**PENNSYLVANIA BAR ASSOCIATION COMMITTEE
ON LEGAL ETHICS AND PROFESSIONAL RESPONSIBILITY
and
PHILADELPHIA BAR ASSOCIATION PROFESSIONAL GUIDANCE COMMITTEE
JOINT FORMAL OPINION 2022-300**

ETHICAL CONSIDERATIONS IN THE HANDLING OF FLAT, EARNED UPON RECEIPT AND NON-REFUNDABLE FEES

I. Introduction and Summary

In 1995, the Pennsylvania Bar Association Committee on Legal Ethics and Professional Responsibility issued Formal Opinion 1995-100, "Ethical Considerations In Connection With Retainers Paid On Account Of Legal Services." In the opinion, the Committee concluded, *inter alia,* that (1) "non-refundable retainers are permissible but any arrangement for a non-refundable retainer must be confirmed by the clear and unambiguous language of a written statement provided to the client or a written agreement between the attorney and client," and (2) "in the absence of a clear written statement or agreement to the contrary, retainer payments must be deposited into a client escrow account."

In response to inquiries relating to Opinion 1995-100, the PBA Committee on Legal Ethics and Professional Responsibility and the Philadelphia Bar Association Professional Guidance Committee issue this Joint Opinion to clarify whether, and under what conditions, non-refundable fees may be deposited into the attorney's operating account. The Committees conclude that, if the fee is not only simply a "flat fee" but a fee deemed "earned upon receipt," attorneys may deposit these fees into an operating account rather than a Rule 1.15 IOLTA account or other Trust account. Any fee not "earned upon receipt" is deemed an "advance" fee which may only be deposited into the operating account if the client provides informed consent, confirmed in writing in accordance with Rule 1.15(i).

II. Pertinent Pennsylvania Rules of Professional Conduct

The issues in this Opinion implicate Pennsylvania Rules of Professional Conduct 1.0, 1.4, 1.5 and 1.15.

Rule 1.0 (“Confirmed in Writing”) states in relevant part:

> (b) “Confirmed in writing,” when used in reference to the informed consent of a person, denotes an informed consent that is given in writing by the person or a writing that a lawyer promptly transmits to the person confirming an oral informed consent. See paragraph (e) for the definition of “informed consent.” If it is not feasible to obtain or transmit the writing at the time the person gives informed consent, then the lawyer must obtain or transmit it within a reasonable time thereafter.

Rule 1.0 (“Informed Consent”) states in relevant part:

> (e) “Informed consent” denotes the consent by a person to a proposed course of conduct after the lawyer has communicated adequate information and explanation about the material risks of and reasonably available alternatives to the proposed course of conduct.

Rule 1.4 (“Communication”) states in relevant part:

> (b) A lawyer shall explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation.

Rule 1.5 (“Fees”) states in relevant part:

> (a) A lawyer shall not enter into an agreement for, charge, or collect an illegal or clearly excessive fee. The factors to be considered in determining the propriety of a fee include the following:
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> (1) whether the fee is fixed or contingent;
> (2) the time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly;
> (3) the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer;
> (4) the fee customarily charged in the locality for similar legal services;
> (5) the amount involved and the results obtained;
> (6) the time limitations imposed by the client or by the circumstances;
> (7) the nature and length of the professional relationship with the client; and
> (8) the experience, reputation, and ability of the lawyer or lawyers performing the services.
>
> (b) When the lawyer has not regularly represented the client, the basis or rate of the fee shall be communicated to the client, in writing, before or within a reasonable time after commencing the representation.

Comment [2] to Rule 1.5 provides in pertinent part: “A lawyer may require advance payment of a fee, but is obliged to return any unearned portion . . . .”

Rule 1.15 ("Safekeeping Property") states in relevant part:

> (b) A lawyer shall hold property of clients or third persons that is in a lawyer's possession in connection with a representation separate from the lawyer's own property.
> * * *
> (i) 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, *unless the client gives informed consent, confirmed in writing*, to the handling of fees and expenses in a different manner. (emphasis supplied).

Pa.R.P.C. 1.15(a)(10) defines "Rule 1.15 Funds" as "funds which the lawyer receives from a client or third person in connection with a client-lawyer relationship, or as an escrow agent, settlement agent or representative payee, or as a Fiduciary, or receives as an agent, having been designated as such by a client or having been so selected as a result of a client-lawyer relationship or the lawyer's status as such. When the term "property" appears with "Rule 1.15 Funds," it means property of a client or third person which the lawyer receives in any of the foregoing capacities.

Pa.R.P.C. 1.15(a)(11) defines a "Trust Account" an "account in an Eligible Institution in which a lawyer holds Rule 1.15 Funds. A Trust Account must be maintained either as an IOLTA account or an a Non-IOLTA account." The Committees consider advance fees/retainers to be "Rule 1.15 funds" that must be deposited into an IOLTA or other Trust account. Conversely, flat fees paid in advance, and earned on receipt, are not "Rule 1.15 funds," and Rule 1.15 would not apply to those funds because they are not "to be withdrawn by the lawyer only as fees are earned or expenses incurred" as set forth in Rule 1.15(i).[1]

III. <u>Discussion</u>

Rule 1.5(b) requires that "[w]hen the lawyer has not regularly represented the client, the basis or rate of the fees shall be communicated to the client, in writing, before or within a reasonable time after commencing the representation." This rule does not require a formal engagement letter or fee agreement, just some "writing" that memorializes the agreement between the lawyer and the client on payment. The best practice, consistent with promoting the communications required by Rule 1.4(b) is for a lawyer to prepare a formal letter that the client co-signs or otherwise formally acknowledges at the inception of the attorney-client relationship specifying the nature of the engagement and how a one-time non-refundable fee will be handled by the lawyer.[2]

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[1] Rule 1.15 Cmt [2], states in part: "With little exception, funds belonging to a client or third party must be deposited into a Trust Account as defined in paragraph (a)(11), and **funds belonging to the lawyer must be deposited in a business operating account** maintained pursuant to paragraph (j)." (emphasis added). Cmt [7], states in part: "Lawyers often receive funds from which the lawyer's fee will be paid. **Unless the fee is non-refundable, it should be deposited to a Trust Account and drawn down as earned.** The lawyer is not required to remit to the client funds that the lawyer reasonably believes represent fees owed." (emphasis supplied).

[2] The Opinion acknowledges that attorneys may use other methods, such as electronic signatures, to confirm the terms of their representation. The Committees note that any method that requires the client to affirmatively confirm the terms of the engagement is acceptable.

Rule 1.5 contains no requirement that the fee agreement stipulate whether the fee is to be maintained in an IOLTA or other Trust account or may be deposited into an operating account, but this Rule must be read in conjunction with Rule 1.15. When there is a "flat fee" arrangement, the lawyer should specifically state whether the fee is intended to be non-refundable and earned upon receipt. *See*, *ODC v. Ostrowski*, 135 DB 2008 (2009) (holding that because disclosure of fee as a "flat fee" was insufficient to transform the retainer automatically into lawyer's personal property, the fee should not have been deposited into the attorney's operating account; the disclosure failed to specify that the funds were nonrefundable and earned upon receipt).

Although Rule 1.15(i) requires that the lawyer deposit fees "paid in advance" in an IOLTA account, a fee agreement that describes a fee as "non-refundable" *and* "earned upon receipt" should not be considered a fee "paid in advance" and the lawyer is not required to deposit the fee into an IOLTA or other Trust account. As a best practice, to assure that there is no misunderstanding, the lawyer also should specifically state in the fee agreement that the lawyer is not depositing the fees into an IOLTA or other Trust account. Although a client's written confirmation is not required, it would reduce the likelihood of confusion by having the client do so.

Confirming the agreement to deposit these fees into an operating account explicitly documents the expectations of both the attorney and the client, and would allow the lawyer to deposit the flat fee into the lawyer's operating account. *See* Pa. Bar Ass'n Comm. on Legal Ethics and Prof'l Responsibility Formal Opinion 1995-100 (August 1, 1995) (stating that refundable retainers may be deposited into an attorney's operating account if a writing provided to the client so states in unambiguous terms).

One example of a disclosure that would meet these requirements is: "Lawyer and client agree that the fee in this matter (1) is a flat, non-refundable fee which is earned upon receipt and covers the following work (insert scope of the engagement), (2) will not be deposited into an attorney IOLTA or other Trust account to be billed against, and (3) will be deposited in the lawyer's operating account."[3] We caution that the phrase "earned upon receipt" is still subject to the limitations of Rule of Professional Conduct 1.5 and does not, by itself, justify retention of a fee where commensurate legal services have not been rendered.

The Committees note that, when the engagement has concluded, the lawyer must still determine whether to refund any portion of the fee. "One of the justifications for allowing lawyers to charge a flat fee has been that both the lawyer and the client assume risk. The lawyer assumes the risk that the work may become unduly time intensive; the client assumes the risk that the lawyer will expend less time on the matter than if the lawyer charged an hourly rate." State of Maine, Board of Overseers of the Bar, Ethics Op. 211 (2014). "As with all fee agreements, however, a non-refundable retainer may not be 'illegal or clearly excessive.'" Pa. Bar Ass'n Comm. on Legal Ethics and Prof'l Responsibility Formal Opinion 1995-100 (August 1, 1995).

[3] In North Carolina State Bar Formal Ethics Opinion 5 (2004), North Carolina State Bar Counsel opined that no fee is non-refundable because of an attorney's obligation not to charge an excessive fee. That Opinion recommends use of the term "prepaid flat fee" rather than "non-refundable flat fee."

Most of the opinions on this issue from other jurisdictions address the inherent risks where the client terminates the engagement before its completion. The concern expressed in these opinions is that a dissatisfied client will not wish to forfeit monies paid as part of the non-refundable (and possibly excessive) fee in order to discharge the attorney and secure substitute counsel. *See, e.g.*, D.C. Ethics Op. 355 (2010). That is not the situation addressed in this Opinion, which assumes that the matter was handled through to its completion. Nevertheless, the attorney must evaluate whether the fee is excessive under the circumstances. When making that evaluation, the lawyer should consider the factors listed in Rule 1.5(a). Any excess must be returned promptly to the client.

IV. <u>Conclusion</u>

As outlined above, the Committees conclude:

- Any fee not "earned upon receipt" is deemed an "advance" fee, which may only be deposited into the operating account if the client provides informed consent, confirmed in writing, in accordance with Rule 1.15(i); and,
- When a fee is deemed to be "earned upon receipt," attorneys may deposit the fee into an operating account rather than a Rule 1.15 IOLTA account or other Trust account, provided that the attorney specifically states in the fee agreement that the fee is intended to be non-refundable and earned upon receipt.

CAVEAT: THE FOREGOING OPINION IS ADVISORY ONLY AND IS NOT BINDING ON THE DISCIPLINARY BOARD OF THE SUPREME COURT OF PENNSYLVANIA OR ANY COURT. THIS OPINION CARRIES ONLY SUCH WEIGHT AS AN APPROPRIATE REVIEWING AUTHORITY MAY CHOOSE TO GIVE IT.