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SUPREME COURT OF NEW JERSEY
Disciplinary Review Board
Docket No. DRB 92-120

IN THE MATTER OF

HUGO L. MORAS,

AN ATTORNEY AT LAW

Decision and Recommendation
of the
Disciplinary Review Board

Argued: May 20, 1992

Decided: July 23, 1992

John J. Janasie appeared on behalf of the Office of Attorney Ethics.

Robert H. Jaffe appeared on behalf of respondent.

To the Honorable Chief Justice and Associate Justices of the Supreme Court of New Jersey.

This matter arose from a demand audit performed by the Office of Attorney Ethics (OAE), pursuant to R.1:21-6(g). The formal complaint charged respondent with recordkeeping violations, commingling of personal and trust funds and knowing misappropriation of client funds.

The facts are as follows:

Admitted to the New Jersey bar in 1975, respondent is a sole practitioner in South Orange, Essex County. On October 8, November 5 and December 15, 1986, Christopher D. McKay, an auditor with the OAE, conducted an audit of respondent's attorney records for the period July 1, 1983 through September 30, 1986. The audit uncovered the following improprieties:

I. RECORDKEEPING VIOLATIONS

Respondent did not maintain receipts or disbursements journals for either the trust or the business account; did not keep a running checkbook balance; did not always maintain client ledger sheets, and did not prepare bank reconciliations and schedule of client ledger balances, all in violation of R.1:21-6.

II. THE LIVINGSTON OAK INVESTMENTS MATTER

From October 8, 1985 through June 1986, respondent made several disbursements from his trust account to Livingston Oak Investments (Livingston Oak), a partnership in which he had a one-third interest (Exhibit P-5 at 10). Those disbursements totalled $7,374.50. Livingston Oak was the owner and landlord of the real property where respondent maintained his law office. The complaint charged respondent with knowing misappropriation of trust funds to satisfy his personal obligations to Livingston Oak.

At the DEC hearing, respondent conceded that said payments represented rent obligations of his office to the partnership. He contended, however, that the withdrawals had been covered by earned legal fees left in his trust account.

III. THE HUGHES MATTER

Isabel Hughes was respondent's friend of long-standing. Also, as an employee of her husband's real estate agency, she referred numerous clients to respondent. On November 20, 1985, Mrs. Hughes telephoned respondent to request that he issue to her order a check

from his trust account in the amount of $17,900. The check was designed to set aside a judgment of foreclosure on real property in which Mrs. Hughes had an interest. According to Mrs. Hughes, the attorneys for the mortgagee insisted on receiving either a certified or a trust account check. Hence her request to respondent for a trust account check, which was to be covered by a corresponding check from her.

On the afternoon of November 20, 1985, Mrs. Hughes stopped by respondent's office to pick up the trust account check and deliver her check to him. She gave respondent two checks: one for $2,664 from a John J. Scura, payable to Isabel and Walter Hughes and endorsed over to respondent, and the other for $15,236, in the form of a personal check from Mrs. Hughes. Respondent, in turn, issued a trust account check No. 673 for $17,900, dated November 20, 1985, and payable to Isabel Hughes (Exhibit P1-B2).

There is little agreement about what happened immediately after the exchange of the checks. According to the OAE auditor, respondent confessed to him that, before he issued the $17,900 trust account check, he telephoned Mrs. Hughes' bank to determine if there were sufficient funds in her account. The bank informed him that there were not. Still according to the auditor, despite this knowledge, respondent issued the trust account check to Mrs. Hughes. Respondent also admitted to the auditor that he had not immediately deposited the $15,000 Hughes check because of the lack of sufficient funds. In fact, respondent never deposited this check in his trust account.

Mrs. Hughes, in turn, testified that, at the time that she presented the checks to respondent, she believed that there were enough funds in her account to cover them because she had arranged for a friend to advance her equivalent funds. She admitted that she still had not deposited the friend's check in her account when she gave respondent the $15,000 check, but she knew that her friend had more than enough funds in her account to cover the loan. Much to her dismay, however, two or three days after respondent issued her the $17,900 check, she learned from him that her account did not contain $15,000, presumably because her friend's check was not negotiable. Mrs. Hughes denied any suggestions that she had disclosed to respondent that her own check was not good at the time that she presented it to him.

Respondent's testimony was at odds with the OAE auditor's. According to respondent, Mrs. Hughes had first told him that the checks that would be exchanged for his trust account check were from a bankruptcy trustee and from the Hughes agency. When he gave Mrs. Hughes the $17,900 check, he did not examine the two checks. The following day, he discovered that, contrary to his belief, the $15,000 check was not a company check, but, instead, Mrs. Hughes' personal check. He then telephoned the bank and found out that her account had insufficient funds to cover his trust account check. He quickly contacted Mrs. Hughes, who assured him that the funds would be in the account immediately. Notwithstanding this promise, Mrs. Hughes did not give the funds to respondent forthwith and, in fact, never repaid the $15,000 in

full, as seen below.

Respondent admitted that he did not stop payment on the check, although he had the opportunity to do so. He candidly testified that

> I felt that I would start a chain reaction down the line that would probably be catastrophic, and I mean call me naive or bad judgment, but she told me she would give me the money. This woman had never done anything to make me think she was dishonest because I had dealt with her. I had believed her. Looking back, in hindsight, it was probably the worse thing I have ever done in my career, but I trusted her. That's what it came down to here.

[T1/30/91 136]

The $17,900 check cleared respondent's trust account on November 27, 1985, thereby invading client funds. At the DEC hearing, respondent conceded that the $17,900 withdrawal caused him to be out of trust, although no checks were ever returned for insufficient funds. Respondent also admitted that he did not have enough legal fees in the trust account to cover the $15,000 deficiency (T3/7/1991 107-108).

Ultimately, Mrs. Hughes paid $12,500 to respondent, mostly by way of real estate commissions that she received. Respondent was unable to recall or produce a schedule of payments. He remembered only that the repayments were "in the two to three thousand-dollar range," and that the first took place within two months of November 10, 1985. In the summer or fall of 1989, after respondent retained counsel to represent him in the disciplinary proceedings, he deposited $2,500 of his own funds into the trust account to make up

for the shortage.[1]

IV. THE MURPHY MATTER

In addition to his business and trust accounts, respondent maintained another trust account titled "special collection account," where all payments from collection matters were deposited. On July 24, 1985, respondent deposited $9,000 in settlement proceeds from a personal injury matter handled in behalf of Edward Murphy. Respondent explained that the settlement had been deposited in the special collection account, instead of the regular trust account, because routinely checks cleared faster when processed through the special collection account.

On August 27, 1985, respondent issued to Murphy a check for $5,933.33, representing the net settlement proceeds. On August 28, 1985, when the check was presented to the bank for payment, it was returned for insufficient funds. When Murphy so informed respondent, the latter forthwith deposited his personal funds into the account and reissued a check to Murphy, which included interest and costs.

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[1] In his brief and at the Board hearing, respondent's counsel argued that there is substantial question on whether respondent was out-of-trust, other than inadvertently for a short time in December 1985, even though Mrs. Hughes never fully reimbursed respondent for the $17,900 check. Counsel pointed to a $5,300 fee earned in the Costanzo matter, which respondent left in his trust account in December 1985. The Board rejected counsel's argument. It is unquestionable that respondent was out-of-trust in November 1985, when he issued the $17,900 trust account check to Mrs. Hughes. It is also unquestionable that the proofs clearly and convincingly demonstrate an invasion of clients' funds. Indeed, on November 27, 1985, when respondent should have been holding $26,061.23 on behalf of two clients, Costanzo and Mock/Ciarfello, his trust account balance was only $20,993.44. In addition, respondent admitted, at the DEC hearing, that he was out-of-trust.

As argued by the presenter, the negative balance in the special collection account was the result of a "charge-back" system, whereby the bank in which respondent had his business account would automatically charge the special collection account in the event of insufficient funds to cover checks drawn against the business account. In the Murphy matter, the deficiency in the special collection account was caused by a $1,150 check from the business account that was returned unpaid. According to the presenter, this "charge-back" practice led to the knowing invasion of the Murphy funds in August 1985.

Respondent did not dispute the cause for the Murphy overdraft. He denied, however, that he had knowledge of the "charge-back" system or had authorized its implementation. His testimony in this regard was corroborated by his secretary, Theresa Donatiello. Both respondent and Ms. Donatiello testified that the latter had communicated to the bank that this "charge-back" system was unacceptable.

At the conclusion of the DEC hearing, the panel found that respondent had committed several recordkeeping improprieties (first count). The panel also concluded that there was no evidence of knowing misappropriation in the Livingston Oaks matter because the record did not clearly and convincingly establish that the fees left in respondent's trust account had been insufficient to cover the payments to Livingston Oaks. The panel concluded, however, that respondent commingled personal and trust funds when he failed

to remove his earned legal fees from the trust account (second count). In addition, the panel found that respondent knowingly misappropriated trust funds when he became aware of the trust account shortage caused by the Hughes check and allowed it to continue until late in 1989, a period of approximately four years (third count). Lastly, the panel found that there was no clear and convincing evidence that respondent had authorized or had knowledge of the "charge-back" system that led to the invasion of client funds in the Murphy matter (fourth count).

CONCLUSION AND RECOMMENDATION

Upon a de novo review of the record, the Board is satisfied that the conclusions of the DEC that respondent's conduct was unethical are fully supported by clear and convincing evidence. The Board, however, is unable to agree with the DEC that respondent knowingly misappropriated client funds.

The DEC properly found that respondent was guilty of poor accounting practices, in violation of R.1:21-6 and RPC 1.15(d). The DEC also properly found that the evidence was insufficient to allow a conclusion of knowing misappropriation in the Livingston Oaks and in the Murphy matters. Indeed, respondent testified that the withdrawals to Livingston Oak had been covered by legal fees that remained in his trust account and there was no evidence that he had authorized, acquiesced to or even been apprised of the "charge-back" system. Accordingly, like the DEC, the Board cannot

conclude that respondent misused client funds with knowledge and deliberation.

The Board, however, is unable to agree with the DEC's finding that respondent misappropriated client funds in the Hughes matter, à la In re Brown, 102 N.J. 512 (1986). The factual setting in Brown differs greatly from the circumstances attendant to this matter.

In Brown, the attorney deposited in his trust account a $20,000 check from a client. He then disbursed those funds without waiting for the check to clear the account. After the $20,000 check was dishonored, the client was unable to come up with the necessary funds to replenish the attorney's trust account. In fact, the client ultimately filed for bankruptcy. The result was a $20,000 shortage in the trust account.

Thereafter, the attorney did nothing to notify the affected parties or to make restitution. Instead, the attorney engaged in a steady practice of invading the funds of one client to pay another. This "lapping" process continued for more than four years.

Two years after the $20,000 deficiency occurred, the attorney's financial difficulties grew worse. In order to satisfy outstanding liens on personal taxes owed by the attorney, the Internal Revenue Service seized $8,000 from an interest-bearing account that the attorney had opened for a client, but that, curiously, listed the attorney's -- not the client's -- social security number. Once again, the attorney resorted to "lapping" to

pay off his client. By then, the trust account shortage had increased to $28,000.

During a four-year span, the attorney's half-hearted attempts to return the purloined funds to the trust account were confined to leaving earned legal fees in the account. These feeble efforts scarcely made a dent in the $28,000 shortage.

More egregiously, the attorney's continuous pilferage of clients' funds was also aimed at self-gain. For with the misappropriated funds of one client the attorney not only paid other clients but also financed his monthly rent for his law office and his secretary's salary.

In ordering the attorney's disbarment, the Court noted that the steps that he had taken to "'correct' the situation amounted to nothing less than the knowing invasion of one client to pay another client," and that he had personally benefitted from his misconduct by the satisfaction of his IRS obligation, the avoidance of the re-mortgaging of his house, and the running of his law office on money that belonged to his clients. In re Brown, supra, 102 N.J. at 516.

Here, respondent's actions also created a deficiency in his trust account when he issued a check against uncollected funds and, the next day, he discovered that one of Mrs. Hughes' checks was not backed up by sufficient funds. But he did not do so knowingly. The evidence does not clearly and convincingly demonstrate that respondent knew, on November 25, 1985, the date he issued his $17,900 trust account check to Mrs. Hughes, that her $15,000 check was not good. Unquestionably, the use of his trust account to

accomodate a friend's interests was improper, as was his issuance of a trust account check before the clearing of the equivalent funds designated to cover it. Nonetheless, respondent's conduct did not constitute knowing misappropriation of clients' funds.

Furthermore, respondent acted with dispatch upon discovering that one of the checks was not covered by sufficient funds. He quickly contacted Mrs. Hughes, who assured him that the monies would be given to him immediately. He had no reason to doubt her, given their long-standing friendship and business dealings. Mrs. Hughes' explanation that the elderly friend who had lent her the monies had forgotten to deposit her own monies in her account also appeared reasonable to him. Clearly, his actions in this regard did not resemble Brown's, who knew that his client would be unable to make good on the $20,000 check because he had filed for bankruptcy.

Moreover, both respondent and Mrs. Hughes testified that Mrs. Hughes had made periodic reimbursement payments to respondent to the extent of $12,500 beginning within two months of the issuance of the trust account check. Neither respondent nor Mrs. Hughes could recall when each installment payment was made and respondent's shabby records made it impossible for the OAE auditor to so verify.

Furthermore, it is unquestionable that respondent ultimately deposited personal monies into the trust account in 1989 when "it became apparent to [him] that [Mrs. Hughes] wasn't making any more payments," T3/7/1991 70, thus restoring the account to its in-trust

position.

In sum, respondent improperly utilized his trust account to accomodate a friend's interests, issued a trust account check against uncollected funds, and acted recklessly when he did not stop payment on the $17,900 check for reasons that, albeit altruistic, are wholly unjustifiable. Coupled with his recordkeeping violations (first count) and the commingling of personal and client funds by leaving earned legal fees in his trust account (second count), respondent's serious misconduct warrants a three-year suspension. A five-member majority so recommends. Two members would have disbarred respondent. Those two members were convinced that respondent's failure to make restitution upon discovering the trust account shortage constituted knowing misappropriation. In those two members' view, respondent's inaction for a period of four years cannot be distinguished from the conduct exhibited by the attorney in In re Brown, supra, 102 N.J. 512 (1986), where, as here, the attorney resorted to a "lapping" process by utilizing funds of one client to pay another until full restitution was made, four years after the occurrence of the deficiency. Two members did not participate.

The Board further recommends that respondent be required to reimburse the Ethics Financial Committee for administrative costs.

Dated: 7/23/92

By: [signature]
Raymond R. Trombadore
Chair
Disciplinary Review Board