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UTAH STATE BAR

Ethics Advisory Opinion Committee

Opinion No. 00-04

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Issue: What are a lawyer's ethical duties to a third person who claims an interest in proceeds of a personal injury settlement or award received by the lawyer?

Opinion: When a lawyer receives funds or property and knows a third person claims an interest in the funds or property, the lawyer must first determine whether the third person has a sufficient interest to trigger the duties stated in Rule 1.15(b). Only a matured legal or equitable claim—such as a valid assignment, a judgment lien, or a statutory lien—constitutes an interest within the meaning of Rule 1.15 so as to trigger duties to third persons under Rule 1.15. If no such interest exists, the lawyer may disburse the funds or property to the client. If such an interest exists, the lawyer must comply with the duties stated in Rule 1.15. Where the client does not have a good-faith basis to dispute the third person's interest, the lawyer must promptly notify the third person, promptly disburse any funds or property to the third person to which that person is entitled, and render a full accounting when requested. If the client has a good-faith basis to dispute the third person's interest, and instructs the lawyer not to disburse the funds or property to the third person, the lawyer must promptly notify the third person that the lawyer has received the funds or property and then must protect the funds or property until the dispute is resolved.

Background: Lawyers sometimes receive funds or property in which third persons, such as medical providers or other creditors of the lawyer's client, claim an interest. The Office of Professional Conduct of the Utah State Bar has advised the Ethics Advisory Opinion Committee that it has received complaints from medical providers alleging that lawyers representing plaintiffs in personal injury matters have not distributed amounts from personal injury settlements or awards to reimburse them for medical services provided to the lawyer's client. In cases of this nature, the medical provider and the patient may have agreed that the patient may defer payment for medical services until the time of a personal injury settlement or

award, at which time the provider's invoices will be paid. The medical provider may also rely on a statutory lien or an assignment. Medical providers without a statutory lien or an assignment may demand payment from funds held by the lawyer based on facts such as the client's promise to pay the provider when a settlement or award is received or the lawyer's use of the provider's bill in proving damages. In other cases, non-medical service providers, sellers of goods, or judgment creditors may claim rights in funds or property in a lawyer's possession. The Office of Professional Conduct has requested that the Committee issue a formal opinion regarding matters involving third-party claims to proceeds of a personal injury settlement or award received by a lawyer.

Analysis: Rule 1.15 of the Utah Rules of Professional Conduct specifically addresses a lawyer's duties when safekeeping property for clients or third persons. It states, in pertinent part:

(b) 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 with the client, a lawyer shall promptly deliver to the client or third person any funds or 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. (fn1)

Rule 1.15 does not differentiate between the duties a lawyer owes a client and those owed a third person when safekeeping property.

The rule addresses three distinct duties. First, if a client or third person "has an interest" in property or funds received by a lawyer, the lawyer must promptly notify the client or third person. Second, the lawyer must promptly deliver the funds or property to the client or third person who is "entitled to receive" the funds or property. (fn2) Third, if requested by the client or third person, the lawyer must promptly render a full accounting regarding the property. Generally, there will be no controversy surrounding who is entitled to the funds or property that the lawyer is safekeeping and application of Rule 1.15 will be simple. When a dispute exists between the client and a third person as to who is entitled to the funds or property in the lawyer's possession, applying Rule 1.15 requires additional analysis.

Not every claim made by a third person triggers the duties expressed in Rule 1.15. Rather, these duties are triggered when the lawyer receives funds or property and the lawyer knows (fn3) that a third person "has an interest" in the property or funds. It thus becomes necessary to determine

what is meant by "has an interest" under Rule 1.15. A third person who "has an interest" is different from a third person who merely claims an interest. Subsection (b) of Rule 1.15 speaks of interests that are "claim[ed]." In subsection (c) of Rule 1.15, the drafters of the rule chose the language "has an interest." A person who "has an interest" has something stronger than a mere claim or demand for payment. This interpretation is supported by an official comment to Rule 1.15, which states:

Third parties, such as a client's creditors, may have just claims against funds or other property in a lawyer's custody. A lawyer may have a duty under applicable law to protect such third-party claims against wrongful interference by the client and accordingly may refuse to surrender the property to the client. (fn4)

Professors Hazard and Hodes have analyzed the significance of this comment as follows:

The fact that a third party "expects" funds held by the lawyer to be the source of payment would not justify a lawyer's refusal to obey the instructions of his client to turn over the entire amount. The Comment to Rule 1.15 uses the phrases "just claims" and "duty under applicable law" to suggest that the third party must have a matured legal or equitable claim in order to qualify for special protection. Only in such cases may it be said that failure to recognize the third-party interest is a species of fraud upon creditors or fraud upon the rendering court. (fn5)

Only those claims that rise to the level of a "matured legal or equitable claim" constitute an "interest" and trigger the duties owed under Rule 1.15. For example, a valid assignment of the funds in question could be such a claim. Certainly, a statutory or judgment lien that attaches to the specific property or funds in question or a court order requiring that the specific property or funds be turned over to the third party is such an interest. A lawyer's knowledge that the client owes bills, even if the lawyer knows that the creditor expects to be paid out of the proceeds of a settlement or judgment, does not give rise to such duties unless the creditor has an interest in the proceeds within the meaning of Rule 1.15.

This conclusion is consistent with prior opinions of this Committee. For example, in Opinion No. 96-03, the Committee stated that "[a]bsent dishonesty, fraud, deceit or misrepresentation, [an] attorney has no ethical obligation to honor personally the client's agreements to pay medical providers out of a settlement or judgment." The Committee noted that it was not addressing "agreements that expressly impose an obligation on the attorney or create a lien on the funds that are handled by the attorney." (fn6) In a prior opinion, the Committee applied a similar approach to a lawyer's refusal to pay for services rendered to the lawyer's

client at the lawyer's request. (fn7)

Even where a third person has a sufficient interest to invoke the duties expressed in Rule 1.15(b), a lawyer ordinarily should not simply hand over the funds or property to the third person against the client's instructions. (fn8) The comments to Rule 1.15(b) emphasize that "a lawyer should not unilaterally assume to arbitrate a dispute between the client and the third party." (fn9) Where a third person has a sufficient interest to trigger the duties expressed in Rule 1.15(b) and a client in good faith instructs the lawyer not to pay the third person, the lawyer must hold the funds or property until the dispute is resolved, or, if resolution seems unlikely, interplead the funds or property. Retaining and protecting the funds will not be a violation of the lawyer's duty to the client because, under Rule 1.15(b), the lawyer is only required to disburse to the client those funds to which the client is "entitled." If there is a third-party "interest" within the meaning of Rule 1.15(b), the client is not "entitled" to the funds. (fn10)

To summarize, when a lawyer receives funds or property and knows a third person claims an interest in the funds or property, the lawyer must first determine whether the third person has an interest sufficient to trigger the duties expressed in Rule 1.15(b). Only a matured legal or equitable claim—such as a valid assignment, a judgment lien (fn11) or a statutory lien—constitutes a sufficient interest to trigger duties to third persons under Rule 1.15(b). If no such interest exists, the lawyer may disburse the funds or property to the client. If such an interest exists, the duties expressed in Rule 1.15 are triggered. If the client does not dispute the third person's interest, the lawyer must promptly notify the third person, promptly disburse any funds or property to the third person to which that person is entitled and render a full accounting when requested. If the client has a good-faith basis to dispute the third person's interest and instructs the lawyer not to disburse the funds or property to the third person, the lawyer must promptly notify the third person that the lawyer has received the funds or property and then must protect such funds or property until the dispute is resolved. (fn12)

Application: In the discussion that follows, we apply the foregoing analysis to a number of hypothetical situations posed by the Office of Professional Conduct of the Utah State Bar.

Example 1: The medical provider has a written "lien" which states that the client has agreed that the medical provider will defer payment for the medical services until the time of any settlement or award and then receive payment from the client directly from the settlement funds. In this example, the written "lien" has been sent to the lawyer.

First, the lawyer must determine whether the medical

provider has a sufficient interest to trigger the duties expressed in Rule 1.15(b). Such an interest must be a matured legal or equitable claim. A valid assignment of the proceeds of a settlement or award of which the lawyer has knowledge is a sufficient interest. Whether a written "lien" creates a valid assignment must be determined under applicable law. (fn13) If it does, the lawyer must promptly notify the medical provider when the lawyer receives any settlement funds. If the client does not, in good faith, dispute the interest, the lawyer must then promptly disburse the funds to the medical provider and render an accounting if requested. If the client disputes the interest in good faith, the lawyer must protect the funds until the dispute is resolved.

Example 2: The medical provider does not have a written "lien," but the client has informed the lawyer orally that he received the medical services from the provider. The client informs the lawyer that the client is not paying for the services. The lawyer knows the medical provider expects to be paid out of any settlement or award. The lawyer may have used the charges for the medical services to compute damages in a settlement demand for special and general pain and suffering damage.

In this situation, the medical provider does not have a matured legal or equitable claim to the settlement proceeds or any award. The medical provider might have obtained a statutory lien against the proceeds or a valid assignment of the proceeds, but evidently did not do so. (fn14) If the client instructs the lawyer to pay for the services out of the settlement proceeds, the lawyer may do so. If the client instructs the lawyer not to pay the medical provider from the proceeds, the lawyer has no duties to the medical provider and would breach a duty to the client by not following the client's instructions.

Example 3: The client has not paid a public utility company for services for six months, and the client stalls any collection effort by promising to pay when the settlement funds come in. Now the company sends a letter to the lawyer demanding payment.

The public utility company does not have an interest within the meaning of Rule 1.15(b) and therefore the duties expressed in Rule 1.15(b) do not apply.

Example 4: A judgment creditor serves a writ of garnishment on the lawyer and obtains a garnishment lien against the client's fund held in the trust account.

Here, the creditor has a matured legal claim in the form of a garnishment lien. The lawyer must notify the judgment creditor when the lawyer receives funds subject to the garnishment lien, and, if the client has no good-faith basis for disputing the validity of the lien, the lawyer must

disburse the funds or property in the amount of the lien to the creditor and render a full accounting if requested. If the client has a good-faith basis to dispute the lien, after promptly notifying the judgment creditor that the lawyer has received the funds, the lawyer must protect the funds until the dispute is resolved.

Example 5: In a family law matter, the lawyer for one spouse accepts funds as a tender of settlement from the other spouse's lawyer regarding past-due support payments. The receiving lawyer deposits the funds in his trust account, but refuses the settlement. The receiving lawyer then refuses to return the funds to the other lawyer, claiming the funds in the trust account are his client's, whatever the final settlement is.

Here, the lawyer has received tendered funds subject to an express condition that the settlement proposed be accepted. The funds belong to the other party to the matter and cannot be paid to the lawyer's client until the condition is satisfied. The lawyer should have returned the funds when the settlement was refused because the condition upon which they were received will not be satisfied. (fn15)

Conclusion: Third-party claims to funds or property held by a lawyer, where known to the lawyer, require the lawyer's careful attention to Rule 1.15(b). The lawyer must determine whether the third person has a matured legal or equitable claim sufficient interest to trigger the duties stated in Rule 1.15(b). If no such interest exists, the lawyer may disburse the funds or property to the client. If such an interest exists, the lawyer must comply with the duties stated in Rule 1.15(b). Where the client does not dispute the third person's interest, the lawyer must promptly notify the third person, promptly disburse any funds or property to the third person to which that person is entitled, and render a full accounting when requested. If the client has a good-faith basis to dispute the third person's interest, and instructs the lawyer not to disburse the funds or property to the third person, the lawyer must promptly notify the third person that the lawyer has received the funds or property and then must protect the funds or property until the dispute is resolved.

We emphasize that independent ethical considerations and principles of substantive law may govern circumstances not addressed in this opinion. A lawyer's dishonesty, fraud, deceit or misrepresentation to a third party in connection with a client's obtaining goods or services is a violation of Rule 8.4(c). (fn16) For example, a lawyer who knows a client intends subsequently to avoid obligations to creditors but in spite of this knowledge assists the client to obtain goods or services under false pretenses will have committed an ethical violation. Under principles of agency law, a lawyer acting as a client's agent may become personally liable to third parties for goods or services provided to the

client.

Footnotes

1. Utah Rules of Professional Conduct 1.15(b).

2. A lawyer's violation of the ethical duty to pay over funds to third parties has been held to be a ground for discipline. *See In re George McCune*, 717 P.2d 701 (Utah 1986) (under former Rule of Professional Conduct II, § 3, requiring lawyers to pay or deliver money or property "to the person entitled thereto within a reasonable time," lawyer disbarred for failing to pay over to co-counsel and court reporter funds paid by client for payment of their invoices). In Utah, a lawyer's obligation to pay or deliver money or property to the person entitled to it is reinforced by a criminal statute, Utah Code Ann. § 78-51-42, which provides: "An attorney and counselor who receives money or property of his client in the course of his professional business and who refuses to pay or deliver the same to the person entitled thereto within a reasonable time after demand is guilty of a misdemeanor."

3. Rule 1.15(b) does not specify what level of belief or knowledge a lawyer must have to impose the duties specified in the rule. We agree with the analysis of the State Bar of Arizona that a lawyer must have actual knowledge of a third party's interest before acting under Rule 1.15(b). Arizona Ethics Op. 98-06 (Ariz. St. Bar June 3, 1998), <www.azbar.org/ethicsopinions> (level of cognition must be inferred when not specified; comments to Rule 1.15(b) concerning "just claims," and lawyer's "duty under applicable law to protect" third-party claims, and lawyer's obligation not to "unilaterally assume to arbitrate" matters between client and third party strongly infer that a lawyer must have actual knowledge of a third party's interest before acting). Under the Rules of Professional Conduct, "knowingly," "known," or "knows" "denotes actual knowledge of the fact in question. A person's knowledge may be inferred from the circumstances." Utah Rules of Professional Conduct, Preamble, comment.

4. Utah Rules of Professional Conduct 1.15, cmt. (emphasis added).

5. Geoffrey C. Hazard, Jr. & W. William Hodes, *The Law of Lawyering* & #8212; A Handbook on the Model Rules of Professional Conduct § 1.15:302, at 460 (2d ed. Supp. 1994).

6. Utah Ethics Advisory Op. 96-03, 1996 WL 227377, n.1 (Utah St. Bar).

7. Utah Ethics Advisory Op. 98, 1989 WL 509364 (Utah St. Bar): "Absent dishonesty, fraud, deceit or misrepresentation, disputes resulting from the failure of an attorney to make payment for services rendered by third

parties should be treated as questions of substantive law, which should be examined under traditional contract and agency doctrines, rather than questions of the ethical propriety of the attorney's actions."

8. In cases where a court order or statute requires a lawyer to turn funds over to a third party, such as a client's bankruptcy trustee, the lawyer must comply with the court order or statute even if the client directs otherwise. *See, e.g.*, 11 U.S.C. § 542(a); *Utah Farm Production Credit Ass'n v. Labrum*, 762 P.2d 1070 (Utah 1988) (affirming contempt sanctions against debtor's lawyer who paid himself out of funds and released remaining funds to client in spite of court order to hold funds for client's bankruptcy trustee).

9. Utah Rule of Professional Conduct 1.15(b), cmt.

10. *See, e.g.*, *Leon v. Martinez*, 638 N.E.2d 511, 514 (NY 1994); *Berkowitz v. Haigood*, 606 A.2d 1157, 1158 (N.J. Super. Ct. Law Div. 1992); *Herzog v. Irace*, 594 A.2d 1106, 1109 (Me. 1991).

11. A judgment which has not become a lien on the proceeds of a personal injury settlement or award is not a sufficient interest under Rule 1.15(b). Kansas Ethics Op. 92-14 (Kan. St. Bar Nov. 5, 1992), www.ksbar.org/ethics.

12. This approach is similar to that adopted by numerous states in addressing the same issue. *See, e.g.*, Alaska Ethics Op. 92-3, <www.alaskabar.org> (Alaska St. Bar); Arizona Ethics Op. 98-06, <www.azbar.org/ethicsopinions> (Ariz. St. Bar); Connecticut Informal Ethics Op. 95-20 (Conn. St. Bar), <www.ctbar.org/ethics/cbaethics.htm>; District of Columbia Ethics Op. 251 (D.C. St. Bar Oct. 18, 1994); Ohio Ethics Op. 95-12 (Ohio St. Bar Oct. 6, 1995); Rhode Island General Informational Op. 7 (R.I. St. Bar Apr. 10, 1997); South Carolina Bar Advisory Op. 94-20, <www.sctbar.org/apps/reference/ethicsopinions/ethics.stm> (S.C. St. Bar); *see also Restatement (Third) of the Law Governing Lawyers* § 57; *Lawyer's Manual on Professional Conduct* (ABA/BNA) § 45:1101-10; Irene M. Ricci, *Trust Account: Client Trust Funds: How to Avoid Ethical Problems*, 11 Geo. J. Legal Ethics 245, 254-55 (1998).

13. The Committee is not empowered to decide legal, as opposed to ethical, questions. Utah Ethics Advisory Opinion Comm. Rules of Proc. § III(b)(3) (1996).

14. Hospitals can create a lien on proceeds of any settlement or judgment under Utah's Hospital Lien Law. *See* Utah Code Ann. §§ 38-7-1 to -8. State assistance automatically becomes a lien on any proceeds under Utah's Medical Benefits Recovery Act. *See* Utah Code Ann. § 26-19-5.

15. *See In re Shannon*, 179 Ariz. 52, 876 P.2d 548 (Ariz. 1994) (lawyer for personal injury plaintiffs received from

defendant's counsel insurance company check for the amount of the judgment marked "full satisfaction of judgment" along with a form of satisfaction of judgment and a letter specifying that the check should be cashed only upon the return of the executed satisfaction; lawyer disciplined for violating Rule 1.15 by depositing check without executing satisfaction).

16. Rule 8.4(c) provides: "It is professional misconduct for a lawyer to: . . . (c) Engage in conduct involving dishonesty, fraud, deceit or misrepresentation."

Rule Cited:

1.15