Fortifying a Law Firm's Ethical Infrastructure: Avoiding Legal Malpractice Claims Based on Conflicts of Interest

Susan Saab Fortney  
*Texas A&M University School of Law, susanfortney2014@gmail.com*

Jett Hanna

Follow this and additional works at: [https://scholarship.law.tamu.edu/facscholar](https://scholarship.law.tamu.edu/facscholar)  
Part of the [Legal Ethics and Professional Responsibility Commons](https://scholarship.law.tamu.edu/facscholar), and the [Legal Profession Commons](https://scholarship.law.tamu.edu/facscholar)

**Recommended Citation**  
Available at: [https://scholarship.law.tamu.edu/facscholar/244](https://scholarship.law.tamu.edu/facscholar/244)

This Article is brought to you for free and open access by Texas A&M Law Scholarship. It has been accepted for inclusion in Faculty Scholarship by an authorized administrator of Texas A&M Law Scholarship. For more information, please contact aretteen@law.tamu.edu.
I. Introduction ........................................... 670
II. Formulating Systems to Avoid and Manage Conflicts ............................................. 674
   A. Procedures and Controls in Law Firms .......... 675
   B. Conflict Checking and Client Screening........... 681
      1. Whose Interests Should Be Analyzed........... 681
         a. Non-attorney Staff Members ................. 682
         b. Prospective Clients and Declined Clients ........................................... 683
         c. Former Employers of Attorneys and Staff ........................................... 683
         d. Attorneys for Other Parties .................. 684
         e. Business Interests of Attorneys and Staff ........................................... 684
         f. Adverse Parties .................................. 684
         g. Co-plaintiffs and Co-defendants ............. 685
         h. Allies ............................................ 685
         i. Family Members ................................... 685

* Parts of this Article were presented at the St. Mary's Law Journal annual Symposium on Legal Malpractice and Professional Responsibility held on Friday, March 1, 2002.

** Professor of Law, Texas Tech University School of Law. Professor Fortney teaches, among other courses, Legal Ethics and Malpractice, Advanced Legal Ethics, Torts, and Professional Responsibility. I thank the members of the St. Mary's Law Journal for their assistance and the opportunity to participate in the Law Journal's Symposium on Legal Malpractice and Professional Responsibility.

*** Senior Vice President for Underwriting and Administration for Texas Lawyers' Insurance Exchange (TLIE). His duties have included claim management, loss prevention education, and management of computer operations. J.D., University of Texas 1983; B.B.A. summa cum laude, Management Science and Computers, Southern Methodist University 1980.
I. INTRODUCTION

In his concurring opinion on the lack of constitutional protection for hard-core pornography, Associate Justice Potter Stewart expressed frustration in attempting to “define what may be indefinable.” Rather, he resorted to a subjective, instinctive standard in stating the now oft-quoted expression, “I know it when I see it.”

Similarly, attorneys may boldly dive into client representation naively believing that they too will know (a conflict) when they see it. Such a non-systematic approach to identifying conflicts of interest can leave attorneys and their firms exposed to conflicts of interest claims. As suggested by the size and frequency of legal malpractice claims and disqualification motions involving conflicts of interest, a significant number of attorneys and firms have failed to see and address serious conflicts of interest. A Harris and Asso-

2. Id.; see also Sarah F. Warren, Art: To Fund or Not to Fund? That Is Still the Question, 19 CARDozo ARTS & ENt. L.J. 149, 178 (2001) (noting that “an attempt to define something that is inherently subjective is fraught with complication”).
AVOIDING LEGAL MALPRACTICE CLAIMS

A study of 1,100 firms with over 35 attorneys ("Harris Study") revealed that the most significant errors alleged in the largest malpractice claims involved conflicts of interest.4

All conflicts of interests can be characterized as "serious" because a conflict effectively gives a disgruntled client or an adversary a kind of "wild card." With such a "wild card," the disgruntled client possesses a great deal of leverage in refusing to pay outstanding fees and in seeking a refund of fees previously paid. A jointly represented client might also "play the card and require the withdrawal of the attorney (and the attorney's law firm) entirely from the case."5 Clients who suffer damages as a result of conflicts might also bring legal malpractice suits alleging breach of fiduciary duty and negligence claims. In bankruptcy practice, the court may deny compensation for legal services and reimbursement of expenses if an attorney is not a "disinterested person at any time during his employment."6 Another risk is that an adversary can ask or force the conflicted attorney to withdraw from representation. An attorney who withdraws due to a conflict of interest may also face a fee forfeiture.

Depending on the applicable legal malpractice policy and the alleged malpractice, conflicts of interest claims may not be covered. Even when the claim is covered by insurance, the insured attorney or firm will still be responsible for the deductible under the policy and future insurance premium surcharges based on claims experience. Other costs relate to the time and resources devoted to de-

4. Sean M. Fitzpatrick & Catherine Gallo, Managing Professional Liability Risk at Large Law Firms: New Harris Study Yields Valuable Insights, 580 P.L.I. 1029, 1034 (1998), WESTLAW 580 P.L.Iit 1029; see also A.B.A. STANDING COMM. ON LAWYERS' PROF'L LIAB., PROFILE OF LEGAL MALPRACTICE CLAIMS: 1996-1999 (2000) (on file with the St. Mary's Law Journal) (reporting that ABA studies of malpractice claims in 1985, 1995, and 1999 indicate that 3.45%, 3.79%, and 5.12%, respectively, of claims were due to conflicts of interest errors). The American Bar Association study assigns one cause of error to each claim, and does not consider the influence of a conflicts of interest allegation on claims involving other alleged errors. Id. Texas Lawyers' Insurance Exchange ("TLIE") statistics indicate that in claims filed in 1996 or later, 16.4% of all claims included an alleged conflicts of interest. Interview with Jett Hanna, Senior Vice President for Underwriting and Administration for TLIE (Apr. 22, 2002). Such claims accounted for 22.5% of all losses and defense costs paid in the same period. Id. TLIE's statistics suggest that allegations of conflicts of interest increase the severity of losses in malpractice claims. Id.


fending conflicts claims and disqualification motions. In addition to the tangible costs, conflicts hurt the reputation and standing of those attorneys whose integrity has been attacked. “Conflicted” attorneys can face discipline and sanctions imposed by courts and regulators. Even when a perceived conflict does not result in a court action or sanction, clients may simply decide not to use the offending attorney, or may make comments that generate unwanted publicity. Finally, conflicts of interest claims damage the legal profession when the public loses “trust and confidence in the integrity of the bar, the judiciary and the administration of justice.”

Understanding the consequences of conflicts claims and the risks of relying on subjective determinations by individual attorneys, risk management experts have recommended the adoption of policies and procedures to avoid conflicts of interest. During the last two decades, many attorneys and firm managers have heeded the recommendation to implement conflicts of interest procedures and systems. Data obtained in the Harris Study confirmed that firms that utilized conflicts of interest systems and other risk manage-

7. See generally Kurt Eichenwald, Enron’s Collapse: The Lawyers’ Former Client Raises Questions of Conflict, N.Y. TIMES, Jan. 18, 2002, at C7, 2002 WL 8719471 (reporting that a former client of the law firm of Boies, Schiller & Flexner accused the firm of having a conflict when a lawyer who did not work on his case agreed to represent an Enron employee). The Enron employee was to be an adverse witness in the client’s case, but the case was dismissed prior to the time that the firm began representing the Enron employee. Id. The New York Times article reveals no other connection between the two matters. Id.


9. E.g., Dee Crocker, The Problem with Conflicts, 54 Or. St. B. Bull. 41, 41 (1994), WESTLAW 54-MAR ORSBB 41. Ms. Crocker, loss prevention counsel for the Oregon Professional Liability Fund, explains that measures can “reduce the likelihood of a conflict or reduce the possibility that others will perceive that a conflict exists.” Id.; see also A.B.A. Lawyer’s Desk Guide to Preventing Legal Malpractice 56 (2d ed. 1999) (urging firms to establish “stringent procedures” for identifying and resolving various conflicts situations that arise).

10. See Sean M. Fitzpatrick & Catherine Gallo, Managing Professional Liability Risk at Large Law Firms: New Harris Study Yields Valuable Insights, 580 P.L.I. 1029, 1033 (1998), WESTLAW 580 PLI/Lit 1029 (noting that “even the use of relatively more conventional risk management techniques, such as having a risk management partner and regularly circulating new client memos, has increased substantially”). According to the Harris Study, 85% of firms used conflict-checking software as compared to only 16% ten years earlier. Id.
Avoiding Legal Malpractice Claims

Prevention of conflicts of interest requires several steps. To begin with, an attorney must have sufficient information to determine when a conflict of interest exists, and utilize this information to analyze the potential for conflicts. In a law firm, controls and structures to allow this analysis must be available, coupled with a culture and incentives that support risk management efforts so that the controls work as planned.

Conflicts of interest systems, along with other risk management systems, help to form what has been called the ethical infrastructure of the firm. In 1991, Professor Ted Schneyer coined the term “ethical infrastructure” to refer to “a law firm’s organization, policies, and operating procedures” that control the ethical quality of law practice. While firms are investing more time and resources in building an ethical infrastructure, conflicts of interest continue to perplex and plague firms, as illustrated by a recent $400 million conflicts of interest claim against a Philadelphia-based firm. Are such conflicts of interest claims the inevitable price of providing legal services, or do such claims indicate cracks in a firm’s ethical infrastructure?

To answer the question on the inevitability of conflicts, Part II of this Article describes measures that law firms can take to detect

---

11. See id. at 1035 (explaining the relation of risk management practices to the number of claims). “While not significant to the 95% certainty level,” the risk management measures taken which inversely related to the total amount paid in claims, included using conflicts of interest checking software and circulating new client memoranda at least every two weeks. Id.

12. Ted Schneyer, Professional Discipline for Law Firms?, 77 CORNELL L. REV. 1, 4 (1991). In advocating professional discipline of firms as entities, Professor Schneyer points to the “evidentiary problems of pinning professional misconduct on one or more members of a lawyering team, the reluctance to scapegoat some lawyers for sins potentially shared by others in their firm, and especially the importance of a law firm’s ethical infrastructure and the diffuse responsibility for creating and maintaining that infrastructure.” Id. at 11.


and manage conflicts. Part II goes on to analyze the effect of the firm’s ability to avoid conflicts claims on a firm’s ethical infrastructure. Part III focuses on some of the most common conflicts situations that result in malpractice claims and sanctions. The discussion includes selected conflicts cases that illustrate problems and patterns. The conclusion, Part IV, urges firm managers to reassess the efficiency and long-term benefits of devoting time and resources to conflicts avoidance and management.

II. FORMULATING SYSTEMS TO AVOID AND MANAGE CONFLICTS

Attorneys should take several steps in order to avoid conflicts of interest claims. Attorneys must obtain sufficient knowledge of the facts regarding proposed representation to begin a conflict analysis. In particular, it must be understood whose interests need to be analyzed. Once attorneys have knowledge of the parties and interests, they must determine the extent to which those interests conflict. In law firms, a combination of formalized controls and policies are essential to assure proper analysis of conflicts. The policies and controls must include development of appropriate responses to the analysis. The need for formalized controls and policies grows as the firm and number of clients represented grows. This section of the Article examines the complexity of identifying, analyzing, and dealing with conflicts of interest.

A. Procedures and Controls in Law Firms

Law firms must develop policies, procedures, and controls regarding conflict detection and avoidance. Ethics rules generally require that partners in a law firm establish a system to assure that all lawyers in the firm conform to the rules and to require supervising lawyers to assure the ethical compliance of subordinate lawyers and staff. Correspondingly, firm liability results from the breaches of its constituents. Practicing in professional corporations, limited liability partnerships, and limited liability companies may act to insulate the assets of "innocent" attorneys from the acts of other attorneys in a law firm. However, even when the organizational structure of a firm eliminates vicarious liability, the failure to take precautionary steps risks the firm's malpractice insurance experience ratings, reputation, and assets. Ultimately, limited liability entities do not reduce the risk of conflict claims.

16. Model Rules of Prof'L Conduct R. 5.1 (2001). The term "partners" under the Model Rules includes shareholders in a professional corporation. Model Rules of Prof'L Conduct, Terminology [6] (2001). The Texas Rules do not have a provision parallel to Model Rule 5.1 affirmatively requiring that partners set up such systems. Thus, Texas would not recognize a failure to have such systems as constituting a violation of the rules, but civil liability for failing to have such a system is not determined by the rules. When this Article discusses disciplinary rules, the American Bar Association Model Rules are referenced even though each state enacts its own disciplinary rules. On February 5, 2002, the American Bar Association House of Delegates amended the Model Rules. See A.B.A., Center for Professional Responsibility, at http://www.abanet.org/cpr/e2k-202report.html (last visited Mar. 22, 2002) (providing a summary of what rules were changed and a link to the redline version of changes to the Model Rules). Unless otherwise stated, all references to the Model Rules in this Article are to the previous version of the rules.


18. See Restatement (Third) of the Law Governing Lawyers § 58(1) (2000) (stating that "[a] law firm is subject to civil liability for injury legally caused to a person by any wrongful act or omission of any principal or employee of the firm who was acting in the ordinary course of the firm's business or with actual or apparent authority").

19. 1 Ronald E. Mallen & Jeffery M. Smith, Legal Malpractice §§ 5.4-5.6, at 480-81, 495-96, 509-10 (5th ed. 2000).

20. See Jett Hanna, Legal Malpractice Insurance and Limited Liability Entities: An Analysis of Malpractice Risk and Underwriting Responses, 39 S. Tex. L. Rev. 641, 645-48 (1998) (arguing that the risk of malpractice loss is not affected positively or negatively by the existence of limited liability entities). But see Susan Saab Fortney, Professional Responsibility and Liability Issues Related to Limited Liability Law Partnerships, 39 S. Tex. L. Rev. 399, 421 (1998) (arguing that limited liability entities have increased the likelihood of ethical violations and malpractice claims because their structure "may actually undermine partners' willingness to get involved in firm management and risk management activities").
Conflict avoidance must be viewed in conjunction with the management of the entire firm, and not simply as a subsystem isolated from other firm processes. Several partners of the Shearman & Sterling law firm eloquently summarized the purpose of and difficulties inherent in the formulation of such policies and procedures in law firms:

As lawyers we have duties to our clients, to third parties in limited circumstances, to government regulators, to the courts, to our partners, to our employees, and to our community. Often it is not easy to reconcile these responsibilities. The policies and procedures we adopt to meet these duties must be designed to deal appropriately with them, not just to satisfy formal legal and ethical requirements. These policies and procedures communicate our values and aspirations to legal and non-legal staff. Whatever policies and procedures we adopt, they must be workable, respected, and effective. An articulated policy or procedure that is not followed is likely to be a source of problems.

The terms "policies," "procedures," and "controls" come from the language of business management. A policy is a statement of the goals of an organization, and includes the general methods that will be used to meet firm goals. Policies often are broadly worded position statements that casual observers may dismiss as platitudes. However, policies serve the important purpose of focusing the work to be done on procedures and controls. Ideally, once policies

21. See Joel F. Henning, Quality Assurance: Much More Than Minimizing Malpractice, TOTAL QUALITY MANAGEMENT FOR LAW FIRMS 29-35 (1992) (emphasizing that complete quality assurance in law firms involves meeting competence standards, meeting client needs and expectations, and satisfying firm member expectations).


Policy, for example, a procedure policy; general guidelines on the attitudes and orientation towards an issue in an organization.

Procedure (Approach), a way in which a task, activity, or process is executed; the way in which the unit meets the performance requirements presented in the criteria covering principles, policies, systems, processes, approaches, and techniques.

Control, that part of a management activity that directs the action so that needs, expectations, and other requirements are met as planned.

Id.
for an organization are developed, each proposed action can be examined in light of all policies.

It almost goes without saying that most law firms would have a policy to avoid violating the disciplinary rules. Whether stated formally or not, one goal of virtually every law firm and firm lawyer is profitability. Firms generally have a simultaneous goal of providing legal services at a reasonable cost. In addition, firms wish to respond to client needs quickly. A law firm may choose to concentrate its practice on one side of a docket or a transaction area, or to avoid simultaneously working on transactional and litigation aspects of matters. While concentrating in particular practice areas may avoid some potential conflicts, the reasons for excluding some types of practice are not always to minimize conflict problems. Concentration may create economic efficiency that is lost if too many areas of expertise are included in a firm's repertoire.

A workable conflict avoidance system serves all law firm goals to the extent possible, and addresses points of friction between these goals. However, such a system does come at a cost. Decisions on


25. See generally Jonathan R. Macey & Geoffrey P. Miller, An Economic Analysis of Conflict of Interest Regulation, 82 Iowa L. Rev. 965, 965 (1997) (noting that conflicts of interest rules generally lend predictability to the expectations attorneys and clients have about attorney-client relationships, encourage efficient provision of legal services, and restrict the supply of lawyers).


We recognize that the cost of our services is an important consideration for you, and we strive to provide you with outstanding value. POTTER MINTON's internal structure is designed to allow us to operate in an environment in which we can be cost effective and provide the highest value for our clients.

Id.

27. Id. (expressing that “[w]e understand the importance of responsive service . . . [t]he depth of our practice means that we are prepared to meet your legal needs efficiently and in a timely manner, even in emergency situations”).


Id.
how to react to conflict situations may result in less revenue for a law firm. The firm will decline some matters as conflict situations are identified. Client costs may increase as a result of conflict avoidance measures.\textsuperscript{29} Clients often save money by sharing the services of a single lawyer. If clients cannot use attorneys with whom they have long term relationships due to conflict concerns, they incur additional expense in educating new lawyers.\textsuperscript{30} The process of developing policies, procedures, and controls utilizes resources that might otherwise be channeled into providing legal services. The process of checking and analyzing conflicts consumes precious attorney and staff time,\textsuperscript{31} and might inhibit a law firm's ability to react in a time sensitive matter. If a conflict procedure is perceived to take too long to follow, or is perceived to be unnecessarily restrictive on freedom of action, attorneys may ignore or try to circumvent the procedure.\textsuperscript{32}

On the other hand, losses from failure to deal with conflict situations also reduce firm revenue. Lost reputation may lead to loss of clients. Malpractice settlements and judgments undermine the economic viability of the firm. "[A] conflicts program avoids potential sanctions, disgorged fees, malpractice judgments, and higher professional liability insurance premiums."\textsuperscript{33} Taking a lax position

\begin{itemize}
  \item \textsuperscript{29} \textit{Restatement (Third) of the Law Governing Lawyers} § 121 cmt. b \textsuperscript{(2000)}.
  
  \item \textsuperscript{30} \textit{Id.}
  
  \item \textsuperscript{31} See Rochelle Cheifetz, \textit{Asking All the Right Questions: Researching Possible Conflicts of Interest}, LLRX.COM, at http://www.llrx.com/extras/conflicts.htm (last visited Mar. 12, 2002) (offering a humorous and insightful discussion of the overhaul of a conflict of interest system).
  
  As in many firms, the amount of work [necessary to conduct conflicts checks] has increased. A corresponding increase in the request for conflict research has kept the Conflict Researcher more than just a little busy. And, as in most firms, the budget hasn't increased. I was able to get permission to have a student work with the Conflicts Researcher for 10 hours a week. I also have one of our Summer Interns assigned to that area. I'm still trying to get additional staff.
  
  \textit{Id.} LLRX.com is the Law Library Resource Xchange and often has interesting articles on law firm technology. LLRX.COM, at http://www.llrx.com (last visited Apr. 22, 2002).
  
  \item \textsuperscript{32} See Rochelle Cheifetz, \textit{Asking All the Right Questions: Researching Possible Conflicts of Interest}, LLRX.COM, at http://www.llrx.com/extras/conflicts.htm (last visited Mar. 12, 2002) (stating that "[w]e weren't 'just' running the names through the system so a search didn't take 15 minutes anymore . . . . When an attorney would become exasperated and cry, 'Why do you need that? It's simple, just run it through the system!' we would have to go through the explanations all over again").
  
  \item \textsuperscript{33} Robin Dearmon, \textit{Mechanics and Methods of Conflict of Interest Management}, 3 No. 4 \textit{Legal Malpractice Report} 8, 9 (1992), WESTLAW 3 NO. 4 LMALR 8.
\end{itemize}
with regard to conflicts of interest may result in more clients and more time to work on the client matters, but in the long-term may result in loss of some clients and in unexpected costs to the firm.\footnote{44}{See generally \textit{Restatement (Third) of the Law Governing Lawyers} § 121 cmt. b (2000) (noting both the affirmative ethical purposes to be advanced and the competing economic and practical considerations which lead to a conclusion that "[p]rohibition of conflicts of interest should therefore be no broader than necessary").}

Once a firm’s goals, as expressed through policies, are in place, development of procedures and controls can begin. Procedures are a means to achieving policy. “Indeed, one must question whether there is any true policy decision in a sophisticated organization if there is not a plan to implement it.”\footnote{35}{Stephen R. Volk et al., \textit{Law Firm Policies and Procedures in an Era of Increasing Responsibilities}, 48 \textit{Bus. Law.} 1567, 1567 (1993), WESTLAW 48 BUSLAW 1567.} Controls are mechanisms for assuring that procedures are in fact followed. A basic conflict avoidance procedure, for example, is to compare the parties adverse to a proposed client to the database of all past and present firm clients. A control for this procedure is to prevent the attorney from billing hours until the attorney has confirmed that he has actually performed the database comparison.

In a smaller law firm, development of policies is frequently carried out by consensus of the partners or shareholders, either formally or informally. As firm size increases, work through consensus becomes more difficult. Managing partners are common at larger firms where committees often deal with various aspects of firm operations. One or more committees may be assigned to develop aspects of policies, procedures, or controls that may affect conflict avoidance. Accordingly, ethics committees are commonplace. Such committees may be charged with a quasi-judicial role in resolving difficult conflicts questions for the firm. In some cases, a single partner is given the ability to play such a role.\footnote{36}{1 \textsc{Ronald E. Mallen} \& \textsc{Jeffrey M. Smith}, \textit{Legal Malpractice} § 2.3, at 60 (5th ed. 2000).} A quality control committee with a broad charge to make recommendations regarding work quality may address issues affecting conflict avoidance.\footnote{37}{\textit{Id.}} Regardless of the structure of firm management, all three aspects of management—policy, procedures, and controls—deserve attention.
Firm management must address many issues to create conflict avoidance policy, procedures, and controls. One common tool used by firms is a database of past and current clients. Management must decide which parties and types of information it will include in a database. Controls and policies are necessary to assure appropriate use of the database. The form of new matter memoranda and controls to assure review of the memoranda must also receive attention. Additionally, procedures and controls that force attorneys to use engagement letters and non-engagement letters can minimize the likelihood of fee disputes and claims from unintended clients.

Ongoing education of firm members regarding conflict avoidance is critical. Periodically, firm attorneys and staff need to be reminded of the reasons for procedures. In addition, attorneys and staff need to be alerted to new developments in the law of conflicts just as critically as they are educated in their areas of expertise.

To ensure the success of a conflict avoidance plan, management must devote resources to conflict avoidance. Attorneys who do not participate in such functions also need access to such resources when faced with unique conflict situations. Such resources may include publications, online research capabilities, and seminars regarding legal and technological developments related to conflict avoidance. Often, state law requires that insurers provide loss prevention materials to insureds and privileges may attach to discovery of information provided by insurers.

Even when conflict procedures and controls are perfect on paper, one additional element is essential within a law firm to assure proper use of those controls—an environment fostering respect for the ideal of conflict avoidance, as well as for the procedures and the controls used to carry out that policy. This environment should dissuade any characterization of the procedures and controls as hindrances to economic or other goals. Of course, permit-

38. See Tex. Ins. Code Ann. art. 5.15-3 (a)-(b) (West Supp. 2002) (requiring insurers offering professional liability insurance to provide loss control information).

39. See id. 5.15-3(f) (precluding loss control information from discovery and admission as evidence).

40. See Karen K.H. Bell, Managing Conflict of Interest Situations, at http://www.practicepro.ca/pmatica/conflict.pdf (last visited Mar. 20, 2002) (asserting that a conflicts checking system only succeeds where there “is a commitment to use the conflict checking system by every member of [the] firm”).
ting occasional exceptions should be discouraged. If exceptions are made for senior firm members, the message sent to junior firm members may be that the bureaucracy of conflict avoidance procedures can be safely ignored.

B. Conflict Checking and Client Screening

The first line of defense against a conflict of interest claim is a system for checking for potential and actual conflicts prior to the beginning of representation. A conflicts check is the process of identifying the persons whose interests an attorney must consider, and determining whether those interests require action in order to avoid conflict related claims. The following discussion reviews the key elements of a conflicts checking system and the degree to which such a system can effectively avoid conflicts claims.

1. Whose Interests Should Be Analyzed

The search for potential conflicts of interest begins with understanding the interests of the attorney and client, and must extend to understanding their relationships with various people and entities. Attorney interests which could conflict with client objectives include law firm, family, business, and other interests.\(^4\) The attorney and all firm members have a responsibility to avoid representation that violates ethical duties.\(^4\) Consequently, attorneys must avoid representation where confidential information may be shared\(^4\) and where the objectives of one client’s representation conflicts with the objectives of another client.\(^4\) Similarly, client interests which could conflict with attorney interests can include the interests of a number of additional persons.

The list of persons and entities that may have material differences in objectives is quite long and goes beyond the commonly assumed roles of attorneys and their clients.\(^4\) In an article describ-
ing persons who may need to be in a conflicts database, the Oregon Professional Liability Fund lists the following groups, emphasizing that their list is incomplete:

1. **Litigation**: Insured, Plaintiff(s), Defendant(s), Insurer, Guardian Ad Litem, Spouse, Expert Witness(es), Lay Witness(es).

2. **Corporate**: Owner, Spouse, Buyer(s), Partner(s), Shareholder(s), Subsidiaries, Affiliates, Opposing Party, Seller(s), Officer(s), Director(s), Key Employees.

3. **Probate**: Deceased, Spouse, Children, Heirs, Devisees, Trustee(s), Guardian(s), Conservator, Personal Representative.

4. **Estate Planning**: Testator, Personal Representative, Spouses, Children, Heirs, Devisees, Trustee, Guardian.

5. **Dissolution**: Client, Children, Spouse, Grandparents.

6. **Criminal**: Client, Witness(es), Co-defendant(s), Victim(s).

7. **Workers' Compensation**: Injured Worker, Employer, Insurer.

8. **Bankruptcy**: Client, Creditors, Spouse.

9. **Your firm**: All Lawyers, Employees, Spouses, Parents, Siblings, In-laws.

10. **Other**: Declined Clients, Adverse Parties, Prospective Clients.46

As well, the following general classes of persons, in addition to attorneys and clients, may have interests that need to be considered in analyzing potential conflict situations.

a. **Non-attorney Staff Members**

Partners and lawyers having supervisory authority must take reasonable steps to assure that non-attorney staff members do not act

in a manner incompatible with the ethical obligations of the firm and its constituent attorneys. As agents of the law firm, legal assistants must conform to the same ethical obligations as the firm.

b. Prospective Clients and Declined Clients

Communications between a person seeking legal representation and the attorney considering the possibility of representing that person fall within the scope of the attorney-client privilege. For that reason, attorneys must consider the interests of prospective and declined clients who pass confidential information to the firm. If a law firm does not represent a client, but is "marketing" for possible later representation, the firm should develop a method of tracking such activities. Even if the firm receives no confidential information, the firm could be embarrassed if it accepts other conflicting representation in the midst of the marketing effort.

c. Former Employers of Attorneys and Staff

Knowledge of client confidences is imputed to all associated lawyers of the law firm. Consequently, when one firm member joins another firm, the knowledge of that attorney can be imputed to the new firm. Similar considerations apply to staff who have worked at one firm and moved to another. While mechanisms to avoid such sharing of confidences may make it possible for a firm to represent

---

47. See Model Rules of Prof'l Conduct R. 5.3 (2001) (charging supervising attorneys with oversight and responsibility to answer the ethical conduct of nonlawyer assistants).


50. Id. § 123 (establishing that law firm employees who are not attorneys owe duties of confidentiality as agents of the lawyer). However, the knowledge of a non-lawyer employee is not imputed to subsequent firms for which the non-lawyer employee may work. Id. Even though there is no imputation of knowledge to the new law firm, any actual sharing of knowledge is prohibited. See id. § 124 (discussing situations in which the imputation is removed).

51. See Phoenix Founders, Inc. v. Marshall, 887 S.W.2d 831, 835 (Tex. 1994) (holding that screening a legal assistant from a case eliminated the need to disqualify a law firm).
a client in a particular situation, the firm must have a way of identifying which situations may call for such procedures.

d. Attorneys for Other Parties

Law firm membership is very fluid.\textsuperscript{52} Because an adverse lawyer or a lawyer representing a client with a potentially conflicting interest might join a law firm at any time, firms need to track which attorneys represent opposing or potentially conflicting interests.

e. Business Interests of Attorneys and Staff

When a firm member has an interest in a business venture that competes with a client, the possibility of impermissible conflict is evident.\textsuperscript{53} Even when the firm member has a business interest that is at present aligned with that of the client, a potential for a harmful conflict exists. For example, if an attorney is a shareholder in a corporate client, the attorney may be in a position to benefit from shareholder litigation asserting that the client violated securities laws by failing to disclose important information.\textsuperscript{54}

f. Adverse Parties

Representation in related matters can be easily overlooked if an adverse party is not tracked. For example, a potential conflict arises if one lawyer in a firm has sued an adverse party for damages and the adverse party consults with another firm member regarding asset protection planning.

\textsuperscript{52} See Robert W. Hillman, Professional Partnerships, Competition, and the Evolution of Firm Culture: The Case of Law Firms, 26 J. CORP. L. 1061, 1065-66 (2001) (discussing the mercurial nature of a law firm’s make up).

\textsuperscript{53} See \textit{Restatement (Third) of the Law Governing Lawyers} § 125 cmt. c (2000) (discussing personal and financial conflicts of interest).

\textsuperscript{54} Problems other than pure conflict problems can arise in such circumstances. For example, a firm attorney may have civil and criminal liability for insider trading based on knowledge a firm member obtains from working on client matters. \textit{See} Securities Exchange Act, 15 U.S.C.A. § 78t-1 (1997) (prohibiting trading based upon nonpublic information).

Any person who violates any provision of this chapter or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information shall be liable in an action in any court of competent jurisdiction to any person who, contemporaneous with the purchase or sale of securities that is the subject of such violation, has purchased . . . or sold . . . securities of the same class.

\textit{Id.}
g. Co-plaintiffs and Co-defendants

Parties who appear to be formally aligned in a litigation matter with a client may nonetheless have a different objective with regard to representation.\textsuperscript{55} Co-plaintiffs may have potential claims against each other or may be competing for a limited pool of funds, such as a small insurance policy.\textsuperscript{56} Conversely, it is common for co-defendants to assert that another co-defendant should bear all liability. In fact, plaintiffs often hope that co-defendants will blame each other for the plaintiffs’ damages.\textsuperscript{57}

h. Allies

As with co-parties in litigation, the positions of persons with seemingly similar interests in transactions may actually differ significantly. For example, it is not uncommon for partners to make different contributions to a partnership. Issues regarding valuation of partnership interests may arise.\textsuperscript{58} As well, parent and subsidiary entities can have differing interests.\textsuperscript{59} In the representation of entities, there is almost always a potential for the constituents of the entity to have interests that differ from those of the entity.\textsuperscript{60}

i. Family Members

Family relationships change suddenly, often with little warning. Given the risk of divorce, attorneys can never assume that members of the same family have identical interests. For example, husbands and wives do not always share the same interests in estate planning.\textsuperscript{61} Family members may have differing interests for purely economic reasons as well. If two family members are in the same car accident, one might be hurt in a different way and might require more or less compensation than the other. One family

\begin{itemize}
  \item \textsuperscript{55} Restatement (Third) of the Law Governing Lawyers § 128 cmt. d (2000).
  \item \textsuperscript{56} Id.
  \item \textsuperscript{57} Id.
  \item \textsuperscript{58} Id. § 130 cmt. a, illus. 4 & 5.
  \item \textsuperscript{59} Id. § 131 cmt. d.
  \item \textsuperscript{60} Restatement (Third) of the Law Governing Lawyers § 131 cmt. c, e, & f (2000).
  \item \textsuperscript{61} Id. § 130 cmt. c, illus. 1 & 2.
\end{itemize}
member may even assert a cause of action against another family member.\(^{62}\)

j. Third Parties Financing Representation

In a number of circumstances, non-clients will fund representation of clients. Such situations include defense of insureds under an insurance policy or defense of a constituent of an entity. In these situations, the law includes protections for the client against the influence that the third party attempts to exercise by virtue of the power of the purse.\(^ {63}\)

Clearly, there are numerous parties whose relationships may create conflicts of interest for a party. In order to avoid such conflicts, all of these relationships and interests must be considered.

2. When Interest Needs to Be Evaluated

The timing of the evaluation of potential conflicts of interests is very important. The disciplinary rules require disclosure of potential conflicts of interest prior to the commencement of the potentially conflicting representation.\(^ {64}\) Certainly, an attorney has a better chance to take action to avoid an actual conflict, or to decline further representation where appropriate, if the potential for conflict is detected as early as possible.\(^ {65}\) However, even after the initial evaluation and commencement of representation, a potential conflict can occur at any phase of representation.

Some potential conflicts may be obvious simply from knowledge of the parties whose interests are being compared. To avoid ethical

\(^{62}\) See Vincent R. Johnson & Alan Gunn, Studies in American Tort Law 801-807 (2d ed. 1999) (discussing the erosion, and in some cases, outright elimination of family immunities from tort liability).

\(^{63}\) See generally Todd R. Smyth, Duty of Insurer to Pay for Independent Counsel When Conflict of Interest Exists Between Insured and Insurer, 50 A.L.R. 4TH 932, 935-36 (1986) (noting that protections afforded are not consistent from state to state and may be governed by a combination of statutes, ethics opinions, and case law). Some states view both the insurer and insured as clients under Model Rule 1.7(a) or (b), while others view the insurer as a third party paying for the client-insured's legal costs under Model Rule 1.8(f). Id.

\(^{64}\) Model Rules of Prof'l Conduct R. 1.7 cmt. 1 & 2 (2001) (requiring attorneys to decline to work on matters involving impermissible conflicts and mandating withdrawal if an impermissible conflict arises during the course of representation).

\(^{65}\) Robin Dearmon, Mechanics and Methods of Conflict of Interest Management, 3 No. 4 Legal Malpractice Report 8, 9 (1992), WESTLAW 3 NO. 4 LMALR 8.
violation and malpractice claims, attorneys need to evaluate the potential for conflicts of interest immediately upon the first contact with a prospective client, prior to receiving confidential information. This suggests a need for a preliminary screening of all prospective representations based on the most basic of information, such as the name of the potential client, obviously adverse parties, and the general area of concerns involved in representation.

Once confidential information is obtained from the prospective client, the matter should be evaluated once again, taking into account any additional parties whose interest may be involved. If the prospective client becomes an actual client, the attorney must assess potential conflicts of interest that arise during the course of the representation. As new parties in the matter appear, and as the interests of the client, attorneys, and the firm change, the potential for conflicts of interest must be addressed again. This continuing need to address potential conflicts of interest is manifested in all types of representation, litigation or transactional. For example, in personal injury cases, investigation may reveal new, potentially responsible, parties. Sources of insurance for payment of a judgment may also be discovered. In a real estate transaction, a lender may be added or an engineering firm may be secured to help with analysis of a site plan. As such parties appear, the potential for conflicts of interest between the client and these parties may require additional evaluation.

Current clients often ask attorneys to take on matters that constitute new representations requiring a different conflict analysis. Vinson & Elkins, L.L.P.'s representation of Enron illustrates this
situation very well. In the course of representing Enron, Enron officials asked Vinson & Elkins to investigate the legality of actions taken by certain Enron officials.70 An Enron employee, recognizing the potential for conflict, sent a letter suggesting that Vinson & Elkins not conduct the investigation.71 Nevertheless, Enron hired the firm to carry out the investigation.72 A spokesman for Vinson & Elkins stated that the law firm “was not asked to examine [their] own legal work.”73 As the spokesman’s comment implies, investigation of the validity of the firm’s own legal work would pose a potential conflict of interest. When a client asks its attorneys to evaluate the law firm’s own work, the attorneys and the firm have a motive to find that the work was proper, thus avoiding a possible malpractice claim. Clearly, this presents an avoidable conflict.

A situation that requires a reevaluation of potential conflicts is the hiring of new lawyers and staff by a law firm.74 When attorneys and staff change firms, their new firms need to determine a way to check potential conflicts stemming from their old firms. A former firm may quite legitimately refuse to provide potential access to confidential client information that may be part of a conflicts system to an attorney who is no longer associated with that firm. Less defensible, but a reality nonetheless, is a law firm’s refusal to provide information which may allow the departing attorney to compete with the former firm. If the new firm has tracked opposing counsel and counsel for other parties in its matters prior to making a lateral hire, many of these difficulties may be avoided.

3. Acquiring Sufficient Information to Perform the Analysis

Information sufficient to perform a meaningful analysis of potentially conflicting interests can be obtained in a number of ways. This section considers the advantages and limitations of each of these methods, explaining how a combination of methods improves the likelihood that conflicts will be detected. As a starting point, attorneys and staff members possess some level of knowledge of

71. Id.
72. Id.
73. Id.
AVOIDING LEGAL MALPRACTICE CLAIMS

past and present conflicts. With this knowledge, attorneys should recognize some potential conflicts without consulting other sources. Attorneys should also impress on staff members the importance of identifying and dealing with conflicts. This instruction enables staff members to assist attorneys in identifying potential conflicts.

a. Database and Software Methods

In general, relying on memory and training alone is not sufficient to assure that an attorney has the information necessary to avoid conflicts of interest. A common question on malpractice insurance applications asks for a description of methods used to avoid conflicts. Solo attorneys often answer by noting that they rely on memory alone. Reliance on memory proves dangerous for several reasons. As an attorney ages or his or her health changes, memory may become less certain. Failure to maintain some type of list of

75. See A.B.A., 1999 Legal Technology Survey Report, 146-47, 300-01 (showing that 54.43% of surveyed firms used conflicts of interest checking software). By category, 53.28% of solo firms used such software, as did 56.10% of small firms averaging five lawyers, 60% of medium sized firms with an average of 44 lawyers, and 85.71% of large firms with an average of 239 lawyers. Id. “Database” usually connotes a computerized method. See Gerry Malone, The Malpractice Crisis: What Can You Do About It?, THE DOCKET, Jan.-Feb. 1987, reprinted in TEX. LAWYERS' INS. EXCH., Conflict of Interest Systems, at 1 (on file with the St. Mary's Law Journal). Index card systems are no doubt still in place in some firms, and when properly used would assist in detection of conflict of interest issues. Id.; see also LawCommerce.com, Top Legal Software, at http://www.lawcommerce.com/emarketplace/dir_software_vendors.asp (last visited Mar. 12, 2002) (providing a hyperlinked list of law office software that may have some of the features discussed in this section).

76. See TEX. LAWYERS' INS. EXCH., Electronic Forms, at http://www.tlie.org/forms/newpkg.rft (last visited Mar. 12, 2002) (requiring a set of questions for new clients). One question in particular asks:

22. Does the applicant have written policies regarding avoidance of conflicts of interest?

[ ] YES [ ] NO

If yes, provide copies. Please include policies regarding business dealings with clients and service as an officer or director for a client.

If no, describe the methods used to avoid conflicts of interest, or check which of the following methods you use:

[ ] Memory [ ] Discussion with other firm members [ ] Computer [ ] Index files
[ ] Interoffice Memos.

Id.

parties with potentially conflicting interests could make it difficult for a solo attorney to join other lawyers in a firm. Informal methods of sharing information, such as simply orally asking the other attorneys in the firm whether they know of any problems with anticipated representation, become tenuous as more attorneys work together. Consultation of a list of parties, at the very least, may reveal the need for additional research or analysis that would not occur with reliance on memory alone.

The consultation of databases of information regarding parties, and particularly clients, has become a standard method of conducting "conflicts checks." These databases are helpful, but are not foolproof. Consider first the scope of information that is put into such a database for a firm. As noted above, there are many types of parties, other than attorneys and clients, who may have potentially conflicting interests that should be evaluated. Too often, the database maintained by firms is no more than a client list.

Some firms rely on their accounting system for conflict information. Unfortunately, such systems may only include the person paying the bills, but no information on the client. A field for the

that memory loss can be associated with many causes, including aging, Alzheimer's, head injuries, strokes, drug and alcohol use, and brain disorders); see also The Online Allergy Center, Symptoms, at http://www.onlineallergycenter.com/symptoms/ (last visited Mar. 27, 2002) (stating that even allergies can result in short term memory loss).


79. Rochelle Cheifetz, Asking All the Right Questions: Researching Possible Conflicts of Interest, at http://www.llrx.com/extras/conflicts.htm (last visited Mar. 12, 2002). Cheifetz describes the process her firm followed until they revised their system:

[1] The attorney (or secretary) filled out the Conflict Search Request form and send (sic) it to the appropriate MIS person.
[2] The names were run through the Conflict Database and the printout was sent back to the attorney, who would have to review it to see if there were any "conflicts." If there were, that attorney would contact the responsible attorney for the client posing the possible "conflict." They would then discuss and clear up the conflict. Waivers were obtained when necessary.
[3] The Conflict Search Request would then be attached to New Billing Client/Matter Form and find its way to Accounting, where a client/matter number would be assigned and the data input into the Accounting System, which fed into the Conflict Database.

Id.

80. See id. (stating that the firm relied on the accounting system for entry of conflict information).
description of the matter might include the style of the case, and thus adverse parties. However, in an audit conducted by one of the authors of this Article, the space for adverse parties was limited so “et al.” was commonly used in lieu of listing all parties to the litigation. Such a database falls short of the type necessary to reveal the basic information needed to evaluate the potential for conflicts of interest.

A conflicts database should contain detailed information about clients, as well as information about non-clients, when appropriate. Generalized contact management software allows entry of contacts of many types, and could conceivably be used to store a conflicts database. However, such software may have to be customized to allow entry of the complex relationships that may be involved in legal representation. Case management software may also be of use in the conflicts checking process. This software often contemplates searchable entry of witnesses and other persons related to a representation that might not be entered into a simple client list. Case management software may be generalized for use by all types of attorneys, or may be tailored for a narrow practice area. In a diversified firm, however, the case management software for one practice area might not be suitable for other practice areas. If specialized case management software does not accommodate all areas of firm practice and cannot be integrated with generalized case

81. Contact management software, which may also go by the names of customer relations management software (“CRM”) or personal information manager (“PIM”) describes a broad range of programs. Ed Poll, CRM Solutions for Small Firm Budgets, at http://www.lawcommerce.com/smallfirm/qa_edPoll.asp (last visited Mar. 30, 2002) (describing that such programs attempt to provide the user with physical addresses, phone numbers, and email addresses for all “contacts”). Common additional features include calendars, scheduling, and email storage and retrieval. Id. Some of these programs permit the user to group contacts into classifications with a comment field that could be utilized for conflicts research. Id. Sophisticated CRM programs also allow analysis of marketing efforts. Id. Examples of generalized contact management software that might be used by a law firm include Microsoft Outlook, Act!, and Goldmine. Id.

82. Most generalized case management software is offered by vendors who may offer other integrated modules, often including a conflicts module. See Abacus Law, What are the Most Popular Features of Abacus Law, at http://www.abacuslaw.com (last visited Mar. 30, 2002) (offering both litigation and non-litigation case management modules). Often the primary purpose of case management software is management of a particular kind of practice. See also The Plaintiff, Software Specifically for Plaintiff Attorneys, at http://www.theplaintiff.com/software.html (last visited Mar. 27, 2002) (describing software that focuses on coordinating information used in a plaintiff attorney’s practice).
management software, the firm may need to consider purchase or development of conflict of interest software.

For economic efficiency and encouragement of proper use of conflict checking software, any conflict checking software should be integrated with other firm software. For example, if the name of a client is entered into the system in order to set up a file for the client, that name should not have to be reentered into another system to allow future conflict checking. Ideally, accounting, billing, case management, and conflict checking software packages should allow seamless sharing of information.83

Whether conflicts reviews are conducted using a manual or computerized system, their effectiveness depends largely on the data included in the system and the diligence of attorneys in following established procedures. It is commonly said that "a conflicts check can only be as good as the information entered in the system."84

Various cases illustrate how insufficient or incorrect information contributes to a firm’s failing to detect conflicts during routine checks. Conflicts cases involving information mistakes or lapses include situations involving data entry errors, such as misspellings of names. In one unreported Texas case, an attorney-arbitrator ran a conflicts check on the parties involved in arbitration.85 Unfortunately, the attorney erroneously used the name “Texacoma” instead of “Texakoma,” the proper name of the party.86 Because of the misspelling, the conflicts check did not reveal that the attorney’s firm previously represented a client in litigation against Texakoma.87

83. See generally Steven Schmidt, PCLawPro Version 5.51, at http://www.pclaw.com/news/lot_pclawpro_2001.htm (last visited Mar. 12, 2002) (reporting that “a law firm should only have to enter information once . . . . [n]ot once in case management software, then once in time and billing software and once more in accounting software”). “However, the problem with software that does everything is it usually doesn’t accomplish individual tasks as well as more specialized software.” Id.


86. Id. at *2.

87. See id. at *4 (noting that the court, in concluding that the adverse interest should have been disclosed, set aside the arbitration award, because, in the court’s opinion, the failure to disclose evidenced partiality).
Sophisticated technology can compensate for certain types of database errors. For example, the use of soundex searches helps avoid certain types of name confusion.\(^8\) Soundex searches rely upon phonetic similarity of names rather than exact spelling.\(^9\) For example, searching for “Smith” using a soundex method will find “Smyth,” “Smithe,” and “Schmidt.”\(^9\) However, soundex searches do not find all possible misspellings of names, and in some circumstances may return voluminous results. Still, combinations of technology in data retrieval software can minimize the errors that may find their way into databases.

In addition, lag time in the entry of information creates obstacles in using the database. Some of this problem may be alleviated with appropriate controls, but not all lag time can be overcome in this manner. For example, the firm could prevent billing a client until completion of a conflicts check. No control, however, can address all possibilities, such as the need of attorneys to input names of their new spouses or new investments.

Maintenance of attorney investment information in a database could be a sensitive issue for a law firm. An argument can be made that investments in publicly traded companies do not usually pose a risk of a conflict claim. As discussed below, the risk of a serious conflict grows as the size of firm member holdings increase. Regardless of the size of interest, the database should indicate when firm members are officers, directors, trustees, or employees of entities.\(^9\)

The scope of information included in the database affects how well it helps to avoid conflict claims. One article recommends

\(^{88}\) See Conflict Checker Software, at http://www.seabill.com/cc.html (last visited Mar. 12, 2002) (using “Sound Alike Sleuth” to find “names that sound like other names, even if the spelling is different”).

\(^{89}\) See EMILY ANNE CROOM, THE GENEALOGIST'S COMPANION AND SOURCEBOOK 16 (1994) (noting that soundex coding was first developed to assist in indexing census information in 1880). Soundex coding recognizes that there are six consonant groups with very similar sounds and that all the vowels are frequently confused. Id. The consonants y, w, and h are ignored unless they are the first letter of a name. Id. Doubled letters and letters repeated from the same group are ignored. Id.

\(^{90}\) Robin Dearmon, Mechanics and Methods of Conflict of Interest Management, 3 No. 4 LEGAL MALPRACTICE REPORT 8, 8 (1992), WESTLAW 3 NO. 4 LMALR 8.

\(^{91}\) RONALD E. MALLEN, THE LAW OFFICE GUIDE TO PURCHASING LEGAL MALPRACTICE INSURANCE 77 (Robert J. Romero ed., 1999) (explaining that claims directly arising out of such positions are usually excluded by malpractice insurance). Coverage for law services to such entities may be excluded as well. Id.
twenty different pieces of information that should be recorded in a central database for each client, with additional information required for entities, attorneys and staff, and key vendors for the law firm. Although a database requiring too much information could slow firm processes unnecessarily, thorough and comprehensive information "makes it much easier to quickly assess the seriousness of a potential conflict." A database is often only a starting point for analyzing the potential for conflict. For example, in a situation where the database reveals that a proposed client wants the attorney to sue a current client of the firm, the disciplinary rules generally do not require that the attorney refuse to engage in the proposed representation if there is no substantial relationship between the two matters. In such a situation, the database simply indicates a need for analysis of other information, such as firm files and information that firm members working on the matter have obtained informally.

Perhaps the most difficult type of potential conflict to identify through a database is a positional conflict. A positional conflict is one in which clients, whose interests are not otherwise adverse, are affected differently by different interpretations of the law. The classic example of a positional conflict is one in which one client of the firm takes one position on appeal and another client takes the opposite position. While such conflicts may not rise to a level where they require action under the disciplinary rules, it is not uncommon for corporate clients to demand that law firms refrain from representing competing positions, regardless of whether the

92. A.B.A. LAWYER'S DESK GUIDE TO PREVENTING LEGAL MALPRACTICE 80, 81 (2d ed. 1999). The suggested information includes client name, social security number, matter name, attorneys and staff members who work on the matter, a description of the matter, known parties with conflicting or potentially conflicting interests and their relation to the client, other professionals serving the client, file status, opposing counsel, date file opened, date representation commenced, file number, date conflict check requested, date initial conflict check cleared, firm member confirming conflict check, date of file closing and destruction, date representation ended, and comments. Id. at 80.


94. MODEL RULES OF PROF'L CONDUCT R. 1.7(b) (2001).


96. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 128 cmt. f, illus. 5 & 6 (2000).
disciplinary rules mandate disclosure and consent. 97 Not only will computers fail to determine all the positions that have or will be taken by different clients, but the entry of all potential legal positions is simply impossible. 98

Limiting practice to narrow areas can reduce the chance of positional conflicts for some law firms. For example, if a firm only defends or prosecutes personal injury actions, the firm reduces the chance that it will take opposing positions interpreting statutes of limitation. However, the possibility of conflicts is not entirely eliminated. In pursuing a cross claim, a defense firm may need to assert that the statute of limitation has not run in a particular case. Conversely, a counterclaim against a plaintiff may force a plaintiff’s firm to consider a statute of limitation defense that is contrary to the legal positions taken on behalf of other clients.

More and more firms are engaging in research beyond data contained in firm databases and files. Some law firms now research clients in a number of ways, including performing background and credit checks, or monitoring certain external databases for evidence of potentially conflicting interests. These efforts help fill in gaps as clients often give less than complete information to their lawyers, sometimes out of ignorance or negligence, and sometimes intentionally. The volume of information available regarding corporate clients may warrant use of external data. 99 External databases can directly update or supplement in-house conflict


98. Cf. Jett Hanna, Loss Prevention for AnyLawFirm.com, 5 LPL ADVISORY 2, (ABA Standing Comm. on Lawyers’ Prof’l Liab.) Fall 2001, at 3 (on file with the St. Mary’ Law Journal) (indicating that computers can perform legal analysis, as well as help sort out the various positions taken by clients). E.g., Texas Last Will & Testament, at www.txwills.com/ (last visited Mar. 17, 2002) (allowing a client to answer questions and receive a will after answering a series of questions). However, such software does not perform a complete legal analysis under every conceivable scenario. Id. Exceptions to an expected pattern of answers prevent the client from receiving a will. Id.

99. Robin Dearmon, Mechanics and Methods of Conflict of Interest Management, 3 No. 4 LEGAL MALPRACTICE REPORT 8, 9 (1992), WESTLAW 3 NO. 4 LMALR 8 (suggesting that Dun & Bradstreet databases may be useful in researching potential corporate conflicts); see also Rochelle Cheifetz, Asking All the Right Questions: Researching Possible Conflicts of Interest, at http://www.llrx.com/extras/conflicts.htm (last visited Mar. 12, 2002) (stating that “[w]e had to explain [to attorneys] why we had to research a particular company and its subsidiaries so the process would take longer than before”).
software. Interestingly, a recent discussion with an ethics partner at a large Midwest law firm indicated that outside research of clients and interests has become an important part of that firm’s conflicts avoidance procedures.

One author recently opined that “[n]ew conflict-tracking software must be further developed to overtake the database as the primary computerized means of tracking client conflicts.” This recommendation appears to confuse the software that utilizes databases with the data in the databases. Databases are collections of data that can be accessed, updated, compared, and analyzed by software, but are distinct from programs and software. Databases contain the raw information upon which software performs manipulations. Undoubtedly, the manner in which the data is manipulated by software to assist conflict analysis can be improved, but the logic of such manipulations still depends upon models of analysis developed by humans and translated into software. “[S]oftware is a tool and not a solution,” and human factors will continue to affect the functioning of all conflict avoidance measures.

100. Wendy R. Leibowitz, Client Conflict Software: No Panacea, Nat’l L.J., July 21, 1997, at A13 (stating that a representative of one software company providing conflicts software indicated that “new versions of the software may allow the data to be updated continuously via a Dun & Bradstreet or Standard & Poor’s news service”).

101. As with some of the information in this Article based on law firm audits, the actual source of this information is being kept confidential.

b. Firm Discussion of Matters: New Matter Memoranda

This section of the Article began by noting that the knowledge and memory of individual attorneys and staff cannot assure proper conflict detection. However, given the limitations of conflicts of interest software, knowledge and memory must not be ignored. As one general counsel for a large law firm put it, "I don't know what kind of software you could ever purchase that would replace that intake meeting every week." Firms can use a number of methods to tap this reservoir of personal knowledge and institutional memory.

In smaller firms, daily or weekly conferences where lawyers discuss potential and pending matters can help avoid conflict situations. One attorney may identify a problem which another attorney does not have sufficient information or insight to recognize. As firm size increases, however, circulation of new matter memoranda often substitutes for the whole-firm meeting.

Typically, all attorneys in a firm are to review memos outlining potential new representations to confirm that they do not perceive a potential problem with the representation. The circulation of a conflicts memorandum provides additional protection because individual attorneys may be able to recognize conflicts not revealed in checking data in either a manual or computer system. In underscoring the importance of conflicts memoranda, one court explained that "[t]here is no substitute for the actual circulation of conflicts memos to determine whether [there] are any disqualifying conflicts that do not appear in the computer database."

Of course, circulation of new matter memoranda is only effective if all attorneys in the firm seriously review them. Difficulties in

---

methods and devices . . . will represent an ideal solution." Id. Drucker addresses "intake sheets," but appears to confuse client information provided at intake with new matter memoranda. See id. at 559 (describing the basics of "intake sheets").

105. The source of this information is being kept confidential.

106. See A.B.A. LAWYER'S DESK GUIDE TO PREVENTING LEGAL MALPRACTICE 80 (2d ed. 1999) (noting guidelines to prevent conflicts of interest).


108. See A.B.A. LAWYER'S DESK GUIDE TO PREVENTING LEGAL MALPRACTICE 82 (2d ed. 1999) (recommending review of "new matter sheets" by all attorneys and staff within twenty-four hours). The authors know that this is not the common manner of dealing with new matter memoranda in larger firms, though it may work in a smaller firm. More typical is a rule that assumes there are no conflict objections if no attorney has voiced objections within a certain time period.
the circulation process may render new matter memoranda impotent in certain circumstances. For example, an attorney on vacation may have insight regarding a particular situation that will have to await his return to the office. Similarly, the urgency of situations may require that an attorney begins representation before all attorneys respond to a new matter memorandum. Consequently, new matter memoranda should be viewed only as a partial cure for the inadequacies of databases. Obviously, all resources should be utilized to detect potential conflicts of interests. While reliance on memory alone becomes less viable due to the vast number of parties and relationships that a law firm encounters, computer software is not infallible either. A law firm should combine the strengths of the available software with human efforts to gain the best probability of avoiding conflict situations.

4. Analysis Process

Once the parties with potentially conflicting interests have been identified, someone must analyze the conflict. Analysis of a conflict involves evaluating:

1. All potential or actual conflicts;
2. The consequences of proceeding in light of the existence of a conflict;
3. Possible steps to address conflicts; and
4. The effectiveness of steps to avoid the consequences of conflicts.

This suggested analysis is somewhat broader than the minimum required by the disciplinary rules. Such an approach reflects the need to take into account all firm goals. Even when no actual conflict exists under the disciplinary rules, allegations of conflicts of interest can aggravate a malpractice claim based on a simple mistake or on oral discussions between an attorney and client.

Proper analysis of conflicts ultimately relies upon the analytical capabilities and good intentions of the persons performing the evaluation. Therefore, the training and education of the person performing the analysis is always imperative. Performing a correct

109. See generally Marilyn Lindgren Cohen, Do You Have a Conflict? Take This Self-Quiz to Find Out, 56 OR. ST. BAR. BULL. 33 (1996), WESTLAW 56-MAY ORSBB33 (providing an example of a disciplinary rule-driven analysis).
AVOIDING LEGAL MALPRACTICE CLAIMS

analysis may require knowledge of reference materials and access to those materials.

When a conflict analysis is performed within a law firm, firm resources can enhance the opportunity for correct analysis. Firm resources may include review of conflict analysis by a senior attorney or an ethics partner. In various situations, review by an expert outside the firm may be advisable. If the firm does not have procedures for determining when conflict analysis is reviewed, the analysis that occurs, by default, is that of the individual attorney or staff member who faces the situation.

5. Appropriate Responses to Analysis

If a potential conflict exists, attorneys may choose from a range of responses. In some cases, the disciplinary rules mandate rejection of a proposed representation. As well, state or federal law may prohibit dual representation in certain criminal matters. In some situations, consent to conflicts of interest may not be an option for a client. Governmental clients may not be able to consent to conflicts of interest. Similarly, parties who are adversaries in litigation, such as divorcing spouses, cannot validly consent to con-

110. See A.B.A., Center for Professional Responsibility, at http://www.abanet.org/cpr/202report.html (last visited Mar. 22, 2002) (noting that the ABA House of Delegates recently passed a version of comments to Model Rule 1.6). The revision reads as follows:

[7] A lawyer's confidentiality obligations do not preclude a lawyer from securing confidential legal advice about the lawyer's personal responsibility to comply with these Rules. In most situations, disclosing information to secure such advice will be impliedly authorized for the lawyer to carry out the representation. Even when the disclosure is not impliedly authorized, paragraph (b)(2) permits such disclosure because of the importance of a lawyer's compliance with the Rules of Professional Conduct.

Id. The ethical posture of informal consultation with an outside attorney, or an expert such as a law professor, has been the subject of significant discussion. Whether the relationship between the outside attorney or expert is treated as an attorney-client relationship in the absence of formal engagement is not entirely clear. See ABA Comm. on Ethics and Prof'l Responsibility, Formal Op. 98-411 (1998) (treating informal consulting as an attorney-client relationship in some respects, but not others); Jett Hanna, Moonlighting Law Professors: Identifying and Minimizing the Professional Liability Risk, 42 S. Tex. L. Rev. 421, 434-44 (2001) (arguing that professors, when not explicitly engaged as attorneys, are similar to legal assistants and treated as such under rules of agency, unauthorized practice statutes, and disciplinary rules).

111. See Restatement (Third) of the Law Governing Lawyers § 122 cmt. g (2000) (discussing when representation is prohibited by law).

112. See id. (explaining the extent to which a government client may consent to a conflict of interest).
The Restatement (Third) of the Law Governing Lawyers provides that consent is not effective in other circumstances where "it is not reasonably likely that the lawyer will be able to provide adequate representation to one or more of the clients." The Model Rules of Professional Conduct embody a similar concept: "[A] client may consent to representation notwithstanding a conflict[;] . . . however[,] . . . when a disinterested lawyer would conclude that the client should not agree to the representation under the circumstances, the lawyer involved cannot properly ask for such agreement or provide representation on the basis of the client's consent."

In other situations, nothing forces attorneys and firms to accept representation simply because a strong case can be made that the disciplinary rules permit proposed representation. An attorney can reject a proposed representation simply because the potential conflict makes him uneasy. "Based on concern about a conflict of interest under self-imposed standards more exacting than (the Restatement standards), a lawyer ordinarily may decline a representation . . . or withdraw." Similarly, if a conflict situation arises during the course of representation, the attorney is required to withdraw in certain circumstances, and may withdraw if the client is not prejudiced, even when withdrawal is not mandated.

Disciplinary rules may permit the use of certain types of mechanisms to avoid the consequences of potential or actual conflicts of interest. Disciplinary rules require disclosure of the existence of potential conflicts and consent to the representation by the affected clients in the following situations: conflicts with a lawyer's financial or other interests; business transactions between a law-

113. See id. (commenting that directly adverse parties cannot consent to joint representation).
114. Id. § 122 (2)(c).
117. See Model Rules of Prof'l Conduct R. 1.16(a) (2001) (stating that if the representation is illegal or violates disciplinary rules, the lawyer is impaired, or the client discharges the attorney, the attorney must withdraw).
118. Id. 1.16(b). Model Rule 1.16(b) provides specific grounds for withdrawal, with the most permissive allowing withdrawal when "a client insists upon pursuing an objective that the lawyer considers repugnant or imprudent." Id. 1.16(b)(3).
119. Id. 1.7(b).
yer and client;\textsuperscript{120} representation of two or more clients in the same matter;\textsuperscript{121} or representation of one client in a matter adverse to another current or former client.\textsuperscript{122}

In some situations, disciplinary rules require written consent by the client to commencement or continuation of the representation.\textsuperscript{123} Ideally, attorneys should document both the disclosure and consent whether or not disciplinary rules require such a writing.\textsuperscript{124} Written communications provide evidence of the disclosure made while reinforcing the seriousness of the decision to retain an attorney with potentially conflicting interests. Attorneys who find themselves in a "swearing match" before a fact-finder often discover that the fact-finder believes a client's version of events.\textsuperscript{125}

In any situation where a potential conflict deteriorates into an actual conflict, the attorney must complete the required disclosure and consultation. Disclosure should be made so that lay clients understand the communication, even if it is detailed. A careful lawyer must be cognizant that a defective disclosure renders consent ineffective.

Screening, popularly called "Chinese Walls," may be used in some situations to avoid imputation of conflicts of interests when lawyers change firms. The Restatement only permits screening if: (1) confidential information communicated to a prohibited lawyer is unlikely to be significant, (2) screening measures will eliminate participation in representation by the screened lawyer, and (3) notice of the screening is given to affected clients.\textsuperscript{126} Some jurisdictions, and the Model Rules, simply do not recognize Chinese Walls

\textsuperscript{120} Id. 1.8(a)(1).
\textsuperscript{121} \textit{Model Rules of Prof'L Conduct} R. 1.7(b) (2001).
\textsuperscript{122} Id. 1.7(a), 1.9, 1.11.
\textsuperscript{123} Id. 1.8(a)(3) (addressing transactions between the attorney and client).
\textsuperscript{124} Karen K.H. Bell, \textit{Lawyers' Prof'L Indem. Co., Managing Conflict of Interest Situations} 13 (1998). This booklet is produced and distributed by the mandatory insurance program for Ontario lawyers. While the sources of Canadian ethics law obviously differ in some respects from American law, the differences in conflict avoidance techniques used are minimal.
\textsuperscript{125} The general public does not hold a high opinion of the legal profession. \textit{See A.B.A., Perceptions of the U.S. Justice System} 50 (1999), at http://www.abanet.org/media/perception/perceptions.pdf (discussing survey results that indicate only 14\% of persons surveyed were extremely or very confident in lawyers). The odds are that only a few attorneys will be in any given jury pool, and it is likely that the plaintiff in a legal malpractice case will use preemptory strikes to eliminate lawyers from the jury panel completely.
\textsuperscript{126} \textit{Restatement (Third) of the Law Governing Lawyers} § 124(2) (2000).
as sufficient cures for the threat of breach of confidentiality.\textsuperscript{127} In addition, deciding to have a Chinese Wall requires effective implementation. Cracks in the wall may risk both breaching confidentiality and representing conflicting interests.

A potentially unappreciated byproduct of a conflicts analysis is that a given situation may demonstrate a need for a procedure or policy to avoid similar conflict situations. Accordingly, law firms should create procedures to solicit comments from attorneys and staff regarding problems that do not appear to be addressed by the conflicts system.\textsuperscript{128}

C. Engagement Letters and Contracts

The adoption of firm policies and procedures requiring documentation of all representation can avoid conflict claims.\textsuperscript{129} The use of engagement letters and client contracts can prevent future conflicts. Clients should sign an engagement letter or a contract which sets forth the services that the attorney will provide and the manner in which the firm will be compensated.\textsuperscript{130} If a third party is to pay for the representation, then the third party should receive notice that the third party is not the client. Other third parties who are not represented by counsel and who may have some reason to believe that the attorney is representing their interests should re-

\textsuperscript{127} See Petroleum Wholesale v. Marshall, 751 S.W.2d 295, 301 (Tex. App.—Dallas 1988, no writ) (opining that "the erection of a Chinese wall does little to dissipate the public's perception of the appearance of professional impropriety, because, in the end, the public has no way of knowing whether a breach in the Chinese wall might ever occur"); see generally Mark Hansen, \textit{Model Rule Rehab: House Tackles Tough Issues as Ethics Debate Begins}, A.B.A. J., Oct. 2001, at 81 (noting that the ABA House of Delegates rejected a proposal by the ABA Ethics 2000 commission that would amend the Model Rules to allow screens).


\textsuperscript{129} Other types of ethics questions and claims can also be avoided by documenting the nature of representation. If the scope of representation is properly documented, the attorney may be able to demonstrate that all requested services were performed in the face of an allegation that the attorney should have performed additional services. If the fees are clearly stated at the outset of representation, the client is less likely to balk at paying fees because of disagreements over what the fee agreement was.

\textsuperscript{130} \textit{Model Rules of Prof'l Conduct} R. 1.5(c) (2001) (strongly encouraging the use of written fee agreements); \textit{id.} 1.5(b) (stating that fee agreements should be communicated "preferably in writing").
ceive written notice that they are not clients and that they should seek other counsel. In particular, constituents of an entity represented by an attorney should be advised in writing that they are not clients if that is the attorney's intention. As well, persons seeking legal advice who are not accepted as clients should receive a declination in writing.

Utilizing rigorous procedures to document who is and who is not a client avoids conflict claims by minimizing the chance that someone that an attorney does not consider to be a client will claim that the attorney represents her interests. Such unintended clients may present the worst type of conflict threat. Because the attorney does not consider them to be clients, the attorney will not consider their interests when checking for and analyzing conflicts.

Controls can assist a firm in assuring proper use of engagement letters and fee contracts within the firm. In a firm where hourly billing is the norm, prevention of entry of billable time without confirmation of the existence of the fee agreement or engagement letter may be possible. Promulgation of standard engagement letters, fee agreements, disclaimers of representation, and declination letters can help firms avoid repetition of difficult situations and provide attorneys with resources to keep documentation requirements from becoming too onerous.

III. **Common Conflict Claims**

While conflicts of interests arise in a vast variety of situations, one common thread is the risk that the attorney-client relationship will suffer ill effects as a result of competing interests. As defined in the Restatement (Third) of Law Governing Lawyers, "[a] conflict of interest is involved if there is a substantial risk that the

---

131. See id. 4.3 (stating that "[w]hen the lawyer knows or reasonably should know that the unrepresented person misunderstands the lawyer's role in the matter, the lawyer shall make reasonable efforts to correct misunderstanding). The Model Rule does not mandate a writing, but does require a lawyer to correct misunderstandings of the attorney's role. Id.


133. See GEOFFREY HAZARD & WILLIAM HODES, LAW OF LAWYERING § 10.4 (2001) (stating that "a conflict of interest exists whenever the attorney-client relationship or the quality of the representation is 'at risk,' even if no substantive impropriety—such as a breach of confidentiality or less than zealous representation—in fact eventuates").
lawyer's representation of the client would be materially and adversely affected by the lawyer's own interests or by the lawyer's duties to another current client, a former client, or a third person.\textsuperscript{134} Using this definition, conflicts fall into three categories: (1) conflicts between the attorney's interests and client's interests, (2) conflicts between and among clients, and (3) conflicts involving third party interference with the attorney-client relationship. From these categories, this Article identifies common conflicts that are difficult to defend.\textsuperscript{135} Following a brief description of each type of conflict, this section suggests measures for detecting and dealing with particular conflict situations.

A. Conflicts Involving Attorneys' Entrepreneurial Activities

Without doubt, the most difficult conflicts to defend are those conflicts where the attorney's personal interest conflicts with client interests. As explained by counsel to the insurer providing malpractice coverage to the nation's largest law firms, "entrepreneurial activity by the lawyer or the law firm complicates an already difficult defense task . . . [because plaintiffs can] seize on such activities to support their claims that the defendants were careless, distracted lawyers, influenced by a personal profit motive and other conflicts of interest."\textsuperscript{136} The fundamental concern with such activities is that

\textsuperscript{134} \textit{Restatement (Third) of the Law Governing Lawyers} § 121 (2000).
\textsuperscript{135} See Mark C.S. Bassingthwaighte & Robert D. Reis, \textit{The Top Ten Malpractice Traps & How to Avoid Them}, MONT. L\textit{AW.}, Jan. 2000, at 11, WESTLAW 25-JAN MTLAW 7 (listing the most common conflicts of interest situations). The identification of particularly "troublesome" conflicts was based on the authors' own experiences in monitoring and reviewing hundreds of legal malpractice cases and grievances in which conflicts of interest were challenged. See also Mark C.S. Bassingthwaighte & Robert D. Reis, \textit{The Top Ten Malpractice Traps & How to Avoid Them}, MONT. L\textit{AW.}, Jan. 2000, at 11, WESTLAW 25-JAN MTLAW 7 (listing the following conflicts as the most common and potentially dangerous: (1) "representation of two parties in a matter," (2) "representation of opposing theories of law for different but similarly situated clients," (3) "representation of opposing sides of an issue, even though the clients are not involved with one another," (4) "personal involvement in a client's business interests," (5) "service as a director or officer of a client company," (6) "an unclear statement of non-representation in situations where a clear conflict of interest exists," and (7) "conflicts arising from law firm acquisitions and lateral hires").
“the lawyer’s independence, objectivity and judgment will be—or will be perceived to be—seriously compromised.”

When entrepreneurial activities give rise to conflicts of interest claims, juries recognize the fiduciary nature of the attorney-client relationship. Court opinions describe attorneys as fiduciaries of the “highest order,” who “owe their clients utmost good faith, fidelity, and trust when carrying out the performance of legal services.” A basic tenet of fiduciary law is that the fiduciary should not benefit at the expense of the client.

Anytime an attorney enters a business transaction with a client, there is a risk of overreaching due to the attorney’s legal skill and training, as well as the client’s trust and confidence. To avoid abuse, disciplinary rules require that attorneys take special precautions relating to business transactions with clients. If an attorney is accused of violating

137. Id. at 4.

138. A jury charge will rely on state law for defining “fiduciary” or “fiduciary duty.” See Comm. on Pattern Jury Charges, State Bar of Tex., Texas Pattern Jury Charge PJC 104.1 (2000) (providing a charge example stating that “a relationship of trust and confidence existed if Paul Payne justifiably placed trust and confidence in Don Davis to act in Paul Payne’s best interest”). More guidance may be given in the charge if desired. See generally Charge of the Court, in Mitsubishi Aircraft Int’l v. Fulbright & Jaworski, No. 401, 464-A (333rd Judicial Dist., Travis County, Tex. Feb. 27, 1989) (on file with the St. Mary’s Law Journal) (defining “fiduciary relationship” to include “those informal relations which exist whenever one party trusts and relies upon another, as well as technical fiduciary relations[, and providing that]...[t]he relationship between an attorney and his client is highly fiduciary in nature”).

139. Bruce Zucker, Attorneys Who Enter into Business Transactions with Their Clients: A Presumption of Undue Influence, Malpractice, and Impropriety, 1 J. LEGAL ADVOC. & PRAC. 7, 7-8 (1999); see also In re Lowther, 611 S.W.2d 1, 2 (Mo. 1981) (opining that attorneys doing business with clients is “wrought with pitfalls and traps and the [c]ourt is without choice other than to hold the attorney to the highest of standards”).

140. See Model Rules of Prof’l Conduct R. 1.7 cmt. 6 (2001) (noting that the lawyer’s interests should not adversely affect those of the client).


142. Under the Model Rules of Professional Conduct, attorneys engaging in business transactions with clients must comply with the general conflict provisions under Model Rule 1.7 and the more specific provisions of Model Rule 1.8(a). Model Rules of Prof’l Conduct R. 1.7, 1.8(a) (2001). Model Rule 1.8(a) prohibits an attorney from entering a business transaction with a client or knowingly acquiring an ownership, possessory, security or other pecuniary interest adverse to a client unless:

1) the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing to the client in a manner which can be reasonably understood by the client; 2) the client is given a reasonable opportunity to seek the advice of independent counsel in the transaction; and 3) the client consents in writing thereto.
applicable rules relating to business transactions with clients, "the burden of persuasion is on the lawyer to show that the transaction was fair and reasonable and that the client was adequately informed."\textsuperscript{143} In a legal malpractice case alleging breach of fiduciary duty, the plaintiff can rely on the "well-established presumption of undue influence when lawyers engage in business transactions with clients."\textsuperscript{144} This presumption "can only be overcome by clear and convincing evidence that (1) the transaction was fair, (2) full disclosure was made to the client, and (3) [the client] had the opportunity to seek the advice of independent counsel."\textsuperscript{145} If the attorney cannot successfully rebut the presumption of undue influence, the court can declare the transaction void, and the attorney can be held liable for a breach of fiduciary duty.\textsuperscript{146}

Another significant risk of engaging in business dealings with clients relates to the fact that malpractice claims associated with such transactions may not be covered under the attorney's professional liability policy. Depending on the plaintiff's allegations and the term of the applicable policy, the insurer may deny coverage on the basis that the claims are not covered under the insuring agreements, which limit coverage to claims arising out of acts or omissions in rendering legal services to others. If the plaintiff alleges some conflict in rendering legal services, the insurer may rely on policy exclusions that eliminate coverage for claims relating to business activities of attorneys, regardless of whether the claim arises out of the rendering of legal services.\textsuperscript{147} Some underwriters include broad business pursuit exclusions because of their concern over the exposure when attorneys wear two hats, as well as because of the difficulty in determining when the attorney was acting as a business person and when the attorney was serving as legal counsel. This determination need not be made if the policy includes a broad business pursuit exclusion that eliminates coverage for all

\textsuperscript{143} Model Rules of Prof'l Conduct R. 1.8(a) (2001).

\textsuperscript{144} Restatement (Third) of the Law Governing Lawyers § 126 cmt. a (2000).

\textsuperscript{145} Id.

\textsuperscript{146} Id.

claims relating to attorneys’ business dealings. In discussing how a business pursuit exclusion may jeopardize insurance coverage, legal malpractice expert Ronald E. Mallen explains that it is a “status exclusion” that “turns on the ownership interest, not the activity.”

Despite the liability exposure and insurance risks associated with engaging in business activities with clients, many attorneys cannot resist the temptation. These transactions take numerous forms. Common business transactions involving clients include loans to and from clients and attorneys taking an equity position in a business venture as a fee. When an attorney takes stock in lieu of a fee, the attorney faces a conflict between professional interests as the company’s attorney and the attorney’s personal interests as a company shareholder. Conflicts also arise out of attorney investments in the same venture with a client or investments in a venture that is adverse to a client’s interests. Regardless of the specific form of conflicts, all entrepreneurial activities involving clients can leave the “entrepreneurial” attorney exposed to disciplinary and civil liability, and the firm, and possibly firm partners, exposed to vicarious liability.

Given the possible consequences of entrepreneurial activities, firms should take steps to identify and address conflicts regarding business dealings related to clients. While many firms have extensive procedures to avoid potential problems related to representing...
different clients with conflicting interests, firms are far less likely to have procedures to identify potential conflicts between the interests of clients and the personal financial interests of firm attorneys. 152 Without such procedures, the firm and its attorneys will not be prepared to identify and address these serious conflicts of interest.

Clearly, risk management should include formulating a firm policy that specifically deals with entrepreneurial activities of firm attorneys. Attorneys representing each practice area should participate in drafting the policy which sets forth the firm’s position on business transactions involving clients because attorneys’ business activities take different forms. A threshold determination is for firm partners to decide whether business dealings involving clients will be strictly prohibited or merely regulated. For example, the partners might wisely decide to prohibit all attorneys from taking stock in lieu of fees or serving on the board of directors of for-profit corporations. Short of prohibiting certain activities, the partners may impose restrictions such as requiring firm approval before an attorney accepts any directorship, trusteeship, or similar office in any private or public organization. 153

One other restriction that limits malpractice exposure is imposing a ceiling on the maximum ownership interest that the firm or its attorneys can obtain in a client business. Arguably, when firm “in-

152. Stanley Keller, Tax, Business, and Succession Planning for the Growing Company, 71 A.L.I. 407, 420 (1997), WESTLAW SB71 ALI-ABA 407. A 1987 survey conducted by the Subcommittee on Quality Control of the ABA Business Law Section (“ABA Business Law Section Survey”) revealed that virtually all respondent firms had “extensive procedures to avoid potential difficulties when representing different clients with conflicting objectives,” but were far less likely to have procedures to identify potential conflicts between the interest of clients and the personal financial interest of lawyers within the firm. Id. According to the survey, thirty-one of the fifty respondent firms had formal policies which either prohibited lawyers in their firm from investing in clients or investing jointly with clients or require advance approval of such investments. Id.

153. Id. at 421. The ABA Business Law Section Survey revealed that 50% of the respondent firms forbid or require some form of consent before a firm attorney accepts any directorship, trusteeship, or similar office of any charity or other not-for-profit corporation. Id. A 1995 mail survey of all Texas law firms with ten or more attorneys revealed that 68% of the respondent firms required prior approval or simply prohibited firm principals from serving as officers or directors of for-profit entities. See Susan Saab Fortney, Are Law Firm Partners Islands Unto Themselves? An Empirical Study of Law Firm Peer Review and Culture, 10 GEO. J. LEGAL ETHICS 271, 282-83 (1997) (noting that as expected, the results also indicated that the larger the firm, the more likely it is to monitor principals’ directorship activities).
vestments are small, they do not 'make a difference' in a law firm's behavior." This view is reflected in the policy of one Silicon Valley firm which limits investment to $50 thousand or one percent of the founder's stock in order to avoid the appearance of any effect on the attorney's legal judgment. Above all, the aggregate personal investments of all firm attorneys should not be of such magnitude to distract a lawyer from giving disinterested, candid legal advice.

Once firm partners have determined what restrictions to impose on entrepreneurial activities, the policy should specifically describe the restrictions and the procedures for complying with ethics rules. Obviously, the specific approach used by firms will depend on their size and resources. Risk management experts with the firm's malpractice carrier can assist attorneys in formulating policies and procedures that are suitable for their particular firm. For small and mid-sized firms, a general counsel for one carrier recommends the following guidelines for attorneys choosing to accept the risks of business transactions with clients:

1. Screen the clients in whom you invest carefully;

2. Require that all partners or a designated conflicts committee approve each investment;

3. Require that clients sign a detailed disclosure statement covering all points discussed in ABA Formal Opinion 00-418, Acquiring Ownership in a Client in Connection with Performing Legal Services;

4. Decline stock options in lieu of fees;

5. Set a limit on the amount of each investment, such as an agreement of no more than five percent ownership interest in a single client;

154. See Bruce Dallas & Heather Stack, Securities Law & the Internet: Doing Business in a Rapidly Changing Marketplace, 1188 PLI 233, 255 (2000), WESTLAW 1188 PLI/Corp 233 (suggesting that the impact of a particular company's success or failure is minimal if investments are made through a firm fund rather than being made by individual attorneys).

155. Id. at 256.

(6) Consider requiring that investments be made by the firm rather than by individuals;

(7) Require that investments be held for a minimum period; and

(8) Review the legal malpractice policy, recognizing that some policy exclusions are only triggered by ownership interests exceeding a specific percentage ownership.¹⁵⁷

As noted in Part II, the conflicts system regularly used by the firm should also include information on certain investments of firm attorneys. Without such information in the system, a conflicts check alone will not reveal if a firm attorney has an interest adverse to a prospective or current client. As an additional safeguard, circulation of a "new client matter memo" to all firm attorneys will give each attorney an opportunity to recognize when she has an investment or other interest adverse to that of a client which should be revealed.

Regardless of the size of the firm, policies and procedures should identify a specific ethics partner or committee to be responsible for monitoring all attorney entrepreneurial activities involving clients. A designated ethics partner or committee can provide scrutiny, objectivity, and distance in evaluating when and how firm attorneys participate in entrepreneurial activities related to clients.

Most importantly, the ethics counsel or committee should devote time to educating firm members so that they can intelligently spot and avoid conflicts of interest problems related to entrepreneurial activities. While different educational approaches can be used, the goal remains to deputize each attorney to detect and avoid conflicts.

A few reported cases illustrate how conflict traps related to entrepreneurial activities could have been avoided through education and improvements in the ethical infrastructure of the firm providing the legal services. The first case deals with attorney investment in a venture adverse to clients and the second involves attorney investment in the same venture with a client. The third case in-

¹⁵⁷. See Anne E. Thar, Taking an Equity Interest in a Client—Is It Worth the Risk?, 89 ILL. B.J. 101, 102 (2001) (concluding that the guidelines will "at least improve the odds" of gambling and investing in a client, even though it is not a bet the author would be willing to take).
volves an attorney who borrowed money from a client and his
firm’s subsequent vicarious liability.

*State v. Callahan*\(^{158}\) is a disciplinary case arising out of a sale of
real property in which John Callahan acted as the attorney for both
the buyer and seller-complainant.\(^{159}\) In upholding the indefinite
suspension of the attorney, the Supreme Court of Kansas identified
a number of improprieties, including the fact that the attorney did
not disclose to the seller the attorney’s close business ties to the
buyer.\(^{160}\) By failing to decline the engagement, the attorney cre-
ated the appearance that his legal judgment was impaired by his
personal investment interests.\(^{161}\) Ethics education might have
helped this attorney appreciate the risks of representing a buyer
whose interests were adverse to the attorney’s investment partner.
Had information on the attorney’s personal investments been in-
cluded in the firm’s conflicts system, the potential conflict could
have been detected when the conflicts check was completed.

By adopting policies and following procedures related to invest-
ment ventures with clients, attorneys might have avoided the con-
flicts of interest claims made against them in *K.M.A. Associates,
Inc. v. Meros*.\(^{162}\) In *K.M.A.*, an attorney and his partner “bailed
out” a time-share project owned by the client.\(^{163}\) In an attempt to
help their client with financing, the defendant-attorney and his law
partner entered into a partnership agreement with the client.\(^{164}\)
Under the agreement, the investors organized by the attorney ac-
quired fifty percent interest in the project.\(^{165}\) Through a series of
loans and transactions, the attorney eventually acquired all of the
assets of the partnership.\(^{166}\)

On appeal of a summary judgment for the attorneys, the court
allowed the plaintiff to pursue a legal malpractice claim.\(^{167}\) In
reaching its conclusion, the court emphasized the fact that business

\(^{158}\) 652 P.2d 708 (Kan. 1982).
\(^{159}\) State v. Callahan, 652 P.2d 708, 709 (Kan. 1982).
\(^{160}\) *Id.* at 711.
\(^{161}\) *Id.* (citing Ethical Consideration 5-15 from the ABA Code of Professional
Responsibility).
\(^{164}\) *Id.*
\(^{165}\) *Id.*
\(^{166}\) *Id.*
\(^{167}\) *Id.*
transactions between a client and attorney are subject to the "closest scrutiny." The court stated that "[t]he burden is placed upon an attorney to establish by clear and convincing evidence the fairness of an agreement or transaction purporting to convey a property right from a client to his attorney." Attorneys who understand this burden can avoid malpractice claims such as the ones asserted in *K.M.A.* The specific claims in that case could have been avoided if the firm had a policy banning all investments with clients, or a policy limiting the ownership interest that attorneys can possess in a client business. While such a policy limits the autonomy of the individual attorney, it protects firm partners and the firm itself from possible malpractice claims.

Examination of the facts in *Phillips v. Carson* suggests how a law firm policy can help limit the vicarious liability of the firm and its attorneys. In *Phillips*, the Supreme Court of Kansas considered the liability of firm partners for the acts and omissions of a specific partner who borrowed money from a firm client. Recognizing that the question of whether the partner was carrying on usual business of the firm was a disputed fact issue, the court overturned a summary judgment granted for the firm and its partners. The court referred to various firm practices and the lack of a firm policy prohibiting a partner from transacting business with a client. Clearly, such a policy could have helped the firm establish that the individual attorney's loans were not within his authority as a partner of the firm.

Ultimately, with instances of attorney entrepreneurial activities involving clients, thorough disclosure and documentation is an essential step in minimizing conflicts of interest claims. Given the

169. *Id.* (quoting *Smyrna Developers, Inc. v. Bornstein*, 177 So. 2d 16 (Fla. Dist. Ct. App. 1965)).
172. *Id.* at 836.
173. *Id.*
174. *See Monco v. Janus*, 583 N.E.2d 575, 581 (Ill. App. Ct. 1991) (explaining that full and frank disclosure of all relevant information related to an attorney's business transaction with a client is a factor in determining if an attorney overcomes the presumption that the transaction proceeded from undue influence exercised by the attorney); *see also* Bruce Zucker, *Attorneys Who Enter into Business Transactions with Their Clients: A Presumption of Undue Influence, Malpractice, and Impropriety*, 1 J. LEGAL ADVOC. & PRAC. 7, 8-11
strict disclosure requirements, attorneys who fail to meet these re-
requirements effectively become guarantors of the business deal with 
the client. One legal malpractice expert captured this looming risk, 
noting that when "trouble develops with the business deal, [a] cli-
ent might swiftly become a former client and [the lawyer] might 
swiftly become a defendant."

B. Conflicts Relating to Fee Agreements

Another common conflicts problem involving personal interests 
of attorneys arises out of fee agreements between attorneys and 
their clients. At the time that a prospective client enters a fee 
agreement with an attorney, the attorney possesses a great deal of 
autonomy in setting the fee and payment terms. While the fee 
must be reasonable and comply with applicable disciplinary rules 
and law, fee agreements are largely a matter of arms-length negoti-
ation between the attorney and client. This situation radically 
changes after the attorney and the prospective client enter into an 
attorney-client relationship. Once an attorney-client relationship is 
established, attorneys who seek to change fee and payment terms 
effectively create a conflict of interest. Specifically, the conflict 
arises because the attorney-fiduciary's interest in earning a fee con-
flicts with the client-principal's reliance on the original terms of the 
fee agreement.

The Restatement (Third) of the Law Governing Lawyers now 
includes a specific section dealing with contracts entered into dur-

(1999) (applying the California Rules of Professional Conduct); Lee E. Hejmanowski, 
Note, An Ethical Treatment of Attorneys' Personal Conflicts of Interest, 66 S. CAL. L. REV. 
881, 905-09 (1993) (applying the Model Rules of Professional Conduct in a discussion of 
the disclosure and consent requirements).

175. ROBERT E. O'MALLEY, New Clients/New Matters, in The Quality Pursuit, Ass-
suring Standards in the Practice of Law 104, 111 (Robert Michael Greene ed., 
1989).

176. Compare Restatement (Third) of the Law Governing Lawyers § 34 cmt. b 
(2000) (stating "[i]n general, clients and lawyers are free to contract for the fee that the 
client is to pay"), with In re Estate of Goldstein, 509 N.Y.S.2d 984, 987 (Sur. Ct. 1986) 
(explaining that "[u]nless unconscionable or illegal on its face, a retainer is like any other 
contract and therefore, is presumed to be fair unless the contrary appears").

177. See Joseph M. Perillo, The Law of Lawyers' Contracts is Different, 67 FORDHAM 
L. REV. 443, 452 (1998) (describing that in a fee dispute with a client, the attorney must 
carry the burden of persuasion on all issues concerning the propriety and reasonableness of 
the fee). This burden is imposed for a number of reasons including the fact that the attor-
ey is the person who drafts the contract and undertakes to become a fiduciary. Id.
ing an attorney's representation of a client. Under the Restatement, such contract modifications are subject to strict scrutiny if they are not made within a reasonable time after the lawyer has begun to represent the client. To enforce the agreement, the attorney must show that the contract and the circumstances of its formation were fair and reasonable to the client. This Restatement provision on enforceability reflects the well-established rule that attorneys have the burden to insure that contract terms are fair and reasonable when the contract is entered into subsequent to employment. This can be a heavy burden to overcome because a presumption of unfairness or invalidity attaches to contracts for compensation entered into while the attorney-client relationship exists.

Notwithstanding these accepted rules, many attorneys create conflicts with their clients when they modify their agreements. Those attorneys who forge into contract modifications without appreciating the conflicts face possible discipline and obstacles when they try to enforce the new terms. If a court considers the modification to be a serious breach of fiduciary duty, the attorney may also face a fee forfeiture of amounts previously paid. Under the terms of the attorney's legal malpractice policy, such a fee dispute may not be covered.

Improvement of a firm's ethical infrastructure can help attorneys deal with the risks associated with changing fee agreements after the attorney-client relationship has commenced. Above all, ethics training can help attorneys appreciate the applicable disciplinary rules and fiduciary principles that apply to contract modifications. With this understanding, attorneys should recognize the impor-

179. Id.
180. See Baye v. Grindlinger, 432 N.Y.S.2d 624, 625 (N.Y. App. Div. 1980) (reversing a summary judgment granted for the attorney who sought to collect two promissory notes executed by the client during trial in which the attorney was representing the client).
181. Archer v. Griffith, 390 S.W.2d 735, 739 (Tex. 1964) (referring to Pomeroy, Equity Jurisprudence, § 960d (5th ed. 1941)); see also Lustig v. Horn, 732 N.E.2d 613, 619 (Ill. App. Ct. 2000) (holding that "[a]s a matter of public policy, once raised, a presumption of undue influence must be rebutted by the attorney by 'clear and convincing' evidence").
182. See Matthew Nielson, Burrow v. Arce: Too Much Ado About Nothing?, 52 BAYLOR L. REV. 487, 495 (2000) (stating that "an overwhelming number of cases have held that fee forfeiture is appropriate when an attorney places another's or his own interests in direct conflict with a client's interest").
tance of screening prospective clients. A firm policy can impress on attorneys the importance of carefully screening clients to evaluate a number of factors, including the ability of clients to pay fees. If prospective clients can afford fees, there is less of a risk of having to make new fee arrangements and later take proprietary interests to secure fees.

At the outset of representation, attorneys should set fair fees that the attorney can live with for the duration of the attorney-client relationship. Setting an adequate fee up-front often eliminates any perceived need to later alter the fee terms. When an attorney is concerned about prolonged representation, the attorney can address fee increases in the original fee agreement. To avoid questions, the provisions for upward adjustment of fees should be based on some objective indicator or formula. Use of an indicator or formula avoids a situation in which the increase appears to be a discretionary exercise of an attorney's subjective judgment. By setting the basis for an adjustment in the original agreement, attorneys can effectively increase fees without modifying the terms of the original agreement.

When increases are not provided for in the original agreement, the firm should have some mechanism for evaluating whether modification of the fee agreement is worth the risk of disciplinary and malpractice claims. One approach is to require that all proposed modifications be approved by the ethics partner/committee or a managing partner. When consulted, the partners can scrutinize the wisdom and approach to modifying the fee agreement. Above all, steps should be taken to create a "burden of proof" file to demonstrate that the modification was reasonable and fair to the client. In addition to documenting full disclosure, the attorneys should urge the client to seek independent counsel to protect the client's interests. Depending on the situation, the firm may offer to defray some of the costs associated with retaining independent counsel.

At the conclusion of representation, attorneys should send termination letters to communicate to the client that work is complete. Such termination letters should dispel any reasonable expectation of the existence of an attorney-client relationship. Thereafter, a new engagement would require a new fee agreement. If the termination letter clarifies that the firm no longer represents the client, the new fee agreement should be treated like any other agreement entered into at the outset of representation, rather than
as an agreement entered into during representation. As discussed below, termination letters can also help attorneys avoid problems related to conflicts between and among clients.

C. Conflicts Involving the Representation of Multiple Clients

Regardless of the nature and size of a law practice, conflicts of interest involving representation of multiple clients appear to be inevitable. Generally speaking, these conflicts fall into two broad categories: conflicts between and among the interests of parties under current representation and conflicts between the interests of former clients and current clients. Most commonly, conflicts involving simultaneous representation in a business context arise when attorneys form entities or represent an entity and its constituents. Less obvious conflicts arise when attorneys take a position for one client that is adverse to another client's position in an unrelated matter. Litigators also face conflicts involving jointly represented persons when settlements put one client in a better position than other jointly represented parties. Litigators and non-litigators alike should be concerned about the second category of conflicts in which an attorney takes a position adverse to a former client.

While each type of conflict triggers different considerations, the avoidance of all conflicts involving multiple representation of clients requires that attorneys understand applicable rules and principles so that they can first recognize, and then address, possible conflicts. Firm managers must take steps to educate attorneys on various types of multiple representation that pose risks. Such education helps promote a "conflict-sensitive" practice among all firm attorneys.183

Ethics training, coupled with procedures for identifying and dealing with conflicts, are important features of a firm's conflicts of interest policy.184 The policy should have separate sections that apply to conflicts based on simultaneous representation of clients and successive representation of clients. Each section should address

183. See Charles W. Wolfram, The Uncertain Realm of Former-Client Conflicts, 403 P.L.I. 165, 172 (1990) (emphasizing the "vital importance of firm-wide systems and agreement on high levels of compliance and aggressive in-firm pursuit of conflicts inquires").

184. See David W. Evans, Ethical Issues and Financial Data, 1004 P.L.I. 229, 231 (1997), WESTLAW 1004 PLI/Corp 229 (providing a description of objectives of a conflicts of interest policy, along with an example).
the specific procedures for detecting and addressing possible conflicts. A firm's system for identifying potential problems should be the focal point of a conflicts of interest policy. Without doubt, the actual success of a system in protecting the firm and its clients depends on the comprehensiveness of the system and compliance with established procedures.

A number of cases reveal how gaps in systems lead, or at least contribute, to conflicts problems. Undoubtedly, the most glaring oversight occurs when attorneys fail to conduct a conflicts check. A firm that fails to conduct a conflicts check will not be able to defend its position on the basis of lack of knowledge. In one probate case, the court unequivocally stated, "[a]ny time a law firm undertakes representation of a client, it has an obligation to do a conflicts check to ensure that no conflict exists between clients."

Cases also suggest that delegating the task of conducting a conflicts check to support staff can lead to problems. For example, in the disqualification case of Parkinson v. Phonex Corp., no conflicts check was completed, notwithstanding the fact that the attorney asked an assistant to prepare a conflicts check for circulation among firm members. The lesson from this case is that attorneys should assume responsibility for ensuring that conflicts checks are conducted. As a back-up measure, the firm should create obstacles to work being performed until a conflicts check is completed. One safeguard that firms commonly use is to create a kind of "firewall," preventing the opening of files or billing of time before a conflicts review is done. Even for current clients of the firm, the

185. Estate of Fogleman v. Fegen, 3 P.3d 1172, 1179 (Ariz. Ct. App. 2000). In this case, the court clarified that "all attorneys involved in probate matters have a duty to check for possible conflicts before representing a personal representative or administering an estate." Id. at 1180.


187. See Parkinson v. Phonex Corp., 857 F. Supp. 1474, 1475 (D. Utah 1994) (holding that the disqualification of the plaintiff's law firm was not required where another attorney in the plaintiff's law firm represented the named defendant for a period of one month).

188. See In re Enviroyne Indus., Inc., 150 B.R. 1008, 1014 (Bankr. N.D. Ill. 1993) (questioning the sufficiency of the firm's practice of using a clerk to run a computerized conflict check).

189. See Lee A. Pizzimenti, Screen Verid: Do Rules About Ethical Screens Reflect the Truth About Real-Life Law Firm Practice?, 52 U. MIAMI L. REV. 305, 322 (1997) (adding that one survey of 156 firms comprised of fifty or more lawyers in Michigan, Illinois, Pennsylvania, and Oregon found that virtually all respondent firms indicated that new files could not be opened without a conflicts review).
firewall should deter attorneys from performing work until a new conflicts check is completed on any new matter. The firm's policies and procedures should also have mechanisms for triggering a conflicts check when there are new developments in a case.\textsuperscript{190}

In tackling conflicts between clients, attorneys need to classify clients as either current clients or former clients. Model Rule 1.9 applies to conflicts involving former clients, while Model Rule 1.7 deals with conflicts involving current clients.\textsuperscript{191} These rules give attorneys more latitude to take positions adverse to former clients as compared to current clients.\textsuperscript{192} Therefore, attorneys who want more freedom to accept representation and avoid disqualifying conflicts should communicate to the client when representation commences and terminates. For example, firm policies and procedures should require the use of engagement letters that expressly state that representation in a new matter will require a new engagement letter. To define when the attorney-client relationship ends and to negate the possibility that a client will be treated as a current client, one ethics expert suggests that firms consider including the following provision in engagement agreements:

Unless [the client] has paid the firm a general retainer, all engagements are on a case-by-case basis rather than an ongoing basis. When the firm completes its services for the client, the relationship of attorney and client is concluded, regardless of whether the firm has formally closed its files and regardless of whether the client has completed payment of any outstanding fees and expenses.\textsuperscript{193}

Termination letters can also be used to eliminate a client's expectation of continuing representation.\textsuperscript{194}

\textsuperscript{190} For example, when a new party is to be added to litigation, an attorney should not be able to obtain a firm check to pay the fees for adding the new party until the attorney has completed a conflicts check with information related to the new party.

\textsuperscript{191} \textit{Model Rules of Prof'L Conduct} R. 1.9, 1.7 (2001).

\textsuperscript{192} \textit{Id.} Under Model Rule 1.9, former client consent is not required for an attorney to undertake representation of a client whose interests are materially adverse to the interests of a former client if the current representation and former matter are not "substantially related" to each other. \textit{Id.} 1.9. On the other hand, Model Rule 1.7 requires client consent after consultation anytime representation of one client is directly adverse to another client or when representation of one client may be materially limited by the attorney's responsibilities to another client. \textit{Id.} 1.7.

\textsuperscript{193} \textsc{Nathan M. Crystal}, \textit{Professional Responsibility: Problems of Practice and the Profession} 24 (2d ed. 2000).

\textsuperscript{194} See generally A.B.A. \textit{Lawyer's Desk Guide to Preventing Legal Malpractice} 97 (2d ed. 1999) (providing a sample closing letter).
IV. Conclusion: Rethinking the Inevitability of Conflict Claims

The above discussion reveals the complications inherent in trying to avoid conflict claims and their consequences. Mechanical failures in conflicts systems can result in conflicts not being detected. Such mechanical failures may be either in system design or input, or a combination of the two. While certain aspects of conflict avoidance are mechanical, human factors intrude at many levels. Ultimately, decision-makers, collectively or individually, must decide whether to accept particular representation. In this decision-making process, the lack of understanding or education can undermine the desire to avoid conflicts. Economic pressures may also tempt individual attorneys and firms to risk representation, despite questionable conflicts issues. Most significantly, an atmosphere which does not foster respect for the need to avoid conflicts can render ineffective even the most sophisticated system.

Admittedly, firms and attorneys are motivated to make a profit providing legal services. In seeking to maximize profit through business generation and production, attorneys may focus on the short-term benefits of accepting representation, even when "conflicts red flags" beckon caution. The perspective is reflected in the title of "conflicts resolution counsel" used by some in-house firm counsel. The title suggests that the attorney’s goal is to "fix" a situation by resolving conflicts, rather than declining representation. Such a cultural attitude can be reshaped when firm principals appreciate the long-term efficiency and financial benefit of conflicts systems and risk management.

Today, attorneys’ assessment of the value and costs of monitoring conflicts must take into account the risk of fee forfeiture for a breach of fiduciary duty. Under the Restatement and case law, attorneys can now be forced to disgorge fees for such a breach.

even without proof of damages.\textsuperscript{196} By implementing controls to avoid conflicts of interest, attorneys significantly improve their ability to defend claims based on breach of fiduciary duty. When precautions are taken, a disgruntled client should not be able to prove an intentional breach of duty. Precautionary efforts should also assist the firm in defeating negligent breach of fiduciary claims.\textsuperscript{197}

Despite precautionary efforts, conflicts may still arise. For those inevitable conflicts, two law and economics scholars recommend reforming conflicts regulation.\textsuperscript{198} Specifically, Professors Jonathan R. Macey and Geoffrey P. Miller advocate a market approach that would allow attorneys to compensate their clients and former clients for the right to engage in conflicting representation of other clients.\textsuperscript{199}

In the final analysis, attorneys must evaluate the efficiency of devoting time and resources to conflicts avoidance. By spreading the costs of monitoring across a firm’s entire portfolio of business, firm managers may recognize that it is more efficient to invest in monitoring than to roll the dice and run the risk of fee forfeiture and other serious penalties associated with impermissible conflicts. For modern law firms, the problems posed by protecting against conflicts claims may be a cost of doing business, but they are a cost worth paying.

\textsuperscript{196} Restatement (Third) of the Law Governing Lawyers § 37 (2000) (noting that “[a] lawyer engaging in clear and serious violation of duty to a client may be required to forfeit some or all of the lawyer’s compensation for the matter”). The Reporter’s Notes, comment c, include numerous examples of breaches justifying fee forfeiture. Id. § 37 cmt. c.

\textsuperscript{197} See id. § 49 cmt. d (2001) (noting that an attorney who acts with reasonable care is not liable in damages for breach of fiduciary duty). For example, an attorney who performs an “adequate” conflicts search may not be liable. Id. at illus. 2. Because a competently maintained conflicts system would not have revealed the conflict, the attorney is not liable for negligent or intentional breach of fiduciary duty. Id.

\textsuperscript{198} See Jonathan R. Macey & Geoffrey P. Miller, An Economic Analysis of Conflict of Interest Regulation, 82 Iowa L. Rev. 965, 1003 (1997) (recommending revising ethics rules to “explicitly recognize the utility of a market-based solution” to dealing with client consent to conflicts).

\textsuperscript{199} See id. (discussing the dynamics of clients and attorneys “negotiating” consent).