



WSBA

WASHINGTON STATE BAR ASSOCIATION

May 6, 2016

Washington State Office of Insurance Commissioner
Commissioner Mike Kreidler
c/o Jim Tompkins
PO Box 40258
Olympia, WA 98504-0258

Re: Matter No. R 2015-06, Requiring notice to third party claimants by insurers;
Comment of Washington State Bar Association

Dear Commissioner Kreidler:

The Washington State Bar Association (WSBA) was established in 1933 as a unified bar and it functions as an instrumentality of the Washington Supreme Court. The WSBA's mission is to serve the public and the members of the Bar, to ensure the integrity of the legal profession, and to champion justice. Under authority delegated by the Court, the WSBA regulates the practice of law in the public interest and performs other professional association functions on behalf of its membership. Among its regulatory responsibilities are the admission, licensing, and discipline of lawyers, limited practice officers, and limited license legal technicians. The WSBA has more than 37,000 lawyer members, and more than 25,000 of them are actively licensed to practice law.

Washington lawyers maintain the highest standards of ethical conduct and serve clients and the public with honesty, diligence, and integrity. It is the unfortunate case, however, that some practitioners stray from these ideals and transgress the ethical constraints established for the profession. By imposing disciplinary sanctions for unethical conduct, the lawyer discipline system protects the public, maintains public confidence and trust in the legal system, and deters other lawyers from similar behavior. The WSBA also administers Washington's Lawyers' Fund for Client Protection — funded by an annual assessment of WSBA members by order of the Supreme Court — to relieve or mitigate pecuniary loss sustained by victims of dishonest conduct in the practice of law.

While punitive and remedial measures are key components of an effective system of professional regulation, preventive measures also play a crucial role in protecting the public from the risks presented by lawyer misconduct. For this reason, the American Bar Association Standing Committee on Client Protection has developed and promoted nationwide adoption of a number of important preventive programs, among which is the ABA Model Rule on Payee Notification. The Model Rule, which has been adopted in fifteen U.S. jurisdictions, is intended to serve as a deterrent to the dishonest conduct of a claimant's lawyer with respect to receipt of payment on

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third-party liability claims. When an insurer provides contemporaneous notice of delivery of proceeds directly to the claimant, it becomes exceedingly difficult for an unscrupulous lawyer to successfully conceal an unauthorized settlement, deceitfully delay payment of insurance proceeds, or to outright misappropriate those proceeds after receiving them. Because payee notification is an achievable, commonsense, and effective approach to addressing a known risk to the public, the WSBA Board of Governors and the WSBA Chief Disciplinary Counsel support the Commissioner's proposal to adopt R 2015-6, which is closely based on the ABA Model Rule on Payee Notification.

The Commissioner is aware of the case of Edward J. Callow (now disbarred and convicted of theft and money laundering), arising from Mr. Callow's 2011 theft from his elderly and disabled client following issuance of a \$500,000 insurance-settlement check, a theft that was detected during the course of a WSBA Office of Disciplinary Counsel investigation of a trust account overdraft. Although Mr. Callow's misconduct was relatively high profile, it is not the only known instance of its type. Another example is the case of Brian Boddy (now resigned in lieu of disbarment and convicted of multiple counts of theft), who stole more than \$400,000 from personal injury clients between 2011 and 2013. In a number of those matters, Mr. Boddy led his clients to believe their cases were ongoing when a settlement had already been reached; he then forged client signatures on documents in order to obtain the settlement proceeds for his own use. And Thomas Sughrua (disbarred in 2008) settled a client's personal-injury claim without her knowledge, received a settlement check for \$8,750, failed to notify the client of receipt of the funds, endorsed the check in the client's name and deposited it into his trust account, and intentionally misappropriated some of the funds for his own use. In each of these cases, a payee notification rule would have minimized or eliminated the risk of loss to the claimant.

Matters like these, and the harm done to the claimant-victims of the misconduct, make a strong case for adoption of a payee notification rule.

During this rulemaking process, arguments have been advanced by insurance-industry associations in opposition to payee notification.¹ Because a number of these arguments appear to be based on misimpressions about the purpose and scope of regulatory systems and rules administered by the WSBA, we wish to address them briefly.

It has been argued that the WSBA discipline system is itself capable of adequately protecting consumers from unethical and illegal lawyer conduct without the need for payee notification. Relatedly, it is argued that enhanced disciplinary sanctions would be a more effective approach and more likely to influence lawyer behavior. These arguments call to mind Benjamin Franklin's proverb, "An ounce of prevention is worth a pound of cure." We agree that the Washington Supreme Court and the WSBA maintain an effective system of lawyer discipline; lawyers who have committed such misconduct should be (and have been) severely disciplined. But even the harshest sanction available, disbarment, only protects future consumers from harm by that disbarred lawyer. It does not protect those already harmed by that lawyer, nor does it

¹ See Letter from Christian John Rataj, Senior Director, National Association of Mutual Insurance Companies, to Insurance Commissioner (July 28, 2015); Letter from Kenton Brine, Assistant Vice President, Property Casualty Insurers Association of America, to Insurance Commissioner (July 31, 2015).

directly protect the public from potential future harm by other lawyers. The point of payee notification is prevention of harm. Moreover, disciplinary sanctions and remedies are invoked only if and when misconduct comes to light. While we can point to a number of relevant instances where a consumer has been financially injured and a lawyer has been severely disciplined, of at least equal concern are the instances that we do not know about. When, unbeknownst to the client, a lawyer receives a substantial sum from an insurer, a misappropriation or other wrongful disposition of funds is potentially undetectable. In the Callow case, for example, had it not been for the fortuity of a trust account overdraft, the theft might never have been discovered, Mr. Callow's client would likely have remained successfully misled, and Mr. Callow and his insurance-adjuster accomplice might have swindled more than \$165,000 with impunity. Although the full extent of this species of undetected fraud is unknowable, it can hardly be doubted that the risk calls for an ounce of prevention.

It has been argued that the Office of the Insurance Commissioner's adoption of a payee notification rule would constitute regulation of the lawyer-client relationship and improperly encroach on the regulatory authority of another agency. As pointed out by the ABA Standing Committee on Client Protection,² payee notification does not regulate lawyer conduct or the practice of law. It regulates the conduct of insurance companies only, and does so as a supplemental means of protecting the public from a known risk of harm. That the harm in question would result from a lawyer's violation of the Rules of Professional Conduct does not convert insurance regulation into lawyer regulation. At most, it encourages and promotes lawyer compliance with legal/ethical obligations, just as the criminal law against theft promotes lawyer compliance with legal/ethical obligations. But it does not give the Office of the Insurance Commissioner authority over lawyers or represent an attempt to regulate the practice of law.

It has also been suggested that the Lawyers' Fund for Client Protection suffices to remedy losses caused by lawyer theft in this context. To be sure, the Lawyers' Fund is available, in appropriate cases, to mitigate this type of loss. But a Lawyers' Fund gift can only ever be an after-the-fact, restorative remedy, capable of assisting those sophisticated enough to file an effectual application and determined enough to await the Fund's review and approval processes. Indeed, a client may have to endure a long period of financial hardship in the wake of a theft of insurance proceeds before this remedy becomes available. Additionally, as pointed out by the ABA Standing Committee on Client Protection,³ a theft of this nature may be too large to be fully reimbursed by the Lawyers' Fund.⁴ Because it is not preventive, a Lawyers' Fund gift does nothing to assuage the trauma and stress necessarily experienced by victims of lawyer dishonesty. A genuinely preventive mechanism such as payee notification, by contrast, is designed to deter wrongdoing before any money is misappropriated and dissipated. In some

² Letter from Lindsey D. Draper, Chair, ABA Standing Committee on Client Protection, to Insurance Commissioner 2 (Dec. 4, 2015) [hereinafter ABA Letter].

³ ABA Letter, at 1-2.

⁴ In Washington, a Lawyers' Fund gift is limited to \$75,000. See WSBA Lawyers' Fund for Client Protection, *Trustees' Annual Report* (Dec. 2015), at 4. In the Callow and Boddy cases, for example, a Lawyers' Fund gift could only partially compensate claimants whose losses substantially exceeded \$75,000.

circumstances, such ex ante protection may eliminate the risk of loss entirely.

Finally, it has been argued that payee notification is inconsistent with Washington's Rule of Professional Conduct (RPC) 4.2 (Communication with Person Represented by a Lawyer). Not so. This argument appears to be premised on the idea that, because insurance companies are typically represented by counsel, the company's notification of a represented claimant in compliance with the payee notification rule could expose the insurance company's lawyers to disciplinary action. Again, as observed by the ABA Standing Committee on Client Protection,⁵ the rule entails an administrative notification only. It does not require any communication by an insurance company lawyer with a represented claimant. Even more important, perhaps, is the provision in RPC 4.2 that suspends operation of the rule when the communicating lawyer "is authorized to do so by law." Should the Office of the Insurance Commissioner adopt the payee notification rule, then the insurance company's notification would be "authorized by law" within the meaning of RPC 4.2 in the unlikely event that an insurance company's lawyer were somehow involved. To our knowledge, in the fifteen jurisdictions that have adopted payee notification, no lawyer has ever been disciplined under RPC 4.2 for facilitating compliance with the rule.

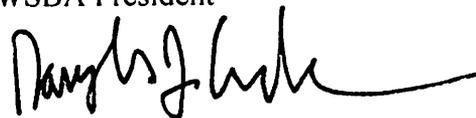
In sum, because payee notification is a reasonable, ABA-endorsed measure to protect the public, the Washington State Bar Association and its Chief Disciplinary Counsel strongly support adoption of the proposed payee notification rule by the Office of the Insurance Commissioner.

If you have any questions regarding the positions stated herein, please direct them to Chief Disciplinary Counsel Douglas J. Ende, at (206) 733-5917 or douge@wsba.org.

Sincerely,



William D. Hyslop
WSBA President



Douglas J. Ende
WSBA Chief Disciplinary Counsel

⁵ ABA Letter, at 2.