Supreme Court of New Jersey
Disciplinary Review Board
Docket No. DRB 21-142
District Docket No. XIV-2017-0542E

In the Matter of	:
Richard J. Pepsny	:
An Attorney at Law	:

Decision

Argued: October 21, 2021

Decided: December 21, 2021

Hillary K. Horton appeared on behalf of the Office of Attorney Ethics.

John A. Zohlman, III appeared on behalf of respondent.

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

This matter was before us on a recommendation for a reprimand filed by a Special Master. The formal ethics complaint charged respondent with having violated RPC 1.7(a)(2) and (b)(1) (conflict of interest); RPC 1.8(a) (prohibited business transaction with a client); RPC 1.15(a) and the principles of In re

Wilson, 81 N.J. 451 (1979), and In re Hollendonner, 102 N.J. 21 (1985) (knowing misappropriation of escrow funds); RPC 1.15(b) (failure to promptly deliver funds to a third party); RPC 1.15(c) (failure to safeguard funds); RPC 8.4(b) (commission of a criminal act that reflects adversely on a lawyer's honesty, trustworthiness, or fitness as a lawyer in other respects); and RPC 8.4(c) (conduct involving dishonesty, fraud, deceit or misrepresentation).

Although we determine that respondent committed misconduct, we are unable to reach a consensus on the proper quantum of discipline. As set forth below, four members found that respondent negligently misappropriated escrow funds and voted to impose a three-month suspension. One Member also found that respondent negligently misappropriated escrow funds and voted to impose a one-year suspension. Four Members found that respondent knowingly misappropriated escrow funds and, therefore, voted to recommend to the Court that he be disbarred.

Respondent earned admission to the New Jersey bar in 1993 and has no prior discipline. During the relevant timeframe, he maintained a practice of law in Red Bank, New Jersey.

The facts of this matter are largely undisputed, although respondent denied having violated any RPCs.

Respondent maintained an attorney trust account (ATA) and an attorney business account with Bank of America. In 2014, he represented Capital City Equities IV, LLC (CCE) in connection with its purchase of two adjacent parcels of real estate in Toms River, New Jersey (the Property). CCE secured an acquisition and development loan from the grievant in this matter, Alpha Funding Solutions, LLC (AFS), to finance its purchase of the Property and to build two modular homes – one on each parcel. Initially, AFS funded a $196,717.70 loan towards the acquisition of the Property. Thereafter, a schedule of draws required AFS to disburse an additional $303,286.70 to fund the construction and installation of the two modular homes.

In addition to his representation of CCE, respondent also served as the escrow and settlement agent for the loan transaction. Accordingly, the AFS loan proceeds flowed through his ATA, pursuant to its closing instructions, as lender. Respondent prepared the HUD-1 settlement statement, which listed two $29,000 disbursements from the AFS loan proceeds, earmarked as down payments to Westchester Modular Homes, INC (WMH), the vendor constructing the two modular homes. In connection with the closing of the loan, consistent with the HUD-1 and AFS's closing instructions, respondent disbursed a total of $58,000 to WMH, by way of the two $29,000 transfers, which comprised loan proceeds advanced by AFS to partially fund the construction of the two modular homes.

The HUD-1 specifically designated $29,000 to WMH for the first modular home and $29,000 to WMH for the second modular home, listed by the address of each parcel.

Prior to the closing of the loan, respondent had agreed to provide a $30,000 short-term loan to Robert Casper, a principal of CCE. That sum was the exact amount of cash that AFS required CCE to advance to consummate the closing. Respondent testified that he provided the $30,000 loan to CCE to enable it to close on July 11, 2014 and admitted that the terms of the loan were not reduced to writing. Additionally, respondent did not personally possess $30,000 to loan to CCE and, therefore, he borrowed the funds from his brother, Steven Pepsny, and deposited them in his ATA for the benefit of CCE. The terms of the loan between the brothers also was not reduced to a writing, but the $30,000 cash sum was reflected on the HUD-1. The presenter argued that the HUD-1 clearly stated that the funds were to be used for the purchase of the Property. In turn, respondent's counsel argued that the $30,000 was required to close the loan, but that there was no specific designation as to how those particular funds were to be utilized.

The OAE charged respondent with having failed to adequately advise CCE and Casper to consult with independent counsel regarding the $30,000 loan. In turn, respondent argued that he had obtained a written waiver of any

attendant conflict through his July 11, 2014 correspondence, which was signed by Lou Casper, Kenny Halvorsen, and Dan Lieberman, principals of CCE, and that the correspondence was sufficient to meet his obligations under the RPCs. However, respondent conceded that (1) although he sent the July 11, 2014 correspondence – which he referred to as a conflict letter – the specific terms of the $30,000 loan arrangement were not included in the letter, and (2) he "absolutely" should have included the terms in the correspondence.

Respondent described the $30,000 loan arrangement as an informal agreement with clients he trusted and had known for a "very long time." He described CCE as a newly-formed LLC and Robert Casper as a good friend. However, respondent admitted that the arrangement could have exposed his client, CCE, to liability – for example, if it ultimately decided to pay back the $30,000 loan to him, rather than pay off the AFS mortgage. He further admitted that he "should never have agreed to lend money to a client and remain[ed] involved in the transaction representing the client," and that an appearance of impropriety was created by the loan.

Respondent also testified that he did not personally disclose the loan to the lender, AFS, but believed that he had no affirmative obligation to do so, because the mortgage constituted a hard-money loan and there was no lender

requirement that the source of the funds be disclosed.[1] Respondent maintained that there was no inquiry by AFS into the source of the funds and, thus, there had been no misrepresentation to AFS regarding the source of the funds. However, he conceded that, as the settlement agent, he should have disclosed such information to AFS. Notwithstanding, respondent testified that AFS was aware of both the existence of the loan and his intention to purchase one of the modular homes, once CCE completed the development project.

Mark Callazzo, a fifty-percent owner of AFS, testified that the construction of the two modular homes was crucial to the purpose and security of the loan transaction, and that AFS maintained enough money in the construction reserves to complete the project, so that they did not have to rely on CCE to complete it. Callazzo further testified that, from AFS's perspective, maintaining the $58,000 in deposit funds with WMH "was vitally important to [AFS's] security in the loan." Accordingly, AFS specifically required this $58,000 portion of the loan proceeds to be disbursed directly to WMH, as part of the closing instructions for the loan, because AFS did "not want the borrower to have access to those funds." Rather, AFS required that that $58,000 "be

[1] A hard-money loan is a type of loan secured by real property. Hard-money loans are typically used in real estate transactions, when the lender is an individual or company, as opposed to a bank.

earmarked specifically and only for [WMH]" to construct the modular homes, which made the underlying project valuable and worth AFS's investment.

Callazzo testified that AFS, as a hard-money lender, financed $166,660.70 and required the buyer to contribute $30,000 cash toward the loan. Callazzo further testified that he believed that the $30,000 listed on the HUD-1 was from the borrower. According to Callazzo, AFS had asked if the funds were the borrower's money but did not confirm the source of the funds. Callazzo testified that he "certainly" was not aware that the funds were a loan from the settlement agent to the borrower, and that, in his view, it was important that a borrower's own funds be utilized so that they had "skin in the game." Callazzo admitted that CCE was not obligated to disclose to AFS the source of the $30,000 loan, but he believed that respondent, as the escrow and settlement agent, had an obligation to disclose the source of the funds. He further testified that, if AFS had known that the borrower's source for the $30,000 was another loan, AFS would have declined to fund the transaction.

Robert Goldenberg, Esq., AFS's attorney, testified that he was familiar with respondent because they had conducted prior closings together. He testified that neither respondent nor CCE informed him that respondent and his brother were the source of the $30,000 in cash that the borrower advanced for the closing. However, Goldenberg testified that, unlike banking lenders, hard-

money lenders are not typically concerned with the sourcing of funds advanced by a borrower at closing, because borrowers often have a passive investor.

Subsequent to the closing of the loan, AFS asserted that CCE defaulted on the construction portion of the loan, but, according to respondent, CCE disputed that it had defaulted. It is, however, undisputed that AFS subsequently refused to advance further funding to CCE under the $303,286.70 construction portion of the loan. Thereafter, respondent, Casper, and John Colucci, who was a representative of WMH, participated in a July 24, 2014 telephone conference wherein respondent was asked to provide Colucci with wire instructions to refund $26,000 of the $58,000 modular home deposit advanced by AFS to respondent's ATA.

On July 24, 2014, presumably after the telephone conference, Louis Casper, Robert Casper's brother and a managing member of CCE, sent wiring instructions for respondent's ATA. That correspondence stated:

> Please recall that at the time of our closing we sen[t] you two deposits in the amount of $29,000.00 each to start production on each of the above referenced homes. As we discussed, our lender changed up our draw schedule after our closing and they have now decided that they will not fund the deposit for the second home until we have received our building permits from Toms River.
>
> Accordingly, we ask that you keep $3,000.00 from the second deposit to cover you for the sealed plans, but return the remaining $26,000.00 to our attorney's trust

> account in accordance with the attached wiring instructions. We now need the $26,000.00 to continue with the engineering and site work so that Matt can get the building permits in place without delay. We will return the $26,000.00 production deposit once Matt secures the building permits and we receive the draw from our lender.
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> [CEx.2.][2]

Notably, neither respondent nor AFS were copied on this correspondence. On July 28, 2014, WMH returned to respondent $26,000 of the $58,000 modular home deposit advanced by AFS.[3] Respondent testified that, prior to his receipt of the $26,000 from WMH, Casper had told him that CCE was going to "replace" the deposit with WMH. According to respondent, on July 29, 2014, a few days after respondent's conversation with Casper, he received a $26,000 check from WMH. He conceded that the check came from WMH, and not CCE, but explained that it was his understanding that it was WMH's policy to return the funds to the original source – namely, respondent's ATA. Respondent testified that he assumed that WMH returned the funds because the initial deposit had been replaced by CCE. In further support of his belief that the funds had been replaced, respondent testified that the deposit had been classified as

[2] "CEx." refers to the exhibits attached to the formal ethics complaint, dated January 9, 2018.

[3] During the ethics hearing, respondent testified that WMH returned the $26,000 via a check, not a wire transfer.

"nonrefundable" on the modular company's order form and, therefore, he "had no reason to believe that they were anything other than nonrefundable and had been replaced." Respondent testified that he trusted Casper's representation that the WMH deposit funds had been replaced.

Respondent used the $26,000 returned by WMH, plus an additional $4,000 provided directly by CCE, to repay his brother's $30,000 loan to CCE. However, CCE had not replaced the $26,000 deposit held by WMH.[4] Respondent admitted that he failed to verify that CCE had replaced the $26,000 deposit prior to his disbursement of ATA funds to his brother on July 29, 2014 – the same date he received the funds in his ATA. Specifically, he admitted that he did not contact WMH to confirm that the deposit funds had been replaced, nor did he request a copy of the check from CCE to WMH representing the replacement funds. Respondent further admitted that he should have verified that the $26,000 had been replaced prior to his distribution of the funds to his brother. Respondent

[4] In his January 21, 2016 reply to the OAE's inquiry about the matter, respondent stated that he had "no personal knowledge as to whether the Borrower[, CCE,] ha[d] replaced the deposit money," and that he only became aware of the issue with the deposit eight months after the closing. At the ethics hearing, respondent testified that, nine months after the transaction took place, Callazzo had accused him of impropriety with respect to the disbursement of the $26,000 production deposit. He testified that he was surprised by the allegation, and that he paid Callazzo $1,000 to "keep things on hold" until he could retrieve his file and investigate the matter. It was at this time, in March 2015, that respondent became aware of CCE's position that AFS had defaulted on the loan agreement and, in response, that CCE had withdrawn its working capital from the project. At this time, respondent also became aware that the $26,000 deposit with WMH had not been replaced by CCE.

maintained that he would not have disbursed the funds to his brother if he had known that CCE had not replaced the deposit. During his testimony, respondent had no explanation for why CCE would need to "replace" the AFS deposit funds as a prerequisite to pay back the $30,000 loan, rather than simply use independent funds to pay back the loan.

During the ethics hearing, the Office of Attorney Ethics (the OAE) emphasized respondent's knowledge that only $26,000, not the full $30,000 required to repay the loan, was returned to respondent by WMH. Respondent explained that CCE provided him with a separate check in the amount of $6,112.91, which included the $4,000 necessary to pay back the loan, plus $2,112.91 required to clear title to the Property.

The OAE further alleged that, at the time respondent repaid the $30,000 loan to his brother, he was aware that CCE and AFS were involved in a dispute regarding whether CCE had defaulted and, thus, AFS had a competing claim to the $58,000 in loan proceeds previously disbursed to WMH. In turn, respondent argued that he had not knowingly received or disbursed AFS's funds without authorization. Specifically, he testified that he was aware that the parties had a dispute over the construction draw schedule and that CCE alleged that AFS was in default of their loan agreement but maintained that he believed AFS's position had remained unchanged, because the deposit was intact, based upon his reliance

on Casper's representation that the deposit funds had been replaced. However, during his testimony, respondent also admitted that he was aware that the $58,000 deposit represented loan proceeds advanced by AFS, and that he understood that the deposit was required to be held intact by WMH.

AFS's attorney, Goldenberg, testified that neither CCE nor respondent informed him that $26,000 of the $58,000 modular home deposit had been returned to respondent's ATA. Respondent testified that he had not disclosed to AFS the return of $26,000 from the deposit, even though the lender expected the $58,000 deposit to be held by WMH. Respondent asserted that, because he believed that the $26,000 deposit had been replaced, he did not have a duty to notify AFS that CCE had repaid the loan. Respondent admitted that he did not seek permission from AFS prior to his distribution of the funds to his brother, but that it would have been wise for him to have done so. Moreover, respondent conceded that, up until the time that CCE actually replaced the $26,000 deposit, AFS had a claim to the funds.

In March 2015, eight months after CCE had repaid the $30,000 loan, Callazzo, on behalf of AFS, contacted WMH to confirm that the modular home deposit was intact and discuss what would happen in the event of a foreclosure by AFS. Callazzo testified that he was "very shocked" to learn that the full $58,000 deposit was no longer held by WMH. He further testified that the

$58,000 deposit was AFS's funds, advanced at the loan closing. Callazzo testified that, initially, he was unaware that respondent had used $26,000 of the $58,000 deposit to pay back a loan to his brother and that, had he known, he would have objected and directed his attorney to intervene on behalf of AFS to obtain the $26,000.

Upon being made aware that the full $58,000 deposit was not held intact by WMH, Callazzo's attorney contacted WMH and directed them not to release any portion of the remaining $32,000 in deposit funds. The March 25, 2015 correspondence read as follows:

> We represent Alpha Loan Servicing, LLC ("Alpha") the holder of the first mortgage lien encumbering the above referenced Premises. On or about July 11, 2014 you received an attorney's escrow check in the amount of $29,000.00 from [Respondent], the attorney for Capital City Equities IV, LLC ("Borrower"), the owner of the Premises, representing the initial production deposit, Order #14-054 ("Deposit"). These funds were advanced by Alpha in conjunction with that certain construction loan agreement between Alpha and Borrower and in accordance with the Settlement Statement signed by the parties at the closing of the loan.
>
> Please be advised that at any time during which you are holding the Deposit no amount, either in whole or in part, shall be released or returned to any party other than to Alpha and only in accordance with express written instructions signed either by Mark Callazzo or David Hansel, the managing principals of Alpha.

[Ex.32.][5]

Callazzo also believed that respondent, as the settlement agent, owed him a fiduciary duty to safeguard the modular home deposit funds that had been returned to him in July 2014. Callazzo testified that, upon learning that WMH had returned $26,000 of the deposit to respondent's ATA, he was relieved, because he considered an attorney escrow account to be "sacred," but when he contacted respondent, he became aware, for the first time, of the $30,000 loan to CCE and respondent's disbursement of the $26,000 to repay it. He testified that he requested that the $26,000 be repaid to AFS. Callazzo testified that respondent never indicated any belief that the $26,000 had been "replaced," and that respondent sent him $1,000[6] with subsequent checks to follow. However, Callazzo testified that he received no additional funds from respondent, and that, ultimately, AFS was unable to complete the project and sought to sell "just two pieces of unapproved dirt . . . and recoup as much as [they] can."

At the July 11, 2014 closing, respondent signed the HUD-1, which contained the following statement above his signature: "This Settlement Statement which I've prepared is a true and accurate account of this transaction. I've caused or will cause the funds to be disbursed in accordance with this

[5] "Ex." refers to the OAE's exhibits admitted into evidence at the ethics hearing.

[6] Respondent never sought the return of the $1,000 he paid Callazzo.

statement." The document further stated "[i]t is a crime to knowingly make false statement to the United States on this or other similar form."

The OAE alleged that the HUD-1, which was prepared by respondent, falsely represented that he had disbursed $58,000 to WMH via two separate deposits of $29,000, when, in fact, only $32,000 was disbursed to WMH, considering return of the $26,000 after the closing. Therefore, the complaint charged respondent with having violated RPC 8.4(b) by committing criminal acts reflecting adversely on his honesty, trustworthiness or fitness as a lawyer, particularly, by violating: 18 U.S.C. §§ 1001 and 1010 (fraudulent statement on the HUD); N.J.S.A. 2C:20-4 (theft by deception); N.J.S.A. 2C:21-3 (fraud related to public records and recordable instruments); N.J.S.A. 2C:21-4 (falsifying or tampering with records); and N.J.S.A. 2C:28-2 (false swearing). For the same alleged misconduct, the complaint charged respondent with violating RPC 8.4(c).

Respondent denied those allegations and testified that the HUD-1 was accurate; that, in connection with the closing, the $58,000 modular home deposit was disbursed to WMH; and that the dispute between AFS and CCE did not occur until after the closing. Callazzo also testified that the HUD-1 was accurate at the time of the closing.

At the conclusion of the ethics hearing, respondent's counsel moved for a directed verdict[7] and argued that the OAE had failed to prove, by clear and convincing evidence, that respondent had violated any RPCs. Specifically, counsel argued that there was no evidence to support the claim that respondent knowingly signed a false HUD-1 settlement statement. Indeed, he argued that respondent, Callazzo, and Goldenberg all testified that the settlement statement was accurate. Respondent's counsel conceded that, at some point after the closing, $26,000 of the deposit funds were returned to respondent and deposited in his ATA, but he argued that there was no proof that the HUD-1 settlement statement was fraudulent or contained a misrepresentation.

Counsel further argued that respondent had no duty to notify AFS regarding the return of the deposit funds from WMH. He argued that, per the HUD-1, the $30,000 was not specifically allocated to reduce the purchase price, but that it was to be utilized both to reduce the purchase price and to be applied against closing costs.

Counsel also argued that respondent reasonably had relied on Casper's verbal representation that the $26,000 in deposit funds had been replaced, citing the fact that the deposit was non-refundable and that respondent had no reason

[7] We understand this motion to have been a motion to dismiss pursuant to R. 1:20-5(d)(2) ("a motion to dismiss at the conclusion of the presenter's case in chief").

to believe Casper had not been forthright. Therefore, respondent's counsel asserted, respondent had not engaged in fraud or deceit. He maintained that, based on the lack of knowledge that the $26,000 in deposit funds had not been replaced, respondent could not have knowingly misappropriated funds.

Counsel argued that, in typical RPC 1.7 violation cases, no conflict letter exists. In contrast, he argued that, in the instant case, respondent prepared a detailed conflict letter, all parties were informed of the terms of the transaction, and the conflict letter was signed. Counsel argued that, although the conflict letter did not mention the $30,000 loan to CCE from respondent and his brother, CCE was clearly informed that respondent was the source of the funds, because CCE closed the loan using the $30,000 provided by respondent. He maintained that respondent had no obligation to inform the lender, AFS, regarding the source of the $30,000.

In turn, the OAE argued that respondent had a duty, as the settlement agent, to (1) advise the lender of the source of the $30,000 because, in his role as a fiduciary, he certified that the funds would be disbursed in accordance with the HUD-1, and (2) advise the lender if any of the loan proceeds were returned to him. The OAE argued that respondent knew that $58,000 of AFS's loan proceeds were earmarked for WMH and, in July 2014, $26,000 of the $58,000 was returned to his ATA, which he indicated were "settlement funds" on his

client ledger. The OAE argued that respondent's failure to inform AFS that the deposit funds were returned was deceitful and, thus, constituted a violation of RPC 8.4(c). The OAE also argued that respondent violated RPC 8.4(b) because, although the HUD-1 was accurate when it was submitted, it constituted a misrepresentation upon the subsequent the return of a portion of the deposit.

The OAE argued that respondent knowingly misappropriated escrow funds because, despite his knowledge that the $26,000 in returned settlement funds belonged to AFS, he disbursed the funds to his brother without AFS's prior authorization. Further, the OAE asserted that respondent had engaged in self-help, in violation of his duties as the settlement agent and his obligations to AFS, which required that he confirm that the purported replacement funds had been provided to WMH. The OAE emphasized that respondent knew that the loan funds were in dispute, and that the only way he could pay back his brother was to use the WMH deposit funds. The OAE stressed that respondent's failure to inform AFS about the returned deposit funds or the subsequent disbursement to his brother was further proof of his knowing misappropriation.

The OAE argued that, even if respondent believed that the $26,000 deposit with WMH had been replaced by CCE, he had an obligation, as the escrow agent for the transaction, to confirm that his belief was correct. It further argued that respondent's belief could not honestly have been held, based on the fact that

CCE repaid only a portion of the funds directly, using $26,000 from the WMH deposit to make up the vast majority – $26,000 of $30,000 – required for the repayment.

The OAE argued that respondent also violated RPC 1.8 because he entered into a business transaction to acquire an ownership interest adverse to his client, and the terms of the transaction were not fully disclosed and reduced to a writing. It further argued that the conflict letter prepared by respondent was insufficient, pursuant to RPC 1.7, because it failed to secure a written waiver to the conflict created by respondent's $30,000 loan to his client, CCE.

The Special Master denied respondent's application for a directed verdict. However, he stated that a "[k]nowing [misappropriation] would require that, by clear and convincing evidence it be established that [respondent] was aware, A, that the deposit had not been repaid; and, B, the money returned to him was at that point disputed."

Respondent, through counsel, argued that the OAE failed to prove, by clear and convincing evidence, that he had violated any of the charged RPCs. Regarding the criminal charges, respondent argued that nothing in the record suggested that the HUD-1 was fraudulent and, therefore, those charges should be dismissed. Regarding the charged violations of RPC 8.4, respondent argued that he lacked the required intent to find a violation of the Rule, because the

HUD-1 was complete and accurate, no evidence was presented that he knowingly signed a false HUD-1, and he disbursed the funds according to the HUD-1. Likewise, respondent argued that there was no intentional misrepresentation regarding the source of the borrower's funds because he did not have an affirmative obligation to disclose the source, as corroborated by the testimony of Callazzo and Goldenberg.

Respondent further argued that he did not engage in dishonesty, fraud, or deceit, in violation of RPC 8.4(c), related to the returned $26,000 in deposit funds. He argued that the OAE had offered no evidence to dispute that Casper had verbally represented to him that the $26,000 deposit had been replaced by CCE. Respondent argued that he relied upon Casper's statement that the deposit funds had been replaced and the fact that the purchase order stated that the deposits were nonrefundable. He maintained that he, thus, lacked the intent to deceive required for an RPC 8.4(c) violation. He maintained that from July 11, 2014, the date of the closing, until he was confronted by Callazzo, in March 2015, he was unaware that the WHM deposit had not, in fact, been replaced.

Respondent argued that the violations of RPC 1.15(a) through (c) had not been proven, because he was not obligated to notify AFS, the lender, that he received deposit funds back into his ATA. He argued that a "key fact" was that

Callazzo was equally unaware, until March 2015, that the deposit funds had been returned to respondent.

Respondent argued that he had not violated RPC 1.7(a)(2) or RPC 1.7(b)(1), because he prepared a comprehensive conflict letter that was signed by the involved parties, who knew about the $30,000 loan from respondent's brother to him and, ultimately, to CCE. Respondent further argued that he did not violate RPC 1.8(a), because he and his clients entered into a business transaction, the terms of which were disclosed, and the clients signed the conflict letter. Respondent acknowledged that his conflict letter did not specifically address the $30,000 loan but argued that the "only logical inference" that could be drawn from the record was that CCE was aware that respondent was the source of the funds, because it brought the loaned funds to the closing, without which it could not have closed. He argued that the technical omission is not a violation, because all parties were informed of the conflict and expressly waived it. He further argued that the record contained no evidence that CCE or Casper did not understand or agree to the transaction.

On June 26, 2019, respondent's counsel informed the Special Master that pending criminal charges against respondent, which arose from the same facts underpinning this matter, had been presented to a Monmouth County Grand Jury and that a No Bill had been returned. He argued that, consequently, the charged

violation of RPC 8.4(b), based upon respondent's violation of N.J.S.A. 2C:20-4(c) (theft by deception), could not be sustained and was barred. He further argued that the reliance upon a criminal statute as a basis for a violation of the RPCs was now unsupportable. Counsel also suggested that the Grand Jury found that respondent had not engaged in misappropriation.

The OAE argued that the Grand Jury's return of a No Bill was not dispositive of the disciplinary proceedings. Specifically, the OAE cited In re Gallo, 178 N.J. 115 (2003), wherein the Court explained:

> [H]ad respondent been tried and acquitted of the [criminal] charges, this Court would not have been bound by those findings because the standard in a criminal case is proof beyond a reasonable doubt, whereas a disciplinary proceeding is governed by the lesser standard of clear and convincing evidence. In re Pennica, 36 N.J. 401, 419 (1962); see also id. at 418 ("Acquittal of a member of the bar following trial of a criminal indictment is not res judicata in a subsequent disciplinary proceeding based on substantially the same charge or conduct."); In re Rigolosi, 107 N.J. 192, 526 (1987) (disbarring attorney for bribery despite acquittal on all criminal charges); In re Callahan, 70 N.J. 178, 358 (1976) (same); In re Hyett, 61 N.J. 518, 296 (1972) (same). As there are no restrictions on the scope of disciplinary review in a case of an attorney who was not charged with a crime or who was acquitted of a crime, there is no commonsense or policy justification for imposing such restrictions when an attorney has pled guilty to a crime. This Court's disciplinary oversight responsibility cannot be curtailed by artificial impediments to the ascertainment of truth.
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> [Id. at 120-21.]

The OAE, citing In re Nazmiyal, 235 N.J. 22 (2018), and In re McEnroe, 172 N.J. 324 (2002), argued that a violation of RPC 8.4(b) can be sustained even if an attorney is never charged or convicted of a criminal offense. It further noted that double jeopardy does not apply to disciplinary proceedings, which are not criminal in nature, citing In the Matter of Thomas De Seno, DRB 10-247 (December 13, 2010) (slip op. at 11), and In re Legato, 229 N.J. 173 (2017).

Regarding the criminal statutes, the Special Master found that "[t]here is not a scintilla of evidence presented to suggest the content of the settlement sheet (HUD-1)[. . .] is false or misleading. All funds are accounted for and disbursements are accurately reflected." Accordingly, the Special Master found that respondent did not violate RPC 8.4(b). As outlined below, the Special Master determined that respondent had committed misappropriation, but that it was negligent as opposed to knowing and, therefore, found that there was no violation of RPC 8.4(c), because respondent lacked the required intent.

Regarding the most serious of the charges – respondent's alleged knowing misappropriation of escrow funds – the Special Master stated that the most significant question before him was "the nature and extent of the obligation imposed on the Respondent" upon his receipt of the returned portion of the WMH deposit funds. The Special Master questioned whether it was unreasonable for respondent to have believed that CCE had provided

replacement funds to WMH. The Special Master ultimately determined that respondent's belief was not unreasonable, finding that it was bolstered, versus undermined, by respondent's receipt of the additional $6,112.91 from CCE. Based upon the record before him, the Special Master determined that he could not conclude, by clear and convincing evidence, that respondent was aware that the deposit funds had not been replaced by CCE. The Special Master stated that the OAE faced a "very difficult situation" of having to establish a knowing misappropriation absent an admission by respondent. He noted that there was:

> [N]o direct testimony to suggest [that] the Respondent solicited WMH to return the money, which clearly would have given the Respondent actual knowledge that the funds were not provided to WMH by CCE. Absent that specific knowledge, it cannot be determined [that] the Respondent knowingly misappropriated the funds which were returned by disbursing them to his brother.
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> [1SMR,p6.] [8]

The Special Master determined that he could not infer a knowing misappropriation based upon respondent's disbursement of the returned deposit funds to his brother. He found that respondent's failure to take the necessary

[8] "1SMR" refers to the Special Master's February 4, 2021 report.

steps to ensure that CCE had replaced the deposit funds with WMH was negligent and violated RPC 1.15(b) and RPC 1.15(c).[9]

The Special Master also found that respondent violated RPC 1.7(a)(2), RPC 1.7(b)(2), and RPC 1.8(a) by failing to disclose to AFS the source of the $30,000 loan.

In conclusion, the Special Master found that respondent engaged in a conflict of interest, in violation of RPC 1.7(a)(2), RPC 1.7(b)(2), and RPC 1.8 (a), failed to promptly deliver funds to a third party, in violation of RPC 1.15(b), and failed to safeguard funds, in violation of RPC 1.15(c).[10] He directed the OAE to provide respondent's disciplinary history prior to his recommendation of the appropriate discipline.

The OAE reported that respondent had no disciplinary history. It argued that, although the summary of the Special Master's Report stated that RPC 1.15(a) (knowing misappropriation) was dismissed, the content of the decision held that the lesser included charge of negligent misappropriation had been found. It suggested that the appropriate quantum of discipline, based on the

[9] The Special Master's summary stated that "[t]he alleged ethical violations of RPC 1.15(a) (Knowing Misappropriating Funds) is dismissed" but the decision clearly states that the Special Master found respondent's misappropriation to be negligent as opposed to knowing, which is a violation of RPC 1.15(a).

[10] See footnote 9, above, regarding respondent's negligent misappropriation of escrow funds, in violation of RPC 1.15(a).

Special Master's findings, which included negligent misappropriation, was a three-month suspension because of (1) the serious economic harm that respondent's misconduct caused to AFS; (2) respondent's lack of remorse; and (3) respondent's failure to return the full $26,000 in deposit funds, despite having had opportunities to do so. The OAE referenced supporting disciplinary authority for the recommended three-month suspension.

In turn, in his brief, respondent argued that the alleged violation of RPC 1.15(a) was dismissed. He argued that an admonition was the appropriate quantum of discipline for the RPC violations found by the Special Master, which, in his view, did not include negligent misappropriation. Respondent also requested that the following be considered in mitigation: (1) his lack of disciplinary history in twenty-seven years at the bar; (2) his commitment to public service and pro bono work; (3) his lack of intent to engage in dishonesty, fraud, deceit, or misrepresentation; (4) the determination of the Special Master that there was no dishonesty, fraud, deceit, or misrepresentation; and (5) his willingness to comply with the highest standards of the legal profession.

On April 29, 2021, the Special Master recommended the imposition of a reprimand. He stated that the OAE conceded that reprimands are the quantum of discipline typically imposed for committing negligent misappropriation[11] and

[11] The Special Master did not address the conflicting statements in his February 4, 2021

engaging in a conflict of interest. The Special Master considered, in aggravation, that AFS suffered economic injury, for which respondent was partially responsible. He stated that there was "a plethora of mitigating factors, which suggest the [OAE's] recommended discipline of suspension would be overly harsh." Specifically, the Special Master considered, in mitigation, respondent's lack of disciplinary history in twenty-seven years at the bar and that respondent's misconduct was an isolated incident, which he believed suggested that there was no likelihood of reoccurrence.

In its brief to us, and during oral argument, the OAE reiterated its position that respondent knowingly misappropriated escrow funds that belonged to AFS, for which he should be disbarred.

In turn, respondent maintained that the Special Master correctly found that respondent had a reasonable belief that the WMH deposit funds had been replaced and, thus, properly dismissed the RPC 1.15(a) charge. Respondent conceded that he had committed minor misconduct and asserted that an admonition was the appropriate quantum of discipline.

* * *

report, as outlined in footnote 9 (above), but it is again clear that the Special Master found that respondent negligently misappropriated escrow funds, in violation of RPC 1.15(a).

Following a de novo review of the record, we are satisfied that the Special Master's finding that respondent's conduct was unethical is supported by clear and convincing evidence. We are divided, however, on whether respondent's misappropriation was negligent or knowing and, consequently, are divided on the appropriate quantum of discipline to be imposed. We are unanimous in other findings of misconduct and will begin our analysis on that common ground.

Unanimous Findings of Misconduct

In addition to misappropriation (whether it be negligent or knowing), we all agree that respondent committed additional misconduct. RPC 1.7(a) prohibits a lawyer from representing a client if the representation involves a concurrent conflict of interest. Under the Rule, a concurrent conflict of interest exists if:

> (1) the representation of one client will be directly adverse to another client; or
>
> (2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client, or a third person or by a personal interest of the lawyer.

Under RPC 1.7(b), however, "[n]otwithstanding the existence of a concurrent conflict of interest under paragraph (a)," a lawyer may represent a client, if:

> (1) each affected client gives informed consent, confirmed in writing, after full disclosure and consultation;

> (2) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;
>
> (3) the representation is not prohibited by law; and
> (4) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal.

We unanimously find that respondent engaged in a concurrent conflict of interest, in violation of RPC 1.7(a)(2), because he represented CCE as the borrower in a transaction, acted as the settlement agent for the transaction and, at the same time, had competing financial interests in the transaction – both as a lender and as a potential buyer of one parcel of the Property.

As RPC 1.7(b) provides, despite the existence of a concurrent conflict of interest, an attorney may represent a client, under certain conditions, which include obtaining informed, written consent. In the absence of compliance with all provisions of RPC 1.7(b), an attorney violates RPC 1.7(a)(2). We have consistently emphasized that RPC 1.7(b) operates as a saving provision and, thus, violation of that subpart does not constitute an ethics violation. See In the Matter of Gary L. Mason, DRB 19-448 (October 20, 2020) (slip op. at 6 n.4); In re Mason, 244 N.J. 506 (2021) (finding a violation of RPC 1.7(a)(2) only, despite inclusion of RPC 1.7(b)(1) charge in the formal ethics complaint).

The first provision of RPC 1.7(b) states that the lawyer may proceed with

the representation if, among other things, "each affected client gives informed consent, confirmed in writing, after full disclosure and consultation" (emphasis added). Here, respondent's conflict letter is insufficient because it only addressed part of the conflict and, thus, did not constitute a full disclosure. Specifically, the correspondence addressed the inherent conflict of respondent's representation of the parties and his intent to purchase one of the parcels subject to the transaction, but it did not address the terms of the $30,000 loan.[12] As a result, the correspondence also failed to comply with the second provision of RPC 1.7(b), because it failed to address how the loan might affect respondent's ability to provide competent and diligent representation to each affected client. In the instant matter, we find that there was a significant risk that respondent's representation of CCE and its members would be materially limited by his personal interest. Indeed, that risk was realized when respondent engaged in self-help and put his own interest in recouping the $30,000 loan over CCE's interest in the completion of the real estate transaction.

In that same vein, respondent admittedly failed to provide the required written disclosure or to obtain the informed, written consent of CCE regarding the $30,000 loan in connection with their business transaction. Therefore,

[12] Although it is clear from the record that CCE and its members knew that respondent was the source of $30,000 loan which they brought to the closing, the Rule requires that the terms of the loan be fully disclosed and agreed to in writing.

respondent also violated RPC 1.8(a), which expressly requires such documentation.

We agree with the Special Master that there is insufficient evidence to find, by clear and convincing evidence, that respondent violated RPC 8.4(b) or RPC 8.4(c). Specifically, nothing in the record suggests that the information contained within the four corners of the HUD-1 was inaccurate, misleading, or fraudulent at the time it was executed. Indeed, AFS confirmed that the HUD-1 was accurate at the time of the closing and disbursements of the loan proceeds. Indeed, the instant case focused on the return of deposit funds to respondent's ATA well after the closing. Additionally, both AFS and its attorney agreed that they did not inquire as to the source of the $30,000 that CCE, the borrower, brought to the closing, and acknowledged that such investors or borrowers typically have a passive investor.

Moreover, a violation of RPC 8.4(c) requires intent. See, e.g., In the Matter of Ty Hyderally, DRB 11-016 (July 12, 2011). Although we differ on whether respondent should have accepted Casper's representation that the $26,000 deposit had been replaced, we agree that there is insufficient evidence in the record to find that respondent was on actual notice that the WMH deposit funds had not been replaced. Thus, we conclude that there is insufficient

evidence to find that respondent had the intent required to constitute a violation of RPC 8.4(c).

It is well-settled that, absent egregious circumstances or serious economic injury, a reprimand is appropriate discipline for a conflict of interest. In re Berkowitz, 136 N.J. 134, 148 (1994). However, if the conflict of interest arises from a business transaction between a lawyer and client, the minimum measure of discipline is usually an admonition. See, e.g., In the Matter of David M. Beckerman, DRB 14-118 (July 22, 2014) (during the course of the attorney's representation of a financially-strapped client in a matrimonial matter, he lent the client $16,000, in monthly increments of $1,000, to enable him to comply with the terms of a pendente lite order for spousal support; further, to secure repayment for the loan, the attorney obtained an impermissible mortgage from the client on his share of the marital home; the attorney also paid for the replacement of a broken furnace in the client's marital home; by failing to advise the client to consult with independent counsel, failing to provide the client with written disclosure of the terms of the transactions, and failing to obtain his informed written consent to the transactions and to the attorney's role in them, the attorney violated RPC 1.8(a); he also violated RPC 1.8(e) (providing financial assistance to a client in connection with pending or contemplated litigation) and In the Matter of Frank J. Shamy, DRB 07-346 (April 15, 2008)

(attorney made small, interest-free loans to three clients, without advising them to obtain separate counsel; the attorney also completed an improper jurat; significant mitigation considered).

Reprimands have been imposed when the loan involves a significant amount of money, when the attorney engages in multiple business transactions without the client's informed written consent, when the attorney is guilty of additional ethics infractions, or when aggravating factors are present. See, e.g., In re Rajan, 237 N.J. 434 (2019) (attorney, while representing his client in the purchase of a property that the client intended to develop into a hotel, introduced the client to two other clients who agreed to fund fifty percent of the hotel project; when the client could not fund his fifty percent share, a holding company formed by the attorney and his brother and brother-in-law lent $450,000 ($350,000 of which was the attorney's) to the client so that he could close the transaction; the attorney, thus, acquired a security and pecuniary interest adverse to his client and became potentially adverse to the other clients; the attorney did not advise his clients to consult independent counsel, and he did not obtain their informed, written consent to the loan transaction; the attorney also represented the client in the real estate transaction and received $32,500 in legal fees; violations of RPC 1.7(a) and RPC 1.8(a); despite the attorney's unblemished disciplinary record, the absence of harm to the client, his

acceptance of responsibility, and his expression of remorse, we imposed a reprimand because he exercised such poor judgment; the attorney's prior service as a member of a district ethics committee was considered both in aggravation and in mitigation); In re Allegra, 229 N.J. 227 (2017) (attorney who represented a client in a number of matters engaged in a sexual relationship with her after her application for citizenship was denied, a violation of RPC 1.7(a)(2); he also borrowed $17,500 from her, a violation of RPC 1.8(a); despite significant mitigating factors, we imposed a reprimand, given both conflicts of interest); In re Amato, 231 N.J. 167 (2017) (attorney made three loans, totaling more than $528,000, to his client, and entered into a business transaction involving a currency transaction, all in violation of RPC 1.8(a); despite the attorney's lack of a disciplinary record, his admission of wrongdoing, and the lack of harm to the client, he received a reprimand, given the large amount of money involved); and In re Futterweit, 217 N.J. 362 (2014) (attorney, in lieu of legal fees, agreed to share in the profits of his client's business, without first advising the client, in writing, of the desirability of seeking the advice of independent counsel and obtaining the client's written consent to the transaction, a violation of RPC 1.8(a); the attorney also violated RPC 1.5(b) (failure to set forth in writing the basis or rate of the attorney's fee); in aggravation, we noted that the attorney had given inconsistent statements to the district ethics committee, that he had a

prior admonition for failure to communicate with a client, and that he had never acknowledged any wrongdoing or showed remorse for his conduct).

Most like the attorney in Rajan, who received a reprimand, respondent engaged in a business transaction with a client, which resulted in a conflict of interest, and he failed to obtain the client's informed, written consent to the conflict. Also like the attorney in Rajan, respondent committed other ethical infractions and, up until this instance, had an unblemished disciplinary record.

Members Finding Negligent Misappropriation

In addition to our unanimous findings, Vice-Chair Singer and Members Boyer, Joseph, and Menaker adopt the Special Master's finding that respondent's misappropriation of escrow funds was negligent. However, those Members diverge from the Special Master's recommended imposition of a reprimand and, for the totality of respondent's misconduct, as exacerbated by the significant, demonstrable harm to AFS, determine to impose a three-month suspension.

Specifically, those Members determine that there is insufficient evidence, considering the unique facts of this case, to conclude that respondent committed knowing misappropriation. The Members find that respondent had a reasonable belief that the WMH deposit funds had been replaced and, thus, was negligent in disbursing the AFS loan proceeds to which he had been entrusted.

Considering respondent's failure to take any steps to confirm the replacement of the funds, the harm to AFS, as well as the additional misconduct committed by respondent, those Members determine to impose a three-month suspension.

Generally, a reprimand is the appropriate discipline for negligent misappropriation. See, e.g., In re Osterbye, 243 N.J. 340 (2020) (attorney reprimanded when his poor recordkeeping practices caused a negligent invasion of, and failure to safeguard, funds owed to clients and others as a result of real estate transactions, in violation of RPC 1.15(a); his inability to conform his recordkeeping practices despite multiple opportunities to do so also violated RPC 8.1(b) (failure to cooperate with disciplinary authorities)); In re Mitnick, 231 N.J. 133 (2017) (attorney reprimanded for violations of RPC 1.15(a) and (d) (failure to comply with the recordkeeping requirements of R. 1:21-6); as the result of poor recordkeeping practices, the attorney negligently misappropriated more than $40,000 in client funds held in his trust account; the attorney had an unblemished disciplinary record in a thirty-five-year legal career); In re Rihacek, 230 N.J. 458 (2017) (attorney reprimanded for negligent misappropriation of client funds held in the trust account, various recordkeeping violations, and charging mildly excessive fees in two matters; no prior discipline in thirty-five years); and In re Weinberg, 198 N.J. 380 (2009) (attorney negligently misappropriated client funds as a result of an unrecorded wire

transfer out of his trust account, because he failed to regularly reconcile his trust account records; his mistake when undetected until an overdraft occurred; attorney had no disciplinary history).

Although respondent was not charged with poor recordkeeping, in violation of RPC 1.15(d), an apt comparison can be made from the facts of the instant matter, wherein respondent failed to conduct a proper accounting to confirm that the $30,000 deposit with WHM was replaced, prior to disbursing the equivalent funds from his ATA, resulting in his negligent misappropriation of those entrusted funds. Like the attorney in Osterbye, who was reprimanded, respondent's failure to take any steps to confirm the replacement of the WMH deposit resulted in his negligent misappropriation of AFS's loan proceeds. Just like the attorneys in Mitnick and Rihacek, who also received a reprimand, respondent has a long standing unblemished disciplinary history; twenty-seven years to be exact.

In addition to the other reasons set forth, Vice-Chair Singer and Members Boyer, Joseph, and Menaker would not find a knowing misappropriation because, at the time of the closing, the funds were disbursed in accordance with everyone's instructions, including AFS. Once the deposit was released to WMH at closing, pursuant to instructions approved by AFS, respondent's duties as closing agent with respect to those funds were discharged.

When WMH sent monies to respondent months after the closing, there was no operative escrow arrangement imposing responsibility upon respondent to safeguard those funds for the benefit of AFS. In the view of these Members, in a case in which the OAE is seeking to disbar respondent for knowing misappropriation, such a duty cannot be inferred under these circumstances. Because these Members do not find clear and convincing evidence of an escrow arrangement imposing a duty on respondent to safeguard funds for the benefit of AFS when the funds were sent to respondent by WMH many months after the closing, these Members conclude that there is no clear and convincing evidence of knowing misappropriation.

Accordingly, Vice-Chair Singer and Members Boyer, Joseph, and Menaker conclude that, standing alone, respondent's violations of RPC 1.7(a), RPC 1.8(a), and RPC 1.15(a), warrant the imposition of a reprimand. Considering the additional negligent misappropriation, those Members determined that respondent's misconduct warrants the enhancement of discipline to a censure. Those Members then weighed the substantial harm caused to the lender, AFS, by respondent's negligent conduct as a fiduciary. In re Torre, 223 N.J. 538, 545-46 (2015) (citing financial harm as an aggravating factor, where client lost seventy percent of her life savings through an unsecured loan to respondent the terms of which were "neither fair nor reasonable").

Despite the mitigation present in this case, including respondent's unblemished disciplinary history, those Members determine that the nature of respondent's misconduct warrants a short term of suspension.

Member Campelo also adopts the Special Master's finding that respondent's misappropriation of escrow funds was negligent, based on respondent's belief that the WMH deposit funds had been replaced. However, Member Campelo also rejects the Special Master's recommended imposition of a reprimand and voted to impose a one-year suspension for the totality of respondent's misconduct. Specifically, Member Campelo finds that respondent's negligence, amplified by the resulting substantial, economic harm caused to AFS, was so egregious as to justify a one-year term of suspension.

Members Finding Knowing Misappropriation

Chair Gallipoli and Members Hoberman, Petrou, and Rivera find that respondent knowingly misappropriated escrow funds and, therefore, decline to adopt the Special Master's finding that respondent's misappropriation of escrow funds was negligent. Accordingly, those Members also diverge from the Special Master's recommended imposition of a reprimand.

Instead, those Members determine that respondent knowingly misappropriated the $26,000 in entrusted funds, in violation of the principles of

Wilson and Hollendonner, and recommend to the Court that he be disbarred. In the view of those Members, respondent's claimed belief that the funds no longer constituted escrow funds, because they had been "replaced" by respondent's client, CCE, was neither credible nor reasonable. Consequently, the $26,000 utilized by respondent to repay the $30,000 loan constituted escrow funds, which he had not authorization to disburse for any purpose other than the WMH deposits, as AFS had required in connection with the loan.

In Wilson, the Court described knowing misappropriation of client trust funds as follows:

> Unless the context indicates otherwise, 'misappropriation' as used in this opinion means any unauthorized use by the lawyer of clients' funds entrusted to him, including not only stealing, but also unauthorized temporary use for the lawyer's own purpose, whether or not he derives any personal gain or benefit therefrom.
>
> [In re Wilson, 81 N.J. 455 n.1.]

Six years later, the Court elaborated:

> The misappropriation that will trigger automatic disbarment under In re Wilson, 81 N.J. 451 (1979), disbarment that is 'almost invariable' . . . consists simply of a lawyer taking a client's money entrusted to him, knowing that it is the client's money and knowing that the client has not authorized the taking. It makes no difference whether the money is used for a good purpose or a bad purpose, for the benefit of the lawyer or for the benefit of others, or whether the lawyer intended to return the money when he took it, or

> whether in fact he ultimately did reimburse the client; nor does it matter that the pressures on the lawyer to take the money were great or minimal. The essence of Wilson is that the relative moral quality of the act, measured by these many circumstances that may surround both it and the attorney's state of mind, is irrelevant: it is the mere act of taking your client's money knowing that you have no authority to do so that requires disbarment . . . . The presence of 'good character and fitness,' the absence of 'dishonesty, venality or immorality' – all are irrelevant.
>
> [In re Noonan, 102 N.J. 157, 159-60 (1986).]

This principle also applies to other funds that the attorney is to hold inviolate, such as escrow funds. In re Hollendonner, 102 N.J. 21 (1985). Specifically, in Hollendonner, the Court extended the Wilson disbarment rule to cases involving the knowing misappropriation of escrow funds. The Court noted the "obvious parallel" between client funds and escrow funds, holding that "[s]o akin is the one to the other that henceforth an attorney found to have knowingly misused escrow funds will confront the [Wilson] disbarment rule . . . ." In re Hollendonner, 102 N.J. at 28-29.

Respondent conceded the fact that AFS, as a lender, had an interest in the $58,000 modular home production deposit, including at the time a portion of the deposit was returned to him, post-closing. In fact, it is undisputed that the $58,000 constituted AFS loan proceeds, which were subject to the conditions AFS had imposed, as a lender. Indeed, the status of that $58,000 as earmarked

funds, subject to the fiduciary obligations discussed in Wilson and Hollendonner, is the very origin for the entire CCE "replacement" theory advanced by respondent.[13] Seventeen days after the loan closing, $26,000 of the $58,000 deposit was returned to respondent by WMH. Respondent deposited those funds in his ATA and, notably, classified the returned deposit on his CCE client ledger as "settlement funds." Yet, respondent admittedly failed to hold the returned $26,000 inviolate in his ATA, as he was duty-bound to do, until all interested parties authorized the release of the funds to respondent and his brother. Respondent, thus, violated RPC 1.15(a) and the principles of Wilson and Hollendonner. It is clear from the record that respondent almost immediately disbursed the full $26,000 of returned deposit funds to his brother, toward the repayment of the $30,000 loan, in violation of RPC 1.15(c).

As we opined in In the Matter of Robert H. Leiner, DRB 16-410 (June 27, 2017) (slip op. at 21), "[c]lient funds are held by an attorney on behalf, or for the benefit, of a client. Escrow funds are funds held by an attorney in which a third party has an interest. Escrow funds include, for example, real estate deposits (in which both the buyer and the seller have an interest) and personal

[13] In the view of the four Members finding knowing misappropriation, respondent's reliance on the "replacement" theory to excuse his use of escrowed funds, coupled with his testimony that he would not have disbursed the escrowed funds had he known that the deposit had not been replaced, only further demonstrates respondent's clear awareness of his fiduciary duty to hold those escrow funds inviolate, and his utter failure to take the simple step of confirming such "replacement" with WMH.

injury action settlement proceeds that are to be disbursed in payment of bills owed by the client to medical providers." The Court agreed. In re Leiner, 232 N.J. 35 (2018).

Further, any argument that there was no formal escrow agreement governing the distribution of the AFS loan proceeds fails, as respondent readily conceded that he had a fiduciary duty to safeguard the AFS loan proceeds – both in connection with the initial closing and in connection with the return of those funds to his ATA. See In the Matter of Lyn P. Aaroe, DRB 19-219 (February 6, 2020) (slip op. at 46) (finding that, collectively, the documents underlying the transaction functioned as an escrow agreement, as they bound the attorney to disburse the funds in a particular manner; the attorney was disbarred for his knowing misappropriation of the escrow funds); In re Aaroe, 241 N.J. 532 (2020).

Like the attorney in the recent case In re Mason, 244 N.J. 506 (2021), respondent failed to obtain authorization from all parties with an interest in the funds to release or use the funds that he was duty-bound to hold in escrow. In Mason, the attorney was disbarred for releasing investors' escrow funds prior to the satisfaction of a required condition precedent, despite his assertion of a claimed belief that the investors had authorized the release of the funds. See also In re Gifis, 156 N.J. 323 (1998) (holding that escrowed funds cannot be

disbursed without all interested parties' prior authorization and observing that ignorance of the law does not exonerate an attorney from responsibility for the knowing misuse of escrow funds).

Respondent admittedly failed to even notify AFS that the $26,000 deposit, in which he conceded AFS had an interest, was returned to his ATA, in violation of RPC 1.15(b). Indeed, eight months later, when AFS was made aware that the deposit funds had been returned to respondent's trust account and subsequently disbursed by him, AFS demanded the return of the full $26,000 deposit, of which respondent promptly returned $1,000.

In the view of the Members finding knowing misappropriation, respondent's claim that he honestly believed that the $26,000 in modular home deposit funds had been replaced lacks credibility. Although he argued that the funds were marked as "non-refundable" on the purchase order and, thus, he had no reason to believe otherwise, the "non-refundable" funds were, in fact, returned to respondent's escrow account at CCE's request, on notice to respondent. It defies logic to conclude that respondent believed his client, CCE, had "replaced" the $26,000 modular home deposit in order to pay $26,000 toward his brother's loan. Stated differently, the Members see no colorable reason why, if CCE possessed the $26,000 to repay respondent's brother, it would not need to "replace" the modular home deposit as a precondition to

making that repayment. The more logical conclusion is that CCE did not have funds independent of the $26,000 portion of the modular home deposit with which to make the payment to respondent's brother, that respondent was aware of that fact or chose to ignore the likelihood of the fact, and that respondent, thus, facilitated CCE's invasion of the AFS loan proceeds to pay back the loan to his brother.

Attorneys have escaped disbarment for their improper or premature release of escrow funds when they have held reasonable, although mistaken, beliefs that, for one reason or another, the release of the escrow funds was appropriate. See, e.g., In re De Clement, 214 N.J. 47 (2013) (motion for discipline by consent; reprimand for attorney who failed to safeguard funds in which a client or third party had an interest, and released a portion of $75,000 he had agreed to hold in escrow, in connection with a joint venture agreement between his client and a third party, without first obtaining the third party's consent; no escrow provision governed the attorney's actions, but the $75,000 check deposited by the attorney included a notation identifying it as an escrow deposit, and the joint venture agreement identified the attorney as the "escrow attorney;" the attorney, however, was never provided a copy of the joint venture agreement, and improperly relied on his client's assurance that he was allowed to use a portion of the escrow funds to cover expenses associated with the joint

venture); In re Holland, 164 N.J. 246 (2000) (reprimand for attorney who was required to hold, in trust, a disputed fee in which she and another attorney had an interest; instead, the attorney took the fee, in violation of a court order; the attorney claimed that she believed that a subsequent court order had entitled her to the entire fee, and, thus, she had made a mistake, rather than knowingly defied a court order; those defenses were rejected); and In re Milstead, 162 N.J. 96 (1999) (reprimand for attorney who disbursed escrow funds to a client, in violation of a consent order).

Stated differently, the above cases can be characterized as fact patterns where "premature disbursement" or disbursement under a colorable dispute occurred. In this case, however, the record contains no support for the proposition that respondent had such a mens rea. In the view of the Members finding knowing misappropriation, respondent's failure to make any effort to confirm whether CCE had replaced the $26,000 in modular home deposit funds is crucial.

As we are aware, in In re DiLieto, 142 N.J. 492 (1995), the Court made clear that "[a]n attorney cannot satisfy his or her professional responsibility with respect to escrow funds by simply relying on information from a client . . . 'It is not enough simply to follow a client's instructions.'" (quoting In re Wallace, 104 N.J. 589, 593 (1986)). See also In re Frost, 171 N.J. 308, 324 (2002). Stated

differently, prior to releasing escrow funds, an escrow holder is duty-bound to obtain the express permission of all parties to the escrow arrangement.

Moreover, although CCE was indebted to respondent, it used very little of its own funds to repay respondent and his brother. Instead, CCE elected to repay respondent from AFS's deposit funds that had been held by WMH, plus a $4,000 direct payment. The Members finding knowing misappropriation respectfully reject the Special Master's finding that respondent's receipt of a separate check from CCE, which included $4,000 in loan repayment funds, bolstered the reasonableness of respondent's belief that the $26,000 deposit funds had been replaced. Instead, those Members find that the fact that CCE only directly reimbursed respondent $4,000 of the funds owed should have prompted respondent to question whether the $26,000 deposit had, in fact, been replaced. Undeterred by the questionable circumstances, respondent admittedly made no effort to verify that the deposit was, in fact, replaced prior to his almost immediate disbursement of the funds. Respondent stuck his head in the sand, and then argued that he was unaware that the $26,000 deposit had not been replaced by CCE. Respondent's behavior was unreasonable, and his argument is uncompelling; simply put, respondent failed to take the simple step of contacting WMH to confirm that the $26,000 deposit had been replaced and,

instead, almost immediately disbursed the funds, without regard to AFS's interest therein – of which he was acutely aware.

Previously, In the Matter of Jordan B. Comet, DRB 17-353 (June 8, 2018) we determined, and the Court agreed, that the attorney had negligently, not knowingly, misappropriated entrusted funds, based on his mistaken belief that he was entitled to the funds for his legal fee (slip op. at 2).[14] In Comet, the attorney and the client discussed the retainer fee; the client assured the attorney that the retainer fee had been wired, although it had not; the attorney failed to confirm receipt of the wired fee; the attorney performed work on behalf of the client; the attorney mistakenly relied upon the client's assurance that the fee was wired and, subsequently, transferred legal fees out of his trust account; and, as a result, the attorney invaded other clients' funds held in the account (slip op. at 5, 6, 10, 14, and 28). Adding credibility to the reasonableness of Comet's mistaken reliance on his client's representation that the retainer fee had been wired, the client testified that he intended to provide the retainer fee, the attorney provided legal services to him, and he never notified the attorney that the retainer fee had not been wired (slip op. at 13, and 46). In the instant matter,

[14] We recommended that Comet be censured for his negligent misappropriation, but the Court determined to impose a three-month suspension.

there was no such testimony from Casper or CCE to support respondent's theory of reasonable reliance.

Recently, in In the Matter of Dominic V. Caruso, DRB 20-191 (April 30, 2021) (slip op. at 28-29), we rejected the attorney's argument that, after having requested that the client wire funds to cure an escrow shortfall, he reasonably relied on the client and expected that the funds were wired, thus, curing the shortfall. Instead, we determined that Caruso had knowingly misappropriated entrusted funds by his knowing creation of the escrow shortfall, both when he used entrusted funds to pay his personal tax debt and when he paid himself a legal fee, especially in consideration of the fact that the escrow arrangement required the authorization of three interested parties, and we recommended his disbarment (slip op. at 67,70). We found that Caruso failed to confirm that the client's transfer of funds occurred, and that this misconduct fell "short of his obligations as a New Jersey attorney and as a fiduciary and escrow agent." Caruso (slip op. at 17, 29). The Court, however, disagreed by way of Order, finding that Caruso had committed only negligent misappropriation, and imposed a six-month suspension. In re Caruso, 248 N.J. 426 (2021).[15]

[15] The Order did not expressly determine whether Caruso had reasonably relied on his client's representation that funds had been wired.

Here, similarly, respondent alleged to have reasonably relied on Casper's representation that the deposit funds were replaced but failed to confirm that the replacement had occurred. Additionally, just like the attorney in Caruso, respondent used entrusted funds for his own, personal benefit – to repay the loan advanced to respondent and his client by his brother. We reject respondent's reasonableness argument, because like Caruso, respondent knowingly engaged in self-help at the expense of entrusted funds, which resulted in his failure to satisfy his fiduciary obligations as the settlement agent.

More recently, In the Matter of Karina Pia Lucid, DRB 20-216 (July 9, 2021), we addressed a similar application of the principles of Wilson and Hollendonner based upon the reasonableness of the attorney's conduct and her reliance on a client. In Lucid, the attorney instructed her client, Petrelli, to "immediately" send funds to cover a settlement and she believed that Petrelli would follow her instruction (slip op. at 2-3). Thereafter, despite knowing that her trust account did not hold any funds for the benefit of Petrelli, the attorney intentionally issued a $5,500 trust account check to MS Services on Petrelli's behalf, without the authorization of other clients whose funds were held in the account and ultimately invaded, in an effort to preserve Petrelli's settlement with MS Service (slip op. at 4, and 28). Lucid reasoned that Petrelli had been a good client who always paid his bills in a timely fashion and, therefore, she had "full

anticipation" that she would receive his check and that it would clear the account before the check issued to MS Services was negotiated (slip op. at 4). Ultimately, Petrelli's check came late, resulting in the invasion of other clients' funds.

Our majority decision found that Lucid had knowingly misappropriated $5,500 in entrusted funds (slip op. at 20). The Court, however, disagreed by way of Order, and determined that Lucid had committed only negligent misappropriation. The Court imposed a censure. In re Lucid, 248 N.J. 514 (2021).

Unlike the attorney in Lucid, who opined that she had utilized $5,500 in entrusted funds to benefit her client – to preserve a transaction in which time was of the essence, which in fact did occur to the client's benefit – respondent's misconduct did not benefit any client and it caused significant harm to AFS. The $26,000 deposit – almost five times greater than the sum in question in Lucid, was never replaced, by respondent, Casper or CCE, aside from respondent's meager $1,000 payment. The real estate transaction fell through, and AFS's only option was to sell the Property in an effort to recoup its losses. The significant harm to AFS cannot be ignored and, clearly, distinguishes the instant matter from Lucid.

In the view of the Members finding knowing misappropriation, respondent's behavior is most akin to that of the attorney in In the Matter of

Stephanie A. Hand, DRB 21-015 (September 16, 2021), whose disbarment we recently and unanimously recommended to the Court. In that matter, Hand served as the escrow agent in connection with two real estate transactions in which a lender's loan proceeds were required to consummate the transactions. In the Matter of Stephanie A. Hand, DRB 21-015 (September 16, 2021) (slip op. at 23). Rather than abide by the lender's requirements, Hand violated them. Ibid. In evaluating Hand's behavior, we noted that, in recent history, our view of the fiduciary duties required of attorneys in escrow situations has been distilled into clear guidance. We explained that, although our application of Hollendonner to such situations is not necessarily more expansive, it has been more finely tuned to the factual scenarios presented and explained in recent decisions. We found that Hand disbursed loan proceeds in violation of the lender's requirements, and thus committed knowing misappropriation, contrary to the principles of Wilson and Hollendonner. Id. at 27-28. After considering the "totality of the circumstances presented in the matter," the Court disbarred Hand. In re Hand, __ N.J. __ (2021).

Here, as in Hand, respondent disbursed loan proceeds in violation of the lender's requirements. The identified Members concluded that he also committed knowing misappropriation of escrow funds, in violation of RPC

1.15(a) and the principles of Wilson and Hollendonner, requiring his disbarment.

Although the Court has acknowledged the harshness of the Wilson rule, particularly because, prior to the misappropriation under scrutiny, respondent had always conducted himself in an exemplary fashion, the Court has refused to carve out an exception to the Wilson rule, citing the overriding need to "preserve the confidence of the public in the integrity and trustworthiness of lawyers." Id. at 535. Therefore, Chair Gallipoli and Members Hoberman, Petrou, and Rivera found that respondent knowingly misappropriated escrow funds and voted to recommend to the Court that he be disbarred.

We further determine to require respondent to reimburse the Disciplinary Oversight Committee for administrative costs and actual expenses incurred in the prosecution of this matter, as provided in R. 1:20-17.

Disciplinary Review Board
Hon. Maurice J. Gallipoli, A.J.S.C. (Ret.),
Chair

By: 
Johanna Barba Jones
Chief Counsel

SUPREME COURT OF NEW JERSEY
DISCIPLINARY REVIEW BOARD
VOTING RECORD

In the Matter of Richard J. Pepsny
Docket No. DRB 21-142

Argued: October 21, 2021

Decided: December 21, 2021

Disposition: Other

Members	Three-Month Suspension	One-Year Suspension	Disbar
Gallipoli			X
Singer	X		
Boyer	X		
Campelo		X	
Hoberman			X
Joseph	X		
Menaker	X		
Petrou			X
Rivera			X
Total:	4	1	4

Johanna Barba Jones
Chief Counsel