THE NATIONAL LAW JOURNAL

JUNE 14, 2010

Daily Updates at NLJ.COM

An ALM Publication

LAWYERS REPRESENTING LAW FIRMS

A SPECIAL REPORT

ISTOCKPHOTO/NICO BLUE

When should a firm retain outside counsel?

Step is needed when there's a potential claim by a client, to avoid conflicting fiduciary duties.

BY ARTHUR D. BURGER

Every law firm needs at least one qualified lawyer who is answerable for making sure that the firm complies with its ethical duties. Many firms have enlarged upon this role, having one or more full-time inside counsel as well as an in-house ethics committee and support staff.

The ethics rules encourage law firms to have inside lawyers play this role, and firms protect the arrangement by providing confidentiality to the usual internal workings of this process. A growing number of courts, however, have rejected assertions of attorney-client privilege for internal firm discussions when the firm develops interests that conflict with the interests of current firm clients. In those instances, retention of outside counsel can cure the problem, so firms need to know when to seek outside legal advice.

A lot can go wrong in a law firm, and so inside ethics counsel have a lot to keep track of. For most firms, conflicts of interest top the list. Every time a firm takes on a new matter—typically at least several times each day—potential conflicts need to be promptly, yet thoroughly, flagged and

addressed. Potential conflicts of interest are also implicated when new lawyers join a firm. Other items on the watch list include the firm's marketing material and Web site; supervision of support staff; ensuring preservation of client confidentiality; monitoring potential problems such as sanctions motions or motions to disqualify; and troubleshooting of various shapes and sizes.

To handle all this, firms need an inside ethics counsel who is knowledgeable in the specialized and elusive body of law of legal ethics. The inside counsel must be respected by the firm's lawyers, have the backing of firm management and the ability to deal with strong personalities. In short, inside counsel must have the juice to say "no" to powerful partners and have the judgment to know when to say it.

The American Bar Association Committee on Ethics and Professional Responsibility is on record endorsing the propriety and value of law firms using inside ethics advisers. In ABA Opinion No. 08-453, the committee recognized that, because Model Rules 5.1 and 5.3 require that managing partners take measures to reasonably ensure that their law firms comply with the ethics rules, an internal structure or system is needed.

The committee further stated that a firm's internal discussions about a client's case will usually not create a conflict of interest with the client, and the firm need not disclose the internal discussions. The committee reasoned that a firm's interest in getting advice about its ethical duties is in sync with the interests of its clients. The committee quoted with approval from New York Bar Association Opinion 789, stating that internal discussions by lawyers seeking advice is "a required part of the work of carrying out the representation."

The rationale that the firm's discussions are all about doing a better job for the client breaks down, however, when the firm becomes worried about its own potential liability to an existing client. When the firm starts circling its wagons against a client, it becomes "us against them."

Law firms, like any other organization, can use inside counsel and invoke attorney-client privilege for communications with such counsel. *U.S. v. Rowe*, 96 F.3d 1294 (9th Cir. 1996).

Unlike other organizations, however, all of the lawyers in a firm have a fiduciary duty to all current firm clients. Therefore, when a firm is considering how to handle a potential claim against it by a client, any lawyer in the firm who is acting as inside counsel in that matter owes conflicting fiduciary duties to that client and to the firm. Those conflicting duties have been found to eliminate the premise of a claim of attorney-client privilege against the client.

Although law firms have sought to reverse the trend, there is a growing line of cases rejecting assertions of privilege by firms when a client seeks disclosures relating to their claim against a firm. The most recent such decision is *Asset Funding Group v. Adams and Reese*, 2009 U.S. Dist. Lexis 48420 (E.D. La. 2009). Similarly, in *Thelen Reid & Priest LLP v. Maryland*, 2007 U.S. Dist. Lexis 17482 (N.D. Colo. 2007), the court noted that lawyers "should and do" seek legal advice regarding their ethical obligations from other lawyers in their firm but held that, "once the law firm learns that a client may have a claim against the firm," they cannot claim privilege when that client seeks disclosure. See also *Burns v. Hale and Dorr*, 242 F.R.D. 170 (D. Mass. 2007).

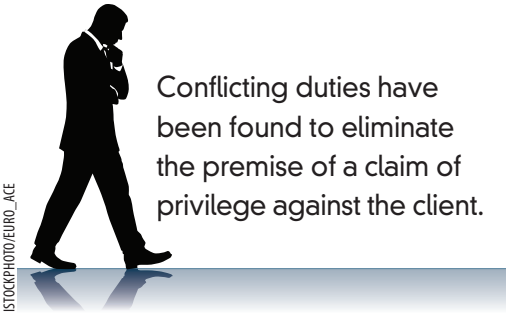
This impediment to invoking a privilege can be avoided if a firm retains outside counsel, because outside counsel have no such duties to a firm's clients. Moreover, outside consultations do not violate client confidentiality under Rule 1.6(b)(4), which permits lawyers to share confidential client information with outside counsel when it is done to obtain "advice about the lawyer's compliance with these Rules."

DEVELOPING A SYSTEM

Regardless of whether outside counsel is ultimately used, there are some basic practices that will enhance the likelihood that a firm can succeed in protecting its decision-making process. First, even for routine internal communications, the basic rules for establishing a privilege should be followed. So, for example, communications with inside counsel should be labeled as "confidential and privileged" and shared only with those within the firm who need to know. As with any other parties, law firms must treat communications as privileged if they expect courts to do so.

As to the referenced case law, firms should be alert for events that trigger a need for outside advice. (Those events may also coincide with a need to notify the firm's malpractice carrier of a potential claim.) It's easiest to make this pivot when a firm retains outside counsel who will be available on a regular basis and who is familiar with the firm's practice and its personnel.

In addition, as often stated but rarely done, discussions regarding sensitive matters should be through face-to-face meetings rather than through hurried e-mail exchanges by busy lawyers. Invariably, such e-mails, when scrutinized later by third parties, tend to appear flip and insensitive, even when that was not the intent. Moreover, face-to-face discussions allow the participants to focus and reach more reasoned decisions.



ISTOCKPHOTO/EURO_ACE

A firm may have information suggesting that a lawyer in the firm is impaired by substance abuse or mental illness. In such instances, firms have a duty to get the facts in order to ensure that clients' interests are protected and that third parties are not harmed. See ABA Ethics Opinion No. 03-429. In these instances, firms should seek guidance from appropriate health care providers. State bars frequently have lawyer assistance programs that may be helpful, as well. If a firm concludes that a lawyer's impairment renders him unreliable, the impaired lawyer should be replaced or at least supervised.

In other instances, a firm may suspect that a lawyer in the firm has engaged, or is engaging, in fraudulent conduct. Here again, the rights of clients and third parties may be affected, and the firm must find out the truth and take definitive remedial action. A firm should consider using outside counsel to conduct the investigation, and the benefits may not go beyond privilege issues.

Such highly charged and sensitive matters are more credibly and effectively dealt with by an outsider who does not carry the emotional link to the suspected lawyer and who can approach the inquiry objectively. An outside review also permits a firm to reasonably rely on the findings, although reliance may result in a waiver of any privilege as to the investigation.

Regardless of the nature of the issue, for both inside counsel and outside counsel, law firms are organizations, and Model Rule 1.13 applies to their representation. As a result, both inside and outside counsel must remain mindful that the firm itself is the client—not the individual lawyers or employees in the firm. Therefore, as required by Rule 1.13, counsel who receives information of improper conduct by a firm lawyer who insists on continuing his wrongful conduct regardless of harm to the firm must convey the facts up the ladder to the firm managers. In those situations, counsel should be alert to a potential conflict between the firm and an individual firm lawyer and the need to advise that lawyer to retain separate counsel.

Although implementing sound procedures is important, in the final analysis a firm's success in avoiding claims of wrongdoing often will also depend on whether the firm culture recognizes the seriousness of its professional obligations. Procedures alone don't work when nobody cares.

Arthur D. Burger chairs Jackson & Campbell's professional responsibility practice group in Washington. He was a member of the District of Columbia Bar Legal Ethics Committee from 2003 to 2009. He can be reached at aburger@jackscamp.com.