NEW YORK STATE BAR ASSOCIATION

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COMMITTEE ON PROFESSIONAL ETHICS

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Via email to jdrohan@dlkny.com and matt.feinberg@yahoo.com

Jacqueline Drohan and Matthew Feinberg, Co-Chairs of the Task Force on Emerging Digital Finance and Currency

Dear Jacqueline and Matthew:

I provide comments on behalf of the New York State Bar Association Professional Ethics Committee. The Report and Recommendations of the Task Force on Emerging Digital Finance and Currency was distributed to our Committee. In light of our Committee's charter, we focused solely on the sections that deal with the New York Rules of Professional Conduct. We offer the following comments:

In Article 6, the report raises three ethical issues: (1) whether an advance payment of fees in cryptocurrency must be placed in the attorney's trust account, (2) whether a payment in crypto might be deemed a business transaction with a client subject to Rule 1.8(a), and (3) whether a payment in cryptocurrency might be deemed to be an excessive fee if the value of the crypto increases.

Advance Payment of Fees

With regard to advance payment of fees, the report cites ABA 505 (2023), Nebraska Opinion 17-03 and Maryland Opinion 2022-01, all of which identify as a problem the inability to custodize cryptocurrency in an attorney trust account. The ethical rules in these jurisdictions differ from those in New York. The general rule in New York is set forth in Rule 1.5, Cmt. [4]: "A lawyer may require advance payment of a fee, but is obliged to return any unearned portion."

This rule has been explained in several opinions issued by our Committee, issued under both the Former Code of Professional Responsibility and the current Rules.

In N.Y. State 983 (2013), we opined that a lawyer may retain the unearned portion of a prior retainer on conclusion of a matter, at the client's request, as advance payment of fees for future legal services and that such advance payment may be treated as client-owned funds depending on what is agreed with client. We noted that under our opinions, the parties may choose one of two options. One option is to treat advance payment of legal fees as *client funds*, in which case the lawyer must deposit the advance payment into an escrow/trust account. Alternatively, the

parties may agree to treat advance payment of fees as the *lawyer's own*. Under this second option, the lawyer may use the money as the lawyer chooses (except that the lawyer may not deposit it in a client trust account), subject only to the requirement that any unearned fee paid in advance be promptly refunded to the client upon termination of the employment.

In N.Y. State 816 (2007), we observed that a lawyer may ethically accept an advance payment retainer, place such funds in the lawyer's own account, and retain any interest earned.

In N.Y. State 570 (1985), we observed that fees paid to a lawyer in advance of services rendered are not necessarily client funds and need not be deposited in a client trust account. Therefore, any interest earned on these fee advances may be retained by the lawyer. However, the lawyer is obliged to return any portion of the fee advance that is not earned during the representation. "Absent an agreement to treat an advance fee payment as client property, it would be inappropriate for the lawyer to deposit advance fees in a client trust account, as this would constitute commingling." In other words, the default position in New York is that advance payment fees are treated as the lawyer's property and thus, absent agreement otherwise with the client (to treat such funds as the client's funds), ***should not be placed in an attorney trust account***. It follows that New York does not require or even permit an advance payment in cryptocurrency to be placed into an attorney trust account unless the client requires it.

Accepting property in payment of legal fees, including the issue of excessive fees

This topic is covered in Rule 1.5, Cmt [4]: "A lawyer may accept property in payment for services, such as an ownership interest in an enterprise, providing this does not involve acquisition of a proprietary interest in the cause of action or subject matter of the litigation contrary to Rule 1.8(i). A fee paid in property instead of money may, however, be subject to the requirements of Rule 1.8(a), because such fees often have the essential qualities of a business transaction with the client."

Whether property used to pay legal fees may be deemed excessive is discussed in Rule 1.8, Cmt. [4F]:

> [4F] A lawyer must also consider whether accepting securities in a client corporation as payment for legal services constitutes charging or collecting an unreasonable or excessive fee in violation of Rule 1.5. Determining whether a fee accepted in the form of securities is unreasonable or excessive requires a determination of the value of the securities at the time the agreement is reached and may require the lawyer to engage the services of an investment professional to appraise the value of the securities to be given. The lawyer and client can then make their own advised decisions as to whether the securities-for-fees exchange results in a reasonable fee.

This Committee has issued opinions on accepting an interest in property in payment of legal fees, especially in the context of payment in stock. In the following opinions, we analyzed the practice as a business transaction with a client.

In N.Y. State 990 (2013), we held that a lawyer may accept stock in Client B as all or part of the fee in the matter as long as the lawyer determines that the fee is not excessive for the work performed by the lawyer, the terms of the transaction are fair and reasonable to Client B, Client B is advised in writing of the desirability of seeking the advice of independent legal counsel and is given a reasonable chance to do so, and Client B signs a writing that describes the transaction and the lawyer's role in the deal, including whether the lawyer is acting for the client in the acquisition of the stock.

In N.Y. State 913 (2012), we found that a lawyer may accept an equity interest in a client if the lawyer complies with Rule 1.8(a) governing business transactions with clients and the acceptance does not otherwise create a conflict for the lawyer or result in an excessive fee. We concluded that Rule 1.8(a) applies to negotiation of a fee in which a lawyer is to receive an equity interest in a client or the client's company. Comment [4C] accompanying Rule 1.8(a) says in relevant part: "This Rule also does not apply to ordinary fee arrangements between client and lawyer reached at the inception of the client-lawyer relationship, which are governed by Rule 1.5. The requirements of the Rule ordinarily must be met, however, when the lawyer accepts an interest in the client's business or other nonmonetary property as payment of all or part of the lawyer's fee."

Recommendations

Article 6 of the Report, on page 114, recommends that the Association provide guidance as to whether attorneys can accept crypto as advanced payment for legal services. Our Committee does not issue many *sua sponte* opinions because we believe our opinions are most useful when informed by facts presented by a specific inquirer asking about the inquirer's own proposed conduct. Among the benefits of having a specific inquirer, we can dialogue with such inquirer in order to clarify facts and motivations. We expect that relevant inquiries will provide us with the opportunity to provide guidance in this evolving area and look forward to offering guidance where we can.

Sincerely,

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Chair