A PERSONAL INJURY LAWYER CANNOT SERVE TWO MASTERS:

Ethics in Medical Lien Factoring

BY SAMUEL D. GEORGE, ESQ.

Let's talk about factoring. I know what you're thinking: what does expressing a polynomial as the product of unfactorable polynomials with integer coefficients have to do with law? Ok, maybe that's not precisely what you're thinking; regardless, that's not the type of factoring relevant here. I'm referring to medical lien factoring in the personal injury arena, a practice that can implicate the Nevada Rules of Professional Conduct. Admittedly, there will be some math, but if you have a grasp of basic addition and subtraction, we'll get through it.

In personal injury cases, when a plaintiff can't afford medical treatment, medical providers are often willing to render care and take a lien in lieu of cash, treating the plaintiff on a lien basis. Under this practice, victims obtain prompt medical care, and medical providers secure future compensation. But cash-flow is important, and the prospect of legal recovery is speculative, so providers will routinely trade the full amount of their future recovery (i.e., the face value of their medical lien) in exchange for an immediate cash payment, discounted for risk and other factors. Basically, after treating a plaintiff on a lien, providers sell their lien receivables to factors or underwriters, which then collect the expenses when the case is resolved. Meanwhile, the zealous plaintiff's attorney litigates the case, usually to the point of compromise, and negotiates a discount on the lien to maximize the client's net recovery.

At some point, opportunistic legal professionals entered the factoring market by establishing their own companies to purchase medical liens. In April 2017, the Committee on Ethics and Professional Responsibility issued Formal Opinion No. 53, in which it opined that personal injury lawyers cannot maintain their undivided loyalty and judgment while representing injured plaintiffs on one hand, and on the other hand holding medical liens.[1] After all, the plaintiff benefits from the maximum lien discount, whereas the lien holder benefits from the maximum lien satisfaction. According to the committee, these divergent interests have the potential to undermine the lawyer's advocacy, so attorneys who own medical liens violate the rules—even if the liens are not related to cases of their own.[2]

After the committee issued the opinion, some lawyers in the business insulated themselves from their factoring activities by erecting superficial alter-

continued on page 29

continued from page 27

Ethics in Medical Lien Factoring

ego screens. Attorneys have thus inquired: is it ethical for lawyers to instruct someone else, like a close friend or family member, to create and manage such a company? Clearly, the answer is no.

To state what is hopefully obvious, merely working through someone else hardly mitigates the ethical dangers pointed out by the committee. In the analogous case *In re Cellino*, New York attorneys extended loans to their clients to help fund litigation in contravention of New York's analog to Rule 1.8(e), which prohibits lawyers from providing financial assistance to clients.[2] Then, to avoid violating the rule directly, one of the attorneys helped his cousin organize a company to make the same loans.[3] Not only did the attorneys help establish the business, but the attorney also controlled the company, and the cousin was just a front.[4] But under Rule 8.4(a), lawyers are prohibited from using another person to do that which they cannot do themselves.[5] The attorneys in *In re Cellino* violated New York's version of Rule 8.4(a), because they continued to make loans to their clients under the guise of arms'-length transactions; so, they were suspended.[6]

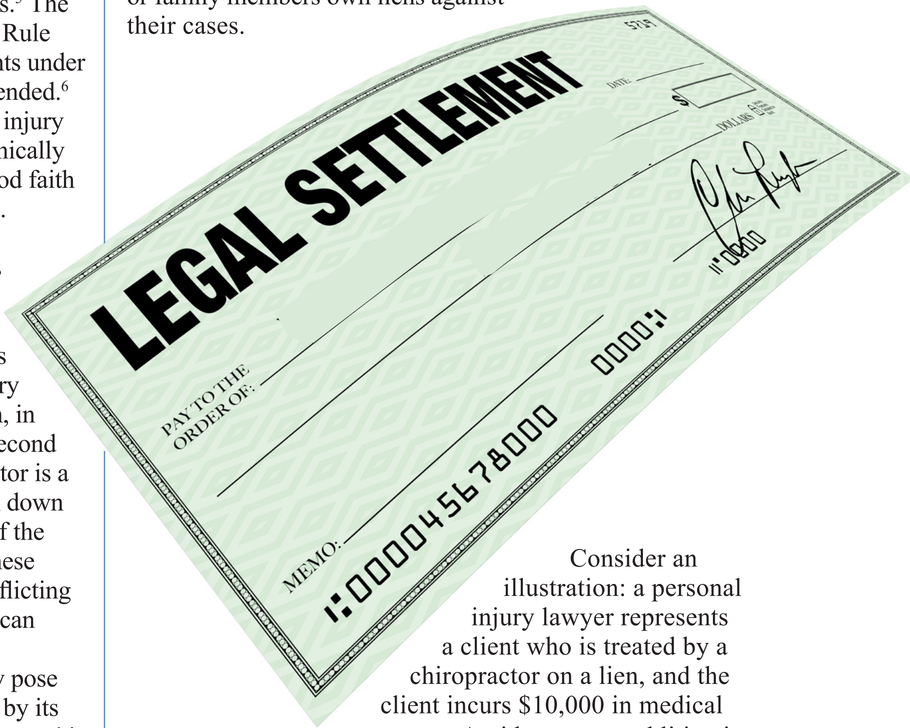
Well that makes good sense, but what if the personal injury lawyer doesn't organize or control the factor? Can s/he ethically acquire a passive stake in a lien-factoring enterprise in good faith and without any intent to circumvent the rules? Not likely.

When a personal injury lawyer obtains an interest in litigation-related medical liens, certain practical dynamics emerge. In the event that an attorney fortuitously acquires a lien encumbering one of his or her own settlements, even if the attorney's interest derives from his or her equity in the factor, the attorney acquires a pecuniary interest that is unavoidably adverse to the client's position, in violation of Rule 1.8(a). This conflict exists because the second round of lien negotiation between the attorney and the factor is a zero-sum game, i.e., the attorney cannot negotiate the lien down without directly and proportionally affecting the margin of the underwriter. As the committee expressed in its opinion, these dynamics in turn force an attorney to choose between conflicting loyalties owed to both a client and a business; this choice can result in fiduciary breaches to either or both.[7]

While not all technically adverse interests necessarily pose a significant risk of impairing representation, the opinion, by its terms, applied to all situations in which a lawyer has an ownership interest in a factor, not just those alter-ego situations illustrated by *In re Cellino*.[8] Surely the committee appreciated that the extent to which lawyers' interests in a factor threatens their representation depends on the extent of that interest and the relative revenues of their companies and practices. But it's impossible to quantify the point at which an attorney's ownership interest in a factor *actually* starts affecting professional judgment. And conflicts of interest under Rule 1.7(a)(2) exist when there is a substantial risk that representation will be materially impaired.[9] So, whether the interest is 50 percent or 10 percent, the attorney-shareholder risks splitting allegiance between two masters, and the risk that advocacy will be affected is unethically high.

Now for the hard question: what if intimate friends or relatives of attorneys start underwriting medical liens entirely on their own, without any encouragement from or entrepreneurial tie to the lawyers? Is it unethical for a personal injury lawyer to be *closely related* to a factor in the personal injury space? Maybe. That an ethical breach can emanate from relationships rather than conduct is supported by Rule 1.7(a). As the rules instruct, in such cases, the question is one of proximity and degree.[10] When the relationship between a lawyer and a factor is intimate or extensive, there are at least two appreciable risks present: the possibility of collusion and the disclosure of confidential information.

Though perhaps we shouldn't presume that attorneys have a proclivity for self-interested behavior, this seemingly innocuous scenario is ripe for collusion. In the scenarios discussed above, in which attorneys have a stake in medical liens against each others' cases, they may be tempted to forge gentlemen's agreements to exchange favorable lien discounts. And risks of similar anti-competitive collusion exist when a lawyers' intimate friends or family members own liens against their cases.



Consider an illustration: a personal injury lawyer represents a client who is treated by a chiropractor on a lien, and the client incurs $10,000 in medical expenses. Amidst protracted litigation, the chiropractor sells the lien for $4,000, and the acquiring factor is owned and operated by the lawyer's brother. In their not-so-adversarial negotiations, the brother reveals his reservation price of $5,000, i.e., the lowest price he is willing to accept, so they agree on a lien-satisfaction price of $7,000. Then, surreptitiously, they split the factor's $2,000 surplus. In this scenario, the lawyer's brother receives $1,000 more than his reservation price, and the lawyer receives $1,000 that he or she would never have received. This arrangement won't impair the attorney's fees revenue, because the attorney charges the contingency fee to the gross settlement before payment of expenses. Everyone benefits at the plaintiff's expense.

A lawyer's close relationship with a factor also creates a risk that the lawyer will disclose confidential information.

continued on page 31

continued from page 29

Ethics in Medical Lien Factoring

Factoring exists in other industries, and there the price of receivables depends on the creditworthiness of the account debtor. In the personal injury space, however, the price of medical liens depends on the merits of the legal case, or rather, the likelihood of the plaintiff's favorable recovery. Because the lawyer's close friend or loved one has more at stake on the lien than the attorney, the attorney may be tempted to share legal impressions, confidential information or other information about the merits of the case, in an effort to subtly suggest that the relative not discount the lien. Again, because of the way the attorney calculates contingency fees, the attorney's revenue is unaffected by the tip.

Ultimately, whether personal injury lawyers purchase medical liens directly, purchase them through an alter ego, own a passive interest in a factor or have a close personal relationship with someone who does, the risks of conflicts, collusion and disclosure are real. Lawyers should be particularly vigilant in recognizing these potentially problematic relationships, identifying their ethical risks, and taking steps to confront and resolve those risks. **NL**

1. *See* Standing Comm. on Ethics & Prof's Responsibility, Formal Op. 53 (2017).
2. *See In re Cellino*, 21 A.D.3d 229, 798 N.Y.S.2d 600 (2005), *reinstatement granted*, 37 A.D.3d 1206, 827 N.Y.S.2d 901 (2007).
3. *See id*.
4. *See id*.
5. *See* Nev. R. Prof'l Conduct R. 8.4(a).
6. *See In re Cellino,* 21 A.D.3d at 235, 798 N.Y.S.2d at 606.
7. *See* Formal Op. 53.
8. *See id*.
9. *See* Nev. R. Prof'l Conduct R. 1.7(a)(2).
10. *See id*. at cmt. 26.

SAMUEL D. GEORGE studied economics at the University of Utah, and he studied law at Indiana University (Maurer) and BYU. He is an associate with the law firm of Marquis Aurbach Coffing and represents clients in real estate, labor and employment, landlord/tenant, and other civil litigation and transactional matters.

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