New York State Bar Association

Committee on Professional Ethics

Opinion 763 – 5/15/03 (22-01)	Topic:	Third-party payments by credit card; fees deducted from such payments before remittance to client.
Modifies: N.Y. State 117 (1969) N.Y. State 362 (1974)	Digest:	Not improper for lawyer to accept collection payments from debtors by credit card on behalf of creditor-client where funds are placed in trust account and proper safeguards employed, and all requirements regarding contingent or fixed fee forms of engagement are met. Legal fees may be deducted from such payments before remittance to client if not excessive or in dispute; if disputed, lawyer may not withdraw disputed fees, must forward payment to client to the extent not in dispute and must attempt to resolve dispute. If applicable, the lawyer must submit matter to fee dispute resolution program.
	Code:	DR 2-106(A); 2-106(B); 2-106(C)(2)(b); 2-106(D); 2-106(E); 4-101; 9-102(A); 9-102(B)(4). EC 2-17; 2-19; 2-20; 2-21; 2-23; 9-5.

QUESTION

May an attorney whose practice includes debt collection matters (1) accept payment by credit card on behalf of a client from the client's debtors; (2) transfer the payment collected into an IOLA[1] or other trust account to be held until a netted payment

[1] N.Y. Jud. Law § 497.

is remitted to the client; (3) deduct from the trust account an agreed upon sum as the attorney's legal fee, together with all related disbursements except for credit card service fees; (4) remit the netted payment to the client; and (5) pay all applicable credit card service fees from the attorney's own operating account?

OPINION

A law firm's practice, in large part, includes the representation of one or more creditors in connection with debt collection matters. The Committee is advised that, customarily in this type of practice, an attorney who has successfully collected unpaid sums from a debtor retains approximately 25% of funds collected as a legal fee and remits the remaining 75% to the creditor-client. For purposes of this opinion, the Committee assumes that all fees to be paid to the law firm will not be "excessive" under the factors set forth in DR 2-106(A) of the Code.

The law firm proposes to initiate a payment program whereby debtors of creditor-clients could pay their overdue accounts, or the judgments the firm has obtained against them, by credit card. The debtor would authorize payment either telephonically or by in-person execution of the law firm's credit card debit form. The debtor is to receive full credit for any payment charged, and the client will ultimately receive all monies collected, less only the firm's agreed upon legal fee and the disbursements which are to be deducted prior to remittance.

By undertaking such a program, the firm will be acting in much the same manner as a "merchant" in a retail establishment. When dealing with a retail merchant, a merchant credit card bank charges "points" against any credit card payment that the merchant has received for the sale made. The firm advises that the bank charge is approximately 2% of each dollar of payment received. "Discounts" may be offered to a merchant based on the amount of credit card charges.

In N.Y. State 362 (1974) and N.Y. State 117 (1969), as well as N.Y. State 399 (1975), this Committee answered in the affirmative the question of whether a lawyer could participate in a bank charge card system where the agreement with the bank permits the lawyer's clients to pay for legal services by credit card. Certain minimal safeguards, however, were to be incorporated into any such plan. A*ccord,* Utah State Bar Op. 97-06[2]; So. Carolina Bar Ethics Advisory Opinion 98-08[3]; Colo. Bar Ass'n Opinion 97/98-01.[4]

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[2] The attorney may, among other things, (a) accept cash or a check from a client to be held against unearned fees or costs when the attorney knows that the client obtained funds through use of a credit card; (b) enter into a retainer agreement with a client under which the client gives the attorney a credit card number and authorizes charging the client's credit card when fees are earned and costs incurred; and (c) place a notice on bills to clients that credit card payment is accepted. The opinion also noted that by accepting credit card payments, the attorney has no obligation to enter into a bank-charge credit card arrangement.

Preliminarily, the Committee observes that when N.Y. State 117 and N.Y. State 362 were written, the use of credit cards was not as common as it is today and the payment of legal fees by credit card was a novelty. With over thirty years of credit card history to look back upon and little abuse of the arrangement by lawyers or banks, the Committee has reconsidered the safeguards listed in its earlier opinions. In so doing, the Committee concludes that it is no longer necessary to require that the agreement between the lawyer and the bank provide that, in any possible suit against the client, the bank waive all defenses which a holder in due course might have. The Committee also observes that the prohibition against any display of a decal in the lawyer's office has been superseded by substantive law.[5] This Committee does not pass upon issues of law, but restricts its opinions solely to ethical issues arising under the Code. Therefore, to the extent herein provided, the requirements of N.Y. State 117 and N.Y. State 362 are modified.

In the present inquiry, and unlike the situations posed in our prior opinions, the monies to be received by the lawyer from credit card payments are from third persons, not clients directly, and are primarily the property of the creditor-client. The payments only partially comprise the lawyer's legal fee. For this reason, the funds must be placed in the lawyer's trust account (or an IOLA account, if the amount of funds received from each transaction is small and/or is to be held for a short period of time). *See generally* DR 9-102, EC 9-5; *see also* N.Y. Jud. Law § 497.

DR 9-102(A) provides that:

> A lawyer in possession of any funds or other property belonging to another person, where such possession is incident to his or her practice of law, is a fiduciary, and must not misappropriate such funds or property or commingle such funds or property with his or her own.

See also DR 9-102(B) which requires, in part, that funds belonging to other persons also be kept in separate accounts, properly identified.

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[3] Client's credit card may be charged for fees so long as the attorney notifies the client before charges are billed to the credit card and offers the client an opportunity to question errors.

[4] Credit card payments may be accepted under certain circumstances so long as the arrangement is fair and reasonable, confidentiality is assured, and the attorney's independence is not compromised.

[5] In *Bates v. State Bar of Arizona,* 433 U.S. 350 (1977), the United States Supreme Court held that lawyers had a First Amendment right to truthfully advertise prices for routine legal services. At the time that N.Y. State 117 and N.Y. State 362 were issued, New York and other states did not permit advertising of any kind. *Bates* and its progeny are controlling on this issue. DR 2-101(A) of the Code now requires that "A lawyer … shall not use or disseminate or participate in the preparation or dissemination of any public communication or communication to a prospective client containing statements or claims that are false, deceptive or misleading."

After deposit of the payment in the trust account, the law firm then proposes to deduct its fees and disbursements before remitting the netted sum to the client. DR 9-102(B)(4) provides that:

> Funds belonging in part to a client or third person and in part presently or potentially to the lawyer or law firm shall be kept in such special account or accounts, but the portion belonging to the lawyer or law firm may be withdrawn when due unless the right of the lawyer or law firm to receive it is disputed by the client or third person, in which event the disputed portion shall not be withdrawn until the dispute is finally resolved.

A written agreement with the client will help to minimize the chance of any dispute arising over fees. *See* EC 2-19 and EC 2-23. In circumstances where, as here, the law firm plans to deduct its fee before remitting payment to the client, it is particularly important that there be no misunderstanding regarding legal fees.

If the firm's fee is solely dependent on the collection of funds from debtors, the fee arrangement is contingent and a written agreement is not only advisable, but required. DR 2-106(D) provides that:

> Promptly after a lawyer has been employed in a contingent fee matter, the lawyer shall provide the client with a writing stating 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 a settlement, trial or appeal, litigation or other expenses to be deducted from the recovery and whether such expenses are to be deducted before or, if not prohibited by statute or court rule, 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 determination.

See also EC 2-20.

Whether fees are contingent or fixed, the firm will be required (subject to narrow exceptions[6]) to provide each client for which it commences a new matter with a written letter of engagement (22 N.Y.C.R.R. § 1215.1, effective March 4, 2002, and DR 2-106(C)(2)(b)) providing an explanation of the scope of legal services to be provided, the fees to be charged and the firm's billing practices, and, if applicable, providing notice of

[6]Exceptions are: "(1) representation of a client where the fee to be charged is expected to be less than $3000, (2) representation where the attorney's services are of the same general kind as previously rendered to and paid for by the client, or (3) representation in domestic relations matters subject to Part 1400 of the Joint Rules of the Appellate Division (22 NYCRR) or (4) representation where the attorney is admitted to practice in another jurisdiction and maintains no office in the State of New York, or where no material portion of the services are to be rendered in New York." 22 N.Y.C.R.R., Part 1215 § 1215.2, effective March 4, 2002.

the client's right to arbitration. 22 N.Y.C.R.R. Part 137 ("Fee Dispute Resolution Program") and DR 2-106(E). *See also* EC 2-19 and EC 2-23.

In the event a good faith dispute over fees arises with the client,[7] fees for services may not be withdrawn by the firm from the trust account until the dispute is finally resolved. Except for the amount in dispute, the balance of the funds should be remitted promptly to the client. If the dispute cannot be amicably resolved by the lawyer and client, the law firm must comply, if applicable, with requirements of the fee dispute resolution program recently promulgated as Part 137 of the Rules of the Chief Administrator of the Courts,[8] or promptly take other steps to "resolve amicably any differences on the subject." EC 2-23.

With regard to charges by the merchant credit card bank incurred in consequence of the firm's credit card program, such charges may be deducted from the sum remitted to the client if this arrangement is part of the understanding with the client;[9] otherwise these charges should be deducted from the firm's fees or paid by the firm from its operating account and not passed on to the client.

CONCLUSION

A law firm whose practice includes debt collection matters (1) may accept payment by credit card on behalf of a client from a client's debtors; (2) should transfer any payments collected by the law firm into an IOLA or other trust account where the payment is to be held until the netted amount can be remitted to the client; (3) may deduct from the trust account an agreed upon sum as the law firm's legal fee, together with all disbursements, so long as the fee is not excessive or in dispute; (4) may not withdraw any amount on account of fees that are disputed, and must promptly forward to the client the balance owing to the client; (5) may deduct the costs and expenses associated with the credit card service from the payment to be forwarded if agreed to by the client; otherwise, the lawyer should pay such expenses out of the firm's fees or its operating account; and (6) should promptly remit the netted payment to the client.

Depending on the nature of the fee arrangement with the client, the law firm should also comply with all requirements of DR 2-106(E) if the fee is contingent, or, alternatively, comply, if applicable, with 22 N.Y.C.R.R. § 1215.1. In the event of any dispute regarding the fee, the law firm should attempt to resolve all disputes amicably and promptly and, if applicable, should comply with the fee dispute resolution program set forth in 22 N.Y.C.R.R., Part 137.

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[7] It is assumed that there is little likelihood of a dispute arising between the lawyer and the debtor because payments will only be received by the firm if the collection matter has been resolved and the debtor agrees or wishes to pay the collection amount by credit card.

[8] 22 N.Y.C.R.R., Part 137 ("Fee Dispute Resolution Program") and DR 2-106(E).

[9] *Cf.* So. Carolina Bar Ethics Advisory Op. 98-08 (where, under an attorney's agreement with a credit card company, the latter charges an administrative fee, the attorney may pass such costs on to the client, provided the total fee is "objectively reasonable.")