Ethics Advisory Opinion Committee

Opinion Number 17-06 (Revised)

Issued August 16, 2018

ISSUES

1. The opinion request involved several issues in the practice of consumer Chapter 7 (liquidation) bankruptcies.[1] The issues discussed also have relevance in lawyer advertising, client conflicts, and unbundling legal services.[2] The issues presented include:

a. Is a lawyer's advertisement of a "$99" or "Zero Down" for a consumer Chapter 7 liquidation bankruptcy misleading under Rule 7.1 of the Utah Rules of Professional Conduct? Is it misleading to advertise that such a price is good for a limited time or that a promotion with this price has been extended?

b. What are the ethical constraints when requesting the client sign a post-petition attorney fee contract which will not be discharged?

c. What disclosures must be made if the lawyer intends to sell the rights to collect the post-petition attorney fee contract to a litigation financing company? Does a relationship with the buyer of the attorney fee contract create a conflict of interest under Rule 1.7 of the Utah Rules of Professional Conduct?

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[1]This response is reflective of information given the Ethics Advisory Opinion Committee (the "**Committee**"). The Committee was not asked to approve a business model nor does it do so. It is up to the individual lawyers concerned to evaluate their business practices with respect to compliance with the Utah Rules of Professional Conduct, and other applicable law, and the guidance given below.

[2] This opinion replaces the prior version of Opinion 2017-06.

d. Are the attorney fees reflected in the post-petition contract reasonable when the attorney sells her rights to those fees at a deep discount under Rule 1.5 of the Utah Rules of Professional Conduct?

OPINION

2. Without providing the consumer further information, advertisement of a "$99" Chapter 7 bankruptcy or a "Zero Down" Chapter 7 bankruptcy is false and misleading under Rule 7.1(a) of the Utah Rules of Professional Conduct because the price refers only to the filing of the initial petition. The price does not include the mandatory filing fee as well as work to be done subsequent to the filing of the petition such as preparation of schedules, meeting of creditors, and reaffirmation agreements. All of these subsequent activities are necessary to obtaining a final discharge of debt which, of course, is the purpose of a consumer bankruptcy. Unless the follow up work is done, the bankruptcy will ultimately be dismissed. The consumer will have wasted both time and money.

3. In connection with the disclosures required under paragraph 2 above to avoid running afoul of Rule 7.1(a) of the Utah Rules of Professional Conduct, an attorney must disclose that her fees for post-petition work will be more substantial and not dischargeable in the consumer bankruptcy. The attorney cannot "unbundle" the filing of the petition unless it is reasonable under the circumstances to do so. Further, no case can be unbundled where prohibited by statute, case law or court rules.

4. While it is not a violation of the Utah Rules of Professional Conduct to sell a lawyer's accounts receivable, the client must be fully informed with respect to the transaction. The client must be offered the same discounted price. The client must consent in writing to the sale and must be informed that the legal fees for post-petition work are not dischargeable. The

lawyer must inform the client that the legal financing company will collect the fee and if there were to be a dispute between the finance company and the client, the lawyer would not represent the client.

5. The fee charged the client (including the finance company discount) must be reasonable. Reasonable fees in consumer bankruptcy are governed by Rule 1.5(a) of the Utah Rules of Professional Conduct.

ANALYSIS

6. The Issues addressed in this Opinion reflect the growing disconnect between individuals of modest means who need legal services and the ability for lawyers to serve those needs without incurring personal financial hardship. The Utah State Bar has long recognized this disconnect. Programs have been established to serve the needs of modest means consumers. Every lawyer has a duty to perform pro bono services. Yet, individuals who need to file Chapter 7 liquidation do so because creditors are garnishing wages or threatening foreclosure. The Utah State Bar cannot reasonably expect that these needs will be met pro bono. Accordingly, it is not sufficient in this Opinion to merely declare practices of the consumer bankruptcy bar to be unethical. Rather, this Opinion is intended as a guide to the consumer bankruptcy bar in order to aid them in serving their clients while avoiding violations of the Utah Rules of Professional Conduct. While this Opinion discusses the consumer bankruptcy bar, the provisions on advertising, unbundling of services where allowed by law, and full disclosure to the clients are applicable to all lawyers.

7. It takes money to do a consumer bankruptcy. There is a substantial filing fee which may be paid in installments. If the filing fee is not paid, the case will be dismissed. In order to get relief from creditors, a petition must be filed with the court. Typically, the low

advertised price refers to the attorney's work in preparation of the petition.[3] Thereafter, there is post-petition work, including filing a schedule of the debtor's affairs, attending a meeting of creditors, and negotiating any affirmation of debt agreements. In the hypothetical given the Committee, the post-petition, attorney fees range from $1,000 to $2,000.[4]

8. Most individuals in Chapter 7 liquidation do not have funds to pay the lawyer for post-petition work that will not be discharged in the bankruptcy.[5] According to the hypothetical, the lawyer informs the client that additional work must be done in order to accomplish the goal of discharged debt. The client has the choice of hiring the filing lawyer, hiring another lawyer, or doing the work themselves as a *pro se* litigant.

9. Pre-petition attorney fees are dischargeable as is any other debt. Post-petition attorney fees are not dischargeable and must be paid even after all other debts are discharged.[6] Care must be taken to include only fees generated post-petition in the post-petition attorney fee contract. Care must also be given to full disclosure of the necessity for further work and the amount to be charged. As individuals in consumer bankruptcy are perhaps hiring a lawyer for

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[3]A representation that speed is needed in filing the initial petition is subject to the duty of diligent representation under Rule 1.3 of the Utah Rules of Professional Conduct. A false representation that speed in filing is needed is precluded as a "false or misleading communication about the lawyer's services" and thus, precluded by Rule 7.1(a) of the Utah Rules of Professional Conduct.

[4]The Committee does not opine on matters of bankruptcy law, as indeed those matters are beyond the scope of the interpretation of the Utah Rules of Professional Conduct. Rule 8.4(d) precludes conduct that is prejudicial to the administration of justice. Utah R. Prof. Cond. 8.4(d). A lawyer must comply with all general and local rules of the bankruptcy court, and this Opinion does not mean to imply or suggest otherwise.

[5]This is a major difference between Chapter 7 liquidation and Chapter 13 reorganization. Legal fees for Chapter 13 may be paid as part of the debtor's plan for reorganization. The lawyer, however, has a duty of competence and diligence under Rule 1.1 and 1.3 to effectively counsel the client as to the risks and benefits of relief under both chapters. It would be a violation of those rules if the lawyer placed the client in Chapter 13 merely to enhance the lawyer's ability to collect his fee. *See* Utah R. Prof. Cond. 1.1 & 1.3.

[6]The Committee expresses no opinion on when a debt might be considered post-petition under applicable bankruptcy law. Such a question goes beyond the interpretation of the Utah Rules of Professional Conduct.

the first time in their lives, the lawyer has a duty of fully informing the client in advance about these matters.

10. The hypothetical given the Committee indicated that a law firm "factoring" company would buy the notes of debtors covering post-petition attorney fee costs at a discount rate on such contracts of thirty percent. In cases of non-payment, the "factoring" company would "gently" pursue payment from the client. The factoring company would have no recourse to the lawyer but would look solely to the client for payment. The hypothetical indicated that a large percentage of Utah Chapter 7 bankruptcies are financed in this manner.

11. A lawyer is allowed to limit the scope of her engagement if the limitation is reasonable under the circumstances and the client gives informed consent.[7] *See* Utah R. Prof. Cond. 1.2(c). Rule 1.5(b) requires that the scope of the representation and the basis or rate of the fee be communicated to the client, "preferably in writing." Utah R. Prof. Cond. 1.5(b). This is particularly applicable when the lawyer agrees to perform only a portion of the services needed to accomplish the goals of a legally unsophisticated client. In *In re Seare,* the Nevada

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[7] "Informed Consent" denotes the agreement by a person to a proposed course of action after the lawyer has communicated adequate information and explanation of the material risks of and reasonably available alternatives to the proposed course of action. *See* Utah R. Prof. Cond. 1.1(f). Further

> when a lawyer and a client or potential client are discussing the scope of a proposed representation, the lawyer usually has superior knowledge about what the scope of the undertaking would be in the absence of a limiting agreement. Accordingly, the lawyer should have the responsibility for identifying and specifying any limitations and should presumptively bear the consequences of any misunderstanding. For this reason, both Rule 1.2(c) and Restatement [of the Law Governing Lawyers] § 19 appropriately require that any limitation on the scope of a representation be reasonable (which is to say not harmful to the client) *and* that the client give informed consent. Thus, the client will have been told about and accepted the risks that are inherent in contracting for limited legal services....

Geoffrey C. Hazard, Jr. , W. William Hodes, Peter R. Jarvis, THE LAW OF LAWYERING § 5.10 (2005-2 Supp.).

bankruptcy court discussed the ethical problems of "unbundling" bankruptcy services at great length and explained, in pertinent part:

> These facts present the legal issue of when consumer bankruptcy attorneys . . . may limit the scope of their representation, a practice colloquially referred to as "unbundling." While unbundling is permissible, it must be done consistent with the rules of ethics and professional responsibility binding on all attorneys. Those rules allow a lawyer to limit his or her representation *only when it is reasonable under the circumstances to do so, and only when the client gives informed consent to the limitation.*

In re Seare, 493 B.R. 158, 176 (Bankr. D. Nev. 2013) (emphasis added). The Committee adopts the discussion in *In re Searle* regarding ethical concerns of unbundling services in bankruptcy that Utah attorneys should consider, as follows:[8]

> Unbundling raises concerns, however. The push to limit representation may come from the attorney, who often benefits from and has superior knowledge of the possible ramifications of excluding certain services.
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> > There are strong reasons for protecting those who entrust vital concerns and confidential information to lawyers. . . . Clients inexperienced in such limitations may well have difficulty understanding important implications of limiting a lawyer's duty. Not every lawyer who will benefit from the limitation can be trusted to explain its costs and benefits fairly. . . . In the long run, moreover, a restriction could become a standard practice that constricts the rights of clients without compensating benefits. The administration of justice may suffer from distrust of the legal system that may result from such a practice. Those reasons support special scrutiny of noncustomary contracts limiting a lawyer's duties, particularly when the lawyer requests the limitation.
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> *Restatement (3d) of Law Governing Lawyers* § 19 (2000).
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> There is a particular concern in consumer bankruptcy practice that attorneys will unbundle services that are essential or fundamental to bankruptcy cases and clients' objectives.

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[8]Of course, should the United States Bankruptcy Court for the District of Utah decide that unbundling of Chapter 7 petitions is not allowed, this opinion relates only to situations in which unbundling is allowed by law. The Committee expresses no opinion as to local Utah bankruptcy rules and law.

> A lawyer walks a perilous path in attempting to limit the services provided to bankruptcy debtors. Making an effective disclosure of the risks of such an arrangement, and obtaining informed consent, may be impossible in some cases. As noted, some lawyer services are so fundamental and essential to effective representation, no amount of disclosure and consent will suffice. Instructing a debtor to "go it alone" in any significant aspect of the bankruptcy case exposes counsel to possible criticism, and worse yet, a potential for sanction.

Hon. Jim D. Pappas, *Simple Solution = Big Problem*, 46 ADVOCATE (IDAHO) 31, 33 (2003).

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In spite of the concerns that unbundling raises, the ABA amended Model Rule 1.2(c) in 2002 to expressly allow limited-scope representation and provide a mechanism to regulate it. [Michele N. Struffolino, *Taking Ltd. Representation to the Limits: The Efficacy of Using Unbundled Legal Servs. in Domestic Relations Matters Involving Litig.*, 2 ST. MARY'S J. LEGAL MAL. & ETHICS 166, 215 (2012) ("Struffolino");] AM. BAR ASS'N, ANNOT. MODEL RULES OF PROF. COND. 38 (2011) ("ANNOTATED RULES"). The ABA's goal was to "encourage attorneys to provide some assistance to low- and moderate-income litigants who could not otherwise afford full representation." [Struffolino, at 215] (citing AM. BAR ASS'N, STANDING COMM. ON THE DELIVERY OF LEGAL SERVS., AN ANALYSIS OF RULES THAT ENABLE LAWYERS TO SERVE PRO SE LITIGANTS 8 (2009)); ANNOTATED RULES 38 (citing AM. BAR ASS'N, LEGISLATIVE HISTORY: THE DEVELOPMENT OF THE ABA MODEL RULES OF PROF. COND., 1982-2005 at 55 (2006)). ABA Model Rule 1.2, which Nevada has adopted verbatim, states that "[a] lawyer may limit the scope of representation if the limitation is *reasonable under the circumstances* and the client gives *informed consent.*" Nev. R. Prof. Cond. 1.2(c) (2011) (emphasis supplied).

Shortly after the ABA amended the rule, the ABA published the *ABA Handbook,* a report on limited scope legal assistance. The *ABA Handbook* emphasizes that the majority of people in our nation are low and moderate income, and that often they cannot afford to pay lawyers in litigation. *Id.*at 3. Limited scope legal representation can make the judicial process fairer by providing greater access to justice. *Id.* at 3-4. The ABA quoted a long time limited-service practitioner for the proposition that unbundling should be client driven—"[i]n this legal relationship, 'the client is in charge of selecting one or several discrete lawyering tasks contained within the full-service package.'" *Id.* at 7 (quoting FORREST S. MOSTEN, UNBUNDLING LEGAL SERVS.: A GUIDE TO DELIVERING LEGAL SERVS. A LA CARTE 1 (2000)).

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> If limited representation is selected, "the lawyer must also alert the client to reasonably related problems and remedies that are beyond the scope of the limited-service agreement." [*ABA Handbook*] at 68. In a related ethics opinion, the Los Angeles County Bar Association put it this way,
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> > The attorney has a duty to alert the client to legal problems which are reasonably apparent, even though they fall outside the scope of retention, and to inform the client that the limitations on the representation create the possible need to obtain additional advice, including advice on issues collateral to representation.
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> *Id.* at 69 (quoting Los Angeles County Bar Ass'n, Prof. Responsibility & Ethics Comm., Ethics Op. 449 (March 1988)).

*In re Sear*le, 493 B.R. at 184-86.

12. A lawyer should not automatically assume that "unbundling" the filing of a petition is reasonable under the circumstances of the case. Indeed, propriety of unbundling a petition may be the *exception rather than the usual practice*.[9] Recent bankruptcy ethics cases demonstrate the concerns of the bankruptcy courts. In *In re Seare,* the majority of the client's unsecured debt was a judgment for fraud. 493 B.R. at 171. The lawyer failed to investigate the nature of the judgment and thus failed to learn that this debt was non-dischargeable. *Id.* at 190-91. He then filed an unbundled and worthless Chapter 7 petition. *Id.* at 173. The attorney was

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[9] The Committee recommends careful consideration of Justice O'Connor's warning concerning flat fees in "simple" cases:

> Until one becomes familiar with a client's particular problems, there is simply no way to know that one is dealing with a 'routine' divorce or bankruptcy. Such an advertisement is therefore inherently misleading if it fails to inform potential clients that they are not necessarily qualified to decide whether their own apparently simple problems can be handled by 'routine' legal services. Furthermore, such advertising practices will undermine professional standards if the attorney accepts the economic risks of offering fixed rates for solving apparently simple problems that will sometimes prove not to be so simple after all.

Shapiro v. Kentucky Bar Ass'n, 486 U.S. 466, 485-86 (1988).

required to disgorge all fees and present a copy of the court's opinion to any future client when the attorney proposed to unbundle the filing of a petition. *Id.* at 224-27.

13. *In re Minardi*, 399 B.R. 841 (Bankr. N.D. Okla. 2009), concerned a lawyer's attempt to limit services to exclude negotiation of reaffirmation agreements. *Id.* at 843. The court found that the "decision to reaffirm an otherwise dischargeable debt plays a critical role in the bankruptcy process—so critical, that assistance with the decision must be counted among the necessary services that make up competent representation of a Chapter 7 debtor." *Id.* at 848. Particularly, the court explained that an agreement for limited representation does not exempt a lawyer from the duty to provide competent representation. *Id.* at 849-52.

14. The Idaho bankruptcy court provides that "'an attorney, in accepting an engagement to represent a debtor in a bankruptcy case, will find it exceedingly difficult to show that he properly contracts away any of the fundamental and core obligations such an engagement necessarily imposes. Proving competent, intelligent, informed, and knowing consent of the debtor to waive or limit such services inherent to the engagement will be required.'" *In re Grimmett*, 2017 WL 2437231, 2017 Bankr. LEXIS 1492, at *15 (Bankr. D. Idaho June 5, 2017) (quoting *In re Castorena*, 270 B.R. 504 , 530 (Bankr. D. Idaho 2001)).

15. If a consumer bankruptcy lawyer presents unbundled legal services, she must comply with Rule 7.1's limitations on false or misleading communications. A representation is false or misleading if it "contains a material misrepresentation of fact or law, or omits a fact necessary to make the statement considered as a whole not materially misleading." Utah R. Prof. Cond. 7.1(a). It would be materially misleading if a bankruptcy lawyer unbundled services and did not explain in detail, preferably in writing, what additional services would be needed to accomplish the client's goal. Just as in *Seare*, it would not be sufficient to remain silent when it

is well known that an adversary proceeding is likely to occur. Further, statements indicating that the one-time fee is "for a limited time" or has "been held over" are misleading[10] if not accurate.

16. It is not unlawful for lawyers to sell or encumber their accounts receivable, whether or not the work has been accomplished. Sale or encumbrance of accounts receivable is not sharing fees with a non-lawyer. Utah R. Prof. Cond. 5.4(a). This is equally true for consumer bankruptcy lawyers. As the Texas Court of Appeals explained in *Counsel Financial Services v. Leibowitz*:

> The main thrust of Leibowitz's argument is that loans such as those at issue in this case fundamentally violate public policy as articulated in the disciplinary rules, which as a general rule prohibit lawyers from sharing legal fees with non-lawyers. However, Texas case law allows an attorney to assign accounts receivable, consisting of consisting of current or future, earned or unearned, attorney fees as property securing a transaction. Moreover . . . there is a significant difference between sharing legal fees with a non-lawyer and paying a debt with legal fees.

2013 WL 3895317, 2013 Tex. App. LEXIS 9252, at *27-28 (Tex. Ct. App. 13th Dist. July 25, 2013)(citations omitted).

17. There are a number of potential pitfalls, however, in litigation funding. All of these pitfalls must be discussed with the client. Because of a regular relationship with the funding company, the possibility of a current conflict of interest between the lawyer's interest, the client's interest and the interest of the funding company in being paid, the lawyer must

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[10] Those statements may be unlawful under the Utah Consumer Sales Practices Act, Utah Code Ann. § 13-11-1, *et seq.* The Utah Consumer Sales Practices Act provides that it is a deceptive act to knowingly or intentionally indicating the subject of a consumer transaction is available to the consumer for a reason that does not exist, such as "going out of business" or lost our lease," when those statements are not true. *Id.* § 13-11-4(2)(d). A lawyer who makes false statements about a certain fee being available for only a limited time is guilty of misconduct pursuant to Rule 8.4 of the Utah Rules of Professional Conduct. By making such false statements, the lawyer engages in conduct involving dishonesty, fraud, deceit or misrepresentation.

comply with Rule 1.6(b) of the Utah Rules of Professional Conduct. The client must give informed consent, confirmed in writing, when waiving any such conflicts.

18. The lawyer has but one client and must maintain confidentiality and loyalty towards that client. "Although litigation funding companies are not subject to lawyers' rules of professional conduct, the lawyers whose clients receive funding are." Geoffrey Hazard, W. William Hodes & Peter Jarvis, THE LAW OF LAWYERING § 8.26 (2014 Supp.). Chief among the pitfalls are client confidentiality and protecting the independence of the attorney. Further we call attention to Utah Ethics Advisory Opinion 13-05 which discusses the extent to which a lawyer may involve herself in helping the client apply for financial assistance.

19. Finally, the hypothetical raises questions as to the reasonableness of the consumer bankruptcy lawyer's fees. If the lawyer is willing to do the work with a thirty percent discount, we question, but do not resolve, whether the total fee is reasonable.[11] There are, however, guidelines. The consumer bankruptcy lawyer, like all other lawyers, is subject to the reasonable fee provisions of Rule 1.5 of the Utah Rules of Professional Conduct, which is determined by the time and labor required, the novelty and difficulty of the questions involved, and the skill required to perform the legal services properly. Other factors include the likelihood that accepting the matter would preclude taking other employment by the lawyer. A reasonable fee might be the fee customarily charged in the locality for similar services. Finally, the reasonableness of a fee depends upon the experience, reputation and ability of the lawyer performing the service.

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[11] Other bankruptcy attorneys claim that in cases of financed Chapter 7 bankruptcies, the financing lawyer increases his fee by as much as 50% to 184%. This Opinion should not be read as indicating approval of such price increases. Indeed, such price increases may implicate Rule 1.7(a)(2) of the Utah Rules of Professional Conduct, in that the representation of a client might be adversely impacted by the personal interest of the lawyer.