

Rules: 1.5, 1.15, 1.16

Subjects: Fees; client property; termination of representation

Summary: Lawyer may not deposit a flat fee directly into the operating account when it is possible that the entire fee may not be earned and must refund any unearned amounts upon termination of representation

Lawyer is engaged to defend a criminal case. Lawyer and Client have entered a written agreement charging a flat fee for providing representation through certain case milestones. Lawyer has asked if that money must be deposited into Lawyer's trust account or if it may be deposited directly into the operating account.

BACKGROUND

Lawyer is engaged to represent Client on a felony charge. They entered a written fee agreement providing that, for a flat fee of \$[REDACTED], Lawyer will "defend client until the charges are dismissed, through a jury trial, or through sentencing should client enter into a plea agreement or should client be found guilty at trial." The agreement further provides that Lawyer may deposit the fee directly into the office operating account rather than the trust account and designates the flat fee as Lawyer's property.

Lawyer does not send Client monthly bills or statements of work but keeps "diligent records" of the work performed. Lawyer states that this is done to demonstrate compliance with the factors of Rule 1.5(a), which are used to determine what constitutes a reasonable fee. Additionally, Lawyer states that financial stability is maintained so that, should Client terminate Lawyer's representation, Lawyer can refund "any unearned portion of the fee."

Lawyer now asks if the \$[REDACTED] can be deposited directly into an operating account or if it must be held in Lawyer's trust account. Lawyer poses this question against the backdrop of several identified rules. First, Lawyer recognizes the requirement that any fee must be reasonable according to the factors in Rule 1.5. Second, Lawyer recognizes that under Rule 1.16(d), should Client discharge Lawyer, it triggers a duty to refund any unearned portions of the fee. Lastly, Lawyer recognizes that under Rule 1.15 there is a duty to segregate disputed funds if discharge by Client occurs even if the original flat fee is deposited in Lawyer's operating account as a "non-refundable," "flat fee," "retainer," or other designation.

Although Lawyer has asked the specific question of whether the fee may be deposited directly into an operating account rather than a trust account, that question ultimately depends on several subordinate questions. The Committee restates the ultimate question as follows:

May Lawyer deposit directly into their operating account a non-refundable flat fee for a defending a criminal case through dismissal, trial, or sentencing?

ANALYSIS

To address Lawyer's question it is necessary to work, in order, through the questions of non-refundable fees, flat fees, refunding fees upon termination of a representation, and fee reasonableness. The answers to these subordinate questions lead to the ultimate answer of whether Lawyer may deposit the fee at issue here directly into the operating account.

1) "Non-refundable fees" are permissible only in limited circumstances

The first question turns on Lawyer's description of the \$[REDACTED] as a "non-refundable flat fee" for representation through dismissal, trial, or sentencing upon conviction. The written agreement between Lawyer and Client states this sum is Lawyer's property upon payment. Lawyer acknowledges, however, that if Client discharges Lawyer prior to one of these events, a refund may be required under Rule 1.16(d).

Although Lawyer has not specifically asked, it is necessary to consider if it is permissible to charge a non-refundable fee. Typically, it is not. It is not in the circumstances presented.

Unsurprisingly, this question has been considered in most jurisdictions. *See* Professional Responsibility in Criminal Defense Practice 3d, § 7:9.50. Many states explicitly bar charging a non-refundable fee. *Id*; *see e.g.*, Alaska Opinion 2009-1; Minn. RPC 1.5(b)(3). Other states do not bar non-refundable fees, but limit their scope and terms. *Id*; *see also Matter of Hirschfeld*, 960 P.2d 640 (Ariz. 1998). The fundamental limit on any "non-refundable" fee arrangement is that it may not preclude, explicitly or in effect, the ability of a client to discharge a lawyer. *See e.g.*, *In re Mance*, 980 A.2d 1196, 1204-05 (D.C. 2009); Georgia Op. 03-1. Many jurisdictions conclude that a flat fee is inevitably tied to completion of some task, act, or milestone in the representation such as drafting a document or completing a trial, and a fee is not "earned" until completion of that task. Absent such completion, some or all of the fee collected may be required to be refunded under Rule 1.16(d) if the lawyer is discharged. *See e.g.*, *In re Kendall*, 804 N.E.2d 1152 (Ind. 2004); *Iowa Supreme*

Court Bd. of Professional Ethics and Conduct v. Frerichs, 671 N.W.2d 470, 476 n.1 (Iowa 2003); *Matthew v. State Bar*, 781 P.2d 952 (Cal. 1989). Overall, almost 39 jurisdictions either explicitly bar, or only allow with significant limits, non-refundable fees while only four allow a truly non-refundable fee. See *Professional Responsibility in Criminal Defense Practice* 3d, § 7:9.50.

An exact picture of what jurisdictions allow is blurry because an important distinction exists between a “non-refundable fee” and a “retainer.” The former commonly refers to lump sums attributable to particular services, the latter a charge to guarantee a lawyer’s availability. See *e.g.*, Louisiana RPC 1.5(f) (2004) (fees paid to retain lawyer’s general availability become the property of lawyer upon payment); Texas Ethics Op. 611 (2011) (only fees reasonably necessary to obtain lawyer’s future availability may be made non-refundable). For this analysis, it is crucial to distinguish between a “general retainer” paid to ensure the lawyer will be available during a defined time period (regardless of whether work is actually undertaken) and a “specific retainer” which is paid to engage the lawyer on a specific representation. What may be made non-refundable is highly dependent on this distinction. See *e.g.*, *Iowa Supreme Court Bd. of Professional Ethics and Conduct v. Apland*, 577 N.W.2d 50, 54-55 (Iowa 1998).

Confusion is heightened by the common use of the term “retainer” to refer to advance payment of fees held in trust to be applied to future billings. See ABA/BNA Lawyer’s Manual on Professional Conduct, 41:2007, *citing* Ethics and Practice of Collecting a Fee Owed by a Client, 20 Fam. L. Forum, no. 1, at 3 (2011). A true “retainer” paid to ensure attorney availability or to confirm engagement is earned at the time of payment so may be non-refundable; advance payment of fees tied to particular work is not earned until the work is done and therefore must be refundable. *Apland*, 577 N.W.2d at 57-58.

The Committee has previously considered non-refundable fees. See South Dakota Ethics Opinion 2000-5; South Dakota Ethics Opinion 2000-5A. Our position was in line with the majority of districts: 1) flat fee agreements are not prohibited by the Rules; 2) any fee must be reasonable under Rule 1.5; 3) fees may not be strictly “non-refundable” regardless of the scope of work actually performed as it unduly infringes on the client’s freedom to select, or change, their lawyer; and 4) a non-refundable fee is distinct from a “retainer” paid to “ensure the lawyer’s availability.” *Id.*

In line with these ideas, the Committee holds that Lawyer cannot charge a “non-refundable fee” which is fully earned at the outset of the representation.

2) Flat fees are permissible

A second included question is the propriety of flat fees generally. Flat fees for particular services are not prohibited or even disfavored. South Dakota Ethics Opinion 2000-5A. A flat fee must be reasonable, however. *See e.g., In re Disciplinary Action Against Hoffman*, 834 N.W.2d 636, 644-45 (N.D. 2013). The facts in *Hoffman* are strikingly similar to Lawyer's situation (Lawyer called the case to the Committee's attention). The Committee agrees with the majority view that charging a flat fee for a criminal representation is permissible. *See e.g., In re Connelly*, 55 P.3d 756, 761-62 (Ariz. 2002). In this respect, the agreement between Lawyer and Client for a flat fee is acceptable.

3) Unearned fees must be refunded upon termination of representation and must be segregated pending any dispute about the fee amount

The next question that presents itself is what happens if Lawyer and Client end their relationship prior to completion of the work set out in their written agreement (dismissal, trial, or sentencing after conviction)? As Lawyer acknowledges, Rule 1.16(d) provides the answer: upon termination of representation, advance fee payments not earned must be refunded.

Hoffman held that it was unreasonable not to refund any portion of a flat fee when discharged by the client prior to dismissal, completion of the trial, or sentencing. *Hoffman* at 643, 647. So too here, Lawyer's agreement with client is a fee of \$[REDACTED] for representation through dismissal, trial, or sentencing upon conviction; if Client dismisses Lawyer prior to one of those benchmarks, the entire fee would not be "earned" and some portion would need to be refunded. *Id.* Indeed, Lawyer seems to recognize this, citing sufficient financial stability and liquidity to segregate funds in the amount of any disputed fee should the need arise. The Committee agrees with *Hoffman* that Lawyer would have an obligation to refund some portion of the fee if discharged prior to the case milestones stated in the fee agreement.

The Committee likewise agrees with the *Hoffman* court that if the need to refund some portion of the flat fee arises, Lawyer has an obligation to segregate the disputed fees until the dispute is resolved. *Id.* at 647; Rule 1.15. Lawyer again seems to acknowledge this obligation.

It is important to note that *Hoffman* required a refund of fees because the lawyer had not completed the scope of work identified in the written fee agreement. A different result may have followed with a different statement of work. For example, Lawyer could state other fee amounts for different units of work such as representation through a preliminary hearing, any suppression or

pretrial litigation, trial, sentencing, etc. An expanded statement of units of work, and corresponding flat fees, may ease the obligation to segregate funds if Lawyer is discharged or the full scope of work triggering the full fee is not completed.

4) Any fee must be reasonable for the work actually performed

Any fee must be reasonable for the work performed in the end. *Id* at 646. Lawyer has not asked Committee if the total fee is reasonable here. While it is not strictly necessary to resolve that issue to answer the question posed, it inevitably inserts itself in the discussion. *Id* at 647 (flat fee may constitute lawyer windfall if client terminates representation and all fees must be assessed for reasonableness). Reasonableness is always a fact specific determination so it becomes impossible to opine on every permutation of how the course of Lawyer's representation of Client may progress. At one end of the spectrum, the flat fee agreed to seems reasonable for representation through trial; at the other end, it is excessive if Client terminates Lawyer's representation early in the case. What fee is reasonable will inevitably depend on how much and what work is done and the other criteria of Rule 1.5.

5) Fees may not be directly deposited into an operating fund until they are earned without the prospect of refund

We have stated in our prior opinion that a fee arrangement "that would not, under any circumstances" allow for a reasonableness review under Rule 1.5 violates the Rules. South Dakota Ethics Opinion 2000-5A. Here, direct deposit of the full fee in Lawyer's operating account could frustrate repayment of unearned or unreasonable fees. It is therefore not a permissible arrangement under the collective operation of Rules 1.5, 1.15, and 1.16. The Committee concludes that lawyer may not deposit the full \$ [REDACTED] directly into Lawyer's operating account.

In reaching this conclusion, the Committee is persuaded by the reasoning of the Iowa Supreme Court in *Apland*. 577 N.W.2d at 55-56. This is the position of most to have addressed the question. See Lester Brickman, *Nonrefundable Retainers Revisited*, 72 N.C. L. Rev. 1, 41 (1993) citing Lester Brickman, *The Advance Fee Payment Dilemma: Should Payments Be Deposited to the Client Trust Account or to the General Office Account?*, 10 Cardozo L. Rev. 647, 650 n.20, 654 nn. 47-48 (1989). It is the position adopted in Colorado, one of the jurisdictions most tolerant of non-refundable fees. See *In re Sather*, 3 P.3d 403, 411 (Colo. 2000), opinion modified on denial of reh'g, (June 12, 2000). It is the position taken by the Committee here.

The Committee believes that this is a felicitous and harmonious reading of Rules 1.5, 1.15, and 1.16. Additionally, it is superior public policy: it shields client funds from creditors of a lawyer, prevents misappropriation by those lawyers less scrupulous than Lawyer in keeping adequate funds for refunds, and facilitates resolution of a fee dispute by having tracked and segregated funds. *Apland*, 577 N.W.2d at 56. The Committee is persuaded this is the preferable course.

However, it is not the position of all. *See* Professional Responsibility in Criminal Defense Practice, § 7:9, n. 6. While action in conformity with an opinion of the Committee is protected, it is difficult to say that action in conformity with the binding opinions of other jurisdictions is precluded. In short, this is not a situation where the Committee can opine with certainty that its opinion is the necessary course to avoid discipline. That authority lies elsewhere. *See* SDCL § 16-19-29.

CONCLUSION

Lawyer has asked if it is permissible to collect a non-refundable fee then deposited directly into Lawyer's operating account under the circumstances presented. We conclude that it is not.

This conclusion, while simple in the end, does rely on each step in the chain of reasoning. To the degree they are instructive to Lawyer and others, the Committee restates them explicitly:

- A) Flat fees are permissible under the terms and requirements in Rule 1.5.
- B) While a general retainer to guarantee attorney availability may be charged and deemed fully earned when it is charged, a totally non-refundable fee for services typically may not be.
- C) While a lawyer may require an advance fee "retainer" at the outset of the representation, and require replenishment or supplementation of that amount, a lawyer must refund any unearned portions of the fee upon termination of the representation under Rule 1.16(d).
- D) All fees must be reasonable under the criteria of Rule 1.5 and any fee arrangement must not preclude a reasonableness review of the fee.
- E) If a dispute occurs, funds equal to the total fee or amount in dispute must be held segregated from all other funds.
- F) Because a direct deposit of the entire fee into Lawyer's operating account in this case would frustrate achieving these purposes, the Committee concludes that the fee must initially be deposited into Lawyer's trust account to be drawn upon only as fees are earned.

As a final matter, while many of these principles are of general application, the Committee cautions that each fee agreement will likely be fact specific and lawyers should assess those situations individually.