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New York State Bar Association
Committee on Professional Ethics

Opinion 996 (1/3/14)

Topic: Escrowed client funds

Digest: Client funds in a lawyer's escrow account may not be shielded from lawyer's creditor by transferring them to an escrow account held by the lawyer's lawyer.

Rules: 1.15; 8.4

FACTS

1. The inquiring lawyer ("L1") represents another lawyer ("L2") who owes money to a third party. As part of that representation, L1 is trying to negotiate an installment payment agreement with the third party, but has been unsuccessful. L1 is concerned that L2's creditor may seek to levy on L2's escrow account, which contains unearned advance payment retainers paid by L2's clients. So as to protect those funds, L2 would like to transfer the funds to L1, to be held in L1's escrow account. So long as the funds belong to L2's clients and L2 continues to represent those clients, L1 would maintain the funds in L1's escrow account; once L2 earns the funds, L1 would disburse them in whatever manner L2 directs.

QUESTION

2. May L2 properly transfer the unearned advance payment retainers from L2's escrow account to L1's escrow account, and may L1 receive those funds, for the purpose of protecting the funds from levy by a third party?

OPINION

3. The inquiry is governed by Rule 1.15 of the New York Rules of Professional Conduct ("the Rules"). Rule 1.15(a) provides: "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." Rule 1.15(b)(1) provides in part that funds belonging to another person but in the lawyer's possession incident to the practice of law shall be maintained in a special account or accounts "in the lawyer's own name, or in the name of a firm of lawyers of which the lawyer is a member, or in the name of the lawyer or firm of lawyers by whom the lawyer is employed."

4. The funds at issue are advance payment retainers from L2's clients that have been paid to, but not yet earned by, L2. *See* N.Y. State 983 ¶5 & n.6 (2013) (distinguishing advance

payment retainers from general retainers). L2 may agree with those clients to treat such funds as belonging to the clients until earned, or alternatively, to treat the funds as belonging to L2 subject to an obligation to return any ultimately unearned amounts to L2's clients. *See* N.Y. State 983 ¶4 (2013); N.Y. State 816 ¶¶ 4-7 (2007). The inquiry does not explicitly state whether L2's clients agreed with L2 on one of these options. However, it does state that the funds are being maintained in L2's escrow account. We assume that the funds are being held in that account properly, which is to say that the funds do not yet belong to L2, but rather are being treated as belonging to L2's clients until earned. See N.Y. State 983 ¶4; N.Y. State 816 ¶ 5. Because the funds currently belong to persons other than L2, but are in L2's possession incident to the practice of law, they constitute property subject to Rule 1.15.

5. Under Rule 1.15, L2 must continue to maintain these advance payment retainers belonging to L2's clients in L2's escrow account. That requirement is subject to client direction, in that L2 must comply with any given client's request for disbursement of that client's funds. *See* Rule 1.15(c)(4). But there is no suggestion in the current inquiry that any client has requested that L2 disburse escrow funds to L1, much less that all the clients have done so, as would be required for L2 to pursue the proposed course of action. Absent such direction from all affected clients and as long as the funds remain unearned, L2 may not transfer them to L1 or anyone else other than the clients to whom the money belongs.

6. We note some matters beyond the scope of our response. There are legal questions about whether the proposed transfer of the client's escrowed funds would tend to serve the purpose of avoiding levy by L2's creditor. These include the questions whether the funds in the L2's escrow account, which are unearned retainer fees not yet belonging to L2, would even be subject to levy under the circumstances, and whether the funds, if they could appropriately be transferred to the L1's escrow account, would be any better protected from the creditor. The Committee does not opine on questions of law as opposed to ethics, and in any event, the propriety of the proposed transfer does not turn on its efficacy.

7. Another kind of legal question is more relevant to ethical propriety. L1 does not ask about the lawfulness of the proposed transfer of the client's escrowed funds for the purpose of avoiding levy by the L2's creditor, but the propriety of the proposed conduct depends in part on whether such conduct is known by L1 or L2 to be in violation of law. Under the facts presented, L1 already is representing L2 in negotiating with the creditor, those negotiations have been unsuccessful, and L2 and L1 are contemplating the transfer from L2 to L1 for the specific purpose of protecting the L2's escrowed funds from being levied upon by the creditor. It is relevant to consider whether there would be anything fraudulent about the proposed transfer or whether, for example, L1 and L2 might reasonably believe that the purpose of transfer would be to protect from a wrongful rather than a legitimate attempt to levy. We note only that whether the proposed transfer would be fraudulent or otherwise unlawful, although a legal question, would implicate various rules of legal ethics. *See* Rule 1.2(d) (a lawyer shall not "counsel a client to engage, or assist a client, in conduct that the lawyer knows is illegal or fraudulent, except that the lawyer may discuss the legal consequences of any proposed course of conduct with a client"); Rule 8.4(b) (a lawyer shall not "engage in illegal conduct that adversely reflects on the lawyer's honesty, trustworthiness or fitness as a lawyer"); Rule 8.4(c) (a lawyer shall not "engage in conduct involving dishonesty, fraud, deceit or misrepresentation").

8. If L1 and L2 were free under Rule 1.15 to engage in the proposed transfer of funds, then they would need to consider legal questions such as those mentioned above, and the ethical consequences of the answers to those questions. However, because the proposed transfer would violate Rule 1.15, they need not reach such issues.

CONCLUSION

9. Funds held by a lawyer as advance payment retainers belonging to the attorney's clients and not yet earned by the lawyer must be held in the lawyer's escrow account and may not be transferred into the escrow account of another lawyer who represents the attorney holding the advance payments.

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