

Rules: 1.5, 1.6, 1.15, and 1.16

Subject: Disposition of Client Trust Account Funds

Summary: A Lawyer may not take possession of unearned funds remaining in a Client's trust account even if the Client has discontinued communication with and cannot be located by Lawyer after a diligent search, and even if an operative fee agreement appears to permit the lawyer to do so.

BACKGROUND

Lawyer began representing Client regarding what was hoped to be an uncontested divorce under a flat-fee arrangement. The fee agreement between the Lawyer and Client, signed by the Client states

“[i]f Client fails to communicate with [Lawyer], any unclaimed retainer funds will become property of [Lawyer] after one year. Client understands that the retainer is a deposit to ensure payment of fees and expenses and not a flat fee.”

Before the divorce action was filed, Client left the state, requested that the divorce be postponed, and indicated that Client would contact Lawyer upon returning to the state. This occurred two years ago. Lawyer has had no further contact with the Client. The Lawyer cannot reach the Client by email or telephone. The Lawyer, admittedly, has not attempted to reach Client by mail. But this is because Lawyer believes the Client likely still lives with Client's spouse, and that any communication might be received and read by the spouse. Lawyer reasonably believes Client simply decided to no longer pursue a divorce, and that representation has effectively terminated.

There is a small amount (less than \$100) remaining in Lawyer's Client trust account that belongs to Client. It was intended to cover the filing fee for the divorce proceeding.

Lawyer has asked the Committee if it is permissible for Lawyer to invoke the language, above, from the fee agreement, and take possession of the funds. If not, what must Lawyer do with them? Lawyer has also inquired whether there is any retainer language Lawyer could include in future fee agreements to address the overarching issue of an unresponsive client that has funds remaining in trust.

Lawyer has posed this question in light of Rules 1.5 and 1.15 of the South Dakota Rules of Professional conduct, and ethics opinions from South Dakota and other jurisdictions where similar issues were addressed under similar rules.

For example, Lawyer recognizes that, under Rule 1.5, any fee must be “reasonable,” but remarks that the small amount involved here (less than \$100) might militate against application of that rule in this specific instance.

Lawyer likewise acknowledges Rule 1.15, which imposes an obligation of “safekeeping” regarding client property. Lawyer notes that some other jurisdictions have modified Rule 1.15 to

require attorneys to remit unclaimed funds to those jurisdictions' IOLTA programs, although South Dakota has not done so. Lawyer also notes that one of the Committee's previous opinions, Opinion No. 98-11, provided that, in the event of a client's death, an attorney should maintain the funds in trust until a valid claim is made or until they escheat to the state, but suggests this opinion may not be strictly on point.

Finally, Lawyer has noted that a 2006 formal ethics opinion in North Carolina opined that it was permissible for an attorney to include provisions in fee agreements assessing up to a certain amount per year as a "dormancy fee;" but that the New Hampshire Bar Association had issued an article cautioning against provisions in fee agreements that unclaimed funds are forfeited to the Lawyer.

ANALYSIS

Lawyer's situation is governed generally by Rules 1.5, 1.6, 1.15, and 1.16, which govern, respectively, fees, confidentiality, safekeeping of property, and a lawyer's obligations upon termination of representation, including return of client funds. This opinion is also informed by a recent opinion issued by this Committee, Opinion 2019-01, and an older opinion, Opinion 98-11.

For the reasons that follow, the Lawyer must maintain the funds at issue in an account segregated from the Lawyer's operating account unless the Client is located or otherwise claims the funds, or some other substantive legal obligation outside the scope of the Committee's purview requires the Lawyer to take other action.

I. Client funds must be returned to a client when representation is terminated, or kept safe and segregated from the lawyer's funds until the client is located.

As a starting point, Rule 1.16(d) provides in part that "[u]pon termination of representation, a lawyer shall take steps to the extent reasonably practicable to protect a client's interests, such as . . . refunding any advance payment of fee or expense that has not been earned or incurred." So generally, any advance payment of a fee or expense not yet earned or incurred by the lawyer must be returned upon termination of representation. Importantly, here, the funds being held by Lawyer were specifically designated to cover the filing fee of a legal action that was never filed. Therefore, the expense was not incurred, and the funds remain Client property.

Assuming the representation has terminated, Lawyer appears to have diligently attempted to satisfy Rule 1.16(d). Specifically, it has been reasonable for Lawyer to not send the funds or communications to the address where the Lawyer believes Client resides (with Client's spouse), because this might violate Rule 1.6(a), i.e., a lawyer "shall not reveal information relating to the representation of a client," subject to certain exceptions not relevant here. However, "reasonably practicable" steps to return the funds under Rule 1.16(d) would include Lawyer continuing to periodically attempt to contact Client about the funds.

Meanwhile, the funds remain Client's property. Rule 1.15(a) provides that 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. Funds shall be kept in a separate account maintained in the state where the lawyer's office is situated, or elsewhere with the consent of the client or third party."

Absent some exception or other Rule, the Lawyer must retain the funds in trust because they are Client's property.

II. The forfeiture provision of the fee agreement is not enforceable.

Lawyer has inquired whether the language in Lawyer's fee agreement contemplating Client's forfeiture of unclaimed retainer funds permits Lawyer to take possession of those funds, particularly here, where the fund is nominal. This would not be acceptable under Rule 1.5, regardless of the amounts involved. Rule 1.5 provides that a lawyer may not "make an agreement for, charge, or collect an unreasonable amount for fees or expenses" subject to a multi-factor analysis regarding reasonableness. However, under the language of the Lawyer's fee agreement, it is the Client's mere failure to communicate (as opposed to the Lawyer performing some service, or incurring some fee related to the representation) that triggers the forfeiture. This appears to preclude a finding that any amount, regardless of how small, has been "reasonably" earned or incurred. The fee agreement's language precludes a meaningful "reasonableness" analysis, because it is not contingent on the "reasonableness" of any particular fee, which the Committee has previously stated is unacceptable. *See* South Dakota Ethics Opinion 2019-01 ("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") (quoting South Dakota Ethics Opinion 2000-5A).

III. The size of the fund is insufficient to justify assessing fees related to the search.

Lawyer has also inquired whether Lawyer could take possession of some or all of the funds as legal fees related to the time or expense incurred in attempting to find the Client. There are opinions from other jurisdictions applying Rule 1.5 to this situation that contemplate a lawyer being compensated for *costs incurred* in attempting to locate a Client, such as postage, telephone bills, and even a private investigator's services, if the fund is substantial enough to justify them. *See* Virginia LEO 1673; Utah State Bar Ethics Advisory Opinion Committee Opinion No. 97-01. The Committee agrees, here, that the Lawyer could appropriately deduct from the funds at issue actual costs incurred by the Lawyer to locate the Client, because that would constitute an "expense" under Rule 1.5.

Assessing attorneys' fees for the search to justify retention of the funds, however, is another matter. At least one out-of-state opinion suggests "[a]ttorney's . . . fees associated with the search might appropriately be paid out of the trust fund." *See* Utah State Bar Ethics Advisory Opinion Committee Opinion No. 97-01 at fn. 2. However, that very same opinion states

“[c]learly expending all of the money held in trust to locate the client is not warranted and violates the rule of safely keeping a client’s property” before stating that, for large sums of money, such fees *might* be reasonable. (*Id.* ¶ 2.)

The Committee declines to opine there can never be circumstances where the size of the client fund might justify a lawyer spending time to locate the client and then billing the client attorneys’ fees because that situation is not presented here. Here, where there is less than \$100 in funds, assessing the Client attorneys’ fees for the search would be unreasonable under Rules 1.5 and 1.15.

IV. Other substantive law may dictate Lawyer’s future conduct.

This leaves Lawyer in the position of maintaining the funds at issue indefinitely. However, the Committee has previously provided guidance in a related circumstance that appears applicable here. In Opinion 98-11, a lawyer represented a client who died before completion of the representation, with over \$200 remaining in the client’s trust account. The lawyer believed the client had no spouse or children, and that no estate had been opened or ever would be opened. The lawyer asked how the funds should be disposed of. The Committee noted that it was possible that some party (such as the client’s surviving parents or client’s creditors) might assert a claim against the funds. The Committee then noted that the *ABA/BNA Lawyers Manual on Professional Conduct* had reported a decision from Missouri requiring a lawyer in a similar circumstance to “continue to make reasonable efforts to find the heirs, if further leads arise, and must keep the funds in the account until they escheat to the state.” (Opinion 98-11 at 2, (citing ABA/BNA § 45:1201).) The Committee also noted the ABA/BNA Manual suggested that “the lawyer may petition the appropriate court for judicial determination regarding the disposition, or the lawyer may follow the procedures contained in the state’s disposition of abandoned property laws.” (*Id.*) Ultimately, the Committee determined that the lawyer had to maintain what appeared to be abandoned client property “until a lawful claim is made to it or it escheats to the state” or “pursuant to an order of a court of appropriate jurisdiction.” (*Id.*)

Although the facts here are admittedly different, the Committee believes the rationale of this earlier Opinion still applies. In the case of so-called “missing” clients, many jurisdictions either allow, or even require, a lawyer to dispose of the “missing” client’s property according to the state’s abandoned property procedures. (*See* ABA/BNA § 45:1206 (citing ethics opinions from Alabama, Arizona, Colorado, Connecticut, Louisiana, Maryland, New York, North Carolina, Oregon, South Carolina, Utah, and Vermont).)

This Committee does not opine on matters of substantive law, and it cannot opine whether South Dakota’s own statutes regarding escheat of unclaimed property (SDCL Chapter 43-41B) apply here, but consistent with former Opinion 98-11, Lawyer should consider whether Lawyer already has or eventually will have an obligation to comply with these or similar statutes.

In addition, to ensure consistency with the directives of Opinion 98-11, Lawyer could, in theory, ask a court to resolve this issue, although there may be practical issues outside the scope of the Committee's purview (i.e., notice to the Client, confidentiality, etc.) that foreclose this option.

V. A "dormancy" fee *might* be enforceable, if reasonable.

On a related note, Lawyer asks whether Lawyer could include a provision in future fee agreements to the effect that a reasonable "dormancy" fee will be charged each year against remaining funds in a client's trust account which are not claimed after a reasonable period of time after notice. Lawyer notes that the North Carolina State Bar in its Opinion 2006-15 stated that this was acceptable if (1) the client gives written consent to the fee; (2) the fee violates no state law regarding fees charged for holding unclaimed property; and (3) the fee is reasonable under Rule 1.5.

It is the Opinion of the Committee that Lawyer may include a "dormancy" fee in future written fee agreements, but to comply with Rule 1.5, the fee must be reasonable, given the Lawyer's typical costs associated with administering the account in which the funds are held, and the amount of the funds at issue in relation to the overall balance of funds held by Lawyer in the account. Put another way, the fee must be set at an amount that reasonably approximates Lawyer's true anticipated administrative costs associated with maintaining the funds. The Committee (and perhaps Lawyer) cannot define this reasonable fee in advance because it will likely vary depending on the circumstances of a given situation. In addition, the fee agreement would need to not violate any unclaimed property statutes that might preclude assessment of such a fee, such as SDCL Chapter 43-41B, which is a substantive issue that is outside of the Committee's purview.

CONCLUSION

In conclusion, it is the Committee's Opinion that:

- A. The funds in Lawyer's trust account are neither "attorney fees" nor "costs" that Lawyer has earned from the representation of Client and, therefore, must generally be returned to the Client, or retained until the Client can be located;
- B. Lawyer has been reasonably diligent in attempting to locate and/or communicate with Client to return the funds, but must continue to periodically attempt to do so;
- C. Lawyer may not take possession of the funds based on the attorney/client fee agreement provision providing for forfeiture of the funds;
- D. Because the amount of the funds is nominal, Lawyer may not take possession of the funds under the theory that they would represent fees earned while attempting to locate

the Client, although the Committee does not state or imply there could never be a circumstance where that would be appropriate, such as in the case of a large fund;

- E. Lawyer should consider whether there are state abandoned property laws or other laws that might dictate what Lawyer must do with the funds; and
- F. Lawyer could, in the future, use a fee agreement that contemplates a “dormancy fee” for retention of a client’s funds, so long as the fee would violate no substantive law regarding unclaimed property, but any fee would have to be consented to in writing, and would have to be reasonable in relation to the actual costs Lawyer incurs in retaining funds.