup> Rule 1.15(c)(3).

<sup>71</sup> Rule 1.15(c)(3). If the bank provides electronic confirmation of checks written on the account, the lawyer is not required to maintain the original canceled checks. Electronic checking is permissible for trust accounts if all requirements of Rule 1.15 are met. Rule 1.15 cmt. [6].

<sup>72</sup> Rule 1.15(c)(4).

<sup>73</sup> For example, guardians, committees, personal representatives, conservators, testamentary trustees, and trustees under deeds of trust.

other fiduciary relationships, an annual accounting is required. LEO 1617 recognizes that the form of an accounting for a non-Title-26 relationship may vary considerably based on the circumstances of the relationship. In cases when a lawyer has little or no discretion, a simple receipt and disbursement summary might be appropriate. In other cases it should be sufficiently detailed to allow the person receiving it to determine if the lawyer has appropriately exercised the discretion entrusted to him or her. The person to whom the accounting is to be rendered depends on the nature of the fiduciary relationship. If the lawyer's client is the primary beneficiary of the relationship, the accounting is to go to the client. In the case of a trust, the accounting should go to the income beneficiaries. If the person to whom an accounting should be rendered is under a disability, the accounting should go to the guardian or committee of that person. If there is no guardian or committee, or if the lawyer is the guardian or committee, the accounting should go to a member of the person's family. LEO 1617 holds that the duty of accounting may not be waived.

A lawyer who complies with the requirements of the Rules of Professional Conduct concerning his or her real estate settlement escrow account should also satisfy the requirements of the RESA statutes that apply to such accounts. Lawyers serving as settlement agents, however, should remember that they have an additional obligation to register as settlement agents with the Virginia State Bar.<sup>74</sup> The RESA statutes also require lawyer settlement agents to carry an errors and omissions malpractice policy with a minimum of \$250,000 in coverage, a blanket fiduciary bond or employee dishonesty insurance with a minimum of \$100,000 in coverage, and a surety bond with a minimum of \$100,000.<sup>75</sup>

Lawyers should segregate their trust and fiduciary accounts from other accounts. While segregation by financial institutions might be the best course of action, at the very least the checks and deposit slips of each account should be distinguished by color, size, or some other form of noticeable differentiation to avoid confusion.

Daily posting is worth the inconvenience it may cause. The more time that passes, the hazier information becomes and the greater the likelihood of a mistake. Even though a trial balance of the client ledger is only required on a quarterly basis, keeping a running balance in individual client accounts updated, particularly if disbursements are being made from those accounts, is advisable. Not only do overpayments present an awkward and embarrassing situation for the lawyer who attempts to collect them, but they can present very serious disciplinary problems.<sup>76</sup>

The importance of good recordkeeping cannot be overemphasized. The lawyer's records should be sufficiently clear and detailed to allow an outsider to understand them with a minimum amount of explanation or intervention. It is both good business and good sense to regard the rules of Rule 1.15 as minimum requirements.

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<sup>74</sup> Va. Code § 55-525.30(A).

<sup>75</sup> Va. Code § 55-525.20(B).

<sup>76</sup> See *infra* ¶ 1.9 (discussion of conversion).

## 1.8 DEPOSITS INTO TRUST ACCOUNTS—COMMINGLING

All funds received by a lawyer on behalf of a client, other than reimbursement of expenses and advances, are required to be deposited in the lawyer's trust account.<sup>77</sup> The deposit is to be made intact, that is, in the form and the amount in which the lawyer received it.<sup>78</sup> Mixed client funds and nonclient funds are also to be deposited into the trust account. Joint funds must be deposited into the account even if the lawyer and client are agreeable to direct negotiation of a check made payable to them jointly.<sup>79</sup> The nonclient part is to be withdrawn when the deposit instrument clears.<sup>80</sup>

Earned and undisputed fees received from a client are not required to be deposited into a trust account.<sup>81</sup> Except for funds reasonably necessary to pay service or other charges on the account or to maintain a minimum balance in order to avoid the imposition of service fees, the lawyer may not deposit any of his or her funds into the trust account.<sup>82</sup> In accordance with the majority rule, Virginia treats unearned retainers (advance fees) as funds that must be deposited in the trust account until they are earned.<sup>83</sup> A similar rule should apply to advances for anticipated expenses.<sup>84</sup>

A lawyer is under a duty to notify the client promptly of funds received from third parties on the client's behalf and to deposit them in the trust account.<sup>85</sup> It should be noted, however, that the status of lawyer does not of itself give a lawyer power to endorse checks made out in the client's name.<sup>86</sup>

Authorities interpreting similar rules have been reluctant to allow lawyers to deposit their funds in their trust accounts for any reason.<sup>87</sup> Virginia has interpreted the service charge exception of Rule 1.15(a) as allowing a lawyer to deposit from his or her own funds an amount equal to two years' anticipated charges for the account.<sup>88</sup>

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<sup>77</sup> Rule 1.15(a). The rules are silent on any time requirement for the deposit. The RESA statutes require that funds be deposited no later than the second business day following their receipt. Va. Code § 55-525.24(A).

<sup>78</sup> Rule 1.15(d)(2).

<sup>79</sup> LEO 704.

<sup>80</sup> Rule 1.15(d)(2).

<sup>81</sup> LEO 585. See also LEO 1372, which holds that an attorney who does not receive any client funds or advance fees need not maintain an open trust account.

<sup>82</sup> Rule 1.15(a).

<sup>83</sup> *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 45:101; Hazard & Hodes, *supra* note **Error! Bookmark not defined.**, at 458. See the discussion of fee agreements in paragraph 3.6.

<sup>84</sup> Payments by the client for expenses already incurred by the lawyer may go directly to the lawyer. Rule 1.15(a).

<sup>85</sup> *In re Baldwin*, 271 S.E.2d 626 (Ga. 1980); Rule 1.15.

<sup>86</sup> *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at § 19.4. An irrevocable assignment of the funds represented by the check in favor of the lawyer may give the lawyer the power to endorse the check. LEO 734. Notification to the client and accounting for disbursement of the proceeds are still required.

<sup>87</sup> Michigan Formal Ethics Op. M-7.

<sup>88</sup> LEO 1510.

The trust account offense of commingling occurs either when a lawyer deposits client funds into an account other than a designated trust account<sup>89</sup> or when a lawyer deposits his or her own funds in the trust account. It can even occur when a lawyer fails to withdraw earned fees from the trust account in a timely fashion.<sup>90</sup> It occurs by definition when a lawyer uses one account as trust account and business account.<sup>91</sup> The offense occurs and discipline is appropriate even though no client funds are misused and no client is deprived of the use of his or her money.<sup>92</sup> While seemingly harmless in and of itself, commingling is the beginning of the slippery slope leading to the more culpable offense of conversion.<sup>93</sup>

*Attorney Grievance Commission v. Dacy*<sup>94</sup> demonstrates the seriousness with which the courts apply the prohibition against commingling. The lawyer in *Dacy* represented a savings and loan institution in real estate financings. There were often problems in getting available funds from the savings and loan into the lawyer's escrow account in a timely fashion. The lawyer's employee developed a plan in concert with employees of the savings and loan by which the loan proceeds were deposited first into the lawyer's personal account and from there transferred to the escrow account so they were available in a timely fashion. Although the plan was seemingly innocuous and no one was hurt, the Maryland court nevertheless suspended the lawyer.<sup>95</sup>

*Fitzsimmons v. State Bar*<sup>96</sup> demonstrates that a lawyer may benefit from rules requiring the deposit of clients' funds in a trust account. The lawyer in *Fitzsimmons* received a large amount of cash on behalf of his client. The lawyer testified that a portion of the payment was intended as a fee to him and the remainder was transferred in kind to a third party at the direction of the client. No receipt from the third party was obtained. The client subsequently denied authorizing the lawyer to transfer the funds to the third party. Had the lawyer deposited the amount in his trust account and memorialized his disbursement and the direction of the client, he would have left a clear paper trail as to the disposition of the funds. By not doing so he not only exposed himself to disciplinary sanctions but also left himself open to a claim of conversion by his client.<sup>97</sup>

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<sup>89</sup> *In re Hessler*, 549 A.2d 700 (D.C. 1988); *In re Franklin*, 516 A.2d 171 (D.C. 1986); *In re Ray*, 368 N.W.2d 924 (Minn. 1985).

<sup>90</sup> *In re Maran*, 402 A.2d 924 (N.J. 1979); LEOs 1263, 1262.

<sup>91</sup> Philip F. Downey, Comment, *Attorneys' Trust Accounts: The Bar's Role in the Preservation of Client Property*, 49 Ohio St. L.J. 275 (1988).

<sup>92</sup> *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 45:503.

<sup>93</sup> Carpenter, *supra* note **Error! Bookmark not defined.**, at 339.

<sup>94</sup> 542 A.2d 841 (Md. 1988).

<sup>95</sup> See also *Attorney Grievance Comm'n v. Kemp*, 496 A.2d 672 (Md. 1985) (lawyer attempted to excuse deposit of funds into his personal account on grounds that he had changed banks for his escrow account and had not received checks or deposit slips for new account).

<sup>96</sup> 667 P.2d 700 (Cal. 1983).

<sup>97</sup> See also *State v. Pringle*, 667 P.2d 283 (Kan. 1983) (indicating that keeping client's funds in cash, even at request of client, may violate escrow account requirements).

## 1.9 WITHDRAWALS FROM THE TRUST ACCOUNT—CONVERSION

Not only is a lawyer required to deliver promptly or pay over his or her client's property when requested,<sup>98</sup> but the lawyer is also under a duty to follow the client's directions with respect to the disposition of the client's property and follow any limitations on the use of the property imposed by the client.<sup>99</sup> The rules regarding disbursements from trust accounts follow the general concepts of agency, which require an agent to follow the directions of the principal and make the agent responsible for property that is not returned or is misdelivered.<sup>100</sup>

Perhaps no issue generates more problems than the lawyer's right to withdraw sums from funds held on behalf of the client to which the lawyer claims entitlement as fees or reimbursements. A lawyer may only withdraw amounts from the trust account on his or her own behalf if the lawyer has a clear right to withdraw the sums, the amount proposed to be withdrawn is the correct amount, and the time for withdrawal is appropriate.<sup>101</sup> Notice of the proposed withdrawal is required to be given to the client.<sup>102</sup> Merely sending a bill that is not paid may be sufficient to entitle a lawyer to pay the bill from funds held on behalf of the client in appropriate circumstances.<sup>103</sup> A South Carolina opinion holds that a lawyer can apply credit balances on certain matters against amounts the client owes for other matters if the payment is due and the right to receive the payment is not disputed but advised that it would be prudent to obtain the client's consent.<sup>104</sup> A lawyer who is fired must return to the client any unused funds held on behalf of the client, together with an accounting.<sup>105</sup>

LEOs 1322 and 1606 permit an attorney to charge a "retainer" to insure his availability in future matters and as consideration for the attorney's unavailability to adverse parties. "Nonrefundable retainers," however, are improper where those funds are actually sums entrusted to the attorney as an advance payment for his services on a specific matter.

A lawyer may not withdraw funds on his or her own behalf from funds held for the client if the lawyer's right to receive them is disputed by the client. If the lawyer's right to receive the payment is disputed, the disputed portion may not be withdrawn

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<sup>98</sup> Rule 1.15(b)(4).

<sup>99</sup> *Pickus v. Virginia State Bar*, 232 Va. 5, 348 S.E.2d 202 (1986); *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 45:110; Martin J. Kurzer et al., *Attorneys' Trust Accounts—Rules and Pitfalls*, 55 Fla. B. J. 355 (1981). A lawyer who is directed by a client to retain the client's funds in a trust account may do so without violating any ethical precept as long as the lawyer has no reason to believe the client is involved in fraudulent activity. Rhode Island Ethics Op. 93-19.

<sup>100</sup> *Eaton v. Calig*, 446 N.E.2d 218 (Ohio Ct. App. 1982); *Restatement (Second) of Agency* § 402 (1958).

<sup>101</sup> Wolfram, *supra* note **Error! Bookmark not defined.**, at 182; *see also* LEO 868 (fees paid from funds remitted by third party).

<sup>102</sup> LEOs 1187, 734.

<sup>103</sup> LEO 1187 holds that an attorney may pay an outstanding invoice for services rendered in another matter from funds collected in a pending matter provided the fees owed are not disputed by the client and notice, as well as an accounting of the application of the proceeds, is provided to the client's last known address. *But see Attorney Grievance Comm'n v. McIntire*, 405 A.2d 273 (Md. 1979); LEO 1489.

<sup>104</sup> South Carolina Bar Ethics Advisory Op. 88-08.

<sup>105</sup> *See generally* LEO 1132.

until the dispute is finally resolved.<sup>106</sup> A lawyer may intercept funds received on behalf of the client, however, if the lawyer has a claim to fees and may continue to hold those funds until such time as the fee issue is resolved.<sup>107</sup> If a lawyer cannot resolve the dispute with the client, the lawyer may have no choice but to interplead the disputed funds and have the issue resolved by the court. A lawyer holding a deposit for the sale of the client's real estate may not apply a portion of the deposit against the client's outstanding bills, even with the client's consent. In *In re Kramer*,<sup>108</sup> the client seller's consent was not sufficient to authorize the withdrawal, because until the closing occurred, the purchaser had an interest in the funds as well.

Missing clients present special problems. A lawyer who cannot find the client may not unilaterally distribute to himself or herself sums held on behalf of a client.<sup>109</sup> As a general rule, the inability to obtain directions from the client will effectively freeze the client's funds in the lawyer's account.<sup>110</sup> LEO 548 requires that a lawyer conduct a diligent effort to determine the owner of funds and to have the funds paid over to the appropriate individual. At the very least, this will require a first-class mailing to the client at the client's last known address. In instances involving larger sums, checking postal records and telephone numbers may be appropriate. The lawyer may deduct the costs incurred in attempting to locate the missing client from the funds but may not charge a fee for his or her work in searching. The lawyer may not ask the client to agree in advance that the lawyer may keep any unclaimed funds.<sup>111</sup> Funds held in the trust account may be used to defray the reasonable costs of locating the client whose funds they are. The amount that is reasonable is based on the probability of success of the particular method. An explanation of how the funds are used must be provided when the client is found.<sup>112</sup>

If ownership cannot be established, the unidentified funds must be held until the statute of limitations has run with respect to any claims that might be made for those funds. At that time, the lawyer may treat the funds as abandoned property under section 55-210.1 *et seq.* of the Virginia Code.<sup>113</sup>

Lost checks are considered in LEO 415. This opinion allows the lawyer to segregate the funds represented by a missing check and hold them in a separate interest-bearing instrument until the matter is resolved.

Before a lawyer may make disbursements from the trust account on behalf of a client, the lawyer must have available funds in the account on that client's behalf. In

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<sup>106</sup> Rule 1.15(a)(3)(ii).

<sup>107</sup> LEO 996; Philadelphia Bar Ass'n Professional Guidance Comm., Op. 91-40.

<sup>108</sup> 442 N.E.2d 171 (Ill. 1982).

<sup>109</sup> Michigan Ethics Op. CI-1143.

<sup>110</sup> LEO 458.

<sup>111</sup> LEO 1644. *But see* LEO 458, which permits a Legal Aid Society office to obtain a client's written consent to treat unused client funds as a donation, provided a full explanation is given and no undue pressure is exerted upon the client.

<sup>112</sup> LEO 1673.

<sup>113</sup> LEO 832. The Standing Committee on Legal Ethics is unwilling to opine whether there are alternatives for the disposition of unclaimed funds in addition to the abandoned property statute. LEO 1644.

determining whether funds deposited on a client's behalf are available for disbursement, Virginia opinions make a distinction between transactions subject to the statutes governing real estate settlement procedures (hereinafter "RES statutes," formerly the Wet Settlement Act) and other transactions.

In transactions subject to the RES statutes,<sup>114</sup> a lawyer may disburse funds immediately against loan funds received in any of the forms permitted by the Act.<sup>115</sup> The permissible forms of loan funds include cash; wired funds; certified checks; checks issued by the state or a political subdivision of the state; cashier's and teller checks; checks issued by a financial institution in the fifth Federal Reserve district, the accounts of which are insured by an agency of the federal government; drafts issued by a federally chartered credit union that are drawn on the United States Central Credit Union; checks issued by an insurance company subject to regulation by the State Corporation Commission that are drawn on a financial institution in the fifth Federal Reserve district with insured accounts; and checks issued by a federal or state savings and loan or savings bank operating in Virginia that are drawn on the Federal Home Loan Bank of Atlanta.<sup>116</sup> While acknowledging that this will result in using the funds of other clients when disbursement is made against checks representing loan funds that have not been collected, the Standing Committee on Legal Ethics nevertheless believes the risk of loss is sufficiently small given the magnitude of inconvenience to justify application of RES statutory principles. A lawyer who receives instructions from a lender that prevent compliance with the RES statutes must request the lender to revise its instructions.<sup>117</sup> A lawyer acting as settlement agent may not deliver the proceeds before recordation of the applicable instruments.<sup>118</sup>

Even with the relatively liberal rules of the RES statutes, there are some basic limitations on the funding of real estate settlements that apply to other transactions as well. Disbursements cannot be made with postdated checks<sup>119</sup> or with instructions not to negotiate the check until the following day,<sup>120</sup> nor may disbursements be made against a cashier's check that has been deposited after the bank has officially closed for the day.<sup>121</sup>

It should be emphasized that the scope of the RES statutes is relatively narrow, as it applies only to the funds for financing of property with no more than four residential units.<sup>122</sup> It does not apply to cash transactions or mortgage financing

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<sup>114</sup> Va. Code §§ 55-525.8 to -525.15.

<sup>115</sup> LEOs 753, 454, 183, 1255. LEO 183 is followed by an Editor's Note incorporating by reference all subsequent amendments to the RES statutes.

<sup>116</sup> Va. Code § 55-525.8. LEO 1466 provides that a lawyer disbursing funds in a real estate transaction to the seller's lawyer must use one of the forms of disbursement enumerated in the RES statutes .

<sup>117</sup> LEOs 1255, 900. *Cf.* LEO 1565.

<sup>118</sup> Va. Code § 55-525.11; LEOs 663, 281. While LEO 813 indicates that it may not be an ethical violation if all interested parties have agreed upon an earlier disbursement, this opinion appears to have been overruled by LEO 1116. The RESA statutes provide that a settlement agent may record documents before disbursement with the consent of all parties to the transaction. Va. Code § 6.1-2.23(D). *See also* LEO 900.

<sup>119</sup> Connecticut Informal Ethics Op. 90-13; New Jersey Ethics Op. 609.

<sup>120</sup> LEO 614.

<sup>121</sup> LEO 898.

<sup>122</sup> Va. Code § 55-525.9.

for projects that involve something other than four or fewer residential units. Furthermore, it only applies to funds provided by the lender and does not cover, for example, funds provided by the client to cover the costs of the transaction. Transactions or funds outside the scope of the RES statutes should satisfy the requirements set forth below.

Outside the RES statutes, a very different rule applies as to when funds are available for disbursement, and the principles of the RES statutes may not be followed.<sup>123</sup> Four legal ethics opinions pertaining to the disbursement of insurance proceeds to clients make it very clear that in transactions that are not covered by the RES statutes, disbursements may only be made from collected funds regardless of the creditworthiness of the maker of the check and regardless of any arrangements the lawyer has made with the bank as to the immediate availability of funds.<sup>124</sup> These opinions take the very firm position that disbursements for a client from deposits that are not collected funds represent an impermissible use of the funds of one client to cover checks written on behalf of another client.

It is important to remember that there is a distinction between collected and available funds. In general, funds are likely to be available before they are collected. Funds are available when they are credited against a depositor's account. Even though available, the funds are subject to being charged or offset if the deposited instrument is subsequently not paid. Funds are collected when they have been irrevocably credited to an account and may not be charged. A lawyer who uses a bank that has a policy on the crediting of funds which would cause an otherwise appropriate check on the lawyer's trust account to be dishonored will violate Rule 1.3 if he or she continues to use the bank with this knowledge.<sup>125</sup>

*In re Moras*<sup>126</sup> is a good example of the problems that result when a well-meaning lawyer ignores the requirement of only drawing on collected funds. In *Moras*, the lawyer was approached by a long-time and trusted client who asked the lawyer to exchange an escrow account check for the client's personal check. The escrow account check was needed to stave off a pending financial crisis. The next day, the lawyer discovered there were not sufficient funds in the client's account to cover the client's check, but took no action to stop payment on the escrow account check. A protracted negotiation with the client ensued, which ultimately resulted in the lawyer recovering the full amount of the escrow account check from his client. While the New Jersey court found that the lawyer had not made a knowing misuse of his other clients' funds in covering the escrow account check to the client in question, a suspension was still appropriate.

The trust account offense of conversion occurs when a client's funds are diverted to a purpose other than for the benefit of the client or not in accordance with

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<sup>123</sup> LEO 614.

<sup>124</sup> LEOs 704, 1256, 1248, 1021.

<sup>125</sup> LEO 1797.

<sup>126</sup> 619 A.2d 1007 (N.J. 1993).



the client's directions. Conversion is the most serious of trust account offenses—the punishment is presumptively disbarment.<sup>127</sup>

In its simplest form, conversion consists of a lawyer intentionally using trust account funds for his or her own benefit.<sup>128</sup> It also results from unauthorized loans to third parties,<sup>129</sup> loans to the lawyer,<sup>130</sup> or the use of one client's funds for the benefit of another client.<sup>131</sup> Advances of costs of litigation on behalf of other clients and payment of payroll taxes from trust account funds constitute conversion.<sup>132</sup> The conversion need not be voluntary but may result from a levy on client funds in the lawyer's possession.<sup>133</sup>

Conversion occurs any time the balance in a lawyer's trust account is less than the amount of client funds that are supposed to be in that account.<sup>134</sup> Deposit of a client's funds into an overdrawn trust account is conversion without more.<sup>135</sup> State of mind, evil intentions, or ultimate loss to the client are not relevant to determining whether a conversion has occurred.<sup>136</sup>

*Committee on Professional Ethics & Conduct v. Brodsky*<sup>137</sup> indicates the breadth of the conversion concept. Brodsky had instructed his broker to purchase stock for the benefit of a client trust. Some five weeks after the instruction, he discovered that the broker, while making the purchase from his client's funds, had erroneously credited the stock to the lawyer's personal account and that the stock had declined in value. Brodsky at that point determined to keep the stock and make the client whole by reimbursing the trust for the cost of the stock. Brodsky testified he had taken this action for fear his client would lose trust in him. While Brodsky ultimately sold the stock for a profit that he kept, the court focused on his decision to keep the stock and reimburse the client as the point of conversion. The court found that once Brodsky had determined the stock had been erroneously credited to his account, he should have taken prompt action to have it transferred to the name of his client regardless of the loss. His failure to do so constituted conversion for which he was disciplined.

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<sup>127</sup> *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 45:506. Conversion of property belonging to a non-client may be a violation of Rule 8.4. *Annotated Model Rules*, *supra* note **Error! Bookmark not defined.**, at 269.

<sup>128</sup> *In re Warhaftig*, 524 A.2d 398 (N.J. 1987); *In re Hollendonner*, 504 A.2d 1174 (N.J. 1985); *State v. Aldrich*, 237 N.W.2d 689 (Wis. 1976).

<sup>129</sup> *Cogdill v. First Dist. Comm.*, 221 Va. 376, 269 S.E.2d 391 (1980).

<sup>130</sup> *Attorney Grievance Comm'n v. Pattison*, 441 A.2d 328 (Md. 1982).

<sup>131</sup> *Office of Disciplinary Counsel v. Kanuck*, 535 A.2d 69 (Pa. 1987).

<sup>132</sup> *In re James*, 548 A.2d 1125 (N.J. 1988).

<sup>133</sup> *In re Enstrom*, 472 N.E.2d 446 (Ill. 1984).

<sup>134</sup> *Delk v. Virginia State Bar*, 233 Va. 187, 355 S.E.2d 558 (1987); *Doyle v. State Bar*, 648 P.2d 942 (Cal. 1982); *In re Clayter*, 399 N.E.2d 1318 (Ill. 1980); *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 45:501.

<sup>135</sup> *In re Franklin*, 516 A.2d 171 (D.C. 1986). *But see Grievance Committee of the Board of Overseers of the Maine Bar*, Op. 43, which implied that a lawyer might have a period of time to cover an overdraft created solely by funds deposited but not available in his or her account.

<sup>136</sup> *Maddy v. First Dist. Comm. of Va. State Bar*, 205 Va. 652, 139 S.E.2d 56 (1964); *Delk v. Virginia State Bar*, 233 Va. 187, 355 S.E.2d 558 (1987); *Wright v. Virginia State Bar*, 233 Va. 491, 357 S.E.2d 518 (1987).

<sup>137</sup> 318 N.W.2d 180 (Iowa 1982).

While a lawyer may well have the same duties as to funds entrusted to the lawyer by third parties as the lawyer does to funds entrusted to the lawyer by clients,<sup>138</sup> the lawyer's duty to honor claims of third parties to client funds in his or her possession is limited. In general, a lawyer is only obliged to honor third-party claims to client funds in the lawyer's possession if there is some type of contractual obligation or independent legal obligation, such as an execution on a judgment, to do so.<sup>139</sup> In *American State Bank v. Enabnit*,<sup>140</sup> a lawyer who previously forwarded his client's funds to a creditor of the client did not become liable to the creditor when the lawyer stopped sending funds at the direction of the client. Even though there was evidence the creditor had forbore action on the basis of representations of the lawyer, there was not a sufficient commitment on behalf of the lawyer to make him liable to the creditor. On the other hand, a lawyer who agreed to hold the client's funds in trust pending the resolution of a proceeding to lift a default judgment against the client was responsible to the person holding the judgment when it appeared that the client's funds were represented by a check not backed with sufficient funds.<sup>141</sup> A lawyer must also honor the client's assignment of his or her interest in a lawsuit to a third party over the objections of the client. The court found that the ethical duty to deliver a client's funds and property to him or her is superseded by the client's pre-existing assignment of those funds.<sup>142</sup>

## 1.10 MITIGATING CIRCUMSTANCES—VICARIOUS RESPONSIBILITY

Lawyers are strictly accountable for trust account violations. Good faith, inadvertence, and lack of harm are not relevant in determining whether a violation has occurred.<sup>143</sup> Drug abuse, alcoholism, general office mismanagement, or payment of restitution do not provide defenses to trust account violations.<sup>144</sup> Nor do consent or ratification by the client.<sup>145</sup> Retroactive approval or consent by the client to loans, even where the client had made loans to the lawyer in the past, is not sufficient to prevent disbarment.<sup>146</sup> At the most, these factors may mitigate the punishment that is imposed.<sup>147</sup> A lawyer who has a certified public accountant to keep the lawyer's books

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<sup>138</sup> See *supra* ¶ 1.3.

<sup>139</sup> Rule 1.15 Comment [4]; Hazard & Hodes, *supra* note **Error! Bookmark not defined.**, at § 19.6. See also Connecticut Bar Comm. on Prof'l Ethics, Op. 94-8. LEO 1747 found such a third party obligation when a lawyer agreed to pay a client's medical bills from an anticipated recovery on behalf of the client.

<sup>140</sup> 471 N.W.2d 829 (Iowa 1991).

<sup>141</sup> *Director Door Corp. v. Marchese & Sallah, P.C.*, 127 A.D.2d 735 (N.Y. 1987). A lawyer who holds funds in escrow pending the resolution of competing claims of a client and a third party is representing conflicting interests and the full disclosure and consent of all affected parties is required. Nebraska Ethics Op. 87-4.

<sup>142</sup> *Bonanza Motors v. Webb*, 657 P.2d 1102 (Idaho Ct. App. 1983).

<sup>143</sup> *Annotated Model Rules*, *supra* note **Error! Bookmark not defined.**, at 252.

<sup>144</sup> Mental illness, though not permitted as a defense, may be taken into consideration as mitigation. *Florida Bar v. Condon*, 647 So. 2d 823 (Fla. 1994); *In re Howle*, 363 S.E.2d 693 (S.C. 1988).

<sup>145</sup> *In re Haupt*, 297 S.E.2d 284 (Ga. 1982).

<sup>146</sup> *In re Pierson*, 690 A.2d 941 (D.C. 1997).

<sup>147</sup> *In re Deragon*, 495 N.E.2d 831 (Mass. 1986); *In re Brown*, 427 S.E.2d 645 (S.C. 1993); *In re Glasschroeder*, 335 N.W.2d 621 (Wis. 1983); *In re Peckham*, 340 N.W.2d 198 (Wis. 1983); *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 45:504, 45:507, 45:508; Downey, *supra* note **Error! Bookmark not defined.**, at 278.

is responsible for trust account violations that occur as a result of the CPA's inadequate bookkeeping. At the very least, a lawyer has the duty to make sure the CPA understands the rules regarding trust accounts.<sup>148</sup>

The personal accountability of a lawyer for the lawyer's trust account is the basis of a Connecticut opinion that finds it improper for a lawyer to "loan" his trust account to a former partner to allow him to conduct a real estate closing. The opinion finds that the practice creates a misimpression as to the responsibility for the closing that approaches fraud.<sup>149</sup>

A lawyer may not ignore the bookkeeping side of the practice to attend to substantive matters on behalf of clients and to build the practice.<sup>150</sup> The duty of a lawyer to use proper office procedures extends to the proper supervision and management of his or her employees.<sup>151</sup> The lawyer must maintain strict oversight over the employees as the lawyer's duties with respect to the trust account are not delegable.<sup>152</sup> The ABA Model Record Keeping Rules require that only lawyers make withdrawals from trust accounts.<sup>153</sup> Ethics decisions of several jurisdictions, while not imposing a lawyer-only rule, have made it very clear that lawyer signatures are a preferable control over the disbursement of trust account funds.<sup>154</sup> While the liability for an ethical violation of partners of a lawyer in violation of the trust account rules is unclear, the innocent partners do have civil liability for their partner's defalcations.<sup>155</sup>

An example of lawyer liability for the actions of others is found in *In re Scanlan*.<sup>156</sup> Scanlan hired a secretary without checking her references and did not discover she was under indictment for embezzlement. Scanlan subsequently discovered that the secretary was stealing funds from his office account. Scanlan agreed not to fire the secretary on the condition that she make restitution. Unbeknownst to him, the secretary made restitution from Scanlan's trust account.<sup>157</sup> The secretary also loaned Scanlan \$10,000, which she said came from the sale of her house, to help him through hard times. In fact the money came from Scanlan's trust account. Even though the court found that the bank had erroneously paid some of the checks, it upheld Scanlan's suspension on the grounds that he had failed to adequately supervise his employee.

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<sup>148</sup> See *Florida Bar v. Weiss*, 586 So. 2d 1051 (Fla. 1991).

<sup>149</sup> Connecticut Bar Comm. on Professional Ethics, 93-19.

<sup>150</sup> *In re Johnson*, 520 A.2d 3 (N.J. 1987).

<sup>151</sup> See, e.g., *Florida Bar v. Carlton*, 366 So. 2d 406 (Fla. 1978) (secretary's self-help in protecting her salary contributed to trust account problem); *Attorney Grievance Comm'n v. Dacy*, 542 A.2d 841 (Md. 1988) (commingling violation was found from secretary's efforts to expedite availability of funds at real estate closing).

<sup>152</sup> Michigan Formal Ethics Op. R-7 (1990).

<sup>153</sup> *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 45:1005.

<sup>154</sup> California Standing Comm. on Professional Responsibility and Conduct, Formal Op. 88-87; Michigan Formal Ethics Op. R-7; Minnesota Ethics Op. 12.

<sup>155</sup> *Blackmon v. Hale*, 463 P.2d 418 (Cal. 1970).

<sup>156</sup> 697 P.2d 1084 (Ariz. 1985).

<sup>157</sup> Scanlan apparently did not review his accounts after the defalcation or put any safeguards in place.

## SECTION 2: BUSINESS TRANSACTIONS WITH CLIENTS

### 2.1 IN GENERAL

Lawyers' business transactions with their clients have always invoked serious scrutiny by the courts. In 1850, the United States Supreme Court declared:

There are few of the business relations of life involving a higher trust and confidence than that of attorney and client, or, generally speaking, one more honorably and faithfully discharged; few more anxiously guarded by the law, or governed by sterner principles of morality and justice; and it is the duty of the court to administer them in a corresponding spirit, and to be watchful and industrious, to see that confidence thus reposed shall not be used to the detriment or prejudice of the rights of the party bestowing it.<sup>158</sup>

Contemporary commentators have been more direct in admonishing lawyers to steer clear of business relationships with clients. Professor Wolfram noted: "Much can be said in favor of an absolute prohibition against a lawyer having nonprofessional business relationships with a client."<sup>159</sup> While lawyers are subject to the general duties of loyalty expected of fiduciaries,<sup>160</sup> because of their supposed superior knowledge and skill and the client's confidence that that skill and knowledge will be used for the client's benefit, lawyers have been held to very high standards in justifying their business relationships with clients.<sup>161</sup> The ABA has identified a lawyer's inappropriate involvement in a client's interests as one of the top ten malpractice traps.<sup>162</sup> Nevertheless, lawyers continue to become involved in business relationships with their clients. Not only do these relationships offer lawyers additional opportunities to use their knowledge and judgment on behalf of clients,<sup>163</sup> they also offer the opportunity for financial reward.

The concerns regarding a lawyer's business dealings with a client<sup>164</sup> find their expression in Rule 1.8(a), which provides as follows:

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<sup>158</sup> *Stockton v. Ford*, 52 U.S. 232, 247 (1851).

<sup>159</sup> Wolfram, *supra* note **Error! Bookmark not defined.**, at 479.

<sup>160</sup> *See, e.g., Restatement (Second) of Agency* §§ 403, 404 (1958).

<sup>161</sup> *Restatement of the Law Governing Lawyers* § 126 cmt. a; *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 51:503; Hazard & Hodes, *supra* note **Error! Bookmark not defined.**, at § 12.4; *see also Restatement (Second) of Agency* § 390 (1958).

<sup>162</sup> *Malpractice Desk Guide*, *supra* note **Error! Bookmark not defined.**, at 42.

<sup>163</sup> Wolfram, *supra* note **Error! Bookmark not defined.**, at 479.

<sup>164</sup> A client for these purposes is anyone who relies on a lawyer for legal services, even if only on an occasional basis. *Annotated Model Rules*, *supra* note **Error! Bookmark not defined.**, at 147.

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.<sup>165</sup>

The scope of the rule regarding business dealings with clients is not limited to direct lawyer-client relationships but extends to lawyers who are affiliated with the client's lawyer<sup>166</sup> and to clients doing business with members of the lawyer's family to the extent the lawyer serves as an intermediary.<sup>167</sup>

## 2.2 ACTIVITIES AND RELATIONSHIPS

Almost any type of economic relationship between a lawyer and a client, other than cash remuneration for services rendered, is a potential business transaction subject to Rule 1.8(a). An equal sharing of profits and losses and the alleged lack of adversity of interests as a result of the equality do not save a transaction from the principles of Rule 1.8(a).<sup>168</sup> The only economic relationships that are clearly excluded are standard commercial transactions between a lawyer and client that are substantially the same as commercial transactions between the client and third parties.<sup>169</sup>

Loans from a client to a lawyer invoke the principles of Rule 1.8(a),<sup>170</sup> as do loans from the lawyer to the client<sup>171</sup> and guarantees of a client's obligations by a

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<sup>165</sup> Rule 1.8 is reproduced in its entirety at Appendix 1. Criteria similar to the rules of Rule 1.8(a) are also used in evaluating a lawyer's civil liability to a client in a joint business undertaking. Closely related to Rule 1.8(a) is Rule 1.8(b), which prohibits a lawyer from using information relating to the representation of a client for the advantage of the lawyer or a third party or to the disadvantage of the client unless the client consents after consultation or the information is obtained independently of the attorney-client relationship. Some of the authority cited in this section refers to DR 5-104(A), the CPR counterpart of Rule 1.8(a), as there does not appear to be any substantive difference between the two provisions on the points in question.

<sup>166</sup> Rule 1.8(k); *Restatement of the Law Governing Lawyers* § 126 cmt. a.

<sup>167</sup> Rhode Island Ethics Op. 93-4.

<sup>168</sup> *Committee on Prof'l Ethics & Conduct v. Qualley*, 487 N.W.2d 327 (Iowa 1992).

<sup>169</sup> *Annotated Model Rules*, *supra* note **Error! Bookmark not defined.**, at 146. It appears that this exclusion applies when the lawyer is the consumer in these transactions rather than the purveyor of goods or services. *Restatement* § 126. An ancillary business is not considered a standard commercial transaction. *Id.*, cmt. c. See *infra* ¶ 2.5, Ancillary Businesses.

<sup>170</sup> *Heubusch v. Boone*, 213 Va. 414, 192 S.E.2d 783 (1972); *In re Watkins*, 534 S.E.2d 794 (Ga. 2000); *In re Harris*, 741 P.2d 890 (Or. 1987); Model Rule 1.8(a) cmt. 1; LEO 1489.

lawyer.<sup>172</sup> Purchasing assets from clients,<sup>173</sup> purchasing a judgment against a client,<sup>174</sup> and participating in a business enterprise with a client all invoke the business transaction rules.<sup>175</sup>

The lawyer does not have to be the person initiating or pursuing the relationship for the business transaction rules to apply. Maryland Ethics Document 86-78 addressed the issue of a client who persistently pressured his lawyer to be allowed into a partnership holding racehorse brood mares. After being admitted to the partnership, the client had a change of heart and ceased meeting his financial obligations to the partnership, claiming among other things that the lawyer had violated DR 5-104(A), the CPR counterpart of Rule 1.8(a), in bringing him into the partnership. While the Maryland Bar ultimately refused to take a position on the merits because of the factual issues presented, it held that DR 5-104(A) applied to the investment.

A common problem is the lawyer who takes an interest in a business enterprise or “a piece of the action” in lieu of a fee. *Committee on Professional Ethics & Conduct v. Mershon*<sup>176</sup> is an example of the pitfalls of this relationship. In that case, a lawyer, his client, and an engineer joined together in a land development enterprise. The lawyer and engineer each contributed their services in return for their interest in a new corporation to conduct the enterprise while the client contributed the land. Inability to obtain financing prevented them from carrying the transaction to fruition. The client subsequently demanded his land back. The lawyer transferred his stock back to the corporation, but the engineer refused to follow suit, leaving the client as a joint owner with the engineer of a corporation owning the land. While the lawyer was found to be honest and forthright, he was nevertheless disciplined for failing to advise his client of their differing interests and failing to advise his client how to protect the client’s interest.<sup>177</sup> Similar reasoning has also been applied to a lawyer receiving an unsecured loan from his client in lieu of a fee<sup>178</sup> and to a lawyer receiving a percentage of the profits of an enterprise as compensation for his guarantee of a loan.<sup>179</sup>

The business relationship rules also apply to indirect dealings between a lawyer and a client. Rule 1.8(a) or its equivalent has been applied to a lawyer

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<sup>171</sup> *Goldman v. Kane*, 329 N.E.2d 770 (Mass. App. Ct. 1975); *In re Drake*, 642 P.2d 296 (Or. 1982). See also LEO 1269, which proscribes an attorney’s loan of funds to a client for living expenses where the loan is secured by the client’s recovery.

<sup>172</sup> LEO 578.

<sup>173</sup> *Annotated Model Rules*, *supra* note **Error! Bookmark not defined.**, at 1495; Rhode Island Ethics Advisory Op. 88-31; LEO 340.

<sup>174</sup> New Jersey Ethics Op. 663.

<sup>175</sup> *In re Harris*, 741 P.2d 890 (Or. 1987); LEO 1027. See also LEO 1586, which applies the principles of Rule 1.8(a) to a situation where an attorney seeks to have his client sign an engagement agreement containing a mandatory arbitration clause.

<sup>176</sup> 316 N.W.2d 895 (Iowa 1982).

<sup>177</sup> See also *Monco v. Janus*, 583 N.E.2d 575 (Ill. App. Ct. 1st Dist. 1991); *In re Lowther*, 611 S.W.2d 1 (Mo. 1981); Michigan Ethics Op. MI-CI-1059; LEO 1593.

<sup>178</sup> *In re Watson*, 482 N.E.2d 262 (Ind. 1985).

<sup>179</sup> *In re Bishop*, 686 P.2d 350 (Or. 1984).

purchasing property from the sole beneficiary of an estate represented by the lawyer,<sup>180</sup> to a partnership of which the lawyer was a general partner selling a liquor license to the lawyer's client,<sup>181</sup> and to a purchase of property from a client by a lawyer's corporate alter ego.<sup>182</sup>

The courts will resolve uncertainties as to the existence of a lawyer-client relationship in favor of the relationship for purposes of extending the principles of Rule 1.8(a) to the relationship.<sup>183</sup> *In re Gant*<sup>184</sup> involved a lawyer who, with his wife and a client and the client's wife, entered into a partnership. Even though the lawyer prepared some documents pertaining to the partnership, he claimed that no lawyer-client relationship existed. The court ruled that when a lawyer is a partner in a business partnership that had no outside lawyer, it will be presumed that he or she did some legal work on behalf of the partnership. A similar analysis was used in *Worth v. State Bar*,<sup>185</sup> in which a lawyer claimed he was acting as an investment promoter and not as a lawyer. Even where a lawyer-client relationship does not exist, courts may find a fiduciary relationship that produces similar obligations as the lawyer-client relationship.<sup>186</sup>

### 2.3 PROHIBITED ECONOMIC RELATIONSHIPS

Except for a lien to secure fees and expenses or a reasonable contingent fee in a civil case, a lawyer may not acquire a proprietary interest in the cause of action or subject matter of litigation he or she is undertaking for a client.<sup>187</sup> The ABA has interpreted this prohibition to require that a lawyer retain other counsel to prosecute a claim the lawyer holds jointly with a client.<sup>188</sup> The ABA has also opined that the rule prevents a lawyer who is handling an FCC license application from taking an ownership interest in the applicant as compensation. The opinion reasoned that the ownership interest in the applicant is essentially an ownership interest in the success of the licensing proceeding.<sup>189</sup> If followed, this opinion would appear to preclude an ownership interest as compensation in almost any licensing situation. The District of Columbia has refused to follow the ABA position and has allowed ownership interests in FCC applicants to be given to lawyers as compensation. The District of Columbia

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<sup>180</sup> *In re McGlothlen*, 663 P.2d 1330 (Wash. 1983).

<sup>181</sup> *Attorney Grievance Comm'n v. Collins*, 457 A.2d 1134 (Md. 1983).

<sup>182</sup> *Sodikoff v. State Bar*, 535 P.2d 331 (Cal. 1975).

<sup>183</sup> *Nicholson v. Shockey*, 192 Va. 270, 64 S.E.2d 813 (1951) (formality not an essential element of employment of an attorney; a contract may be express or implied). *But see Freeman v. Lauritzen*, H028531, 2006 Cal. App. LEXIS Unpub. 3906, 2006 WL 1195916 (Cal. App. 6th Dist. filed May 5, 2006), where no attorney-client relationship was found.

<sup>184</sup> 645 P.2d 23 (Or. 1982).

<sup>185</sup> 551 P.2d 16 (Cal. 1976).

<sup>186</sup> *Heine v. Colton, Hartnick, Yamin & Sheresky*, 786 F. Supp. 360 (S.D.N.Y. 1992).

<sup>187</sup> Rule 1.8(j).

<sup>188</sup> ABA Informal Op. 1397.

<sup>189</sup> ABA Formal Op. 279.

reasoned that the interests were more in the nature of a contingent fee than an interest in the litigation itself.<sup>190</sup>

Virginia treats an assignment of proceeds in marital property to pay a lawyer's fees in a domestic proceeding to be a prohibited interest in litigation except in narrow circumstances. For the exception to apply, all matters relating to the use, possession, division, and sale of the property must be conclusively adjudicated in a final order. Even then, the client must consent after full disclosure, the terms of the transaction must be fair and reasonable, and the client must be advised that he or she may seek independent representation and be given an opportunity to do so.<sup>191</sup>

A lawyer representing a client in connection with contemplated or pending litigation may not guarantee or advance financial assistance to the client. The lawyer may advance the costs and expenses of litigation as long as the client remains liable for such expenses.<sup>192</sup> The lawyer may also guarantee the litigation-related charges made by the client's physician as long as the client remains ultimately liable for those charges.<sup>193</sup> A lawyer may also execute a contract with a client's healthcare provider authorizing payment of fees owed to that provider from the client's recovery.<sup>194</sup> Advances for expenses for indigent defendants<sup>195</sup> is the only exception to this rule.<sup>196</sup>

While a lawyer can ask a finance company to make a loan to a client<sup>197</sup> or make loans himself or herself to clients of other lawyers,<sup>198</sup> other indirect actions to avoid the prohibition on advancing expenses have met with little success.<sup>199</sup> A lawyer may not have one client loan money to the lawyer's personal injury clients while their cases are pending,<sup>200</sup> nor may the lawyer loan money to a loan company that will make

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<sup>190</sup> District of Columbia Ethics Op. 179.

<sup>191</sup> Rule 1.5(d); LEO 1653.

<sup>192</sup> Rule 1.8(e)(1).

<sup>193</sup> LEO 582. The Committee specifically notes here and at other relevant opinions that Rule 1.8(e)(2) permits an attorney to pay litigation costs and expenses on behalf of an indigent client. See also LEOs 1060 and 1237, which hold that a client's refusal to reimburse costs advanced by the attorney does not *per se* require that the attorney file suit to recover the funds, but that a "consistent policy of not proceeding against clients for collection of expenses advanced" would be improper.

<sup>194</sup> LEO 1182. The Committee cautions, however, that since such a contract could interfere with the attorney-client relationship, a release or waiver signed by the client authorizing direct payment to the provider may be more effective.

<sup>195</sup> Rule 1.8(e)(2). Before the adoption of the Rules of Professional Conduct, it appeared that the exception for indigent defendants may have been limited to death penalty cases. See LEO 997.

<sup>196</sup> *Shea v. Virginia State Bar*, 236 Va. 442, 374 S.E.2d 63 (1988); Connecticut Informal Ethics Op. 90-3; Pennsylvania Professional Guide Op. 86-8; LEO 485. An attorney may compromise a claim in litigation for advanced expenses against a former client for less than the amount owed as long as a valid agreement requiring the reimbursement of expenses was in effect at the outset of the representation. Ohio Supreme Court Bd. of Comm'rs on Grievances and Discipline, Op. 94-5.

<sup>197</sup> LEO 1155. The practice was approved as long as the lawyer guaranteed the loan. LEO 1379 takes the analysis further, holding that an attorney may supervise his or her client's execution of the lender's documents at the attorney's office and subsequently return those documents to the lender.

<sup>198</sup> South Carolina Bar Ethics Op. 92-06.

<sup>199</sup> A lawyer cannot refer a client to a finance company for a loan to pay the lawyer's fee when the finance company requires that the lawyer pay a percentage of the fee to the finance company. Ohio Supreme Court Bd. of Comm'rs on Grievances and Discipline, Op. 94-7.

<sup>200</sup> LEO 1219. The opinion notes this practice may also present issues of champerty and maintenance.



loans to clients, even if the funds are not earmarked for the clients and the lawyer will have no influence in the ultimate lending decision.<sup>201</sup>

Publication or literary rights are given special attention by the Rules. A lawyer may 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 until the conclusion of all aspects of the matter giving rise to the representation of a client.<sup>202</sup>

## 2.4 FULL AND ADEQUATE DISCLOSURE; INDEPENDENT COUNSEL

A lawyer who enters into a business relationship with a client is held to a higher standard than simple arm's length dealing.<sup>203</sup> The lawyer is held to the highest good faith. In approaching the issue of disclosure, the lawyer should acknowledge that he or she is about to undertake a transaction which is presumptively invalid<sup>204</sup> and should remember that he or she will be deemed to occupy a position of superior knowledge and skill and any ambiguities or uncertainties will be construed against the lawyer.<sup>205</sup> In many cases, the lawyer must be able to look beyond personal and business relationships that may create a false sense of security<sup>206</sup> and remember that he or she will bear the burden of justifying that the required level of disclosure has been met.<sup>207</sup>

In only a very few cases are a lawyer's clients found to be sufficiently informed and sophisticated for the lawyer to avoid significant disclosure to the client. In *Atlantic Richfield Co. v. Sybert*,<sup>208</sup> a lawyer arranged a sale between two of his clients. The clients were aware they shared a common lawyer. The clients subsequently closed the transaction directly without paying the lawyer the real estate commission to which the seller had allegedly agreed. The seller (Atlantic Richfield) defended the claim on the grounds that proper disclosure had not been made. The court found that the lawyer's relatively informal disclosure was appropriate, as each client was sophisticated in business matters and each of them had its own general counsel to which it looked for legal advice. The court noted that the lawyer had acted only as

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<sup>201</sup> LEO 1441.

<sup>202</sup> Rule 1.8(d). Note that Rule 1.6, pertaining to confidentiality, may independently prohibit the use of information in these circumstances.

<sup>203</sup> *Abstract & Title Corp. v. Cochran*, 414 So. 2d 284 (Fla. Dist. Ct. App. 4th Dist. 1982).

<sup>204</sup> See *Thomas v. Turner's Adm'r*, 87 Va. 1, 12 S.E. 149 (1890) ("All dealings between attorney and client, for the benefit of the former, are presumptively fraudulent and void."); see also *Livermon v. Lloyd*, 155 Va. 940, 157 S.E. 146 (1931) and *Norman v. Insurance Co. of N. Am.*, 218 Va. 718, 239 S.E.2d 902 (1978) (client may presume that his or her attorney has no interest that will interfere with the attorney's devotion to the client's cause).

<sup>205</sup> Hazard & Hodes, *supra* note **Error! Bookmark not defined.**, at § 12.4.

<sup>206</sup> *Malpractice Desk Guide*, *supra* note **Error! Bookmark not defined.**, at 156.

<sup>207</sup> *Thomas v. Turner's Adm'r*, 87 Va. 1, 12 S.E. 149 (1890); *Bruce's Ex'x v. Bibb's Ex'x*, 129 Va. 45, 105 S.E.2d 570 (1921); *Lowrey v. Will of Smith*, 543 So. 2d 1155 (Miss. 1989); *In re McGlothlen*, 663 P.2d 1330 (Wash. 1983); Wolfram, *supra* note **Error! Bookmark not defined.**, at 481.

<sup>208</sup> 456 A.2d 20 (Md. 1983).

broker, but had he participated in actual negotiations, a more stringent standard might have been applied.<sup>209</sup>

The explicit requirement of the opportunity to seek the advice of independent counsel was not found in DR 5-104(a), the CPR equivalent of Rule 1.8(a). Even so, many courts looked to the presence of independent counsel or the lawyer's advice to clients that they should consult with independent counsel as being an important element of the required disclosure.<sup>210</sup>

The lawyer's disclosure concerning independent counsel should be meaningful. A simple reference that the lawyer was agreeable to having someone else look at the papers,<sup>211</sup> or a suggestion that the client get independent counsel, is not sufficient.<sup>212</sup> The lawyer must convey to the client sufficient information to know why independent counsel is important.

At least one court has held that even when a client consults independent counsel, that counsel must take care to address obvious concerns and issues before the presumptive invalidity of a transaction between a client and a lawyer is overcome. *In re Will of Moses*<sup>213</sup> concerned a lawyer who was a beneficiary of a will prepared by a third-party lawyer for the beneficiary lawyer's client. The beneficiary lawyer argued that the presence of independent advice showed there was no undue influence. The court refused to find the presumption of undue influence arising from the lawyer's confidential relationship with his client to be rebutted. It focused on the drafting lawyer's failure to question the client as to why she was ignoring her family in favor of the beneficiary lawyer and to explore the client's relationship with the beneficiary lawyer. The court found that the drafting lawyer had not rendered sufficiently meaningful advice to negate the presumption of undue influence.<sup>214</sup>

Full disclosure means more than simple disclosure of the terms of the transaction. The lawyer must disclose and discuss with the client all relevant facts and circumstances the client needs to make a decision.<sup>215</sup> In particular, the disclosure should focus on the differing interests of the lawyer and client and how those differing

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<sup>209</sup> See also *Pollock v. Marshall*, 462 N.E.2d 312 (Mass. 1984) (client's sophistication minimized disclosure required of lawyer who received equity interest in his client).

<sup>210</sup> Timothy R. Bevevino, Comment, *Attorney-Client Business Transactions: An Analysis of the Ethical Problems*, 6 J.L. & Com. 443, 459-61 (1986); Kristina M. Crosswell, Comment, *Attorney Client Relationship—Undue Influence—Fiduciary Duty Mandates That Attorney Advise Client to Secure Independent Advice and Counsel Before Accepting Benefit from Client*, 60 Miss. L.J. 657 (1990). At least one commentator has taken the position that despite the textual differences on independent counsel, Rule 1.8 and DR 5-104(A) are functionally equivalent in their application. Hazard & Hodes, *supra* note **Error! Bookmark not defined.**, at 262.

<sup>211</sup> *In re Gant*, 645 P.2d 23 (Or. 1982).

<sup>212</sup> *In re Smyzer*, 527 A.2d 857 (N.J. 1987).

<sup>213</sup> 227 So. 2d 829 (Miss. 1969). *But see Mullins v. Ratcliff*, 515 So. 2d 1183 (Miss. 1987).

<sup>214</sup> Rule 1.8(c) forbids a lawyer to solicit, for the lawyer or his or her relative, any substantial gift from a client. The rule also prohibits a lawyer from drafting an instrument that gives the lawyer or relative a substantial gift, including a testamentary gift, unless the lawyer is related to the client.

<sup>215</sup> See *In re Bruce's Ex'x v. Bibb's Ex'x*, 129 Va. 45, 105 S.E.2d 570 (1921) (attorney must disclose to client all information and advice he or she would have been bound to give if he or she was not interested in the transaction); see also *Musselman v. Willoughby Corp.*, 230 Va. 337, 337 S.E.2d 724 (1985).

interests may affect the lawyer's exercise of discretion on behalf of the client.<sup>216</sup> The disclosure should address not only actual conflicts but potential conflicts as well.<sup>217</sup> Any potential interest of the lawyer that may affect either his or her judgment or loyalty to the client must be disclosed. It may be necessary for the lawyer to disclose his or her own financial condition to the client, particularly when that would be a material consideration to a third party in a similar transaction.<sup>218</sup> Obvious risks, such as the implications of making a usurious loan, must also be disclosed.<sup>219</sup> In cases where a lawyer is receiving a commission for putting clients in a transaction, it has been held that the lawyer must do more than simply disclose the commission. The lawyer must make an affirmative effort to exercise due diligence in investigating the opportunity on behalf of the client.<sup>220</sup> A lawyer may have a duty to disclose less costly alternatives to the client, even if the lawyer is "at the market."<sup>221</sup> Doubts as to the adequacy of the disclosure are to be resolved in favor of the client.<sup>222</sup> There is a strong preference for written disclosure, although there is no absolute requirement that disclosure be in writing.<sup>223</sup>

A lawyer who confronts the scope of the required disclosure must acknowledge that in some cases it will not be possible to give the disclosure as fully as required. It is not appropriate for a lawyer to ask for consent if a disinterested lawyer would determine that the client should not agree to the transaction. A Florida opinion pertaining to lawyers owning an insurance agency found that the possible conflicts were such that they could not be cured by consent. The opinion noted that the conflict that results when the lawyer gives the client advice on whether the client must have insurance and the type and amount of insurance is so significant that it is not appropriate for the lawyer to ask for the client's consent to attempt to resolve it.<sup>224</sup>

## 2.5 ANCILLARY BUSINESSES

For many years the American Bar Association took the view that it was improper for lawyers to engage in almost any business activity concurrently with the practice of law.<sup>225</sup> In recent years, barriers to joint occupations have broken down due to the increasing interdisciplinary nature of the practice of law,<sup>226</sup> the desire of

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<sup>216</sup> *In re James*, 452 A.2d 163 (D.C. 1982); *Committee on Prof'l Ethics & Conduct v. Mershon*, 316 N.W.2d 895 (Iowa 1982); *In re Bishop*, 686 P.2d 350 (Or. 1984).

<sup>217</sup> Bevevino, *supra* note **Error! Bookmark not defined.**, at 452.

<sup>218</sup> *In re Johnson*, 826 P.2d 186 (Wash. 1992).

<sup>219</sup> *Heubusch v. Boone*, 213 Va. 414, 192 S.E.2d 783 (1972); *Florida Bar v. Black*, 602 So. 2d 1298 (Fla. 1992).

<sup>220</sup> *In re Breen*, 830 P.2d 462 (Ariz. 1992).

<sup>221</sup> *Restatement of the Law Governing Lawyers* § 126 cmt. e.

<sup>222</sup> LEO 187.

<sup>223</sup> *In re Bishop*, 686 P.2d 350 (Or. 1984); *In re Drake*, 642 P.2d 296 (Or. 1982); *Restatement of the Law Governing Lawyers* § 126 cmt. g; Bevevino, *supra* note **Error! Bookmark not defined.**, at 457.

<sup>224</sup> Florida Ethics Op. 90-7.

<sup>225</sup> ABA Informal Ops. 709 (real estate), 520 (mortgage loans), 424 (life insurance). The ABA allowed participation in a title and abstract company if the client consented after full disclosure. ABA Informal Op. 731.

<sup>226</sup> Marjorie Meeks, *Alter[ing] People's Perceptions: The Challenge Facing Advocates of Ancillary Business Practices*, 66 Ind. L.J. 1031 (1991).

lawyers to provide “one-stop shopping” for their clients,<sup>227</sup> and of course, the additional financial reward. As a result, lawyers have become involved in a number of ancillary business activities closely related to the practice of law, such as the sale of insurance, consulting and lobbying services, and real estate sales. Lawyers’ participation in ancillary businesses presents serious ethical issues and has also been identified as an area of increasing malpractice exposure.<sup>228</sup>

Title insurance is one of several ancillary businesses that have been approved by Virginia ethics opinions. LEO 187 reverses an earlier legal ethics opinion and holds that a lawyer may purchase title insurance for clients from an entity in which the lawyer has an ownership interest if the lawyer discloses to clients the nature of their conflicting interests on the sale of the insurance and if the clients consent.<sup>229</sup> LEO 603 approves an extension of the holding of LEO 187 to a situation in which the title insurance entity occupied the same premises as the lawyer’s office and used the same employees, and the lawyer’s firm served as general counsel to the title insurance agency.<sup>230</sup> A lawyer may not be compensated by a title insurance company in which he or she has an ownership interest in a manner that is directly proportional to the volume of business or referrals to the agency.<sup>231</sup> The lawyer may, however, be given an opportunity to purchase stock in the agency in proportion to the comparative size of his or her real estate practice as long as the practice does not violate the provisions of section 38.2-4614(A) of the Virginia Code or similar state or federal anti-kickback statutes.<sup>232</sup>

Using rationales similar to those of LEO 187, Virginia has also approved a lawyer receiving a real estate commission from a client;<sup>233</sup> a lawyer participating in a real estate firm when the lawyer handles real estate closings of buyers and sellers represented by the firm;<sup>234</sup> consulting services;<sup>235</sup> billing services;<sup>236</sup> accounting services;<sup>237</sup> court reporting services;<sup>238</sup> insurance products;<sup>239</sup> bail bond services;<sup>240</sup> and human resource consultations.<sup>241</sup> Virginia has also approved a law firm using a

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<sup>227</sup> *Malpractice Desk Guide*, *supra* note **Error! Bookmark not defined.**, at 158.

<sup>228</sup> *Id.* at 43.

<sup>229</sup> See also LEOs 1647, 1564, 1152, 1072, 886, 591, 545. Other states have not been so lenient. See *In re Opinion 682 of Advisory Comm. on Professional Ethics*, 687 A.2d 1000 (N.J. 1997); Rhode Island Supreme Court Ethics Advisory Panel, Op. 96-26.

<sup>230</sup> See also LEO 712. But see LEO 1405, which prohibits a title company from paying the salaries of law firm staff.

<sup>231</sup> LEO 1564.

<sup>232</sup> LEO 1647. This LEO also appeared to approve an annual reallocation of stock among beneficiaries based on volume through a buy-sell arrangement.

<sup>233</sup> LEO 209.

<sup>234</sup> LEO 302.

<sup>235</sup> LEO 1318.

<sup>236</sup> LEO 1016.

<sup>237</sup> LEO 1163.

<sup>238</sup> LEO 1198.

<sup>239</sup> LEO 1311.

<sup>240</sup> LEO 1254.

<sup>241</sup> LEO 1658.

subsidiary organization to perform nonlegal services,<sup>242</sup> and acceptance by an attorney of a fee or commission from an entity that purchases commercial paper in exchange for referring clients who hold such paper to that entity.<sup>243</sup>

Several existing Virginia LEOs addressing the ancillary business issue appear to be grounded on both DR 5-101(A) and DR 5-104(A) of the CPR.<sup>244</sup> Other LEOs do not clearly reference the provisions of the CPR on which they are based. In none of the opinions, however, is there an explicit requirement that the client have the opportunity to seek independent counsel for the relationship to be appropriate. To the extent these opinions were based on DR 5-104(A), it appears that Rule 1.8(a) would now require the opportunity to seek independent counsel in similar situations and that the existing authority should be understood as correspondingly limited.<sup>245</sup>

A lawyer engaged in an ancillary business has a duty to keep that business separate from the lawyer's practice. LEO 1318, which pertains to a lawyer providing a single billing for a joint legal/counseling business, requires that the lawyer separately state the legal fee and the counseling fee. In accordance with the general escrow account rules regarding funds of a person other than the lawyer, the check received for the entire bill must be deposited in the lawyer's escrow account and the amount due the counseling practice disbursed in a timely fashion. The client must receive a full accounting of the disbursement of each check. In a mixed-services venture, such as a federal licensing proceeding involving technical services and legal issues where lawyers and nonlawyers join in a package of services for clients, there must be disclosure to the customer-client that the law firm participant will be separately providing legal services of a specific value.<sup>246</sup> A lawyer conducting both a law practice and an ancillary business in the same space should consider, at the very least, separate signs and separate telephone lines for each business and securing client confidences through the use of locked files or similar devices.<sup>247</sup> LEO 1658 approves a common logo and similar letterhead for a law firm and its ancillary business as long as the public is not misled or confused as to the role of each firm. The logo and name of the ancillary business must make it clear that it provides nonlegal services. LEO 1658 also approves a joint marketing approach as long as the public is not misled as to the roles of the respective entities and the ancillary business is not held out as practicing law.

Perhaps the largest ethical concern regarding ancillary businesses is the potential for tying relationships with clients and the preservation of arm's length dealings. Ethics opinions caution that the ancillary business/law practice relationships should be neither a feeder for the business' clients to the law practice

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<sup>242</sup> LEO 1083.

<sup>243</sup> LEO 1581.

<sup>244</sup> *See, e.g.*, LEOs 1658, 1564.

<sup>245</sup> Contrast the discussion of LEO 1515 in paragraph 2.6.

<sup>246</sup> District of Columbia Ethics Op. 172; *see* Arizona Ethics Op. 93-01 (concerning a lawyer's participation in a "complete eviction service" with nonlawyers).

<sup>247</sup> Florida Proposed Ethics Op. 88-15; Ohio Supreme Court Bd. of Comm'rs on Grievances and Discipline, Op. 94-9; LEO 1564.

nor a funnel for the law practice's clients to the ancillary business.<sup>248</sup> LEO 1658 indicates that referrals from the ancillary business to the law firm are permissible as long as sufficient information is provided the client to enable the client to make an informed decision.

There are other ethical issues as well. A Virginia opinion holds that as part of the required disclosure regarding business relationships, a lawyer must disclose to a client that the lawyer has a business relationship with the client's adversary.<sup>249</sup> The issue of assisting nonlawyers in the unauthorized practice of law is also implicated.<sup>250</sup> Lawyers providing temporary services to other lawyers in the form of both staff and professional legal services face significant problems in dealing with potential conflicts and disclosure of confidences as the staff and lawyers move from place to place.<sup>251</sup> The same problem confronts lawyers or law firms who employ them.

LEO 1564 addresses the issue of conflicts between a lawyer's personal interests and the interests of his or her client in the context of the ancillary business of title insurance. While lawyer ownership of title agencies is permitted, use of the agency by the lawyer's client will trigger the obligation of disclosure and consent. It is suggested that the disclosure be in writing and cover premium costs, binder fees, title examination fees, closing fees, and other charges and that a suggestion of the availability of alternative sources of title insurance be included.

A lawyer's performance of legal work or service as an officer or director of the title agency is permitted as long as there is no conflict between the performance of those activities and the client's interest. The lawyer may also conduct closings for clients for which insurance is issued by his or her agency if disclosure and consent are present. If the lawyer holds a title insurance license, however, the lawyer cannot act as an agent for the issuance of insurance involving his or her client or directly or indirectly perform all of the essential functions of such an agent.<sup>252</sup>

The lawyer may not be compensated by the agency for the volume of business referred or premiums paid by clients. The lawyer may not receive a fixed salary unless it is substantially related to work actually done, nor may the title insurance company subsidize the lawyer's overhead. Receipt by the lawyer of interest on escrow funds of the title agency is inappropriate if the lawyer "steered" the client to the title agency to avoid the prohibition against the lawyer receiving interest on escrow account funds. Periodic dividends or comparable distributions are permitted as are fees for work actually rendered or reimbursement for legitimate expenses.

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<sup>248</sup> Florida Proposed Ethics Op. 88-15; Iowa Ethics Op. 88-15; Ohio Supreme Court Bd. of Comm'rs on Grievances and Discipline, Op. 94-7; South Carolina Advisory Op. 93-05.

<sup>249</sup> LEO 1311. Presumably there would be an additional duty to check business customers for possible conflicts with legal clients. There may also be conflicts between the ancillary business and a lawyer's former client. LEO 1658.

<sup>250</sup> Los Angeles County Bar Ass'n Ethics Comm., Formal Op. 413; South Carolina Advisory Op. 93-05.

<sup>251</sup> LEO 1850; State of California Standing Comm. on Professional Ethics and Conduct, Formal Op. 1992-126; Nevada Formal Ethics Op. 6.

<sup>252</sup> Similar principles were applied to a lawyer-life insurance agent in LEO 1754.

A lawyer engaging in an ancillary business has a higher duty of care and a higher responsibility than a layperson engaged in the same business.<sup>253</sup> While authorizing ancillary business relationships, several states have cautioned that the Code of Professional Responsibility also applies to a lawyer in the conduct of the ancillary business.<sup>254</sup>

ABA Model Rule 5.7, which was not adopted by Virginia when it adopted the Rules, provides that a lawyer engaged in the provision of law-related services will be subject to the Rules of Professional Conduct if either (i) the services are provided to the client without distinction from the legal services provided by the lawyer; or (ii) the services are provided by a separate entity controlled by the lawyer if the lawyer fails to take reasonable steps to assure that the person using the services knows they are not legal services and the protections of the lawyer-client relationship do not apply. Law-related services for this purpose are services that might be reasonably performed in conjunction with and are related in substance to the practice of law. Examples include financial planning, title insurance, trust services, test services, and economic analysis. Even if the requirements of Model Rule 5.7 are met and the Rules of Professional Conduct do not apply to the ancillary business, the commentary to Model Rule 5.7 cautions that the triangular relationship between the attorney, the ancillary business, and the client must be evaluated under the full disclosure and consent rules of Model Rule 1.8.

A lawyer engaging in an ancillary business must recognize the conflicts, consent, and other issues arising from his or her status as a lawyer and must give these issues consideration while engaging in the ancillary business. The lawyer must also be aware of incurring liability for defaults of the ancillary business on a guarantor theory, as he or she may be the deep pocket to which clients turn when there is a problem. The defense that the lawyer was nothing but a “humble, barefoot, legal technician may be unavailable for problems arising from an ancillary business.”<sup>255</sup>

## 2.6 LAWYER AS A FIDUCIARY

The issues a lawyer faces in business relationships with a client come into sharp focus in the case of a lawyer who also serves as a personal representative, trustee, or attorney-in-fact for a client. Courts, the American Bar Association, and state bars have wrestled with the appropriateness of a lawyer serving as a fiduciary

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<sup>253</sup> *Restatement of the Law Governing Lawyers* § 10, cmt. g. See also LEO 1819, finding that the Rules of Professional Conduct apply to an attorney who works for a lobbying firm and represents clients only for purposes of lobbying, although the precise application of the Rules may be fact specific. LEO 1819 holds further that if the lobbyist/attorney allows confusion to enter his relationship with his client as to his non-legal capacity, that lawyer may not be able to avoid application of the Rules to his relationship with that client.

<sup>254</sup> Los Angeles County Bar Ass’n Standing Comm. on Legal Ethics, Formal Op. 413; Ohio Ethics Op. 90-9; South Carolina Bar Advisory Op. 93-05; *see also* Connecticut Bar Ass’n Comm. on Professional Ethics, Informal Op. 89-10. *See generally* LEOs 1442, 1325. *In re Unnamed Attorney*, 645 A.2d 69 (N.H. 1994), established that under certain circumstances, a professional conduct committee may be permitted to audit the accounts of a lawyer’s ancillary business.

<sup>255</sup> *Malpractice Desk Guide*, *supra* note **Error! Bookmark not defined.**, at 158-59.

for a client and how the issues of conflicts of interest, disclosure, and consent between the lawyer and the client should be addressed.

Virginia addressed several of the issues regarding lawyers serving as fiduciaries in LEO 1515. LEO 1515 answers five specific questions regarding the lawyer serving as a fiduciary for the client:

1. Must there be a pre-existing client relationship for the lawyer to prepare an instrument in which he or she is named as a fiduciary for the client?
2. What disclosure is required of fees that the lawyer will receive as a fiduciary?
3. May lawyers retain themselves or their firms as lawyers for the entities for which they are serving in a fiduciary capacity?
4. Are there any minimum standards of professional competence imposed on lawyers serving as fiduciaries for their clients?
5. May a lawyer initiate conversations with a client as to who might be an appropriate fiduciary for the client?

While most LEOs are non-binding, LEO 1515 has a special status as one of the few LEOs expressly approved by the Virginia Supreme Court and thus has acquired the status of a decision of the court. As a result, it should be regarded as binding authority on Virginia lawyers.

Perhaps the most significant aspect of LEO 1515 is its treatment of the lawyer becoming a fiduciary for a client as a potential conflict between the lawyer's personal interests (the additional compensation that the lawyer will receive) and the client's interests, which invokes the provisions of DR 5-101.<sup>256</sup> As a result, LEO 1515 requires that the naming of the lawyer be a fully informed and volitional act on the part of the client.

A lawyer is obliged not to use his or her position as a lawyer to exert undue influence on the client's choice of a fiduciary. LEO 1515 takes the position that undue influence is a factual question to be resolved on a case-by-case basis. However, it notes that the absence of a pre-existing relationship greatly enhances the potential for a finding of undue influence, while the existence of a prior relationship mitigates a possible finding of undue influence.<sup>257</sup>

A lawyer must provide full disclosure to the client of the potential fees the lawyer may charge for serving as a fiduciary. This disclosure is to be made before the client executes the instrument creating the fiduciary relationship. The disclosure

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<sup>256</sup> LEO 1515 does not rest on DR 5-104(A). The counterpart of DR 5-101 in the Rules is Rule 1.7, which requires consent after consultation but does not explicitly require the opportunity to obtain independent counsel. See the discussion in paragraph 2.4.

<sup>257</sup> See also LEO 1534.



should be in writing and signed by the client. The writing may either be the will, trust, or other instrument creating the relationship, or it may be a separate writing. The disclosure must also address any tax, investment fees, or fees for other services that will be charged over and above the basic fees for service as a fiduciary.

The possible retention by a lawyer of himself or herself or his or her firm to provide separate legal services is treated as a separate conflict of interest requiring consent after disclosure. Consent after disclosure may be obtained from the client when the applicable instrument is prepared, by consent after disclosure of all remainder beneficiaries of an estate, or by the consent of all income and vested remainder beneficiaries of a trust.

LEO 1515 notes that as a general matter, standards of fiduciary competence were subjects beyond its purview. However, it reminds Virginia lawyers that the standards of the CPR will apply to them in evaluating their conduct as fiduciaries. The opinion directs the attention of Virginia lawyers to two specific CPR provisions that have a bearing on the issue: DR 6-101(A),<sup>258</sup> which requires that a lawyer only act in matters for which he or she is competent; and DR 6-102(A),<sup>259</sup> which prevents a lawyer from limiting liability to clients for malpractice.

LEO 1515 allows lawyers to initiate the conversation with their clients as to who might serve as fiduciaries. It warns, however, that the lawyer must take into consideration the client's sophistication regarding legal matters and the client's physical, emotional, and mental state. Any form of communication that has a substantial potential for or involves overpersuasion or overreaching is prohibited.

LEO 1515 extends its requirements regarding disclosure and consent to instruments that name the lawyer as counsel in addition to those that name the lawyer as fiduciary. It also extends these standards to the issue of security or the lawyer-fiduciary's bond. Other issues to be discussed include the competence and personal service of the proposed fiduciary or lawyer and matters of financial stability. The decision should also focus on alternatives to the probate system and their implications.

While focusing on the questions answered by LEO 1515 is a necessary exercise for the prospective lawyer-fiduciary, the inquiry should not be limited to addressing only these issues. The opinion reminds lawyers that the act of becoming a fiduciary for a client is an act that is subject to the requirements of DR 5-101(A).<sup>260</sup> Thus, the lawyer should discuss the matter with the client in a manner designed to fully satisfy the requirements of full and adequate disclosure discussed above. In addition to fees and other alternatives, the lawyer should address any actual or potential limitations on the lawyer's ability to act, the extent to which the lawyer intends to delegate work to third parties, and continuity should the lawyer become unavailable either on a temporary or a permanent basis. Issues of the financial stability of the lawyer and his or her firm may also be important. Even though LEO 1515 does not require a lawyer

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<sup>258</sup> The current counterpart is Rule 1.1.

<sup>259</sup> The current counterpart is Rule 1.8(h).

<sup>260</sup> The current counterpart is Rule 1.7. *See supra* footnote 256.

to specifically address fees charged by other entities for similar services, a good-faith attempt to address the larger disclosure issue will almost inevitably involve some type of comparative analysis. In short, the lawyer should undertake to advise and counsel the client on the choice of the lawyer as a fiduciary in the same fashion as the lawyer would counsel the client regarding the choice of a third party.

Potential conflicts of interest and conflicts of loyalty between the lawyer's duties as a fiduciary should also be discussed. The client may be expecting the lawyer to take a position as a fiduciary that may be inconsistent with the lawyer's fiduciary duties to third parties. Even though the client may not have made his or her expectations clear, the lawyer's knowledge of family affairs or the lawyer's representation of other family members may indicate the potential for such a conflict.

While dealing with lawyers for fiduciaries, rather than lawyers serving as fiduciaries, *In re Estate of Halas*<sup>261</sup> demonstrates a potential area of conflict for lawyer-fiduciaries. The case involved the Chicago law firm of Kirkland and Ellis and the estate of the son of George "Papa Bear" Halas. Kirkland and Ellis represented the senior Halas as the executor of the estate and individually; the Bears Football Club, Inc. (a corporation that owned the Chicago Bears), stock in which was the principal asset of the estate; officers, directors, and other shareholders of the corporation (other members of the Halas family); and one of the two trustees (another Halas family member). It is evident from the opinion that the interests of the divorced wife of the decedent and those of the two children of the decedent's prior marriage who were significant beneficiaries of the estate and various trusts were dramatically different from those of the members of the Halas family individually. Kirkland and Ellis furthered the interests of the Halas family in a recapitalization of the Bears for estate-freezing purposes and participated in various activities to the detriment of the interests of the divorced wife and children. The court found that the improper multiple representation showed an absence of good faith on the part of the lawyers in failing to satisfy their fiduciary obligations to the beneficiaries.

Conflicts of interest and conflicts of loyalty are reminders of the overall consideration that in some instances no amount of disclosure and counsel will be appropriate. The lawyer should be keenly aware of potential problem areas and should not hesitate to steer clients to third parties when the lawyer concludes that it is simply not appropriate for him or her to serve as a fiduciary.

## **SECTION 3: FEES**

### **3.1 IN GENERAL**

Attitudes toward lawyers and their fees have changed considerably since the American Bar Association declared:

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<sup>261</sup> 512 N.E.2d 1276 (Ill. App. Ct. 1st Dist. 1987).

In fixing fees it should never be forgotten that the profession is a branch of the administration of justice and not a mere money getting trade.<sup>262</sup>

More typical of the current view is: “Lawyers, like taxi cabs, are for hire.”<sup>263</sup> While the practice of law has certainly become more like a trade with the advent of advertising and similar practices, it is important to remember that lawyers do not have the freedom to price their services solely on what the market will bear. They must acknowledge the limitations and restraints on those fees imposed by applicable ethical rules and guidelines.<sup>264</sup> At the same time, however, there must be an attorney-client relationship for these rules to apply. They do not apply to attorney fees of third parties that a nonclient may be obligated to pay by contract.<sup>265</sup>

The Arizona Bar has taken the position that a lawyer’s knowledge of another lawyer’s clearly excessive fee triggers an obligation to report that attorney’s misconduct even when the fee was subsequently reduced to a reasonable level.<sup>266</sup> Virginia’s position on the subject is murky, but it does not appear to have adopted the per se rule applicable in Arizona.<sup>267</sup> While a single case of excessive fees does not support a RICO claim, there is at least the implication that a pattern of excessive fees may support such a claim.<sup>268</sup>

A lawyer’s fee must be reasonable.<sup>269</sup> The Rules of Professional Conduct (the Rules) indicate that the following criteria will be used in evaluating the reasonableness of a fee:

- (1) the time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly;
- (2) the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer;

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<sup>262</sup> ABA Formal Op. 151; see also ABA Formal Op. 302, in which the ABA declared that no lawyer should have to bid competitively for clients.

<sup>263</sup> G.H.L. Fridman, *Lawyers as Agents*, 36 U. New Brunswick L.J. 10 (1987).

<sup>264</sup> Not only do inappropriate fees present ethical problems, but they may present a defense to payment as well. Hazard & Hodes, *supra* note **Error! Bookmark not defined.**, at § 8.4. A New York City opinion provided that while preparation of a bill may be delegated to a nonlawyer, the lawyer remains responsible for any billing improprieties and the reasonableness of the bill. Association of the Bar of the City of New York, Op. 94-9.

<sup>265</sup> LEO 1645.

<sup>266</sup> Arizona Ethics Op. 94-09.

<sup>267</sup> LEO 1562. The Committee notes here that, where information about an attorney’s ethical violations may be a client confidence or secret, the client’s consent must be obtained before disclosure.

<sup>268</sup> See *McDonald v. Schenker*, 18 F.3d 491 (7th Cir. 1994).

<sup>269</sup> Rule 1.5(a); see *Campbell County v. Howard*, 133 Va. 19, 112 S.E. 876 (1922); The Virginia Supreme Court has ruled that expert testimony is not required to establish the reasonableness of attorney fees in a suit brought to collect these fees. *Seyfarth, Shaw, Fairweather & Geraldson v. Lake Fairfax Seven Ltd. P’ship*, 253 Va. 93, 480 S.E.2d 471 (1997). A fee may always be reviewed for reasonableness. *Annotated Model Rules*, *supra* note **Error! Bookmark not defined.**, at 68.

- (3) the fee customarily charged in the locality for similar legal services;
- (4) the amount involved and the results obtained;
- (5) the time limitations imposed by the client or by the circumstances;
- (6) the nature and length of the professional relationship with the client;
- (7) the experience, reputation, and ability of the lawyer or lawyers performing the services; and
- (8) whether the fee is fixed or contingent.<sup>270</sup>

The *Restatement* suggests that it would be appropriate to determine if the client made a free and informed choice, to consider whether the fee was within a range commonly charged by other lawyers, and to inquire whether there were factors that subsequently made it unreasonable.<sup>271</sup>

A fee arrangement must be evaluated both at the time it is entered into and at the conclusion of the matter.<sup>272</sup> A fee that is reasonable at the outset may become unreasonable in retrospect.<sup>273</sup> In each case the question focuses on the value of the lawyer's services in the abstract, not their value to the particular client. A lawyer's duties with respect to fees also extend to expenses incurred on behalf of the client.<sup>274</sup> The rule of reasonableness also applies to disbursements on behalf of a client.<sup>275</sup> A lawyer should beware of clients who seem unconcerned about fees as well as those who seem too concerned about fees, as each is a warning of potential future problems with the client.<sup>276</sup>

A lawyer's fee must be adequately explained to the client.<sup>277</sup> If the lawyer has not regularly represented the client, the amount, basis, or rate of the fee must be communicated to the client before or within a reasonable time after the commencement of the representation.<sup>278</sup> Comment [2] to Rule 1.5 elaborates on the type of communication required. It states:

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<sup>270</sup> Rule 1.5(a).

<sup>271</sup> *Restatement of the Law Governing Lawyers* § 34 cmt. c.

<sup>272</sup> *McKenzie Constr., Inc. v. Maynard*, 758 F.2d 97 (3d Cir. 1985); *In re Swartz*, 686 P.2d 1236 (Ariz. 1984).

<sup>273</sup> Hazard & Hodes, *supra* note **Error! Bookmark not defined.**, at 124.

<sup>274</sup> *Id.* at 116.

<sup>275</sup> *Restatement of the Law Governing Lawyers* § 34 cmt. a.

<sup>276</sup> *Malpractice Desk Guide*, *supra* note **Error! Bookmark not defined.**, at 34.

<sup>277</sup> Rule 1.5(b).

<sup>278</sup> Rule 1.5 does not require the communication to be in writing, much less that there be a written fee agreement. Even so, the Commentary notes that a written agreement reduces the possibility of a misunderstanding.

It is not necessary to recite all the factors that underlie the basis of the fee, but only those that are directly involved in its computation. It is sufficient, for example, to state that the basic rate is an hourly charge or a fixed amount or an estimated amount, or to identify the factors that may be taken into account in finally fixing the fee.

The Comment further notes that a letter, memorandum, receipt, or copy of a fee schedule may be a sufficient communication.

### 3.2 CONTINGENT FEES

A lawyer may not charge a contingent fee for criminal defense<sup>279</sup> and may only charge a contingent fee in domestic relations cases in rare instances.<sup>280</sup> Comment [6] to Rule 1.5 indicates that the “rare instances” requirement is met only when each of the following conditions is met:

(a) the contingent fee is for the collection of, and is to be paid out of (i) accumulated arrearages in child or spousal support; (ii) an asset not previously viewed or contemplated as a marital asset by the parties or the court; (iii) a monetary award pursuant to equitable distribution or a property settlement agreement;

(b) the parties are divorced and reconciliation is not a realistic prospect;

(c) the children of the marriage are or will soon achieve the age of maturity [sic] and the legal services rendered pursuant to the contingent fee arrangement are not likely to affect their relationship with the non-custodial parent;

(d) the client is indigent or could not otherwise obtain adequate counsel on an hourly fee basis; and

(e) the fee arrangement is fair and reasonable under the circumstances.

These rules would appear to supersede a number of LEOs issued under the Code of Professional Responsibility (CPR) addressing contingency fees in domestic relations cases.<sup>281</sup>

In those cases where a contingent fee is permitted, there must be an agreement that states in writing the method by which the fee is calculated and specifically addresses the percentages that accrue to the lawyer, the expenses to be deducted from

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<sup>279</sup> It is permissible to charge a contingent fee in a forfeiture proceeding even though it may be related to a criminal proceeding as long as the forfeiture proceeding itself is not a criminal proceeding. LEO 1748.

<sup>280</sup> Rule 1.5(d).

<sup>281</sup> See, e.g., LEOs 1674, 1062, 850, 778, 667, 588, 569, 423, 405, 189. The current rule is very similar to that adopted in LEO 1606.

the recovery, and whether the fee is computed on the gross recovery or the recovery net of expenses.<sup>282</sup> On the conclusion of a contingent fee matter, the lawyer must provide the client with a statement showing the fee and its calculation.<sup>283</sup> An unsigned contingent fee agreement is not enforceable on the grounds of promissory estoppel.<sup>284</sup>

There must be some element of uncertainty as to a client's recovery to justify a contingent fee.<sup>285</sup> Courts have upheld discipline imposed on lawyers for the collection of contingent fees on accidental death benefits;<sup>286</sup> for collecting the inheritance of the sole beneficiary of an estate;<sup>287</sup> and for collecting "med pay" insurance benefits<sup>288</sup> in cases in which there was no real uncertainty as to collection. On the other hand, contingency fees on "med pay" claims against a tortfeasor's insurance have been permitted when the services of a lawyer were necessary to collect on the coverage.<sup>289</sup>

In addition to satisfying the requirement of uncertainty of recovery, contingent fees must satisfy the reasonableness standard applied to other fees.<sup>290</sup> The reasonableness standard requires an examination of the appropriateness of the fee on billing as well as at the initiation of the engagement.<sup>291</sup> The amount of time involved, the difficulty of the legal issues involved, and the benefit to the client are relevant factors. A Virginia opinion held that it is improper to use a contingent fee structure that requires the client to pay a fee equal to the higher of 20 percent of any recommended settlement that is rejected or 25 percent of any court recovery.<sup>292</sup> In the case of fees set by a state agency, it is improper for a lawyer to enforce a private contingent fee agreement to recover fees in excess of those awarded by the agency.<sup>293</sup>

In *McKenzie Construction, Inc. v. Maynard*,<sup>294</sup> the court set aside a contingent fee agreement calling for a fee of 33 percent of the recovery when the recovery was \$195,000 and billing at the lawyer's normal hourly rate would have justified a fee of

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<sup>282</sup> Thus, unlike other engagements, contingent fee cases explicitly require a written fee agreement.

<sup>283</sup> Rule 1.5(c); LEO 1606.

<sup>284</sup> *Fasing v. LaFond*, 944 P.2d 608 (Colo. Ct. App. 1997). See also *Foodtown, Inc. v. Argonaut Ins. Co.*, 102 F.3d 483 (11th Cir. 1996).

<sup>285</sup> LEO 1606.

<sup>286</sup> *Westchester County Bar Ass'n v. St. John (In re St. John)*, 43 A.D.2d 218, 350 N.Y.S.2d 737 (N.Y. App. Div. 1974).

<sup>287</sup> *Florida Bar v. Moriber*, 314 So. 2d 145 (Fla. 1975).

<sup>288</sup> *Attorney Grievance Comm'n v. Kemp*, 496 A.2d 672 (Md. 1985); LEOs 1641, 1461. An hourly rate or flat rate for medical payments claims may be appropriate. But see *Lawyer Disciplinary Bd. v. Morton*, 569 S.E.2d 412 (W. Va. 2002) (court declined to impose a per se disapproval of contingent fees on med pay recovery); LEO 1641.

<sup>289</sup> LEO 1696.

<sup>290</sup> *Lawyers' Manual*, supra note **Error! Bookmark not defined.**, at 41:901.

<sup>291</sup> Michigan Ethics Op. R-162.

<sup>292</sup> LEO 365.

<sup>293</sup> *Hudock v. Virginia State Bar*, 233 Va. 390, 355 S.E.2d 601 (1987). Compare LEO 515, which gives a lawyer some flexibility to charge less than the statutory commission for a trustee on a deed of trust, and LEO 912, which gives a lawyer the ability to collect a greater commission from the noteholder than that allowed by statute if the noteholder agrees and only the statutory commission is charged in the accounting for the foreclosure.

<sup>294</sup> 758 F.2d 97 (3d Cir. 1985).

\$4,000.<sup>295</sup> While the court indicated it would normally be reluctant to upset contingent fee agreements, it found it appropriate to do so, considering the amount of time expended by the lawyer.<sup>296</sup>

In *In re Swartz*,<sup>297</sup> the Arizona Supreme Court upheld discipline in a case that involved no difficult issues in which the lawyer produced a \$150,000 recovery without much work after insurance carriers offered a relatively quick policy limits settlement. After the payment of expenses, the satisfaction of the lien of the workers' compensation carrier, and the payment of the lawyer's fee, the client received no recovery. The court was not impressed with the lawyer's argument that reducing his fee would not have benefited his client, as the claim of the workers' compensation lien was sufficient to absorb any reduction in fees.<sup>298</sup>

It would appear that a contingent fee in a structured settlement should be based on the present value of the settlement, not the total value.<sup>299</sup> In the absence of an agreement, it is not proper to take the entire contingent fee out of the initial payment of a structured settlement.<sup>300</sup>

The American Bar Association Committee on Ethics and Professional Responsibility addressed a number of issues raised by contingent fees in Formal Opinion 94-389. This opinion holds that contingent fees are proper in cases where a client can afford to pay and when liability is clear as long as the amount of recovery is uncertain. Escalating and contingent percentages are also approved, as are arrangements based on early settlement offers, although a flat percentage arrangement for all stages of a case may raise reasonableness questions. The opinion emphasizes that in all cases, the size of the fee must be reasonable and appropriate notwithstanding the manner of its calculation.

### 3.3 PERCENTAGE FEES

Virginia has traditionally measured fiduciary compensation on a percentage basis. While the Virginia Code provides for reasonable compensation for fiduciaries,<sup>301</sup> the Virginia Supreme Court has not hesitated to approve a percentage of the amount coming into the hands of the fiduciary as an appropriate measure of compensation. In general the court has approved five percent as an appropriate measure of fiduciary

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<sup>295</sup> It is significant to note that the lawyers in *McKenzie* had rejected a request from their client to reduce the fee before the litigation. Negotiations with the client might have avoided the litigation.

<sup>296</sup> *But see Hayes v. Parker*, 177 Va. 70, 12 S.E.2d 750 (1941).

<sup>297</sup> 686 P.2d 1236 (Ariz. 1984).

<sup>298</sup> *See Roos v. Fallers (In re Conservatorship of Fallers)*, 889 P.2d 20 (Ariz. Ct. App. 1994).

<sup>299</sup> *Nguyen v. Los Angeles County Harbor/UCLA Med. Ctr.*, 48 Cal. Rptr. 2d 301 (Cal. App. 2d Dist. 1995); *In re Fox*, 490 S.E.2d 265 (S.C. 1997).

<sup>300</sup> *In re Myers*, 663 N.E.2d 771 (Ind. 1996).

<sup>301</sup> Va. Code § 26-30.

compensation, but it has not hesitated to use either a higher or lower amount in the proper circumstances.<sup>302</sup>

There is a trend away from percentage fees in other jurisdictions. Many courts are evaluating fees of lawyers as fiduciaries in the same fashion as other fees of lawyers.<sup>303</sup> Under this analysis, the fee of the lawyer is based on the reasonable value of the lawyer's services without taking into consideration the value of the services to the particular client. As the Virginia Code, the CPR, and the Rules all apply a reasonableness standard in evaluating fees, and the actions of the lawyer as fiduciary are governed by the Rules, it would not be surprising to see Virginia courts move away from the use of a percentage to evaluate the fees of Virginia lawyer-fiduciaries.

### 3.4 HOURLY RATES

Courts and other authorities have not hesitated to challenge fees based on hourly rates when the fees charged were excessive. In *Bushman v. State Bar*,<sup>304</sup> the California Supreme Court upheld lawyer discipline for a fee arrangement in a simple custody matter in which the lawyer took his client's note for \$5,000 in addition to an agreement providing for compensation at an hourly rate. The client was on public assistance and the court found that the amount of the fee charged by the lawyer greatly exceeded the value of the work.

A Washington appellate court has adopted the criteria of the ABA Code of Professional Responsibility in evaluating hourly fees in a guardianship proceeding. The court reduced the legal fees allowed the guardian, criticizing the large number of hours spent on the case and the presence of a second counsel. The court noted that the time involved was only one factor in determining the appropriateness of the fee. Other factors to be considered were the benefit to the client, the propriety of the hourly rate, and the relevance of the hours charged to the work at hand.<sup>305</sup>

It is not proper for a lawyer to bill a client for unskilled labor at an amount in excess of the rate that would have been charged by others.<sup>306</sup> A Michigan ethics opinion held that a lawyer cannot charge a client the normal rate for the time the lawyer is being deposed by an adverse party during discovery.<sup>307</sup> It is also not appropriate to charge for time spent as the result of inexperience or inefficiency.<sup>308</sup>

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<sup>302</sup> See, e.g., *Perrow v. Payne*, 203 Va. 17, 121 S.E.2d 900 (1961); *Bickers v. Shenandoah Valley Nat'l Bank*, 201 Va. 257, 110 S.E.2d 514 (1959); *Pritchett v. First Nat'l Bank*, 195 Va. 406, 78 S.E.2d 650 (1953); *Gregory's Ex'r v. Parker*, 87 Va. 451, 12 S.E. 801 (1891); see also Va. Code § 26-30.

<sup>303</sup> *Estate of Davis*, 509 A.2d 1175 (Me. 1986); *In re Estate of Freeman*, 311 N.E.2d 480 (N.Y. 1974); *In re Estate of Preston*, 560 A.2d 160 (Pa. Super. Ct. 1989).

<sup>304</sup> 522 P.2d 312 (Cal. 1974).

<sup>305</sup> *In re Guardianship of Hallauer*, 723 P.2d 1161 (Wash. Ct. App. 1986).

<sup>306</sup> *Florida Bar v. Shannon*, 376 So. 2d 858 (Fla. 1979).

<sup>307</sup> Michigan Ethics Op. RI-3.

<sup>308</sup> *Annotated Model Rules*, supra note **Error! Bookmark not defined.**, at 65.



An hourly rate fee arrangement produces an economic incentive for a lawyer to be less than candid with the client as to the amount of time actually spent on the client's case.<sup>309</sup> Commentators have enumerated several types of abuse of hourly rate fee structures, including make-work; double or triple billing clients for the same period of time; arbitrary time charges for telephone calls; and billing of personal time.<sup>310</sup>

The ABA Committee on Ethics and Professional Responsibility addressed the subject of hourly billing in Formal Opinion 93-379. This opinion held that if a lawyer and client have agreed that the lawyer will be compensated on an hourly basis, the lawyer may only charge the client for time actually spent on the client's work. Multiple clients may not be billed for the same work or for the same period of time. Billing one client for travel while billing another for work actually performed during the travel is disapproved.<sup>311</sup> Billing a client based on the amount of time it took to complete the work on behalf of another client is not permissible. Any economies realized as the result of multiple client relationships must be passed on to the clients. Churning and make-work are disapproved, as the lawyer may only charge the client for the time reasonably required to complete the task at hand. Lawyers cannot charge their clients for general overhead expenses, but they may charge their clients for specific disbursements for the client's benefit. Absent an agreement to the contrary, a lawyer may not charge a client more than the actual out-of-pocket costs for such items as copies, travel, telephone calls, and similar items.<sup>312</sup> A surcharge may not be placed on these charges. While a lawyer can suggest possible fee enhancement to the client, it is improper for the lawyer to unilaterally submit an enhanced bill. Virginia has made it clear that in the case of a client who has been told he or she will be billed on a time basis, charges for administrative fees, processing fees or value billing percentage increases, or adding hours to the bill to reflect value are fraudulent, unreasonable, and inadequately explained.<sup>313</sup>

### 3.5 HYBRID AND OTHER FEES

The ABA has tentatively approved a reverse contingent fee agreement in which the lawyer's fee would be based on the amount of money the lawyer has saved the client. The opinion requires that the amount saved be reasonably determinable and the client must give his or her fully informed consent.<sup>314</sup>

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<sup>309</sup> Lisa G. Lerman, *Lying to Clients*, 138 U. Pa. L. Rev. 659, 674 (1990).

<sup>310</sup> *Id.*; William G. Ross, *The Ethics of Hourly Billing by Attorneys*, 44 Rutgers L. Rev. 1 (1991).

<sup>311</sup> See also Nassau County Bar Association Committee on Professional Ethics, Opinion 95-4, which indicated that billing a client for travel time during which the lawyer makes telephone calls billed to other clients is not permitted, and California State Bar Standing Committee on Professional Responsibility and Conduct, Formal Opinion 1996-147, which indicated that separate clients cannot be billed for time spent simultaneously on the work of each without an express agreement to the contrary and that the amount must not be unconscionable.

<sup>312</sup> Flat rate charges to a file that do not reflect actual expenses are arbitrary and inappropriate. Connecticut Ethics Op. 94-24; LEO 1648. *But see* LEOs 1056, 710.

<sup>313</sup> LEO 1648.

<sup>314</sup> ABA Formal Op. 93-373.

An adjusted hourly rate as an alternative to the contingent fee has been suggested. Under this approach, the basic fee agreement would call for compensation based upon the amount of hours spent, but the hourly rate would be adjusted based on the difficulty of the case, the risk of recovery, and other factors normally used to justify contingent fees.<sup>315</sup>

Virginia has tentatively approved a combination hourly rate-contingency arrangement; the Committee noted, however, that it was subject to the requirement that the overall fee be reasonable.<sup>316</sup> The reasonableness of such an arrangement is evaluated both at the time the fee agreement is signed and at the time of termination. A lawyer using such an arrangement must take particular care to make sure it is fully explained.<sup>317</sup>

So-called value-added fees are appropriate provided that the practice is adequately disclosed to the client. The client may not, however, be billed at a multiple of the lawyer's hourly rate when the client has been told the fee will be based on the amount of time involved.<sup>318</sup> A fee agreement that gives a lawyer essentially unbridled discretion to adjust the amount of a bill to reflect a particularly satisfactory or good result is not appropriate unless it also requires that the client give consent to the adjustment.<sup>319</sup> An agreement that allows a lawyer to charge an hourly fee until settlement and then allows the lawyer to choose between an hourly or contingent fee is inherently unreasonable and will not be enforced.<sup>320</sup>

Fixed fees are encouraged because of the certainty they provide to clients. Fixed fees paid in advance are subject to the rules applicable to advanced legal fees discussed below.<sup>321</sup>

### **3.6 FEE AGREEMENTS**

There must be an agreement to pay fees to support a claim for legal fees. Absent an explicit agreement, however, a lawyer cannot charge a person who is not a client a legal fee.<sup>322</sup> A series of opinions pertaining to real estate closings make it clear that a lawyer may not charge a fee to a nonclient party unless the fee is for ministerial services and advance notice of the charge is given to the other party in

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<sup>315</sup> See Harold See, *An Alternative to the Contingent Fee*, 1984 Utah L. Rev. 485; Kevin M. Clermont & John D. Currihan, *Improving on the Contingent Fee*, 63 Cornell L. Rev. 529 (1978).

<sup>316</sup> LEO 1766.

<sup>317</sup> LEO 1812.

<sup>318</sup> LEO 1648.

<sup>319</sup> Connecticut Ethics Op. 94-13.

<sup>320</sup> Ohio Supreme Court Bd. of Comm'rs on Grievances and Discipline, Op. 94-7. See also *In re Lansky*, 678 N.E.2d 1114 (Ind. 1997), in which a similar provision plus authorization to settle without the client's consent resulted in a suspension.

<sup>321</sup> LEO 1606.

<sup>322</sup> See, e.g., LEO 1442.

sufficient time for the other party to avoid imposition of the fee by taking appropriate action.<sup>323</sup>

A lawyer who has made a fee arrangement may not unilaterally change it to his or her benefit even if the lawyer perceives that a good result has been produced.<sup>324</sup> A fee agreement may be modified during a representation as long as the charge is fairly negotiated.<sup>325</sup> Deception and misrepresentation regarding the size of a fee or its calculation also raise serious disciplinary issues.<sup>326</sup> A lawyer who has agreed to a referral from a legal aid service as a pro bono case may not charge the referred client a fee.<sup>327</sup>

While implicit in the discussion of contingent fees and hourly fees discussed above, it should be emphasized that an agreement or a client's consent to a fee arrangement will not save a lawyer from discipline. In *Florida Bar v. Moriber*,<sup>328</sup> the lawyer defended a disciplinary violation action for charging an improper contingent fee on the grounds that the client knew what he was getting into, consented to the arrangement, and continued to raise no objection or complaint after disciplinary proceedings were brought against the lawyer. The Bar refused to acknowledge any of these factors as significant in determining whether a violation occurred.

In an ethics opinion,<sup>329</sup> the Wisconsin Bar opined on the following disclosure of the manner in which a firm proposed to charge its clients:

Our fees will be based upon the ethical rules governing our practice. The amount of our statement will be the fair value of services provided taking into account the time spent by the lawyer involved, the type of service we are being asked to perform, any special level of expertise required, the size and scope of the matter, the results obtained and other relevant considerations.

The proposed disclosure paralleled the provisions of ABA Model Rule 1.5, which Wisconsin had adopted. While the opinion acknowledged that the proposal might adequately disclose the basis of the firm's fees for those clients who had significant experience in dealing with lawyers, it emphasized that the communication must be meaningful to the client.

It has been suggested that a good fee agreement should contain the following elements:

1. What the lawyer is doing and not doing;

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<sup>323</sup> LEOs 1228, 1204, 1177, 1148, 927, 922, 911, 878, 425; see LEO 1277, which approved a notice of fees in general terms in a trustee's advertisement for a foreclosure sale.

<sup>324</sup> *Stinson v. Feminist Women's Health Ctr.*, 416 So. 2d 1183 (Fla. Dist. Ct. App. 1st Dist. 1982); LEO 1188.

<sup>325</sup> LEO 1705.

<sup>326</sup> *Myers v. Virginia State Bar*, 226 Va. 630, 312 S.E.2d 286 (1984).

<sup>327</sup> LEO 1691.

<sup>328</sup> 314 So. 2d 145 (Fla. 1975).

<sup>329</sup> Wisconsin Ethics Op. E-91-2.

2. How the client's bill will be calculated and how the bill is to be paid;
3. When payment is expected;
4. What will happen if the client does not pay;
5. Whether there is a finance charge;
6. Whether the lawyer may withdraw if the fee is not paid; and
7. How the lawyer is to be compensated if he or she is discharged before the engagement is completed.<sup>330</sup>

Other possible subjects include possible liens for unpaid fees and charges for costs and expenses. Virginia ethics opinions have approved provisions of fee agreements imposing a flat percentage charge for expenses if the client consents after disclosure, but only in non-litigation and non-contingent fee cases.<sup>331</sup> A fee agreement may not limit the client's right to terminate the lawyer to only those circumstances in which good cause is shown nor may it appoint the lawyer as the client's attorney-in-fact to settle cases.<sup>332</sup>

In drafting fee agreements, lawyers should be mindful that ambiguities or uncertainties in the agreements are construed against the lawyer, and the lawyer bears the burden of proving that the client fully understood its terms.<sup>333</sup> *Severson & Werson v. Bolinger*<sup>334</sup> addressed the issue of a fee agreement that obligated a client to pay a firm's "regular hourly rates." When the agreement was entered into, hourly rates of various lawyers in the firm were disclosed to the client. Thereafter, the hourly rates were raised and the client was billed at the increased hourly rates. The court held that absent disclosure that the rates would be increased, the client was entitled to hold his lawyers to the hourly rates he had been quoted, as the fee agreement was to be strictly construed in the client's favor.<sup>335</sup>

*May v. Sessums & Mason, P.A.*<sup>336</sup> provides an interesting lesson in drafting. The fee agreement in that case provided for a basic hourly rate but also indicated the lawyer could request an amount in addition to the amount based on the hourly charge. The attorney requested a significant "additional amount," which the client refused to pay. Based on the language of the agreement, the court found no contractual obligation to pay the additional amount. The court further found that the

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<sup>330</sup> Adapted from *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 41:2002.

<sup>331</sup> See LEOs 1056, 710.

<sup>332</sup> Arizona Ethics Op. 94-02; see also *Cohen v. Radio Elec. Officers' Union*, 645 A.2d 1248 (N.J. Super. Ct. App. Div. 1994), which invalidated a six-month notice requirement for termination in a fee agreement.

<sup>333</sup> *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 41:112; Hazard & Hodes, *supra* note **Error! Bookmark not defined.**, at § 8.9.

<sup>334</sup> 235 Cal. App. 3d 1569 (Cal. App. 1st Dist. 1991).

<sup>335</sup> See also *Garnick & Scudder, P.C. v. Dolinsky*, 701 N.E.2d 357 (Mass. App. Ct. 1998). But see *Thomas v. Sinclair*, C037926, 2003 Cal. App. Unpub. LEXIS 3787, 2003 WL 1871106 (Cal. App. 3d Dist. filed Apr. 14, 2003).

<sup>336</sup> 700 So. 2d 22 (Fla. Dist. Ct. App. 2d Dist. 1997), *review denied*, 705 So. 2d 571 (Fla. 1998). See also *Franklin & Marbin, P.A. v. Mascola*, 711 So. 2d 46 (Fla. Dist. Ct. App. 4th Dist. 1998).

existence of a written contract precluded any additional recovery by the lawyer on the ground of quantum meruit.<sup>337</sup>

Nonrefundable retainers have been generally discouraged or limited.<sup>338</sup> Virginia opinions divide nonrefundable retainers into two categories. A payment that is made solely to secure a lawyer's availability for future services may be nonrefundable.<sup>339</sup> It is treated as the property of the lawyer from the moment it is paid. A payment in advance for services to be rendered, on the other hand, remains the property of the client until it is earned. As such it must be deposited into the lawyer's trust account and only disposed of in accordance with the rules governing trust accounts.<sup>340</sup> A nonrefundable payment characterized as a payment for availability with respect to particular matters but that is eligible to be credited against a bill for services in these matters is treated as an advance payment of fees and thus remains the property of the client until it is earned.<sup>341</sup> In some cases a fee contract may provide that a portion of an advance fee is considered earned when paid to the lawyer.<sup>342</sup> It should be noted, however, that the amount so designated must be both reasonable and appropriate. On termination of the representation for any reason, the lawyer is required to return to the client any advance payment of fees that have not been earned.<sup>343</sup>

Arbitration of fee disputes with clients is encouraged by several states.<sup>344</sup> Both the District of Columbia and Michigan, however, provide that fee agreements with mandatory arbitration provisions are only permissible if the client has the advice of independent counsel concerning the arbitration provisions.<sup>345</sup> Virginia takes a similar position with respect to mandatory malpractice claim arbitration and would presumably follow the District of Columbia and Michigan on fee arbitration.<sup>346</sup> At least one court has held that a client cannot back out of an agreement to arbitrate a fee dispute.<sup>347</sup>

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<sup>337</sup> *King v. Young, Berkman, Berman & Karpf, P.A.*, 709 So. 2d 572 (Fla. Dist. Ct. App. 3d Dist. 1998) ("bonus provision" held void and unenforceable).

<sup>338</sup> *In re Cooperman*, 187 A.D.2d 56 (N.Y. App. Div. 2d Dep't 1993), *aff'd*, 633 N.E.2d 1069 (N.Y. 1994); *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 41:2004; Hazard & Hodes, *supra* note **Error! Bookmark not defined.**, at § 8.5; LEO 1606.

<sup>339</sup> LEOs 1606, 1178.

<sup>340</sup> LEO 1178. The unearned portion of the fee remains the property of the client. As such, it is subject to a garnishment against the client. LEO 1807.

<sup>341</sup> *El-Amin v. Virginia State Bar*, 257 Va. 608, 514 S.E.2d 163 (1999); LEOs 1606, 1332. *See also In re Thonert*, 693 N.E.2d 559 (Ind. 1998); *Iowa Supreme Court Bd. of Prof'l Ethics & Conduct v. Apland*, 577 N.W.2d 50 (Iowa 1998); *but see Bunker v. Meshbesher*, 147 F.3d 691 (8th Cir. 1998).

<sup>342</sup> LEO 1606.

<sup>343</sup> Rule 1.16(d).

<sup>344</sup> *See Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 41:2001.

<sup>345</sup> District of Columbia Ethics Op. 211; Michigan Ethics Op. RI-2.

<sup>346</sup> LEOs 1707, 638; *see also* Arizona Ethics Op. 94-05. There is a reluctance to extend the scope of a blanket arbitration provision to transactions outside the direct representation. *See Mayhew v. Benninghoff*, 62 Cal. Rptr. 2d 27 (Cal. App. 4th Dist. 1997).

<sup>347</sup> *Titus & McConomy v. Jalisi*, 713 A.2d 646 (Pa. Super. Ct. 1998).

Upon a client's request, the lawyer must provide an itemized breakdown of the bill showing legal fees, costs, and related expenses.<sup>348</sup> A lawyer must also provide the client an accounting of fees paid from advanced fees held in the lawyer's trust account.<sup>349</sup> While detailed breakdowns of advances are not required, they are encouraged.<sup>350</sup> At the very least, the bill should disclose sufficient information on its face to allow the client to determine whether the billing is in accordance with their agreement with the lawyer. A lawyer may not mask attorney fees in the bill by including them within a separately itemized category such as title insurance.<sup>351</sup>

### 3.7 DIVISION OF FEES

A lawyer may divide fees with another lawyer who is not in the same firm if, before legal services are rendered, the client consents to the participation of all lawyers involved and the terms of the division are disclosed to and consented to by the client. The total fees must be reasonable.<sup>352</sup> Fees may be divided between attorneys who were previously associated in a law firm or between any successive attorneys in the same matter, if the total fee is reasonable.<sup>353</sup> If the requirements of Rule 1.5(e) are met, the rule authorizes the payment of pure referral fees to lawyers who will not provide any services or assume any responsibility to the client with respect to those services.<sup>354</sup> The lawyer should be aware, however, that the Virginia Code as well as the Rules of Professional Conduct proscribe the use of "runners" or "cappers" to solicit employment for the lawyer in return for referral fees.<sup>355</sup>

In general, a lawyer may not share legal fees with a non-lawyer except in the case of payments to the estate of a deceased lawyer or in connection with a firm-wide compensation plan.<sup>356</sup> While Rule 5.4(a)(4) allows discounted payment of fees from a credit card company, the exception has been narrowly construed. LEO 1764 found that a proposed payment arrangement was improper where the entire fee would be due at the beginning of the engagement, a finance company would pay the lawyer his entire fee, minus a discount, in advance of any services, and the client would make monthly payments to the finance company.

LEO 1783 dealt with collection on a promissory note that provided for lawyers' fees of 25 percent when the lawyer actually charged based on a lower, hourly rate. The lawyer would disburse to the client lender the difference, including an amount that exceeded reimbursement for the lender's actual cost for the legal services. The opinion finds that allowing the client to keep the difference between the amount of fees

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<sup>348</sup> LEO 214.

<sup>349</sup> LEO 681.

<sup>350</sup> Iowa Ethics Op. 88-16.

<sup>351</sup> South Carolina Bar Ethics Advisory Op. 87-09; LEO 1220.

<sup>352</sup> Rule 1.5(e).

<sup>353</sup> Rule 1.5(f).

<sup>354</sup> LEO 1739. When consent is not possible, a court-ordered division is acceptable. LEO 1760.

<sup>355</sup> Va. Code § 54.1-3939 *et seq.*; Rule 7.3(d).

<sup>356</sup> Rule 5.4(a).

provided in the note and the amount actually charged is permissible, because it does not compromise the purpose of Rule 5.4(a).

LEO 1744 opined that lawyers who are acting on behalf of a nonprofit entity as its employees, without charging fees, may turn over to the nonprofit any legal fees awarded by the court.

### 3.8 COLLECTION AND TERMINATION OF EMPLOYMENT

There is no ethical requirement that a lawyer's fees be paid in cash.<sup>357</sup> Payment may be made by credit card as long as there is full recourse from the card sponsor to the lawyer if the client refuses to honor the credit card statement for the fees.<sup>358</sup> A lawyer may take a note for fees but may not sell the note to a bona fide purchaser, who would not be subject to any defense the client may have against collection arising out of the lawyer-client relationship.<sup>359</sup> The note may even be secured by a deed of trust, but the transaction must also pass scrutiny under the rules regarding business dealings with clients, discussed above.<sup>360</sup> A lawyer may take a partial assignment of a claim for a fee, but cannot charge an extra contingency fee for collecting the claim.<sup>361</sup> Barter transfers or in-kind payments have also been approved, but it is improper for a broker to take a percentage commission on fees paid in this fashion.<sup>362</sup> Furthermore, payments of advance fees in kind require the same separation and safekeeping of the property until the fee is earned as advance payments of cash fees would require.<sup>363</sup>

LEO 186-B provides that a lawyer may not automatically impose a finance charge on clients' accounts. If the client has agreed to the amount of the fees and is able to pay but desires that payment be deferred for convenience, an interest charge may be imposed if the client agrees to the amount and imposition of the charge and retains the right of prepayment without penalty. The opinion reminds lawyers of their obligation to perform pro bono work where clients are not able to pay reasonable fees.<sup>364</sup> LEO 1247 considerably expands the scope of LEO 186-B and allows a lawyer to provide in an agreement with the client that bills are due within 30 days of the statement date, after which a finance charge will be imposed. LEO 1247 indicates any

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<sup>357</sup> LEO 1577 provides that an attorney may establish a 900-service telephone number for bankruptcy advice as long as (i) the message includes a statement that it is general information, not legal advice, and the listener should not try to solve his or her problem based on the advice; (ii) the message does not include any false, misleading, or deceptive statements; and (iii) the lawyer advises the caller that he or she will be charged for the call and that there are substantial limitations as to the general applicability of the information; *see also* Ohio Ethics Op. 93-1; Pennsylvania Ethics Op. 91-15. Utah would create an attorney-client relationship in this situation. Utah Bar Ethics Advisory Op. Comm., Op. 96-12.

<sup>358</sup> LEO 186-A; *see also* Alabama Ethics Op. RO-93-19. LEOs 1848 and 999 describe the proper procedures for clearing credit card payments through the lawyer's trust account.

<sup>359</sup> Connecticut Ethics Op. 87-3.

<sup>360</sup> Connecticut Bar Ass'n, Informal Op. 97-4.

<sup>361</sup> *Berman v. Linnane*, 679 N.E.2d 174 (Mass. 1997).

<sup>362</sup> LEO 558.

<sup>363</sup> *Id.*

<sup>364</sup> *See also* LEOs 1595 and 642, dealing with interest charged on outstanding costs advanced on behalf of clients.

such agreement would be subject to both federal and state laws regarding consumer credit and similar matters.<sup>365</sup>

The fee properly payable in a lawyer-client relationship that is terminated before completion of the task to be performed may be significantly different from what the parties initially contemplated. If the lawyer withdraws without good cause, he or she may forfeit all right to compensation.<sup>366</sup> A lawyer who breaches a duty to a client may forfeit all or part of the lawyer's compensation depending on the seriousness of the violation, the willfulness with which it was committed, and the impact of the breach on the value of the lawyer's work.<sup>367</sup>

A client has the right to terminate the lawyer at will.<sup>368</sup> If the lawyer is terminated by the client and has substantially performed the task to be completed, the lawyer may be entitled to all or substantially all of the contemplated fee.<sup>369</sup> In other circumstances, the client's former lawyer is only allowed to recover a fee from the client based on the legal theory of quantum meruit, which awards fees based on the reasonable value of the lawyer's services even if the lawyer has been terminated by the client without cause.<sup>370</sup> Quantum meruit evaluates the services themselves and not the value of the services to the client.<sup>371</sup> However, quantum meruit cannot serve as a basis for recovering a greater amount than the lawyer has contracted to be paid.<sup>372</sup> A terminated lawyer who is holding an advance payment of fees as client funds in a trust account must continue to hold them until the issue of the compensation to which the lawyer is entitled is resolved.<sup>373</sup>

Self-help or offsets against other funds of the client held by the lawyer are not appropriate to deal with fee disputes.<sup>374</sup> As a result, disputes often result in negotiations between lawyers and clients. LEO 1246 describes the progress of one such negotiation. A client made an initial payment of \$500 to a law firm that reviewed his case. The client did not retain the firm and subsequently asked for a refund. A dispute between the firm and the client arose concerning whether the payment was

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<sup>365</sup> See *Peterson v. Gustafson*, 584 N.W.2d 660 (Minn. Ct. App. 1998), which approved 18 percent interest in a situation in which a lawyer had rigorously complied with various credit reporting and disclosure rules.

<sup>366</sup> *Faro v. Romani*, 641 So. 2d 69 (Fla. 1994); *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 41:2013. A discharge for cause, however, may not cut off a lawyer's right to compensation on a quantum meruit basis. *Searcy, Denney, Scarola, Barnhart & Shipley v. Scheller, P.C.*, 629 So. 2d 947 (Fla. Dist. Ct. App. 4th Dist. 1993).

<sup>367</sup> *Restatement of the Law Governing Lawyers* § 37.

<sup>368</sup> Wolfram, *supra* note **Error! Bookmark not defined.**, at 545.

<sup>369</sup> *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 41:2013.

<sup>370</sup> *Heinzman v. Fine, Fine, Legum & Fine*, 217 Va. 958, 234 S.E.2d 282 (1977); *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 41:2012; Wolfram, *supra* note **Error! Bookmark not defined.**, at 546.

<sup>371</sup> The Standing Committee on Legal Ethics has refused to opine whether the quantum meruit amount of an attorney discharged during litigation is determined at the time of discharge or on conclusion of the litigation. LEO 1620. If requested, however, the discharged attorney must give an itemized statement of the services provided to the client and may not withhold the itemization in an effort to coerce a favorable settlement of the issue. LEO 1571. See *O'Rourke v. Cairns*, 683 So. 2d 697 (La. 1996), in which the court evaluated a quantum meruit claim on the basis of the Rule 1.5 factors and then adjusted them downward to reflect the seriousness of the attorney's misconduct.

<sup>372</sup> *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 41:2015.

<sup>373</sup> Rhode Island Ethics Advisory Panel, Op. 91-56; LEO 1246.

<sup>374</sup> *Johnson v. State Bar*, 12 Cal. App. 4th 1561 (Cal. App. 2d Dist. 1993).



only for the initial review of the case or was a retainer to be applied against future services. The firm gave the client the option of a refund of \$100 in return for a release, fee arbitration, or a referral to a lawyer through a lawyer referral service whose decision would be determinative. The client rejected all three alternatives. The opinion concludes that the law firm had no alternative but to continue to hold the money until the dispute was resolved by appropriate legal means. Presumably, interpleader would be an appropriate remedy.<sup>375</sup>

There is a division of opinion as to whether a lawyer may compromise a fee in return for the release of a malpractice claim.<sup>376</sup> A New York opinion allows the compromise of a fee in return for the release of a malpractice claim if the lawyer has been discharged or has quit, the client is fully apprised of the facts surrounding the claim, and the lawyer has advised the client to obtain independent counsel to assist in the matter. The opinion cautions that the lawyer may not use possession of the client's file as leverage to obtain the release.<sup>377</sup> A Maryland opinion, on the other hand, holds that it is improper for a lawyer disbursing a client's funds to ask that the client sign a "settlement statement" that, among other things, provides that the client is satisfied with the lawyer's representation.<sup>378</sup> Virginia has allowed a lawyer to negotiate a release with a client, but only if the matter to which the release relates has been concluded.<sup>379</sup>

A lawyer may not unilaterally withdraw from the representation if the client does not pay the fees.<sup>380</sup> A lawyer representing a client in litigation may ask the court for leave to withdraw, but it is the court that decides the propriety of the withdrawal rather than the lawyer.<sup>381</sup> If the lawyer is not allowed to withdraw, he or she must continue to participate actively in the case.<sup>382</sup> In other circumstances, the lawyer should take appropriate steps to ensure that the client's interests are not prejudiced.

Notwithstanding a statutory lien to secure fees,<sup>383</sup> a lawyer's actual right to withhold files and work product is limited. All original client-furnished documents and all originals of legal instruments or official documents in the lawyer's possession are the property of the client and must be returned to the client upon termination of the representation at the client's request, regardless of whether the client has paid the bill.<sup>384</sup> If the lawyer wishes to have copies, they must be made at the lawyer's expense. Also upon termination and the client's request, the client must be furnished

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<sup>375</sup> The lawyer can continue to assert a lien in the funds pending resolution of the dispute. LEO 996.

<sup>376</sup> *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 41:2010.

<sup>377</sup> New York Bar Ass'n, Ethics Op. 591.

<sup>378</sup> Maryland Ethics Op. 86-46.

<sup>379</sup> LEO 1550.

<sup>380</sup> *Lawyers' Manual*, *supra* note **Error! Bookmark not defined.**, at 41:2008.

<sup>381</sup> Rule 1.16(c); LEO 974.

<sup>382</sup> *Id.*; *see also* Minnesota Ethics Op. No. 4.

<sup>383</sup> Va. Code § 54.1-3932.

<sup>384</sup> Rule 1.16(e). Comment [11] to this rule notes that paragraph (e) does not require disclosure of materials if the disclosure would be prohibited by law.

copies of the following documents from the lawyer's file regardless of whether the client has paid the lawyer's bill:

lawyer/client and lawyer/third-party communications; the lawyer's copies of client-furnished documents (unless the originals have been returned to the client pursuant to this paragraph); transcripts, pleadings, and discovery responses; working and final drafts of legal instruments, official documents, investigative reports, legal memoranda, and other attorney work product documents prepared or collected for the client in the course of the representation; research materials; and bills previously submitted to the client.<sup>385</sup>

While the lawyer may ask the client to pay for such copies, the client's refusal to do so does not excuse the lawyer from providing the copies. Billing records and documents prepaid for internal use of the lawyer and his or her firm, however, are not required to be produced. The lawyer is required to furnish requested items only once and does not have to provide multiple copies. Provision of copies of documents on an item-by-item basis during the representation, however, is not sufficient.<sup>386</sup>

The statutory lien to secure fees may also extend to client funds in the lawyer's possession.<sup>387</sup> However, any funds in excess of the amount for which the lien is claimed must be remitted to the client with an accounting of the funds on which the lawyer claims a lien.<sup>388</sup>

There is no direct ethical prohibition against suits for fees.<sup>389</sup> A fee agreement can provide that a client is responsible for reasonable fees incurred in efforts to collect amounts due under the agreement.<sup>390</sup> Fees can also be referred to collection agencies as long as the confidences and secrets of the client are preserved and appropriate steps are taken to avoid controversy with the client.<sup>391</sup> It is improper to pursue a claim for fees to judgment after the fees have been paid.<sup>392</sup> A lawyer suing a client for a fee has the burden of proving (i) the terms of the contract, (ii) that all appropriate disclaimers were made, and (iii) the value of the lawyer's services.<sup>393</sup> A lawyer may only disclose confidential information to the extent reasonably necessary to collect fees.<sup>394</sup> Before suing a client for fees, a lawyer would do well to remember the advice of

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<sup>385</sup> *Id.*

<sup>386</sup> *Id.*

<sup>387</sup> See ¶ 1.9 of Section 1.

<sup>388</sup> LEO 1591.

<sup>389</sup> LEO 995. A Michigan opinion held that it is not appropriate to sue a client for a fee if the lawyer is still representing the client. Michigan Ethics Op. R-159.

<sup>390</sup> LEO 1667. A flat charge of \$500 is improper. *Id.*

<sup>391</sup> LEO 946.

<sup>392</sup> LEO 972.

<sup>393</sup> *Restatement of the Law Governing Lawyers* § 41.

<sup>394</sup> Rule 1.6(b)(2) and Comment [10a].

the ABA Standing Committee on Professional Liability: “A nearly foolproof way to be sued for legal malpractice is to sue a client for fees.”<sup>395</sup>

## CONCLUSION

While the lofty position taken by the ABA Committee on Ethics and Professional Responsibility in Formal Ethics Opinion 151 that the practice of law “is a branch of the administration of justice and not a mere money getting trade” may seem out of place in an era of lawyer advertising, intense competition among lawyers for business, and the metamorphosis of law firms into replicas of the business entities they represent, it is a reminder of the underlying nature of the lawyer-client relationship. The laissez-faire standards of the marketplace are not appropriate to evaluate a lawyer’s economic relationships with clients.

The ethical rules regarding a client’s funds, business relationships with clients, and fees charged to clients, while important in themselves, are reminders of the larger concerns regarding a lawyer-client relationship. A lawyer is a fiduciary for the client. The fiduciary relationship extends into both the economic and non-economic aspects of the lawyer-client relationship. Faithful adherence to the standards required of third-party fiduciaries and close attention to the specific requirements of the Virginia Rules of Professional Conduct will satisfy a lawyer’s obligation with respect to clients’ money both in fact and in spirit.

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<sup>395</sup> *Malpractice Desk Guide*, *supra* note **Error! Bookmark not defined.**, at 43.

## **APPENDIX 1: SELECTED VIRGINIA RULES OF PROFESSIONAL CONDUCT AND COMMENTARY**

### **RULE 1.5 Fees**

(a) A lawyer's fee shall be reasonable. The factors to be considered in determining the reasonableness of a fee include the following:

(1) the time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly;

(2) the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer;

(3) the fee customarily charged in the locality for similar legal services;

(4) the amount involved and the results obtained;

(5) the time limitations imposed by the client or by the circumstances;

(6) the nature and length of the professional relationship with the client;

(7) the experience, reputation, and ability of the lawyer or lawyers performing the services; and

(8) whether the fee is fixed or contingent.

(b) The lawyer's fee shall be adequately explained to the client. When the lawyer has not regularly represented the client, the amount, basis or rate of the fee shall be communicated to the client, preferably in writing, before or within a reasonable time after commencing the representation.

(c) A fee may be contingent on the outcome of the matter for which the service is rendered, except in a matter in which a contingent fee is prohibited by paragraph (d) or other law. A contingent fee agreement shall state in writing the method by which the fee is to be determined, including the percentage or percentages that shall accrue to the lawyer in the event of settlement, trial or appeal, litigation and other expenses to be deducted from the recovery, and whether such expenses are to be deducted before or after the contingent fee is calculated. Upon conclusion of a contingent fee matter, the lawyer shall provide the client with a written statement stating the outcome of the matter and, if there is a recovery, showing the remittance to the client and the method of its determination.

(d) A lawyer shall not enter into an arrangement for, charge, or collect a contingent fee:

- (1) in a domestic relations matter, except in rare instances;  
or
- (2) for representing a defendant in a criminal case.

(e) A division of a fee between lawyers who are not in the same firm may be made only if:

- (1) the client is advised of and consents to the participation of all the lawyers involved;
- (2) the terms of the division of the fee are disclosed to the client and the client consents thereto;
- (3) the total fee is reasonable; and
- (4) the division of fees and the client's consent is obtained in advance of the rendering of legal services, preferably in writing.

(f) Paragraph (e) does not prohibit or regulate the division of fees between attorneys who were previously associated in a law firm or between any successive attorneys in the same matter. In any such instance, the total fee must be reasonable.

## COMMENT

*Basis or Rate of Fee*

[1] *ABA Model Rule* Comment not adopted.

[2] When the lawyer has regularly represented a client, they ordinarily will have evolved an understanding concerning the basis or rate of the fee. In a new client-lawyer relationship, however, an understanding as to the amount, basis, or rate of the fee should be promptly established. It is not necessary to recite all the factors that underlie the basis of the fee, but only those that are directly involved in its computation. It is sufficient, for example, to state that the basic rate is an hourly charge or a fixed amount or an estimated amount, or to identify the factors that may be taken into account in finally fixing the fee. A written statement concerning the fee reduces the possibility of misunderstanding. Furnishing the client with a simple letter, memorandum, receipt or a copy of the lawyer's customary fee schedule may be sufficient if the basis or rate of the fee is set forth.

[3] *ABA Model Rule* Comment not adopted.

*Terms of Payment*

[4] A lawyer may require advance payment of a fee, but is obliged to return any unearned portion. *See* Rule 1.16(d). A lawyer may accept property in payment for services, such as an ownership interest in an enterprise, providing this does not involve acquisition of a proprietary interest in the cause of action or subject matter of the litigation contrary to Rule 1.8(j). However, a fee paid in property instead of money may be subject to special scrutiny because it involves questions concerning both the value of the services and the lawyer's special knowledge of the value of the property.

[5] An agreement may not be made whose terms might induce the lawyer improperly to curtail services for the client or perform them in a way contrary to the client's interest. For example, a lawyer should not enter into an agreement whereby services are to be provided only up to a stated amount when it is foreseeable that more extensive services probably will be required, unless the situation is adequately explained to the client. Otherwise, the client might have to bargain for further assistance in the midst of a proceeding or transaction. However, it is proper to define the extent of services in light of the client's ability to pay. A lawyer should not

exploit a fee arrangement based primarily on hourly charges by using wasteful procedures. When considering whether a contingent fee is consistent with the client's best interest, the lawyer should offer the client alternative bases for the fee and explain their implications. Applicable law may impose limitations on contingent fees, such as a ceiling on the percentage. In any event, a fee should not be imposed upon a client, but should be the result of an informed decision concerning reasonable alternatives.

*Contingent Fees in Domestic Relations Cases*

[6] An arrangement for a contingent fee in a domestic relations matter has been previously considered appropriate only in those rare instances where:

(a) the contingent fee is for the collection of, and is to be paid out of (i) accumulated arrearages in child or spousal support; (ii) an asset not previously viewed or contemplated as a marital asset by the parties or the court; (iii) a monetary award pursuant to equitable distribution or under a property settlement agreement;

(b) the parties are divorced and reconciliation is not a realistic prospect;

(c) the children of the marriage are or will soon achieve the age of maturity and the legal services rendered pursuant to the contingent fee arrangement are not likely to affect their relationship with the non-custodial parent;

(d) the client is indigent or could not otherwise obtain adequate counsel on an hourly fee basis; and

(e) the fee arrangement is fair and reasonable under the circumstances.

*Division of Fee*

[7] A division of fee refers to a single billing to a client covering the fee of two or more lawyers who are not in the same firm. A division of fee facilitates association of more than one lawyer in a matter in which neither alone could serve the client as well, and

most often is used when the fee is contingent and the division is between a referring lawyer and a trial specialist.

[8] *ABA Model Rule* Comment not adopted.

*Disputes over Fees*

[9] If a procedure has been established for resolution of fee disputes, such as an arbitration or mediation procedure established by the bar, the lawyer should conscientiously consider submitting to it. Law may prescribe a procedure for determining a lawyer's fee, for example, in representation of an executor or administrator, a class or a person entitled to a reasonable fee as part of the measure of damages. The lawyer entitled to such a fee and a lawyer representing another party concerned with the fee should comply with the prescribed procedure.

VIRGINIA CODE COMPARISON

With regard to paragraph (a), DR 2-105(A) required that a "lawyer's fees . . . be reasonable and adequately explained to the client." The factors involved in assessing the reasonableness of a fee listed in Rule 1.5(a) are substantially similar to those listed in EC 2-20.

Paragraph (b) emphasizes the lawyer's duty to adequately explain fees (which appears in DR 2-105(A)) but stresses the lawyer's duty to disclose fee information to the client rather than merely responding to a client's request for information (as in DR 2-105(B)).

Paragraph (c) is substantially the same as DR 2-105(C). EC 2-22 provided that "[c]ontingent fee arrangements in civil cases have long been commonly accepted in the United States," but that "a lawyer generally should decline to accept employment on a contingent fee basis by one who is able to pay a reasonable fixed fee...."

With regard to paragraph (d), DR 2-105(C) prohibited a contingent fee in a criminal case. EC 2-22 provided that "contingent fee arrangements in domestic relation cases are rarely justified."

With regard to paragraph (e), DR 2-105(D) permitted division of fees only if: "(1) The client consents to employment of additional



counsel; (2) Both attorneys expressly assume responsibility to the client; and (3) The terms of the division of the fee are disclosed to the client and the client consents thereto.”

There was no counterpart to paragraph (f) in the *Virginia Code*.

#### COMMITTEE COMMENTARY

The Committee believes that DR 2-105 placed greater emphasis than the *ABA Model Rule* on the Full Disclosure of Fees and Fee Arrangements to Clients and therefore added language from DR 2-105(A) to paragraph (a) and from DR 2-105(D)(3) to paragraph (e). The Comment to paragraph (d)(1) reflects the Committee’s conclusion that the public policy concerns which preclude contingent fee arrangements in certain domestic relations cases do not apply when property division, support matters or attorney’s fee awards have been previously determined. Paragraph (e) eliminates the requirement in the *Virginia Code* that each lawyer involved in a fee-splitting arrangement assume full responsibility to the client, regardless of the degree of the lawyer’s continuing participation. The requirement in the *Virginia Code* was deleted to encourage referrals under appropriate circumstances by not requiring the lawyer making the referral to automatically assume ethical responsibility for all of the activities of the other lawyers involved in the arrangement. However, such an arrangement is acceptable only if the client consents after full disclosure, which must include a delineation of each lawyer’s responsibilities to the client.

#### RULE 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 for the advantage of the lawyer or of a third person or to the disadvantage of the client unless the client consents after consultation, except as permitted or required by Rule 1.6 or Rule 3.3.

(c) A lawyer shall not solicit, for himself or a person related to the lawyer, any substantial gift from a client including a testamentary gift. A lawyer shall not accept any such gift if solicited at his request by a third party. A lawyer shall not prepare an instrument giving the lawyer or a person related to the lawyer any substantial gift from a client, including a testamentary gift, unless the lawyer or other recipient of the gift is related to the client. For purposes of this paragraph, a person related to a lawyer includes a spouse, child, grandchild, parent, or other relative or individual with whom the lawyer or the client maintains a close, familial relationship.

(d) Prior to the conclusion of all aspects of a matter giving rise to the 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, provided the client remains ultimately liable for such costs and expenses ; 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) 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, except that a lawyer may make such an agreement with a client of which the lawyer is an employee as long as the client is independently represented in making the agreement.

(i) A lawyer related to another lawyer as parent, child, sibling or spouse, or who is intimately involved with another lawyer, 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) 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, unless prohibited by Rule 1.5.

(k) While lawyers are associated in a firm, none of them shall knowingly enter into any transaction or perform any activity when one of them practicing alone would be prohibited from doing so by paragraphs (a), (b), (c), (d), (e), (f), (g), (h), or (j) of this Rule.

## COMMENT

*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. Similarly, paragraph (b) does not limit an attorney's use of information obtained independently outside the attorney-client relationship.

[2-5] *ABA Model Rule* Comments not adopted.

[6] A lawyer may accept ordinary gifts from a client. For example, an ordinary 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.

[7-8] *ABA Model Rule* Comments not adopted.

*Literary Rights*

[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).

[10] *ABA Model Rule* Comments not adopted.

*Person Paying for a Lawyer's Services*

[11] 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, Rule 1.7 concerning conflict of interest, and Rule 5.4(c) concerning the professional independence of a lawyer. Where the client is a class, consent may be obtained on behalf of the class by court-supervised procedure.

*Family Relationships Between Lawyers*

[12] 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.

[13-15] *ABA Model Rule* Comments not adopted.

*Acquisition of Interest in Litigation*

[16] 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 or payment of the costs of litigation set forth in paragraph (e).

VIRGINIA CODE COMPARISON

With regard to paragraph (a), DR 5-104(A) provided that a lawyer "shall not enter into a business transaction with a client if they have differing interests therein and if the client expects the lawyer to exercise his professional judgment therein for the

protection of the client, unless the client has consented after full

and adequate disclosure . . .” EC 5-3 stated that a lawyer “should not seek to persuade his client to permit him to invest in an undertaking of his client nor make improper use of his professional relationship to influence his client to invest in an enterprise in which the lawyer is interested.”

Paragraph (b) is substantially similar to DR 4-101(B)(3) which provided that a lawyer should not use “a confidence or secret of his client for the advantage of himself, or a third person, unless the client consents after full disclosure.”

Paragraph (c) is substantially similar to DR 5-104(B) which stated that a lawyer “shall not prepare an instrument giving the lawyer or a member of the lawyer’s family any gift from a client, including a testamentary gift, except where the client is a relative of the donee.” EC 5-5 stated that a lawyer “should not suggest to his client that a gift be made to himself or for his benefit. If a lawyer accepts a gift from his client, he is peculiarly susceptible to the charge that he unduly influenced or overreached the client. If a client voluntarily offers to make a gift to his lawyer, the lawyer may accept the gift, but before doing so, he should urge that the client secure disinterested advice from an independent, competent person who is cognizant of all the circumstances. Except in those instances in which the client is related to the donee, a lawyer may not prepare an instrument by which the client gives a gift to the lawyer or to a member of his family.”

Paragraph (d) has no direct counterpart in the *Virginia Code*. EC 5-4 stated that in order to avoid “potentially differing interests” a lawyer should “scrupulously avoid [literary arrangements with a client] prior to the termination of all aspects of the matter giving rise to the employment, even though [the lawyer’s] employment has previously ended.”

Paragraph (e)(1) incorporates the provisions of DR 5-103(B), including the requirement that the client remain “ultimately liable” for such advanced expenses.

Paragraph (e)(2) has no direct counterpart in the *Virginia Code*, although DR 5-103(B) allowed a lawyer to advance or guarantee expenses of litigation as long as the client remained ultimately liable.

Paragraph (f) is substantially similar to DR 5-106(A)(1) and DR 5-106(B). DR 5-106(A)(1) stated: “Except with the consent of his client after full and adequate disclosure under the circumstances, a lawyer shall not . . . [a]ccept compensation for his legal services from one other than his client.” DR 5-106(B) stated that “[a] lawyer shall not permit a person who recommends, employs, or pays him to render legal services for another to direct or regulate his professional judgment in rendering such legal services.”

Paragraph (g) is substantially similar to DR 5-107, but also covers aggregated plea agreements in criminal cases.

The first portion of Paragraph (h) is essentially the same as DR 6-102(A), but the second portion of Paragraph (h) has no counterpart in the *Virginia Code*. The new provision allows in-house lawyers to arrange for the same indemnity available to other officers and employees, as long as their employers are independently represented in making the arrangement.

Paragraph (i) has no counterpart in the *Virginia Code*.

Paragraph (j) is substantially the same as DR 5-103(A).

Paragraph (k) had no counterpart in the *Virginia Code*.

#### COMMITTEE COMMENTARY

The Committee added “for the advantage of himself or a third person” from DR 4-101(B)(3) to paragraph (b) as a further limitation on a lawyer’s use of information relating to representation of a client.

The Committee added a further time limitation to paragraph (d)’s restriction. Borrowing language from EC 5-4, the restriction on agreements giving a lawyer literary or media rights extends through the conclusion of “all aspects of a matter giving rise to the representation.”

In Rule 1.8(e)(1), the Committee retained the requirement in DR 5-103(B) that a client must “remain ultimately liable for [litigation] expenses.” However, the Committee adopted the limited exception for indigent clients that appears in Rule 1.8(e)(2).



After lengthy debate, the Committee adopted 1.8(h), which retains the general prohibition on lawyers prospectively limiting their malpractice liability to clients (which appeared in *Virginia Code* DR 6-102). However, the Committee added a limited exception that allows in-house lawyers to arrange for the type of indemnity that other officers and employees of entities may obtain. The Committee voted to insist that the client be independently represented in agreeing to any such arrangement.

In 1.8(i), the Committee adopted the *ABA Model Rule* approach, which permits lawyers who are members of the same nuclear family to represent clients adverse to each other, as long as both clients consent after full disclosure. The *Virginia Code* was interpreted to create a non-waivable *per se* conflict of interest in these circumstances. See LEO 190 (April 1, 1985).

#### RULE 1.15 Safekeeping Property

##### (a) Depositing Funds.

(1) All funds received or held by a lawyer or law firm on behalf of a client or a third party, or held by a lawyer as a fiduciary, other than reimbursement of advances for costs and expenses shall be deposited in one or more identifiable trust accounts or placed in a safe deposit box or other place of safekeeping as soon as practicable.

(2) For lawyers or law firms located in Virginia, a lawyer trust account shall be maintained only at a financial institution approved by the Virginia State Bar, unless otherwise expressly directed in writing by the client for whom the funds are being held.

(3) No funds belonging to the lawyer or law firm shall be deposited or maintained therein except as follows:

(i) funds reasonably sufficient to pay service or other charges or fees imposed by the financial institution or to maintain a required minimum balance to avoid the imposition of service fees, provided the funds deposited are no more than necessary to do so; or

(ii) funds in which two or more persons (one of whom may be the lawyer) claim an interest shall be held in the trust account until the dispute is resolved and there is an accounting and severance of their interests. Any portion finally determined to belong to the lawyer or law firm shall be withdrawn promptly from the trust account.

##### (b) Specific Duties. A lawyer shall:

(1) promptly notify a client of the receipt of the client's funds, securities, or other properties;

(2) identify and label securities and properties of a client, or those held by a lawyer as a fiduciary, promptly upon receipt;

(3) maintain complete records of all funds, securities, and other properties of a client coming into the possession of the lawyer and render appropriate accountings to the client regarding them;

(4) promptly pay or deliver to the client or another as requested by such person the funds, securities, or other properties in the possession of the lawyer that such person is entitled to receive; and

(5) not disburse funds or use property of a client or third party without their consent or convert funds or property of a client or third party, except as directed by a tribunal.

(c) Record-Keeping Requirements. A lawyer shall, at a minimum, maintain the following books and records demonstrating compliance with this Rule:

(1) Cash receipts and disbursements journals for each trust account, including entries for receipts, disbursements, and transfers, and also including, at a minimum: an identification of the client matter; the date of the transaction; the name of the payor or payee; and the manner in which trust funds were received, disbursed, or transferred from an account.

(2) A subsidiary ledger containing a separate entry for each client, other person, or entity from whom money has been received in trust.

The ledger should clearly identify:

(i) the client or matter, including the date of the transaction and the payor or payee and the means or methods by which trust funds were received, disbursed or transferred; and

(ii) any unexpended balance.

(3) In the case of funds or property held by a lawyer as a fiduciary, the required books and records shall include an annual summary of all receipts and disbursements and changes in assets comparable in detail to an accounting that would be required of a court supervised fiduciary in the same or similar capacity; including all source documents sufficient to substantiate the annual summary.

(4) All records subject to this Rule shall be preserved for at least five calendar years after termination of the representation or fiduciary responsibility.

(d) Required Trust Accounting Procedures. In addition to the requirements set forth in Rule 1.15 (a) through (c), the following minimum trust accounting procedures are applicable to all trust accounts.

(1) Insufficient Fund Reporting. All accounts are subject to the requirements governing insufficient fund check reporting as set forth in the Virginia State Bar Approved Financial Institution Agreement.

(2) Deposits. All trust funds received shall be deposited intact. Mixed trust and non-trust funds shall be deposited intact into the trust fund and the non-trust portion shall be withdrawn upon the clearing of the mixed fund deposit instrument. All such deposits should include a detailed deposit slip or record that sufficiently identifies each item.

(3) Reconciliations.

(i) At least quarterly a reconciliation shall be made that reflects the trust account balance for each client, person or other entity.

(ii) A monthly reconciliation shall be made of the cash balance that is derived from the cash receipts journal, cash disbursements journal, the trust account checkbook balance and the trust account bank statement balance.

(iii) At least quarterly, a reconciliation shall be made that reconciles the cash balance from (d)(3)(ii) above and the subsidiary ledger balance from (d)(3)(i).

(iv) Reconciliations must be approved by a lawyer in the law firm.

(4) The purpose of all receipts and disbursements of trust funds reported in the trust journals and ledgers shall be fully explained and supported by adequate records.

**Comment**

[1] A lawyer should hold property of others with the care required of a professional fiduciary. Securities should be kept in a safe deposit box, except when some other form of safekeeping is warranted by special circumstances. For purposes of this Rule, the term “fiduciary” includes personal representative, trustee, receiver, guardian, committee, custodian, and attorney-in-fact. All property that is the property of clients or third persons should be kept separate from the lawyer's business and personal property and, if monies, in one or more trust accounts. Separate trust accounts may be warranted when administering estate monies or acting in similar fiduciary capacities.

[2] Separation of the funds of a client from those of the lawyer not only serves to protect the client but also avoids even the appearance of impropriety, and therefore commingling of such funds should be avoided.

[2a] In relation to (b)(5), consent can be inferred from the engagement agreement or any consequential agreement between the lawyer and the client regarding the disbursement of fees, i.e., when earned fees are routinely withdrawn from the lawyer's trust account upon an accounting to the client, when costs and expenses of litigation are routinely withdrawn, or when other fees/costs or expenses are agreed upon in advance.

[3] Lawyers often receive funds from third parties from which the lawyer's fee will be paid. If there is risk that the client may divert the funds without paying the fee, the lawyer is not required to remit the portion from which the fee is to be paid. However, a lawyer may not hold funds to coerce a client into accepting the lawyer's contention. The disputed portion of the funds should be kept in trust and the lawyer should suggest means for prompt resolution of the dispute, such as arbitration or mediation. The

undisputed portion of the funds shall be promptly distributed.

[4] Paragraphs (b)(4) and (b)(5) do not impose an obligation upon the lawyer to protect funds on behalf of the client's general creditors who have no valid claim to an interest in the specific funds or property in the lawyer's possession. However, a lawyer may be in possession of property or funds claimed both by the lawyer's client and a third person; for example, a previous lawyer of the client claiming a lien on the client's recovery or a person claiming that the property deposited with the lawyer was taken or withheld unlawfully from that person. Additionally, a lawyer may have a duty under applicable law to protect such third-party claims against wrongful interference by the client, and accordingly may refuse to surrender the property to the client. For example, if a lawyer has actual knowledge of a third party's lawful claim to an interest in the specific funds held on behalf of a client, then by virtue of a statutory lien (e.g., medical, workers' compensation, attorneys' lien, a valid assignment executed by the client, or a lien on the subject property created by a recorded deed of trust) the lawyer has a duty to secure the funds claimed by the third party. Under the above described circumstances, paragraphs (b)(4) and (b)(5) require the lawyer either to deliver the funds or property to the third party or, if a dispute to the third party's claim exists, to safeguard the contested property or funds until the dispute is resolved. If the client has a non-frivolous dispute with the third party's claim, then the lawyer cannot release those funds without the agreement of all parties involved or a court determination of who is entitled to receive them, such as an interpleader action. A lawyer does not violate paragraphs (b)(4) and (b)(5) if he has acted reasonably and in good faith to determine the validity of a third-party's claim or lien.

[5] The obligations of a lawyer under this Rule are independent of those arising from activity other than rendering legal services. For example, a lawyer who serves as an escrow agent is governed by the applicable law relating to fiduciaries even though the lawyer does not render legal services in the transaction.

[6] Nothing in this Rule is intended to prohibit an attorney from using electronic checking for his trust account so long as all requirements in this Rule are fulfilled. It is the lawyer's responsibility to assure that complete and accurate records of the receipt and disbursement of entrusted property are maintained in accordance with this rule. Many businesses are now converting paper checks to automated clearinghouse (ACH) debits. Authorized ACH debits that are electronic transfers of funds (in which no checks are involved) are allowed provided the lawyer maintains a record of the transaction as required by this rule. The record, whether consisting of the instructions or authorization to debit the account, a record or receipt from the financial institution, or the lawyer's independent record of the transaction, must show the amount, date, recipient of the transfer or disbursement, and the name of the client or other person to whom the funds belong.

### **Prior Rule Comparison**

This rule is substantially the same as the original Rule 1.15 adopted January 1, 2000 except that the language has been substantially simplified for ease of understanding and the portions regarding the Financial Institutions duties redacted as they are appropriately incorporated into the "Trust Account Notification Agreement" signed by all Virginia approved financial institutions.

### **Committee Commentary**

The Committee chose to modify the rule for ease of understanding and enforcement with no substantive changes to a lawyer's safekeeping property and recordkeeping requirements.

#### **RULE 1.16 Declining or Terminating Representation**

(a) Except as stated in paragraph (c), a lawyer shall not represent a client or, where representation has commenced, shall withdraw from the representation of a client if:

(1) the representation will result in violation of the Rules of Professional Conduct or other law;

(2) the lawyer's physical or mental condition materially impairs the lawyer's ability to represent the client; or

(3) the lawyer is discharged.

(b) Except as stated in paragraph (c), a lawyer may withdraw from representing a client if withdrawal can be accomplished without material adverse effect on the interests of the client, or if:

(1) the client persists in a course of action involving the lawyer's services that the lawyer reasonably believes is illegal or unjust;

(2) the client has used the lawyer's services to perpetrate a crime or fraud;

(3) a client insists upon pursuing an objective that the lawyer considers repugnant or imprudent;

(4) the client fails substantially to fulfill an obligation to the lawyer regarding the lawyer's services and has been given reasonable warning that the lawyer will withdraw unless the obligation is fulfilled;

(5) the representation will result in an unreasonable financial burden on the lawyer or has been rendered unreasonably difficult by the client; or

(6) other good cause for withdrawal exists.

(c) In any court proceeding, counsel of record shall not withdraw except by leave of court after compliance with notice requirements pursuant to applicable Rules of Court. In any other matter, a lawyer shall continue representation notwithstanding good cause for terminating the representation, when ordered to do so by a tribunal.

(d) Upon termination of representation, a lawyer shall take steps to the extent reasonably practicable to protect a client's interests, such as giving reasonable notice to the client, allowing time for employment of other counsel, refunding any advance payment of fee that has not been earned and handling records as indicated in paragraph (e).

(e) All original, client-furnished documents and any originals of legal instruments or official documents which are in the lawyer's possession (wills, corporate minutes, etc.) are the property of the client and, therefore, upon termination of the representation, those items shall be returned within a reasonable time to the client or the client's new counsel upon request, whether or not the client has paid the fees and costs owed the lawyer. If the lawyer wants to keep a copy of such original documents, the lawyer must incur the cost of duplication. Also upon termination, the client, upon request, must also be provided within a reasonable time copies of the following documents from the lawyer's file, whether or not the client has paid the fees and costs owed the lawyer: lawyer/client and lawyer/third-party communications; the lawyer's copies of client-furnished documents (unless the originals have been returned to the client pursuant to this paragraph); transcripts, pleadings and discovery responses; working and final drafts of legal instruments, official documents, investigative reports, legal memoranda, and other attorney work product documents prepared or collected for the client in the course of the representation; research materials; and bills previously submitted to the client. Although the lawyer may bill and seek to collect from the client the costs associated with making a copy of these materials, the lawyer may not use the client's refusal to pay for such materials as a basis to refuse the client's request. The lawyer, however, is not required under this Rule to provide the client copies of billing records and documents intended only for internal use, such as memoranda prepared by the lawyer discussing conflicts of interest, staffing considerations, or difficulties arising from the lawyer-client relationship. The lawyer has met his or her obligation under this paragraph by furnishing these items one time at client request upon termination; provision of multiple copies is not required. The lawyer has not met his or her obligation under this paragraph by the mere provision of copies of documents on an item-by-item basis during the course of the representation.

#### COMMENT

[1] A lawyer should not accept or continue representation in a matter unless it can be performed competently, promptly, without improper conflict of interest and to completion.

*Mandatory Withdrawal*

[2] A lawyer ordinarily must decline or withdraw from representation if the client demands that the lawyer engage in conduct that is illegal or violates the Rules of Professional Conduct or other law. The lawyer is not obliged to decline or withdraw simply because the client suggests such a course of conduct; a client may make such a suggestion in the hope that a lawyer will not be constrained by a professional obligation.

[3] When a lawyer has been appointed to represent a client, withdrawal ordinarily requires approval of the appointing authority. *See* also Rule 6.2. Difficulty may be encountered if withdrawal is based on the client's demand that the lawyer engage in unprofessional conduct. The court may wish an explanation for the withdrawal, while the lawyer may be bound to keep confidential the facts that would constitute such an explanation. The lawyer's statement that professional considerations require termination of the representation ordinarily should be accepted as sufficient.

*Discharge*

[4] A client has a right to discharge a lawyer at any time, with or without cause. Where future dispute about the withdrawal may be anticipated, it may be advisable to prepare a written statement reciting the circumstances.

[5] Whether a client can discharge appointed counsel may depend on applicable law. A client seeking to do so should be given a full explanation of the consequences. These consequences may include a decision by the appointing authority that appointment of successor counsel is unjustified, thus requiring the client to proceed *pro se*.

[6] If the client is mentally incompetent, the client may lack the legal capacity to discharge the lawyer, and in any event the discharge may be seriously adverse to the client's interests. The lawyer should make special effort to help the client consider the consequences and, in an extreme case, may initiate proceedings for a conservatorship or similar protection of the client. *See* Rule 1.14.



*Optional Withdrawal*

[7] A lawyer may withdraw from representation in some circumstances. The lawyer has the option to withdraw if it can be accomplished without material adverse effect on the client's interests. Withdrawal is also justified if the client persists in a course of action that the lawyer reasonably believes is illegal or unjust, for a lawyer is not required to be associated with such conduct even if the lawyer does not further it. Withdrawal is also permitted if the lawyer's services were misused in the past even if that would materially prejudice the client. The lawyer also may withdraw where the client insists on a repugnant or imprudent objective.

[8] A lawyer may withdraw if the client refuses to abide by the terms of an agreement relating to the representation, such as an agreement concerning fees or court costs or an agreement limiting the objectives of the representation.

*Assisting the Client upon Withdrawal*

[9] Even if the lawyer has been unfairly discharged by the client, a lawyer must take all reasonable steps to mitigate the consequences to the client. Whether or not a lawyer for an organization may under certain unusual circumstances have a legal obligation to the organization after withdrawing or being discharged by the organization's highest authority is beyond the scope of these Rules.

*Retention of Client Papers or File When Client Fails or Refuses to Pay Fees/Expenses Owed to Lawyer*

[10] Paragraph (e) eschews a "prejudice" standard in favor of a more objective and easily-applied rule governing specific kinds of documents in the lawyer's files.

[11] The requirements of paragraph (e) should not be interpreted to require disclosure of materials where the disclosure is prohibited by law.

VIRGINIA CODE COMPARISON

Paragraph (a) is substantially the same as DR 2-108(A).

Paragraph (b) is substantially similar to DR 2-108(B) which provided that a lawyer “may withdraw from representing a client if: (1) Withdrawal can be effected without material prejudice to the client; or (2) The client persists in a course of conduct involving the lawyer’s services that the lawyer reasonably believes is illegal or unjust; or (3) The client fails to fulfill an obligation to the lawyer regarding the lawyer’s services and such failure continues after reasonable notice to the client; or (4) The representation will result in an unreasonable financial burden on the lawyer or has been rendered unreasonably difficult by the client.”

Paragraph (c) is identical to DR 2-108(C).

Paragraph (d) is based on DR 2-108(D), but does not address documents in the lawyer’s files (which are handled under paragraph (e)).

Paragraph (e) is new.

COMMITTEE COMMENTARY

The provisions of DR 2-108 of the *Virginia Code* derived more from *ABA Model Rule* 1.16 than from its counterpart in the *ABA Model Code*, DR 2-110. Accordingly, the Committee generally adopted the *ABA Model Rule*, but substituted the “illegal or unjust” language from DR 2-108(B)(2) for the “criminal or fraudulent” language of the *ABA Model Rule*. Additionally, the Committee substituted the language of DR 2-108(C) for that of paragraph (c) of the *ABA Model Rule* to make it clear that a lawyer, in circumstances involving court proceedings, has an affirmative duty to request leave of court to withdraw. The Committee recommended paragraph (e) instead of a “prejudice” standard as being more easily understood and applied by lawyers.

**APPENDIX 2: PART 6, SECTION IV, PARAGRAPH 20, RULES OF  
THE SUPREME COURT OF VIRGINIA**

**20. Maintenance of Trust Accounts; Notice of Election Requirements—**

Every trust account maintained by an active member of the VSB under Rules of Professional Conduct 1.15 shall also be maintained at a “financial institution approved by the Virginia State Bar” and maintained in accordance with this paragraph and Rule 1.15. A “financial institution approved by the Virginia State Bar” includes regulated state or federal chartered banks, savings institutions, and credit unions that are properly licensed and authorized to do business, have federal insurance on deposits, and have entered into and agreed to abide by a Virginia State Bar Approved Financial Institution Agreement. (See Appendix A which the Virginia State Bar reserves the right to amend or modify upon notice to all approved financial institutions.) The Virginia State Bar shall maintain and publish from time to time a list of approved financial institutions.

**A. Interest-bearing Trust Accounts.** A lawyer may maintain funds of clients in one or more interest-bearing accounts in one or more financial institutions, whenever the lawyer has established and follows record-keeping, accounting, clerical, and administrative procedures to compute and credit or pay periodically, but at least quarterly, pro rata to each client the interest on such client’s funds less fees, costs, or expenses charged by the lawyer for the record-keeping, accounting, clerical, and administrative procedures associated with computing and crediting or paying such amounts.

**B. IOLTA Accounts.** A lawyer may deposit funds of a client in an identifiable interest-bearing trust (IOLTA) account for which the lawyer has not established procedures to compute and credit or pay pro rata net earnings to such client whenever:

1. At the time of such deposit the lawyer reasonably expects that the fees, costs, or expenses which the lawyer would be entitled to charge under Paragraph 20(A) would equal or exceed the pro rata interest on such client’s funds (The determination of whether the funds of a client or third person can earn income in excess of fees, costs or expenses the lawyer would be entitled to charge under paragraph 20(A) shall rest in the sound judgment of the lawyer or law firm, and no lawyer shall be charged with an ethical impropriety or breach of professional conduct based on the good faith exercise of such judgment); and
2. The financial institution has agreed to:
  - a. Periodically, but at least quarterly, remit to the Legal Services Corporation of Virginia (LSCV) interest or dividends on the average monthly balance of each such account or as otherwise computed in accordance with such bank’s standard accounting practice, provided that such rate of interest shall not be less than the rate paid by such bank to regular, non-attorney depositors;
  - b. Transmit with each remittance to LSCV a statement identifying the name of the lawyer or law firm from whose account the remittance is sent, the rate of interest applied, the period for which the remittance is made, the total amount of

interest earned, the service charges or other fees assessed against the account, if any, and the net amount of interest remitted;

c. Transmit to the depositing lawyer or law firm at the same time a report showing the amount paid to LSCV from such interest-bearing account, the rate of interest applied, the fees assessed, if any, and the average account balance for the period for which the report is made;

d. Charge no fees against an IOLTA trust account that are greater than the fees charged to non-attorney depositors, except that an IOLTA remittance fee may be charged to defray the depository institution's administrative costs attributable to calculating and remitting the interest to LSCV; other allowable fees are per check charges, per deposit charges, a fee in lieu of a minimum balance and sweep fees. Allowable, reasonable fees may be deducted from interest or dividends earned on an IOLTA account, provided that such charges or fees shall be calculated in accordance with the Financial Institutions' standard practice for non-IOLTA customers. Fees or charges in excess of the interest or dividends earned on the IOLTA account, for any month or quarter, shall not be taken from the interest or dividends of any other IOLTA account. Fees for wire transfers, insufficient funds, bad checks, stop payment, account reconciliation, negative collected balances, and check printing are not considered customary account maintenance charges and are not deductible from the interest or dividends earned on the IOLTA account. All other fees including those non-customary fees just listed are the responsibility of the lawyer or law firm, who in turn may absorb these specific costs or pass along those fees to the client(s) being served by the transaction in accordance with attorney/client agreements. Financial Institutions may elect to waive any or all fees on IOLTA accounts in recognition of their charitable nature;

e. Collect no fees from the principal deposited in the IOLTA trust account;

f. Pay all or part of the funds deposited in such interest-bearing trust account upon demand or order. An IOLTA account may be an interest-bearing check account, a money market account with or tied to check-writing, a sweep account which is a government money market fund or daily overnight financial institution repurchase agreement invested solely in or fully collateralized by United States government securities, or an open-end money market fund solely invested in or fully collateralized by the United States government securities; and

g. Agree and abide by all provisions in the Virginia State Bar Approved Financial Institution Agreement.

3. Interest accruing on such accounts and paid by the financial institution to LSCV shall be used for funding 1) civil legal services to the poor in Virginia, 2) LSCV's administrative expenses, and 3) the

creation and augmentation of a reserve fund for the same purposes.  
C.Non-interest-bearing Trust Accounts. A lawyer may deposit funds of a client in an identifiable non-interest-bearing trust account for which the account accrues no interest or dividends so long as the attorney or law firm receives no consideration or benefit from the Financial Institution for opening a non-interest bearing trust account or for converting from an IOLTA account to a non-interest bearing trust account. A lawyer who elects not to participate in the maintenance of an interest-bearing trust account as described in Paragraph 20(B) must submit such an election in accordance with the procedures set forth in Paragraph 20(F) of this rule.

D.Reporting to Client. A lawyer who elects to deposits funds of a client in an account pursuant to Paragraph 20(B) or (C) shall not be required to seek permission from such client in making the election. As to funds deposited in accordance with Paragraph 20(B), a lawyer shall not be required to compute or report to such client any payment to LSCV of interest or dividends by the banking institution on funds in any such account wherein the client’s funds have been deposited by the lawyer.

E.Law Firm Trust Accounts. A law firm of which any participating lawyer is a member may maintain the account(s) on behalf of any or all lawyers in the firm.

F.Opt-Out of IOLTA Account. A lawyer who elects to open an IOLTA account shall obtain a “Request to Establish IOLTA Account” form from LSCV. A lawyer who elects not to maintain an IOLTA account shall make such election on a “Request to Opt-Out” form provided by LSCV.

#### **APPENDIX A**

Virginia State Bar Approved Financial Institution Agreement

This Virginia State Bar Financial Institution Agreement (“Agreement”) is made this \_\_\_\_\_ day of \_\_\_\_\_, by and between the Virginia State Bar and \_\_\_\_\_, (“Financial Institution”).

#### **WITNESS:**

The undersigned, an officer of the Financial Institution executing this Agreement, being duly authorized to bind said institution by this Agreement, hereby applies to be approved as a depository to receive escrow, trust, or client funds, as defined in Part 6, § IV, Para. 20, of the Rules of Supreme Court of Virginia, or any successor provision(s), from attorneys for deposit in what are hereinafter referred to as “Trust Accounts.” The Financial Institution agrees to comply with the following requirements, or any successor provisions:

- 1.**Notification to Attorneys or Law Firm**. To notify the attorney or law firm promptly of an overdraft in any Trust Account or the dishonor for insufficient funds of any instrument drawn on any Trust Account held by it.
- 2.**Notification to Bar Counsel**. To report the overdraft or dishonor to Bar Counsel of the Virginia State Bar, as set forth in Paragraph 5 of this Agreement.
- 3.**Audit of Trust Account**. To provide reasonable access to the Virginia State Bar of all records of the Trust Account if an audit of such account is ordered pursuant to court order, or upon receipt of a subpoena therefor. The financial institution may charge for the reasonable costs of producing these records.
- 4.**Interest Calculation**. The financial institution shall not engage in the practice of “negative netting” as to IOLTA trust accounts.
- 5.**Form of Report**. That all such reports shall be substantially in the following format:

In either case of a dishonored instrument or an instrument

presented against insufficient funds in a Trust Account, but honored by the financial institution, the report shall be identical to the notice customarily forwarded to the depositor and shall include the name and address of the depositor notified, including the name of the lawyer responsible for the account, as well as a copy of the dishonored instrument, if such copy is normally provided to the depositor. In addition, the report shall identify the financial institution reporting the overdraft, the account number, the date of the overdraft, the name of the person making the report, their address and telephone number and date. The report shall be made simultaneously with and within the time provided by law for notice of dishonor to the depositor or, in the case of instruments that are honored by the financial institution, within five (5) banking days after the date of presentation for payment against insufficient funds.

**6. Consent of Attorneys or Law Firms.** The Financial Institution may require, as a condition to opening an attorney Trust Account, the written consent of the attorney or law firm opening such account to the notification to Bar Counsel of the Virginia State Bar as set forth in Paragraph 2 of this Agreement.

**7. Change of Name or Corporate Form.** If a Financial Institution changes its name, merges or otherwise affiliates with, or is acquired by another entity, the successor Financial Institution shall promptly notify Bar Counsel of the change and whether the successor institution wishes to serve as a financial institution approved by the Virginia State Bar for attorney Trust Accounts and enter into an Agreement.

**8. Termination of Agreement.** This Agreement may terminate upon thirty (30) days notice from the Financial Institution in writing to Bar Counsel that the institution intends to terminate the Agreement on a stated date and that copies of the termination notice have been mailed to all attorneys and law firms that maintain Trust Accounts with the Financial Institution or any branch thereof. Notice to the Bar Counsel shall be sent by certified mail to the Virginia State Bar, Attention: Bar Counsel, 707 E. Main Street, Suite 1500, Richmond, Virginia 23219? 2800. This agreement may also be canceled without prior notice by Bar Counsel of the Virginia State Bar if the financial institution fails to abide by the terms of the agreement.

**9. Binding Effect.** This Agreement shall be binding upon the Financial Institution and any branch thereof receiving Trust Accounts.

**10. Definition.** For purposes of this agreement the following definitions will apply:

- a. "Notice of Dishonor" refers to the notice which, pursuant to Uniform Commercial Code Section 3-508(2), must be given by a drawee bank before its midnight deadline.
- b. "Insufficient funds" refers to a state of affairs in which there is an insufficient collected balance in an account as reflected in the financial institution's accounting records, so that an otherwise properly payable item presented for payment cannot be paid without creating an overdraft in the account.
- c. "Dishonored" shall refer to instruments that have been dishonored because of insufficient funds as defined above.
- d. "Negative Netting" refers to the practice of a financial institution

collecting some part or all of the fees assessed during a stated period of time against any IOLTA account that has failed to generate enough interest to pay assessed fees from the positive interest generated by other IOLTA accounts and deducting those fees from the total interest remitted to the Legal Services Corporation of Virginia for that time period.

IN WITNESS WHEREOF, the Financial Institution has executed this Agreement on the date and year written above.

ATTEST:

\_\_\_\_\_  
Name of Financial Institution

\_\_\_\_\_  
Address of Financial Institution

\_\_\_\_\_  
By \_\_\_\_\_  
Officer's Name  
(Please print)

\_\_\_\_\_  
Officer's Signature

\_\_\_\_\_  
Corporate Office Held



**APPENDIX 3: ESCROW ACCOUNT RECORD-KEEPING AND ACCOUNTING FORMS**

Adapted from David Ross Rosenfeld and Michael J. Rost,  
*Lawyer Trust and Fiduciary Accounts: Canon 9 and IOLTA*,  
*Virginia Lawyer*, 9-12, September 1993

**CASH DISBURSEMENTS JOURNAL**

(Checkbook)

<p style="text-align: right;">_____ <b>20</b> _____</p> <p><b>TO:</b> _____</p>	
<b>FOR:</b> _____	<b>TOTAL</b>
	<b>THIS CHECK</b>
	<b>OTHER</b>
	<b>BALANCE</b>

**CASH RECEIPTS JOURNAL**

(Checkbook)

<b>DEPOSIT RECORD</b>		
<b>DATE</b>	<b>SOURCE</b>	<b>AMOUNT</b>
<b>TOTAL</b>		



APPENDIX 3

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PERIODIC TRIAL BALANCE

QUARTER ENDING DATE	CLIENT	BEGINNING QUARTER BALANCE	TOTAL QUARTER RECEIPTS	TOTAL QUARTER DISBURSED	QUARTER END BALANCE	ATTY. INITIALS/ DATE

**Quarterly Reconciliation**

<b><u>PERIODIC RECONCILIATION</u></b> FOR ESCROW ACCOUNT # _____ QUARTER Beginning _____ & Ending _____	
CLIENT	SUBSIDIARY LEDGER BALANCE
<b>TOTAL</b>	
CHECKBOOK BALANCE AT END OF QUARTER	
ATTORNEY INITIALS/DATE	



#### APPENDIX 4: SUMMARIES OF CITED LEGAL ETHICS OPINIONS

- | LEO#  | Summary of Opinion  |
|-------|---|
| 183   | The Committee considered the question of when an attorney may ethically disburse loan proceeds deposited to that attorney's trust account incident to a residential real estate settlement. Mindful of the fact that some funds wired by lenders to an attorney's trust account are drawn on out-of-state banks, the Committee determined nonetheless that provided the form of the funds deposited was in accord with applicable provisions of the Wet Settlement Act, the attorney can disburse immediately upon receipt of the funds.  |
| 186-A | Reconsidering Formal Opinion 150, Bar Council determined in this formal opinion that an attorney's participation in a plan providing for the use of credit cards for the payment of legal fees was acceptable in "recognition and appreciation of economic reality." The Committee determined that advances against fees could be paid by credit card but must be deposited to trust if unearned. The Committee held further that where a client was financially unable to pay an attorney's fee, the availability of a credit card "should not deter the attorney from his obligation to perform pro bono work." |
| 186-B | In this formal opinion, Bar Council considered the imposition of finance charges on outstanding client accounts and held that an automatic imposition of a finance charge would be ethically impermissible. But in situations where an attorney and client agree that a finance charge may be applied, provided it is reasonable, it may be imposed with prior advance notice to the client.  |
| 188   | An attorney may conduct a real estate title search and procure title insurance for a client through an agency or company in which the attorney has an ownership interest. The Committee reviewed prior legal ethics opinions, applicable statutes, and DR 5-101(A) and concluded that   |

- such actions were not ethically impermissible, provided the client consents after full disclosure.
- 189 The use of contingent fee agreements in matrimonial matters is ethically impermissible except in “extremely rare” circumstances.
- 209 It is not improper for a seller’s attorney to receive a portion of the commission of his client’s real estate agent, provided the client consents after full disclosure.
- 214 It is improper for an attorney to refuse to provide his client with an itemized breakdown of fees and costs incurred by the client in connection with the representation.
- 280 It is improper for an attorney to receive the interest earned on a client’s funds held in trust or escrow.
- 281 It is improper for an attorney to pay realtors’ commissions at the time of settlement and prior to title bringdown and recording.
- 302 A partner in a real estate firm may represent the seller and/or purchaser in a legal capacity where the property has been sold by either the attorney or his real estate firm so long as the client consents after full disclosure.
- 330 An attorney representing a client who has been involuntarily committed who in the course of his representation receives a redeemable airline ticket due to shortly expire should redeem the ticket and place the proceeds in trust.
- 340 An attorney representing an estate may ethically purchase an estate asset, provided there is consent and full and complete disclosure to all interested parties.
- 365 It is impermissible for an attorney to include a provision in his personal injury contingent fee agreement which provides that the client’s refusal to accept a settlement offer will result in the attorney’s receiving a higher percentage of the recovery.



- 392 An attorney may not earn interest on funds held in trust.
- 405 An attorney may represent a client seeking payment of alimony on a contingent fee basis where the amount due has been outstanding for seven years and the client is otherwise indigent.
- 415 An attorney may ethically withdraw net settlement proceeds from his trust account, and place them in a separate interest-bearing account pending resolution of the issue, where those proceeds were drawn on the attorney's trust account by a check which, although honored by the seller's bank and deposited to the seller's account, was never presented to the attorney's bank for payment.
- 423 An attorney may not enter into a contingent fee arrangement with this matrimonial client.
- 425 A closing attorney employed by the purchaser may not impose a fee upon the seller, absent an agreement with the seller and the seller's attorney.
- 454 Referencing Formal Opinion 183, the Committee held that an attorney may immediately disburse certified funds from his trust account.
- 458 A legal aid office may not use funds from its trust account, deposited to cover costs for clients whom they cannot now locate. The legal aid society may, however, at the outset of a representation have clients sign a consent form authorizing the use of client funds as a donation to the office.
- 515 An attorney serving as trustee under a deed of trust in a foreclosure proceeding may charge a fee lower than the amount provided by statute.
- 545 An attorney may be a shareholder in a title insurance agency when the management of that agency is restricted to an organization in which one or more of the attorney/ shareholders has ownership control, and where agency shareholders receive agency profits as timely distributions

as opposed to direct commissions or payments tied to profits with respect to specific policies at closing transactions.

- 548 An attorney may retain funds left in an escrow account, provided the attorney follows the procedures outlined including auditing the account to make a good faith effort to determine the ownership of the funds, maintaining the funds in an interest-bearing account for a period of time sufficient to permit the attorney to conclude that no timely claim can be made upon the funds.
- 558 An attorney may participate in a barter system where referrals are made to him by an “exchange broker,” he receives a “credit” to his barter account for legal services provided, and a “debit” from that account when he “purchases” goods and services from other members. But it is improper for the broker to receive a commission on legal services whether in cash or kind, the attorney may not receive services in kind before his fees are earned, and legal fees whether paid in cash or kind must be reasonable. Any advertising of the barter arrangements must not be false or misleading.
- 569 An attorney may represent a spouse in either a contested or uncontested divorce where he previously represented the husband and wife in the purchase of their marital home, provided the attorney did not acquire confidences or secrets in the prior representation.
- 578 An attorney who assumed a note and guaranteed payment along with a husband and wife can sue the wife, following his purchase of the note and the husband’s bankruptcy filing, to enforce her obligations under the note.
- 582 An attorney may guarantee charges made by a physician for litigation-related activity so long as the attorney’s client remains responsible.
- 585 Earned fees and undisputed attorney fees belonging solely to the attorney may be deposited directly to the attorney’s operating or personal accounts.

- 588 An attorney may pursue child support arrearages on a contingent fee basis under the very specific set of facts outlined in the LEO.
- 591 It is not improper for attorneys to be a stockholders in a title insurance company where the attorneys receive dividends but no salaries or other compensation, and disclosure of the relationship between the attorneys and the agency is made to clients.
- 603 A law firm may process applications for title insurance through a title company in which the law firm has a “business interest,” even though the title company employees are paid by the law firm, space is charged between the firm and the agency, and the law firm serves as legal counsel to the title agency, provided the title insurance carrier and title applicants consent after full disclosure and the transactions are not unconscionable.
- 614 An attorney may not immediately disburse non-real estate settlement funds held in trust, and the failure to deposit those funds into trust is improper. A law firm may not deposit settlement proceeds to trust, then disburse to the client from the firm operating account the client’s share of those proceeds, subsequently reimbursing the operating account from trust to cover this disbursement.
- 638 A retainer agreement may include a provision for binding arbitration or nonbinding but admissible arbitration in the event of a dispute, provided the client consents after full disclosure, and after the client is advised to seek independent counsel in regard to the advisability of such a provision.
- 642 An attorney may charge interest to a client on fees earned but not yet paid, and costs advanced but not yet reimbursed, provided the interest is being charged pursuant to a prior agreement between the parties, the client is able to make the payments but desires to defer same for the client’s convenience, the interest rate does not violate the law, and the client has the right to prepay without penalty.

- 663 A real estate attorney may not disburse funds prior to title vesting in the buyer and before the establishment of a perfected lien position with respect to the lender.
- 667 A contingent fee in collection of child support arrearages is improper unless the children are or will soon attain majority, the attorney has satisfied himself that the arrangement will not undermine the non-custodial parent's parent-child relationship, the prospective client is indigent, and the fee arrangement is fair and reasonable under the circumstances.
- 681 An attorney has a duty to account to his client, upon request, for all or any part of a fee paid.
- 695 An attorney with his office in the District of Columbia who generates the majority of his clients from Virginia satisfies his Canon 9 obligations if he opens an attorney trust account with a Virginia bank that agrees to comply with DR9-103(B)(1).
- 697 It is not improper for the trust account of a deceased attorney to be turned over the attorney's estate where a diligent good faith review of the account is conducted to determine the ownership of the funds, and any funds that cannot be attributed to a client are held in an interest-bearing account for a period of time sufficient to insure that no successful claim could be made upon the funds within any applicable statute of limitations.
- 704 It is improper for an attorney and client to negotiate a settlement check at the payor bank and disburse the funds without first running the funds through the attorney's trust account. It would also be improper for the attorney and client to convert the funds to a cashier's check payable to the attorney and client and then immediately disburse the funds.
- 710 An attorney may charge a client a predetermined percentage of a legal fee as administrative costs in non-litigation matters, provided that the attorney explains fully to the client the method by which the fee is calculated and

- the client consents. In litigation cases, the client must pay the actual costs associated with the case file.
- 712 The findings in LEO 603 are reaffirmed in situations where a title agency is merely an agency of an independent title insurance company and not a title insurance company in and of itself.
- 724 A licensed DC attorney may ethically maintain his trust account for Virginia clients in a Virginia bank. An attorney may have a non-lawyer as signatory on his trust account, provided he maintains proper supervision and ultimate authority.
- 734 An attorney may endorse a check payable to his client pursuant to an irrevocable assignment and apply the proceeds to legal fees owed to the attorney. But the attorney must first send notice to the client's known address as well as provide an accounting showing the intended application of the proceeds.
- 753 An attorney may disburse funds pursuant to the terms of Wet Settlement Act.
- 778 An attorney may not collect child support arrearages pursuant to a contingent fee agreement where the child is 9, has recently visited with the non-custodial parent, and the client is not indigent.
- 813 DR 9-102 establishes what funds must go into escrow and the conditions under which those funds may be withdrawn. Drawing a factual distinction between LEO 663, the Committee determined that often the timing for disbursement of proceeds, and the circumstances under which that may be done, is often fact specific.
- 831 A law firm may not place a client's funds in an interest-bearing account that will result in the firm receiving an automatic administrative fee equal to 15 percent of the funds, even though the interest earned by the funds will be credited against an overhead fee charged by the firm to the client.

- 832 An attorney may dispose of funds held in his trust account for some time, belonging to clients with whom he has had no contact recently, pursuant to the provisions of section 55-210.1 of the Virginia Code.
- 850 Restating the requirements of LEO 667, the Committee applied the three factors enumerated there in approving a contingent fee contract for the collection of child support arrearages owed by the father of a partially retarded child.
- 878 Absent a prior agreement, the purchaser's real estate attorney may not charge the seller a fee for the release of deeds of trust.
- 886 An attorney who is a limited partner, stockholder, officer, or director of a title insurance company may purchase title policies for his purchaser clients where he conducts the closings, provided the attorney's interest in title company is disclosed.
- 898 An attorney may deposit a cashier's check payable to his firm into the firm trust account after the bank has closed and then immediately disburse the funds.
- 900 Noting that the passage of Senate Bill 536 may moot or revise this opinion, the Committee reminded attorneys of their obligations to comply with the terms of the Wet Settlement Act as the Act pertains to recordation of instruments, following the instructions of the lender, and disbursement of funds. Specifically, an attorney has a duty to comply with the Act and with the lawful instructions of the lender. Where the two conflict, the attorney must notify the lender that he must comply with the act and thereafter do so.
- 911 A buyer's attorney may charge a seller a reasonable fee for proper compliance with IRS Form 1099 requirements, provided the seller is advised in advance of the charge to be assessed and given the opportunity to avoid that charge. **NOTE:** this opinion was withdrawn by the Committee following passage of the Technical Corrections and

- Miscellaneous Reserve Act of 1988, which prohibits a separate charge for preparation of IRS Form 1099.
- 912 An attorney may charge a noteholder more than the 5% trustee's fee to foreclose, provided that the fee is reasonable and not passed on to the debtor.
- 922 A buyer's attorney may charge a seller a reasonable fee for release of deeds of trust and for compliance with IRS Form 1099 requirements, provided the seller is advised in advance of the charges to be assessed and given the opportunity to avoid those charges for what are basically ministerial duties. (See note on LEO 911, above.)
- 927 A buyer's attorney may charge a seller a reasonable fee for release of deeds of trust and for compliance with IRS Form 1099 requirements, provided the seller is advised in advance of the charges to be assessed and given the opportunity to avoid those charges for what are basically ministerial duties. (See note on LEO 911, above.)
- 946 It is not per se improper for an attorney to refer client accounts payable to a collection agency, provided the client's secrets and confidences are protected.
- 972 A violation of applicable rules may have occurred where a law firm that filed suit against a client for fees owed, which amount was paid in full by the client prior to the court date, obtained judgment against that client nonetheless, failing to inform the tribunal of the payment.
- 974 A lawyer represented a client in a divorce case. The client failed to pay the attorney's fees and ceased communication with the attorney. The attorney's motion to withdraw was denied since the client could not be served with notice of the motion. During the course of the case, an issue was appealed to the Supreme Court for which a writ was subsequently granted. The attorney may move to withdraw, but if he is not permitted to do so, he cannot fail to prosecute the appeal based upon the client's refusal to communicate with him or pay his fees. If a gross imposition is placed upon the attorney due to the client's failure to pay

- fees owed, and the attorney is granted leave to withdraw, the attorney may file suit against the client during the pendency of the appeal.
- 994 The Committee determined that an attorney who qualified as administrator for a deceased attorney's estate one year previously, and who has complied with applicable statutory publication requirements, may distribute the funds to the attorney's heirs.
- 995 An attorney was fired by his army officer client in a divorce proceeding at a time when the attorney was owed \$8,000 in fees. The client had previously agreed to pay \$250 per month but reduced his payment to \$100 per month after the attorney was fired. The Committee determined that the attorney could file suit against the client, but could not advise his commanding officer of the situation as this would violate DR 4-101.
- 996 An attorney successfully represented a client in a contract dispute which went to trial. At the conclusion of the trial, \$2,500 was collected from the defendant, and the attorney was owed over \$3,000. The Committee opined that the attorney could place a lien on the funds held in trust, provided the client owed the firm money for fees. The Committee noted further that although DR 9-102(B)(1) requires that an attorney promptly notify his client of funds received on his behalf, that does not necessarily require disbursement of those funds to the client.
- 997 Distinguishing LEO 485, the Committee determined that it is not improper for an attorney to advance the costs of litigation in a death penalty case on behalf of an indigent client where there is no hope or expectation that the attorney will ever be repaid.
- 999 A law firm that accepts credit cards may have all funds collected by the credit card company deposited to trust, even though some of those funds may be earned fees, provided that funds belonging to the law firm are promptly withdrawn to the firm's operating account.



- 1016 An attorney and a bookkeeper may form a business offering billing services to law firms, provided only information necessary for collection is provided and client confidences and secrets are protected, and provided that the attorney's work for other law firms will not compromise his independent judgment on behalf of his own clients.
- 1021 Even where an attorney has an arrangement with his bank whereby the bank either honors all trust checks presented or where the bank permits immediate credit of deposited funds without waiting for clearance, the attorney may not immediately disburse non-certified settlement proceeds.
- 1027 An attorney may represent the legal affairs of a business in which he has a personal or financial interest, provided he can do so without compromising his professional judgment and provided the client consents after full disclosure.
- 1056 A firm may ethically charge a pre-set overhead charge in non-litigation matters, provided the client consents after full disclosure. In non-litigation matters, the client must pay the actual expenses associated with the case file, and in contingent fee cases, the client must remain ultimately responsible for costs incurred.
- 1060 In a personal injury case, a law firm may advance expenses for medical records to his client's doctor, provided the client remains ultimately responsible for those costs.
- 1062 Under the facts set forth in this LEO, the Committee determined that an attorney may enter into a contingent fee contract with his client seeking to obtain a valuable marital asset not contemplated by the parties' PSA. In this case, the parties were divorced and had no children, and the client was not able to pay a reasonable hourly rate.
- 1072 Noting that LEO 187 explicitly overruled LEO 174-A, the Committee opined that there is no per se prohibition against an attorney obtaining title insurance policies for clients where the attorney has an ownership interest in the title company.

- 1083 It is not improper for a law firm to form and invest in a non-legal subsidiary business. Under the facts presented, the subsidiary business would be run by non-lawyers, the law firm would act as counsel to the subsidiary, and both entities would refer clients to each other, while not “steering” clients. The Committee expressed reservations regarding the potential for conflicts of interest and the unauthorized practice of law.
- 1089 In the absence of client consent, it would be improper for a law firm to represent itself in a collection suit against a former client. Under the facts of the LEO, a law firm conducted a closing, neglected to include a credit to the buyer on the HUD-1, which the seller admitted should have been given but refused to pay. The law firm paid the buyer, and was cautioned to hire outside counsel to pursue the seller.
- 1116 It is improper for an attorney to disburse a builder’s proceeds and builder’s construction loan payoff prior to recordation of the lender’s deed of trust, even where the builder and the lender have authorized the attorney to do so.
- 1132 Overruling LEO 431, the Committee determined that even upon discharge by his client, a lawyer must take reasonable steps for the continued protection of his client’s interests.
- 1148 A buyer’s attorney may not charge a seller fees absent a prior agreement to which the seller consents.
- 1152 Considering again the issue of attorney owned title agencies, the Committee restated its position that an attorney may issue title policies to his clients through a title agency in which he holds an ownership interest, provided there is full and adequate disclosure and client consent.
- 1155 A personal injury attorney may attempt to persuade a finance company to offer loans to his clients to help them pay for costs of living, which would be repaid from the proceeds of any settlement of the case. The finance company may conduct an independent investigation of the

facts of the case to assess the risks of making the loan and any information obtained that the attorney did not already have would be provided at no cost to the attorney. The attorney may not act as a guarantor of the loan.

- 1163 An attorney who is also a certified public accountant may represent clients for whom he also prepares tax returns and performs other accounting services, including auditing the clients' accounts, provided that he discloses his dual role to his clients, discloses his own business interests, and the client consents.
- 1170 A law firm that also owns a title company refers its law firm clients to the title company for settlement services and deposits funds of law firm clients in interest-bearing accounts. The interest earned on those accounts is retained by the law firm, not accounted for to the client, and at settlement the clients were required to sign an authorization disclosing the fact that the funds would earn interest which would then be credited to the firm. Under these facts, the Committee determined that the firm may not earn interest on funds held by clients of the firm which have been steered to the lay title company in which the attorneys have ownership interests, but no such restriction applies to clients of the title company who are not also clients of the firm. The Committee stated further that where an attorney offers his client the choice of other title companies in which he does not have an ownership interest, this restriction would not apply. The Committee cautioned, however, that since the attorney and client have differing business interests, full disclosure must be made of the conflict and client consent obtained.
- 1177 A law firm conducting settlement services on behalf of purchasers, where the sellers are represented by their own attorney, may not charge the seller legal fees for services performed incident to the closing absent a prior disclosure of the fees which will be charged and the agreement of the seller to pay those fees. *See also* LEO's 647, 878, and 911.
- 1178 The Committee stated the differences between "advance legal fees" and a "retainer" finding that an advance of legal

fees remains the property of the client until earned by the attorney and thus must be maintained in trust. A retainer, on the other hand, is paid periodically to the firm to ensure its availability, and unavailability to other potential clients, and is the property of the firm upon receipt. The Committee was also asked to address whether the interest earned on an advance legal fee may be maintained by the law firm. Relying upon LEO 650, the Committee stated that interest may only be earned on client escrow funds under the circumstances set forth in LEO 650 and in any case does not become the property of the attorney under any circumstances.

- 1182 An attorney may enter into a contractual agreement with a personal injury client's healthcare provider guaranteeing payment of that provider's fees from any recovery, provided the client remains ultimately responsible. In circumstances where the provider wishes the attorney to guarantee payment of his costs from any recovery, the attorney may do so, provided the client executes a release or consent form authorizing the attorney to pay the provider regardless of any subsequent dispute that may arise between the client and the provider. In no case may an attorney agree to pay a witness a contingent fee.
- 1187 Where a law firm receives proceeds on behalf of a client for a case where the client owes the firm fees arising out of an earlier representation, the firm may deduct from the funds held fees owed for the earlier representation, provided the client does not dispute the fees owed and has been properly invoiced for them. The Committee noted that the attorney should send to the client's last known address a notice and an accounting of the receipt of the check and the intended application of the proceeds toward the client's financial obligation to the attorney.
- 1188 In a divorce case where an attorney had previously agreed to accept \$1,500 as his total fee, the attorney may not thereafter accept a higher fee proposed by his client's estranged spouse for the purpose of equalizing the fees each would have to pay to their attorneys. An attorney's fee must be reasonable and adequately explained to the client and,

absent client consent after full disclosure, this increased fee cannot be assessed.

- 1198 An attorney wishes to become a limited partner in a court reporting business which would offer services to his clients at a rate considerably less than current market rates. The attorney wishes to offer these services to his client and to other attorneys. The Committee determined that the attorney could do so, provided he obtained his client's consent after full and adequate disclosure, which could include information concerning commissions or fees the attorney would earn due to the client's employment of the court reporting service. The Committee also cautioned that any doubts about the sufficiency of any disclosure would be resolved in the client's favor.
- 1204 Where a purchaser is represented by his own counsel incident to a closing, the seller's attorney who is also the settlement agent may not impose a settlement fee upon the purchaser absent the purchaser's prior agreement to the fee.
- 1219 A law firm wishes to have one of its wealthy clients advance loans for living expenses to personal injury clients, securing those loans with a promissory note providing for 15% interest and making repayment contingent upon the client receiving a settlement. In cases where no settlement was obtained, the lender-client would absorb the loss, and the law firm would have no repayment responsibility to the lender client. The Committee opined that this arrangement was violative of DR5-105(B) and (C) in that the attorneys could not adequately represent the interests of these multiple clients. The Committee discussed the possibility of the arrangement violating the statutory prohibitions against champerty and maintenance but did not reach these legal issues.
- 1220 Closing attorneys must accurately record on the settlement statement all fees and costs associated with the closing including attorney fees. Including the settlement attorney's fee for title searches in the title insurance premium is not ethically permissible.

- 1228 The Committee again considered the propriety of a purchaser's attorney charging a fee to a seller for the performance of certain acts incident to a closing, including the preparation of documents and release of liens, absent the prior agreement of the seller. The Committee withdrew LEO 911 in light of passage of the Technical Corrections and Miscellaneous Reserve Act of 1988, which prohibits a charge for preparation of IRS Form 1099.
- 1237 An attorney advanced the expenses of litigation in a medical malpractice suit on behalf of a widow who agreed to be responsible for those costs. The day before the panel hearing the widow instructed the attorney not to proceed. One bill remained outstanding, and the widow refused to pay. In order to protect his credit, the attorney paid the invoice and wishes to know if he must pursue his client to collect the amounts paid. The Committee opined that an attorney does not have an affirmative obligation to file suit against his client to recoup costs advanced if the attorney has reason to believe that the suit will be fruitless. But a consistent policy of not pursuing clients under these circumstances would be improper.
- 1238 A law firm that mainly represents DC clients but also has an office in Virginia must segregate retainer funds paid by Virginia clients from the firm's DC clients since retainers become the property of the attorney upon payment in DC. Any interest earned on retainers paid by Virginia clients must be treated in accordance with applicable disciplinary rules.
- 1246 A law firm was consulted by a client who paid the firm \$500 that the firm deposited to escrow. After reviewing the file, the client decided that he did not wish to proceed in the manner in which the firm recommended and terminated the engagement. Due to the brevity of the relationship, no written fee agreement was prepared. The firm takes the position that the \$500 is now earned as it was paid to the firm for investigation of the case. The client wishes the money refunded. The Committee concluded that the funds must be maintained in escrow until the dispute is resolved by appropriate legal means.

- 1247 A law firm wishes to include in its fee agreements a provision stating that interest will be charged automatically on balances due after the thirty day billing cycle. The Committee referred back to LEO Formal Opinion 186-B wherein Council determined that the automatic imposition of interest is improper. The Committee noted the circumstances under which interest may be imposed, including where the fee is otherwise reasonable and the client has the ability to pay, and provided the client is entitled to prepayment in full without penalty.
- 1248 A law firm wishes to disburse settlement proceeds to a client after receiving those proceeds but before the hold period has elapsed. The Committee determined that since DR 9-102(B)(4) requires that an attorney release funds or securities being held by him to persons legally entitled to receive them, unless the hold period has elapsed, the client is not yet legally entitled to the funds.
- 1254 A group of criminal defense attorneys may ethically invest in a bail bond business in which non-lawyers will manage the daily business of the company and in which the attorneys will not serve as officers or directors, provided the attorneys disclose their ownership interest to any clients they refer to the bail bond business. The attorneys may also represent the legal interests of the bail bond business, but may not do so if it is contrary to the interests of any of their criminal defense clients.
- 1255 A law firm may honor the request of a lender to waive all future certified funds received incident to closings conducted by the firm, provided the lender is notified that settlement proceeds must be in a form authorized by the Wet Settlement Act. The Committee reminded the firm of an attorney's duty not to disburse escrowed funds to a person not entitled or not yet entitled to receive funds held in escrow.
- 1256 A law firm may not obtain a line of credit from a bank to a cover personal injury settlement proceeds that have not yet cleared the firm's trust account where that line of credit would be used to advance to the client their settlement

proceeds. The firm would be improperly acquiring an interest in the outcome of the litigation, and could conceivably commingle funds in the firm trust account where the line of credit is used to cover an insurance company check that is returned for insufficient funds.

- 1262 A law firm has several escrow accounts that are held for the benefit of investment partnerships and into which funds are paid for the benefit of the investment partners, one of whom is an attorney. The committee opined that, once funds paid into the account for the benefit of the attorney, they must be drawn out so as to avoid improper commingling. The Committee noted further, in combining LEO 1263, that since there is no self reporting requirement under DR 1-103, the duty to report commingling or misappropriation arises where the attorney reasonably believes that the commingling reflects adversely upon another attorney's fitness to practice law. Where the violation has been rectified, the attorney must still make this determination.
- 1263 See the discussion of LEO 1262, above.
- 1265 An attorney may not invest client escrow funds in overnight repurchase agreements that are 100% collateralized by the U.S. Government and Agency Securities but are not "insured" by the FDIC. The Committee determined that the proposed investment vehicle is not a "bank" as defined under DR9-102(A) and (C) and violates the insurance requirements of those rules.
- 1269 This inquiry involved two scenarios, the first in which a lawyer wishes to learn of the propriety of a third party making loans to his personal injury clients. The Committee referred the attorney to LEO 1155 as dispositive of his inquiry. The second inquiry involved the attorney himself making loans to his clients, loans that the Committee determined are impermissible since the attorney would be gaining a financial interest in the litigation.
- 1277 Attorney A advertises a foreclosure sale as substitute trustee under a deed of trust and includes in the ad the



requirement that the purchaser pay certain costs and fees associated with the foreclosure. The successful purchaser retains counsel and is nonetheless charged a settlement fee and fee for a title search by Attorney A. The Committee determined that the ad of the foreclosure sale was sufficient notice to the purchaser of the fees and costs he would be expected to pay regardless of his retention of his own attorney.

- 1311 An attorney engaged in litigation involving insurance companies wishes to become a licensed insurance agent and sell insurance to law firms against whom the attorney's firm litigates cases. The lawyer also inquired about the propriety of him representing clients against firms to whom he has sold insurance products. The Committee determined that these arrangements would not be impermissible, provided the client consents after full disclosure.
- 1318 An attorney runs a law business in conjunction with his law practice and offers both services to his clients, billing them for both services, which are delineated as "legal fees" and "consulting services" on the bill. The client then pays the law firm one check for both services. The Committee determined that this arrangement is permissible, provided the client consents after full disclosure, and provided that the funds are first deposited to the firm's trust account and timely disbursed to the consulting service.
- 1325 An attorney represented a foreign corporation in a South American country where the rules applicable to representations treat lawyers as the commercial representative of the company with the powers and liabilities of a member of the Board of Directors. Such a representative may represent the company in legal actions, need not be an attorney, and does not need the authority of a tribunal to withdraw from representation. The company failed to pay fees and wrote a defamatory letter to the foreign government that put the attorney at risk of personal danger. Under the circumstances, the Committee opined that the attorney may withdraw without leave to do so since the applicable rules in the county in which he is practicing permit him to do so. The Committee also

specifically adopted the conclusions reached in ABA Formal Opinion 336 to the extent that DR1-102(A)(4) embraces conduct beyond that limited to an attorney's actions as an attorney and includes his actions as a fiduciary. Should an attorney violate his fiduciary duties to a client, he can be disciplined even where the relationship is not one of attorney-client.

- 1372 An attorney need not maintain a trust account where his practice is such that he does not receive client funds.
- 1379 Referring to LEO 1155, the Committee restated its position that an attorney may persuade a finance company to loan money to his personal injury clients and guarantee repayment from the settlement proceeds, provided the attorney does not guarantee or co-sign the loan. The Committee then went further, finding that the attorney may receive the loan documents from the finance company, have his client execute those documents in his office and then return those documents to the finance company, since the attorney is undertaking no contractual obligations to the finance company.
- 1405 Referencing section 38.2-4614 of the Virginia Code and an Attorney General opinion issued January 15, 1982, the Committee also determined that the payment by an attorney-owned title company of law firm salaries, and payments to the law firm for advertising, goods and services, would violate DR 5-101(A) and 5-106(A)(2).
- 1417 Attorney A is a director and stockholder in a bank (that he also represents in legal matters) into which he routinely deposits client funds including those in excess of \$100,000. The Committee determined that the applicable rules only require that the bank be insured by the FDIC and do not require that all clients funds be insured. The Committee held further that the attorney's interest in the bank is such that it must be disclosed to his clients who must then consent to the deposit of their funds with that bank. Finally, the Committee held that if the attorney became aware of the bank's status becoming precarious, his duty to

his clients would prevent deposit of their funds there without specific authorization from the client to do so.

- 1441 An attorney wished to make loans to a finance company that routinely made loans to his personal injury clients. The attorney's funds would not be used to make loans to his client, nor would repayment of those funds be tied in any way to resolution of the attorney's cases. The Committee determined nevertheless that the arrangement amounted to the attorney advancing funds to his clients and acquiring a financial interest in their cases, albeit indirectly, and was thus impermissible.
- 1442 An attorney may not charge a non-client a legal fee for preparation of documents without first informing the non-client that the fee will be imposed. Further, an attorney may not refuse to record release documents pending payment of his fee as this unduly prejudices his client and amounts to an intentional failure to complete the tasks for which he was retained.
- 1461 An attorney may not charge a contingent fee for the collection of med pay payments as this task is ministerial in nature and the fee would thus be per se unreasonable.
- 1466 An attorney representing a purchaser will "close" a transaction in which the seller is represented by separate counsel, hold and then disburse the funds to the seller's counsel. The Committee opined that the funds must still be in a form authorized by the Wet Settlement Act. The Committee stated further that any charge to seller must be disclosed and agreed to prior to the closing in order to be properly assessed.
- 1469 An attorney opens a title company the sole business of which is to conduct residential real estate settlements and all legal work is referred to outside counsel, with the exception of the preparation of deeds and notes. Interest is earned on funds deposited to the title company escrow account that is retained by the title company and not accounted for to clients. The Committee determined that the preparation of notes and deeds by the attorney created

an attorney-client relationship between the attorney and the title company clients such that the funds must be treated in accordance with DR 9-102.

- 1489 It is not per se improper for an attorney to accept a loan from a client during the pendency of litigation so long as there is full and adequate disclosure and the arrangement is not unconscionable. All doubts will be resolved in the client's favor. As to what constitutes full and adequate disclosure, the Committee referred to LEOs 187, 1097, 1198, and 1254. In this case, the Committee opined further that if the attorney applied payments on the loan against legal fees owed without prior disclosure of his intention to do so since he is obligated to notify his client promptly of his receipt of funds on the client's behalf, maintain a complete record of those funds, and render an appropriate accounting to clients regarding those funds.
- 1510 An attorney may deposit his own funds into his trust account sufficient to cover two years worth of bank charges for maintaining that account.
- 1515 Addressing a wide ranging series of questions concerning an attorney's obligations when serving as personal representative or trustee on behalf of a testator client, the Committee first considered the question of whether or not an attorney who drafts documents in which he is named executor or trustee must have a pre-existing attorney-client relationship in order to appropriately do so. Finding that a pre-existing relationship is not necessary, the Committee nevertheless noted that under those circumstances the possibility of overreaching or undue influence are lessened. The Committee also noted that while the rules do not preclude in-person solicitation per se, there are circumstances in which it is prohibited and an attorney should be mindful of those circumstances.

The Committee next considered the question of what disclosure need be made, if any, of the attorney's fees that will be charged when the attorney is named to serve as executor or trustee and if such a disclosure is required, when it must be made. The Committee opined that the

attorney's fees should be disclosed to the testator prior to the execution of the document naming the attorney as fiduciary, preferably in writing either in the document itself or in a separate writing. The Committee noted further its opinion that the attorney should suggest that the testator investigate fees that would be charged by others for the same service.

The Committee next considered the question of whether the attorney/executor may retain the services of his law firm to perform legal services for the testator and if so, whether that should be disclosed and, if so, when. The Committee opined that the disclosure is required and should be made prior to the execution of the relevant documents. The Committee also noted that the retention of the attorney's law firm places the attorney's own business interests at odds with the interests of his client. As such, full disclosure of this conflict must be made to the testator.

The Committee next considered the issue of fiduciary competence. Concluding that the standards for competence of Virginia attorneys is a question of law and thus beyond the Committee's purview, the Committee nevertheless makes reference to ABA Formal Opinion 336 and LEO 1325 which provide that an attorney acting as fiduciary who violates his duty such that he could have been disciplined had the relationship been one of attorney-client can be disciplined.

Finally, the Committee addressed the question of whether an attorney may make suggestions to his client as to appropriate fiduciaries. The Committee determined that an attorney may properly suggest professional fiduciaries such as banking institutions and is not prohibited from suggesting that the testator name the attorney but must be mindful of undue influence and overreaching, taking into consideration the testator's health and state of mind, sophistication, and the circumstances of the solicitation. The Committee concluded that these factors apply whether the document names the attorney as fiduciary or directs the fiduciary to employ the attorney for legal services.

- 1534 An attorney who prepared a will and trust for her non-blood relative godmother in which she and her sister were named as ultimate beneficiaries violated DR 5-104(B). It was not per se improper for the attorney to both draft the documents and be named as executor/trustee, provided the client consented after full disclosure.
- 1550 An attorney who failed to file his client's personal injury case within the applicable statute of limitations may ethically have his client sign a release in consideration for payment by the attorney of funds to the client, provided there is full and adequate disclosure, the client is first advised to seek independent counsel, and provided the transaction is not unconscionable.
- 1562 The Committee considered the obligation of a Fee Arbitration Committee to report an attorney to the ethical authorities and determined that an attorney's agreement in and of itself to submit to fee arbitration is not sufficient to impose a reporting requirement upon the Fee Arbitration Committee members, nor would the attorney's refusal to submit to arbitration trigger such a requirement. But if any member of the Fee Arbitration Committee concluded, to a reasonable degree of certainty, that a disciplinary rule violation has occurred that reflects adversely on the lawyer's honesty, trustworthiness, or fitness to practice in other respects, then a report is mandated under DR 1-103(A). The Committee held finally that, where an attorney's fees are not adequately explained to a client prior to the a fee arbitration, an explanation provided at that arbitration will not satisfy the requirement of DR 2-105 that an attorney's fees be explained to the client.
- 1564 This compendium opinion sets forth the ethical requirements of an attorney associated with or having an ownership interest in a title insurance agency. This Opinion reviews all earlier opinions and, to the extent any earlier opinions conflict with the findings herein, they were expressly overruled.

The Committee considered four specific issues, the first of which was the attorney ownership of title insurance

agencies. Under these circumstances, the Committee determined that the attorney's law firm must maintain separate office space, signage, and telephone listings, and must be careful to maintain separate and secure client files, especially in those situations where the attorney and the title agency employ overlapping staff. The Committee cited to RESPA and section 38.2-4614 of the Virginia Code, which prohibit kickbacks, specifically noting that the attorney's ownership interest does not constitute a violation of these provisions in and of itself.

The Committee next considered the issue of attorney compensation by the title agency finding that it is per se improper for an attorney to be compensated by a title insurance agency in which he has an ownership or other financial interest in a manner directly tied to the volume of business or number of referrals the attorney generates. The Committee stated further that the attorney may not receive a fixed salary from the agency unless it is substantially related to services rendered. Thus, the attorney is permitted to receive compensation in the form of periodic dividends on stock or similar distributions due to his ownership interest, legitimate fees based upon services rendered, or reimbursement of reasonable expenses actually incurred.

Indirect remuneration from interest earned on escrow accounts is improper where the attorney has steered the client to the title agency, as are payment by the title agency of law firm salaries and goods, services, and advertisements rendered to the law firm.

The Committee determined next that an attorney who holds a license as a settlement agency for the title insurance agency may not represent parties to the settlement transaction. This conflict does not exist under six specific circumstances enumerated in the Opinion.

Finally, the Committee cautioned that full and adequate disclosure to the client must be made of a potential conflict of interest under certain circumstances set forth in the opinion.

1565 In this opinion, the Committee declined to opine as to the facts presented due to the fact that interpretations of law, specifically the Truth in Lending Act and the Wet Settlement Act, were required and thus were beyond the purview of the Committee.

1571 Attorney B worked with Attorney A as an independent contractor, going out on his own entirely and severing that relationship. B took a personal injury client with him and prior to a settlement demand being made requested that A submit an accounting of fees to which A believed he was entitled. Despite two written requests, A refused to do so. A also sought to enforce an employment contract between attorney B and Attorney A that provided that B pay A 70% of all attorneys fees generated on files opened while B was in A's employ. This requirement was at odds with the personal injury client's retainer agreement, which provided for a quantum meruit assessment.

The Committee determined that Attorney A had an obligation under DR 2-105 to provide an accounting of fees he claimed to be owed, and his refusal to do was improper. The Committee restated the situations under which attorney misconduct must be reported to the Bar, and cautioned against using a threat of such a report to gain advantage in a civil matter.

1577 An attorney wishes to set up a 900 number on which pre-recorded segments would be presented to callers seeking general advice about bankruptcy protection. There would be no in-person contact, general information only would be provided, and the callers would be directed to consult with an attorney at the end of the recorded message. The Committee determined that this was not improper, provided the message was clear that general information only would be provided and the message contained no false, fraudulent, or misleading material.

1581 The Committee determined that an attorney may ethically receive a commission from a company to whom he referred clients who hold commercial paper where that company will purchase that commercial paper. Naturally, full and



adequate disclosure is required, and the attorney may not provide the client with legal advice regarding the transaction.

- 1586 A law firm with offices in DC, Maryland, and Virginia may ethically include in its retainer agreements a mandatory fee arbitration requirement for fee disputes and require that the disputes be resolved before the DC Arbitration Board. Full and adequate disclosure must be given to the client of all possible consequences of submitting to fee arbitration, and the transaction must not be inequitable or unconscionable.
- 1591 The Committee again considered the circumstances under which an attorney may assert a common law possessory lien against funds held in escrow to pay for outstanding fees due to the attorney. The Committee restated the proposition that such a lien is not per se improper, provided the client is notified of the receipt of the escrow funds, an accounting of fees owed is provided, and any excess funds are delivered promptly to the client.
- 1595 A personal injury law firm may include in its fee agreements a provision requiring the payment of interest on costs advanced by the firm that are not reimbursed within thirty days, provided the costs and expenses are reasonable and adequately explained to the client. The Committee restated its earlier restrictions that any deferred payment be for the benefit of the client, the interest rate must be in accord with law, and the client must have the right to prepay in full without penalty.
- 1606 This compendium opinion discusses the propriety of fee arrangements. Citing *Heinzman v. Fine, Fine, Legum & Fine*, 217 Va. 958, 234 S.E.2d 282 (1977), the Committee first noted the peculiar nature of attorney-client contracts; the fee provisions contained therein do not and cannot exist in a vacuum and must adhere to the strict requirements of the rules. Any fee agreement provision will never be dispositive of whether or not a violation of the disciplinary rules has occurred, and fees must be reasonable, adequately

explained to the client, and an itemized breakdown of fees must be provided upon request.

The Committee noted that a client must at all times retain the absolute ability to terminate his attorney's services and even where the termination amounts to a breach of an employment contract, the attorney is only entitled to that portion of his fee actually earned and must refund any unearned portion of the fee to the client.

The Committee next considered retainers, restating its earlier definition of a retainer as a payment to ensure an attorney's future availability and/or unavailability to potential adverse parties in the future. These funds are the property of the attorney when received and may thus not be deposited into the attorney's trust account. This is distinct from an advance payment against fees that is not the property of the attorney until earned and must therefore be deposited to trust. The Committee accepted responsibility for the confusion surrounding the terms "retainer" and "advance" and to the extent earlier opinions used the terms incorrectly, those opinions were overruled.

The Committee restated its earlier position that fees may not be designated as "non-refundable" as this violated the disciplinary rules since it impinges upon the client's freedom to terminate the attorney, and if the client discharged the attorney before the fee was earned, the "non-refundable" fee would be per se unreasonable.

- 1617 Discussing an attorney's duties when acting as a fiduciary, the Committee restated its earlier position that an attorney acting as fiduciary nevertheless must comply with applicable disciplinary rules, including the duty to account, and an attorney's actions as fiduciary which would be punishable as disciplinary violations if an attorney-client relationship existed are within the reach of the disciplinary system. The Committee noted further that an attorney serving as a fiduciary under Title 26 discharges his ethical obligations by complying with that statute, and to whom an accounting must be rendered differs based upon the

- circumstances at hand. In any event, the duty of accounting may not be waived.
- 1620 A discharged personal injury attorney must provide an accounting of fees he claims to be owed. The Committee did not address the issue of when that accounting must be provided in an ongoing matter as it was determined to be a legal question.
- 1636 A Virginia law firm receives funds from Virginia clients, which funds are intended to be paid to a foreign law firm for costs incurred by the foreign firm. Under those circumstances, these costs advances must be placed into trust as the funds are not being paid to the firm to reimburse costs already advanced by the Virginia firm.
- 1641 The Committee considered again the propriety of a firm charging a client for the collection of med pay payments and held, again, that such a charge is improper. The facts of this inquiry included calling the fee an “administrative charge” but the Committee determined that such a charge was still not permissible.
- 1644 The Committee discussed the steps necessary to exercise due diligence in locating clients for whom trust funds are being held. The Committee restated its position that a reasonable administrative charge may be assessed and charged against the funds being held.
- 1645 An attorney is not required under applicable rules to provide an itemized accounting of fees owed to a third party who is responsible for payment of those fees but who is not the attorney’s client.
- 1647 Attorneys who are stockholders in a title insurance agency may ethically distribute stock based upon the title insurance premiums generated by each attorney, even where the attorney will therefore receive dividends based upon the volume of business he brought to the title insurance company. This arrangement is distinct from earlier situations deemed impermissible, provided there is no violation of state or federal law.

- 1648 A law firm may not charge a client an additional fee over and above the hourly rate disclosed to the client, referring to that fee as an administrative charge of “value billing,” where that additional amount is not disclosed to the client. Service fees may only be appropriately charged in non-litigation matters and the fee must be disclosed and adequately explained to the client. Masking attorney fees behind service or value fees amounts to a deceptive practice.
- 1653 The Committee considered two scenarios where an attorney wished to have a matrimonial client execute an assignment of proceeds directing that a settlement agent pay the attorney’s fee from the proceeds of the sale of the marital home. In both cases, a final decree had not yet been entered and on that basis the Committee determined that such an assignment improperly gave the attorney an interest in the outcome of the litigation since the all issues with respect to the marital home had not yet been conclusively adjudicated. The Committee noted further that the attorney must also obtain the client’s consent after an adequate full disclosure, the transaction is fair and reasonable, and the client is advised that he may seek independent counsel.
- 1658 A law firm engaged in representing management in employment matters wishes to form a company that would provide human resource counseling to firms. A partner in the firm would be president of the consulting company, the firms would have proximate but separate office space, would have similar corporate logos for marketing purposes, and would not share employees. Referrals would be made between the firms, but client confidentiality would be protected. The Committee determined that the law firm partner may have an ownership interest and serve as president and chairman of the board of the consulting company, provided full and adequate disclosure is given to clients. The Committee held further that the law firm and consulting company may use similar corporate logos and engage in joint marketing, provided the public is not misled or confused and the consulting companies logo makes clear that it does not provide legal services. The firms may share overhead expenses, provided there is a separation between

their signage and office spaces and care is taken to protect client confidences. Referrals between the firms is appropriate, provided full and adequate disclosure is provided to the client, and the law firm may represent the consulting company, provided adequate conflicts checks are conducted. The Committee concluded finally that law firm employees may work for the consulting company in a non-legal capacity but remain subject to the provisions of the Code of Professional Responsibility.

- 1664 In a wide ranging discussion of the requirements imposed upon attorneys to protect client confidences and secrets, specifically where an attorney believes his client file may have historical significance and the attorney wishes to turn it over to historians, the Committee nevertheless held that the attorney may not release the files absent client consent, or he must first ascertain whether the files contain client confidences or secrets. If so, the files may not be turned over. In the facts presented, an entity employed the attorney to represent various clients and an agreement was reached with that entity to maintain and archive those files.
- 1667 An attorney may not permissibly include in his fee agreements a clause providing for the automatic assessment of a \$500 collection fee in the event that he must resort to collection proceedings for outstanding fees. The Committee determined that this violates applicable disciplinary rules since an attorney's fee must be reasonable and adequately explained to the client. Under these circumstances, the collection fee could well exceed the amount due to the attorney and would thus be per se unreasonable. An attorney may include a provision for reasonable attorneys fees to be assessed in the event of collection proceedings.
- 1673 An attorney may use a reasonable amount of client monies held in trust to attempt to locate that client in order to return those funds. In the facts of this case, the attorney wished to hire a private investigator and the Committee held that this was not improper, provided the costs of the investigator did not exceed the amount held in trust, thereby defeating the purpose of the search.

- 1674 Reserved.
- 1691 The Committee found a violation of DR 1-102(A)(4) where an attorney received a referral from a legal aid society with the understanding that the attorney would represent the client on a pro bono basis but negotiated a fee agreement with the client and received a fee for the case.
- 1696 The Committee approved a contingent fee arrangement for the collection of med pay payments that the attorney sought to collect from the tortfeasor's insurance company with whom the client did not have a contractual relationship. In this case, the collection of med pay required application of the attorney's legal skills since the company twice denied the claim and the attorney was required to demonstrate to the insurance company its legal liability. The Committee specifically noted that this analysis does not apply to all med pay collection efforts from third party insurance companies.
- 1705 The Committee approved a conversion of a fee agreement from an hourly rate to a contingent fee in a litigation context where the client requested the change as the only practical way that the client could continue with the litigation, the outcome was not certain, and the attorney's consideration for making the conversion was delaying payment of his fee for nearly four years.
- 1707 Presenting a wide-ranging discussion of the propriety of including a binding fee arbitration provision in engagement contracts, the Committee concluded that such a provision is not per se improper. But citing to *Heinzman v. Fine, Fine, Legum & Fine*, 217 Va. 958, 234 S.E.2d 282 (1977) and authorities from other states, the Committee noted that attorney-client contracts cannot be evaluated in the same manner as other commercial contracts due to the unique nature of the attorney-client relationship, and as such, care must be taken before including a fee arbitration provision to ensure that the client consents after full disclosure, that the disclosure is adequate, and that the client has been given the opportunity to consult with independent counsel.

- 1739 Overruling prior opinions decided under DR 2-105(D), the Committee applied Rule of Professional Conduct 1.5(e), which permits an attorney to pay a referral fee to another attorney or firm and does not require that all attorneys assume responsibility to the client. The Committee noted the restrictions of Rule 1.5(e), specifically, that while these referral fees are now permitted in Virginia, the client must be informed and consent to the participation of all attorneys involved, the terms of the division of the fee must be disclosed, the client must consent preferably in writing and always prior to the referral, and the total fee must be reasonable.
- 1744 The Committee determined that an attorney employee of a non-profit corporation that brings legal actions on behalf of clients, and a private attorney who assists with these cases, may turn over to the corporation court-ordered attorney fee awards. The Committee reasoned that the restrictions of Rule 5.4(a) did not apply since the corporation is not for profit, and the court determines the amount of the fee, and thus the client is not responsible for payment of the fee.
- 1747 The Committee determined that under Rule 1.15(c)(4), a lawyer may not disburse to his clients funds on which a third party has a valid lien or claim, even if the client directs him to do so. The attorney must hold the funds until the dispute between his client and the third party is resolved by appropriate processes.
- 1748 The Committee determined that an attorney may represent a criminal defendant in a civil forfeiture proceeding since (1) the proceeding is actually a civil forfeiture proceeding not a criminal proceeding; (2) it involves a res out of which a contingent fee could be paid; and (3) there exists an uncertainty as to the outcome of the legal matter.
- 1754 An estate attorney who is also a licensed insurance agent may receive a commission from the sale of life insurance products to his estate planning clients, provided the requirements of Rules 1.7 and 1.8 are met. Specifically, during the course of representing a party in estate planning where insurance related products are obtained from the

attorney and insurance agent, it would be improper for the attorney to engage in the representation without full and adequate disclosure to the client. Further, since the transaction will create a business relationship between the attorney and the client, Rule 1.8(a) requires that the transaction must be fair and reasonable and the terms fully disclosed to the client in writing. In addition, the client must be given a reasonable opportunity to seek advice of independent counsel and consent in writing to the transaction.

- 1760 Reserved.
- 1764 An attorney may not enter into an agreement with a finance company whereby his clients will agree to pay a fixed fee that they will then finance through the company at a fixed rate of interest. This arrangement amounts to an improper sharing of legal fees with a non-lawyer in violation of Rule 5.4 insofar as the finance company would pay the attorney a reduced amount, keeping a certain portion as a charge for its services.
- 1766 An attorney may enter into a “mixed” fee agreement with a client providing for both an hourly and contingent fee, provided that the fee ultimately paid is reasonable. The reasonableness of the fee must be viewed in light of application of the very specific factors set forth in Rule 1.5(a). In addition, For a contingent fee to be appropriate, there must be actual risk of nonpayment and a res from which the fee can be paid. LEO 1606.
- 1783 The committee considered the propriety of a foreclosure attorney remitting to his client-lender the excess of the fee paid by the borrower over the actual cost of the foreclosure services and found that this arrangement does not compromise the purpose of Rule 5.4(a). To that extent that prior Legal Ethics Opinions 534, 835, and 1025 are inconsistent with this conclusion, those opinions were overruled.
- 1797 A real estate settlement attorney uses a bank that freezes all funds in his trust account upon a deposit made after hours until such time as that deposit clears. The result of



this policy has been that the bank has bounced trust checks, although the funds were available to cover them. The Committee opined that the attorney may not use this bank with knowledge of this policy since to do so violates Rule 1.3(c) in that the attorney is taking action that prejudices his client, and Rule 8.4, which prohibits an attorney from engaging in deliberately wrongful behavior that occurs each time the attorney writes a check he knows will be “bounced” by the bank.

- 1807 The Committee considered whether or not it is an improper restriction on a client’s freedom to choose a lawyer (and discharge a lawyer) for a former attorney to garnish the advanced legal fees in a subsequent attorney’s trust account. The Committee decided this question in the negative, reasoning that since the new attorney has not yet earned the legal fees, he has no legal claim to them, he holds them only on behalf of the client, and they thus remain the client’s property. As such, the committee opined that it is not a per se violation for an attorney to garnish the funds of a former client that are in a new lawyer’s trust account.
- 1812 An attorney wished to include a provision in his personal injury contingent fee agreements that provided for an alternative hourly fee in the event that the attorney was discharged prior to the conclusion of the case. The Committee determined that when a client terminates a contingent fee agreement before the contemplated services are fully performed, and the fee agreement does not contain an alternative fee arrangement applicable upon early termination by the client, the discharged attorney is entitled to a fee based upon quantum meruit (the reasonable value of the attorney’s services up to the date of termination). *Heinzman v. Fine, Fine, Legum & Fine*, 217 Va. 958, 234 S.E.2d 282 (1977). But under the facts set forth herein, the committee opined that such alternative fee arrangements are permissible in contingent fee contracts so long as the alternative fee arrangements otherwise comply with the Rules of Professional Conduct, including the requirement that the alternative fee arrangement be adequately explained to the client (Rule 1.4 and 1.5(b)), be

reasonable (Rule 1.5(a)), and not unreasonably hamper the client's absolute right to discharge his lawyer, with or without cause, at any point in the representation (Rule 1.16).

- 1819 The Committee considered a situation where a lobbyist who was also an attorney contracted with Customer A to provide lobbying services to prevent Customer B from obtaining certain legislation. During the course of the relationship, however, A was led to believe that the lawyer's skills were one of the elements of governmental services to be provided by the firm, with the lawyer applying his legal knowledge and training to the facts of the situation. Subsequently, the firm informed A that B has now engaged the firm to provide it with governmental and public relations services, including lobbying on the exact same issue as the work done for A. The firm informed A that Rule 1.9 ("Conflict of Interest: Former Client") does not apply to the lawyer or the firm. Customer A has expressed concern about the lawyer's use of information acquired from A. The Committee determined that the question of whether the lawyer created an attorney-client relationship with Customer A, where the lawyer and A disagree on that point, will likely be resolved in the client's favor, and attorneys must be mindful of the higher standard to which their conduct is held.
- 1848 Having received an opinion from Virginia's Attorney General, the Bar approves Virginia lawyers passing along to their client the transactional costs/merchant fees charged by a credit card company when the client uses a credit card -- as long as the lawyer explains the process to the client before the client uses the credit card. Such transactional/service fees may be deducted from the lawyers' trust account, but lawyers using best practices should arrange for the fees to be deducted from the lawyers' operating account. Lawyers must "monitor and personally replace any escrow funds that are subject to a charge back" by a credit card company -- and lawyers using best practices should arrange for any charge backs to come from the lawyers' operating account rather than trust account.

## INDEX

American Bar Association	
Committee on Ethics and Professional Responsibility .....	45, 57
Model Code of Professional Responsibility .....	6
Model Record Keeping Rules .....	15, 25
Model Rules of Professional Conduct .....	6, 37
Standing Committee on Professional Liability .....	56
Business Relationships with Clients	
Activities and relationships	
Examples .....	27
Prohibited .....	29
Ancillary business activities .....	33
Assignment of proceeds .....	30
Conflicts of interest .....	32, 36, 38
Fiduciaries .....	37
Generally .....	26
Independent counsel .....	32
Loans .....	27, 30
Proceeds in lieu of fee .....	28
Proprietary interest in outcome .....	29
Publication or literary rights .....	31
Code of Professional Responsibility	
Generally .....	6
Conflicts of Interest	
Ancillary business relationships .....	36
Attorney as fiduciary .....	37
Disclosure of .....	32
Sale of title insurance .....	36
Disclosure of Conflicts .....	32, 36
Fees	
Agreements .....	48
Arbitration of disputes .....	51
Collection agencies .....	56
Contingent	
Criminal cases .....	43
Domestic cases .....	43
Fee agreements .....	43
Reverse .....	47
Criteria for setting .....	41
Division between attorneys .....	52
Excessive .....	41, 46
Fiduciaries .....	45
Files, ownership of .....	55
Finance charges .....	53

Fixed .....	48
Generally .....	40
Hourly .....	46, 48
Hybrid arrangements .....	47
Interest .....	53
Lien to secure.....	55
Malpractice claims.....	55, 56
Payment of	
Barter or payment in kind .....	53
Credit card.....	53
Percentage, fiduciaries.....	45
Quantum meruit.....	54
Restraints on .....	41
Retainers .....	19, 51
Suits to recover .....	56
Value-added.....	48
Withdrawal from trust account.....	19
Withdrawal or termination of attorney .....	54
Fiduciaries	
Business relationships with clients .....	26, 27
Client funds .....	7, 8, 10, 13
Compensation .....	45
Generally .....	37
Real estate.....	8
IOLTA account .....	11
Loans .....	24, 27, 30
Real Estate Settlement Agents (formerly CRESA).....	8, 10, 12, 16, 17
Real estate settlements (formerly Wet Settlement Act) .....	20, 21
Trust Accounts	
Accountability for.....	24
Accounting .....	13
Commingling funds .....	18
Conversion.....	22
Deposits .....	17
Disbursement .....	19
Disputes .....	19
Interest and investments .....	12
IOLTA .....	11
Joint funds .....	9
Loans .....	24
Missing clients.....	20
Out-of-state clients .....	8
Overdrafts .....	14
Padding of.....	17
Personal property.....	10
Real estate.....	7, 8, 16, 21
Record-keeping.....	13, 24

Retainers .....	17, See Fees
Third-party claims .....	24
Types permissible .....	11
Withdrawals .....	19
Virginia Rules of Professional Conduct	
Rule 1.5 .....	41, 43, 52
Rule 1.8 .....	27, 31, 35
Virginia State Bar	
Approval of financial institutions .....	14
Standing Committee on Legal Ethics .....	6