Session 308: Hot Topics in Inside Counsel-Outside Counsel Attorney Client Relationship Management

The practice of law has seen significant changes in recent years that have redefined relationships between inside counsel and the outside counsel they hire. The need to control legal costs, increased demand for efficiencies, a shrinking legal services market, and increased competition, have resulted in fundamental changes in the basic structure of some attorney-client relationships. If not handled correctly, some of these changes can cause significant tensions and disruption, if not the complete destruction, of the attorney-client relationship, as well as exposure for ethical violations and/or civil liability, and reputational damage all around. This panel of inside and outside counsel will converge and in a single panel explore hot topics in the actual relationship between inside counsel and outside counsel (from outside counsel guidelines, to advanced conflict waivers, to the in-firm privilege), explore what each side needs, discuss what the evolving law governing lawyers demands, and provide possible solutions and best practices for inside and outside counsel in navigating these developing waters. If it is true that expectation is at the root of all disappointment, this panel will provide tools for counsel to facilitate communication and manage expectations on both sides so that the relationship remains as strong as it could be.

Program Chair & Moderator:
Wendy Wen Yun Chang, Partner, Hinshaw & Culbertson LLP

Speakers:
Shawn M. Harpen, Chief Legal Officer and General Counsel, Patrón Spirits International AG
Lily J. Lu, Vice President, Deputy General Counsel and Chief Compliance Officer, IDEXX Laboratories, Inc.
William Yu, Partner, Lewis Brisbois Bisgaard & Smith LLP
1. Outside Counsel Guidelines
   a. Conflicts of Interest - Model Rules 1.7, 1.8, 1.9
   b. Definition of Conflicts
   c. Who is the Client?
      i. Re-definition of "who is the client"
      ii. Parent-Subsidiary Conflicts
         1. ABA Formal Opinion 95-390
      iii. Springing/Thrust Upon Conflicts
         1. Orange County Bar Assn. Formal Opinion 2012-1
   d. Case handling instructions
      i. Duty of Competence - Model Rule 1.1
   e. Disaggregation of Legal Services and Limited Scope Engagements
      i. Duty of Competence - Model Rule 1.1
      ii. Scope of Representation and Allocation of Authority Between Client and Lawyer – Model Rule 1.2
      iii. Duty to Communicate –
         1. Model Rule 1.4
         2. Duty to Educate Client
      iv. Duty to Supervise – Model Rule 5.1, 5.2
   f. Outsourcing
   g. Choice of Law
      i. Rejected by ABA 20/20
      ii. But see comment 8.5
2. Advance Waivers
   a. Model Rules 1.7, 1.8, 1.9
   b. No per se bar
   c. Enforceability depends on the adequacy of the disclosure
   f. In re Shared Memory Graphics LLC, 659 F.3d 1336 (Fed. Cir., 2011)
3. In Firm Privilege
   a. Law firm general counsel holds a general attorney client privilege with firm. US v. Rowe, 96 F.3d 1294 (9th Cir. 1996)
b. Historical Approach – ethics based analysis
   i. Model Rule 1.7
      1. Is an in firm consultation about a current client matter a current client conflict of interest?
   ii. Model Rule 1.7, comment 1 – Duty of Loyalty
   iii. Traditional Approach: No privilege
   iv. Evolution – limited exception on policy grounds
      1. E.g. Thelen Reid & Priest LLP v. Marland (N.D. Cal. 2007) 2007 WL 578989

c. Trend – full privilege recognition – divorced from ethics analysis
   v. Crimson Trace Corp. v. Davis Wright Tremaine LLP (2014) 355 Or. 476
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Outsource, ethically

By WENDY WEN YUN CHANG

Midfirm is a law firm of 20 attorneys. Each attorney carries a healthy case load, and is working at full capacity. Midfirm is retained to defend Farmco, a Fortune50 company, in a multimillion dollar “bet the company” dispute over corn crops, brought by Agrimart. Midfirm is chosen because Midfirm’s partner, 65-year-old Ella Expert, with the assistance of her experienced and well-trained team of assisting attorneys, is one of only a handful of experts in this particular area of the law. Ella is a traditional practitioner, and works best with a yellow pad, a ballpoint pen, and a Dictaphone. While Ella has a computer, her familiarity and comfort level with it is very basic. She has a cell phone, but uses no other technology in her practice. The other members of her team have somewhat of a higher facility with computers and technology, but nothing beyond a basic consumer level understanding.

Farmco has been “paperless” for some time and the vast majority of the evidentiary information relevant to the Agrimart case is in the form of a very large amount of electronic data. There are also numerous issues relating to the alleged integrity of some of the data at issue.

As the litigation gets going, Ella quickly realizes that she must bring in some help. Opposing counsel is Monolith Law, which is making its best efforts to bury Midfirm in paper. The nature of the e-discovery involved is making the case larger than Midfirm can handle on its own. It is also quickly overwhelming the Midfirm attorneys, whose slowness in handling the e-discovery is preventing them from turning to the other substantive legal issues in the case. Midfirm uses old technology, and its attorneys are not certain their searches of the electronic data are discovery issues in a case.

Midfirm has been interpreted to permit an attorney to comply with it through consulting another attorney reasonably believed to be competent, or 2) by consulting another attorney reasonably believed to be competent, or 2) by acquiring sufficient learning and skill before performance is required.

Rule 3-110(C) makes clear that an attorney may comply with her duty of competence, if she herself is lacking in a specific area, either by associating with, or consulting with, an attorney who has such skill, or by acquiring sufficient learning and skill before performance is required. This rule has been interpreted to permit an attorney to comply with it through consulting with a non-attorney expert, and where the non-attorney expert can remedy the attorney’s lack in knowledge, and where the lack is in a non-legal area, such as certain technology issues. See e.g., Cal. State Bar Formal Opinion No. 2010-179, and 2010-184.

The duty of competence under Rule 3-110 includes the duty to supervise the work of subordinate attorneys and non-attorney employee or agents. See Rule 3-110, discussion. This duty would include a duty to supervise those providing the outsourced services. See, e.g. California State Bar Formal Opinion No. 1992-126 (contract temporary attorneys), California State Bar Formal Opinion No. 2004-165 (limited appearance counsel).
An attorney has a duty to provide independent professional judgment on behalf of a client at all times. This duty requires that the attorney remain ultimately responsible for any work product generated for the client by the outsource entity, and the attorney may not delegate to the outsource entity responsibility for, or authority over, legal strategy, questions of judgment or the final product created by the outsource entity for the client. LACBA Form Opn. 518.

Further, a lawyer has a duty to “maintain inviolate the confidence, and at every peril to himself or herself, preserve the secrets of his or her client.” California Business & Professions Code, § 6068(e)(1). Confidential information, for the purpose of Business & Professions Code § 6068(e) includes any information gained in the engagement which the client does not want disclosed or the disclosure of which is likely to be embarrassing or detrimental to the client. California State Bar Formal Opinion No. 2004-165. This duty applies even where the facts may already be a part of public record, or where there are other sources of information. Ibid. (citing LACBA Formal Opinion Nos. 267, 386).

Thus, with certain limited exceptions, a client’s confidential information may not be revealed absent the informed written consent of the client. Rule 3-100(A). Compliance with an attorney’s duty of confidentiality is considered to be an element of the duty of competence. California State Bar Formal Opinion No. 2010-179. In an outsourcing situation, complying with an attorney’s duty of competence may require the revelation of some confidential information to the outsource entity service provider. Such disclosure is permissible so long as the attorney takes reasonable steps to ensure that the contractors agree to confidentiality, and can and will act to maintain it, prior to the disclosure. California State Bar Formal Opinion No. 2004-165 (citing LACBA Formal Opinion 374 and 423 (finding lawyers may use outside contractor data processors for client billings and the like so long as contractors are informed of and agree to keep client information confidential.)) Attorney must consider that some information may be so sensitive that it may NOT make this outside disclosure. Ibid; see also generally California State Bar Formal Opinion No. 2010-179. Such analysis must be made as circumstantially warranted.

Here, the hypothetical raises two potential issues: legal assistance due to understaffing and lack of knowledge, and non-legal assistance related to non-legal technology services. Ella and Midfirm are lacking in both technical knowledge about the specialized technology issues on the ediscovery, as well as the data integrity issues. Midfirm also faces legal staffing issues that are taking them away from being able to address the substantive legal issues relating to the litigation, an area of their specific expertise.

Under Rule 3-110, Ella and Midfirm should, at the very least, consult with an expert to educate themselves about the technical issues they are unfamiliar with, especially as Midfirm formulates recommendations to Farmco relating to the litigation. Given the lack of in-house expertise on the technology issues, the outsourced software issues, and given how lack of expertise is overwhelming Midfirm attorneys and also distracting them from being able to focus on the substantive legal issues, Midfirm could, beyond simple consultation, outsource the day-to-day handling of parts of the technology services, such as parts of the e-discovery document review, so long as at least one Midfirm attorney educated herself sufficiently in consultation with the outsource entity, or with a retained expert consultant, so that such attorney could competently supervise the outsource entity and the service being provided. Such outsourcing would be permissible only after Midfirm had taken sufficient steps to assure itself that the vendor, and those who will be staffing the case, are competent to perform the work adequately, appropriately, and securely. ABA Formal Opinion 08-451. This conclusion is supported by the American Bar Association, which has approved outsourcing, under certain circumstances, of both legal and non-legal support services. ABA Formal Opinion No. 08-451. What outside vendor would be appropriate for the case, legal or non-legal, is a factual and situational analysis, which requires a careful case-by-case review by the decision makers involved.

The Duty to Communicate

California Rules of Professional Conduct Rule 3-500 states:

A member shall keep a client reasonably informed about significant developments relating to the employment or representation, including promptly complying with reasonable requests for information and copies of significant documents when necessary to keep the client so informed.

Business & Professions Code §6068(m) states:

It is a duty of an attorney to “... keep clients reasonably informed of significant developments in matters with regard to which the attorney has agreed to provide legal services.”

In an outsourcing scenario, the attorney must disclose the use of an outside attorney or vendor to the client if that outsourcing is a “significant development.” Factors to consider what constitutes a “significant development” are (a) whether responsibility for overseeing the client’s matter be changed; (b) will the new attorney be performing a significant portion or aspect of the work; or (c) whether staffing of the matter has been changed from what was specifically represented to or agreed to with the client. See California Formal Opinion No. 1994-138 (citing LACBA Formal Opinion No. 473). Further, if attorney knows or reasonably should know the client expects only a specific attorney or specific group of attorneys to work on its matter, the proposed use of other attorneys requires disclosure under Rule 3-500. Ibid.

Here, Farmco retained Midfirm specifically for its expertise in the area of law at issue in the Agrimart litigation. If that understanding was extended to the entirety of the engagement, then Midfirm’s outsourcing of services under the engagement could constitute a “significant development” requiring disclosure to Farmco, a duty of disclosure that should be made in the initial engagement if possible, or if that is not possible (as happened here because the realization did not occur until after the engagement had already commenced), as soon thereafter as the decision to hire an outsource entity is made. California State Bar Formal Opinion No. 2004-165.

Payment of the Outsource Entity’s Fees

California Rule of Professional Conduct Rule 2-200 states:

(A) A member shall not divide a fee for legal services with a lawyer who is not a partner of, associate of, or shareholder with the member unless:

1. The client has consented in writing thereto after a full disclosure has been made in writing that a division of fees will be made and the terms of such division; and

2. The total fee charged by all lawyers is not increased solely by reason of the provision for division of fees and is not unconscionable as that term is defined in rule 4-200.

Neither a member nor a law firm shall directly or indirectly share legal fees with a person who is not a lawyer. . . .
Payment to an outsource entity would not be considered an improper fee split if (1) the amount paid to outside attorney is compensation for work performed and is paid whether or not law firm is paid by client, 2) the amount paid by attorney to outside attorney is not negotiated or based on fees paid to attorney by client, and 3) the outside attorney has no expectation of receiving percentage of fees. California Formal Opinion No. 1994-138.

If Midfirm’s arrangement with the outsource entity meets the foregoing criteria, such arrangement does not constitute an improper fee split. California State Bar Formal Opinion Nos. 1994-138 and 2004-165. Billing the entity’s fee as a cost, or as a separate identified entry, on Midfirm’s bill to Farmco, would also not constitute an improper fee split. Ibid. Finally, there would be no improper fee split if the outsource entity bills Farmco, and is paid by Farmco, directly. Ibid. In these instances, the outside entity is not participating in the division of legal fees paid by the client. LACBA Formal Opinion 518. These types of services are indistinguishable from other types of services that an attorney might purchase, such as paralegal assistance, research clerk assistance, computer research, graphics illustrations or other services. Thus, even if the attorney passes the cost directly to the client, the arrangement does not violate Rule 2-200. Ibid.

If Midfirm contracts for service at an hourly rate from the outsource entity, it would also not constitute a violation of Rule 1-320(A). LACBA Formal Opinion No. 518.

If Midfirm’s contemplated services constitute a “significant development” as discussed above, necessitating disclosure, full disclosure of the nature and extent of the relationship between Midfirm and the outside entity, as well as Midfirm’s intent to charge the outside entity’s fees and costs as a disbursement, should be made to Farmco as early as is possible in the engagement. See, e.g. California State Bar formal Opinion No. 2004-165 and LACBA Formal Opinion No. 473.

Conflicts

Finally, California Rules of Professional Conduct Rule 3-310(C) states:

(C) A member shall not, without the informed written consent of each client:

(1) Accept representation of more than one client in a matter in which the interests of the clients potentially conflict; or

(2) Accept or continue representation of more than one client in a matter in which the interests of the clients actually conflict; or

(3) Represent a client in a matter and at the same time in a separate matter accept as a client a person or entity whose interest in the first matter is adverse to the client in the first matter.

The duty to supervise includes the duty to give assistants appropriate instructions and supervision concerning the ethical aspects of their employment. LACBA Formal Opinion No. 518 (citing Hu v. Fang (2002) 104 Cal. App. 4th 61, 64).

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Here, this duty would require Midfirm to take reasonable steps to satisfy itself that no conflicts exist at outsource entity that would preclude the representation, prior to the commencement of any services by outsource entity.

Conclusion

Midfirm may outsource certain services implicated by the Farmco engagement, subject to the limitations set forth above, and provided that Midfirm supervises all tasks being undertaken, and takes all reasonable steps to retain the ultimate responsibility for the decisions being made, and the services being provided.

Disclaimer: the information in this column is intended to be information and educational only, and does not constitute legal advice. Please cite check all authorities before using.

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[1] All references to “Rule” hereafter, unless otherwise identified, shall refer to the California Rules of Professional Conduct.

[2] While California has not adopted the ABA Model Rules, they may nevertheless serve as guidelines absent on-point California authority or a conflicting state public policy. City & County of San Francisco v. Cobra Solutions, Inc. (2006) 38 Cal. 4th 839, 852. In the absence of related California authority, we may look to the Model Rules, and the ABA Formal Opinions interpreting them, as well as the ethics opinions of other jurisdictions or bar associations for guidance. Rules Prof. Conduct, rule 1-100(A) (Ethics opinions and rules and standards promulgated by other jurisdictions and bar associations may also be considered); State Compensation Ins. Fund v. WPS, Inc. (1999) 70 Cal.App.4th 644, 656.

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May a lawyer represent a corporate subsidiary and, at the same time, take on a representation adverse to that subsidiary’s parent corporation? May that lawyer represent a parent corporation and, at the same time, take on a representation adverse to the parent’s subsidiary? As in many cases of legal and ethical questions, the answer is, it depends.

Specifically, it depends on the particular relationship between the subsidiary and its parent, as well as the relationship between the lawyer and the non-client entity.

Our analysis starts with the basic ethical rules implicated by this tripartite relationship. First, Rule of Professional Conduct 3-310 addresses conflicts of interest and provides that, with respect to concurrent representation of clients, a lawyer “shall not, without the informed written consent of each client . . . [r]epresent a client in a matter and at the same time in a separate matter accept as a client a person or entity whose interest in the first matter is adverse to the client in the first matter.” Rule 3-310(C)(1). Thus, if the lawyer represents one corporate entity in any capacity, Rule 3-310(C)(3) and the lawyer’s duty of loyalty precludes her from taking on another matter adverse to that same entity, regardless how disparate the two matters are. (see Certain Underwriters at Lloyd’s, London v. Argonaut Ins. Co., 264 F. Supp. 2d 914, 919 (N.D. Cal. 2003) (“Simply put, an attorney (and his or her firm) cannot simultaneously represent a client in one matter while representing another party suing that same client in another matter.”) The more interesting question arises when the lawyer represents either the parent or the subsidiary, but not the other, and then is asked to take on an unrelated matter in which she would be adverse to the other entity.

Another rule of particular relevance to this issue is Rule 3-600. That rule provides that when a lawyer represents an organization, “the client is the organization itself, acting through its highest authorized officer, employee, body, or constituent overseeing the particular engagement.” Rule 3-600(A); see also Responsible Citizens v. Super. Ct., 16 Cal. App. 4th 1717, 1726-27 (1993) (“The attorney for a corporation represents it, its stockholders and its officers in their representative capacity. He in nowise represents the officers personally.”) (internal quotation omitted). Rule 3-600(D) further provides: “In dealing with an organization’s directors, officers, employees, members, shareholders, or other constituents, a member shall explain the identity of the client for whom the member acts, whenever it is or becomes apparent the organization’s interests are or may become adverse to those of the constituent(s) with whom the member is dealing.” The effect of Rule 3-600 in the parent/subsidiary context is that the lawyer’s representation of one of the corporate entities does not necessarily preclude the lawyer either from representing the other entity or from being adverse to the other entity. Again, it depends on the circumstances.

Prior to 1997, California courts had not addressed the issue of parent/subsidiary conflicts, although the State Bar issued an opinion in 1989 expressing the view that there was an “alter ego” exception to the general rule that separate corporations, including parents and subsidiaries, should be treated as separate entities for conflicts purposes. Cal. Bar Op. 1989-113; see also Orange County Bar Association Op. 2012-01 (discussing parent-subsidary conflicts in the context of a thrust-upon conflict). The Committee explained that to determine whether this exception applied, the lawyer “should evaluate the separateness of the entities involved, whether corporate formalities are observed, the extent to which each entity has distinct and independent managements and board of directors, and whether, for legal purposes, one entity could be considered the alter ego of the others.” Cal. Bar Op. 1989-113 at 3-4.

A California court first directly addressed this issue in 1997. In Brooklyn Navy Yard Cogeneration Partners, L.P. v. Superior Court, 60 Cal. App. 4th 248 (1997), the court reversed an order granting plaintiff subsidiary’s motion to disqualify counsel who had represented the subsidiary’s parent company in a separate and unrelated matter. The court held that a lawyer may be precluded from representing both entities only where it can be shown that one entity is the alter ego of the other. Id. at 257-58. The court expressly rejected the “notion that a general ‘unity of interests’ between corporate entities is enough to transform a nonclient into a client.” Id. at 253.

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A Representational Trinity: The Parent, the Sub, and the Holy Lawyer

By SCOTT B. GARNER

March 2013

SAMPLE TEST QUESTIONS

Below are sample questions from this month’s MCLE self-assessment test.

1. When a lawyer represents a corporation, she also necessarily represents the shareholders of that corporation.

2. A lawyer may not represent a corporation and, at the same time, represent its shareholders or officers.

3. A party seeking to establish that his former lawyer has a conflict of interest bears the burden of establishing that the lawyer is in possession of confidential information obtained from the former client that could be used against that former client in a current matter.

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Although Brooklyn Navy Yard remains good law, it rarely is followed, as its “alter ego” analysis generally is considered too restrictive. Still, Brooklyn Navy Yard remains instructive in that it was the first case to directly address this issue. And, the framework of its analysis—which it borrows from the State Bar’s Opinion 1989-113—remains helpful. In analyzing the alleged conflict before it, the court sought to answer two questions: (1) whether the parent is a client or entitled to be treated as a client for conflict purposes; and (2) whether the attorney’s duty of loyalty to the subsidiary precludes a representation that is adverse to the parent.” Id. at 254.

The answer to the first question is based on an analysis of Rule 3-600 and, absent specific circumstances suggesting a contrary conclusion, generally will be answered in the negative. Thus, where a lawyer expressly represents, for example, a subsidiary but not a parent, the parent is a mere “constituent” of the client subsidiary (as any other shareholder would be), and is not considered the lawyer’s client. Similarly, where the lawyer represents the parent corporation, she will not automatically be deemed to represent the subsidiary as well. Nor does it matter that, where the parent owns a significant percentage—even 100 percent—of the subsidiary’s stock, it would suffer negative economic consequences (e.g., decline in share value) if the lawyer were to prevail in her action (or transaction) against the subsidiary. Whatever adverse economic consequences were suffered by the parent from the lawyer’s adversity to the subsidiary would be considered an “indirect” adverse consequence—one that “is insufficient to give rise to a breach of the duty of loyalty owed to the parent.” Cal. Bar. Op. 1989-113 at p. 3; but see Certain Underwriters at Lloyd’s London, 294 F. Supp. 2d at 923 (distinguishing the financial harm before it from the financial harm to the parent discussed in State Bar Opinion 1989-113).

Notwithstanding that the lawyer’s representation of one entity does not necessarily mean she also represents the other entity, there certainly may be situations where a lawyer in fact represents both the parent and the subsidiary. Rule 3-600 contemplates as much. Rule 3-600(E) (“A member representing an organization may also represent any of its directors, officers, employees, members, shareholders, or other constituents, subject to the provisions of rule 3-310.”); see also Rule 3-600. Cmt. (“In dealing with a close corporation or small association, members commonly perform professional engagements for both the organization and its major constituents.”). But unless the parties agree to such joint representation, the lawyer will not be deemed to be representing any of the subsidiary’s constituents, including a parent corporation that owns most or even all of the subsidiary’s stock.

Assuming, then, that the lawyer does not represent the parent company, the next question to be asked is whether, in representing one of the organizational entities, the lawyer nonetheless took on some obligation of loyalty to the other entity such that an adversarial relationship would be impermissible. See Flatt, 9 Cal. 4th at 284 (requiring per se disqualification where law firm simultaneously opposes and represents a client, even where two matters are not substantially related). As referenced above, the court in Brooklyn Navy Yard found that such a duty of loyalty to the non-client entity would arise only where the parent and the subsidiary would be “substantially related” (a term also used in State Bar Opinion 1989-113). Id. at 254-55. Thus, presumably the court would utilize the multi-factor test attributed to Associated Vendors, Inc. v. Oakland Meat Co., 210 Cal. App. 2d 825, 838-40 (1962) —a test that essentially seeks to determine whether it would constitute a fraud to adhere to the fiction of separate corporate entities. Id. at 838; see also Morrison Knudsen Corp. v. Hancock, Rothert & Bunshoft, LLP, 69 Cal. App. 4th 223, 249-50 (1998) (citing Oakland Meat Co.’s 14-factor alter ego test).

Two years after Brooklyn Navy Yard, another court of appeal addressed the same issue. In Morrison Knudsen, 69 Cal. App. 4th 223, the court expressly rejected the strict alter ego test applied in Brooklyn Navy Yard in favor of a more circumspect test, often referred to as the “unity of interests” test (a term also used in State Bar Opinion 1989-113). Id. at 262-264. Morrison Knudsen disagreed that many of the factors considered by courts in their alter ego analyses were irrelevant to the issue of conflict of interest. For example, the court noted that whether or not a subsidiary was undercapitalized had “little or no bearing on whether [the two companies] should be treated as one entity for purposes of attorney conflicts of interest.” Id. at 250-51.

In assessing the alleged conflict before it, the Morrison Knudsen court found that the following factors indicated that the two entities indeed should be treated as one for conflict purposes: (1) the parent entity controlled the legal affairs of the subsidiary; (2) the two companies had integrated management and personnel; (3) employees of the client entity could be called as witnesses in the other action; and (4) both entities were covered by the same insurance policy. Id. at 245-47. Yet, what perhaps had the most significance for the court was that the lawyer had obtained confidential information from the parent entity that was “substantially related to the present claim against the subsidiary.” Id. at 245. As the State Bar previously had opined, a lawyer may owe a duty of loyalty to a non-client (here, the parent) “if the attorney has received confidential information from the nonclient under circumstances which create a reasonable expectation that the attorney has a duty of fidelity to the nonclient.” State Bar Op. 1989-113 at p. 4. In Morrison Knudsen, all of these factors taken together compelled the court’s decision that, for conflict purposes, the parent and the subsidiary should be considered a single entity. Unlike Brooklyn Navy Yard’s alter ego test, Morrison Knudsen’s unity of interest test is widely cited as the standard in California.

A conclusion that the parent and the subsidiary are to be considered a single entity under the “unity of interests” test does not necessarily lead to the conclusion that the lawyer may not be adverse to the parent. Rather, once the lawyer determines that the parent and the subsidiary are a single entity for conflict purposes, the lawyer then defaults back to Rule 3-600 and must next determine whether she can be adverse to one of the entities. If, in that circumstance, the lawyer represents the subsidiary, for example, he may not be adverse to the parent company in any matter, whether or not related to her representation of the subsidiary. See Flatt, 9 Cal. 4th at 284. If, on the other hand, the lawyer no longer represents the subsidiary, she may be adverse to the parent as long as the matter is not substantially related to the previous matter in which the lawyer represented the subsidiary. See City and County of San Francisco v. Cobra Solutions, Inc., 38 Cal. 4th 839, 846 (2006) (noting duty of loyalty applies to simultaneous representations, while duty of confidentiality applies to successive representations). A “substantial relationship” between two matters generally is said to exist if the client is likely to have obtained confidential information from her client in the first matter that is material to the second matter. Rule 3-310(E); see also H.F. Ahmanson & Co. v. Salomon Bros., Inc., 229 Cal. App. 3d 1440, 1454 (1991) (“[T]he attorney’s possession of confidential information will be presumed only when a substantial relationship has been shown to exist between the former representation and the current representation, . . .” (internal quotation omitted); All Am. Semiconductor, Inc. v. Hynix Semiconductor, Inc., Nos. C 07-1200, C 07-1207, C 07-1212, C 06-2915, 2008 U.S. Dist. LEXIS 106619, at *16 (N.D. Cal. Dec. 18, 2008) (“In determining whether a substantial relationship exists a court should consider the similarities between the two factual situations, similarities in legal questions posed, and the nature and extent of the attorney’s involvement with the case and whether he was in a position to learn of the client’s policy or strategy.”).

As with most conflicts or potential conflicts, the lawyer usually can address and solve any problems by obtaining an informed written waiver from each client. Thus, when undertaking the representation of one entity in a family of entities, the lawyer should consider the similarities between the two factual situations, similarities in legal questions posed, and the nature and extent of the lawyer’s involvement with the case and whether he was in a position to learn of the client’s policy or strategy.

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[1] Throughout this article, all references to “Rules” are to the California Rules of Professional Conduct.

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Is there a law firm in-house attorney client privilege?

By WENDY WEN YUN CHANG

Consider the following hypothetical. Something happens in the course of an attorney's handling of a legal matter that might be argued to have been the result of the attorney's mistake, either rightly or wrongly. The attorney exchanges emails internally with intra-firm colleagues about how to address the issue and fix any negative result, something that is in both the client and the attorney's interest. Alternatively or additionally, the attorney may exchange emails internally with firm colleagues inquiring about what her ethical responsibilities might be in that situation. Believing her emails to be confidential, attorney freely discusses the dilemma. If a subsequent dispute develops between the law firm and the client over the firm's legal representation on that matter, are attorney's internal emails protected by an in-house attorney client privilege?

To answer the question, we start at the beginning. For purposes of the attorney-client privilege, a “client” is someone who consults a lawyer for the purpose of retention or advice, even if nothing results. Evidence Code §951[1] see also Cal. State Bar Form. Opinion No. 1984-84. The attorney-client privilege applies to communications in the course of professional employment that are intended to be confidential, and follows from the establishment of the professional relationship between client and attorney. Once the relationship is established, the attorney-client privilege attaches to communications made in confidence during the course of the relationship. Moeller v. Sanwa Bank (1997) 16 Cal. 4th 1124, 1130; see also Roberts v. City of Palmdale (1993) 5 Cal.4th 363, 371. “Confidential communication” means information transmitted between an attorney and client during the course of an attorney-client relationship, in confidence, without acts of waiver, and includes a legal opinion formed and the advice given by the lawyer in the course of that attorney-client relationship. Evidence Code, §952. Generally, a client, whether or not a party to a matter, has the right to refuse to disclose, and to prevent another from disclosing, a confidential communication between that client and attorney, if the privilege is claimed by a holder of the privilege. Evidence Code, §954. A client is a “holder of the privilege.” Evidence Code §953.

Classic attorney-client relationship

When our hypothetical attorney consults with her in-house colleagues for advice on how to handle a legal or ethical issue, she is confidentially consulting the attorney colleague for legal advice — technically, a classic attorney-client relationship, which should, under normal circumstances, give rise to an attorney-client privilege covering those communications. See U.S. v. Rowe, 96 F.3d 1294, (9th Cir. 1996). In Rowe, Rowe, a partner, assigned two firm associates to assist in an internal investigation of potential misconduct by a firm attorney. Upon grand jury subpoenaa to the two associates thereafter, seeking to compel their testimony regarding conversations with Mr. Rowe, Rowe and the firm asserted privilege. The trial court ordered the associates to testify. The Ninth Circuit reversed. Finding that the associates were acting as in-house counsel to the law firm, the Court noted that there was “virtual unanimity by American courts”that no distinction would be made between “inside” and “outside” counsel for the purposes of the application of the privilege. Id. at 1296. Communications between the associates and Mr. Rowe/the law firm were privileged, even if rendered in the course of fact finding relating to legal advice. Id. at 1296-97.

Conflicting case law when a client matter is involved

However, in our hypothetical, there is a nuance. Attorney is consulting internal law firm attorney colleagues about an existing client matter. Withholding these communications are, some argue, the withholding of communications relating to the firm’s representation of a client from the client. Is the in-house attorney client privilege nullified in this situation? Cases across the country have come down differently in the analysis.[2] California’s federal courts have weighed in on the issue three times, all originating from the Northern District of California, with no decision offering clear definitive guidance. No published California state court case has yet spoken.

California Rule of Professional Conduct Rule 3-310(3) states:
"A member shall not, without the informed written consent of each client:

(1) Accept representation of more than one client in a matter in which the interests of the clients potentially conflict; or

(2) Accept or continue representation of more than one client in a matter in which the interests of the clients actually conflict; or

(3) Represent a client in a matter and at the same time in a separate matter accept as a client a person or entity whose interest in the first matter is adverse to the client in the first matter.

A conflict of interest exists when a lawyer’s duty on behalf of one client obligates the lawyer to take action prejudicial to the interests of another client. Flatt v. Sup. Ct. (1994) 9 Cal.4th 275, 282, fn.2. Here, the argument is that when attorney seeks legal advice from her intra-firm colleagues, she is a firm client under Rowe, with that representation occurring while the attorney’s representation of the firm's outside client is ongoing. Arguably, this situation triggers questions relating to duty of undivided loyalty which an attorney owes to each of his clients. Truck Ins. Exchange v. Fireman's Fund Ins. Co. (1992) 6 Cal.App.4th 1050, 1056-f.

Thelen court discusses competing public policies

California's take on the existence of a law firm in-house attorney client privilege starts with Thelen Reid & Priest LLP v. Marland, (N.D. Cal. 2007) 2007 WL 578989, a 2007 case out of the Northern District of California. Thelen involved a dispute over entitlement to funds after a qui tam action. Among other discovery disputes, Marland, the firm's client, demanded that the firm produce communications with the firm's in-house counsel, who had advised the firm's handling attorneys. Thelen asserted attorney-client privilege and work product protection. While granting the motion to compel in part, the Thelen court discussed the conflicting policies at stake:

"The court recognizes that law firms should and do seek advice about their legal and ethical obligations in connection with representing a client. This court declines to follow such a strict rule, preferring one that is consistent with a law firm in-house ethical infrastructure. A rule requiring disclosure of all communications relating to a client would dissuade attorneys from referring ethical problems to other lawyers, thereby undermining conformity with ethical obligations. Such a rule would also make conformity costly by forcing the firm either to retain outside counsel or terminate an existing attorney-client relationship to ensure confidentiality of all communications relating to that client. This court declines to follow such a strict rule, preferring one that is consistent with a law firm in-house ethical infrastructure. Accordingly, Thelen is to produce some but not all communications in which a Thelen lawyer seeks or gives advice on the firm's ethical obligation to Marland." Id. at '8. The Court then articulated the following rule: "while consultation with an in-house ethics adviser is confidential, once the law firm is ordered to produce withheld documents except those reflecting in-house consultations on ethical and legal obligations to the client of that subset, Thelen was only required to produce "certain conclusions" of those consultations: 1) communications discussing claims client might have against firm, 2) communications discussing known errors in firm's representation of client, 3) communications discussing known conflicts in representation, or 4) communications reflecting "other circumstances" that triggered 'Thelen's duty to advise client and obtain client consent. Id. "Conflicts include any representation — whether of Thelen itself, CDDO, or another — adversely implicating or affecting the interests of [client], when Thelen was receiving information from and/or providing legal advice to its own lawyers while at the same time continuing to represent [client]." Id. This rule applied to both privilege and work product. Id.

SONICblue Inc. highlights risks of law firm self-representation

A year later, a bankruptcy court weighed in, applying the Thelenrule, but sparingly. In re SONICblue Inc. (Bartco N.D. Cal. 2008) 2008 WL 170562, the law firm had been general corporate, securities, and litigation counsel to SONICblue, and had given a legal opinion. SONICblue eventually filed bankruptcy, with the firm acting as debtor's counsel. Several litigations ensued. Allegations of undisclosed conflicts were asserted against the firm. The firm was disqualified as debtor's counsel. A trustee was appointed and directed by the court to investigate the apparent improprieties and to propose a remedy for the lack of disclosures. The trustee sought discovery from the firm, after he waived SONICblue's attorney client privilege. The firm asserted privilege for communications with its in-house counsel.

In analyzing the privilege issues, the court started with the observation that when a law firm chooses to represent itself, it runs the risk that the representation may create an impermissible conflict of interest with one or more of its current clients, even if one of those clients is the firm itself. In light of these ethical concerns, SONICblue noted that courts have considered the issue have "resoundingly found" that, where conflicting duties exist, the law firm's right to claim privilege "must give way to the interest in protecting current clients who may be harmed by the conflict." Id at '9. "As a result, a law firm cannot assert the attorney-client privilege against a concurrent outside client, when the communications that it seeks to protect arise out of self-representation that creates an impermissible conflicting relationship with the concurrent outside client." Id.

At the same time, the SONICblue court recognized that "public policy encourages lawyers to consult with in-house counsel to understand and comply with their professional responsibilities and ethical restraints." Agreeing with Thelen, the SONICblue court found public policy favored allowing the privilege to be asserted until such time as the firm has, or should have, determined that dual representation of itself and an outside client should not continue without the informed consent of the outside client. In doing so, the court rejected the firm's argument that since it was acting in its personal defense, the fiduciary exception to the privilege did not apply. Turning to applying the Thelen rule to the facts of the case, the court found that the firm had "some inkling of impending ethical issues" in 2005 when internal emails discussed the potential impact of a coverage dispute on the firm's perceived handling of the case. "Nevertheless, the present record does not establish the existence of conflict at that time." The court noted that in June 2006, "at least a potential conflict" existed when the client demanded a tolling agreement from the firm. But the court still found no conflict that would disable the in-firm privilege until Aug. 18, 2006, the date when the tolling agreement was actually executed, at which time the firm's ability to withhold intra-firm communications "became impaired." Id at '10 [4]

E-Pass articulates broader 'full-alignment' standard

The most recent case on the subject in California is the 2011 decision in E-Pass Technologies, Inc. v Moses & Singer, LLP(N.D. Cal. 2011) 2011 WL 3794889. In E-Pass, plaintiff sued their former counsel for malpractice. Plaintiff filed a motion to compel production of documents the firm withheld under the attorney-client privilege and work-product doctrine, described as "email communication with counsel." The E-Pass court framed the issue as "whether and to what extent these privileges apply to communications within a law firm regarding potential claims against the firm arising from its representation of an outside client." Applying Thelen, the court categorized the documents at issue into four categories: 1) communications during the attorney client relationship; 2) post-termination communications that were billed to plaintiff; 3) post-termination communications, unbilled to plaintiff; and 4) communications with third parties.

Pertinent to our discussion, the first category dealt primarily with the firm's representation of E-Pass in an attorneys' fees motion brought against both E-Pass and the firm. The court called the firm's argument "unprecedented" that it could engage in intra-firm communications relating to how to protect itself from liability on the fee motion, while representing E-Pass on that same motion, and
thereafter withhold those communications from plaintiff. “[Firm]’s interests were in conflict with those of E-Pass to the extent its interests were not fully aligned with E-Pass.” The court found if the firm intended to confidentially represent itself on the fee motion, it had a duty to get E-Pass’ informed written consent to the firm’s continuing representation of E-Pass. Because it did not do so, there was no privilege in this category of documents. Id. at *3. By articulating a standard of “full alignment” between the firm’s interest and the outside client’s interest to trigger an impaired privilege, the E-Pass court appears to have employed a broader standard than the “once law firm learns that a client may have a claim against the firm or firm needs client consent” trigger that was articulated in Thelen.

What we are left with is the conclusion that California law on the issue of the law firm in-house attorney-client privilege relating to an ongoing client matter is not definitive. California appears to honor the attorney-client privilege and work product when in-house counsel consults with outside counsel in these situations, but not where the inquiries occur in-house, at least not always. The language of the cases and their factual applications do give rise to some question of where the line between privilege and impairment is drawn. Until the law is clarified in this area, attorneys should proceed with caution.

Disclaimer: the information in this column is intended to be educational only, and does not constitute legal advice. Please cite check all authorities before using.

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[1] Unless otherwise noted, all statutory citations here shall be to California statutes.


[3] Unless otherwise noted, all rules references are to the California Rules of Professional Conduct.

[4] There appears to be no authority that disables the privilege as to a law firm’s communications with outside counsel, even if the firm is still representing its outside client. See e.g. SONICblue, supra., 2008 WL 170562 at *11.

[5] The other 3 categories do not implicate the discussion at issue in this article.

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Ethical and effective use of advance conflict waivers

By WENDY WEN YUN CHANG

Attorneys often ask whether they can insulate themselves from the ramifications of a conflict of interest by seeking a client’s advance waiver of such conflict.

A conflict of interest exists when a lawyer’s duty on behalf of one client obligates the lawyer to take action prejudicial to the interests of another client. Flat v. Sup. Ct. (1994) 9 Cal.4th 271, 282, fn.2. While the California Rules of Professional Conduct prohibit an attorney from accepting or continuing legal representation in a matter with a conflict of interest, the rules also generally permit the attorney to proceed, after written disclosure, with some forms of conflicts also requiring the client’s informed written consent.[1] California Rules of Professional Conduct (“CRPC”), Rule 3-310.[2] Written disclosure is a writing that informs the client or former client of the relevant circumstances and the actual and reasonably foreseeable adverse consequences of the conflict. CRPC Rule 3-310(A). Informed written consent means the client’s or former client’s written agreement to the representation following written disclosure.

Given the wording of the conflicts rules, it is not a surprise that there is no per se prohibition against advance conflict waivers. See Cal. State Bar Formal Opinion No. 1989-115; Los Angeles County Bar Association Formal Opinion 471. While most conflict waivers are a form of an advance waiver at some level, the “advance conflict waivers” discussed in this article seeks as its express purpose that the client waive a conflict that is not yet in existence. It requires some precognition of a future event that may or may not occur. When “informed written consent” is defined as written consent given after adequate disclosure of the potentially reasonably foreseeable adverse consequences, CRPC Rule 3-310(A), the inherent tension between prediction and “informed written consent” are obvious. What, then, is an ethical and enforceable advance conflict waiver? Case law demonstrates this to be an intensely fact-based determination.

An adequate waiver

In Zador Corp. N.V. v. Kwan, (1995) 31 Cal.App.4th 1285, the law firm had a long-standing relationship with the principals of Zador. Zador, along with its independent agent, Kwan, was sued in a real estate dispute. Zador indemnified Kwan, and asked law firm to jointly represent them. Law firm presented Kwan with an advance conflict waiver, which stated:

"...In the event of a dispute or conflict between you and the Co-defendants, there is a risk that we may be disqualified from representing all of you absent written consent from all of you at that time. We anticipate that if such a conflict or dispute were to arise, we would continue to represent you and the "Companies", whose legal interests in this matter are aligned, notwithstanding any adversity between you and the Companies' interests.... We are now asking that you consent to our continued and future representation of the Companies and agree not to assert any such conflict of interest or to seek to disqualify us from representing the Companies, notwithstanding any adversity that may develop. By signing and returning to us the agreement and consent set forth at the end of this letter, you will consent to such arrangement and waive any conflicts regarding that arrangement. Notwithstanding such waiver and consent, depending on the circumstances, there remains some degree of risk that we would be disqualified from representing any of you in the event of a dispute..."

Kwan signed the waiver, and litigation progressed under the joint representation. An actual conflict eventually developed, and on law firm’s advice, Kwan got separate counsel, and reaffirmed the prior agreement that law firm could remain on record for Zador. A dispute later ensued between Zador and Kwan. Zador, using law firm’s services, cross complained against Kwan, based on the same subject matter upon which law firm had jointly represented Zador and Kwan. Kwan moved to disqualify law firm. The trial court granted the motion, finding that the substantial relationship between the representations compelled the result. The Court of Appeal reversed. Finding that the question was governed by the issue of consent, Finding that the question was governed by the issue of consent, the representation following written disclosure.

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SAMPLE TEST QUESTIONS

Below are sample questions from this month's MCLE self-assessment test.

1. A conflict of interest exists when a lawyer’s duty on behalf of one client obligates the lawyer to take action prejudicial to the interests of another client.

[True] [False]

2. Lawyers may never accept an engagement in the face of a conflict of interest with a client.

[True] [False]

3. Written disclosure is a writing that informs the client or former client of the relevant circumstances and the actual and reasonably foreseeable adverse consequences of the conflict.

[True] [False]

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language in the waiver was broad enough to cover law firm’s representation of Zador in Zador’s cross complaint against Kwan. Therefore, disqualification should have been denied.

**Ethical wall plays a role**

In UMG Recordings Inc. v. MySpace (C.D. Cal. 2007) 526 F.Supp 2d 1046, the law firm previously represented UMG. At the time of the original UMG engagement, law firm recognized that it already represented other clients that were likely to have legal disputes with UMG, and so it obtained an advance conflict waiver. The law firm went on to successfully represent UMG in the prior litigation.

Thereafter, UMG filed an unrelated suit against MySpace. MySpace retained law firm to defend it in the litigation. Law firm created an ethical wall and filed an answer containing eighteen affirmative defenses, one of which was the misuse of copyright doctrine. Thereafter, law firm served discovery relating to that affirmative defense, which caused UMG to charge that law firm breached its duty to preserve UMG’s confidential information. UMG moved to disqualify the law firm.

The court found that law firm did transgress its duties to UMG, but denied the motion because it was able to fashion a remedy that achieved the purposes of the ethical rules: i.e., MySpace’s abandonment of the contentions and efforts that created the conflict, the absence of any actual disclosure of confidential information, and the court’s exercise of its inherent authority to preclude MySpace from pursuing such conflict-triggering matters.

The court noted that before accepting the prior representation, law firm had required that UMG agree to an advance conflict waiver as a condition of that engagement. The waiver ultimately reached agreed: (a) regardless of when law firm’s representation of UMG ended, law firm could undertake any representation, even one adverse to UMG, unless the new matter was substantially related to the specific issues and parties involved in law firm’s representation of UMG in the prior matter; (b) in particular law firm could represent an adverse party in litigation involving infringement of intellectual property rights; and (c) law firm would implement certain agreed upon steps if it created an ethical wall to implement the waiver. Finding that law firm had made clear from the beginning that it would not agree to represent UMG without the waiver, law firm did not deal “dubiously” with UMG. “To disqualify [law firm] now would lead to a harsh result, given the minor nature of the conflict and — most importantly — the fact that [law firm] has agreed to abandon the claims and efforts that gave rise to its conflict.” id. at 1065.

**Detailed disclosure protects waiver**

Similarly, in Visa U.S.A., Inc. v. First Data Corp., 241 F. Supp.2d 1100, 1105-1110 (N.D. Cal. 2003), the court denied motion to disqualify plaintiff’s litigation counsel, finding the firm’s advance conflict waiver specifically identified the potential adverse party and the nature of the potential conflict. While an advance conflict waiver need not state the exact nature of the future conflict, the disclosure needs to be sufficiently detailed, and the discussion of the potential future consequences sufficiently accurate, so that the clients’ consent to it is deemed fully informed. Id. An evaluation of whether full disclosure was made and the client made an informed waiver is a fact specific inquiry. Cal. State Bar Formal Opinion No 1989–115. Factors to determine if informed consent include the breadth of the waiver, the temporal scope of the waiver (whether it waived a current conflict or whether it was intended to waive all conflicts in the future), the quality of the conflicts discussion between the attorney and the client, the specificity of the waiver, the nature of the actual conflict (whether the attorney sought to represent both clients in the same dispute or in unrelated disputes), the sophistication of the client, and the interests of justice. Visa, supra. 241 F.Supp. 2d at 1106.

By contrast, where the disclosures in an advance waiver were inadequate, the client’s consent was not informed, and the waivers were not enforceable. Thus, in Concert LP v. Unleever PLC, 350 F. Supp. 2d 796 (N.D. Cal. 2004), the firm sent a proposed engagement letter containing an advanced waiver clause, which stated that the firm was a large firm, and that “it is possible that some of our present or future clients will have disputes or other dealings with you during the time that we represent you. Accordingly, as a condition of our undertaking of this matter for you, you agree that [firm] may continue to represent, or may undertake in the future to represent, existing or new clients in any matter, including litigation, that is not substantially related to our work for you, even if the interests of such clients in those other matters are directly adverse to you. Further, you agree in light of its general consent to such unrelated conflicting representations, [firm] will not be required to notify you of each such representation as it arises.” Id. At 801-802. The District Court, applying California law, disqualified the law firm, finding the advance waiver to be too general and insufficient, holding “even if a prospective waiver of conflict has been obtained, the attorney must request a second, more specific waiver, ‘if the [prospective] waiver letter insufficiently disclosed the nature of the conflict’” id. at 821.

**Enforceability relies on ‘adequacy and quality’**

These cases teach us, then, that enforceability of an advance conflict waiver depends on adequacy and quality of the disclosure in the first instance. Comment [22] to the American Bar Association’s Model Rules of Professional Conduct Rule 1.7 specifically states: “Efficiency of such waivers is generally determined by the extent to which the client reasonably understands the material risks that the waiver entails...”[3] Proposed comment [22] to California’s Proposed Rule of Professional Conduct Rule 1.7 mirrors the ABA:

A lawyer’s disclosure to a client must include: (i) a disclosure to the extent known of facts and reasonably foreseeable consequences; and (ii) an explanation that the lawyer is requesting the client to consent to a possible future conflict that would involve future facts and circumstances that to a degree cannot be known when the consent is requested. The lawyer also must disclose to the client whether the consent permits the lawyer to be adverse to the client on any matter in the future, whether the consent permits the lawyer to be adverse to the client in the current or in future litigation, and whether there will be any limits on the scope of the consent. Whether an advance consent complies with this Rule ordinarily also can depend on factors such as the following: (1) the comprehensiveness of the lawyer’s explanation of the types of future conflicts that might arise and of the actual and reasonably foreseeable adverse consequences to the client; (2) the client’s degree of experience as a user of the legal services, including experience with the type of legal services involved in the current representation; (3) whether the client has consented to the use of an adequate ethics screen and whether the screen was timely and effectively instituted and fully maintained; (4) whether before giving consent the client either was represented by an independent lawyer of the client’s choice, or was advised in writing by the lawyer to seek the advice of an independent lawyer of the client’s choice and was given a reasonable opportunity to seek that advice; (5) whether the consent is limited to future conflicts unrelated to the subject of the representation; and (6) the client’s ability to understand the nature and extent of the advance consent.

In conclusion, advance conflict waivers are not per se unethical. Whether they will be given legal effect depends on the quality and adequacy of the written disclosures given, whether the client reasonably understands the material risks that such waiver entails, and whether the client’s subsequent written consent was, in fact, informed.

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8/6/2014

[2] All references to Rules herein are to the California Rules of Professional Conduct, unless otherwise noted.

[3] CRPC Rule 1-100(A) (ethics opinions and rules and standards promulgated by other jurisdictions and bar associations may also be considered).

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How Limited Is Your Limited Scope Representation?

By Wendy Wen Yun Chang, partner, Hinshaw & Culbertson, LLP, and member, LACBA Professional Responsibility and Ethics Committee. She is the incoming vice chair of the State Bar of California’s Standing Committee on Professional Responsibility and Conduct. She can be reached at wchang@hinshawlaw.com. The opinions expressed are her own.

Whether for reasons of economy, necessity, strategy, or practicality, almost every attorney will, at some point, limit the scope of his or her representation of a particular client matter. In our current legal environment, due to increasing technical advances, practice and industry specialization, economic mandate, and/or client request, the demand or need to limit the scope of one's representation is becoming increasingly common and in some instances may be required. It can be a source of unwelcome surprise to the attorney in an after-the-fact dispute that the law may well find the scope of legal services to be determined by factors beyond what the attorney thought was the initial intention of the parties. It is distressingly easy for a misunderstanding to occur between an attorney and client about scope of services, sincerely or even conveniently intentional, especially after a problem has arisen. While the law is not new, in the current legal environment where it is becoming increasingly common, the law governing limited scope engagements bears review.¹

Except for those situations where an attorney is appointed by the court, the attorney-client relationship is created by some form of contract, express or implied, formal or informal.² An attorney's duties to the client depend on not only the existence of an attorney-client relationship but also the scope of the duties agreed to under contract.³ Thus, an attorney may place reasonable limitations on the scope of legal services by contract under certain conditions.⁴ Indeed, at times a limited scope of services may be required if the engagement requires legal services beyond the attorney's learning and skill.

In 1995 and again in 1999, the Los Angeles County Bar Association Professional Responsibility and Ethics Committee opined that an attorney could limit the scope of representation of a litigation client so long as the limited scope of the representation was fully explained and the client consents to it.⁵ This rule applies equally in a nonlitigation setting. The limitation on scope must also be made expressly clear.⁶ For example, if the intent is to handle the defense of litigation over a piece of property, the engagement letter should say just that and not something broader such as "all legal issues relating to Property."

An attorney also has a duty to alert the client to legal problems that are reasonably apparent even though they fall outside the scope of retention and to inform the client that the limitations on the representation create the possible need to obtain additional advice, including advice on issues collateral to the representation.⁷

In Nichols v. Keller, 15 Cal. App. 4th 1672 (1993), the client sued lawyers for failing to advise him that he had potential claims against third parties, claims that were not within the agreed scope of engagement. The attorneys argued that they had no duty to advise the client or pursue those claims. The court of appeal disagreed:

Generally speaking, a workers' compensation attorney should be able to limit the retention to the
compensation claim if the client is cautioned (1) there may be other remedies which the
attorney will not investigate, and (2) other counsel should be consulted on such matters.
However, even when a retention is expressly limited, the attorney may still have a duty to alert
the client to legal problems which are reasonably apparent, even though they fall outside the
scope of the retention. The rationale is that, as between the lay client and the attorney, the latter
is more qualified to recognize and analyze the client’s legal needs. The attorney need not
represent the client on such matters. Nevertheless, the attorney should inform the client of the
limitations of the attorney’s representation and of the possible need for other counsel. 8

Nichols was applied in Janik v. Rudy, Exelrod & Zieff, where the claimed limited “scope” of duty was
expressly defined in a court order certifying class claims. The court of appeal found that
notwithstanding the court order, the attorney owed the client a duty to at least consider and advise the
client if there were apparent related matters that the client was overlooking and that should be pursued
to avoid prejudicing the client’s interests. 9 Finding that the client could reasonably expect her attorney
to do so, such alert by the attorney would allow the client to consider whether to expand the scope or
pursue the claims in some other manner. 10 A failure to advise of such claims can constitute both a
breach of the standard of care and a breach of the duty of competence. 11

Finally, all general rules of professional responsibility continue to govern an attorney’s engagement
under limited scope. The attorney must be able to provide the legal services competently under the
limited scope, or he or she may not undertake it in such fashion. 12 The attorney must observe conflicts
and confidentiality restrictions, may not improperly withdraw from the engagement, and may not
make an agreement to prospectively limit the attorney’s professional liability. 13

There are good reasons that the full scope of a claim may not or cannot be pursued by a particular
attorney. However, such scope of limitation must be expressly stated, disclosed to, and consented to by
the client, including the express risks of such limitation.

1 Legal issues relating to state court rules surrounding limited scope engagements before a tribunal (see,
e.g., Cal. R. Ct. 3.35-3.37 (civil matters), and R. 5.70-5.71 (family law)) are not addressed herein.


4 Janik v. Rudy, Exelrod & Zieff, 119 Cal. App. 4th 930, 940 (2004); see also Ethics Primer on Limited
Scope Representation, Ethics Hotliner (Fall 2004), available at

5 Los Angeles County Bar Ass'n, Prof'l Responsibility & Ethics Comm., Formal Op. No. 483 (“There is
nothing per se unethical in an attorney limiting the professional engagement to the consulting,
counseling, and guiding self representing lay persons in litigation matters, provided that the client is
fully informed and expressly consents to the representation”); see also Los Angeles County Bar Ass'n,

6 Nichols, 15 Cal. App. 4th at 1687; Los Angeles County Bar Ass'n, Prof'l Responsibility & Ethics Comm.,

7 Id.

8 Nichols, 15 Cal. App. 4th at 1684.

9 Id. at 758.
10 Id. at 759.

11 Los Angeles County Bar Ass’n, Prof’l Responsibility & Ethics Comm., Formal Op. No. 502 (citing Cal. Rules of Prof’l Conduct R. 3-110(A)).

12 Cal. Rules of Prof’l Conduct R. 3-110(A). All rules references herein, unless otherwise noted, are to the California Rules of Professional Conduct. See also In the Matter of Valinoti (Review Dept. 2002) 4 Cal. State Bar Ct. Rptr. 498, 521 (“there is no ‘limited’ appearance of counsel in immigration proceedings”).

13 Los Angeles County Bar Ass’n, Prof’l Responsibility & Ethics Comm., Formal Op. No. 502 (citing, among other authorities, Cal. Rules of Prof’l Conduct R. 3-110, 3-300, 3-310, 3-400, and 3-700).
Recent Developments in Risk Management

Conflicts of Interest – Advance Waivers


**Risk Management Issue:** When are advance waivers of conflicts of interest valid and binding on clients, and what are the requirements that lawyers must meet in order for them to be enforceable?

**The Case:** By agreement dated March 7, 2008 an international law firm undertook to represent defendant client, a retailer, regarding certain “intellectual property litigation and trademark registration” in Asia. The agreement expressly informed the client about the possibility that the law firm’s present or future clients “may be direct competitors of [the client] or otherwise may have business interests that are contrary to [the client]’s interests,” and “may seek to engage [the law firm] in connection with an actual or potential transaction or pending or potential litigation or other dispute resolution proceeding in which such client’s interests are or potentially may become adverse to [the client]’s interests.” The agreement unambiguously explained that the law firm could not represent the client unless the client confirmed that this arrangement was amenable to it, thereby “waiv[ing] any conflict of interest that exists or might be asserted to exist and any other basis that might be asserted to preclude, challenge or otherwise disqualify [the law firm] in any representation of any other client with respect to any such matter.” The agreement also provided, [**2**] “However, please note that your instructing us or continuing to instruct us on this matter will constitute your full acceptance of the terms set out above and attached.”

Notwithstanding this agreement, the client sought to disqualify the law firm from representing a second retailer in this case. The trial court denied the motion to disqualify, and the New York Supreme Court, Appellate Division, First Department unanimously — and almost summarily — upheld the trial court’s decision, holding that it had “providently decided” the motion. The Appellate Division found that “[i]t is undisputed that [the law firm] continued to represent defendant with respect to [the client’s] Asian trademark portfolio” after the client accepted the terms set out in the engagement letter, “and, thus, defendant accepted the terms of the agreement, including waiver of the alleged conflict at issue.” Further, the court noted that “the interests of defendant that [the law firm] represents, namely intellectual property litigation and trademark registration exclusively in Asia, do not conflict with defendant’s interests at issue here . . .” In other words, the court implicitly concluded that the matters were unrelated, and that the law firm held no confidential information from its work on the Asian trademark portfolio that were of any relevance to this matter.

**Comment:** As we indicated in our discussion of the *Galderma* case in the May 2013 issue of the Lawyers’ Lawyer, whether and when law firms should be able to rely on advance waivers of conflicts of interest involves the resolution of competing paradigms of legal ethics. On the one hand, the rules governing conflicts of interest are premised on the fiduciary duties of loyalty and the protection of client confidences. On the other hand, the law governing lawyers recognizes the principles that clients should normally be free to select counsel of their choice, free from outside interference, and that client consent can, in appropriate circumstances, form a proper basis for overcoming prohibitions on conduct that would otherwise be impermissible.
Unlike the court in *Galderma*, the New York court summarily disposed of the motion to disqualify based upon the straightforward language of the advance waiver in the engagement letter. It appears from the transcript from the lower court decision that the letter containing the waiver was reviewed by a lawyer in the client’s in-house law department. Although the waiver wasn’t countersigned, the client proceeded to engage the firm, and the firm undertook the engagement on the basis of the letter. In that respect, therefore, this case goes further than *Galderma* in allowing a firm to rely on a waiver that it has supplied to the client and that has been reviewed by independent counsel and not rejected, even if it was not explicitly countersigned and agreed to. The case therefore represents another step along the way of recognition that sophisticated clients should be — and will be — held to understand, and be bound by, explicit advance waivers.

**Risk Management Solution:** Although this court did not go through the extended analysis that the Texas court did in *Galderma*, the steps recommended in our report about that case bear repeating as a useful checklist for law firms seeking to obtain enforceable advance waivers from sophisticated clients:

- **First,** as to existing or presently identifiable potential conflicts, in order for a waiver to have the greatest likelihood of being upheld, disclosure of both the specific facts and the potential adverse consequences should be made.

- **Second,** as to advance or blanket waivers of potential future conflicts, the disclosure should be as comprehensive and detailed as is possible, laying out the foreseeable types of adversity and the nature of the potential negative consequences for the client.

- **Third,** as to waivers of both existing and future conflicts, these should be obtained in circumstances that — as far as possible — preclude the client from later averring that the client did not understand the meaning or implications of the waiver. Waivers standing the greatest likelihood of being upheld are those where the client actually received independent legal advice with respect to the waiver — but a very significant element of the decision in this case is that in-house counsel for a corporation can serve that independent function.

Accordingly, the ideal signatory of a conflict waiver letter is a client’s independent counsel — whether in-house, or outside. At a minimum, lawyers should advise clients to obtain the advice of independent counsel before signing waivers of conflicts, and, preferably, clients should be required to do so before lawyers proceed based on the waiver. Generally, this is easier where an in-house counsel is available, but, when there is not, if the law firm believes that there is any likelihood that it will later need to rely on the waiver, the case is even stronger for requiring the affected client to have another lawyer review the waiver letter before signing it.

**In-Firm Privilege – Requirements for Creation of Attorney-Client Privilege for Communications With Law Firm General Counsel**


**Risk Management Issue:** What are the requirements for establishing attorney-client privilege for in-firm communications between law firm attorneys and a law firm’s in-house counsel in connection with matters relating to a client after wrong-doing is alleged?

**The RFP Family Partnership Case:** In April 2007, plaintiff client hired defendant law firm in connection with a commercial foreclosure matter. Nearly a year into the foreclosure, a notice of claim was sent to the law firm alleging legal malpractice. The participating attorneys consulted the law firm’s in-house counsel, a partner designated to respond to ethical questions and risk management issues. Following the consultation, the law firm sought to withdraw from representation. Meanwhile, the client requested that the law firm continue with the post-foreclosure sale of the property, and it did so.
In June 2012, upon completion of the sale, the client sued the law firm, alleging legal malpractice and other claims. The client sought to depose the law firm’s attorneys and to obtain the intra-firm consultations with in-house counsel. The client claimed that the communications were not protected from disclosure unless the law firm withdrew from representation as counsel before seeking the advice; or the firm fully disclosed to the client there was a conflict of interest and obtained the client’s informed consent to seek legal advice during the representation. The law firm moved for a protective order on the grounds that the communications were privileged.

The trial court granted the motion. On interlocutory appeal, the Supreme Judicial Court of Massachusetts affirmed, holding that confidential communications between law firm attorneys and a law firm’s in-house counsel can be protected by the attorney-client privilege from disclosure to a client who has asserted malpractice claims. For the defendant to invoke the privilege, the court held that four criteria must be met: (1) the law firm has designated in-house counsel; (2) the in-house counsel has not performed work on the matter that the suit is based upon or for a substantially related matter; (3) the client is not billed for the communications; (4) the consultations are kept confidential.

The court found that here, the law firm had met all four conditions. The court noted that the attorney-client privilege exists not only for the lawyer to give professional advice, but also for the attorney to receive information to enable giving sound advice. The court acknowledged that it is not always clear when the interests of the client and the firm have become adverse and at what point a withdrawal is required. The court stated that a broad protection would encourage firm members to seek risk management help promptly and allow for the correction of mistakes. The court emphasized that is in the best interests of both the client and the law firm to have ethical issues be examined by a competent advisor. Moreover, the court found that even though it was preserving the privileged nature of the communications, the client must still receive full and fair disclosure regarding the facts of the representation from attorneys.

Comment: The case is significant because the court declined to adopt or credit the “current client” exception to the application of the attorney-client privilege in this case that some earlier decisions from other courts had developed. The “current client” exception utilizes the rule of imputation (Rule 1.10) to assert that the lawyers in a law firm cannot represent both a client and itself when the firm and client have a conflict of interest, causing confidential intra-firm communications to lose their privilege on the theory that the firm’s fiduciary duty to its current client outweighed the right to claim the privilege. The court held that this would lead to a great deal of dysfunction and would preclude or chill efforts by lawyers to seek help when ethical conundrums arose.

As a result, the court declined to adopt this exception.

The St. Simmons Waterfront, LLC Case: In 2006, plaintiff client hired defendant law firm in connection with a condominium development project. The law firm was retained to draft purchase form contracts which would be utilized during the pre-selling of condominiums in a development project planned for construction. Citing defects in the purchase contracts, numerous purchasers rescinded their purchase contracts in late 2007 and early 2008. After a client conference call in February 2008 regarding the problems with the purchase contracts, the law firm’s participating attorneys contacted the firm’s in-house counsel seeking advice. Shortly thereafter, additional advice from outside counsel was sought.

In 2009, the client sued the law firm for malpractice. During discovery, the client sought to depose and obtain communications and documents from the firm’s in-house counsel, as well as outside counsel. The law firm objected and sought protective orders based upon attorney-client privilege and work product doctrine. The trial court granted the motion to compel, except to the firm’s communications with outside counsel. The appellate court vacated the trial court’s ruling and created a new framework to address the issue in conformity with the Rules of Professional Conduct. Thereafter, the Supreme Court of Georgia vacated the appellate court’s decision. In reaching its decision, the Supreme Court held that intra-firm communications should be treated like any other potentially privileged communications without resort to the Rules of Professional Conduct, which it determined were not relevant to the analysis. The Court then remanded the case to the trial court for a determination of whether the law firm could carry the burden of establishing the elements needed to establish the privilege.

Comment: In this case, too, the Supreme Court examined what circumstances might determine whether an attorney-client relationship exists between the in-house counsel and the attorney for purposes of establishing the privilege. The Court noted that such things as the formality associated with the position of “firm in-house counsel,” the maintenance of a separate file for the intra-firm communications, and the existence of billing procedures for matters addressed to the firm’s in-house counsel would figure into the calculus of whether the privilege could
be invoked. The Court specifically found that while the firm might have a conflict of interest in representing itself (through its general counsel) and its client when their interests diverged and a conflict developed, this fact, the rules of conflicts of interest derived from the Rules of Professional Responsibility and the so-called “fiduciary” exception do not apply, and do not abrogate either the attorney-client privilege or work product protection for documents prepared by the firm’s general counsel in responding to enquiries from firm lawyers in connection with matters involving current clients.

Editors’ Note: These two cases represent the second and third decisions of courts to uphold the attorney-client privilege for communications with law firm general, or in-house counsel and to explicitly reject the assertion of principles of conflicts of interest, or fiduciary duties to current clients as reasons to avoid the application of the privilege. (The only court to reach this conclusion previously was the U.S. District Court for the Southern District of Ohio, interpreting Ohio law, in Tattletale Alarm Systems, Inc. v. Calfee, Halter & Griswold, LLP (“Tattletale”), 2011 WL 382627. [This case was considered in the May 2011 issue of the Lawyers Lawyer Newsletter, Volume 16, Issue 2.] The three cases together are powerful precedents for other courts facing these issues, and, hopefully, put to rest the conflicts of interest and fiduciary “exceptions” to the privilege that had previously been adopted in some cases.

Risk Management Solution: These cases extend protections for intra-firm communications so long as certain elements are met to establish the applicability of the privilege. The elements for protection of those communications were described by both courts and should instruct firms regarding the best methods to protect their intra-firm risk management or ethical communications. The elements are:

1. The establishment of a formal position of “in-house” counsel by a lawyer within the firm;
2. For that lawyer’s position as “in house” to be realized in connection with the application of the privilege in any given case, he or she cannot have worked on the underlying matter (or related matter) for which risk management advice is sought;
3. Those matters should not be billed to any external source. This will commonly be accomplished by the use of “risk management” or equivalent “firm matter” billing codes for matters addressed by in-house counsel; and
4. The use of segregated filing for “in house” communications that are kept apart from the underlying matter from which the risk management issue has arisen. Those files should, of course, be kept confidential, especially from the client, so as to avoid a waiver.

Hopefully, by structuring the work of law firm general counsel in conformity with these principles, law firms will be empowered to gain the full benefits of having access to their general counsel on a confidential and privileged basis, whenever professional responsibility questions or issues arise that require guidance, even in connection with current client matters.

Inadvertedly Received Privileged Documents – Applicable Law and Rules When Documents Come From Third Party – Operation of Crime/Fraud Exception

State Bar of California Formal Opinion 2013-188

Risk Management Issue: When an attorney receives from a confidential written communication between opposing counsel and opposing counsel’s client from a non-party, what ethical obligations govern the conduct of the receiving attorney?

The Case: In California, the ethical duties of a lawyer who receives from opposing counsel an inadvertently produced document covered by the attorney client privilege has been long settled through extensive case law:
When a lawyer who receives materials that obviously appear to be subject to an attorney-client privilege or otherwise clearly appear to be confidential and privileged and where it is reasonably apparent that the materials were provided or made available through inadvertence, the lawyer receiving such materials should [1] refrain from examining the materials any more than is essential to ascertain if the materials are privileged, and [2] shall immediately notify the sender that he or she possesses material that appears to be privileged. The parties may then proceed to resolve the situation by agreement or may resort to the court for guidance with the benefit of protective orders and other judicial intervention as may be justified.

**State Compensation Insurance Fund v. WPS, Inc.,** 70 Cal. App. 4th 644, 656-657 (1999) (*State Fund*); **Rico v. Mitsubishi Motors Corp.,** 42 Cal. 4th 807, 817-818 (2007) (*Rico*). The *State Fund/Rico* rule is an objective one. In assessing whether a lawyer has complied with the standard, courts must consider “whether reasonably competent counsel, knowing the circumstances of the litigation, would have concluded the materials were privileged, how much review was reasonably necessary to draw that conclusion, and when counsel’s examination should have ended.”

The question of how the *State Fund/Rico* rule applies when a document is intentionally sent from a source other than the owner of the privilege, or owner’s counsel, without consent, was the subject of this State Bar of California Formal Opinion. In the opinion, the Bar’s Standing Committee on Professional Responsibility and Conduct analyzed a hypothetical where a defense attorney receives an unsolicited email from an anonymous sender, who is a former employee of the opposing party and who attaches a confidential communication between the attorney’s opposing counsel and opposing counsel’s client, which purports to establish that the opposing party has committed a fraud, assisted by opposing counsel. The committee concluded that this factual scenario does not change the application of the *State Fund/Rico* rule, and the ensuing ethical duties of the attorney who receives such communication.

Noting the core value nature of the attorney-client privilege in the American justice system, the committee analyzed the two prongs of the *State Fund/Rico* trigger: (1) whether the documents “obviously appear” or “otherwise clearly appear to be confidential and privileged”; and (2) whether it is “reasonably apparent that the materials were inadvertently disseminated.” On the first prong, Formal Opinion 2013-188 notes that the transmission of information between attorney and client is presumptively privileged, regardless of its content. On the hypothetical, the document is identified as a communication between employer and opposing counsel. Thus, it “obviously appears” or “otherwise clearly appears” to be privileged.

Turning to the second prong, the committee acknowledged that the document was not received from opposing counsel through inadvertence but rather was intentionally transmitted by an anonymous third party. Nevertheless, in light of the strong public policies underlying the *State Fund/Rico* rule to protect the attorney client privilege and work product doctrine, the committee concluded that the *State Fund/Rico* rule should be extended when it is “reasonably apparent that the materials were provided or made available through inadvertence” by the privilege holder’s counsel himself, or when a third party intentionally sends privileged materials to another attorney and it is reasonably apparent that those materials were sent without their owner’s authorization.

Finally, the committee analyzed the potential effect of the crime fraud exception to the attorney client privilege upon the receiving attorney’s ethical duties in this scenario, and concluded that there is no effect. Like any other crime-fraud exception scenario, the recipient attorney would have to establish for a court the *prima facie* elements of the crime-fraud exception through nonprivileged information. As such, the mere assertion that the attachment at issue might (or does) prove fraud is insufficient to abrogate the receiving attorney’s ethical duties to refrain from review of the communication under *State Fund* and *Rico*. The committee declined to opine whether or not the cover email from the ex-employee could be sufficient to prove those *prima facie* elements.

**Comment:** Given that inadvertent transmission of material is a frequent occurrence — among many reasons for which are such digital “traps” as “Reply All” and the autocomplete function in most email systems — we have frequently had occasion in the past to consider this subject. Our previous forays into the subject of inadvertent disclosure and related issues include: discussion of *In re Nitla, S.A. de C.V.*, *The Lawyers’ Lawyer Newsletter*, August 2003, Volume 8, Issue 4; *Maldonado v. State of New Jersey*, *The Lawyers’ Lawyer Newsletter*, April 2005, Volume 10, Issue 2; ABA Formal Opinion 05-437, February 2006, Volume 11, Issue 1; *Rico v. Mitsubishi Motors Corp.*, *The Lawyers’ Lawyer Newsletter*, February 2008, Volume 13, Issue 2 (Note: This is one of the key California cases with which the new Opinion is consistent); *White v. Withers LLP and Marcus Dearle*, *The

Inadvertently Received Privileged Documents, continued on back
In the California formal opinion considered here, which is consistent with extensive case law in the state, California evidently takes an extreme view of the duties of lawyers to others than their clients in protecting the privilege of adverse parties. Other states take different views. At the opposite extreme, Pennsylvania, in a very brief informal opinion, Pennsylvania Bar Ass’n Comm. on Legal Ethics and Professional Responsibility, Inquiry No. 2011-010 [Revised], May 18, 2011, notes that a lawyer’s first duty is to his or her client, and if an attorney receives a document that will assist his or her representation of the client, the lawyer’s duty is to use the document as needed for the benefit of the client and not to protect the person who mistakenly transmitted it, or the adverse party who would otherwise have a privilege claim. In many (perhaps most) state the position remains unclear, either under case law or ethics opinions — especially where, as in the particular circumstance examined in this Opinion, the source of the disclosure is a third party and not the adverse party or its representative. The position is further confused because, even as to materials inadvertently produced by adversaries, the position adopted by the American Bar Association (ABA) in its original ethics opinion on the subject (which required lawyers to stop reading, notify the adversary, and abide by the adversary’s instructions), has been modified by the much more limited rule contained in the most recent version of Model Rule 4.4, (discussed in ABA Formal Opinion 05-437, discussed in the Lawyers’ Lawyer Newsletter of February 2006, Volume 11, Issue 1) and adopted in many states, which merely requires notification of the adversary. The problem with this approach is that it leaves up in the air — and for courts to determine — whether and to what extent the receiving lawyer may still proceed to use the material thus received, or, conversely may be required to return the material to the adverse party and to refrain from using it.

**Risk Management Solution:** Because the governing rules and case law vary so greatly from jurisdiction to jurisdiction as to the proper handling of inadvertently produced material — whether received from the adversary or a third party — or of material deliberately produced by a third party who had no authority to provide the material, guidance for lawyers and law firms as to how to deal with these situations is problematic. Even where a given state’s rules are clear — like California — the applicable rule may not be the rule in place in the lawyer’s home state, as when the situation arises in a litigation before a tribunal in another jurisdiction whose own (different) rules may apply. Accordingly, the best general advice to lawyers is that, whenever they receive material that, for any reason, they believe may have been inadvertently transmitted, or transmitted by someone without authority, they should immediately consult their firm’s general counsel (if there is one) or seek outside professional responsibility advice if not, in order to avoid missteps. The consequences of failing to follow the correct rule may include disqualification, sanctions, loss of fees or fee disgorgement, and even potentially professional discipline. Practice leaders, and law firm general counsel should regularly educate their firms on the need to seek guidance whenever these situations arise.
The Case: Law firm sued a former client for attorney fees incurred during its representation of the former client in a probate matter from 2009 to 2010. Former client counterclaimed against the firm, arguing, among other things, that the firm breached its fiduciary duty to him by failing to disclose and intentionally concealing material information about Attorney A, one of the attorneys working on his case, who had a history of disciplinary proceedings, mental illness, alcoholism, and related arrests. The Colorado Court of Appeals, affirming the trial court, found that the firm had no legal or ethical duty to disclose information about Attorney A’s history of mental illness, alcoholism, and a stayed suspension to practice law absent evidence that any of these issues materially affected his performance as an attorney.

The Court emphasized several facts in reaching this decision. From the outset of the representation, the firm had informed former client that various lawyers would work on his case, and the former client had placed no limitations on how many or which lawyers at the firm could assist. The Court particularly noted that “the former client's retainer agreement with the firm specified that although a specific attorney would "have supervisory responsibility … [the firm would] draw upon the abilities of various members of [the] Firm as necessary or appropriate to handle [former client's] matters efficiently and effectively." Subsequently, the specific attorney sent an email to former client informing him that he was bringing Attorney A onto the case for added experience and assistance.

In addition, the firm, aware of Attorney A's circumstances, had established numerous procedures to monitor Attorney A's alcoholism and other medical issues, and to ensure that his work product did not suffer. Several medical professionals, including Attorney A's treating psychologist, had previously certified him fit to practice law. Most importantly, at no point during the representation was Attorney A "materially impaired." His performance reviews indicated that his work was "excellent," and his supervising attorney never reported any issues.

In these circumstances, the Court found that Attorney A's medical and arrest history was not material to any decision on former client's part to retain him, and thus the law placed no fiduciary duty on the firm to disclose the information. The Court likewise found no violation of either Rule 1.4 or Rule 7.1 of the Rules of Professional Conduct. According to the Court, Rule 1.4 was inapposite because it relates to disclosure of information necessary for a client to give informed consent, and there is no authority requiring a client's informed consent before a law firm can allow an additional attorney to work on a matter. In addition, by signing the retainer letter, former client specifically delegated the decision of who could work on his case to the firm. The Court found that Rule 7.1 was not applicable, because there was no attorney advertisement at issue, but even if it were, there was no violation because the Rule only prohibits material omissions, and the Court had already determined that information relating to Attorney A's background was not material.
Risk Management Solution: Critical to the outcome was the fact that the firm was aware of Attorney A's circumstances and actively monitored his work. The outcome might have been different had the firm permitted Attorney A to work for the client without closely managing that work. Had the Court found that the firm inadequately monitored Attorney A, the firm would have been faced with complex issues resulting from the need to balance its duties to the client with the various statutory protections surrounding employee privacy rights.

The case also enshrines two other important risk management principles. First, it underscores the importance of the need for a carefully constructed engagement letter. The Court specifically referenced the language of the law firm's letter in defeating former client's claim. As here, it is advisable that the engagement letter should include language identifying what attorneys may work on the file, and who will be responsible for staffing and supervising the team.

Second, this case serves as an example of the problem of unintended consequences, namely that lawyers who sue clients for fees often end up on the receiving end of a malpractice or breach of fiduciary duty counterclaim. As we have noted in the past, suing clients for fees is often a counterproductive exercise.

Conflicts of Interest — Representing Corporate Entities

Kentucky Bar Association v. Hines, 2013 WL 3122047

Risk Management Issue: What are the professional and ethical duties of an attorney representing a corporation when a conflict arises between the corporation and its constituents?

The Case: Attorney represented a corporation that was formed by about 100 heirs of a decedent's estate to manage the property — an estate with rich timber and coal holdings. The corporation took title to the property of the estate and facilitated the commercial operation of the assets. The corporation was formed with an eight-person board of directors. Attorney was hired by the corporation to represent it "in connection with any and all actions, claims, sales, leases, purchases whatsoever situated" regarding the land.

Attorney represented the corporation in a variety of contexts, including litigation to recover the proceeds of timber wrongfully harvested and coal wrongfully mined from the land. One of those actions was a claim against a coal company ("Coal Company").

A dispute arose between two factions of the heirs to the estate. One faction was led by Heir A, the president of the corporation. Attorney sided with the other faction after taking the position that Heir A was not eligible to serve as an officer since she was not a true "heir." Following that dispute, Heir A began the process of severing Attorney's engagement with the corporation.

In October 1999, Heir A sent Attorney a letter terminating his services in "marketing the assets of the corporation." The letter asked Attorney to continue working on the litigation against Coal Company. The letter specifically stated that Attorney should make no further deals on behalf of the corporation.

A meeting of the corporation's shareholders was subsequently held where directors and officers were elected. Attorney was present at the meeting and expressed concern that the election of the board and officers was invalid because of the lack of notice. At that time, the board of directors voted to appoint a new general manager of the corporation, ("General Manager"), a CPA.

In October 2000, General Manager sent Attorney a letter and explained he had assigned the responsibility to market the mineral and timber assets, and negotiate leases going forward to another attorney, noting that the president had previously terminated Attorney's employment with respect to those activities. He also asked Attorney to keep him informed about the Coal Company litigation. Attorney responded to this letter with a letter challenging the legality of the election of General Manager, and informing General Manager that he (Attorney) had a lien on all corporate income.
Attorney continued to hold himself out as counsel for the corporation. In October 2001, he wrote a letter to a company, with whom he had previously negotiated a lease for the corporation, stating that he was the only legally recognized representative of the corporation and that he was the contact on the matter. In September 2001, a member of the minority faction, through Attorney, filed a criminal complaint against Heir A and a petition for declaration of rights on behalf of the corporation. The action was eventually converted to a shareholder derivative suit on behalf of the minority shareholders.

In 2005, Heir A filed a bar complaint against Attorney, which resulted in two formal charges by the Inquiry Commission under, among other rules, Rules 1.13(a) of Kentucky's Rules of Professional Conduct. With respect to Rule 1.13(a) the commissioner held that when a corporation is the client, as opposed to individual constituencies of the organization, the lawyer owes the duties to the organization, and that while the lawyer is obliged at times to take certain reasonable measures in the interests of the organization, the steps Attorney took (such as filing the suit on behalf of the minority) were not reasonable. The commissioner found that Attorney's behavior amounted to representation of certain heirs, not the corporation, and that such representation was improper given his employment by the corporation.

The commissioner also found that Attorney made a deliberate choice to side with the faction that opposed the president and that his "loyalty and efforts shifted from the corporate entity" to the anti-president faction. Despite this shift, Attorney did not explain to the corporation "the identity of his new, actual clients" thus violating Rule 1.13(d). Based on these findings of misconduct, the commissioner recommended a 120-day suspension from the practice of law. Attorney sought review of the recommendation.

Attorney argued that he acted properly if his behavior was viewed within the overall context of what was happening with the corporation. He noted that some board members and shareholders were frustrated with what was happening with the corporation and that the board and officer elections deviated from past practice. He argued that there were legitimate questions about who was lawfully authorized to act on behalf of the company, and that his decision-making was difficult because of the volatile situation.

The Kentucky Supreme Court declined to accept these arguments. The court noted that since he was engaged as a lawyer for the corporation, when a derivative action is brought by minority shareholders alleging that the officers and directors are acting wrongly, then there is an inherent conflict in that lawyer representing the plaintiffs. Attorney, by helping the minority faction, violated his duty of loyalty to his corporate client.

Based upon the violation of RPC 1.13(a), the Court upheld Attorney's suspension.

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**Risk Management Solution:** When a dispute arises among the constituents of a corporation, an attorney for the corporation may not take sides, notwithstanding the relationships that he or she may have with the individuals involved. A conflict of interest will almost certainly arise out of any action that a corporate lawyer takes for any particular constituent when a dispute does occur. Once such a dispute does arise, and provided the lawyer does not take sides, the corporation's lawyer may remain in his or her role, if so authorized by the corporation's highest authority. Such disputes come with significant risk of potential claims against the lawyers involved, so that careful documentation of the lawyer's role and responsibilities at every stage is likely to be critical in avoiding liability to the entity or to individual constituencies.

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**E-Mail Communications Between Clients and a Departing Attorney**


**Risk Management Issue:** What are a law firm's ethical duties in handling the email account of a departing attorney?

**The Opinion:** In this Opinion, the Philadelphia Bar Association Professional Guidance Committee considered inquiries from a law firm's managing partner regarding the law firm's management of a departing attorney's email account. Upon the departure, the law firm had programmed the departing attorney's account to send a reply to senders advising that the departing attorney was no longer with the firm. The law firm also opened and read the emails, and forwarded any email to the departing attorney relating to a matter that he retained. The law firm took
the position that any email coming into the firm was "presumptively firm email" and must be reviewed. The departing attorney, however, requested that the firm program his former email account to merely "bounce back" unread emails to senders with an indication that the account had been closed so that no email messages addressed to the attorney would be received — or read — by the firm.

The managing partner inquired as whether the law firm's handling of the departing attorney's email account complied with the ethical rules, or whether the firm must honor the attorney's request that the firm avoid receiving those emails. Noting that the Pennsylvania Rules of Professional Conduct, the rules of other jurisdictions, and the Model Rules of Professional Conduct failed to expressly address the issue, the Committee turned for guidance to a prior Opinion jointly issued by the Committee and the Pennsylvania Bar Association Committee on Legal Ethics and Professional Responsibility addressing ethical obligations in a lawyer's changing of firms. Citing that opinion, the Committee highlighted the duty of lawyers to protect the interests of clients during periods of transition, and explained that "both the departing lawyer and the old law firm owe an obligation to ensure that the interests of the clients in active matters are competently, diligently and loyally represented" in accordance with the Rules. The Committee explained that, in these situations, the old law firm is required to keep clients informed of the impending departure of a responsible attorney, to make clear to an inquiring client that the client may choose to be represented by the departing attorney, to assure that active matters continue to be managed by remaining lawyers, and to assure that the firm will take reasonable steps to protect the client's interests.

Based on these principles, the Committee reasoned that the law firm's practice of opening and reviewing the departing attorney's emails was permissible to the extent necessary to carry out its duties as described above. The Committee also reasoned that simply "bouncing back" the emails to the senders would not fulfill the law firm's duties to ensure that the client's best interests were protected.

A review of the emails is, however, insufficient for the firm to meet its ethical obligations. The Committee advised the law firm that it should include the departing attorney's current contact information in its reply messages informing email senders that the departing attorney is no longer with the firm, and that it must immediately provide to inquiring and former clients sufficient information for the client to make contact with the departing attorney prior to informing email senders that the departing attorney is no longer with the firm, and that it must immediately provide to inquiring and former clients sufficient information for the client to make contact with the departing attorney prior to the law firm offering of its services as an alternative. The Committee also cautioned the law firm against the failure to forward any email received that was meant for the departing attorney.

**Risk Management Solution:** Law firms need to have a policy for handling departing attorneys' email accounts. Since most clients rely on email as the primary method of contacting their attorneys, it is imperative that both the law firm and its attorneys have an understanding of how the law firm will handle post-departure email communications should an attorney leave the firm. As noted by the Committee, while the firm may review emails addressed to a departing attorney in order to make sure that the client's interests are protected, the handling of those emails must also comport with the ethical rules that give clients the choice as to who will represent them going forward when a lawyer leaves the firm.

Arguably, the Opinion requires modification in one respect, namely that once a client has indicated its desire that the departing lawyer and his or her new firm should take over the representation, from that moment forward the law firm should have no interest in the contents of emails from or relating to that client, and indeed would be violating the client's attorney-client privilege with their "new" lawyer in continuing to review the contents of emails sent to the departing lawyer's account. Until that point is reached, however, the Opinion correctly gives the firm the obligation as well as the right to review emails sent to the departing lawyer's account.
Conflicts of Interest – Advance Waivers – Sufficiency of Disclosure – Who Is a “Sophisticated Client”

Galderma Laboratories, L.P. v. Actavis Mid Atlantic LLC (N.D. Tex. Feb. 21, 2013)

Risk Management Issue: When are advance waivers of conflicts of interest valid and binding on clients, and what are the requirements that lawyers must meet in order for them to be enforceable?

The Case: Before Judge Ed Kinkeade of the U.S. District Court for the Northern District of Texas was the motion of plaintiff client to disqualify the law firm from representing the defendants in the underlying litigation. Important to the decision is Judge Kinkeade’s description of the client:

[It] is a worldwide leader in the research, development, and manufacturing of branded dermatological products… headquartered in [Texas]. [The client] and its affiliates have operations around the world, employing thousands of people and reporting worldwide sales of 1.4 billion euros for the year 2011 alone. As a complex, global company, [the client] routinely encounters legal issues and the legal system. [The client] has its own legal department to address these issues. The legal department is headed by its Vice President and General Counsel . . . [The Vice President and General Counsel] is a lawyer who has practiced law for over 20 years and has been general counsel for [the client] for over 10 of those years. In addition to an in-house legal department, [the client], through [the Vice President and General Counsel], frequently engages outside counsel to assist with a wide range of issues. Over the past 10 years, [the client] has been represented by large law firms including [the law firm and two other law firms]. [The client] also engages smaller law firms as needed.

In 2003, when the client became a client of the law firm, the law firm sent the client an engagement letter, which included a broad waiver of future conflicts of interest:

We understand and agree that this is not an exclusive agreement, and you are free to retain any other counsel of your choosing. We recognize that we shall be disqualified from representing any other client with interest materially and directly adverse to yours (i) in any matter which is substantially related to our representation of you and (ii) with respect to any matter where there is a reasonable probability that confidential information you furnished to us could be used to your disadvantage. You understand and agree that, with those exceptions, we are free to represent other clients, including clients whose interests may conflict with ours [sic] in litigation, business transactions, or other legal matters. You agree that our representing you in this matter will not prevent or disqualify us from representing clients adverse to you in other matters and that you consent in advance to our undertaking such adverse representations.

Conflicts of Interest, continued on page 2
The Vice President and General Counsel signed that he understood and, on behalf of the client, agreed to the terms and conditions of engaging the law firm, including the waiver of future conflicts of interest.

Between 2003 and 2012, the law firm provided employment and benefits advice to the client. In 2012 the client, represented by other law firms, initiated intellectual property litigation against a second company. The second company, already a client of the law firm, engaged the law firm to represent it in the litigation. When the client received a copy of the second company’s answer and counterclaims, and became aware that the law firm was representing the second company, the client asked the law firm to withdraw from representing the second company. Instead, the law firm chose to terminate its attorney-client relationship with the client and informed the client that it would not withdraw from representing the second company, because the client had consented to the law firm representing adverse parties in litigation when it signed the waiver of future conflicts in the 2003 engagement letter. The client moved to disqualify.

Judge Kinkeade summarized the issue to be resolved, and the parties’ arguments, as follows: “whether or not [the client], a sophisticated client, represented by in-house counsel gave informed consent when it agreed to a general, open-ended waiver of future conflicts of interest in [the law firm’s] 2003 engagement letter.”

On the one hand, the client argued that its consent was not “informed consent” when its in-house lawyer signed the agreement on its behalf, because the law firm did not advise the client of any specifics with regards to what future conflicts the client might be waiving. On the other hand, the law firm argued that because the client was a highly sophisticated client, a regular user of legal services, and was represented by its own counsel, the waiver language was reasonably adequate to advise the client of the material risks of waiving future conflicts, despite being general and open-ended.

Judge Kinkeade’s decision includes extensive consideration of both the Texas and the Model Rules of Professional Conduct, as well as applicable Fifth Circuit case law. In addition, Judge Kinkeade compared the sufficiency of the law firm’s waiver with the similar waiver considered in Celgene Corp., 2008 WL 2937415, at *8 (July 29, 2008 D.N.J.) (Celgene). [Editors’ Note: the Celgene case was the subject of a Note in the November 2008 The Lawyers’ Lawyer Newsletter.] In particular, Judge Kinkeade noted that “[i]n holding that the waiver language was not reasonably adequate, the Celgene court reasoned that the attorneys seeking the waiver of future conflicts needed to further identify risks to Celgene, such as particularizing generic pharmaceutical companies as a potentially conflicted client and identifying patent disputes as a potential matter where the attorneys may represent a client with conflicting interests. . . . The [Celgene] court also reasoned that the attorneys needed to further explain alternatives such as defining substantially related matters or considering broader limitations such as refraining from representing all general drug companies.” But he concluded that “[t]his type of language is not always necessary for a client to give informed consent,” and that “[i]f such language was always required, general and open-ended consent would never be valid.”

Accordingly, Judge Kinkeade found that “the waiver in the 2003 engagement letter is reasonably adequate to allow clients in some circumstances to understand the material risk of waiving future conflicts of interest. The language disclosed a course of conduct for determining when [the law firm] will be disqualified, explains the material risk that [the law firm] may be directly adverse to the client, and explains an alternative, that the client need not hire [the law firm] if it does not wish to consent.”

The court then examined whether or not the disclosure provided by the law firm was reasonably adequate to allow the client to understand the material risks of waiving future conflicts, in the light of its degree of sophistication, and also whether the client was independently represented in making the waiver. Distinguishing Celgene as based on different standards in place in the Third Circuit and New Jersey, Judge Kinkeade, applying the language of the relevant ABA Model Rules, held that in the Fifth Circuit:

“the test for informed consent is whether the client understands the material risks involved in waiving the future conflict . . . Additional consultation outside of the waiver is not a requirement to obtain informed consent. A lawyer need not inform the client through additional consultation of
facts or implications already known to the client. Accordingly, under the national standard, as opposed to the New Jersey standard, additional consultation is not required for a client to give informed consent when, without it, the client is aware of sufficient information reasonably adequate to make an informed decision.”

Similarly, with respect to the client’s sophistication, Judge Kinkeade held that:

“[w]hen a client has their own lawyer who reviews the waiver, the client does not need the same type of explanation from the lawyer seeking a waiver because the client’s own lawyer can review what the language of the waiver plainly says and advise the client accordingly. The court cannot agree with the Celgene court because to do so would ignore the knowledge and advantage that clients gain by employing their own counsel to advise them, and the national ethical standards clearly compel the court to consider a client’s use of independent counsel.”

Accordingly, Judge Kinkeade’s holding in this case was “that [the client] gave informed consent to [the law firm’s] representation of clients directly adverse to [the client] in substantially unrelated litigation. Because [the law firm’s] representation of [the second company] falls within the scope of that informed consent, [the law firm] is not disqualified from representing [the second company].”

Comment: Whether and when law firms should be able to rely on advance waivers of conflicts of interest involves the resolution of competing paradigms of legal ethics. On the one hand, the rules governing conflicts of interest are premised on the fiduciary duties of loyalty and the protection of client confidences. On the other, the law governing lawyers recognizes the principles that clients should normally be free to select counsel of their choice, free from outside interference, and that client consent can, in appropriate circumstances, form a proper basis for overcoming prohibitions on conduct that would otherwise be impermissible.

This decision vindicates our comment regarding the opposite conclusion reached in Celgene that, based on ethics opinions and case law, if the similar facts had been presented in a jurisdiction other than the Third Circuit and New Jersey, the law firm may well have survived a motion to disqualify it, as did the law firm here. More importantly, the case sets out with great clarity the elements that firms will need to establish if they are going to be successful in relying on broad advance waivers of conflicts involving direct adversity to current clients.

**Risk Management Solution:** Whether or not the same advance waiver would have been enforced against a similarly sophisticated client in other jurisdictions, some useful lessons can be drawn from this decision, and the contrast between this case and Celgene.

- As to existing or presently identifiable potential conflicts, in order for a waiver to have the greatest likelihood of being upheld, disclosure of both the specific facts and the potential adverse consequences should be made.

- As to advance or blanket waivers of potential future conflicts, the disclosure should be as comprehensive and detailed as is possible, laying out the foreseeable types of adversity and the nature of the potential negative consequences for the client.

- As to waivers of both existing and future conflicts, these should be obtained in circumstances that — as far as possible — preclude the client from later averring that the client did not understand the meaning or implications of the waiver. Waivers standing the greatest likelihood of being upheld are those where the client actually received independent legal advice with respect to the waiver — but a very significant element of the decision in this case is that in-house counsel for a corporation can serve that independent function.

Accordingly, the ideal signatory of a conflict waiver letter is a client’s independent counsel — whether in-house, or outside. At a minimum, lawyers should advise clients to obtain the advice of independent
counsel before signing waivers of conflicts, and, preferably, clients should be required to do so before lawyers proceed based on the waiver. Generally, this is easier where an in-house counsel is available. But when there is not, if the law firm believes that there is any likelihood that it will later need to rely on the waiver, the case is even stronger for requiring the affected client to have another lawyer review the waiver letter before signing it.

Legal Fees – Suing for Fees – Engagement Letters – Account Stated


Risk Management Issues: Are engagement letters enforceable if not countersigned by the client? Is a client’s failure to make a timely objection to a lawyer’s bill a sound basis for suing the client for fees?

The Case: In July 2006, plaintiff client hired defendant law firm to perform the legal work in connection with the acquisition of numerous coal companies. The law firm provided an engagement letter containing the terms of their agreement, including: (1) the specific scope of the legal services; (2) a list of billing rates for the law firm’s attorneys, law clerks and paralegals; (3) expenses that may be incurred, to be reimbursed by the client; (4) an explanation of the firm’s billing practices, such as sending a monthly invoice containing the fees and expenses incurred during the previous month, and the firm’s right to impose interest on balances outstanding for more than 30 days; (5) an explanation that the client was free to terminate the attorney-client relationship at any time, and that the law firm would withdraw in compliance with applicable law; and (6) an agreement to waive certain conflicts of interest. The client verbally acknowledged and agreed to these terms. From July 2006 through June 2011, the law firm performed legal services in accordance with the terms of the engagement letter. It regularly sent the client invoices, and, after receiving each invoice, the client never raised an objection, nor requested a reduction of the billed amount. The client periodically paid the invoices, though not in full.

From March 2008 through December 31, 2009, the client repeatedly assured the law firm that it would pay the outstanding balance on its invoices. According to its executives, the client was in the process of obtaining financing for acquisitions of other coal companies, or refinancing its then-existing debt obligations. Afterwards, it would have enough money to pay the outstanding fees and expenses. Based on those representations, the law firm continued to perform legal services on the client’s behalf. As of June 2011, the law firm was owed $2,455,478.86. The client declined to pay, and the law firm sued. The complaint contained two causes of action — for breach of contract, and for an account stated.

The client answered, alleging that the firm had engaged in misconduct in that the firm had conflicts of interest relating to various business transactions between partners of the firm and the client, none of which had been properly disclosed or waived, and that the firm had engaged in “questionable billing practices,” such as billing for 14-hour-plus days and billing entries that were repeated word for word. The client asserted three counterclaims based on the same allegations.

In granting the firm’s motion for summary judgement on its claims, and dismissing the client’s counterclaims, the court found that at no time did the client object to the invoices it had received over the course of the five years of representation. The court held that “[b]ecause of the failure to object, the challenges to the reasonableness of the charges fail.” Nevertheless, the court noted that “even if the court were to review the quality of the invoices, they appear to be adequate, at least in the context of the client’s failure to contemporaneously object – they identify the attorneys to perform the services, the date of the service, a description of the work performed, the hours billed,
and the fee assessed for each block of time charged.” Similarly, the court held that “[a]s for the conflict of interest defense, the valid accounts stated bars [the client’s] breach of contract counterclaim.” In addition, the court held that the firm was entitled to judgement on its breach of contract claim, specifically finding that the failure to obtain the client’s countersignature to the engagement letter would not constitute a violation of New York’s requirement for a written engagement letter, and that even if that requirement had not been met “that, by itself would not preclude [the firm] from seeking recovery of legal fees under such theories as services rendered, quantum meruit and account stated.” Finally, in dismissing the counterclaims, the court held that it was fatal to those claims that the client neither alleged nor proved that it had been damaged in any way by the alleged conflicts of interest.

Risk Management Solution: This case is the exception that proves the rule: “never sue a client for fees.” The case demonstrates the critical importance of using well-crafted engagement letters for all — even very sophisticated — clients. In addition, the case reinforces the importance of the account stated cause of action in states whose substantive law permits them. In this case, the court noted the length of time, the number of bills and the partial payments in determining that the client had had an opportunity to object and had failed to do so. Law firms can assist in creating support for the “failure-to-object” element of account stated claims by accompanying each bill with a cover letter requesting that the client notify the firm promptly if it has any questions or concerns with respect to the bill. In addition, in any matter where the outcome of the engagement involves anything less than the complete attainment of the client’s objectives, it is vitally important, before commencing litigation to collect the fee, to review the file to determine the likelihood of success of any counterclaim for malpractice that may be asserted. Finally, the recent and highly publicized case of another law firm suing for unpaid fees demonstrates that there is an additional and equally critical step that firms should take before commencing fee suits, namely thoroughly reviewing the file (including the email file) relating to the engagement, as well as all of the bills and the underlying time records.

Regulation of Advertising – Meaning of Confidential Information – “Blogging” About Client Matters – Need for Client Consent


Risk Management Issue: May a lawyer write a blog post discussing public information relating to a client without the client’s consent? If a lawyer blogs about cases he won, is this regulated attorney advertising requiring a disclaimer?

Case: A Virginia attorney created and posted in a trademarked blog, which was accessible from his law firm’s website. The blog, which was not interactive, contained posts discussing legal issues and cases, but the overwhelming majority were posts about cases in which the lawyer obtained favorable results for his clients. The posts contained his clients’ names and publicly available information about their cases. He did not ask for his clients’ consent before blogging about their matters, nor did he include a disclaimer anywhere on the blog that his posts constituted attorney advertising or that prior victories do not guarantee future results.

Based on the attorney’s blog posts, the Virginia State Bar charged the lawyer with violating several Rules of Professional Conduct relating to attorney advertising as well as Rule 1.6, which prohibits revealing client confidential information. After a hearing, the Bar found that the lawyer violated Rule 1.6 by “disseminating client confidences” obtained in the course of representation without consent to post. Specifically, the Bar found that the information in the attorney’s blog posts “would be embarrassing or be likely to be detrimental” to clients. The Bar further held that the lawyer violated Rule 7.1 by failing to state on the blog that it contained legal advertising, and also Rule 7.2 by “disseminating case results in advertising without the required disclaimer [that past case results
do not guarantee or predict a similar result].” The Bar imposed a public admonition with terms including a requirement that the lawyer remove case-specific content for which he has not received consent and post a disclaimer that complies with Rule 7.2 on all case-related posts.

The lawyer appealed to a three-judge panel of the circuit court and the court heard argument. The court ruled that the Bar’s interpretation of Rule 1.6 violated the First Amendment and dismissed that charge, but upheld the Bar’s findings with respect to Rules 7.1 and 7.2.

The Virginia Supreme Court affirmed. With respect to Rule 1.6, the Court found that the state may not prohibit an attorney from discussing public information about a client or former client, even if that information is embarrassing or likely to be detrimental to the client. The Court emphasized that all of the lawyer’s blog posts involved cases that had been concluded, and therefore his posts could not prejudice a pending case. The Court also made the broad assertion, “State action that punishes the publication of truthful information can rarely survive constitutional scrutiny.”

Regarding the advertising rules, the Court first determined that the lawyer’s blog posts were commercial speech, specifically lawyer advertising. The attorney argued that his posts were political speech and thus entitled to a higher degree of constitutional scrutiny, but the Court disagreed, noting that the blog posts were predominately about cases where the lawyer received a favorable result for his client, were located on his law firm’s commercial website rather than on an independent site, and did not allow for discourse about the cases by allowing readers to post comments. Thus, the Court reached its conclusion even though, “[The attorney] chose to commingle sporadic political statements within his self-promoting blog posts in an attempt to camouflage the true commercial nature of his blog.” Although the Court disagreed with the Bar’s argument that the posts were inherently misleading, it did find that they had the potential to be misleading. Because the Bar has a substantial governmental interest in protecting the public from potentially misleading attorney advertising, and that the regulations are no more restrictive than necessary, the Court determined that Rules 7.1 and 7.2 do not violate the First Amendment, and the lawyer was required to include a disclaimer on his blog posts that complies with Rule 7.2.

Comment: The Virginia Supreme Court’s striking down as unconstitutional that part of Rule 1.6 prohibiting attorneys from disclosing public information about clients may have potentially far-reaching consequences. Many states have previously disciplined attorneys under Rule 1.6 for failing to secure consent of their clients before revealing potentially embarrassing public information about clients. It bears watching to see if this case starts a trend, or whether it is seen as an outlier.

Risk Management Solution: Lawyers’ and law firms’ free speech rights are subject to constitutionally permissible regulation of commercial speech by professional regulators. States’ appetites for enforcing advertising rules vary widely. As a result, it continues to be important for law firms to take care to monitor all publicly accessible postings involving the firm, its lawyers and their clients.
Personal Interest Conflicts—Investment in Clients or Their Transactions—Malpractice Insurance Coverage—Policy Exclusions


Risk Management Issue: What are the special risks when lawyers invest in their clients, or their clients’ transactions?

The Case: Plaintiff client sued its law firm for legal malpractice. Two attorneys at the firm owned a 27 percent share in the client through a real estate company. An insurance company issued the law firm a professional liability insurance policy that specifically excluded coverage for any claim based upon or arising out of, in whole or in part, the alleged acts and omissions by any insured for a business enterprise in which any insured had a "controlling interest." The insurer brought an action for a declaratory judgment that because of this exclusion, the law firm and the individual members were not entitled to coverage in connection with responding to the client’s malpractice action. The law firm interposed counterclaims against the insurer and made a variety of motions seeking to prevent the granting of the requested declaratory relief. In considering those motions, and the insurer’s own motion for partial summary judgment for the requested relief, and after rejecting the law firm’s various positions not directly focused on the merits of matter, the court considered the core question as to whether the exclusion was effective to avoid coverage, as asserted by the insurer, or was too vague to be enforceable, as asserted by the law firm.

After considering the policy language from two perspectives—the language of the exclusion itself, and the entire policy (in order to develop “a true understanding of what risks are assumed by the insurer and what risks are excluded”)—the court held that the exclusion was not ambiguous in any respect and was valid and effective. Accordingly, the court granted summary judgment to the insurer. In reaching that result, the court found that “the Policy is intended to exclude from coverage any claim resulting from acts on or behalf of a business enterprise in which any insured has a controlling interest. Insurers have many credible reasons not to assume the kind of risk excluded here. First, insurers need ‘to prevent collusive suits whereby malpractice coverage could be used to shift a lawyer’s business loss onto the malpractice carrier[,]’ [citation omitted]. Second, the exclusion seeks to avoid circumstances where an insured intermingles its business relationships with its law practice such that an insurance carrier incurs additional risk of having to cover the insured for legal malpractice claims relating to the conduct of business, rather than out of professional practice.”

Risk Management Solution: That investing in clients constitutes a significant personal interest conflict of interest is clear. This case also illustrates that the ramifications of permitting lawyers to take on engagements where these conflicts exist extend beyond the “mere” risk of claims. Depending on the wording of the firm’s lawyers’ professional liability policy, the claim may be excluded. In order to manage the risk of such claims, as well as the risk of exclusion from coverage, firms need to know if such conflicts may exist before engagements are accepted, in order to determine if the engagement is appropriate. In addition, if
the firm does decide to accept the risks, it also needs to evaluate whether the necessary disclosure has been made to the client, and an appropriate consent obtained. In order for these risk management steps to proceed, the firm first needs to know at the client intake stage that the conflict exists. Accordingly, firms need to consider including a specific disclosure requirement as to this issue on their new client and matter intake forms. Without the information, the first time the firm will learn of the problem is likely to be when the claim is filed. In this case, that meant that not only was there a claim based on a conflict, but that the firm had no insurance coverage for the defense against or to indemnify the claim.

**Engagement Letters—Implications of Failure of Client to Countersign**

**Engagement Letters—Reliance—Suit for Fees**


**Risk Management Issue:** How can a law firm confirm the details and scope of an engagement and protect its fee interest in matters where a client fails to countersign and return the engagement letter, and time is nonetheless of the essence?

**The Case:** A Delaware investment bank retained an Ecuadorian law firm to conduct due diligence on an Ecuadorian company that the bank planned to acquire. The law firm completed its engagement but the deal did not close because the bank was unable to obtain financing. The bank then refused to pay any of the law firm’s fees, claiming that their engagement did not require payment unless the acquisition of the Ecuadorian company actually took place. The law firm sued for breach of contract and equitable relief. After a bench trial, U.S. District Court for the Southern District of New York Judge Miriam Goldman Cedarbaum found for the law firm, ordering the bank to pay the law firm the full amount of outstanding fees and costs, plus interest.

When the bank had initially contacted the law firm, the firm sent an engagement letter including the terms of its hourly fee, a $20,000 advance deposit, and a requirement that the bill be paid upon receipt, or else the bank would be charged interest. The bank did not, at the time, inform the law firm that the bank’s payment of attorneys’ fees was contingent upon the bank’s successful acquisition of the Ecuadorian company. A witness for the bank testified that it was the bank’s “preference” or “practice” to pay if and when the deal closed. The bank had instructed the law firm to begin work immediately due to time exigency, notwithstanding that the law firm had not received a countersigned engagement letter. In connection with the engagement letter, the bank requested two minor changes to the letter, but did not object to any of the payment terms. Nor did the bank inform the law firm its intent not to pay unless the deal closed. The bank never countersigned and returned the engagement letter, despite repeated inquiries by the law firm. Nor did it forward the deposit.

The law firm continued to perform its work to close the deal by the targeted closing date, sending monthly billing statements by email. The bank claimed that it never received the emails and that they landed in the company email junk mail folder, and that the bank therefore did not see the invoices until a few months later, when the law firm started to demand payment. The law firm's records showed repeated email attempts to demand payment of more than $110,000 in fees. The bank never objected to the claim for payment; instead it offered assurances of payment or completely dodged the issue. The law firm completed its work and delivered its report. The bank was ultimately unable to obtain financing to acquire the Ecuadorian company, and the deal fell apart. Two months after the last of the law firm’s work for the bank, the bank emailed the law firm to inform it for the first time that the bank would not pay the law firm’s bills because the deal did not close, and suggested that the law firm help the bank close the deal so that the law firm could get paid. The law firm immediately denied agreement for payment contingent on the deal, and insisted on full payment. Negotiations were unsuccessful and the law firm filed suit for breach of contract, *quantum meruit* and account stated. The bank claimed that the law firm’s fees were excessive.

Applying New York law, Judge Cedarbaum found that an agreement for legal representation does not require a signed contract to be enforceable. Parties can demonstrate the existence of a contract through a showing of objective manifestations of the intent of the parties through the parties’ words and deeds. Silence is acquiescence when a party is under a duty to speak but does not do so such that the silence would mislead the
other party. Although the engagement letter was never signed, the conduct established that the bank accepted the terms of the law firm’s offer by its silence and by its acceptance of the work performed. The court found this to be the result even if it accepted the bank’s position that it never intended to accept the hourly fee terms (as evidenced by the bank’s refusal to execute the engagement letter). The bank’s subjective intent was not enough to avoid the enforcement of the contract.

**Risk Management Solution:** While law firms sometimes find themselves performing legal services in situations where there exist exigency and client demands that those services go forward before the client countersigns the engagement letter, firms in such situations risk being unable to enforce the terms of their engagement letter against the client’s later repudiation. This case is important in that it establishes that law firms may rely on the client’s agreement to the terms of the engagement even in the absence of a counter-signed engagement letter. Better practice is to ensure a “meeting of the minds” by securing agreement on scope and terms of representation as quickly as possible, and not countenancing delay or evasion on this point. Some firms have established a practice of sending a follow-up communication explaining that the client’s continued directions to the firm to provide services will be deemed to be agreement to the terms of the engagement letter. Such a communication helps to establish both that the firm is relying on that conduct as evidencing agreement, and that the reliance is reasonable. The firm here placed itself in a precarious position, and could well have lost its claim in another jurisdiction or under slightly changed facts.

**Confidentiality—Law Firm General Counsel—Fiduciary Duties—Attorney-Client Privilege**

*Garvy v. Seyfarth Shaw LLP, —N.E.2d—, 2012 Ill. App. (1st) 110,115*

**Risk Management Issue:** Are a law firm’s communications with in-house general counsel and outside counsel privileged when a current client sues the firm for malpractice?

**The Case:** Plaintiff client sued defendant law firm for legal malpractice, fraud, and breach of fiduciary duty. In 2001, the client retained the law firm to provide corporate advice related to the management of a family-owned close corporation. Several of the client’s family members filed suit against him in 2004 in the Circuit Court of Cook County, based in part on actions the client had taken pursuant to advice from defendant law firm. The client asked defendant to represent him in the litigation. At the direction of its in-house counsel, defendant law firm sent the client a detailed letter regarding the potential conflicts of interest in its representation of him in the litigation due to the prior advice the firm had given him. The letter strongly encouraged the client to seek independent counsel regarding his consent to waive conflicts.

The client retained independent counsel, who asserted legal malpractice claims against defendant law firm on the client’s behalf and entered into pre-complaint settlement discussions with defendant. The independent counsel sent defendant law firm a letter regarding the settlement negotiations, adding that the client wanted defendant to continue representing him in the litigation. The independent counsel requested that defendant law firm enter into a tolling agreement regarding the client’s claims against defendant, which they did, and settlement discussions continued on the malpractice claims. Defendant law firm retained a third law firm to represent it with respect to the client’s malpractice claims. When defendant law firm raised with the client the issue of withdrawing from representing him, the client objected, arguing that withdrawal could sabotage settlement prospects. After settlement discussions in the litigation terminated unsuccessfully, on the third law firm’s advice, defendant law firm withdrew as the client’s counsel.

Several days later, the client filed a complaint against the law firm. During the discovery process, the client sought the production of the law firm’s internal and external communications related to its representation of the client, including all information related to the client’s legal malpractice claims. The law firm objected to the client’s requests to produce communications between the law firm’s attorneys and both in-house and outside counsel related to the client’s claims against the law firm, contending that the communications were protected by attorney-client privilege or the work-product doctrine. The circuit court ruled against the law firm, which refused to comply with the resulting order that followed, resulting in a civil contempt and $100 fine entered against it.
Second, the appellate court took issue with the lower court’s conclusion that defendant law firm had not fully disclosed the conflicts and that the court could not determine whether the client’s consent to defendant’s continued representation was informed. The appellate court found that it was clear from the record that the conflicts were disclosed, that the client sought independent legal advice, and that his consent to defendant law firm’s continued representation in the litigation was fully informed. In addition, the appellate court noted that the client had entered into a tolling agreement with defendant law firm in order to preserve his malpractice claims. The appellate court expressed disapproval of the client’s attempt to “have it both ways,” stating, “he cannot insist that [defendant law firm] continue to represent him in the litigation while he has malpractice claims pending against [defendant], but then use that continued representation to insist that [defendant law firm] produce all documents related to legal advice sought in relation to the malpractice claims generated during that time.”

Finally, the appellate court rejected the client’s argument that defendant law firm could have no expectation that its communications with counsel would be confidential because of the disclosure requirements imposed by Rules 1.4 and 1.7 of the Illinois Rules of Professional Conduct. To the contrary, as noted by amici, the very rules that the client relies on for that proposition recognize that a lawyer’s confidentiality obligations do not preclude him from seeking confidential legal advice about his own ethical obligations, and that lawyers are permitted to make confidential reports of ethical issues to designated firm counsel (Ill. R. Prof’l Conduct 1.6(b)(4) cmt. 9 and 5.1 cmt. 3). With respect to the client’s work-product claims, the appellate court found that work-product of in-house and outside counsel was not discoverable because the client had not shown that it was impossible for him to obtain information related to his malpractice claims from similar sources.

Risk Management Solution: This case represents a welcome rejection of the case law that has developed holding that, at least as to communications with law firm’s in-house general counsel, there is no attorney-client privilege if the communications relate to a continuing client of the law firm. Those cases hold that the firm’s fiduciary duties to the client “trump” the privilege. Notably, a similar rejection of that reasoning may be found in another recent case, Tattletale Alarm Systems, Inc. v. Calfee, Halter & Griswold, LLP, et al., 2011 WL 382627 (S.D. Ohio 2011), which contains a thorough analysis of the competing legal principles. Central to the Illinois Appellate Court’s determination was the fact that the client had been fully informed as to the potential conflicts of interest arising from the law firm’s continued representation of him. This case underscores the need for thorough conflict waivers documenting that consent was informed. In the absence of such documentation, the decision could have come out quite differently. Although this case upheld the law firm’s right to assert its privilege, firms would be in a stronger position if they did not concurrently represent clients suing them for malpractice. Once claims are asserted against a firm, that firm should, as soon as reasonably possible, cease representing the affected client, at a minimum with respect to the matter that is the subject of the claim.
RPC 4.4—Receipt of Confidential Documents From Third Party—
Motion to Disqualify Counsel


**Risk Management Issue:** When an attorney receives confidential documents regarding a case from an anonymous source, what steps must the lawyer take in order to avoid disqualification and to comply with his or her ethical obligations?

**The Case:** A manufacturer sued its three distributors (collectively, “Petitioners”) for fraud and breach of contract. In an unrelated action commenced prior to that suit, Petitioners sued a former employee of one of the distributors, alleging that he stole trade secrets. The district court in that case permanently enjoined the former employee from distributing any of the stolen information to Petitioners’ “customers, manufacturers, suppliers, or business partners.”

After filing suit against Petitioners, the manufacturer received an anonymous package from Lebanon at its New York headquarters on September 24, 2009. The envelope bore Lebanese stamps and the phrase “Highly Confidential,” but was otherwise unmarked. The package contained a disk and a note stating that the package should be forwarded to the manufacturer’s counsel, an attorney in Las Vegas. On October 15, less than a month after receiving the package, the manufacturer’s counsel served on Petitioners a supplemental pretrial discovery disclosure pursuant to Nev. R. Civ. P. 16.1. The disclosure identified the disk received by the manufacturer from an unidentified source, and included a copy of the disk as well as a copy of the envelope it arrived in. At the time, Petitioners did not object to the manufacturer having the disk.

In January 2010, the manufacturer used some of the documents from the disk in a deposition of one of Petitioners’ employees, and Petitioners still did not object or argue that any of the documents were privileged. On May 14, 2010, nearly eight months after the manufacturer first disclosed its receipt of the disk, Petitioners first objected to the manufacturer’s use and possession of the documents on the disk through a motion to the district court, requesting dismissal of the manufacturer’s case or, in the alternative, prohibition of the manufacturer’s use of confidential and privileged documents and for disqualification of the manufacturer’s counsel. The district court declined to dismiss the case or disqualify the manufacturer’s counsel and his firm. The court found that the manufacturer and its counsel “conspicuously set forth” their receipt of the disk in the Nev. R. Civ. P. 16.1 disclosure, and that neither the manufacturer nor its counsel knew of the injunction Petitioners had against the former employee. The court also concluded that Petitioners failed to show that any of the documents contained on the disk, except a draft affidavit, were privileged. The court excluded the use of the draft affidavit, but otherwise allowed the use of the documents contained on the disk. Petitioners then sought a writ of *mandamus* in the Nevada Supreme Court to instruct the district court to reconsider the disqualification motion.

The Nevada Supreme Court affirmed the factual findings and the decision of the district court, but took the opportunity to adopt a notification requirement for situations where an attorney receives documents or evidence from an anonymous source or from a third party unrelated to the litigation. It also set forth factors for district courts to consider in determining whether an attorney who reviews privileged information under such circumstances should be disqualified.

With respect to notification, the Court found that Nevada has no ethical rules governing the specific situation presented. Petitioners argued that the manufacturer’s counsel’s conduct violated Nev. R. Civ. P. 4.4(a) (“[i]n representing a client, a lawyer shall not . . . use methods of obtaining evidence that violate the legal rights of [a third] person”) and 8.4(d) (“[i]t is professional misconduct for a lawyer to . . . [e]ngage in conduct that is prejudicial to the administration of justice”). The Court found that these rules did not apply because the manufacturer’s counsel did not play any part in obtaining the opposing party’s documents and was not complicit in any actions used to wrongfully obtain these documents. Both parties agreed that Nev. R. Civ. P. 4.4(b), which provides that “[a] lawyer who receives a document relating to the representation of the lawyer’s client and knows or reasonably should know that the document was inadvertently sent shall promptly notify the sender,” was inapplicable because the disk was not inadvertently sent to the manufacturer’s counsel. Nonetheless, the district
court appeared to have applied Rule 4.4(b) by analogy, concluding that the manufacturer’s counsel met his ethical duties because he promptly notified Petitioners of his receipt of the disk.

The Court agreed with the district court’s reasoning in adopting a notification requirement. An attorney who receives documents regarding a case from an anonymous source must promptly notify opposing counsel, or risk being in violation of his or her ethical duties and/or being disqualified as counsel. Notification must adequately put opposing counsel on notice that the documents were not received in the normal course of discovery and describe, with particularity, the facts and circumstances that explain how the document or evidence came into counsel’s or his or her client’s possession. In this case, the Court concluded, the manufacturer’s counsel did just that through a Nev. R. Civ. P. 16.1 disclosure. Therefore, the district court correctly concluded that the manufacturer’s counsel fulfilled his ethical obligations.

The Court then addressed the issue of disqualification. Noting that the Supreme Court of Texas had resolved a similar issue in In re Meador, 968 S.W.2d 346 (Tex. 1998), the Court agreed with the Texas Court’s reasoning that “[w]ithout doubt, there are situations where a lawyer who has been privy to privileged information improperly obtained from the other side must be disqualified, even though the lawyer was not involved in obtaining the information.” However, “it is impossible to articulate a bright-line standard for disqualification where a lawyer, through no wrongdoing of his or her own, receives an opponent’s privileged materials.” The Court then adopted the factors identified by the Texas Court in determining whether disqualification is appropriate. The nonexhaustive list includes: (1) whether the attorney knew or should have known that the material was privileged; (2) the promptness with which the lawyer notifies the opposing side that he or she has received its privileged information; (3) the extent to which the attorney reviews and digests the privileged information; (4) the significance of the privileged information; i.e., the extent to which its disclosure may prejudice the movant’s claim or defense, and the extent to which return of the documents will mitigate that prejudice; (5) the extent to which the movant may be at fault for the unauthorized disclosure; and (6) the extent to which the nonmovant will suffer prejudice from the disqualification of his or her lawyer.

In the instant case, the Court concluded that the factors weighed in favor of the district court’s determination that the manufacturer’s counsel and his firm not be disqualified. Most of the documents on the disk were not privileged, and the manufacturer’s counsel stated that he did not review the document the court determined was privileged. Further, the manufacturer’s counsel made multiple disclosures to Petitioners, which indicated that he was not trying to deceive them or conceal his receipt of the disk from them. Accordingly, the Court denied the petition for writ relief.

Nev. R. Civ. P. 4.4(b) is identical to the ABA Model Rule of the same number. The ABA has stated that “if the providing of the materials is not the result of the sender’s inadvertence, Rule 4.4(b) does not apply to the factual situation. . . . A lawyer receiving materials under such circumstances is therefore not required to notify another party or that party’s lawyer of receipt as a matter of compliance with the Model Rules. Whether a lawyer may be required to take any action in such an event is a matter of law beyond the scope of Rule 4.4(b).” Although Nevada now has law requiring notification, other Model Rules jurisdictions may not. (Some jurisdictions, such as New Jersey and the District of Columbia, go even further than Nevada in the case of inadvertent disclosures, requiring the recipient lawyer, once he or she realizes a document is privileged, to cease reviewing it, notify opposing counsel, and return the document).

Risk Management Solution: The ethics rules in some jurisdictions may not require notification of the opposing party of receipt of materials from an anonymous sender. However, because of the risk of disqualification, if counsel reads a document that turns out to be privileged, even if it was received totally innocently, counsel should be extremely careful before reviewing documents received from an anonymous source and counsel should stop reading immediately if it appears that a document may be subject to a claim of privilege, and consider both the ethics rules and applicable case law in the relevant jurisdiction to determine the scope of his or her obligations as to the materials.
Attorneys’ Fees — Standards for Review of Request for Court Awarded Legal Fees

**Toussie v. County of Suffolk, 2012 WL 3860760 (E.D.N.Y. Sept. 6, 2012)**

**Risk Management Issue:** What are a lawyer's duties and responsibilities when entering and recording time charges, and what standards should attorneys expect courts to apply in reviewing requests for the award of reasonable attorney’s fees pursuant to 42 U.S.C. § 1988?

**The Case:** This decision, assessing entitlement to attorneys' fees, is the final chapter in a decade-long litigation saga arising out a series of alleged constitutional and tort violations by defendant county. Plaintiff buyers alleged that their constitutional rights were violated when the county repeatedly denied them the opportunity to purchase parcels of real estate at county surplus auctions. The buyers sought an order of specific performance directing the county to convey the parcels and an award of damages totaling more than $35 million.

After a two-week trial – which followed years of discovery-related litigation, protracted and unsuccessful settlement negotiations, and dispositive motion practice – the jury gave the buyers a pyrrhic victory in the form of a verdict in their favor of $12,500. The buyers moved for attorneys' fees pursuant to 42 U.S.C. § 1988(b) in the amount of $2,794,929.50, arguing that they had satisfied the criterion for reimbursement of attorneys’ fees as they were a “prevailing party” in the litigation. The county countered that any award of attorneys' fees would be unreasonable and unjust because: (1) the buyers' recovery was *de minimis*; and (2) the request for fees was “so unreasonable and gross[ly] excessive” that it could not have been made in good faith.

The U.S. District Court for the Eastern District of New York acknowledged that the county’s *de minimis* recovery argument presented a close question. Although there was a substantial difference between the judgment recovered and the attorneys’ fees sought, because the buyers recovered more than mere nominal damages, and the jury verdict would likely deter similar due process violations by the county in the future, the buyers’ success was not so trivial that the only reasonable fee would be no fee at all.

The court nonetheless flatly rejected the buyers’ request for attorney fees because the application was so outrageously excessive and unreasonable that it could not possibly have been made in good faith. The court identified seven egregious shortcomings in the attorneys’ fee requests that justified the outright denial of any attorney’s fee award.

First, the court observed that the buyers' lawyers sought attorney fees for claims on which the buyers did not prevail. The court noted that these fee requests “shock[ed] the conscience,” given that counsel affirmatively represented that unrelated fees were excluded, and yet, the fee requests contained numerous extraneous and unrelated billing entries which, the court found, could not have been included by mistake.

Second, the court found that the buyers’ lawyers failed to maintain billing records in a manner that would enable the court to distinguish the claims in the billing entries. The court noted that the lawyers’ bills were replete with vague and generic entries (such as “research,” “summary judgment briefing,” and “trial prep”), which prevented the court from being able differentiate and identify the claims that were being worked on in each time entry.

**Attorneys’ Fees, continued on page 2**
Third, the court held that the buyers’ lawyers failed to segregate their hours spent traveling. More egregiously, they sought full compensation for all travel expenses, despite the court’s having previously ordered that only half of travel time would be recoverable. Again, the court found that the lawyers’ request for complete travel reimbursement appeared to have been purposeful and in bad faith.

Fourth, the court determined that the buyers’ lawyers sought reimbursement of attorneys’ fees at rates that were excessive and unreasonable, and disproportionate to the rates being awarded in the jurisdiction. Specifically, while the lawyers sought an award of fees based on hourly rates ranging from $375 to $905 for counsel, and $250 for a paralegal, the range of reimbursement for attorneys’ fees in the jurisdiction was generally between $250 and $450 per hour. The court noted that the lawyers failed to provide the requisite evidence that their rates were in line with those prevailing in the community for similar services by lawyers with reasonably comparable skill, experience and reputation.

Fifth, the court observed that the buyers’ lawyers sought full reimbursement for billing entries that contained tasks that were redacted and excluded as unrelated to the due process claims. In other words, they had redacted certain unrelated tasks from block billing entries, and yet sought complete reimbursement for the amount of time corresponding to the entire block billing entries.

Sixth, the court observed a significant discrepancy between the lawyers’ respective affidavits and the actual amount of time worked as evidenced by the provided billing records.

Finally, the court concluded that the buyers’ lawyers sought to recover fees that the court had previously determined were unreasonable and excessive.

In sum, the court held that the lawyers’ conduct simply should not and would not be tolerated. Accordingly, the buyers’ motion for attorneys’ fees was denied in its entirety.

**Risk Management Solution:** The lessons of this case go far beyond the realm of court-ordered legal fees. Whether lawyers are seeking fees from a client directly, or from a court, they owe a continuing fiduciary duty to insure that all time entries are accurate. Where clients are paying directly, the rates to be charged – if the matter is to be billed on a time charge basis – must be clearly explained in the engagement letter. All entries must be contemporaneous and sufficiently detailed to enable the reviewer – whether client or court – to determine precisely what services were performed, and when. Unless a client has agreed to “block billing” (aggregating multiple discrete tasks in one time entry), that approach is likely to lead to disputes and to sour the relationship. It ultimately may also deprive the lawyers of the ability or right to collect the fees they are seeking. While this case represents an extreme example of the consequences of not following proper time recording and billing practices, it serves wider notice of the need for firms to supervise, on an ongoing basis, compliance with their billing policies and procedures.

**Document and File Retention — Obligations With Respect to Missing Clients**

**Nebraska Ethics Advisory Opinion for Lawyers, No. 12-07**

**Risk Management Issue:** How long must lawyers and law firms retain client documents and files? What should attorneys do to avoid the problem that clients cannot be located when the time comes for the disposition of their files? What investigation must be undertaken to locate missing clients prior to destruction of their documents and files?

**The Opinion:** The Nebraska Ethics Advisory Board issued this opinion regarding the appropriate handling of a lawyer’s law files after he died. The opinion was requested by an attorney who had been appointed trustee for the protection of another lawyer’s clients after that lawyer died. Some of the deceased lawyer’s files contained original documentation. Many files did not contain adequate information to enable the clients to be contacted and informed that the attorney had died. Given the inability to contact many of the clients, the trustee sought guidance as to what should be done with the client files.
The applicable professional conduct rule, based upon Nebraska’s Rules of Professional Conduct (which track the ABA Model Rules) is Rule 1.15(a). It provides that “property shall be kept by the lawyer and shall be preserved for a period of five (5) years after termination of the representation.” Accordingly, the trustee would be permitted to dispose of the files after five years, assuming that the sole practitioner’s representation of those clients ended when he died. In the meantime, the opinion suggested that the trustee should take steps to try to locate clients using social media, Google, public notices (in newspapers), and perhaps in the case of files with important or valuable materials, by hiring a private investigator.

In deciding whether to retain or destroy a file, the advisory opinion suggested several factors to consider including: (1) whether the file includes original documentation; (2) whether the file includes information which may be necessary in the assertion or defense of the client’s position for any matter in which the statute of limitations has not expired; (3) the client’s reasonable expectations; and (4) the potential relevance of particular matters to some future event (such as a will).

**Comment:** Not every state has a five-year rule (New York, for instance requires financial documents – broadly defined – to be held for seven years from the end of representation). However, every state does have in place ethical requirements with respect to the handling and destruction of client documents and files. This opinion is useful because it addresses the problem of what to do when the client goes missing, and what steps are required to avoid that problem.

**Risk Management Implications:**

First, it is important for attorneys to identify (in writing) when a particular representation ends so that the lawyers (or a future trustee) can establish with certainty when the clock starts to run regarding the time for disposal of the file. This may also start the clock ticking for the statute of limitations in a future potential malpractice claim. Some firms do this by clear language in the original engagement letter, in addition to sending “closing” letters when the engagement is concluded.

Second, it is important for attorneys to obtain sufficient information at the time of engagement — including for individual clients such information as social security numbers and the names and addresses of family members — and to maintain such information throughout the engagement. Again, some firms include an explicit obligation on the part of clients to notify the lawyer or firm if any information relating to their location changes. Even apart from lawyers’ duties to keep clients regularly informed of the progress of their matters under states’ equivalent of Model Rule of Professional Conduct 1.4, the need to keep this information current constitutes an additional reason why regular contact with clients matters.

Finally, for solo practitioners, it is critical that they have some sort of plan in place in the event that they die or become incapacitated. Solo practitioners of all ages need to select and identify another lawyer who has agreed to contact clients to let them know in the event that their attorney can no longer represent their interests and, if the clients so elect, to discharge the lawyer’s duties to complete the clients’ matters.

**Attorney-Client Relationship — Limiting the Scope of the Representation — Identification of the Client — Representing Corporations and (or) Their Constituents**


**Risk Management Issue:** When does representation of a corporate constituent also entail representation of the corporation? What can law firms do to limit the scope of representation and avoid the establishment of an attorney-client relationship in a corporate family context?

**The Case:** The case arises out of the bankruptcy of a corporation and the fraudulent activities of the corporation’s founder and senior managers. During a quarterly review of the corporation’s financial statements, three senior officers revealed they had suspicions of fraudulent activity by the company’s founder. Those three officers resigned shortly thereafter. The corporation’s board of directors agreed to investigate the reasons for the resignations and created a special committee to investigate and report to the board. The special committee hired a law firm to...
investigate the alleged fraudulent activity by the founder and senior managers. The law firm hired a financial consulting company to help its investigation.

Upon conclusion of the law firm’s investigation, the law firm reported that there was no fraud. Relying on the report, the corporation, through its founder, sought to build a production facility and to offer an initial public offering. A minority of the shareholders opposed these actions and the dispute was resolved in court. The court appointed a custodian to be in charge of the corporation’s management and operations. Within days, the custodian uncovered substantial fraud within the company.

Thereafter the corporation went into bankruptcy. The bankruptcy trustee sued the law firm for professional negligence, breach of contract, breach of fiduciary duty, negligent misrepresentation, and vicarious liability (for the financial consulting company’s conduct) arising out of the failure to find the fraud. The trial court dismissed the trustee’s claims, determining that there was no attorney-client relationship or contractual relationship between the law firm and the corporation.

On appeal, the Pennsylvania Superior Court determined that the allegations in the trustee’s amended complaint demonstrated an attorney-client relationship and a contractual relationship between the law firm and the corporation. The court rejected the law firm’s argument that because the retention letter between the law firm and the corporation stated that the law firm would act as counsel for the special committee, it was not representing the corporation.

The court based this conclusion, first, on its interpretation of Delaware law, where the corporation was incorporated, finding that in Delaware a committee created by a board acts on behalf of the corporation’s shareholders and the corporation. The corporation’s board had authorized the special committee to conduct an investigation “on behalf of the company.” When the special committee hired the law firm to investigate the alleged fraudulent activities in the company, the actions of the special committee were for the benefit of the corporation’s shareholders and the corporation itself. Thus, when the law firm undertook to find the fraud and advised the special committee about its findings, those services and the legal advice were essentially being given to the corporate entity.

The court also determined that the law firm’s actions during its representation of the corporation established that the law firm was aware its representation extended to the corporate entity, or at the very least that it represented more than just the special committee. The law firm forwarded its findings and recommendations to the corporation’s founder, who was not on the special committee. After submitting the report to the special committee, the law firm also sent the report to the board. The court held that these actions established that the firm was representing the corporation, and not just the special committee.

**Risk Management Solution:** This case shows that in the corporate arena even an engagement letter that clearly identifies who is the client may not be sufficient to avoid liability to others than the identified client. Because some states (e.g., Delaware) do not allow a law firm to represent a corporation’s board/committee independent from the corporation itself, when a corporation’s board/committee retains a law firm, the law firm should refer to the applicable state law to determine if an attorney-client relationship also forms with the corporation. Whether an explicit waiver from the corporation that expressly approved the limited engagement by the committee would have worked is not resolved. It might be worth trying, but if it is attempted, the second lesson in this case is that even a clear limitation on the identity of the client can be undone if the firm subsequently acts in ways that are inconsistent at the time of engagement.
**TRICK OR TREAT!**

The editors of the Halloween Edition of *The Lawyers’ Lawyer Newsletter* bring you one tasty treat of a case, one nasty trick of a case, and one off-the-wall case involving a judge with an alter-ego, not unlike Dr. Jekyll and Mr. Hyde. We hope these dressed up tales will delight and frighten just in time for All Hallows Eve.

**Trick or Treat Editors’ note:** Advance waivers received a lot of judicial attention over the past year, first with Galderma (see our May 2013 issue) and later with the Macy’s case (below). These cases are definitely a “treat” for law firms that want to have their Halloween candy (engagement with a client) and eat it too (be adverse to the same client in the future), without the risk of a guillotine (disqualification).

**Conflicts of Interest – Advance Waivers**


**Risk Management Issue:** When are advance waivers of conflicts of interest valid and binding on clients, and what are the requirements that lawyers must meet in order for them to be enforceable?

**The Case:** By agreement dated March 7, 2008 an international law firm undertook to represent defendant client, a retailer, regarding certain “intellectual property litigation and trademark registration” in Asia. The agreement expressly informed the client about the possibility that the law firm’s present or future clients “may be direct competitors of [the client] or otherwise may have business interests that are contrary to [the client]’s interests,” and “may seek to engage [the law firm] in connection with an actual or potential transaction or pending or potential litigation or other dispute resolution proceeding in which such client’s interests are or potentially may become adverse to [the client]’s interests.” The agreement unambiguously explained that the law firm could not represent the client unless the client confirmed that this arrangement was amenable to it, thereby “waiv[ing] any conflict of interest that exists or might be asserted to exist and any other basis that might be asserted to preclude, challenge or otherwise disqualified [the law firm] in any representation of any other client with respect to any such matter.” The agreement also provided, [*2] “However, please note that your instructing us or continuing to instruct us on this matter will constitute your full acceptance of the terms set out above and attached.”

Notwithstanding this agreement, the client sought to disqualify the law firm from representing a second retailer in this case. The trial court denied the motion to disqualify, and the New York Supreme Court, Appellate Division, First Department unanimously — and almost summarily — upheld the trial court’s decision, holding that it had “providently decided” the motion. The Appellate Division found that “[i]t is undisputed that [the law firm] continued to represent defendant with respect to [the client’s] Asian trademark portfolio” after the client accepted the terms set out in the engagement letter, “and, thus, defendant accepted the terms of the agreement, including waiver of the alleged conflict at issue.” Further, the court noted that “the interests of defendant that [the law firm] represents, namely intellectual property litigation and trademark registration exclusively in Asia, do not conflict with defendant’s interests at issue here . . . .” In other words, the court implicitly concluded that the matters were unrelated, and that the law firm held no confidential information from its work on the Asian trademark portfolio that were of any relevance to this matter.

**Comment:** As we indicated in our discussion of the Galderma case in the May 2013 issue of the Lawyers’ Lawyer, whether and when law firms should be able to rely on advance waivers of conflicts of interest involves the resolution of competing paradigms of legal ethics. On the one hand, the rules governing conflicts of interest are premised on the fiduciary duties of loyalty and the protection of client confidences. On the other hand, the law governing lawyers recognizes the principles that clients should normally be free to select counsel of their choice, free from outside interference, and that client consent can, in appropriate circumstances, form a proper basis for overcoming prohibitions on conduct that would otherwise be impermissible.
Unlike the court in *Galderma*, the New York court summarily disposed of the motion to disqualify based upon the straightforward language of the advance waiver in the engagement letter. It appears from the transcript from the lower court decision that the letter containing the waiver was reviewed by a lawyer in the client’s in-house law department. Although the waiver wasn’t countersigned, the client proceeded to engage the firm, and the firm undertook the engagement on the basis of the letter. In that respect, therefore, this case goes further than *Galderma* in allowing a firm to rely on a waiver that it has supplied to the client and that has been reviewed by independent counsel and not rejected, even if it was not explicitly countersigned and agreed to. The case therefore represents another step along the way of recognition that sophisticated clients should be — and will be — held to understand, and be bound by, explicit advance waivers.

**Risk Management Solution:** Although this court did not go through the extended analysis that the Texas court did in *Galderma*, the steps recommended in our report about that case bear repeating as a useful checklist for law firms seeking to obtain enforceable advance waivers from sophisticated clients:

- First, as to existing or presently identifiable potential conflicts, in order for a waiver to have the greatest likelihood of being upheld, disclosure of both the specific facts and the potential adverse consequences should be made.

- Second, as to advance or blanket waivers of potential future conflicts, the disclosure should be as comprehensive and detailed as is possible, laying out the foreseeable types of adversity and the nature of the potential negative consequences for the client.

- Third, as to waivers of both existing and future conflicts, these should be obtained in circumstances that — as far as possible — preclude the client from later averring that the client did not understand the meaning or implications of the waiver. Waivers standing the greatest likelihood of being upheld are those where the client actually received independent legal advice with respect to the waiver — but a very significant element of the decision in this case is that in-house counsel for a corporation can serve that independent function.

Accordingly, the ideal signatory of a conflict waiver letter is a client’s independent counsel — whether in-house, or outside. At a minimum, lawyers should advise clients to obtain the advice of independent counsel before signing waivers of conflicts, and, preferably, clients should be required to do so before lawyers proceed based on the waiver. Generally, this is easier where in-house counsel is available, but, when there is not, if the law firm believes that there is any likelihood that it will later need to rely on the waiver, the case is even stronger for requiring the affected client to have another lawyer review the waiver letter before signing it.

**Trick or Treat Editors’ note:** The “unfinished business” rule can certainly be a “trick” for law firms looking to acquire laterals from firms that are failing, or may fail in the near future. We hope that the risk management lessons learned from the “Hell’er case will help you and your firm avoid a long elevator trip in the wrong direction.

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**The ‘Unfinished Business’ Rule – Fraudulent Transfers – Risks in Hiring Attorneys From Failing Law Firms**


**Risk Management Issues:** What are the special financial risks potentially faced by firms seeking to hire lawyers laterally from firms that dissolve? What is the meaning and scope of the “unfinished business” rule - at least under California law as viewed by the Bankruptcy Court for the Northern District of California? What can hiring firms do to manage the risks of the application of the rule in connection with lawyers whom they hire – and what can firms generally do to prevent the issue from arising? What are the implications of this case in the light of the two opposite decisions from the US District Court for the Southern District of New York (discussed in the November 2012 issue of the Lawyers’ Lawyer) on the future of the unfinished business rule – and how should firms deal with the risks while the uncertainty continues?

**The Case:** In 2008, after a global law firm defaulted on its loans, its partners voted to dissolve the partnership pursuant to a written dissolution plan. The dissolution plan included a provision commonly referred to as a “Jewel waiver.” The term refers to a California appellate decision, *Jewel v. Boxer*, 156 Cal. App. 3d 171 (1994), in which the court held that when a lawyer moves from a failing firm to a new firm, the new firm and the lawyer must pay the failed firm any profits on unfinished business taken to the new firm. The law firm’s “Jewel waiver” provision waived the firm’s rights and claims to seek payment of legal fees generated after the departure date of any...
lawyer or group of lawyers with respect to unfinished firm business. After the dissolved law firm filed for Chapter 11 bankruptcy, its plan administrator sued various law firms, to which former partners of the dissolved law firm transferred, to recover profits those firms earned while completing former the dissolved-law-firm client matters that were pending, but unfinished on the date of the dissolved law firm’s dissolution.

The dissolved law firm’s plan administrator moved for summary judgment against all defendants, arguing that the Jewel waiver constituted a fraudulent transfer to the defendant law firms under both federal and California law. U.S. Bankruptcy Judge Dennis Montali first concluded that “unfinished business” meant “any business covered by retainer agreements between the firm and its clients for the performance of partnership services that existed at the time of dissolution,” and that such unfinished business was the dissolved law firm’s property absent the disputed Jewel waiver.

Judge Montali next concluded that the partners who left the dissolved law firm and joined defendant law firms did not provide “reasonably equivalent value” to the dissolved law firm in exchange for the Jewel waiver. Judge Montali reasoned that there was no evidence that any partner would have refused to execute the dissolution agreement absent the Jewel waiver. Thus, the Jewel waiver was not given to the departing partners in exchange for anything. Based on these conclusions and his finding that the dissolved law firm, at the time of the Jewel waiver, was incurring debts that were beyond its ability to pay, Judge Montali ruled that, notwithstanding the Jewel waiver, the transfer of the dissolved-law-firm matters to defendant law firms constituted a fraudulent transfer.

Based upon the existence of a fraudulent transfer and the lack of any affirmative defense by defendant law firms, Judge Montali granted the dissolved law firm’s motions for summary judgment and ordered a trial to determine amount of money earned by defendant law firms as profit on the unfinished business from the dissolved law firm.


Risk Management Solutions: Even if the Geron case is very clearly upheld on appeal, and the Development Specialists case is rejected as to New York law, and the unfinished business rule is abrogated as to hourly fee cases in New York, the rule will remain a problem as to cases where California law governs, as demonstrated by this decision. Accordingly, hiring firms’ due diligence efforts continue to be significantly complicated. Confidentiality obligations generally prevent a potential lateral from revealing the contents of his or her current firm’s partnership agreement, but educating a lateral on the issues that the rule presents — both for the lawyer and the hiring firm — and seeking assurances regarding those risks (e.g., that the lateral’s current firm is not about to dissolve, and whether or not the current firm’s partnership agreement contains an anti-Jewel provision) is reasonable and prudent for hiring firms. Once a lateral lawyer has given notice to his or her solvent former firm and clients have responded to joint notification letters, it may be worth considering whether there is an opportunity to negotiate a fee division with the former firm to avoid the potentially devastating effects of a Jewel claim years later. The opposite, of course, is true when a prior firm is insolvent because agreements that divert assets from an organization on the verge of bankruptcy are risks arguably not worth taking.

Other due diligence procedures may also be worthwhile, if more uncertain, to avoid or at least limit the possibility of these claims. For instance, careful research of publicly available information about the firm which the lateral prospect wishes to leave may produce useful intelligence about the firm’s long-term prospects. Similarly, even firms that resist using “headhunters” to identify potential recruits may wish to consider engaging one or more of these professionals to act as consultants — extra eyes and ears to the market place — to identify firms where there are signs of incipient problems, such as a rash of resumes on the marketplace. Finally, whenever there is the slightest perceived risk that the rule will be applied to work being brought by the lateral to the hiring firm, the financial terms offered to laterally moving lawyers are likely to be significantly circumscribed.

Additionally, law firms generally may seriously consider adopting so-called anti-Jewel provisions, while they are still going concerns, in order to avoid the problems posed to both partners who leave the firm and the firms to which they seek to move, if the prior firm subsequently dissolves. An example of such a provision might be:

The [partners/shareholders/principals] each acknowledge the duty to complete work undertaken for clients while with the firm. However, all [partners/shareholders/principals] and [name of entity/firm] waive any and all rights to receive payment of legal fees generated from unfinished business after dissolution or fees generated by any departing lawyer or group of lawyers following their departure in connection with matters that were in-progress at the time of departure. Following dissolution, each lawyer or group of lawyers shall be solely entitled to the post-dissolution fees they generate from the winding up of [entity/firm name’s] unfinished business.
Limits on Extra-Judicial Activities - Conduct of Judges

In re Advisory Letter No. 3-11, 2013 WL 5269755 (N.J.)

Risk Management Issue: What are the risks if a part-time sitting judge engages in a side-career as an actor and comedian, and what generally are the limits for extra-judicial activities of judges?

The Case: The New Jersey Supreme Court Committee on Extra-Judicial Activities recently considered the question of whether a part time municipal judge could maintain a career as a part time comedian and actor. Judge Vincenzo August Sicari a/k/a Vince August (his stage name) originally began practicing law in New Jersey as a personal injury attorney in the late 1990s under his given name, while pursuing an entertainment career in television, films and commercials under his stage name. He also appeared regularly as a stand-up comedian in a night club in New York. He managed to keep both his legal and acting careers separate during this time period.

In 2007, the mayor of Hackensack, New Jersey appointed Sicari as a part-time municipal court judge. Sicari disclosed his entertainment career to the mayor and he assured the mayor that he had always kept his legal and entertainment professions separate. He never mentioned his practice of law in any comedy or acting routines.

The conflict came to a head when Judge Sicari was asked for an interview with a local New Jersey paper regarding his dual roles as judge and comedian. Sicari had been interviewed for a previous article that discussed his dual professional life when he had been an attorney. Unsure whether he should agree to an interview while a judge, Sicari asked for an ethics opinion from the Advisory Committee. The Advisory Committee told him, in a written opinion, that not only should Sicari not give the interview, but that his entertainment career was incompatible with his service as a sitting municipal court judge.

Sicari appealed, wherein he received an advisory letter from the Advisory Committee. The letter stated that Sicari’s entertainment profession could create an appearance of impropriety. It noted several factors that influenced the Advisory Committee’s decision including a Linkedin account and a website in the name of Vince August which identified himself as an attorney. The Advisory Committee was concerned that viewers of the website might believe that Judge Sicari “shares the same views as the characters he portrays” thereby creating a perception of bias or lack of impartiality, or that it may “impair the dignity and esteem in which the court should be held.”

Sicari appealed to the New Jersey Supreme Court Committee on Extra-Judicial Activities. In its opinion, the Committee emphasized that not only was it concerned with judicial integrity, but also with the appearance of judicial integrity. It noted that judges must conduct their extra-judicial activities so that they do not cast reasonable doubt on the judge’s capacity to act impartially, demean the judicial office, or interfere with proper performance of judicial activities.

The Committee examined various entertainment projects engaged in by Sicari as his alter-ego, Vince August. It looked at a TV show entitled “What Would You Do?”, a show that was described as a social experiment in which members of the public would be presented with situations where they might be expected to intervene or aid a stranger. Shows dealt with such issues as the harassment of gay men in a bar or “shopping while black.” In the “Shopping While Black” episode, Sicari/August played a security guard engaging in racial profiling of black customers.

The Committee reviewed a DVD provided by Sicari that contained some of his comedy club performances. His routines follow current situations where they might be expected to intervene or aid a stranger. Shows dealt with such issues as the harassment of gay men in a bar or “shopping while black.” In the “Shopping While Black” episode, Sicari/August played a security guard engaging in racial profiling of black customers.

Sicari also wrote, directed and produced an award-winning comedy film called “Vinsanity.” Although he referred to it as the centerpiece of his comedy career, Sicari claimed he could not locate a copy of this performance to present to the Committee. His failure to produce a copy of the film to the Committee led it to the belief that “Vinsanity” was likely replete with humor which would be inappropriate for a municipal court judge.

The Committee found that although there was no evidence that Sicari ever conducted himself in the courtroom in any fashion that was unprofessional, his entertainment career created any impression to the public that Sicari could have biases that would be unbecoming for a municipal court judge, largely based upon the characters he played and the jokes he told as his alter-ego Vince August. The Committee found that while Sicari could continue his entertainment career as an attorney practicing in the courts of New Jersey, he could not do so as a sitting municipal court judge.

Risk Management Solution: Choose your career path carefully! This decision focuses on the limitations on the activities of judges and contrasts the competing precepts that judges should not be isolated and should be encouraged to remain active members of the community, while also holding them to a very high standard of conduct within the community. This decision holds that a judge may not portray a character with questionable or controversial activities or views due to the possibility that the performance might be perceived as exhibiting personal biases held by the judge. Taken to its logical conclusion, however, the New Jersey Supreme Court Committee on Extra-Judicial Activities effectively decreed that once any person dons a judicial robe, he or she gives up the right to engage in political or controversial speech that might create the perception of bias, so long as he or she remains a judge.