



# WSBA

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### MEMO

To: Board of Governors  
From: Randy Beitel  
Acting Chief Disciplinary Counsel  
Date: July 10, 2007  
RE: ODC Alternative Rule Proposal Regarding Advance Fees

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One of the dilemmas of lawyer self regulation is that from time to time each of you as a Governor is faced with a conflict between your duty to lawyers as the leaders of their trade association and your duty to the public to regulate lawyers for the protection of the public. This is one of those times.

The issue before you is quite simple. Should a lawyer be allowed to spend the money before the lawyer has actually earned the money?

The premise underlying the majority proposal from the Trust Account Responsibilities and Retainers Task Force (TARRTF) is that this question should be answered in the affirmative. The chief trade association that has been lobbying this issue, the Washington Association of Criminal Defense Lawyers (WACDL), through its BOG and TARRTF representatives, have and will lobby hard for the question to be answered "yes." Ignored and avoided is any true voice of the public you have the duty to protect. Our efforts to have a consumer advocate appointed to the TARRTF were summarily rebuffed. While there was some talk of holding public hearings around the state to get comment from the public, not a single public hearing was held.

Due to the void of any meaningful public participation in the process, the Office of Disciplinary Counsel (ODC) has felt compelled to advocate on behalf of protecting the public. In the interest of protecting the consuming public, we believe that the question should be answered in the negative – that a lawyer should not spend the money until the lawyer has earned the money. To do otherwise violates the two most important principles of trust accounting, that client funds are to be held separate from lawyer funds, and that client funds are to be safeguarded against loss. This is the position taken by the American Bar Association's Model Rules of Professional Conduct that provide that:

A lawyer shall deposit into a client trust account legal fees and expenses that have been paid in advance, to be withdrawn by the lawyer only as fees are earned or expenses incurred.

MRPC 1.15(c). The ABA added this language to their Model Rules in 2002. The Reporter's

explanation of this change included the comment that “The Commission is responding to reports that the single largest class of claims made to client protection funds is for the taking of unearned fees.” ABA Report to the House of Delegates, No. 401(Feb. 2002).<sup>1</sup> ODC is advocating that these advance fees be placed in trust accounts until earned for the same reason. Time and again, we have seen situations where clients paid their flat fee in advance, the funds were immediately put in the lawyer’s general account (under the auspices of former Formal Opinion 186), the work did not get done for one reason or another, but by then the money was gone and the client loses. In situations where the lawyer dies or is forced into bankruptcy before doing the work for which the client has paid an advance fee, if the funds were deposited into the lawyer’s general account, the funds are part of the estate and the client most likely loses. If the funds had been held in trust, the administrator or trustee could refund the unearned fees to the client. Sometimes the aggrieved clients can get a grant from our Lawyer’s Fund, but that takes many months, and until then, they are out of luck.

My July 14, 2006 memo to the TARRTF, which is included with these agenda materials, summarizes typical examples of the problems we have seen. We fully realize that these scenarios are the exception, not the rule – that the overwhelming majority of lawyers who place an advance flat fee in their general account, then go on to do the work to the client’s satisfaction. But in ODC, we are in the business of dealing with the exceptions, and the fact that a matter is an exception to the rule is little comfort to a member of the consuming public who has been harmed.

The clear trend is for the more progressive states to follow the lead of the ABA in protecting the consuming public. We believe Washington should do so as well. We believe a fully informed public would agree.

Like the TARRTF proposal, ODC proposes<sup>2</sup> to add to our RPC 1.15A(c) the language from the Model RPC 1.15(c) requiring that advance fees be held in trust until earned. The difference

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<sup>1</sup> It appears a number of jurisdictions have adopted the ABA Model RPC 1.15(c) language or similar provisions, including Arkansas, Colorado, Delaware, Florida, Hawaii, Iowa, Michigan, Nebraska, Nevada, North Dakota, Rhode Island, and Wyoming. The Supreme Court of New Hampshire has published for comment a proposal to adopt this language.

<sup>2</sup> In his July 10, 2007 memo to the Board, Mark Johnson suggests that the attached rule proposal differs from the position previously taken by ODC. It does not. ODC has long taken the position that other than an availability retainer, advance fees should remain in trust until earned. See the November 23, 2005 memo of Joy McLean and attached Discussion Group Draft Opinion 198 contained in the December 2005 materials of the Board of Governors. Mr. Johnson also appears to question who in ODC developed the attached proposal. The original position in 2005 was developed by Joy McLean, Anne Seidel, Joanne Abelson and myself, with consultation from the other Senior Disciplinary Counsel in ODC. As Acting Chief Disciplinary Counsel, I finalized the attached rule proposal by conforming the original ODC position to the excellent drafting work done by the TARRTF so that the differing proposals would differ only in substance, not in form. Mr. Johnson appears to express surprise at this ODC proposal, but we have been clear since the April 2007 meeting of the TARRTF that ODC would be submitting its own alternative rule proposal to the Board of Governors and Mr. Johnson has previously expressed his agreement with that procedure and made no request for the final ODC alternative proposal to be provided to the TARRTF for review or debate.

between the proposals is that the TARRTF proposal largely guts the model rule language by adding an exception in RPC 1.5(f)(2) that allows a flat fee to be placed in the lawyer's general account. The ODC proposal does not allow that. Both proposals do, however, allow an availability retainer to be placed in the general account, although the TARRTF proposal has such retainers being placed in the general account unless otherwise agreed to, whereas the ODC proposal leaves that to the lawyer's discretion, without the need for client agreement. Apart from these differences, the two proposals are virtually identical.

As a general matter, our trust account rules give client funds a high level of protection. The Board, and ultimately, the Court, has a fundamental decision to make as to whether to allow one type of fees, the flat fee, to be carved out of that sphere of protection. ODC clearly does not think that should happen. But if the Board does ultimately decide to recommend an exception for flat fees, ODC believes that the TARRTF proposal is a well-crafted rule to accomplish that, with one important exception. We believe that if a lawyer is allowed to place a flat fee in the lawyer's general account before doing the work for which the fee is paid, in the event of a dispute regarding the fee, the lawyer should be required to participate in the WSBA Fee Arbitration Program if so requested by the client. This is not a proposal for mandatory fee arbitration. It would only apply if a lawyer chooses to place the funds in the general account before earning them, and would only apply if the lawyer does not otherwise resolve the dispute with the client as to the fee. It is, however, an important provision, because otherwise the client is at a great disadvantage in getting the dispute resolved in a quick and economical fashion. The Bar Association and Supreme Court of Wisconsin recently engaged in about the same debate that we find ourselves facing. It is noteworthy that the new rule adopted this year by the Wisconsin Supreme Court, while allowing a flat fee to be placed in a general account pursuant to a written agreement in much the same fashion as the TARRTF proposed rule, requires the lawyer to participate in fee arbitration when there is a dispute as to that fee.

I look forward to the opportunity to discuss this issue with you.

ODC Rule Proposals Attached

cc: TARRTF members

**RULE 1.5 FEES**

[ODC Proposed Draft – July 10, 2007]

(a)-(e) [Unchanged.]

(f) Fees and expenses paid in advance of performance of services shall comply with Rule 1.15A, subject to the following exception:

(1) A lawyer may charge a retainer, which is a fee that a client pays to a lawyer to be available to the client during a specified period or on a specified matter, in addition to and apart from any compensation for legal services performed. A retainer must be agreed to in a writing signed by the client. If so agreed, a retainer may be considered the lawyer's property on receipt and need not be placed in the lawyer's trust account.

(2) In the event of a dispute relating to a fee under paragraph (f)(1) of this Rule, the lawyer shall immediately refund to the client that portion of the fee, if any, that the lawyer reasonably believes is unearned. If the lawyer and the client disagree about the client's entitlement to a refund or the amount of a refund, the lawyer shall, within 30 days of the accrual of the dispute, deposit into a trust account governed by RPC 1.15A the amount that a reasonably prudent lawyer would believe to be reasonably in dispute. The lawyer shall maintain the funds in trust until the dispute is resolved. The lawyer shall take reasonable and prompt action to resolve the dispute in compliance with Rule 1.15A(g).

(g) A lawyer shall not characterize any fee as "nonrefundable," "minimum," or "earned upon receipt."

**Comment**

[1] – [9] [Unchanged.]

**Additional Washington Comments (10-14Z)**

*Reasonableness of Fee and Expenses*

[10] Every fee agreed to, charged, or collected, including a fee ~~denominated as "nonrefundable" or "earned upon receipt"~~ that is considered a lawyer's property on receipt under paragraph (f)(1), is subject to Rule 1.5(a) and may not be unreasonable.

[11] Under paragraph (a)(9), one factor in determining whether a fee is reasonable is whether the fee agreement or confirming writing demonstrates that the client received a reasonable and fair disclosure of material elements of the fee agreement. Lawyers are encouraged to use written fee agreements that fully and fairly disclose all material terms in a manner easily understood by the client.

Payment of Fees in Advance of Services

[12] In the absence of a written agreement between the lawyer and the client to the contrary that complies with paragraph (f)(1), all advance payments are presumed to be deposits against future services or costs and must, until the fee is earned or the cost incurred, be held in a trust account pursuant to Rule 1.15A. See Rule 1.15A(c)(2). This fee structure is known as an “advance fee deposit.” Such a fee may only be withdrawn when earned. See Rule 1.15A(h)(3). For example, when an advance fee deposit is placed in trust, a lawyer may withdraw amounts based on the actual hours worked. In the case of a flat fee or fixed fee which constitutes complete payment for specified legal services, and does not vary with the amount of time or effort expended by the lawyer to perform or complete the specified services, the lawyer and client may mutually agree, preferably in writing, on a reasonable basis for determining when portions of the fee have been earned, such as specific “milestones” reached during the representation or specified time intervals that reasonably reflect the actual performance of the legal services.

[13] Paragraph (f)(1) provides an exception to the general rule that fees received in advance must be placed in trust, and describes a fee structure sometimes known as an “availability retainer,” “engagement retainer,” “true retainer,” “general retainer,” or “classic retainer.” Under this rule, this arrangement is called a “retainer.” A retainer secures availability alone, i.e., it presumes that the lawyer is to be additionally compensated for any actual work performed. Therefore, a payment purportedly made to secure a lawyer’s availability, but that will be applied to the client’s account as the lawyer renders services, is not a retainer under paragraph (f)(1). A written retainer agreement should clearly specify the time period or purpose of the lawyer’s availability, that the client will be separately charged for any services provided, and whether the lawyer will treat the payment as the lawyer’s property immediately on receipt or whether the lawyer will hold the fee into a trust account until portions of the fee are actually earned by the lawyer’s continued availability to the client.

[14] If a lawyer and a client agree to a retainer under paragraph (f)(1) and the lawyer complies with the applicable requirements, including obtaining agreement in a writing signed by the client, the fee may be considered the lawyer’s property on receipt and need not be deposited into a trust account. See Rule 1.15A(c) (lawyer must hold property of clients separate from lawyer’s own property). For definitions of the terms “writing” and “signed,” see Rule 1.0(n).

[15] In fee arrangements involving more than one type of fee, the requirements of paragraph (f)(1) apply only to the parts of the arrangement that are a retainer. For example, a client might agree to make an advance payment to a lawyer, a portion of which is a retainer with the remainder to be applied on an hourly basis as services are rendered or as a flat fee for specified legal services. The latter portion is an advance fee deposit that must be placed in trust under Rule 1.15A(c)(2). If the requirements of paragraph (f)(1) are met regarding the retainer, those funds may be considered the lawyer’s property on receipt and need not be kept in a trust account. If the payment is in one check or negotiable instrument, it must be deposited intact in the trust account, and if the retainer portion is agreed to belonging to the lawyer upon receipt, it must be withdrawn

at the earliest reasonable time. See Rule 1.15A(h)(1)(ii) & (h)(4). See also Comment [10] to Rule 1.15A (explaining prohibition on split deposits). Although a signed writing is required under paragraph (f)(1) only for the retainer of the fee (and only if the lawyer and client agree that the fee will be the lawyer's property on receipt), the lawyer should consider putting the entire arrangement in writing to facilitate communication with the client and prevent future misunderstanding. See Washington Comment [11].

[16] When a lawyer-client relationship terminates, a lawyer must refund the unearned portion of a fee. See Rule 1.16(d); In re DeRuiz, 152 Wn.2d 558, 574-75, 99 P.3d 881 (2004). Under paragraph (f)(2) of the Rule, if there is a dispute over the amount of a retainer under paragraph (f)(1), the lawyer is obligated to refund to the client that portion of the fee that the lawyer reasonably believes is unearned, even if the fee was considered the lawyer's property on receipt and was not being held in a trust account. In the event of a dispute about the refund amount or the obligation to make such a refund, the lawyer is obligated to place the amount that a reasonably prudent lawyer would believe to be reasonably in dispute into a trust account, at which point the lawyer has an affirmative obligation to attempt to resolve the dispute in accordance with the provisions of Rule 1.15A(g). For the definitions of "reasonably" and "reasonably believes," see Rule 1.0(h) and (i). In determining the efforts that a lawyer should undertake to resolve a dispute under paragraph (f)(2), see Comment [9] to this Rule and Washington Comment [9] to Rule 1.15A.

*Prohibition on "Nonrefundable," "Minimum," and "Earned-Upon-Receipt" Terminology*

[17] Paragraph (g) prohibits a lawyer from characterizing any fee as "nonrefundable" or "earned upon receipt." The term "nonrefundable" is misleading because every fee, however characterized and regardless of the terms of the agreement, must be reasonable under Rule 1.5(a) and is subject to the refund requirement of Rule 1.16(d) upon termination of representation. See Washington Comment [16]. The term "earned upon receipt" is misleading because fees are not actually earned until the lawyer performs the service or otherwise confers a benefit on the client. Paragraph (g) also prohibits a lawyer from characterizing a fee as "minimum." This term is sometimes used by lawyers to describe, for example, a fee that will be no lower than a specified amount, to be credited to the client at an hourly rate as work is performed (often until an initial deposit is "exhausted"), with any additional work to be billed on an hourly basis. Under paragraph (g), the lawyer may not use the term "minimum" to describe this (or any) fee arrangement because the word "minimum" implies that such a fee is nonrefundable. In addition, this fee arrangement is not a "retainer" under paragraph (f)(1) because it does not secure availability alone. An advance of such a fee from a client, therefore, must be deposited in a trust account under Rule 1.15(c)(2), to be withdrawn by the lawyer as it is earned.

**RULE 1.15A: SAFEGUARDING PROPERTY**

*[ODC Proposed Draft – July 10, 2007]*

(a) – (b) [Unchanged.]

(c) A lawyer must hold property of clients and third persons separate from the lawyer's own property.

(1) A lawyer must deposit and hold in a trust account funds subject to this Rule pursuant to paragraph (h) of this Rule.

(2) Except as provided in Rule 1.5(f), and subject to the requirements of paragraph (h) of this Rule, a lawyer shall deposit into a trust account legal fees and expenses that have been paid in advance, to be withdrawn by the lawyer only as fees are earned or expenses incurred.

(3) A lawyer must identify, label and appropriately safeguard any property of clients or third persons other than funds. The lawyer must keep records of such property that identify the property, the client or third person, the date of receipt and the location of safekeeping. The lawyer must preserve the records for seven years after return of the property.

(d) – (j) [Unchanged.]

**Washington Comments**

[1] [Unchanged.]

[2] Client funds include, but are not limited to, the following: legal fees and costs that have been paid in advance (other than retainers complying with the requirements of Rule 1.5(f)), funds received on behalf of a client, funds to be paid by a client to a third party through the lawyer, other funds subject to attorney and other liens, and payments received in excess of amounts billed for fees.

[3] – [7] [Unchanged.]

[8] If a lawyer accepts payment of an advanced fee deposit by credit card, the payment must be deposited directly into the trust account. It cannot be deposited into a general account and then transferred to the trust account. Similarly, credit card payments of earned fees and of retainers considered to be the lawyer's property on receipt under Rule 1.5(f)(1), cannot be deposited into the trust account and then transferred to another account.

[9] – [15] [Unchanged.]