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TO: House Financial Institutions Committee

FROM: Christopher M. Joseph
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RE: HB 2793

DATE: April 30, 2012

Chairman Knox and Members of the Committee:

The Kansas Court of Appeals issued an opinion in *Consumer Law Associates, LLC, v. Stork*, No. 106,115, on March 23. The opinion includes two sentences interpreting the scope of the attorney exemption to the Kansas Credit Services Organization Act (KCSOA). The exemption, K.S.A. 50-1116(b), provides:

> Any person licensed to practice law in this state acting within the course and scope of such person's practice as an attorney shall be exempt from the provisions of this act.

Addressing whether a law firm would also be exempt, the court of appeals concluded:

> We agree with the district court that individuals who are licensed to practice law in Kansas are exempt from regulation by the OSBC. The OSBC exemption does not apply to a limited liability company or any other entity that is not licensed to practice law by the Kansas Supreme Court. See K.S.A. 50-1116(b).

When the legislature decided to include the attorney exemption in the KCSOA, it surely intended to make both lawyers and their law firms exempt. But the court of appeals disagreed. It held that because law firms cannot be licensed to practice law in Kansas, the legislature must have meant to include only individual lawyers. That's a major problem for lawyers who practice law as members of a law firm. The legislature should act to clarify that its intent has always been to include both lawyers and their law firms.

Following the *Stork* decision, most Kansas law firms whose lawyers assist debtors or injured persons will need to register and comply with the KCSOA. These law firms could no longer do the following things, all of which are commonly done now by law firms in Kansas:

(a) A law firm could not delay payment for the purpose of increasing interest, costs, fees, or charges payable by the consumer. K.S.A. § 50-1121(a) (2005). Under this provision, a law firm could not advise a client to stop paying high interest credit cards and begin saving money to buy a car for cash that would be exempt under K.S.A. § 60-2304(c) (2005), a common practice among law firms that assist consumer debtors.

(b) A law firm could not operate as a collection agency. K.S.A. § 50-1121(j) (Supp. 2005). Does this mean that a law firm that helps consumer debtors could not also have a practice where it tries to collect debts for its other clients?

(c) A law firm could not receive or charge any fee in the form of a promissory note or other promise to pay. K.S.A. § 50-1121(k) (2005). Would a law firm that charged its client on an hourly basis have to stop representing its client the moment the client did not pay the firm pursuant to their contract, but promised to pay as soon as she could?

(d) A law firm could not accept or receive any reward, bonus, premium, commission or any other consideration for the referral of a consumer to any person or related entity. K.S.A. § 50-1121(l) (2005). A law firm would be prohibited from referring a client who was injured in an accident to a law firm that handles those types of cases and receiving a referral fee that would otherwise be proper under the Kansas Rules of Professional Conduct. *See* Kan. Sup. Ct. Rule 226, KRPC Rule 1.5(g)

(e) A law firm could not lend money or provide credit to a consumer. K.S.A. § 50-1122(n) (2005). In short, a law firm could not advance costs for its client.

(f) A law firm could not structure a debt management services agreement in any manner that would result in a negative amortization of any of the consumer debts. K.S.A. § 50-1121(p) (2005). That means prioritizing debts nondischargeable in bankruptcy over those that can be discharged would be illegal.

(g) A law firm could not build up funds over time in its trust account to pay priority or nondischargeable debts. K.S.A. § 50-1122(b)(2) (2005).

(h) A law firm would be limited in the amount of fees it could charge even though the fees would otherwise comport with the Kansas Rules of Professional Responsibility. A personal injury law firm's contingent fee would be limited to the amount allowed by statute if a lawyer in the firm agreed to negotiate reduced payments to his client's medical providers, a practice nearly universal among the plaintiffs' bar. Fees would be limited to a one-time consultation fee not exceeding $50 and any credit report obtained would have to be paid from that fee. An additional fee of $20 per month or $5 per month per creditor could also be charged. K.S.A. § 50-1126 (2005). What law firms could afford to stay in business at these rates? How will Kansas consumers benefit from having limited choices available for assistance

in debt counseling or recovery of damages if they are negligently or intentionally injured when law firms that currently offer these services abandon those practice areas?

(i) A law firm would have to obtain a surety bond. K.S.A. § 50-1119 (2005).

(j) A law firm would have to provide a credit education program. K.S.A. § 50-1120 (2005).

(k) A law firm would be required to disclose that it may receive compensation from the consumer's creditors. K.S.A. § 50-1120(c)(7) (2005). How can a firm receive compensation from an adverse party?

(l) A law firm would be required to disclose that it may not solicit other services from its client. K.S.A. § 50-1120(c)(8) (2005). Is the firm prohibited from providing other legal services to its clients while it is providing credit services? A law firm could not write a will for a person for whom it is also negotiating a credit card debt.

(m) A law firm would be prohibited from advertising prior to registration. K.S.A. § 50-1121(f) (2005). That means a lawyer, individually, can advertise but a law firm cannot.

(n) A law firm would be prohibited from taking a security interest. K.S.A. § 50-1121(o) (2005). A firm cannot assert an attorney lien, but an individual lawyer can. If money is collected on that lien, can the lawyer share it with the law firm's partners?

(o) A law firm may no longer "[u]se any communication which simulates in any manner *a legal or judicial process*, or which gives the false appearance of being authorized, issued or approved by a government, governmental agency *or attorney-at-law*." K.S.A. § 50-1121(s) (Supp. 2005).

If a law firm failed to abide by these rules, it would be subject to *criminal penalties, actual damages, punitive damages and attorney fees.* K.S.A. § 50-1131 (2005).

Response to opponents

You may hear opponents claim that Persels is "not a real law firm." I disagree. But more importantly, it is not relevant to setting good public policy. In terms of public policy, the issue is simple – if what Persels does is not the practice of law, then they are not exempt; neither the attorneys or the law firm. Public policy should not be to exclude all Kansas law firms from the KSCOA exemption. That's opponents asking you to throw the baby out with the bath water. It makes all Kansas law firms collateral damage.

The issue for the courts and regulators should be the same for all lawyer and law firms seeking exemption from the KCSOA – is the conduct at issue within the scope of the practice of law of a licensed Kansas attorney. That seems to clearly have been the legislative intent when the attorney exemption was created. The *Stork* decision now makes clarification of that intent necessary.