New York County Lawyers Association

Committee on Professional Ethics

Formal Opinion 753[1]

TOPIC: Disbursement of IOLA Funds to Third Party

DIGEST: A lawyer must direct funds or other property in the lawyer's possession to the client or a third party who is entitled to receive the funds or property. Unless a third party is entitled to funds awarded to a client, a lawyer may send such funds to the third party only if the client directs the transfer and the lawyer does not know that the transfer will assist the client in committing a crime or fraud. The lawyer is not required to comply with the client's request in this circumstance, and may not do so if the transfer would assist the client in committing a crime or fraud. The lawyer must assess whether the information he or she possesses requires further inquiry into the ethical propriety of the client's request to direct the funds to a third party. If further inquiry is warranted, and the inquiry reveals that the client is engaging in a crime or fraud and seeking the lawyer's unwitting participation, the lawyer may terminate the representation if the client will persist in conduct involving the lawyer's services that the lawyer reasonably believes is criminal or fraudulent, and must do so if continuing the representation will result in a violation of the Rules of Professional Conduct or of law. To withdraw, the lawyer must first seek permission of the tribunal (if any) in which the lawyers represents the client if required by the tribunal's rules, and then must take steps to avoid any foreseeable prejudice to the client, which includes returning to the client all funds or other property to which the client is entitled.

RULES OF PROFESSIONAL CONDUCT: 1.0(k), 1.1, 1.2(d), 1.15(c)(4), 1.16(c)(2), 1.16(b)(1), 1.16(d), 1.16(e), 8.4(b, c)

OPINION

1. A lawyer had funds in his IOLA account that his client was entitled to receive. The client requested that rather than receiving the funds directly, the funds be directed to a third party instead. The lawyer believes that the client has requested the funds be sent to a third party in order to avoid creditors or tax consequences from receipt of the funds directly, and questions the ethical propriety of following the client's request.

2. Rule 1.15(c)(4) in the NY Rules of Professional Conduct (the "Rules") provides that "[a] lawyer shall...(4) promptly pay or deliver to the client or third person as requested by the client or third person the funds, securities, or other properties in the possession of the lawyer that the client or third person is entitled to receive." The Rule authorizes the lawyer to send the funds to a third party who would not otherwise be entitled to them at the client's request. But prior opinions in New York and other jurisdictions have not addressed whether a lawyer may comply with a client's direction to send funds to a third party who is not entitled to the funds where the lawyer suspects an improper purpose behind the redirection to a third party. N.Y. State 717(1999); *see, e.g.,* Va. Legal Eth. Op. 1865 (2012); Or. Formal Op. 2005-52 (2005); Fl. Eth. Op. 02-4 (2002); D.C. Bar Op. 283 (2000); D.C. Bar Op. 251 (1994); AK Eth. Op. 92-3 (1992);

[1] Approved for publication on May 4, 2020.

see also Tx. Ctr. Legal Eth. Op. 681 (observing duty to disburse funds to third parties who have "a matured legal and equitable interest," and also noting that this duty survives termination of the lawyer-client relationship). Notably, these opinions did not address a lawyer's obligation to comply with a client's instruction to send funds to a third party where the lawyer suspects an improper purpose behind the redirection to a third party. A lawyer "shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is illegal or fraudulent except that the lawyer may discuss the legal consequences of any proposed course of conduct with a client." Rule 1.2(d). In addition, a lawyer should advise the client regarding the lawfulness of a proposed transaction, and is forbidden from assisting the client in conduct the lawyer knows to be fraudulent or illegal. Rules 1.1.

3. In N.Y. State Opinion 717 (1999), the New York State Bar's Committee on Professional Ethics ("State Bar Committee") concluded that a plaintiff's attorney should pay the holder of a valid lien from the settlement proceeds, and only withhold disputed funds if the client disputes the amount or validity of the lien. In Opinion 717, the legend of the settlement check stated the payment was "for treatment or services," and the lawyer's research revealed that two of the five medical providers who treated the client had outstanding liens against the client. The State Bar Committee first noted the lawyer's obligation to notify the client and holders of valid liens when a check is received, citing DR 9-102(C)(1) (the predecessor to Rule 1.15(c)(1)). The attorney has a further duty to "make a reasonable effort to ascertain whether the [lienholder] has an interest in or is entitled to receive payment from the from the funds in the attorney's possession." 9-102(C)(4).

4. In N.Y. City 2018-4, the Association of the Bar of the City of New York's Committee on Professional Ethics ("City Bar Committee") observed that while the Rules prohibit a lawyer from "knowingly assisting" a client's crime or fraud, they do not explicitly address a lawyer's duty in instances where the lawyer doubts the lawfulness of the client's conduct, and do not require a lawyer to investigate to determine whether providing legal services would assist a crime or a fraud. Instead, the City Bar Committee drew from several Rules and opinions to conclude that in certain instances a lawyer *may* have a duty of inquiry arising from the lawyer's duty of competence under Rule 1.1, as well as a duty to avoid knowingly assisting misconduct. Opinion 2018-4 suggests that a lawyer who assists with a suspicious transaction violates his duty of competence because a reasonable lawyer who has serious doubts would refrain from providing assistance absent an investigation to allay any concerns. Further, the ABA observed that while not ethically required, it is prudent for lawyers to undertake due diligence of clients in appropriate circumstances "to avoid facilitating illegal activity or being drawn unwittingly into a criminal activity." ABA Formal Op. 463 (2013).

5. What constitutes a duty of inquiry will depend on the particular facts and circumstances of the matter. A lawyer must assess the facts that give rise to the lawyer's concerns or suspicions about the particular transaction, and then assess whether the lawyer has enough information to ensure that the lawyer is not participating in or condoning fraudulent or illegal conduct by the client. If the lawyer does not have enough information, the lawyer should inquire further. *See, e.g.*, N.Y. City 2015-3 (2015) (lawyer who believes client involved him in a scam has a duty of competence to investigate further before proceeding with the matter); ABA Informal Op. 1470 (1981) ("a lawyer should not undertake a representation in disregard of facts suggesting that the representation might aid the client in perpetrating a fraud or otherwise committing a crime;" a

lawyer has "a duty of further inquiry" before assisting in a matter where the lawyer is not satisfied that the client's conduct is lawful); *see also In re Dobson*, 427 S.E.2d 166, 1660-68 (S.C. 1993) (attorney sanctioned "for helping client while remaining deliberately ignorant of his client's criminal conduct," and holding that court would "not countenance the conscious avoidance of one's ethical duties as an attorney"). The lawyer may consider whether the client expressed concerns about tax or other liability if he receives the funds directly, expressed concern about outstanding claims against the client by creditors and others, or other facts or similar statements by the client suggesting that the client has an improper purpose in directing payment to a third party.

6. Clearly a lawyer may not knowingly participate in a client's fraud or fraudulent or illegal conduct. The question is whether the lawyer "knows" that the client is involved in, or plans to engage in, fraudulent or illegal conduct. Rule 1.0(k) provides that "knowingly," "known," "know," or "knows" means "actual knowledge of the fact in question," and adds that knowledge may be inferred from circumstances. A lawyer may not avoid knowledge by failing to inquire further when the lawyer is aware of facts or circumstances suggesting that the client is intent on or involved in unlawful conduct. A lawyer may be deemed to have knowledge that the client is engaged in a crime or fraud "if the lawyer is aware of serious questions about the legality of the transaction and renders assistance without considering readily available facts that would have confirmed the wrongfulness of the transaction." Opinion 2018-4 ("Conscious avoidance of the fact in question may also constitute knowledge under the Rules, as under criminal law"). In such circumstances, it will be incumbent upon the lawyer to inquire further before simply following a client's instructions to distribute funds to third parties instead of to the client directly.

7. There are additional considerations. A lawyer's inquiry must be conducted consistent with the lawyer's duty of confidentiality to the client under Rule 1.6. If the lawyer learns that the client is engaging in a crime or fraud, the lawyer should first remonstrate with the client to desist. If the client insists on going forward with fraudulent or illegal conduct, the lawyer cannot participate or allow the lawyer's services to be used in that effort. Withdrawal from continued representation is, in some cases, obligatory and in others, permissive. The lawyer *may* withdraw if the client will persist in conduct involving the lawyer's services that the lawyer reasonably believes is criminal or fraudulent, (Rule 1.16(c)(2)), and *must* withdraw if the lawyer knows that representation will result in a violation of the Rules or of law. Rule 1.16(b)(1); *see also* Rule 8.4(b), (c) prohibiting a lawyer from engaging in "illegal conduct that adversely reflects in the lawyer's honesty, trustworthiness or fitness" and from engaging in conduct involving "dishonesty, fraud or misrepresentation"). The client may consent to the lawyer's withdrawal or not and, in some circumstances, the lawyer may have to move the Court to be permitted to withdraw from the representation if required by the rules of the tribunal in which the lawyer is appearing on behalf of the client. Rule 1.16(d). Upon withdrawal, the lawyer must take steps to avoid foreseeable prejudice to the client, which includes providing reasonable notice to the client, permitting time for employment of other counsel, and delivering to the client all papers and property to which the client is entitled (including the funds at issue in this inquiry). Rule 1.16(e).

CONCLUSION

8. A lawyer must direct funds or other property in the lawyer's possession to the client or a third party who is entitled to receive the funds or property. Unless a third party is entitled to funds awarded to a client, a lawyer may send such funds to the third party only if the client requests the transfer. However, the lawyer is not required to comply with the request, and may not do so if the lawyer knows the transfer would assist the client in committing a crime or fraud. The lawyer must assess whether the information he or she possesses requires further inquiry into the ethical propriety of the client's request to direct the funds to a third party. If the lawyer reasonably suspects that the transfer would be illegal or fraudulent, the lawyer should undertake a reasonable inquiry to allay his or her suspicions. If the inquiry reveals that the client is engaging in a crime or fraud and seeking the lawyer's unwitting participation, the lawyer *may* terminate the representation if the client will persist in conduct involving the lawyer's services that the lawyer reasonably believes is criminal or fraudulent, and *must* do so if continuing the representation will result in a violation of the Rules of Professional Conduct of law. If the lawyer decides to withdraw from the representation, the lawyer must first seek permission for withdrawal if required by the rules of a tribunal in which the lawyer represents the client, and upon withdrawal must take steps to avoid foreseeable prejudice to the client, which includes delivering to the client all of the funds or property in the lawyer's possession to which the client is entitled.