

# **Exhibit E**

**THE ASSOCIATION OF THE BAR OF THE CITY OF NEW YORK**

**FORMAL OPINION 2000-2**

**Topic:** Charging interest on unpaid legal fees

**Digest:** 1. It is not improper for a lawyer to include in a retainer agreement a provision charging interest on unpaid legal fees when the lawyer (1) fully informs the client of the circumstances where interest may be charged, (2) those circumstances, the fee, and the interest rate are reasonable, and (3) the client consent.

2. It is also not improper to charge interest on unpaid legal fees, although the retainer agreement is silent, when the lawyer (1) notifies the client that the lawyer intends to charge a reasonable interest rate on unpaid legal fees, and (2) provides the client with a reasonable opportunity to pay the outstanding unpaid balance before any interest accrues.

**Code:** DR 2-101(C)(3); 2-106; EC 2-17; 2-18; 2-19; 2-23

Question

A lawyer inquires whether she may ethically charge a client interest on unpaid legal fees where (a) the retainer agreement expressly provides that interest will be charged and, alternatively (b) the retainer agreement is silent. Assuming *arguendo* that charging interest is ethical in either of these cases, the lawyer further asks what interest rates ethically may be charged.

A. May a written retainer agreement provide for interest to be charged on unpaid legal fees?

In N.Y. City 1982-6, this Committee previously considered whether a written retainer agreement may ethically provide for an interest charge on unpaid legal fees. In that case, the specific question under consideration was whether an annual interest charge of eighteen percent could be imposed on legal fees not paid within one month of billing. This Committee concluded that it is not improper to assess a reasonable interest charge on unpaid legal bills if (1) "the arrangement is clearly and fully explained to the client in advance and the client understands and consents to the proposed arrangement" and (2) "the arrangement does not result in the charging of an excessive fee." N.Y. City 82-6.<sup>[1]</sup>

In this same vein, N.Y. State 399 (1975) also concluded that it is not *per se* improper for a lawyer to charge interest on delinquent accounts if "the lawyer . . . advise[s] the client prior to performing services of the fact that interest will be charged on delinquent accounts which are delinquent for more than a stated period of time, the stated period is reasonable under all the circumstances of the matter, the rate of interest is reasonable, the fee is not excessive and the client consents to such interest charge." Similarly, in ABA Formal Opinion 338 (1974), the ABA's Committee on Ethics and Professional Responsibility also approved of a lawyer's charging interest, noting: "It is . . . the Committee's opinion that a lawyer can charge his client interest providing the client is advised that the lawyer intends to charge interest and agrees to the payment of interest on accounts that are delinquent for more than a stated period of time." See also C. Wolfram, *Modern Legal Ethics*, § 9.2.2, at 506-7 (1986) ("Most states now permit lawyers to make credit arrangements for the payment of fees, such as through client use of credit cards. By the same token, a fee contract can provide for a stipulated rate of legal interest on amounts due.").<sup>[2]</sup>

Based on these decisions, we conclude that when (1) the lawyer fully informs the client of the circumstances where interest may be charged, (2) those circumstances, the fee, and the interest rate are reasonable, and (3) the client consents, it is not improper for a retainer agreement to provide for charging interest on unpaid legal fees.

B. May a lawyer charge interest on unpaid fees where the agreement with the client is silent?

Having concluded that a lawyer may charge interest on unpaid balances where the retainer agreement provides for it, we now turn to the more difficult issue of whether a lawyer may charge interest on unpaid balances where the retainer agreement is silent. Although our research does not reveal any New York authority in point,<sup>[3]</sup> ethics committees in other states have divided over this issue. Four other committees have allowed it.<sup>[4]</sup> One committee has prohibited the practice.<sup>[5]</sup> Another has conditioned it on client consent.<sup>[6]</sup>

We begin by observing that although libraries have been written about the nature and scope of a lawyer's obligations to her client, there is surprisingly little said about the client's corresponding obligations to the lawyer. Nevertheless, it cannot be seriously debated that where a client retains a lawyer on a fee-paying basis, the client is obligated to honor the fee arrangement.<sup>[7]</sup>

For its part, the Code plainly recognizes that an important obligation of a client to the lawyer is to pay the lawyer's fee in accordance with the fee arrangement. DR 2-110 specifically includes among the grounds of permissible withdrawal the deliberate failure by the client to comply with "an agreement or obligation to the lawyer as to expenses or fees." DR 2-110(C)(1)(f). And, any doubt that the Code's drafters considered the client's payment obligation to be extremely important is dispelled by the potential consequences to the client that the Code allows if a lawyer is forced to collect a fee. Indeed, in this circumstance, the Code creates a limited exception to the lawyer's sacrosanct obligation not to disclose a client's confidences or secrets, which is one of the bedrock duties underpinning the lawyer-client relationship, and authorizes the lawyer "[to] reveal . . . [c]onfidences or secrets necessary to establish or collect the lawyer's fee. . . ." DR 4-101(4). Conversely, it is hardly surprising that there is no provision in the Code precluding a lawyer faced with a client who dishonors a fee arrangement from charging interest.

This Committee yields to no one in refusing to allow the rules of conduct governing our learned profession to become captive to the morals of the marketplace. But this does not mean that in interpreting these rules, we can, or should, ignore commercial reality and the consequences that would attend a rule subordinating the rights of a lawyer to the rights of other creditors seeking payment from a lawyer's client. Certainly, clients can be presumed to act in their own economic self-interest and faced with the choice between paying obligations to other creditors -- all carrying interest charges -- and a legal bill with no interest, the temptation to unduly delay payment of the lawyer's statement can prove irresistible.

Given this reality, we believe allowing interest to be imposed, and placing lawyers on a more equal footing with other creditors can, at least in some situations, serve the salutary purpose envisioned by EC 2-23 of avoiding fee disputes. Conversely, a rule precluding a lawyer from charging interest could foster litigation because a lawyer prevailing in fee litigation can recover prejudgment interest under CPLR § 5001 "from the earliest ascertainable date the cause of action existed." See, e.g., Hecht v. Clowes, 224 A.D.2d 312, 638 N.Y.S.2d 42 (1st Dep't 1996) (under CPLR § 5001, attorney entitled to pre-judgment interest on successful fee claim).

Our conclusion that an interest charge may be imposed is fortified by long-standing New York case law enforcing an "account stated" on behalf of an attorney where a client fails to respond to a bill. In New York, a lawyer may assert a cause of action for account stated against a client "with proof that a bill, even if unitemized, was issued to a client and held by the client without objection for an unreasonable period of time. It is not necessary to establish the reasonableness of the fee since the client's act of holding the statement without objection will be construed as acquiescence as to its correctness." O'Connell & Aronowitz v. Gullo, 644 N.Y.S.2d 870, 871 (3d Dep't) (citations omitted), appeal denied, 89 N.Y.S.2d 803 (1996).<sup>[8]</sup> Significantly, an account stated will be enforced regardless of whether there was an initial retainer agreement between the attorney and client. See, e.g., Ellenbogen & Goldstein, P.C. v. Brandes, 641 N.Y.S.2d 28, 29 (1st Dep't 1996), appeal denied, 89 N.Y.S.2d 806 (1997). An account stated may include interest even though there was initially no express agreement to pay interest. Davison v. Klaess, 280 N.Y. 252, 256 (1939); Emerick Assocs. v. Classic Tool Design Inc., 688 N.Y.S.2d 792, 794 (3d Dep't 1999) (affirming judgment in favor of plaintiff on account stated, finding that "based on plaintiff's express notification that it would begin charging a 1.5% monthly finance charge on all balances past due more than 30 days . . . Supreme Court did not err in its award of interest to plaintiff.").<sup>[9]</sup>

Accordingly, the Committee concludes that when the lawyer (1) notifies the client that the lawyer intends to charge a reasonable interest rate on unpaid legal fees and (2) provides the client with a reasonable opportunity to pay the outstanding unpaid balance before any interest accrues, it is not improper to charge interest on unpaid legal fees although the retainer agreement is silent.

At the same time, the Committee wishes to underscore its strongly held view that it is far better practice to address all the terms of an engagement, including all payment provisions and any interest to be charged on past due bills, in a written retainer agreement entered into at the inception of the engagement. The Committee echoes the cautionary note sounded by the draft Restatement of the Law Governing Lawyers that “[a] lawyer . . . usually has no justification for failing to reach an agreement at the inception of the relationship or pressing need to modify an existing agreement during it. The lawyer often has both the opportunity and the sophistication to propose appropriate terms before accepting a matter.” Restatement of the Law Governing Lawyers, Proposed Final Draft No. 1, § 29A(1) at 42 (March 29, 1996). But not every lawyer at the outset of the engagement will contemplate that the client will fail to discharge her payment obligation and where this occurs, we believe that interest may be imposed under the circumstances set forth.

C. The amount of any interest must be reasonable.

In response to the third inquiry – concerning the appropriate interest rates that can be charged – we note that the fee charged a client shall not be “illegal or excessive” and shall be “reasonable,” see DR 2-106; EC 2-17. Though interest is not part of the fee, but rather compensation for delay in payment of the fee, the rate of interest should be subject to the same reasonableness requirement. Furthermore, any interest charged must also comply with all applicable laws, including usury laws.

[1] In reaching this conclusion, this Committee relied upon DR 2-106 and EC 2-17, EC 2-18 and EC 2-19 of the Code of Professional Responsibility (the “Code”). We did not refer to DR 2-101(C)(3), which we believe also supports this conclusion. On its face, DR 2-101(C)(3) provides that attorneys may include information in advertisements about “credit arrangements accepted.” Because credit arrangements almost always provide for interest to be charged on outstanding balances, DR 2-101(C)(3) strongly suggests interest can be ethically charged under appropriate circumstances.

[2] Also instructive is N.Y. City 1995-1, where we determined that it would not be improper for a lawyer to enter into a relationship with a third party financing the payment of legal fees: “Implicit in any financing plan is the charging of interest. We conclude that if a financing plan . . . otherwise complies with all ethical rules, the fact the client is charged interest is not in and of itself improper so long as full disclosure of that arrangement is made in advance to the client and the client agrees.

[3] In N.Y. City 1982-6 (see page 2 above), we determined that a lawyer could not unilaterally make prospective changes to a fee arrangement contained in a retainer agreement by written notice to the client. Unlike the first part of that opinion where the Committee focused on the propriety of providing for charging interest in a retainer agreement, in the second part of the opinion, the Committee cast its net much more broadly because a “fee arrangement” – in addition to the charging of interest – captures such diverse subjects as retainers, contingent fees and staffing issues, each of which may implicate different ethical considerations. In determining whether a lawyer could unilaterally alter terms relating to these subjects, we did not address, much less decide, the issue before the Committee here: a lawyer’s ability to charge interest when confronted with a client’s breach of the obligation to pay the lawyer in a timely manner.

[4] See Massachusetts 83-1 (1983) (attorney “may ethically charge interest on unpaid balances for legal services previously rendered whether or not the attorney and client agreed to such charging of interest prior to the rendering of services, provided that the client has notice and a reasonable opportunity to pay the balance due without interest.”); Georgia 45 (1985) (attorney can “comply with EC 2-19 and unilaterally

charge interest without a prior specific agreement with a client if notice is given to the client in advance that interest will be charged on fee bills which become delinquent after a stated period of time, but not less than 30 days "); Rhode Island 98-06 (1998) (lawyers may unilaterally charge interest on unpaid legal fees provided "the client receives advance notice with a reasonable opportunity to pay the balance due without interest "); and North Carolina 98-3 (1998) (lawyer may unilaterally charge interest, but only at the legal rate).

[5] West Virginia 93-02 (1993) ("Because the imposition of a finance charge is a new concept which has the potential to confuse the client even further, fairness to the public mandates voluntary, written client consent at the outset of representation. Requesting a client in the middle of representation to consent to such charges would carry with it the implied threat that the attorney might withdraw. Client consent under such circumstances has the potential to be coerced.").

[6] Arizona 86-9 (1986) ("Absent a written fee agreement or the client's consent after notice with opportunity to bring the account current, interest may not be charged on delinquent invoices.").

[7] See e.g., N.Y. State Bar Association, Statement of Client's Responsibilities ¶ 3 (1998) (as adopted by the Administrative Board of the Courts) ("The client must honor the fee arrangement as agreed to with the lawyer, in accordance with law.")

[8] See also Ruskin, Moscou, Evans & Faltischeck, P.C. v. FGH Realty Credit Corp., 644 N.Y.S. 2d 206, 207 (1<sup>st</sup> Dep't 1996) ("Defendant's receipt and retention of the plaintiff law firm's invoices seeking payment for professional services rendered, without objection within a reasonable time, gave rise to an actionable account stated."); Legum v. Ruthen, 621 N.Y.S.2d 649 (2d Dep't 1995).

[9] Milstein v. Montefiore Club of Buffalo, Inc., 365 N.Y.S.2d 301, 303 (4<sup>th</sup> Dep't 1975) (reversing denial of summary judgment to plaintiff on causes of action for account stated and interest; "[h]aving determined that [plaintiffs] are entitled to summary judgment on the first cause of action [for account stated], it follows that summary judgment also should be granted . . . on the second cause of action [for interest on the balance due]. 'The mere presenting of the bill, if there were nothing more, constituted a sufficient demand to start interest running.'" (quoting Davison v. Klaess, 280 N.Y. at 258.)