

STATE BAR OF NEVADA
STANDING COMMITTEE ON
ETHICS AND PROFESSIONAL RESPONSIBILITY

Formal Opinion No. 37
February 1, 2007

QUESTION

May an attorney take a security interest in a client's real property to secure payment for the attorney's fees?

ANSWER

Yes, so long as the attorney complies with S.C.R. 158(1). S.C.R. 158(1) allows an attorney to acquire an interest adverse to a client, including a security interest in a client's real property to secure the payment of the attorney's fee, but only if: (1) the transaction is fair and reasonable to the client; (2) the terms of the transaction are fully disclosed to the client in writing in a manner the client can understand; (3) the client is given a reasonable opportunity to obtain the advice of independent counsel; and (4) the client consents in writing. Such transactions are disfavored by the courts. Consequently, the court will presume that the transaction is improper and places the burden upon the lawyer to prove, by clear and satisfactory evidence, that he or she complied with each of the requirements imposed by S.C.R. 158(1).

AUTHORITIES

In re Discipline of Singer, 109 Nev. 1117, 865 P.2d 315 (1993).

Hawk v. State Bar of California, 754 P.2d 1096 (Cal. 1988).

In re Snyder, 35 S.W.3d 380 (Mo. 2000).

Petit-Clair v. Nelson, 782 A.2d 960 (N.J. Super. Ct. App. Div. 2001).

Nevada Supreme Court Rules 155(1), 157(2), and 158(1).

Connecticut Bar Ass'n Committee on Professional Ethics, *Taking a Security Interest in Client Property to Protect Fees*, Informal Op. No. 97-4 (March 4, 1997).

District of Columbia Bar, *Acceptance of Ownership Interest in Lieu of Legal Fees*, Formal Op. No. 300 (July 25, 2000).

Los Angeles County Bar Ass'n Professional Responsibility and Ethics Committee, Formal Op. No. 492 (Jan. 26, 1998).

Bare, Rob W., "Top 10 Bar Complaints and How to Avoid Them," *Nevada Lawyer* (June 2005).

DISCUSSION

The following opinion considers the ethical issues encountered by a lawyer who desires to take a security interest in a client's real property to secure payment of his fees. The opinion does not discuss the propriety of an attorney accepting as a legal fee something other than money.¹

The answer to the question posed in this opinion depends upon whether accepting a security interest in a client's property to secure an attorney's fee constitutes the acquisition of an interest adverse to the client which is governed by S.C.R. 158(1). The Committee concludes that it does.

S.C.R. 158(1) places restrictions on an attorney's ability to enter into transactions with a client. The rationale for the restrictions contained in S.C.R. 158(1) is the temptation for a lawyer to "temper his or her loyalty to a client where the attorneys' own financial interests are involved."² Specifically, S.C.R. 158(1) provides:

A lawyer shall not enter into a business transaction with a client or knowingly acquire an ownership, possessory, security or other pecuniary interest adverse to a client unless:

- (a) The transaction and terms of which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing to the client in the manner which can be reasonably understood by the client;
- (b) The client is given a reasonable opportunity to seek the advice of independent counsel in the transaction; and
- (c) The client consents in writing.

Accordingly, whether an attorney must comply with the requirements of S.C.R. 158(1) depends upon whether the acceptance of a security interest in a client's real property constitutes the acquisition of an interest adverse to the client.

¹ See Bare, Rob W., "Top 10 Bar Complaints and How to Avoid Them," *Nevada Lawyer* at 27 (June 2005) (noting that it is Bar Counsel's opinion that the acceptance of something other than money to satisfy an attorney's fee is governed by S.C.R. 158(1)); see also District of Columbia Bar, *Acceptance of Ownership Interest in Lieu of Legal Fees*, Formal Op. No. 300 (July 25, 2000) (recognizing that the acceptance of an ownership interest in a corporate client in lieu of an attorney's fee is governed by Rules of Professional Conduct 1.5, 1.7(b), (c), & 1.8(a)); S.C.R. 155(1), 157(2), 158(1).

² *In re Discipline of Singer*, 109 Nev. 1117, 1120, 865 P.2d 315, 317 (1993).

In *Hawk v. State Bar of California*, the California Supreme Court squarely addressed this issue and held that the acceptance of a security interest in a client's real property constituted an acquisition of an interest adverse to the client.³ In *Hawk*, an attorney accepted two notes secured by deeds of trust on his client's real property without fully disclosing the terms of the transaction in a manner that could be understood by the clients. When the client was unable to sell the property to satisfy the notes, the attorney assigned the notes to a third party who foreclosed on the client's property.

The California Supreme Court concluded "that an attorney who secures payment of fees by acquiring a note secured by a deed of trust in the client's property has acquired an interest adverse to the client."⁴ The court began its analysis by noting that *all* transactions between a lawyer and client are suspect and will be closely scrutinized for any unfairness.⁵ The court reasoned that a note secured by a deed of trust to secure the payment of fees gives the lawyer a present interest in the client's property because the lawyer can "summarily extinguish" the client's interest in the property through non-judicial foreclosure, without giving the client an opportunity to dispute the fees.⁶ The court contrasted this with an unsecured promissory note, which would require an attorney to obtain a judgment through a contested judicial proceeding during which the client could contest the fees.⁷ Accordingly, in California, to avoid discipline an attorney may accept a security interest in a client's real property only by satisfying the safeguards set forth in the rules of professional conduct.⁸ As such, the California Supreme Court upheld the four-year suspension imposed on an attorney for failing to comply with the California equivalent of S.C.R. 158(1).

Although the California Supreme Court based its reasoning upon the attorney's ability to summarily extinguish the client's interest in the property, other courts have concluded that the attorney must comply with their state's version of S.C.R. 158(1), even if the attorney seeks foreclosure through judicial action. For example, in *Petit-Clair v. Nelson*, an attorney representing two corporations in litigation obtained a mortgage on the personal residence of the president and secretary of the corporate clients to secure the payment of the attorney's fees.⁹ The attorney did not advise the president and secretary to seek the advice of independent counsel, as required by New Jersey's version of S.C.R. 158(1). When the clients defaulted, the attorney

³ 754 P.2d 1096 (Cal. 1988).

⁴ *Id.* at 1103.

⁵ *Id.* at 1101.

⁶ *Id.* at 1102.

⁷ *Id.*

⁸ *See id.* at 1103; *see also* Los Angeles County Bar Ass'n Professional Responsibility and Ethics Committee, Formal Opinion No. 492 (Jan. 26, 1998) (noting that an attorney must comply with the safeguards imposed by the rules of professional conduct when accepting a security interest in real property to ensure payment of fees by a client when the attorney knows that the client has an interest in the property).

⁹ 782 A.2d 960 (N.J. Super. Ct. App. Div. 2001).

filed a complaint seeking to foreclose upon the property. The trial court set aside the mortgage and the appellate court affirmed.

Like the California Supreme Court's opinion in *Hawk*, the court noted that "[a]ny transaction between an attorney and client is 'subject to close scrutiny and the burden of establishing fairness and equity of the transaction rests upon the attorney.'"¹⁰ The court determined that the mortgage obtained by the attorney was clearly a security interest adverse to the clients, which would require the attorney to comply with the safeguards set forth in New Jersey's version of S.C.R. 158(1).¹¹ Because the attorney failed to advise the clients to retain independent counsel, the court affirmed the decision to void the mortgage.¹²

Nevada Supreme Court precedent is consistent with the decisions in *Hawk* and *Petit-Clair*. Specifically, the Court's opinion in *In re Discipline of Singer* comprehensively applies S.C.R. 158(1) to "all personal financial interests" between a lawyer and client and holds that all such transactions will be carefully scrutinized for "any unfairness on the part of the attorney."¹³ The Court stated that there is a strong "presumption of impropriety" in "any transaction in which an attorney is charged with obtaining a business advantage from a client" and held that this presumption may only be overcome by "clear and satisfactory evidence that the transaction was fundamentally fair, free of professional overreaching, and fully disclosed."¹⁴ Rule 158(1) requires the attorney to "ensure that the client has independent advice in the matter or is given the same information as would have been given by a disinterested attorney."¹⁵ "Technical compliance" with S.C.R. 158(1) will not shield an attorney from discipline.¹⁶

Based upon the Supreme Court's language in *Singer* that the Court will scrutinize all transactions between an attorney and client, it is the Committee's opinion that an attorney may accept a security interest in a client's real property only after complying with the requirements set forth in S.C.R. 158(1). However, because of the strong presumption of impropriety, and the requirement for the attorney to prove, by clear and satisfactory evidence, that the transaction was "fundamentally fair, free of professional overreaching, and fully disclosed," such transactions are

¹⁰ *Id.* at 961.

¹¹ *Id.* at 963; accord *In re Snyder*, 35 S.W.3d 380 (Mo. 2000) (indefinitely suspending an attorney for, among other things, accepting a security interest in client's property to secure the payment of fees without following the safeguards set forth in Missouri's version of S.C.R. 158(1)); Conn. Bar Ass'n Committee on Professional Ethics, *Taking a Security Interest in Client Property to Protect Fees*, Informal Op. No. 97-4 (March 4, 1997) (concluding that Connecticut's version of S.C.R. 158(1) applies to an attorney's "acquisition of a security interest taken in client property to secure payment of a fee").

¹² *Id.*

¹³ 109 Nev. 1117, 1120, 865 P.2d 315, 317 (1993) (emphasis added).

¹⁴ *Id.* at 1120–21, 865 P.2d at 317 (emphasis added).

¹⁵ *Id.* at 1121, 865 P.2d at 317.

¹⁶ *Id.*

not advisable. In addition, should an attorney enter into such a transaction, he or she must be mindful that subsequent events could create a situation where the attorney's representation of the client is materially limited by his own interests, which would violate S.C.R. 157(2). Further, if the real property is the subject matter of the litigation, S.C.R. 158(10) further limits an attorney's ability to enter into such a transaction.

This opinion is issued by the Standing Committee on Ethics and Professional Responsibility of the State Bar of Nevada, pursuant to S.C.R. 225. It is advisory only. It is not binding upon the courts, the State Bar of Nevada, its Board of Governors, any person or tribunal charged with regulatory responsibilities, or any member of the State Bar.