UTAH STATE BAR Ethics Advisory Opinion Committee: Opinion No. 02-01

Issued February 11, 2002

¶ 1 Issue: Do the Utah Rules of Professional Conduct preclude a Utah lawyer from financing litigation costs through a loan from a third-party lending institution, if (a) the lawyer is obligated to repay the loan and (b) the client, by separate agreement with the lawyer, is obligated to reimburse the lawyer for such costs?

¶ 2 Conclusion: The Utah Rules of Professional Conduct do not preclude such litigation-financing arrangements, provided the lawyer discloses to the client the terms and conditions of the loan, the client consents, and the lawyer, but not the client, is obligor on the loan.

¶ 3 Background: A Utah State Bar lawyer seeks an advisory opinion regarding the ethical propriety under the Utah Rules of Professional Conduct of participating in a "recourse" loan program,**1**by which the lawyer would finance the costs of litigation for his client through a third-party lending institution offering loans to lawyers for litigation expenses.

The primary features of a typical program include:

The program allows a lawyer, often a personal-injury lawyer seeking to finance a contingent-fee case, to raise the money at low cost to be invested in litigation expenses. This is accomplished through a low-interest, recourse loan to the lawyer or law firm who uses the potential fees from the case as loan collateral.

Under the terms of the loan, the lending institution advances reimbursable litigation costs, as defined in the loan agreement, to the lawyer. The brochure of one such lending institution claims it advances 95% to 100% of the lawyer's case costs.

The lawyer pays monthly interest charges on funds advanced under the loan, and remits the loan principal upon settlement or resolution of the case. By a separate agreement with the client, the lawyer ultimately recoups litigation expenses and interest charges from the client if the case is successful.

If the case is abandoned or lost, the lawyer is obligated to repay advanced costs and expenses and any outstanding interest to the lender. The lawyer may elect not to receive funding from the lending institution on a particular case if the potential for success is not deemed high enough. The client remains obligated to repay the lawyer for such advanced costs under a separate agreement between the lawyer and the client.

The lending institution recommends the lawyer add language to the client fee agreement that discloses the case-financing transaction. A sample client letter discloses, "If no recovery is obtained, you will be obligated only for disbursements and charges as described below." Such disbursements include photocopying, messenger service, computerized research, videotape recordings, travel expenses, experts, investigators, etc. In disclosing the financing arrangement, the letter states, "You acknowledge and agree that we [the law firm] may borrow funds from time to time to pay certain of the costs referred to above and agree that, in addition to reimbursing us for the amount of such costs, you also will reimburse us for any interest charges and related expenses we incur in connection with such borrowings."

¶ 4 Variations of such financing arrangements are possible, but the essential features for

purposes of this opinion are that the lawyer is obligated to the lending institution to repay the loan principal, and the client is obligated to reimburse the lawyer for advanced litigation costs, plus any applicable interest.

¶ 5 Analysis: The letter requesting our opinion notes a concern with our Opinion 97-11,**2** dealing with a "non-recourse" cost-financing program. In that opinion, we concluded, "An attorney's grant of a security interest in a contingent fee from a particular case to secure a loan constitutes the sharing of fees with a non-lawyer in violation of Utah Rules of Professional Conduct 5.4(a)."**3**In other words, the lender's fee was contingent upon the lawyer's contingent fee. The Committee disagreed with the lender's contention that such an arrangement did not involve fees, but merely a repayment of costs. The opinion added, "Once a security interest in the recovery of contingent fees from a particular case is granted, Rule 5.4 is implicated. Upon that grant, Lender has the right to attach upon default in payment of the loan." That particularized interest would "compromise the lawyer's judgment in a number of ways," primarily by creating potential conflicts between the lawyer and the lender, thereby undermining the lawyer's duty of independent professional judgment and the duty of client loyalty.**4**

¶ 6 The proposed financing arrangement explained above has none of the objectionable features described in Opinion 97-11. Here, the lending institution has no interest in the lawyer's contingent-fee award because, under the separate loan agreement between the lawyer and the lender, the lawyer is obligated to repay the loan whatever the outcome of the case. Because this obligation is not contingent, the lawyer is not compromised, as was the lawyer under the arrangement described in Opinion 97-11. Similarly, in this case, the client, by separate agreement, remains obligated to the lawyer for payment of litigation costs. The lawyer is not compromised because the client's obligation is not contingent upon the outcome of litigation. The arrangement described above simply makes it easier for clients and attorneys to finance litigation and is mutually beneficial to both.

¶ 7 Many other state counterparts to this Committee have considered the professional ethics issues arising under financing arrangements similar to those in this opinion. These advisory opinions have analyzed the proposed financing arrangement in light of their respective rules' prohibitions against fee-splitting arrangements and the lawyer's "independent judgment." In Utah, these ethical standards are found in Rule 5.4(a).**5**The various state bar ethics opinions summarized in the Appendix to this opinion have invariably concluded that litigation-financing arrangements similar to those described above are permissible, provided the attorney remains obligated on the loan and there is full disclosure to the client. Our research has not disclosed a contrary opinion, and we generally concur with the reasoning and conclusions of these opinions.

APPENDIX

Florida

Formal Advisory Opinion No. 86-2, State Bar of Florida (April 15, 1986), asks whether "[l]awyers may charge a lawful rate of interest on liquidated fees and costs either as provided in advance by written agreement or upon reasonable notice." The com mittee's answer, in its entirety, states, "The Committee finds no basis for distinguishing between fees and costs advanced for the purpose of charging interest. Accordingly, the Committee concludes that the Code of Professional Responsibility does not prohibit in advance by written agreement or, in the absence of a written agreement, upon reasonable notice. It is the Committee's view that 60 days would constitute reasonable notice."

Georgia

Formal Advisory Opinion No. 92-1, State Bar of Georgia (January 14, 1992), describes a system for payment of certain costs and expenses in contingency-fee cases where the law firm sets up a draw account with a bank, secured by a note from individual firm lawyers. When a client makes a payment toward expenses incurred on the case, the law firm credits the client's account, and if the case is settled or verdict paid, the firm pays off the client's share of the money advanced on the loan. If no verdict or settlement is obtained, the lawyers are contractually obligated to repay the loan, although the client remains ultimately liable to the lawyer, not the bank, to reimburse such expenses. The opinion raises two issues: whether the bank loan to the lawyer compromises the attorney -client relationship and whether it is ethical to charge clients interest. As to the first issue, the opinion concludes there is no ethical impropriety provided the lawyers "make sure that the bank understands that its contractual arrangement can in no way affect or compromise the lawyer's obligations to his or her individual clients." The opinion similarly concludes on the second issue, "[I]t is permissible to charge interest on such advances only if (i) the client is notified in the contingent fee contract of the maximum rate of interest the lawyer will or may charge on such advances; and (ii) the written statement given to the client upon conclusion of the matter reflects the interest charged on expenses advanced in the matter."

Illinois

Opinion No. 92-9, Illinois State Bar Ass'n (January 22, 1993), posits a different factual arrangement. The question was whether the lawyer may ethically help clients obtain financing. Under the proposed arrangement, the lawyer pays an initial fee of $500 for which he is given the right to submit loan applications from clients. If the loan is approved, the client becomes solely responsible on the loan, but the attorney receives the loan proceeds less a 10% fee. The opinion concluded that an "attorney may ethically assist clients in obtaining loans for payment of attorney fees, providing the attorney protects the client's confidences and meets his fiduciary obligation of complete disclosure."

Missouri

Informal Opinion No. 970066, Missouri Bar Ass'n (August 20, 2001), asks, "If an Attorney borrows money in order to fund the litigation expenses in a case, may an attorney pass the interest on the loan through to the client?" In a terse answer, the Opinion concludes the "Code of Professional Responsibility does not prohibit an attorney from charging a lawful rate of interest on liquidated fees and costs, either as provided in advance by written agreement or, in the absence of a written agreement, upon reasonable notice."

New Jersey

120 N.J.L.J. 252, N. J. Advisory Comm. on Professional Ethics (July 30, 1987), discusses whether "it is appropriate for the firm to advance disbursements" in a contingency fee case. The financing arrangements are virtually identical to those described in the Utah inquiry. Consistent with its counterparts, the Committee found "nothing unethical or contrary to the letter of the rules of the Court, or Rules of Professional Conduct in the proposed provision."

Ohio

Opinion 2001-3, The Supreme Court of Ohio, Board of Commissioners (June 7, 2001), addresses "the ethical propriety of a law firm borrowing money, using the funds to advance costs and expenses of litigation in a personal injury matter accepted on a contingent fee basis, and then passing the interest fees and costs of the loan to the client as expenses of litigation." Again, the financing arrangements are virtually identical to those described in the Utah inquiry. The Ohio Board found: "[T]here is no rule prohibiting a lawyer from obtaining a loan from a third party institution for use in advancing the expenses of litigation provided the

loan is not secured by the client's settlement or judgment. However, the client should be informed."

Texas

Tex. Comm. on Professional Ethics, Op. 465, V. 54 Tex. B.J. 76 (1991), discusses two issues: whether an attorney may "ethically own an interest in a lending institution which loans money to personal injury clients of the attorney," and whether the attorney "may borrow money from a lending institution for case expenses . . . and ethically charge, or pass on, to the client, as part of the expense, the outofpocket [sic] interest or finance charges of the lending institution." The Committee found "an attorney may properly own an interest in a lending institution which loans money to personal injury clients of the attorney," and that "an attorney may properly borrow money from a lending institution for case expenses for a personal injury client, and charge, or pass on, to the client the actual out-of-pocket interest or finance charges of the lending institution."

Tennessee

Advisory Ethics Opinion 98-A-659, Board of Professional Responsibility of the Supreme Court of Tennessee (July 9, 1989), draws a similar conclusion from similar facts described in the Utah inquiry. The Board concludes "a lawyer may advance or guarantee certain expenses" by means of "a lending company or recommending such services to clients."

Footnotes

1.A "recourse loan" in this context is one for which the lawyer would be liable to a lending institution irrespective of the outcome of litigation being financed. *See* Black's Law Dictionary ("recourse loan" under "loan" entries) (7th ed. 1999).

2.Utah Ethics Adv. Op. 97-11, 97 WL 770890 (Utah St. Bar).

3.*Id.* at 1.

4.*Id.* at 2.

5."A lawyer or law firm shall not share legal fees with a nonlawyer" with noted exceptions, none of which is applicable here. Professional Independence of a Lawyer, Utah Rules of Professional Conduct 5.4(a) (2001).