



ETHICS ADVISORY OPINION

18-05

UPON THE REQUEST OF A MEMBER OF THE SOUTH CAROLINA BAR, THE ETHICS ADVISORY COMMITTEE HAS RENDERED THIS OPINION ON THE ETHICAL PROPRIETY OF THE INQUIRER'S CONTEMPLATED CONDUCT. THIS COMMITTEE HAS NO DISCIPLINARY AUTHORITY. LAWYER DISCIPLINE IS ADMINISTERED SOLELY BY THE SOUTH CAROLINA SUPREME COURT THROUGH ITS COMMISSION ON LAWYER CONDUCT.

South Carolina Rules of Professional Conduct: 1.15

South Carolina Appellate Court Rules: 412, 417

Factual Background:

Licensed South Carolina Lawyer wants to accept earnest money deposits from a client through PayPal.

Questions:

- (1) May a lawyer accept an earnest money deposit through PayPal?
- (2) If a lawyer may accept an earnest money deposit through PayPal, when does the lawyer have to transfer the money from PayPal?

Summary:

Lawyer is required to hold property of clients or third persons in connection with representation separate from the lawyer's own property, but can comply with that obligation if the PayPal account in question does not contain Lawyer's own property and appropriate records are maintained. If the funds received into that account are nominal or short-term funds, Lawyer would then be required to transfer those funds to an IOLTA account for safekeeping, in a manner and timing consistent with Rule 1.15(f) obligations prohibiting disbursement from a trust account until funds are deposited and collected.

Discussion:

Lawyers may receive property of clients or third parties in many different forms. When the property received are funds, the obligation of Lawyer in response is independent of the form in which those funds are received. Regardless of whether funds are received in the form of cash, via check, money order, or credit card, Rule 1.15(a) states “A lawyer shall hold property of clients or third persons that is in a lawyer’s possession in connection with a representation separate from the lawyer’s own property....Other property shall be identified as such and appropriately safeguarded.” As Comment [1] to that rule explains, “A lawyer should hold property of others with the care required of a professional fiduciary.” Lawyers are not restricted to having only one trust account, and any account receiving funds of clients or third parties must be treated as a trust account. “All property that is the property of clients or third persons, including prospective clients, must be kept separate from the lawyer’s business and personal property and, if monies, in one or more trust accounts.” *Id.*

Receipt of funds via an online payment service provider such as PayPal, which allows individuals and businesses to transfer funds electronically to an account maintained with that service provider, trigger the same obligations found in Rule 1.15, RPC and Rule 417, SCAR regarding all other trust accounts. Thus, to adequately maintain the required separation from Lawyer’s own property, such account with any service provider must not contain any funds belonging to the Lawyer. The only exception would be for such amounts as are necessary “for the sole purpose of paying service charges on that account.” Rule 1.15(b).

All trust accounts require extensive documentation be kept current. “Complete records of such account funds and other property shall be kept by the lawyer and shall be preserved for a period of six years after termination of the representation.” Rule 1.15(a). Additional financial recordkeeping requirements are contained within Rule 417, SCACR.

Rule 412, SCACR addresses a certain type of trust account, an Interest on Lawyer Trust Accounts (IOLTA), which is likely implicated under the inquirer’s scenario. That rule states that

All nominal or short-term funds belonging to clients or third persons that are placed in trust with any member of the South Carolina Bar practicing law from an office or other business location within the state of South Carolina shall be deposited into one or more IOLTA accounts

Rule 412(b)(1).

“Nominal or short-term” is defined in the rule as funds of a client or third person that “the lawyer has determined cannot provide a positive net return to the client or third person” after consideration of relevant factors outlined in the rule. Rule 412(a)(1) and (d). The “earnest money” referenced by Lawyer in his inquiry likely constitutes “nominal or short-term” funds, and thus those funds initially deposited into the trust account maintained with the online service provider must be moved into Lawyer’s IOLTA trust account.

An additional characteristic of trust accounts generally, however, is a restriction on how and when disbursements therefrom may be made. With an online service provider, transfer from the service provider account into any other account is done via online transfer. Rule 5 within Rule 417, SCACR authorizes electronic transfers from “one client trust account to another client trust account.” However, additional restrictions on disbursements from trust accounts are found in Rule 1.15(f), RPC. That portion of 1.15 states “A lawyer shall not disburse funds from an account containing the funds of more than one client or third person (“trust account”) unless the funds to be disbursed have been deposited in the account and are collected funds.” This requirement is explained as “fundamental to proper trust accounting” in Comment [5] to Rule 1.15.

Certain funds may be treated as collected immediately upon deposit, depending on the manner in which they were received. Rule 1.15(f)(2). Included within the means of deposit that allow for treating the funds as immediately collected is “verified and documented electronic funds transfer.” Rule 1.15(f)(2)(ii). That and other methods listed are identified as “represent[ing] categories of trust account deposits which carry a limited risk of failure so that disbursements may be made in reliance on such deposits without violating the fundamental rule of disbursing only on collected funds.” Comment [7].

However, not all electronic transfers are equal. *See* EAO 12-11 (treating ACH deposits to a trust account as not immediately collected funds due to the reversibility of such deposits, at least until expiration of five banking days after receipt). In this context, online payment service providers such as PayPal have terms of service that are unique to each service provider, subject to change at the provider’s discretion, and which often allow for reversal of credits/payments by clients or third parties to an account on a much more extended timeline than the more heavily-regulated depository institutions that handle traditional checks and “wire transfers.” Thus an “electronic transfer” from an online service provider may not “carry a limited risk of failure” equivalent to more traditional forms of electronic deposit, despite being treated equally under the provisions of Rule 1.15(f)(2).

The risk for the Lawyer in the event of such a reversal of credit/deposit is set forth in Rule 1.15(f)(2), “If the actual collection of deposits described... does not occur, the lawyer shall, as soon as practical but in no event more than five (5) business days after notice of noncollection, deposit replacement funds in the account.”

Accordingly, Lawyer may elect to establish a dedicated trust account via an online payment service provider, but funds received into that account are likely to be nominal or short-term, thus requiring in turn a transfer of those funds to an IOLTA account. Lawyer should be aware of an elevated risk of non-collection under these circumstances in making the individual determination as to whether he is willing to receive funds belonging to third parties via an online payment service provider, PayPal or otherwise.