Just Say No to Arranging Credit for Potential Clients

By Josh Ard

FAST FACTS

Apart from the ethical implications, lawyers who get involved in arranging credit for clients run the risk of creating liability for themselves under various state and federal laws.

Definitions of credit can be very broad, especially under the Equal Credit Opportunity Act.

Accepting credit cards is fine, and it is probably fine to have brochures from lenders in your office. But problems occur when a lawyer takes a more active role in the process.

In trying economic times such as the Great Recession and its aftermath, many potential clients find it difficult to generate the funds to pay legal fees. Some potential sources, such as a home loan, are harder to obtain as property values have plummeted, leaving many owners with no equity to use as collateral. A lawyer might readily think, "Hmm…maybe if I get involved in finding credit for clients and potential clients, I'll get more billings." But for most purposes, lawyers should "just say no" when this thought crosses their minds.

There are a number of problems with this approach. First, there is the obvious ethical question: does helping clients find credit to pay for legal services violate the Michigan Rules of Professional Conduct? Proposed arrangements almost always violate one or more of the subparts of MRPC 1.8—Conflict of Interest: Prohibited

Transactions. For example, a lawyer who directly provides credit[1] violates MRPC 1.8, which states that:

> [a] lawyer shall not provide financial assistance to a client in connection with pending or contemplated litigation, except that
>
> (1) a lawyer may advance court costs and expenses of litigation, the repayment of which shall ultimately be the responsibility of the client; and
>
> (2) a lawyer representing an indigent client may pay court costs and expenses of litigation on behalf of the client.[2]

But what if the lawyer does not technically act as lender but is deeply involved in the credit transaction by helping the client find or qualify for credit? Unfortunately, this arrangement could still violate ethics rules. Michigan Ethics Opinion RI-168 considers a situation in which a lawyer arranges for a client to pay for legal services by a credit card.[3] Guidance is given for avoiding ethical problems under MRPC 1.5(a), 1.6, 1.7, 1.8(a), and 1.15(a) and (b). Ethics Opinion RI-336 addresses a different situation in which the lawyer borrows funds from a third-party lender to finance contingency fee lawsuits.[4] The opinion gives guidance about avoiding issues under MRPC 1.6, 1.8(e), and 5.4(c). The New York City Bar raised other ethical issues in third-party funding of contingency fee lawsuits in Formal Opinion 2011-2,[5] although the opinion, like the Michigan opinion, says this can be done without violating ethics rules.

Clients obviously have risks if they engage in litigation financing; whether they choose to do so and how they should choose a lender are important questions, but are beyond the scope of this article. The primary purpose of this article is to warn Michigan lawyers that ethical violations are far from the only risks involved in helping clients find credit to pay for legal services. Apart from the ethical implications, lawyers who get involved in credit matters run the risk of creating liability for themselves under various other laws.[6] While there may not be a definite violation of the law in the brief examples that follow, the examples should help you appreciate the possible legal risks associated with such a practice.

Consider the following arrangement. Suppose Lawyer Larry forms a partnership with a lender. Clients write four checks to Larry to pay the cost of representation. Check 2 is post-dated by two months, check 3 by four months, and check 4 by six months. The agreement states that no check will be presented for payment until the date on the check, giving the client plenty of time to come up with the funds. Each check is for more than Larry would normally charge,[7] with the difference reflecting the fee for the right to pay later. Larry endorses the checks over to the lender,[8] which immediately gives Larry the amount he ordinarily bills minus the fee. The lender then follows the agreement for when to present the checks for payment.

Aside from any ethical issues with this practice, Larry and his partner are probably engaging in deferred presentment service transactions,[9] an action regulated under Act 244 of 2005—the Deferred Presentment Service Transaction Act.[10] This act legalizes and regulates what is commonly known as payday lending. Entities offering these services must be licensed by the state. Additional requirements include giving special notices, providing required documentation, and determining whether the customer has more than one outstanding deferred presentment service transaction. According to MCL 487.2168:

> if the commissioner finds that a person has violated this act and that the person knew or should reasonably have known that he or she was in violation of this act, the commissioner may order the person to pay a civil fine of not less than $5,000.00 or more than $50,000.00 for each violation.[11]

Care to guess whether a licensed attorney should have known the law?

Even less involvement in credit can create great liability under federal law. Consider the Equal Credit Opportunity Act[12] and the accompanying Code of Federal Regulations.[13] This is essentially a civil rights act for credit and applies to business and consumer credit. There are numerous prohibited bases for making credit decisions under this act, given how broadly it is defined:

> Prohibited basis means race, color, religion, national origin, sex, marital status, or age (provided that the applicant has the capacity to enter into a binding contract); the fact that all or part of the applicant's income derives from any public assistance program; or the fact that the applicant has in good faith exercised any right under the Consumer Credit Protection Act or any state law upon which an exemption has been granted by the Board.[14]

We don't want people who are not trained in the law to offer legal advice. Similarly, lawyers should leave credit matters to others who are licensed in those areas.

What's more, for most purposes of the act, it applies to "a person who, in the ordinary course of business, regularly refers applicants or prospective applicants to creditors…."[15]

Now imagine that Lawyer Lois and Lawyer Linda both refer potential clients to Lucifer Lending, a service that provides credit to pay legal fees. Lois represents personal-injury plaintiffs. Lucifer Lending has told her it will not front costs for clients older than 70 because too many of them die before their debts are paid. So Lois never refers potential clients over the age of 70 to Lucifer Lending.

Linda has observed that non-native speakers of English often don't relate well with juries in her rural county. After interviewing potential clients, if Linda feels that their English is a problem, she discourages litigation and never refers them to Lucifer Lending.

In this example, both Lois and Linda are at risk of being sued under the Equal Credit Opportunity Act. Under the act, a prevailing plaintiff can win costs, attorney fees, and statutory damages of up to $10,000 even if no actual damages can be proven. It is illegal to discriminate against applicants or potential applicants 62 or over. Although Lois did not create Lucifer Lending's policy, she is acting to further it. That's enough to expose her to liability.

Linda's case is perhaps more complicated. It is not a violation for Linda to tell clients the tough truth about litigation as she understands it. She can validly say that, in her opinion, poor English skills decrease a litigant's chance of success. She can further discourage clients from pursuing litigation. The problem arises when she uses that reasoning in a credit decision. The litigants could use their national origin as the basis for liability under the act. Linda could try to separate legal counseling from credit activities, but the distinction could be very tricky for unsophisticated clients, especially clients with less than perfect English proficiency. Simply put, Linda—or any lawyer—probably doesn't want to take that risk.

A more extreme example would be Lawyer Louie, who normally bills later for service but demands immediate payment from unmarried persons. The decision to send a bill later is incidental credit, and making the decision on a prohibited basis would expose Louie to charges under the act.[16]

In summary, there are numerous reasons why a lawyer should not get involved in offering credit to clients. Legal and ethical issues abound. Accepting credit cards is fine, and it is probably fine to have brochures from lenders in your office. But problems occur when a lawyer takes a more active role in the process. It might be tempting in tough economic times, but it is simply not worth the risk. We don't want people who are not trained in the law to offer legal advice. Similarly, lawyers should leave credit matters to others who are licensed in those areas. ■

Josh Ard is former chair of the Elder Law and Disability Rights Section, the Consumer Law Section, and the Unauthorized Practice of Law Committee. He is also a member of the Representative Assembly, the Probate and Estate Planning Section Council, and the Ethics Committee. The opinions expressed in this article are solely those of the author.

FOOTNOTES

1. Note that what counts as credit varies depending on the statute or regulation. The standard practice of giving a client a bill some time after services are provided and expecting payment some time after that is not considered credit for most purposes. It certainly doesn't violate MRPC 1.8, and it doesn't constitute credit for purposes of the Truth in Lending Act. It is incidental credit, however, for purposes of the Equal Credit Opportunity Act, as will be discussed later in this article.
2. MRPC 1.8(e).
3. Michigan Ethics Opinion RI-168, available at <http://www.michbar.org/opinions/ethics/numbered_opinions/ri-168.cfm>. All websites cited in this article were accessed February 23, 2013.
4. Michigan Ethics Opinion RI-336, available at <http://www.michbar.org/opinions/ethics/numbered_opinions/ri-336.cfm?CFID=24836158&CFTOKEN=50035451>.
5. New York Ethics Opinion 2011-02, available at <http://www.nycbar.org/index.php/ethics/ethics-opinions-local/2011-opinions/1159-formal-opinion-2011-02>.
6. Simply accepting credit cards for payments is relatively safe. See Michigan Ethics Opinion RI-344. Also, accepting credit cards for payment does not make a lawyer a creditor under federal laws. See 15 USC 1691 *et seq.*
7. To avoid particular ethical issues, assume the facts are all correctly disclosed to the client beforehand.
8. This discussion, like others in this article, does not involve direct financing by the lawyer but merely involvement with financing provided by others. A lawyer could directly offer deferred presentment services—"pay a higher fee for the promise that I will not cash your checks until the date written on them." The lawyer would presumably be a deferred presentment service provider subject to the act. The lawyer would face more ethical challenges in disclosures and business conflicts and would also bear the risk if the client did not have sufficient funds in his or her account at the time of presentment. Taking actions to collect after such a default creates additional ethical and legal risks.
9. A deferred presentment service transaction is a transaction between a licensee and a customer under which the licensee agrees to pay the customer an agreed-upon amount in exchange for a fee and hold a customer's check for a period before negotiation, redemption, or presentment. MCL 487.2122(g).
10. MCL 487.2121 *et seq.*
11. MCL 487.2168(1).
12. 15 USC 1691 *et seq.*
13. 12 CFR 202.1 *et seq.*
14. 12 CFR 202.2(z).
15. 12 CFR 202.2(l).
16. Please note that to be a creditor subject to the act, Louie must regularly offer credit, which by regulation is more than 25 times a year for most types of credit. 12 CFR 1026.2(a)(17)(v).