

> Scams Targeting Attorneys: Will You Be A Victim?

By Tazewell T. Shepard

INTRODUCTION

Attorneys in Alabama and around the nation are now targets for several types of aggressive frauds, including:

Counterfeit checks—These are usually cashier's checks or certified checks, and their quality ranges from poor to so convincing that even a banker cannot be sure with a casual inspection if they are counterfeit. Money orders and letters of credit have also been counterfeited. A scammer sometimes alters the routing numbers at the bottom of the check so that it will take longer after it is deposited for the issuing bank to send it back as a forgery.

Phishing/spoofing emails—In this context, these terms refer to the act of sending an email falsely claiming to be an actual, reputable business seeking legal assistance. Most often the email is sent from a similar, but slightly different email address to establish an attorney-client relationship so that a counterfeit check, mentioned above, can be used to scam the attorney. When the scam involves the more sophisticated act of hacking a legitimate email account, it is generally used to misdirect funds from a real estate closing or other transaction to a scammer's temporary bank account.

Forged checks—These may be checks drawn against the law firm's bank account. A local client or a party to a transaction in the attorney's office can take a

picture of a law firm check with their cell phone and then later create look-alike forged checks. Long-distance scammers have other ways of obtaining the firm's bank information, such as sending a phony invoice for a nominal amount, just so they can get one of the firm's real signed checks.

Ransomware—This is a basic, but effective, software that encrypts all data on a law firm's computer system, including client files, billing data and email communications, thus rendering them totally inaccessible to the attorney until a ransom is paid to acquire a key code. The malicious software usually gets into the law firm's system when someone at the firm clicks on an attachment to an email, but it can also occur when someone at the firm plugs in an unknown thumb drive. Contacting the scammer and paying the ransom may take weeks or months, and even the FBI probably cannot break the encryption to rescue the law firm's ransomed information and data.

LITIGATION WITH DEPOSITORY BANKS

In the situation involving a counterfeit check, a law firm victimized by a scammer may face litigation with their depository bank concerning the large deficiency in the firm's trust account for funds wired by the firm to a third party (the scammer or his associate) before the counterfeit check is returned un-

paid. Reported cases generally favor the bank rather than the law firm:

In *Wells Fargo, N.A. v. Willoughby*, Case 1:15-CV-129-AA (D. Or. 2015), a federal court considered whether the plaintiff or the defendant attorney should bear responsibility for the forged check loss. Because the attorney was the party best able to prevent the loss, the Court ruled that the *Uniform Commercial Code*, which governed the transaction here, held the defendant responsible. The Court also stated that the Expedited Funds Availability Act (EFAA) requires that banks provide prompt access to valid deposits, but not that banks assume liability for bad checks given to depositors.

In *First Financial Bank, N.A. v. Citibank, NA and Misty McDonald*, Case No. 1:11-CV-226-WTL-DML (S.D. Ind. 2012), the Court granted the bank summary judgment on its claim that the attorney breached UCC warranties by presenting a counterfeit check to First Financial for deposit into her account. However, the Court also granted summary judgment to the defendant attorney on the bank's claim of check deception because there was no evidence that she knew the check was counterfeit when she deposited it.

In *Milavetz, Gallop & Milavetz, P.A., Plaintiff, v. Wells Fargo Bank, N.A.*, Civil No. 12-0875 (D. Minn. 2012), the federal court rejected the plaintiff law firm's claims for fraudulent misrepresentation and suppression of material facts based on the previous representations of bank

employees concerning the bank's fraud detection program. The Court did allow the law firm to pursue their claim against the bank for conversion under state law, based on the argument that the firm was the bailee of its clients' trust account funds.

LITIGATION WITH INSURANCE CARRIERS

Litigation may also occur when an attorney who is the victim of a scam looks to the law firm's insurance carrier for reimbursement of lost firm funds, lost client funds and even lost firm billing revenue. As you might expect, insurance companies often deny liability in such situations, and some law firms have sued their carriers to enforce scam-loss insurance claims.

It is difficult to make a general statement about the likelihood of success in such lawsuits, as each case depends on several factors, including the circumstances of the loss, the terms of the insurance policy and applicable state law. However, the following examples will provide some indications as to how courts have been dealing with cases concerning insurance claims resulting from scams targeting attorneys.

Martin, Shudt, Wallace, Dilorenzo & Johnson v. Travelers Indemnity Company, 2014 WL 460045 (N.D.N.Y. February 5, 2014) involved a counterfeit cashier's check received by the law firm for a debt owed to a new client. The firm deposited the check to its trust account and then wired funds to a bank account designated by the "client." When the fraud was discovered, the bank charged back \$95,000 on the law firm's trust account. The firm made a claim under a business owner's property insurance policy, based on coverage for "direct physical loss of or damage to covered property," including money or securities, "caused by or resulting from a covered cause of loss." However, the New York court accepted the carrier's position that the claim was barred by a policy exclusion for "voluntary parting with any property by you or anyone else to whom you have entrusted the property."

In *Lawyers Mutual Liability Insurance Company of North Carolina v. Mako*, 756 S.E. 2d 809 (N.C. Ct. App. 2014), a new "client" that the lawyer never actually met hired the law firm to collect a large workers' compensation settlement from his former employer. The firm received a cashier's check and distributed most of the funds on the same day, in violation of their own "10-day" policy. When the wire was unsuccessful, the law firm received a second cashier's check and this time successfully wired the funds to a bank in Japan. After learning that both checks were bogus, the law firm filed a \$175,000 claim with their malpractice insurance carrier, but the North Carolina court ruled that policy language excluded coverage for this claim because the firm disbursed funds while the bank still had the right to return the check and revoke the deposit under state law.

In *Chong v. Medmarc Casualty Insurance Company*, 642 F.3d 941 (11th Cir. 2011), a foreign client hired Chong to establish a U.S. subsidiary and sent a cashier's check, which the firm deposited in its trust account. After following the client's instructions to wire most of the funds to another overseas business, the law firm found out that the cashier's check was forged. Chong made a claim and then filed suit based on a professional liability policy that covered all claims of negligence arising from an act or omission in the performance of "professional services." "Professional services" was defined by the policy to include "[s]ervices as a . . . trustee . . . but only for those services typically and customarily performed by an attorney." The district court entered judgment for the insurance company because "there have been no negligent acts or negligent omissions resulting from the performance of, or failure to perform, professional services." However, the Eleventh Circuit panel reversed, finding that management of funds in trust for clients constituted a "professional service" under Medmarc's policy and applicable Florida law. The Court of Appeals remanded the case to the district court for entry of summary judgment for the law firm.

CONCLUSION

There is no clear line of decisions on which a law firm can rely if it becomes a victim of a scam. The results have been disappointing for attorneys litigating with their banks, but some firms have had success making a claim on a property loss policy and perhaps more law firms have obtained positive results from a professional malpractice policy. However, as stated above, the circumstances of the loss, the terms of the insurance policy and applicable state law are important considerations in each case.

Moreover, a reader may get a sense from some of these decisions that the degree of the attorney's negligence in allowing the scam to occur may be at least a background consideration for some courts. Failing to use common sense or to follow your own safeguards and policies certainly will not engender a judge's sympathy.

Finally, if you would like to follow a current case concerning not hacked emails or fake checks, but instead ransomware, consider *Moses Alfonso Ryan Ltd. v. Sentinel Insurance Company, Limited*, PC-2017-1280. In May 2015, an attorney at the Rhode Island law firm clicked on the attachment to an email from an unknown source. The virus encrypted all of the documents and client information on the law firm's computer network, and efforts of the FBI and experts hired by Moses Alfonso were unsuccessful. It took three months for the firm to obtain a Bitcoin account and pay the demanded ransom twice (totaling more than \$25,000) to obtain the decryption key. Moses Alfonso made a claim on their business owner's policy for losses resulting from business income interruption, for the \$25,000 ransom and more than \$700,000 in lost billings. When Sentinel rejected the claim, the law firm filed suit for breach of contract and insurer bad faith. The pending complaint seeks punitive damage and demands a jury trial. <

Taze Shepard is managing partner of Sparkman, Shepard & Morris PC in Huntsville and a member of the Alabama State Bar Board of Bar Commissioners.