February 2010
Volume 15
Issue 1

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The Lawyers' Lawyer Newsletter

Recent Developments in Risk Management

Contingency Fee Agreements – Modification

Weiner v. Burr, Pease & Kurtz, P.C., 221 P.3d 1 (Alaska 2009)

Risk Management Issue: How may firms modify fee arrangements, and what are the pitfalls of doing so?

The Case: The law firm of Burr, Pease & Kurtz, P.C. represented a couple in connection with injuries sustained at a hotel. The firm's original contingency fee agreement provided for a 25 percent fee if the case was settled before a complaint was filed, 33 percent if a lawsuit was filed, and 40 percent if the case proceeded to trial. After the hotel filed bankruptcy, the firm recommended its clients settle for the $1.2 million policy limits insurance proceeds available.

The clients agreed to accept the limits if the firm would reduce its fees. Thereafter, the firm proposed in writing that if it obtained the policy limits settlement without "further substantial litigation," it would charge a reduced fee of $250,000. The clients agreed, but it took more than a year, depositions, a mediation and pretrial preparation before the hotel agreed to pay the policy limit. Litigation then ensued over whether the firm was permitted to charge 33 percent under its original fee agreement, or was restricted to charging $250,000 as the clients claimed. The trial court granted summary judgment in favor of the firm.

On appeal to the Alaska Supreme Court, the clients argued that the firm's amended fee agreement was unethical for violating Alaska's version of Rule E.R. 1.5(c), because it was not in a single integrated writing. They also argued that the fee arrangement impeded their right to decide whether to settle the case. The Court disagreed with the clients and found that the series of letters and e-mails between the clients and the firm satisfied the requirement that the fee arrangement be in writing.

The two key risk management issues addressed by the Alaska Supreme Court were: first, whether the firm violated Alaska Rule of Professional Conduct 1.5(c) by failing to have a single, integrated document that contained the modified fee agreement, and second, whether the modified fee agreement impeded the clients' right to control the decision to settle.

The Court held that because the parties modified their written fee agreement over a series of letters and e-mails, the modified agreement met the writing requirement of the Rule. The Court commented that, while it would have been preferable for the firm to specify what would constitute "substantial further litigation" to trigger the original 33 percent fee, the lower court properly interpreted the term to include more than only in-court proceedings such as hearings and a trial. The clients in this case could not reasonably argue that the work required of the firm to obtain the settlement did not meet that threshold. The modified fee arrangement did not impair the clients' right to determine whether to settle their case, but hinged upon whether the hotel's insurer decided at an early time to accept the clients' policy limits demand. The Court distinguished these facts from an earlier Alaska case that found unlawful a fee agreement that converted a contingency fee to an hourly fee if the client decided to settle at an amount that did not compensate the attorney at least his hourly rate for time spent (*see Compton v. Kittleson,* 171 P.3d 172 (Alaska 2007)).

In addition, the modified agreement did not retroactively impose a fee obligation the clients would not otherwise have been charged. The clients would have paid the firm a flat-fee plus costs if an early settlement had occurred. If the case did not settle at an early stage and "substantial litigation" ensued, the clients were obligated to pay the firm 33 percent of any recovery plus costs, under the original agreement. Because the clients had to pay if they received a recovery under either scenario, the Court concluded that the modified agreement was valid.

Comment: The Court did not address whether the modification to the fee agreement in the first place was a business transaction with the client, subject to the state's version of Model Rule 1.8(a). Typically that rule requires a client to provide informed consent, confirmed in writing, because of the inherent conflict of interest. Presumably the clients did not raise the issue because they wanted to enforce the modified arrangement.

Contingency Fee Agreements – Modification, continued on page 2

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Risk Management Solution: Whenever firms seek to modify a fee arrangement with an existing client, the modification should be defined in plain terms that the client can understand. Because in most situations changing the fee arrangement constitutes a conflict of interest under Rule 1.8 of the applicable rules of professional conduct, the modification should be in writing, and where the modified arrangement is favorable to the lawyer, it should contain the appropriate disclosures, including a recommendation that the client seek independent counsel before consenting. The written modified fee arrangement should also be countersigned by the client.

Fee Agreements – Reference to Separate 'Master Retainer' Schedule, Available But Not Provided to the Client, Not Binding on Client in Fee Dispute

***Alpert, Goldberg, Butler, Norton & Weiss, P.C. v Quinn*, 983 A.2d 604 (N.J.Super. A.D., November 24, 2009)**

Risk Management Issue: May law firms sidestep the ethical rules and fiduciary obligations governing fee arrangements with clients by placing the terms and details in a separate writing, such as a "statement of standard billing practices and policies," which is either provided to or available on request by the affected client?

The Case: Clients, the Quinns, retained the Alpert, Goldberg, Butler, Norton & Weiss, P.C. law firm (the "firm") to represent them in ongoing business litigation. The firm sent the Quinns engagement letters for two separate matters that required advance retainers of $25,000 and $10,000 each. Each letter specified the lawyers' hourly rates, described the types of legal services the clients would be charged for, provided a 10 percent discount for timely payment, and provided examples of the services that would be charged. The Quinns signed the letters, which also provided:

> We also charge for expenses, including out-of-pocket expenses, as well as "in-house" items such as copying. Details on any of these items and our policies will be provided to you upon request; whether or not you request them, you will be bound by our standard billing practices and firm policies in these and other regards, so feel free to ask.

These "standard billing practices and firm policies" were referred to as the firm's "Master Retainer." It consisted of 18 single-spaced type-written pages that permitted the firm to charge, among other things, fees it incurred during any fee dispute with the client, 12 percent interest on outstanding charges, and $50 an hour for "extraordinary secretarial overtime." The Master Retainer also said that the clients would not receive any discount on fees unless they agreed they would not challenge any of the items billed in the "traditional" manner.

The Quinns never asked for or saw the Master Agreement until disagreements over billings and representation had already occurred. After the clients fired the firm, Albert Goldberg sued the Quinns for outstanding fees and costs. Contentious litigation ensued, the results of which were judgments in favor of the firm against the Quinns in the aggregate of more than $160,000. A substantial part of the award derived from charges made pursuant to the Master Retainer, which the trial court found was incorporated by reference into the engagement letters, and hence a part of an integrated enforceable contract.

The New Jersey appellate court vacated the judgments, finding that the Master Retainer contained provisions that were contrary to public policy and in violation of several ethical rules. The fee arrangement between the Quinns and the firm could not be treated as any other arms-length contract, because the transaction gives rise to fiduciary duties on the part of the firm, which the firm was found to have breached. It was the firm's ethical duty to communicate to the Quinns in detail what they would be charging, such that the clients were aware of all such charges at the inception of the relationship, before the clients agreed to the fee arrangement. Inviting the clients to ask to see the Master Retainer was not sufficient.

Comment: The New Jersey appellate court remanded the case for a determination of what the Quinns owed pursuant to the letter agreements only. This result is surprising in that, in many jurisdictions, a finding that the firm had violated its fiduciary duties with respect to some of the charges might result in the firm's forfeiture of all fees charged, or the inability to collect any unpaid fees, or a restriction to the firm's recovery on a "quantum meruit" basis.

Risk Management Solution: Retainer agreements must, standing alone, clearly and thoroughly set forth the basis for every fee and charge to be assessed against the client during the course of the representation for them to be recoverable. If the law firm intends to charge for any item, the charge and the basis for the charge should be explained in detail to the client up front, before entering into any representation agreement. All of the arrangements must conform both to governing ethical rules and fiduciary duties governing the attorney-client relationship.

Outsourcing Legal Services – Ethical Rules Require Informed Consent, Firm Supervision, and Reasonable Fees for Legal and Non-Legal Resources

Ohio Supreme Court Bd. of Commissioners on Grievance and Discipline*, Opinion 2009-9* (Dec. 4, 2009)

Association of the Bar of the City of New York, Committee on Professional Responsibility, *Report on the Outsourcing of Legal Services Overseas* (August 2009)

Risk Management Issue: What are the ethical duties of a law firm regarding outsourcing legal services, and what steps do law firms need to take to comply with those duties?

The Opinions: An opinion and a recent report address ethical challenges law firms face when outsourcing legal services and other, non-legal support. In Opinion 2009-6, the Ohio Board of Commissioners on Grievance and Discipline reported that Ohio law firms are ethically permitted to outsource legal and support services, either domestically or abroad, providing that when doing so they comply with ethical rules. A report issued by the New York City Bar Committee analyzed in greater detail what law firms must do to comply with their ethical obligations when outsourcing legal services abroad.

The Ohio Opinion identified three general categories of ethical obligations that law firms must consider when outsourcing: (1) client disclosure, consultation and informed consent, (2) supervisory oversight of the persons providing outsourced services, and (3) reasonableness of fees for outsourced services.

With respect to the obligations of disclosure, consultation and informed consent, Opinion 2009-6 provides that "pursuant to Prof. Cond. Rules 1.4(a)(2), 1.2(a), and 1.6(a), a lawyer is required to disclose and consult with a client and obtain informed consent before outsourcing legal or support services to lawyers or nonlawyers." Lawyers must abide by their clients' decisions concerning the objectives of the representation and, consistent with 1.4, "shall consult with the client as to the means by which they are to be pursued." Lawyers are not impliedly authorized to outsource services, in part because it requires the disclosure of client confidences outside the law firm. It is therefore required, the Opinion states, that law firms inform their clients that outsourcing will occur and obtain the client's consent to that arrangement in advance.

Regarding responsibility for the conduct of persons providing outsourced services, the Opinion comments that Ohio's Professional Conduct Rules 5.1(c)(1), 5.3(a), and 5.3(c)(1) make lawyers responsible for another's violation of the Rules if the lawyer orders the conduct or, with specific knowledge of the conduct, ratifies it. Outsourcing law firms therefore must make reasonable efforts to ensure that its providers comply with the Rules. The oversight required is "a matter of professional judgment . . . but requires due diligence as to the qualifications and reputation of those to whom services are outsourced and as to whether the requested outsourced services will be provided with competence and diligence as required by Prof. Cond. Rules 1.1 and 1.3, confidences will be protected as required by Prof. Cond. Rule 1.6, and conflicts of interest will be avoided as required by Prof. Cond. Rules 1.7, 1.9, and 1.10."

After reviewing several other jurisdictions' opinions on the propriety of charging fees for outsourced services, the Opinion cites the requirement of Rule 1.5 that a lawyer's fee must be reasonable. It leaves the details of those financial arrangements to the lawyer's professional judgment, but cautions that the Rules require a lawyer to communicate to the client the basis or rate of the fee and expenses – whether services are provided directly by the firm or outsourced domestically or abroad.

The Report issued by the New York City Bar Association addresses the *manner* in which lawyers can meet their ethical obligations when sending work abroad. The Report discusses the obligations to (1) provide competent work and supervision, (2) preserve client confidences, (3) avoid conflicts of interest, (4) make adequate client disclosure and obtain informed consent, and (5) avoid aiding in the unauthorized practice of law. It cautions that physical separation, language barriers, and the differences in legal systems and training in the remote location may pose challenges that cannot be overcome sufficiently to ethically outsource services abroad – but the Report also provides guidance on how to overcome those challenges. Preserving client confidences, for example, may mean something entirely different in the foreign jurisdiction, such that outsource providers may be permitted or even required to divulge information that U.S. law firms are obliged to safeguard. The security of digital data abroad may be different in that electronic client data is more vulnerable to theft, such that law firms may need to require their outsource providers to increase their protective measures before transmitting client information. Likewise, the difference in customs may require unusual steps be taken to ensure that the foreign provider does not have a conflict of interest.

Risk Management Solution: When considering outsourcing either legal or support services, it is essential that law firms understand any material differences in the foreign legal system (such as rules relating to privilege and client confidences). Law firms should identify how the foreign provider tracks clients in order to avoid conflicts of interest, and determine whether electronic information transmitted will be secure. Foreign providers should be interviewed with references checked, and the law firm should gain an understanding into their business practices and supervisory hierarchy. Outsourcing firms should also determine whether the provider has liability insurance and whether it covers the contemplated services. Clients need to be informed in advance of any outsourcing and ideally should consent in writing to the arrangement. Above all, it is recommended that lawyers retain full responsibility for any work product, and utilize it only after a thorough vetting for quality.

E-mails – Use of Employer Provided Addresses and Technology – (Loss of) Attorney-Client Privilege

***Leor Exploration & Production LLC et al. v. Aguiar*, Nos. 09-60136 and 09-60683, S.D.Florida, 2009 WL 3097207 (Sept. 23, 2009)**
***Convertino v. U.S. Department of Justice,* No. 04-0236 (RCL), D.D.C., 2009 WL 4716034 (Dec. 10, 2009)**
***Stengart v. Loving Care Agency, Inc.,* 973 A.2d 390 (N.J.Super.A.D., June 26, 2009)**

Risk Management Issue: How should lawyers address the problem that e-mails sent from their clients' employer-provided e-mail addresses, or communications from clients who use their employer-provided techology to communicate, may not be attorney-client privileged communications?

Editors' Note: This question has previously been discussed in connection with the decision in *Scott v. Beth Israel Medical Center Inc,*. in the *Lawyers' Lawyer* (Vol. 13, Issue 3, April 1, 2008). Three more decisions have recently been handed down considering the same issue.

The Cases: In *Leor Exploration & Production LLC et al. v. Aguiar*, the court considered whether documents the client transmitted by e-mail, using the adverse party's server, thereby lost the attorney-client privilege under Florida law. Citing *In Re Asia Global Crossing, Ltd.*, 322 B.R. 247, 257 (SDNY 2005), and recognizing that these cases must be decided on a case-by-case basis depending on their own facts, the court identified four factors to be considered in determining whether an employee has an expectation of privacy in computer files or e-mail. "These factors are: (1) does the corporation maintain a policy banning personal or other objectionable use, (2) does the company monitor the use of the employee's computer or e-mail, (3) do third parties have a right of access to the computer or e-mails, and (4) did the corporation notify the employee, or was the employee aware, of the use and monitoring policies?"

On the facts, the court concluded that in this case, each of the above factors was indeed present such that there was no reasonable expectation of privacy regarding communications transmitted through the employer's e-mail server, and the court therefore held that the privilege had been lost. Specifically, the court noted that the company's employee handbook advised that the employer owns all electronic communications:

> The [employer's] employee handbook expressly states: "Employees should have no expectation of privacy with regard to communications made over [the employer's] systems." The employee handbook further advises that "[the employer's] representative may access and monitor the use of its systems and equipment from time to time" and that "employees should not use [the employer's] electronic . . . communications systems to communicate, receive, or store information that they wish to keep personal or private." Thus, the Court finds there was no reasonable expectation of privacy regarding communications transmitted through [the employer's] email server.

In *Convertino v. United States Department of Justice*, the plaintiff had filed a complaint against the U.S. Department of Justice (DOJ) alleging that the defendant had willfully and intentionally disclosed information to a reporter for the *Detroit Free Press* in violation of the Privacy Act, 5 U.S.C. §552a. The disclosed information most likely consisted of one or more documents from an investigation into plaintiff's conduct by defendant's Office of Professional Responsibility (OPR). Notably, in considering whether e-mails sent and received by the plaintiff to and from his attorney using his government e-mail address and over the government's server were nevertheless entitled to be treated as privileged, the court cited precisely the same four-prong test from the *In Re Asia Global Crossing, Ltd.* case relied on in *Leor v. Aguiar* — but it reached the opposite conclusion.

Noting that "[e]ach case should be given an individualized look to see if the party requesting the protection of the privilege was reasonable in its actions," the court found in this case that the plaintiff's expectation of privacy was reasonable. The policy maintained by the DOJ did not ban personal use of the department's e-mail, and although the DOJ did have access to personal e-mails sent through this account, the plaintiff "was unaware that they would be regularly accessing and saving e-mails sent from his account. Because his expectations were reasonable, [plaintiff]'s private e-mails will remain protected by the attorney-client privilege."

In *Stengart v. Loving Care*, an employee sent e-mails to her attorney using a company-issued laptop computer through a personal, password-protected web-based (Yahoo!) e-mail account. The e-mails concerned a lawsuit the plaintiff/employee contemplated bringing against her employer, and were sent to the employee's personal attorney prior to her resignation from the company. The employer obtained the e-mails after the [then former] employee sued the company, by making a forensic image of the computer's hard drive and extracting them from the plaintiff's internet browser history.

There was a factual dispute in *Stengart* over whether the company's electronic communications policy was in effect or was merely in draft form at the time she sent the e-mails, and whether the policy applied to the plaintiff (who was an executive). While the New Jersey appellate court noted that the privilege issue should not have been decided absent an evidentiary hearing, it ultimately concluded that the words in the handbook did not convey a clear and unambiguous warning that the employer might attempt to seize and retain personal e-mails sent through the company's computer via the employee's personal e-mail account. The policy explicitly permitted "occasional personal use" of its systems. The court concluded that the e-mails were privileged on public policy grounds, holding that the policy considerations underlying the attorney-client privilege "substantially outweighed" the company's interest in enforcing its computer use and electronic communications policy.

Comment: These cases reinforce the conclusions suggested in our discussion of the earlier case that where a company clearly, explicitly and unequivocally prohibits personal use of its equipment, and advises its employees that it reserves the right to monitor and review their electronic communications and does so, then such employees will have difficulty claiming that communications sent to their attorneys using the employer's technology are entitled to the protection of the attorney-client privilege because they simply had no reasonable expectation of privacy.

Risk Management Solution: Lawyers representing individual clients should consider giving explicit advice at the outset of every representation regarding the use of e-mails for communications that the client or the lawyer wish to have treated as confidential. Conversely, counsel for organizations should consider advising their clients of the need for carefully formulated, strongly worded policies regarding employees' lack of expectation of privacy, and for diligently and repeatedly circulating these policies to all of their employees. Even where counsel for an organization is confident that the client's policy effectively removes its employees' expectation of privacy, an attorney who receives potentially privileged or confidential information of an individual that was intercepted by the organization pursuant to the policy should take great care before unilaterally deciding either to read or to use the intercepted material. In particular, counsel should consider whether the applicable rules of professional responsibility and case law regarding the privilege require some form of notice to the employer, in order to establish the scope of ethical and legal duties under the circumstances presented. Failure to consider the relevant law and rules before using information obtained from employee e-mails may result in disqualification or sanctions, including a directed adverse outcome in the underlying dispute.

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