

BY KENT A. GERNANDER

Nonrefundable Retainers & Other Oxymorons

A lawyer's fee may be fixed or based on time charges; it may be paid in advance or billed as earned. However, an unearned fee, if paid in advance, must be held in a trust account until earned, and must be refunded upon termination of the representation. Calling an unearned fee nonrefundable does not make it so.

These seem straightforward propositions, supported by ethics rules and a growing number of rulings and opinions. However, a number of lawyers continue to stretch the rules by attempting to retain unearned fees. Disciplinary authorities have responded by clarifying and enforcing the rules.

Rule 1.5(b) of the Minnesota Rules of Professional Conduct addresses "agreements for the advance payment of nonrefundable fees to secure a lawyer's availability for a specific period of time or a specific service." Such fees are sometimes called engagement fees or general retainers. They are "paid, apart from any other compensation, to ensure that a lawyer will be available for the client if required."¹ Common examples are situations in which "a client might wish to prevent anyone else from retaining the lawyer in connection with a particular matter. Or a client might

anticipate needing legal services in the future and wish to insure the lawyer's availability at the time, in effect 'taking an option' on the lawyer's services."² The attorney, by committing to an engagement, may forgo other opportunities for representation of clients, because of time constraints or conflicts of interest. Under such circumstances, the

lawyer may treat a reasonable engagement fee as earned upon receipt.³ Such engagement fees must be "reasonable in amount."⁴ An engagement fee satisfies this requirement "if it bears a reasonable relationship to the income the lawyer sacrifices or expense the lawyer incurs by accepting it, including such costs as turning away other clients (for reasons of time or due to conflicts of interest), hiring new associates so as to be able to take the client's matter, keeping up with the relevant field, and the like."⁵ An engagement fee must also be "clearly communicated in a writing signed by the client."⁶

Because such engagement fees are considered earned upon receipt, they are not considered client property and are not to be held in a lawyer's trust account.⁷

Payments for Services Distinguished

An engagement retainer "must be distinguished from a lump-sum fee constituting the entire payment for a lawyer's service in a matter and from an advance payment from which fees will be subtracted. A fee is an engagement retainer only if the lawyer is to be additionally compensated for actual work, if any, performed."⁸ If a fee is intended as compensation for services to be performed it is not earned until the agreed services have been performed. This is true whether the fee is a fixed amount or based on time charges, and whether it is paid in advance or paid as earned. Fees paid in advance for services to be performed are sometimes referred to as special retainers. Lump-sum fees are sometimes referred to as fixed fees or minimum fees. Regardless of terminology, they are not engagement fees and are treated differently.

Upon termination of an engagement, a lawyer is required to refund to the client "any advance payment of fees or expenses that has not been earned or incurred."⁹ This obligation to

refund unearned fees is not dependent upon the circumstances of termination, and applies whether the lawyer fails to perform the agreed services or the lawyer is discharged.

A client is entitled to discharge a lawyer at any time, with or without cause; the discharged lawyer is not entitled to contracted compensation or

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damages, but is limited to recovering the reasonable value of services performed.¹⁰ It is contrary to public policy to permit a lawyer to treat as nonrefundable a client's advance payment for legal services to be performed (as opposed to an engagement fee), because it compromises the client's ability to discharge the lawyer and secure other counsel to complete the representation, thereby holding the client hostage to an unwanted fiduciary relationship.¹¹

A lawyer is required to "deposit all fees in advance of the legal services being performed into a trust account and withdraw the fees as earned."¹² The rule excludes only availability retainers.¹³ If a lump sum fee is paid in advance, good practice would suggest that progress points be specified, permitting portions of the fee to be considered earned at those points in the engagement.

In several states, rules comparable to Minnesota's have been held to prohibit nonrefundable retainers, except availability fees.¹⁴ In others, discipline opinions and rulings have similarly construed comparable rules.¹⁵ In at least one state, a rule of professional conduct defines and clarifies obligations concerning retainers and flat fees.¹⁶



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Lochow & Opinion 15

In Minnesota, the issue may have been clouded for a time by interpretations of the ruling in *In re Lochow*, *supra* n. 3. In that case the Supreme Court held that “attorney fees for payment of services to be performed in the future must be placed in a trust account.” An exception was recognized for availability retainers, reasonable in amount, which could be immediately earned if the purpose were stated and approved in writing by the client. This holding was incorporated in Opinion No. 15, adopted by the Lawyers Professional Responsibility Board on September 13, 1991. It defined “Availability or Nonrefundable Retainers” as “Funds paid by a client or a prospective client to secure a lawyer’s general availability to, or representation of, that client over a specified period of time or for a specific legal matter;” and opined that such retainers “are not required to be deposited into a trust account or held in trust” provided a written retainer agreement is signed by the client, with a specific disclosure above the signature that the funds will not be held in trust and may not be refunded if the client terminates the lawyer’s services. This opinion could have been read to permit a lawyer, with the required disclosures and signature, to collect an advance fee payment for a service without obligation to hold it in trust.¹⁷

Opinion No. 15 was repealed January 26, 2006. Some of its provisions were incorporated in Rules 1.5(b) and 1.15(c), Minn. R. Prof. Conduct. Those rules now require a lawyer to deposit all advance fees into a trust account, except fees paid pursuant to an availability retainer.

Perhaps encouraged by the language of *Lochow* and Opinion 15, some lawyers have collected advance fees for legal services to be performed, treating the fees as nonrefundable and not holding them in trust. Discipline has not yet been imposed for treating an advance fee payment as nonrefundable, although lawyers have been disciplined for failing to communicate the fee in a writing signed by the client and for

failing to deposit unearned fees in a trust account. The Office of Lawyers Professional Responsibility has previously expressed its interpretation of the rule,¹⁸ and intends to continue educational efforts. Consideration may be given to seeking a formal opinion of the Lawyers Board, and discipline may be sought for egregious violations of the Rules.

Lawyers with questions about these and other matters may consult the Advisory Opinion Service of the Office of Lawyers Professional Responsibility. Advisory opinions may be obtained by phone (651-296-3952 or toll-free 1-800-657-3601) or by an email link on the Office website: <http://www.mncourts.gov/lprb/mail-form/AOService.aspx>. ▲

Notes

¹ Restatement, Third, The Law Governing Lawyers, sec.34, Comment (e).

² Geoffrey C. Hazard, Jr. and W. William Hodes, *The Law of Lawyering: A Handbook on the Rules of Professional Conduct* (New York: Law & Business, 1985), sec. 8.5.

³ *In re Lochow*, 469 N.W.2d 91, 98 (Minn. 1991).

⁴ Minn. R. Prof. Conduct, Rule 1.5(b).

⁵ Restatement, Third, The Law Governing Lawyers, sec.34, Comment (e).

⁶ Minn. R. Prof. Conduct, Rule 1.5(b). These and contingent fees are the only kinds of fees that the Rules require be agreed in a writing signed by the client.

⁷ Rule 1.15(c)(5), Minn. R. Prof. Conduct, requires that fees paid in advance of performing services be deposited in trust and withdrawn as earned “unless the lawyer and the client have entered into a written agreement pursuant to Rule 1.5(b).”

⁸ Restatement, Third, The Law Governing Lawyers, sec.34, Comment (e).

⁹ Rule 1.16(d), Minn. R. Prof. Conduct; see Rule 1.5, Comment 4 (“A lawyer may require advance payment of a fee, but is obliged to return any unearned portion.”)

¹⁰ *Lawler v. Dunn*, 145 Minn. 281, 176 N.W. 989 (1920); accord, *Nordling v. NSP*, 478 N.W.2d 498 (Minn. 1991); *Michaelson v. 3M*, 474 N.W.2d 174 (Minn. App. 1991).

¹¹ *In re Cooperman*, 633 N.E.2d 1069, 1072 (N.Y. 1994).

¹² Rule 1.15, Minn. R. Prof. Conduct.

¹³ Rule 1.15(c)(5), Minn. R. Prof. Conduct.

¹⁴ See *Cluck v. Comm’n for Lawyer Discipline*, 214 S.W.3d 736, 740 (Tex. 2007); *In re Kendall*, 804 N.E.2d 1152, 1160 (Ind. 2004); *Bd of Professional Ethics and Conduct v. Frerichs*, 671 N.W.2d 470, 475-77 (Iowa 2003); *In the Matter of Larry D. Sather*, 3 P.3d 403, 411 (Colo. 2000); *Ryan v. Butera*, *Beausang, Cohen & Brennan*, 193 F.3d 210, 216 (C.A.3d Pa. 1999); *Matter of Hirschfeld*, 192 Ariz. 40; 960 P.2d 640, 643 (1998); *In re Salvatore A. Scimeca*, 265 Kan. 742, 760; 962 P.2d 1080, 1091 (1998); *Doherty’s Case*, 142 N.H. 446, 703 A.2d 261, 264 (1997); *In re Cooperman*, 633 N.E.2d 1069, 1072 (N.Y. 1994).

¹⁵ Alabama Opinion Number 1993-21; Michigan Informal Ethics Opinion RI-069 (1991); *Grievance Administrator v. Cooper*, Case No. 06-36-GA (September 17, 2007), reversed by Michigan Sup. Ct. Order dated December 12, 2008, Case No. 135053; New Hampshire Bar Association Ethics Committee Opinion dated January 17, 2008.

¹⁶ Washington RPC 1.5(f). See also Chapter 45, Iowa Court Rules.

¹⁷ See W. Wernz, “Opinion 15: Retainer Fees,” 48 *Bench & Bar of Minnesota* 10 (Nov. 1991), pp. 11-13.

¹⁸ See P. Burns, “Nonrefundable retainers —when are they appropriate?,” *Minnesota Lawyer* (May 7, 2007).