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SUPREME COURT OF NEW JERSEY
Disciplinary Review Board
Docket No. DRB 95-043

IN THE MATTER OF

JOHN A. KLAMO,

AN ATTORNEY AT LAW

Decision of the
Disciplinary Review Board

Argued: July 19, 1995

Decided: December 4, 1995

Nitza Blasini appeared on behalf of the Office of Attorney Ethics.

Louis M. Barbone appeared on behalf of respondent.

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

This matter was before the Board based on a recommendation for discipline filed by the District IV Ethics Committee ("DEC"). The formal complaint charged respondent with violations of RPC 1.15(a) (negligent misappropriation and commingling); RPC 1.15(d) (failure to comply with the recordkeeping requirements of R. 1:21-6); RPC 8.1(b) (failure to cooperate with disciplinary authorities); RPC

5.3(b) (failure to supervise a non-lawyer employee) and <u>RPC</u> 1.1(b) (probably intended as <u>RPC</u> 1.1(a) — gross neglect).

Respondent was admitted to the New Jersey bar in 1982. He has no prior disciplinary history.

Respondent was selected by the Office of Attorney Ethics ("OAE") for a random audit of his records, which occurred at respondent's office on June 2, 1992. At that point, respondent had been a sole practitioner for approximately eight months. Prior to that, he had been a partner in a multi-lawyer firm in which he had no financial management responsibilities.

Respondent was not present on the date of the audit. The OAE auditor, Robert Prihoda, met with Maria Macaluso, who identified herself as respondent's paralegal. During the course of the audit, Prihoda found several recordkeeping deficiencies. Specifically, there were no individual trust ledger sheets for each client or for any attorney funds maintained in the trust account for bank charges; attorney funds maintained in the trust account were in excess of the amount necessary to cover bank charges; funds received for professional services were not deposited into the business account; attorney personal funds and trust funds were commingled; a non-lawyer employee (respondent's secretary) was authorized to sign trust account checks and, finally, checks were disbursed against uncollected funds.

At the conclusion of the audit, Prihoda advised Macaluso of the poor condition of the records and left for respondent a checklist identifying all of the deficiencies discovered during the course of his audit. Thereafter, Prihoda made several unsuccessful attempts to telephone respondent so that he could confirm, prior to sending out a formal deficiency letter, that the information Macaluso provided at the audit was, indeed, accurate.

Prihoda was finally able to speak with respondent in or about the early part of October 1992. Thereafter, on October 22, 1992, Prihoda forwarded to respondent a letter formally outlining all of the recordkeeping deficiencies identified during the audit. That letter also required respondent to submit, within forty-five days, a certification that all of the deficiencies had been corrected. The October 22, 1992 letter was supplemented by another letter the following day, emphasizing the importance of the matter and requiring respondent to submit certain reconstructed records along with his certification.

Respondent did not submit the requested certification and documentation by the expiration of the forty-five day period. Therefore, Prihoda made several attempts to telephone respondent to learn the status of his overdue certification. When Prihoda finally spoke with respondent, he promised to "federal express" the requested information by January 18, 1993. Prihoda received respondent's certification on or about January 22, 1993. However, Prihoda found the certification unacceptable. He wrote to respondent on or about January 28, 1993, instructing him to complete the certification in the form previously provided to him. Prihoda subsequently set a February 19, 1993 deadline for receipt of that certification. When respondent again failed to comply with the deadline, Prihoda wrote yet another letter to respondent, demanding that he supply the appropriate certification and documentation by March 8, 1993 and threatening to refer the matter for disciplinary action in the event of respondent's non-compliance.

Respondent did, indeed, submit his certification by that date. However, the certification was again deemed unacceptable. Moreover, and more seriously, one of the ledger cards that accompanied the certification contained the notation that respondent had left in the trust account a fee in the amount of $6,993.84 to cover a "deficiency which occurred in the early part of 1992." Exhibit 5. Prihoda testified that the notation was the OAE's first indication that there was any shortage in the trust account. Up until that point, Prihoda had assumed that respondent was simply experiencing some recordkeeping problems.

Upon learning of that shortage, Prihoda immediately telephoned respondent's office and spoke with his secretary, Karla Kauffmann. When he began to question her about the deficiency, Kauffmann insisted that he discuss it with respondent instead. Accordingly, Prihoda spoke with respondent and scheduled another audit visit to his office. When Prihoda met with respondent on March 26, 1993, respondent disclosed to him, for the first time, that Macaluso had embezzled money from both the business and the trust account. Respondent did not know the exact extent of the theft. However, he estimated that Macaluso had removed a total of between $10,000 to $20,000 from the two accounts. Respondent had learned of

Macaluso's theft sometime in August of the prior year — only two months after Prihoda's first audit visit and at least seven months before this second visit. At that point, Prihoda asked respondent to submit to the OAE documentation identifying both the amounts and the timing of the thefts. Respondent did so on April 15, 1993. Attachment A to respondent's answer, Exhibit P-11. Respondent was able to identify at least $14,345 in embezzled funds. Because some transactions were accomplished by telephone, he was unable to certify that amount as the full extent of the thefts.

Prihoda admitted that, while respondent might not have discovered the theft by simply reviewing his monthly bank statements (Macaluso had allegedly altered them), a proper reconciliation of the account, such as that required by R. 1:21-6, and the certification process would certainly have disclosed a shortage, warranting further inquiry.

Respondent's secretary, Karla Kauffmann testified that, when respondent left the Avena firm to start his own practice, Macaluso volunteered to help. Shortly thereafter, Macaluso began to take on the recordkeeping responsibilities simply because Kauffmann did not have the time to do it. While Kauffmann continued to disburse checks from the accounts, Macaluso "overlooked" her work. T81.[1] Specifically, Kauffmann testified, Macaluso "reconciled the statements at the end of the month and she made the deposits or any little errands to run to the bank . . . she would go over the work, my additions in the book and then would post everything in columns

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1 "T" denotes the DEC hearing transcript of June 2, 1994.

. . . ." Id. According to Kauffmann, Macaluso was the first person in the office to see the bank statements.

Kauffmann testified that it was she who first learned of a problem in the accounts when she went to the bank to make a deposit in mid-August 1992. At that time, she was advised by bank personnel that respondent's accounts were to be closed out by the end of the week because of the problems they had experienced. Apparently, Macaluso had been advised of this directive sometime earlier but had not shared that information with her or respondent. Upon learning of that intended action, Kauffmann expressed surprise and asked to see the current balances in the accounts. When the balances shown on the bank's computer screen were shown to be substantially lower than her checkbook balances, Kauffmann knew something was amiss.

Kauffmann telephoned respondent that evening at his home and advised him of her discovery. Respondent immediately telephoned Macaluso. Although Macaluso admitted to respondent, during their telephone conversation, that she had stolen funds from both the business and the trust accounts, she was somewhat evasive in terms of the exact or approximate amounts. Therefore, respondent telephoned Kauffmann to ask her to meet him back at the office, where they immediately began the process of trying to identify the nature and extent of the thefts. During their review, respondent and Kauffmann found that Macaluso had altered the bank statements. Specifically, Macaluso had "whited out" those checks representing funds that she had withdrawn and replaced those amounts either with the word "void" or with another amount "so that that balance would represent what [Kauffmann] had in [her] checkbook." T111. In addition, their review disclosed that a number of checks were missing. (It is not clear whether Kauffmann was referring to missing canceled checks or blank checks, which had been removed out-of-sequence and not yet negotiated). Despite Macaluso's theft, all of respondent's clients received all amounts due them. There is no claim to the contrary by the OAE, despite the apparent trust account shortage.

As the first order of business on the following morning, both Kauffmann and respondent went to the bank, advised bank personnel of their discovery, closed out the existing trust account and opened up a new one. They then requested copies of the original bank statements, as Macaluso had altered their originals. Apparently, respondent experienced some difficulty in obtaining these records on an expedited basis.

Kauffmann admitted that she had been aware of some prior intermittent problems in the business account. Specifically, there had been occasions when the business account showed a negative balance. The first such occurrence was in February or March 1992. (It should be noted that respondent's certification identified February 1992 as the first occasion on which Macaluso embezzled funds from the trust account). On that occasion, she brought the matter to respondent's attention. Although respondent's reaction to that information is not clear from the record, Kauffmann testified that the firm was too new to determine the source of the problem.

Respondent admitted that he failed to keep the appropriate records and engaged in prohibited activities (e.g., drawing against uncollected funds and allowing a non-lawyer to sign trust checks). Furthermore, it is clear that he did not instruct Macaluso or Kauffmann on the proper maintenance of the appropriate records. Indeed, respondent himself had no familiarity with the required financial records and procedures, having been in solo practice for only a matter of months at the time of the initial audit. Moreover, respondent testified, he came from a firm in which he had no financial or recordkeeping responsibilities and learned the little he knew by observing the practices of his former employer. Respondent did not attempt to familiarize himself with the recordkeeping requirements of R. 1:21-6. Indeed, when respondent left the multi-lawyer firm and began his own practice, his primary concern was "defining everything where expenses would go." T147.

Respondent testified that Macaluso offered to help him with the bookkeeping in his practice because of their past intimate relationship and then-current friendship. Apparently, respondent and Macaluso had lived together in or about 1977 and had remained friends after their personal relationship had ended. Because Macaluso had some kind of accounting background and Kauffmann did not, respondent accepted Macaluso's offer to help. Respondent maintained that, while he did not involve himself in any aspect of the recordkeeping, he devised a system of "checks and balances":

Kauffmann would write, sign and disburse the checks and Macaluso would balance the monthly statements. T149. Respondent admitted that no one performed a quarterly reconciliation of the records.

Respondent testified that, immediately prior to learning of Macaluso's theft in August 1992, he had become aware of several overdrafts in his business account only. On those occasions, he would question Kauffmann as to the reason, always believing that he had sufficient funds in his business account. Perplexed, he telephoned the bank and learned that there was a "problem" with his account balance. T133. Because he was scheduled to be in court that day (as he was every day), respondent sent Kauffmann to the bank to ascertain the problem. It was on that day that they learned of the thefts.

Respondent's testimony with regard to his immediate subsequent actions was consistent with Kauffmann's. He added, however, that he did not retain the services of an accountant to identify the shortages on a more expedited basis because he could not afford it. As it happens, respondent's sister was a CPA and she ultimately assisted him seven months later in reconciling the records. It is not clear why respondent did not enlist his sister's aid when he initially experienced difficulty in identifying the full nature and extent of the thefts.

Respondent maintained that he did not immediately notify OAE of the thefts for several reasons. His first concern was to identify the thefts and to ensure that no client had suffered any damage. In addition, however, respondent was scared of the ethics consequences the theft might visit upon him, especially after having just been the subject of an audit. Finally, respondent testified that he was not certain of his ethics obligations in this context because: "this is in August and my feeling was the audit had been completed. I didn't have any documentation from the audit board except the June 2, 1992 letter, so at that time my obligation was to the clients and what funds had been missing and to make sure the trust account was whole." T135. However, noteworthy in this regard is respondent's admission both that he had received the deficiency checklist Prihoda left for him and that he and Prihoda had been "bouncing phone calls back and forth" between June 2, 1992 and October 7, 1992, when they were finally able to talk to each other. In spite of the fact that respondent knew of Macaluso's thefts by that date, he mentioned nothing to Prihoda. Rather, he answered only the question Prihoda posed, which was whether respondent had completed correcting the deficiencies noted on the checklist. Respondent simply replied in the affirmative.

In August 1992, ostensibly due to his uncertainty regarding his ethics responsibilities vis-à-vis reporting the theft, respondent sought the legal advice of his former law partner. In respondent's presence, his law partner telephoned several other attorneys throughout the county, including the attorney retained by Macaluso. His former law partner, Macaluso's lawyer and various other unnamed Camden County attorneys reached the decision that "no one would call up the Ethics Board and say there was a theft." Respondent chose to rely on the decision of his former law partner and Macaluso's attorney, as well as various other unnamed, yet "very well known," attorneys in the community. T172-3. Because of respondent's personal relationship with Macaluso, the former law partner advised respondent to require Macaluso to pay him only a sum certain ($10,000) to reimburse him immediately for the funds respondent deposited into the business and trust account. This "sum certain" solution was apparently suggested because respondent could not, at that point, determine the exact extent of Macaluso's thefts. Both respondent and the former law partner felt that respondent should forego any "legal action" against Macaluso because of the past personal relationship. A release memorializing the terms of this agreement between respondent and Macaluso was executed on some undisclosed date. Attachment to respondent's certification of April 15, 1993.

Respondent did not report Macaluso's criminal activity to the prosecutor's office. In addition, in response to a panel member's specific question, respondent admitted that, in order to reconcile the bank statements to the certification he finally submitted to the OAE, it became necessary for him to disclose the trust account shortage and, thus, ultimately, the theft. It is not clear, thus, whether respondent would have disclosed the theft or the shortage to the OAE but for that fact.

Finally, respondent denied that he wilfully failed to cooperate with the OAE. He maintained that his failure to submit timely certifications to the OAE was occasioned by the fact that he had not received all the necessary bank records to enable him to determine the exact amount of Macaluso's theft. Presumably, however, respondent received the September bank statement sometime in October. Since respondent had discharged Macaluso upon discovery of the thefts, one would assume that she no longer had access to respondent's checks and other records at that point. It is not clear, therefore, why respondent could not provide a certification shortly after the receipt of his September 1992 bank statement.

* * *

The DEC found respondent guilty of a failure to maintain those records required by R. 1:21-6, in violation of RPC 1.15(d). The DEC also found respondent guilty of commingling, by virtue of his failure to remove earned fees from his trust account, and of negligent misappropriation, both in violation of RPC 1.15(a). The DEC further found respondent guilty of gross neglect, in violation of RPC 1.1(a). Furthermore, the DEC found that respondent had failed to adequately supervise his non-lawyer employee, Macaluso, in violation of RPC 5.3. Finally, while the hearing panel report is not entirely clear on this point, it appears that the DEC found respondent guilty of a failure to cooperate with the OAE, in violation of RPC 8.1(b). The DEC noted several mitigating circumstances, such as respondent's unfamiliarity with the recordkeeping rules, inexperience as a sole practitioner and, finally, respondent's admission of wrongdoing and apparent contrition. The DEC recommended that respondent receive "the lowest form of discipline available under the new rules and would recommend that discipline, if possible, take the form of mandatory attendance at courses set up by the Supreme Court or Office of Attorney Ethics in maintaining business and trust records and supervision of employees concerning same." Hearing panel report at 6-7.

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Upon de novo review, the Board is satisfied that the DEC's findings of unethical conduct are clearly and convincingly supported by the record.

Respondent delegated his recordkeeping responsibilities to an employee, Macaluso, whom he never instructed or supervised. Moreover, even when respondent's secretary made him aware of at least one overdraft in the business account, respondent did not conduct an investigation. Although it is true that Macaluso altered enough records to make detection of her thefts difficult through a cursory review of the bank records, certainly the records' reconciliations required by the rule would have alerted respondent to a recurrent problem. Respondent himself testified that his accounts were not high-volume at any given point. Having begun his own practice only months before the June 1992 audit, respondent was certainly in the best position to know what was happening in his client's cases, such as settlements, expenses and fees. Respondent simply perceived himself to be too busy to involve himself in recordkeeping responsibilities. The price for respondent's ultimate dereliction was the invasion of client funds. That no client was actually injured was merely fortuitous.

The Board was particularly troubled by respondent's conscious choice to hide Macaluso's thefts from the OAE for a period of over seven months. During that seven-month period, respondent allowed Prihoda to write letter after letter and to make telephone call after telephone call to obtain from him a simple certification. If respondent was unable to provide the certification because he lacked the necessary bank records, he should have said so. He chose instead to avoid a direct confrontation of the issue with the OAE and, in that course, delayed the pending records' audit. Had respondent been forthright from the beginning, the OAE certainly would have directed its energies into more relevant inquiries, which, according to all indications, would have resulted in different treatment of respondent.

While the Board views respondent's less than candid conduct towards the OAE as serious, it cannot conclude that respondent acted out of venality. Rather, he exercised poor judgment as the result of a combination of factors: his inexperience with financial records, the competing demands that become accentuated by solo practice and, most significantly, by his former law partner's misleading, inaccurate legal advice. Instead of conducting a thorough and legitimate research for respondent — his client — the former law partner instead called the Macaluso's attorney for his opinion of respondent's obligation to report Macaluso's client's criminal conduct to the OAE and to contact various other attorneys to learn how they would proceed in respondent's situation. It should have come as no surprise to respondent's counsel that the Macaluso's attorney would not advocate, in the form of opinion or otherwise, any action that would put his client in jeopardy of criminal prosecution. Nor should the former law partner have expected any reaction from his colleagues other than reluctance to report such activity to the OAE. The former law partner should have been ashamed to pass off the results of his own personal poll as "legal advice" — and respondent should have known better than to so readily accept it as such. Clearly, respondent's judgment in this regard was, to some extent, colored by his prior intimate relationship with Macaluso. However, that does not excuse his serious ethics offenses.

The issue of the appropriate quantum of discipline remains. Generally cases involving similar misconduct have resulted in discipline ranging from a reprimand to a term of suspension. The OAE urged the imposition of a reprimand, citing In re Barker, 115 N.J. 30 (1989). In that case, the attorney was publicly reprimanded for flagrant recordkeeping deficiencies, failure to supervise his part-time bookkeeper's work and failure to reconcile his attorney records on a regular basis, all resulting in one instance of negligent misappropriation.

More serious cases of negligent misappropriation have resulted in terms of suspension. See In re James, 112 N.J. 580 (1988) (attorney suspended for three months for serious and inexcusable inattention to accounting details over a twenty-four year period, resulting in negligent misappropriation); In re Gallo, 117 N.J. 365(1989) (attorney suspended for three months for failure to comply with proper accounting procedures over a five-year period); In re Librizzi, 117 N.J. 481 (1990) (attorney suspended for six months for negligent misappropriation of client funds resulting from extremely serious recordkeeping violations, including failure to reconcile his trust account records for twelve years).

More analogous, is In re Stransky, 130 N.J. 38 (1992). In that case, the attorney was suspended for one year for negligent misappropriation, resulting from the complete delegation of his recordkeeping responsibilities to his wife, who was his secretary/bookkeeper, without oversight of her actions. Ultimately, the attorney's wife embezzled more than $32,000 of client funds over a one-year period. The attorney's own funds were also affected by his wife's theft. The Court noted:

> As an individual, it might be reasonable, albeit perhaps unwise, to delegate all personal financial matters to one's spouse. As an attorney, such conduct cannot be tolerated. The attorney's fiduciary responsibility for client trust funds is a non-delegable duty. In turning over his attorney trust account to his wife without any attempt to supervise the disposition of client trust funds, respondent violated that duty. Moreover, his actions set up the scenario through which his wife was able to steal client trust funds.
> [Id. at 44].

Although that attorney was ultimately able to make his clients whole, the Court viewed his ability to do so as "merely fortuitous" before even greater consequences befell him and his clients. See also In re Tysowski, 135 N.J.344 (1994) (attorney suspended for two years for failure to maintain required financial records; negligent misappropriation prompted by his employee's improper practices vis-à-vis the trust account and for gross neglect and pattern of neglect in eleven separate client matters. The attorney had also been the subject of two prior, but recent, private reprimands).

Recently, in In re Hofing, 139 N.J. 444 (1995), the Court adopted the decision of the Board to publicly reprimand an attorney for negligent misappropriation caused by the theft of trust funds by the attorney's employee and friend. The attorney had completely delegated all recordkeeping responsibilities to his employee, who embezzled over $460,000 of trust funds over a four-year period. While the attorney was the only authorized signatory of trust account checks, he as a matter of practice gave his employee trust account checks signed in blank so that she could transact business in his absence. In imposing only a reprimand, the Court took into consideration numerous mitigating factors, including respondent's prior unblemished professional record of thirty-three years; his contribution to the community; his reputation for honesty and integrity among his peers; his prompt disclosure of the true facts to the OAE following his discovery of the improprieties; his full cooperation with the OAE; his cooperation with the Prosecutor's Office in the prosecution and ultimate conviction of his bookkeeper; his quick action in retaining the services of an accounting firm to ascertain the extent and identity of client funds stolen by his bookkeeper; the fact that, as recognized by the OAE, the attorney might not have detected his bookkeeper's defalcation, even if he had diligently reviewed his attorney records, because of the bookkeeper's fabrication of the account journal at the time of the random audit; his prompt restitution to his clients; and his continuing personal and financial injury as a result of his bookkeeper's criminal acts.

Here, like Hofing, there are numerous mitigating factors. Respondent had been in sole practice for only a short period of time when the thefts occurred and would spend a substantial amount of his day in court. Thus, the demands of his new practice were such that little time was left for much of anything else. In addition, once respondent became aware of a problem in his trust account, he acted promptly to identify each incident and to ensure that no client suffered any loss as a result of the thefts. Moreover, respondent reimbursed his trust account for the shortages caused by Macaluso's thefts and has corrected his prior improper practices. In addition, like Hofing, if respondent had reviewed his records, he might not have detected Macaluso's defalcation, given her alteration of the bank statements and journals. Furthermore, respondent submitted numerous letters from former and current clients, attesting to his character and ability. Finally, respondent has no prior history of any ethics infractions.

Under a totality of the circumstances, the Board has unanimously determined to reprimand respondent for misconduct. One member did not participate.

The Board further determined to require respondent to reimburse the Disciplinary Oversight Committee for appropriate administrative costs.

Dated: 12/4/95

LEE M. HYMERLING
Chair
Disciplinary Review Board