

**IN THE
UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT**

No. 00-50139

WASHINGTON LEGAL FOUNDATION, WILLIAM R. SUMMERS,
and MICHAEL J. MAZZONE,

Plaintiffs-Appellants,

v.

TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION; RICHARD TATE,
in his official capacity as Chairman of the Texas Equal Access to Justice
Foundation; THOMAS R. PHILLIPS, Chief Justice, NATHAN R. HECHT,
Justice, CRAIG T. ENOCH, Justice, PRISCILLA R. OWENS, Justice
JAMES A. BAKER, Justice, GREG ABBOTT, Justice, DEBORAH G. HANKINSON,
Justice, HARRIET O'NEILL, Justice, and ALBERTO R. GONZALES, Justice,
in their official capacities as Justices of the Supreme Court of Texas,

Defendants-Appellees.

**APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF TEXAS, AUSTIN DIVISION**

MOTION TO CERTIFY QUESTION TO TEXAS SUPREME COURT

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TEAJF AND ITS CHAIRMAN**

CERTIFICATE OF INTERESTED PERSONS

Washington Legal Found., et al. v. Texas Equal Access to Justice Found., et al., No. 00-50139

The undersigned counsel of record certifies that the following listed persons have an interest in the outcome of this case. These representations are made in order that the judges of this court may evaluate possible disqualification or recusal:

Appellants: Washington Legal Foundation
William R. Summers
Michael J. Mazzone

The Washington Legal Foundation is a nonprofit corporation organized under § 501(c)(3) of the Internal Revenue Code. It has no parent corporations and no stock owned by a publicly held corporation.

Appellants' Counsel: Charles Fried
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Richard A. Samp

Appellees: Texas Equal Access to Justice Foundation
Richard Tate
Hon. Thomas R. Phillips
Hon. Nathan R. Hecht
Hon. Craig T. Enoch
Hon. Priscilla R. Owens
Hon. James A. Baker
Hon. Greg Abbott
Hon. Deborah G. Hankinson
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In Appellants' view, this case "raises complex issues of constitutional law." Appellants' Brief at ii. However, a federal court has a "strong duty to avoid constitutional issues that need not be resolved in order to determine the rights of the parties to the case under consideration."¹ In this case, determination of a state law issue already pending in the Texas court system could resolve the rights of the parties and render moot any constitutional decision of this Court. Accordingly, Appellees request this Court certify this potentially dispositive question to the Texas Supreme Court.

SUMMARY

The linchpin of the United States Supreme Court's prior decision in this case is its statement that "under Texas law the principal held in IOLTA trust accounts is the 'private property' of the client." *Phillips v. Washington Legal Foundation*, 118 S. Ct. 1925, 1930 (1998). On this issue, Texas law governs. If the Supreme Court's conclusion is wrong, and the "principal" in an IOLTA trust account does not belong to the client, Appellants' takings challenge fails at the threshold.

A considerable and growing body of authority suggests that the Supreme Court's *Phillips* decision may not correctly state Texas law. The decision relies for support on the language of two Texas court rules, both of which have been substantively amended in a way that casts serious doubt on the continued viability of the Supreme Court's prior analysis. Moreover, a Texas court of appeals has explicitly and persuasively criticized the *Phillips* holding as an incorrect statement of Texas law.

Pending state court litigation may also moot this case. A licensed Texas attorney has

¹ *County Court of Ulster County, N.Y. v. Allen*, 442 U.S. 140, 154 (1979); see also, e.g., *HC Gun & Knife Shows, Inc. v. City of Houston*, 201 F.3d 544, 548 (5th Cir. 2000) (preferring to decide case on state statutory preemption ground, rather than federal constitutional grounds).

challenged the Texas IOLTA program.² The gist of his claim is that if *Phillips* correctly states Texas law, then attorney participation in IOLTA is tantamount to conversion, the theft of client funds. If this attorney’s claim is sustained on appeal, then substantial restructuring of the Texas IOLTA program would be required, likely mooted this appeal. If the attorney’s claim is not sustained, the likely reason would be that Texas courts authoritatively reject *Phillips*’ view of Texas law governing IOLTA accounts. This outcome also would moot the present appeal.

Respondents therefore respectfully request that the question whether a client has any “private property” right in a Texas IOLTA account be certified to the Texas Supreme Court for decision.

GROUNDS FOR MOTION

1. A Contextual Overview of Relevant Texas Banking Law.

The need for certification can be understood best if one begins with a few well settled rules of banking law. Texas law, as well as the law of every other American jurisdiction, recognizes two types of bank accounts—general and special. *See, e.g., Hudnall v. Tyler Bank & Trust Co.*, 458 S.W.2d 183, 186 (Tex. 1970). These two types of accounts, while similar in outward appearance, have very different legal consequences. When money is deposited into a general account, the depositor relinquishes all title to the funds. The relationship becomes one of debtor and creditor, with the financial institution as debtor. *See, e.g., Hudnall*, 485 S.W.2d at 186; *Bandy v. First State Bank of Overton*, 835 S.W.2d 609, 618-19 n.4 (Tex. 1992). By contrast, a “special account” is a trust or bailment relationship. Title does not pass. Rather, the depositor retains title and ownership

² The state court litigation is *Paulsen v. Texas Equal Access to Justice Foundation*, which is pending in the Texas Supreme Court as No. 00-0468.

of the funds on deposit. *Hudnall*, 485 S.W.2d at 186; *Bandy*, 835 S.W.2d at 618-19 n. 4.

Special deposits or accounts are not often encountered, hence the name “special.” *Cf. Citizens Nat’l Bank of Dallas v. Hill*, 550 S.W.2d 246, 248 (Tex. 1974) (stating that bank deposits “ordinarily” are general accounts). Accordingly, every bank account is presumed to be a general account until proven otherwise. *Hudnall*, 458 S.W.3d at 186; *Texas Commerce Bank v. Townsend*, 786 S.W.2d 53, 54 (Tex. App.–Austin 1990, writ denied).

It should be emphasized that these rules are well settled and were deeply rooted in the common law long before IOLTA programs came on the scene. As early as 1864, the United States Supreme Court recognized:

All deposits made with bankers may be divided into two classes, namely those in which the bank becomes bailee of the depositor, the title to the thing deposited remaining with the latter; and that other kind of deposit of money peculiar to banking business, in which the depositor, for his own convenience, parts with the title to his money, and loans it to the banker, and the latter, in consideration of the loan of the money and the right to use it for his own profit, agrees to refund the same amount, or any part thereof, on demand.

Marine Bank v. Fulton Bank, 69 U.S. 252, 256 (1864). Another court added, nearly three quarters of a century ago, that “[t]here is no principle of the law of banking more firmly established than that relating to the title of money deposited generally in a bank. Such a deposit passes title immediately to the bank, and the relation of debtor and creditor arises” *Lawrence v. Lincoln County Trust Co.*, 131 A. 863, 866 (Me. 1926).

The fact that a case may have constitutional overtones does not necessarily change the general rules of contract and banking law. For example, in 1995 the United States Supreme Court applied general banking law to reject the assertion that a hold on a general account “took” something

from a bankrupt depositor in the constitutional sense. *See Citizens Bank of Maryland v. Strumpf*, 116 S. Ct. 286, 290 (1995). The question was whether an administrative hold placed by the bank on the bankrupt's account was a statutorily prohibited attempt to obtain possession or control of "property" of the estate. *See* 11 U.S.C. § 362 (a) (3). Speaking for a unanimous Court, Justice Scalia answered the question in the negative:

[The bankruptcy trustee's] reliance on these provisions rests on the false premise that [the bank's] administrative hold took something from [the depositor] or exercised dominion over property that belonged to [the depositor]. That view of things might be arguable if a bank account consisted of money belonging to the depositor and held by the bank. In fact, however, it consists of nothing more or less than a promise to pay from the bank to the depositor, and [the bank's] temporary refusal to pay was neither a taking of possession of [the depositor's] property nor an exercising of control over it, but merely a refusal to perform its promise.

Strumpf, 116 S. Ct. at 290. This resounding rejection of a takings claim as applied to a bank account is in perfect accord with well developed common law — and the Texas law — of banking.

2. Considering Phillips in the Context of Texas Banking Law.

Placed in context with the well-settled rules of contract and banking law just outlined, the United States Supreme Court's *Phillips* decision is not easily comprehended. The statement in *Phillips* that "under Texas law the principal held in IOLTA trust accounts is the 'private property' of the client," 118 S. Ct. at 1930, is tantamount to a statement that plaintiff-appellant Michael Mazzone's IOLTA account is a Texas special account. Otherwise, there would be only a debtor-creditor relationship, the account would be "general," and the funds would be the bank's "private property" by transfer of title.

There are two possible bases for the Supreme Court's apparent conclusion that a Texas IOLTA account has the legal incidents of a special account. Each, on examination, is questionable.

First, the Court referred to the language of two Texas court rules, IOLTA Rule 4 and Texas Disciplinary Rule 1.14. *Id.* Both rules use the phrase “client funds,” which might be interpreted to imply some continuing client ownership rights after deposit. However, in the wake of *Phillips*, the Texas Supreme Court has clarified both rules by adding the following language:

Nothing in this or any other of these Rules prohibits the deposit of client funds into a general account or changes the legal relationship between the depositor and financial institution from that established by contract or by applicable state and federal law.³

While the Texas Supreme Court did not issue any explanation for the amendments, it seems abundantly clear that the state’s high court concluded that *Phillips* read far too much into an ambiguous catch phrase and acted to clarify the phrase.

The second basis for the Supreme Court’s seemingly erroneous conclusion might be misplaced reliance on a single Texas decision, *Sellers v. Harris County*, 483 S.W.2d 242 (Tex. 1972). In *Sellers*, the Texas Supreme Court ruled that competing claimants to \$1 million in insurance proceeds placed in a district court clerk’s registry had a right to interest actually earned while the funds were on deposit pending resolution of the lawsuit. The United States Supreme Court quoted *Sellers*’ conclusion that “[t]he interest earned by deposit of money owned by the parties to that lawsuit is an increment that accrues to that money and to its owners.” 118 S. Ct. at 1931, quoting *Sellers*, 483 S.W.2d at 243. This language certainly sounds like the depositor in that case “owned” the funds on deposit. What the Supreme Court may have overlooked, however, is that

³ Order of the Court Approving Amendments to the Rules Governing the Operation of the Texas Equal Access to Justice Foundation and Comment 1 to Rule 1.14 of the Texas Disciplinary Rules of Professional Conduct, Misc. Docket No. 99-9016 (Jan. 25, 1999). The quoted language is from the amendment to IOLTA Rule 4. The amendment to Comment 1 of Disciplinary Rule 1.14 is substantially the same.

Sellers involved a special deposit, not a general deposit of funds.⁴ Accordingly, the *Phillips* decision may unwittingly have elevated a comparatively rare exception to the general rule of Texas banking law to the status of a general, and invariable, rule.

The strong possibility that *Phillips* is premised on a misreading of Texas banking law is underscored by a very recent decision from the Austin Court of Appeals. *See Paulsen v. Texas Equal Access to Justice Foundation*, 1999 WL 1078698, No. 03-98-00709-CV (Tex. App.–Austin, Dec. 2, 1999, pet. pending). The decision cannot be taken lightly, because the Austin Court of Appeals is the same court that issued what is certainly the leading Texas decision, and possibly the leading decision in the nation, on the legal rights created by attorney trust accounts. *See Townsend*, 786 S.W.2d 53; *see also* Randy R. Koenders, Annotation, *What Constitutes Wrongful Dishonor of Check Rendering Payor Bank Liable to Drawer Under UCC § 4-402*, 98 A.L.R. 4th568 (1991) (using *Townsend* as lead case). The Austin Court of Appeals’ opinion in the *Paulsen* case contains some harsh criticism of the United States Supreme Court’s initial opinion in this case:

The *Phillips* decision does appear to have at least overlooked, if not misstated, a large body of Texas banking law that distinguishes between “general” and “special” accounts. *See, e.g., Texas Commerce Bank v. Townsend*, 786 S.W.2d 53 (Tex. App.–Austin 1990, writ denied). In a general account, Texas law is clear that the financial institution holds title to the funds deposited. *See id.* at 54. [The attorney’s] contract with his bank establishing an IOLTA account expressly states that it is a general account. Since the *Phillips* court stated that “interest follows principal,” *Phillips*, 524 U.S. at 165-66, the natural conclusion would be that the interest earned in an IOLTA account belongs to the banks as well. This appears to be in direct conflict with the

⁴ This fact becomes clear when one examines the court of civil appeals decision in *Sellers*. The statutes setting up the depository account in question provided that the money was to be deposited into a “special fund,” and further, that “deposit of funds in the County Treasury shall not in any wise change the ownership of any fund so deposited.” *Harris County v. Sellers*, 468 S.W.2d 950, 954-55 (Tex. Civ. App.–Houston [1st Dist.] 1971), *rev’d*, 483 S.W.2d 242 (Tex. 1972). Thus, both by operation of the common law applicable to special accounts and by the language of the particular statute at issue, the depository bank did not take title to the funds on deposit.

actual *Phillips* holding that interest earned in an IOLTA account is the property of the attorney's client. *See id.* at 172.

Paulsen, 1999 WL 1078698 at 5.

3. The District Court's "General Account" Ruling on Remand.

The only way the Supreme Court's ruling in *Phillips* could mesh with settled Texas contract and banking law would be if attorney Mazzone's IOLTA account was in fact a special deposit. The initial *Phillips* appeal rose from the grant of a pre-discovery motion for summary judgment. *See Phillips*, 118 S. Ct. at 1929. Accordingly, in the absence of a detailed factual record, the Supreme Court may have given Appellees the benefit of the doubt and assumed attorney Mazzone's IOLTA account was a special account. On remand, however, the precise nature of the IOLTA account at issue became the subject of specific inquiry. As the district court's opinion correctly states, "Mr. Mazzone testified that the Dow Cogburn [IOLTA] trust account was a general account." *Washington Legal Foundation v. Texas Equal Access to Justice Foundation*, 86 F. Supp. 2d 624, 631 (W.D. Tex. 2000). The court followed up this conclusion with a specific fact finding that "the Dow Cogburn IOLTA account is and was a general account." *Id.*

In spite of this uncontradicted evidence and attendant specific fact finding, the district court refused to decide whether Dow Cogburn's bank—not attorney Mazzone and certainly not his client—"owns" any "funds" in Dow Cogburn's IOLTA account. Though the district court does not say so, the only principled basis for its refusal to revisit the property issue would be the law of the case doctrine, that is, that the client "owns" the interest on this IOLTA account because the United States Supreme Court has said so. The law of the case doctrine, however, does not apply if "(i) the evidence on a subsequent trial was substantially different, (ii) controlling authority has since made a

contrary decision of the law applicable to such issues, or (iii) the decision was clearly erroneous and would work a manifest injustice.” *North Miss. Comms., Inc. v. Jones*, 951 F.2d 652, 656 (5th Cir. 1992). In this case, all three exceptions are arguably present. Evidence at trial establishes that this IOLTA account is a Texas general account. *See, e.g., Washington Legal Foundation*, 86 F. Supp. 2d at 631. The Texas Supreme Court, the “controlling authority” on matters of Texas law, has changed the court rules on which the *Phillips* decision relied. *See supra* section B. And the Austin Court of Appeals has opined that the *Phillips* ruling is clearly erroneous, in that the Court “at least overlooked, if not misstated, a large body of Texas banking law.” *Paulsen*, slip op. at 10.

CONCLUSION

On the threshold property question, the United States Supreme Court’s *Phillips* decision makes it clear that Texas law governs. *See Phillips*, 118 S. Ct. at 1930. Based on the facts produced at trial, all parties agree that the IOLTA account in this case is a general account. All authority, in Texas and every other American jurisdiction, make it clear that the bank alone holds title to funds in a general account. Appellees respectfully request that the question whether a client has any “private property” right in a Texas IOLTA account be certified to the Texas Supreme Court since determination of this state law issue will resolve the rights of the parties to this case without reaching constitutional issues.

Respectfully submitted,

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EQUAL ACCESS TO JUSTICE
FOUNDATION AND ITS CHAIRMAN**

CERTIFICATE OF SERVICE

The undersigned certifies that a copy of the foregoing instrument was served upon the attorney of record of all parties to the above cause in accordance with Rule 25 of the Federal Rules of Appellate Procedure and Local Rule 28.3(n) on this _____ day of August, 2000 as follows:

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