

Geoffrey M. Trachtenberg
LEVENBAUM COHEN
TRACHTENBERG, PLC

Ethical Rule 1.15: Who Gets a Slice of the Pie?

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Relevant Rules – E.R. 1.15

(d) Upon receiving funds or other property in which a client or third person **has an interest**, a lawyer shall promptly notify the client or third person. Except as stated in this Rule or otherwise permitted by law or by agreement between the client and the third person, a lawyer shall promptly deliver to the client or third person any funds or other property that the client or third person is entitled to receive and, upon request by the client or third person, shall promptly render a full accounting regarding such property.

(e) When in the course of representation a lawyer possesses property in which two or more persons (one of whom may be the lawyer) **claim interests**, the property shall be kept separate by the lawyer until the dispute is resolved. The lawyer shall promptly distribute all portions of the property as to which the interests are not in dispute.

What is an “interest”?

What is a “claimed interest” or “dispute”?

Relevant Comment – E.R. 1.15

[4] The Rule also recognizes that third parties may have ***just claims*** against specific funds or other property in a lawyer's custody, such as a client's creditor who has a lien on funds recovered in a personal injury action. A lawyer may have a ***duty under applicable law*** to protect such third-party claims against wrongful interference by the client. In such cases, when the third-party claim has become a ***matured legal or equitable claim***, the lawyer must refuse to surrender the property to the client until the claims are resolved. A lawyer should not ***unilaterally assume to arbitrate*** a dispute between the client and the third party, but, when there are ***substantial grounds*** for dispute as to the person entitled to the funds, the lawyer may file an action to have a court resolve the dispute.

What are “just claims”? What are “matured legal or equitable claims”?

What does the “substantial grounds” requirement mean?

What are duties under “applicable law”?

What *is* an “interest”?

According to the State Bar’s Ethics Committee:

“An ‘interest’ is a matured legal or equitable claim.”

Source: Arizona Formal Opinion 11-03.

But what is a “matured legal or equitable claim”?

It appears to originate from Professors Hazard and Hodes, who state that “the third party must have a matured legal or equitable claim, such as a lien on specific funds, in order to trigger the lawyer’s duty to hold the funds . . . pending resolution of the dispute.”

Geoffrey C. Hazard, Jr. & W. William Hodes, *The Law of Lawyering*, §19.6 (3d ed. Supp. 2005-2).

What are *potential* “interests”?

☑ **Consensual Liens**

- Chiropractic or Physical Therapy Liens
- Case Advance Loans or Case Funding Loans
- Pharmacy or Rental Car Liens

☑ **Statutory Interests – Rights as a Matter of Law**

- Healthcare Provider Liens, A.R.S. § 33-931, *et seq.*
- Child Support Liens, A.R.S. §§ 25-505, -516 & -521
- AHCCCS, A.R.S. §§ 12-961, 36-2903, -2915 & -2956
- Medicare, 42 U.S.C. § 1395y(b)(2)
- Federal Medical Care Recovery Act (FMCRA), 42 U.S.C. § 265, *et seq.*
- Workmans’ Compensation Liens, A.R.S. § 23-1023(d)
- Med-Pay Liens, A.R.S. § 20-259.01(J)

☑ **Statutory Interests – Rights Based upon Contractual Plans**

- Employee Retirement Income Security Act (ERISA), 29 U.S.C. § 1132(a)(3)
- Federal Employee Health Benefits Act (FEHBA), 5 U.S.C. § 8901, *et seq.*

☑ **Other Potential Interests**

- Attorneys’ Charging Liens
- Equitable assignments or liens

“Matured Legal or Equitable Claims”

“No Interest”	“Interest”
<p>Lien not signed by client <u>or</u> attorney.</p> <p>Attorney has knowledge of medical services provided, but has received no demand of any kind upon the lawyer.</p> <p>Provider simply sends copies of client's medical bills to the attorney.</p> <p>Provider, absent a lien or assignment of any kind, simply sends a letter to the attorney demanding payment for medical bills for the client's accident-related treatment.</p> <p>Provider properly files a timely statutory lien pursuant to ARS § 33-931, <i>et seq.</i>, but fails to present the lien to the attorney.</p> <p>Claim by a “general unsecured creditor.”</p>	<p>Lien, assignment or letter of protection signed by the client <u>or</u> attorney.</p> <p>Attorney orally agrees to reimburse provider from settlement funds.</p> <p>Knowledge of treatment provided under the FMCRA or FEHBA where subrogation rights arise as a matter of law <u>or</u> where a lawyer knows of a contractual reimbursement provision.</p> <p>Medical provider has presented a statutory lien pursuant to ARS § 33-931, <i>et seq.</i>, that is facially incomplete or untimely, but has been recorded with the County Recorder. **</p> <p>** Predates substantial amendments to ARS § 33-931, <i>et seq.</i>, which now expressly provide that unperfected liens are unenforceable.</p>

Source: Arizona Formal Opinions 97-02, 98-06 and 11-03.

“Substantial Grounds”

“E.R. 1.15 is not violated where the lawyer actually has a reasonable, good faith belief that the third party’s claim is without substantial merit. . . . While any ‘good faith doubt’ would implicate E.R. 1.15, a researched, reasonable and good faith belief in the propriety of disbursal is sufficient to render it permissible under the rule.”

Employers Reinsurance Corp. v. GMAC Ins., 308 F.Supp.2d 1010 (D.Ariz. 2004) (Martone, J.).

Undisputed Funds

All settlement proceeds must go into a specific or general trust account and nothing should be disbursed until the client signs off on a disbursement sheet.

All undisputed funds must be promptly disbursed.

Consider using a “Lien Worksheet.”

(1) This portion of the recovery is / is not (**circle one**) from UM/UIM.

(2) \$ _____ **Healthcare Provider Liens (not applicable to UM/UIM)** _____ (**attached**)

_____ Checked Lien Backer for any Healthcare Provider Liens.
_____ Checked internet for liens in *all* counties where treatment occurred
- and -
Put printout of search results in Lien Backer (*i.e.*, even if nothing found).
- or -
Called Recorders' Office in *all* proper counties without internet access
- and -
Put case note in Practice Master (*e.g.*, name of person you spoke with).
_____ If lien was reduced, reduction confirmed in writing and in the file.

(3) \$ _____ **ERISA Subrogation / Liens (Health Insurance)** _____ (**attached**)

_____ Checked Lien and Correspondence Backers for any subrogation claim letters from Rawlings, Primax, any health insurer, etc.
_____ If lien was reduced, reduction confirmed in writing and in the file.
_____ If "drop dead" letter was sent, time limit given in the letter has passed.

(4) \$ _____ **Consensual Liens (Liens Signed By Client)** _____ (**attached**)

_____ Checked Lien Backer for any Consensual Liens.
_____ If lien was reduced, reduction confirmed in writing and in the file.

(5) \$ _____ **Medicaid Lien (AHCCCS)**

Client did / did not (**circle one**) have AHCCCS pay bills.

(6) \$ _____ **Medicare Lien**

Client did / did not (**circle one**) have Medicare pay bills.

(7) \$ _____ **Workers' Compensation Liens (not applicable to UM/UIM)** _____ (**attached**)

Client did / did not (**circle one**) receive benefits from a workers' comp carrier.
_____ Confirmed authority to settle in writing with workers' comp carrier.
_____ If lien was reduced, reduction confirmed in writing and in the file.
_____ Future credit addressed with client and carrier.

(1) Notice

Assuming there is “an interest” by a third-party in any funds held by an attorney, the third-party is *entitled* to “prompt notice” the attorney is holding such funds.

(2) Deliver

Assuming there is “an interest” by a third-party in any funds held by an attorney, the third-party is *entitled* to “prompt delivery” of any undisputed funds.

(3) Accounting

Assuming there is “an interest” by a third-party in any funds held by an attorney, the third-party is *may request* a “full accounting” of any such funds.

Disputed Funds

- ✓ All disputed funds must remain in the trust account until the dispute is resolved.
- ✓ Although an attorney may try to negotiate or otherwise resolve a dispute for a “reasonable period of time,” an attorney may not “unilaterally assume to arbitrate a dispute between the client and the third party.”
- ✓ An attorney may not hold the disputed funds indefinitely or until a statute of limitations runs. After a “reasonable period of time,” an attorney should file “an action,” such as a declaratory relief action or interpleader, to resolve the dispute.

The Rule Needs to Be Amended

- ✓ In general, all a claimant need do to effectively enjoin disbursement is “claim and interest” in a fund or prospective fund.
- ✓ In no other scenario must a lawyer file suit against a third-party – including his own client and other legitimate claimants – in order to determine the rights to funds in the lawyer’s possession.
- ✓ Customarily, if a third-party claims it is owed money, the third-party must file suit.
- ✓ This leads to actual mischief.

Examples of ER 1.15 Abuse

- ❑ Healthcare provider files an ARS 33-931 lien that is not properly perfected (fails to file timely, fails to mail the lien as per the statute). *McReynolds v. Raineri*, CV82004-0298, Yavapai County
- ❑ Healthcare provider claims an ARS 33-931 lien against first-party benefits or refuses to honor an attorney fee reduction.
- ❑ ERISA insurer, who is not self-insured, claims a lien against a tort recovery. *Fernandez v. Rawlings Co.*, CV2004-020323, Maricopa County
- ❑ Healthcare providers claims a lien after being paid by health-insurance, which prohibits balance billing. *Allen v. AZ Bone & Joint Spec.*, CV2005-004815, Maricopa County
- ❑ Healthcare provider claims an ARS 33-931 lien after accepting Medicare or AHCCCS payment. *Sims v. Banner*, CV-01131, USDC

Examples of ER 1.15 Abuse

- ❑ AHCCCS Registered Provider refuses to bill AHCCCS and instead bills the client. *Puch v. Soscia*, CV2011-003623, Maricopa County
- ❑ Workers compensation carrier claiming a lien to recovery without any allowance for attorneys' fees.
- ❑ Chiropractor claiming a lien simply based upon having sent "records and bills" from accident-related treatment.
- ❑ Third-party administrator claiming an ERISA lien against a tort recovery of a church or government employee.
- ❑ ERISA insurer initially claims a lien in writing, then agrees orally that, while they actually have no valid lien rights, they will not "put it in writing."

Pending Changes

R-11-0024 – Proposing the addition of one-sentence to ER 1.15, Comment No. 4 that would allow attorneys to mail “drop dead” letters to third-party claimants with whom there is a dispute about client funds.

R-12-0032 – Proposing a change to ER 1.15 to add a mechanism for sending “drop dead” letters to third-party claimants with whom there is a dispute about client funds.