

# AGENDA ITEM

**DATE:** April 26, 2011

**TO:** Members, Regulation, Admissions and Discipline Oversight

**FROM:** James Towery, Chief Trial Counsel

**SUBJECT:** Posting of Consumer Alert of Significant Loan Modification Misconduct Filed Charges and Petition Filed Pursuant to Business and Professions Code section 6007(c) based on Loan Modification Misconduct on Member's Profile Page--Request for Public Comment

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## EXECUTIVE SUMMARY

Starting primarily with the collapse of the residential real estate market in 2008 and the resulting wave of foreclosures affecting the nation's homeowners, the State Bar began to receive a new type of disciplinary complaint against attorneys. Regrettably, the combination of the subprime mortgage crisis, massive home foreclosures and high unemployment created a perfect storm of opportunity for a relatively small number of unscrupulous attorneys to defraud desperate homeowners trying to save their homes from foreclosure. In exchange for an advanced fee, many of these attorneys promised, but never delivered, loan modification assistance for distressed homeowners.

Some loan modification attorneys were investigated for a multitude of discipline complaints as a result of shared mass advertising campaigns or call centers from "attorney backed" loan modification companies to solicit clients. As a result, one particularly challenging aspect of ensuring public protection against mass loan modification misconduct by attorneys is minimizing the risk of continuing harm when a lawyer remains on active status pending the resolution of filed disciplinary charges alleging significant loan modification misconduct.

Currently, the State Bar posts on its website's member profile page a filed notice of disciplinary charges and any response to the notice, until such time as an order or decision is filed resolving the disciplinary matter. The website does not currently post a petition filed under Business & Professions Code section 6007(c) to enroll an attorney involuntarily on inactive status based on "threat of harm" to clients or the public.

OCTC believes that in order to sufficiently warn the public and prevent future harm to potential clients about lawyers involved in significant loan modification misconduct, the Bar's website policy should be extended to post a Consumer Alert displayed

prominently on the member's profile page. The Consumer Alert and informational text, coupled with a disclaimer, would be posted upon the filing of either a notice of disciplinary charges involving 15 or more cases of loan modification misconduct, or a petition under Business & Professions Code section 6007(c) based on loan modification misconduct (regardless of the number of cases) in the State Bar Court. The second aspect of the proposal involves posting the petition and any response filed pursuant to Business and Professions Code section 6007(c) when the petition relies, in whole or part, on loan modification misconduct.

We are seeking your Committee's authorization to release for public comment, for a period of 45 days, the proposed policy regarding posting a Consumer Alert on a member's State Bar website profile page-as well as posting a petition filed pursuant to Business and Professions Code section 6007 subdivision (c) that relies on loan modification misconduct - as set forth in Attachment A.

For any questions about this agenda item, please contact Jill Sperber, Special Assistant to the Chief Trial Counsel, at [jill.sperber@calbar.ca.gov](mailto:jill.sperber@calbar.ca.gov) or (415) 538-2023.

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## **ISSUE**

Whether the Board Committee on Regulation, Admissions & Discipline should authorize release, for a 45 day period, for public comment the attached proposed policy set forth in Attachment A. The policy contains two parts. First, the State Bar would post on a member's State Bar website profile page a prominently-displayed Consumer Alert (and appropriate disclaimer) on a member's profile page when a filed notice of disciplinary charges includes 15 or more loan modification misconduct cases or a petition filed pursuant to Business and Professions Code section 6007(c) relies, in whole or part, on loan modification misconduct (regardless of the number of cases.) The second part of the policy authorizes posting an involuntary inactive enrollment petition filed under Business & Professions Code section 6007(c)[threat of public harm] when a basis for the application involves loan modification misconduct (regardless of the number of cases), and any response filed by the lawyer, until a decision or order adjudicating the petition issues from the State Bar Court.

## **BACKGROUND**

Due primarily to the collapse of the residential real estate market in 2008 and the resulting wave of foreclosures affecting the nation's homeowners, in 2009, the State Bar began receiving a new type of complaint against attorneys. Regrettably, the combination of the subprime mortgage crisis, massive home foreclosures and high unemployment created a perfect storm of opportunity for a relatively small number of unscrupulous attorneys to defraud desperate homeowners trying to save their homes from foreclosure. In exchange for an advanced fee, many of these attorneys promised, but never delivered, loan modification assistance for distressed homeowners.

Complaints of this type of misconduct soon flooded the disciplinary system. To address the increased volume of loan modification cases inundating the attorney discipline system in California, in 2009, the Office of the Chief Trial Counsel (OCTC) formed the Loan Modification Team to aggressively prosecute California lawyers involved in loan modification misconduct in California and other states. Since 2008, the Office of the Chief Trial Counsel (OCTC) has received roughly 4,800 consumer complaints against lawyers suspected of engaging in loan modification misconduct, which represents approximately 30 percent of the office's workload.

These dishonest lawyers have not only strained the discipline system, the Bar's Client Security Fund is also facing unprecedented numbers of claims for reimbursement by victimized homeowners. Largely due to the wave of loan modification complaints, the Fund's claims quadrupled from 2008 (825 claims) to 2009 (3,028 claims.) Even more requests for reimbursement in 2010 (3,875 claims) have placed an unprecedented strain on the Fund.

### **The Business Model of Mass Solicitation of Homeowners often Leads to a Multitude of Complaints against a Single Attorney.**

State Bar investigations conducted in the past two years have revealed a variety of schemes involving attorneys in this area. A loan modification company is often involved. In order to evade the mortgage consultant laws in effect prior to October 2009<sup>1</sup>, attorneys became invaluable to loan modification companies because lawyers, unlike mortgage consultants, were permitted to charge and collect advanced fees for their services. Mass scale commercial advertisements and cold sales calls from makeshift call centers promised distressed homeowners loan modification rescue and often included preposterous guarantees, such as a 99% success rate or a money back refund guaranteed.

As a result, loan modification companies began advertising themselves as law offices, attorneys or "attorney backed" organizations which would pay the attorney a pro rata share of fees-nominal amounts per file-to use the attorney's name. Another typical scheme is the use of call centers housed in large warehouses staffed by young non-attorney sales people who cold call homeowners and attempt to collect money the same day. Typically, these operations charge between \$1,500 and \$5,000 (usually, the amount of one or two months of mortgage payments, which the client stops paying to devote limited money to purchase loan modification help). All too often, no work results,

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<sup>1</sup> Former Civil Code section 2945.1(b) exempted attorneys from the definition of foreclosure consultant and permitted them to collect advanced fees for performing the work of foreclosure consultants. On October 11, 2009, Senate Bill 94 (codified at Cal. Civ. Code §2944.7) passed, prohibiting attorneys from collecting advanced fees for this work. Collection of an advanced fee by an attorney in violation of Civil Code sections 2944.6 or 2944.7 is a disciplinable offense. (Bus. & Prof. Code §6106.3.)

and the homeowner loses his or her home. And, the loan modification company fails to provide a refund.

## **The State Bar's Disciplinary Response**

There are two principal methods to aggressively prosecute attorneys involved in loan modification misconduct. The most common means is filing a notice of disciplinary charges in the State Bar Court. A notice of disciplinary charges is filed, however, only following a completed investigation of a complaint by OCTC's professional investigators and supervising attorneys and opportunities for the lawyer to reply to the complaint are provided. Since 2009, OCTC has filed 15 notices of disciplinary charges against attorneys for loan modification misconduct, some of which relate to the same attorneys against whom section 6007(c) petitions were filed involving the same cases.

The other avenue-and one used by the Bar's Loan Modification Team-is seeking the attorney's inactive status based on the threat of public harm, pending the resolution of disciplinary charges. Business & Professions Code section 6007(c) (1) provides "[T]he involuntary inactive enrollment of an attorney may be ordered upon a finding that the attorney's conduct poses a substantial threat of harm to the interests of the attorney's clients or to the public...." Because OCTC must file a verified accusation showing that there is a substantial threat of harm to clients or the public, these petitions typically rely on a multitude of investigated complaints. However, some attorneys pose a substantial threat of harm to the public despite only a few pending loan modification misconduct complaints. Since mid-2009, the Loan Modification Team has filed eleven section 6007(c) petitions, ten of which have been granted by the State Bar Court. One matter is currently pending.

## **DISCUSSION**

By statute, hearings and records of original disciplinary proceedings, including filing for involuntary inactive enrollment under Section 6007(c), are public following the filing of a Notice of Disciplinary Charges. (Bus. & Prof. Code §§6086(a)(1), 6086.1(a)(2)(A), 6086.1(b); rule 5.9, Rules Proc. of State Bar.) Until fairly recently, the State Bar did not post the notice of disciplinary charges online.<sup>2</sup> In mid- 2008, the Board of Governors approved a new policy authorizing the State Bar to post a filed notice of disciplinary charges and any reply on a member's profile page on the Bar's website under a section entitled, "Disciplinary and Related Actions."

Upon approval of this policy, the Board recognized that posting this information helps to fulfill the State Bar's duty to protect the public, which includes informing the public about the work of the State Bar, the right of all persons to make complaints against attorneys, and the nature and procedures of the discipline system protection. A true and correct

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<sup>2</sup> In or about July 2005, the State Bar began posting disciplinary decisions and orders on stipulated dispositions on the member's profile page on the State Bar's website.

copy of the filed Notice is now posted as a PDF on the member's profile page on the State Bar website. This is the only way for a member of the public to review disciplinary charges pending against a lawyer on the Bar's website.

In contrast, although such proceedings are also public, a petition filed by the State Bar under Business & Professions Code section 6007(c) to enroll an attorney involuntarily on inactive status based on "threat of harm" to clients or the public, is not currently authorized for posting on the Bar's website.

### **Criteria for a Consumer Alert Posting**

To adequately protect clients and the public from the risk of further harm from lawyers who remain on active status pending prosecution of significant loan modification misconduct, OCTC propose here an extension of the website policy in two parts. The first part consists of posting a Consumer Alert online on the member's State Bar website profile page when 15 or more cases of loan modification are included in a notice of disciplinary charges filed in the State Bar Court.

The business model used by loan modification companies uses mass scale advertising and call center solicitation. Many schemes involve nominal fees or fees under \$5,000. As such, attorneys involved in these schemes often accumulate a multitude of complaints involving similar acts of misconduct based on the particular *modus operandi*. In developing the criteria for this consumer alert proposal, OCTC determined that a monetary threshold is less meaningful than the volume of complaints.

OCTC concluded that a more meaningful definition of "significant" loan modification misconduct involves the filing of at least 15 disciplinary cases. However, a single notice of disciplinary charges may charge an attorney with multiple counts of ethical violations arising from various cases (arising from individual consumer complaints), often listed by case number. The cases, though charged in a single notice, typically involve unrelated clients. This Consumer Alert, coupled by a disclaimer about filed charges, would be posted upon the filing a notice of disciplinary charges including 15 or more cases of loan modification misconduct, regardless of the particular ethical violations implicated.<sup>3</sup>

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<sup>3</sup> Disciplinary charges for loan modification misconduct involve a broad range of possible ethical violations, including but not limited to: aiding in the unauthorized practice of law ( Rule 1-300(A); unauthorized practice of law in another state(Rule 1-300(B)); formation of a partnership with non-lawyer for the practice of law (Rule 1-310, Rules of Prof. Conduct); sharing fees with a non-lawyer (Rule 1-320); giving something of value for the purpose of securing employment (Rule 1-320(B), Rules of Prof. Conduct and Bus. & Prof. Code §6151-6152); false advertising (Rule 1-400, Rules of Prof. Conduct); solicitation for employment (Rule 1-400(C), Rules of Prof. Conduct); failure to perform (Rule 3-110, Rules of Prof. Conduct); failure to refund unearned fees (Rule 3-700((D)(2), Rules of Prof. Conduct); collecting an illegal fee (Rule 4-200(A), Rules of Prof. Conduct); failure to communicate with the client (Bus. & Prof. Code §6068(m)); and collection of an advanced fee in violation of Civil Code section 2944.6 or 2944.7(Bus. & Prof. Code §6106.3.)

OCTC acknowledges that the posted notice of disciplinary charges, once opened and read, discloses any loan modification misconduct complaint filed against a lawyer.<sup>4</sup> However, we believe that stronger public protection measures are warranted to protect current or prospective clients from additional harm by posting a prominently placed Consumer Alert on the State Bar member's profile page.

The proposed Consumer Alert would contain the following message (the words shown in underline provide hyperlinks to the website):

**CONSUMER ALERT** The State Bar of California has filed disciplinary charges against this attorney alleging 15 or more cases of loan modification misconduct. Loan modification misconduct is a serious disciplinary offense prosecuted by the State Bar.

To ensure fair treatment of accused members, a disclaimer would follow any Consumer Alert explaining that filed charges are only allegations and the member is presumed to be innocent until the charges have been proven. The proposed disclaimer language would read as follows:

**DISCLAIMER: Any Notice of Disciplinary Charges filed by the State Bar contains only allegations of professional misconduct. The attorney is presumed to be innocent of any misconduct warranting discipline until the charges have been proven.**

To see a mock-up of the proposed Consumer Alert and Disclaimer on a member's profile page, see Attachment B referring to John Doe #999999. As with the policy on removing a filed notice and any response, the Consumer Alert and Disclaimer would similarly be removed upon the filing of a State Bar Court decision or order.

The second part of this proposal consists of posting a Consumer Alert and accompanying disclaimer upon the filing of a petition seeking the member's involuntary inactive enrollment pursuant to Business and Professions Code section 6007(c) [threat of public harm] when the petition includes, as a basis for application, loan modification misconduct (regardless of the number of cases.)<sup>5</sup> The Consumer Alert and Disclaimer would be removed upon the filing of a State Bar Court decision or order.

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<sup>4</sup> Rule 5.41(B), Rules of Proc. of the State Bar, requires a notice of disciplinary charges to, *inter alia*: "(1) cite the statutes, rules, or Court orders that the member allegedly violated or that warrant the proposed action; (2) contain a statement of facts comprising the violations in sufficient detail to permit the preparation of a defense; [and] (3) relate the stated facts to the statutes, rules or Court orders that the member allegedly violated or that warrant the proposed action...."

<sup>5</sup> To proceed under Business & Professions Code section 6007(c), rule 5.226, Rules of Proc., requires a verified application which must identify any investigation matters or pending disciplinary proceedings relied on by case number and complaining witness name (if any). "Otherwise, the application itself must cite the statutes, rules or court orders allegedly violated, or that warrant involuntary inactive enrollment. It

Interim inactive enrollment requests filed by the State Bar pursuant to Business and Professions Code section 6007(c) are reserved for extraordinary, expedited matters to quickly remove an attorney from the practice of law to avoid further harm pending formal disciplinary charges. The requisite showing of threat of harm could conceivably be demonstrated by a relatively few number of cases if those matters-or the attorney's surrounding misconduct- are sufficiently egregious to warrant interim suspension. OCTC does not believe that a numerical threshold of complaints is warranted to justify a consumer alert warning under these circumstances.

To be consistent with the State Bar's policy on posting filed notices of disciplinary charges, the Bar's website policy should also include posting the filed Section 6007(c ) petition itself-in addition to a prominently placed Consumer Alert- and any reply until the State Bar Court files a decision or order adjudicating the petition.

### **Due Process Safeguards**

OCTC believe that the proposed policy amply satisfies due process considerations of the respondent about whom a Consumer Alert is made.

First, two separate disclaimers will appear on the member's profile page. Both the current disclaimer in the section entitled "Disciplinary and Related Actions" and the proposed disclaimer for posting a Consumer Alert caution that pending charges should not be considered as evidence of culpability until the charges are proven.

More significantly, as explained earlier, a number of due process safeguards are already in place prior to the filing of any notice of disciplinary charges. For example, a notice of disciplinary charges is filed only following a completed investigation of a complaint by OCTC's professional investigators and supervising attorneys, including opportunities for the lawyer to reply to the complaint. An investigation of a loan modification complaint may entail a combination of the following methods: site visit, interview witnesses, request the lawyer to respond to investigative developments in writing, subpoena and review bank records, and exchange information with state and federal agencies investigating the same attorney on related civil or criminal proceedings.

After a completed investigation and written statement of the case is forwarded to the Trials Unit's trial attorney, the attorney has another opportunity to reply and meet and confer with the State Bar to resolve the complaint. In addition, the attorney may also meet with a State Bar Court judge and the Bar's attorney in an early neutral evaluation conference. If the matter is still not resolved by dismissal, admonition or stipulation to discipline or resignation with charges pending, the Bar's prosecutor must determine whether reasonable cause exists to file a notice of disciplinary charges. Notice filing requires "reasonable cause" to believe that a member has committed a violation of the

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must also state the particular acts or omissions that constitute the alleged violation or violations, or that form the basis for warranting involuntary inactive enrollment."

State Bar Act or Rules of Professional Conduct and a “fair, adequate and reasonable opportunity” for the member to deny or explain the matters which are the subject to the notice.” (Rule 2604, Rules Proc. of State Bar.)

Similarly, a petition under section 6007(c) must include, in addition to sufficient proof of the presence and continued risk of substantial client or public harm, a verified application which includes facts supported by declarations, transcripts or requests for judicial notice, alleges disciplinary violations, and relates the facts with particularity to support the rule, order or statutory violations. (Rule 5.226, Rules of Proc.) Any order finding that the lawyer’s conduct poses a substantial threat of harm to clients or the public warranting interim suspension must be based on a finding that “there is a reasonable probability that the State Bar will prevail on the merits of the underlying disciplinary matter.” (Bus. & Prof. Code §6007(c)(2)(C).)

**FISCAL / PERSONNEL IMPACT:**

Some personnel impact is involved, to the extent that staff will be required to identify whether a notice of disciplinary charges involves 15 or more cases of loan modification misconduct or a section 6007(c) petition relied in whole or part on loan modification misconduct, post, and eventually remove the consumer alert and disclaimer upon the filing of a decision or order resolving the proceedings. Where a filed section 6007(c) petition relies upon loan modification misconduct, staff would also be required to identify such petitions, post them, and eventually remove the petition and any response upon the filing of a decision or order resolving the proceedings.

**RULE AMENDMENTS:**

Not applicable.

**BOARD BOOK IMPACT:**

Not applicable.

**RECOMMENDATION**

The Office of the Chief Trial Counsel recommends that the Board Committee on Regulation, Admissions and Discipline release the proposed policy authorizing the posting of a consumer alert online and a Business and Professions Code section 6007(c) petition involving significant loan modification misconduct as set forth as Attachment A, for a 45-day public comment period.

**PROPOSED BOARD COMMITTEE RESOLUTION:**

Should this Board Committee agree with the above recommendation, the following resolution would be appropriate:

**RESOLVED**, that the Board Committee on Regulation, Admissions & Discipline hereby authorizes the release of the proposed policy attached as Attachment A regarding 1) the online posting of a Consumer Alert and disclaimer on the member's State Bar profile page when either 15 or more cases of loan modification misconduct are included in a filed notice of disciplinary charges or loan modification misconduct (regardless of the number of cases) forms the basis, in whole or part, of a filed Business & Professions Code section 6007(c) petition, until the State Bar Court files a decision or order; and 2) the online posting of a Business & Professions Code section 6007(c) petition which relies on loan modification misconduct (regardless of the number of cases), and any response, until the State Bar Court files a decision or order; and it is

**FURTHER RESOLVED**, that the release of the attached policy statement set forth in Attachment A for public comment does not constitute, and shall not be considered, as approval of the Board of Governors of the State Bar of the matters published.