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The Lawyers' Lawyer Newsletter

Recent Developments in Risk Management

In-House Counsel – Admission to the Bar – Loss of Attorney-Client Privilege When General Counsel Not Admitted in Jurisdiction of Principal "Practice"

Gucci America, Inc. v. Guess?, Inc., 2010 WL 2720015 (S.D.N.Y. June 29, 2010)

Risk Management Issue: What should be done to ensure in-house counsel maintain an active license and continuing good standing to practice law, and what are the consequences when in-house counsel fail to maintain such a license?

The Case: U.S. Magistrate Judge James L. Cott held that corporate plaintiff Gucci's communications with its in-house attorney were not privileged because the lawyer was not an active member of any state's bar. Judge Cott reached this conclusion under two separate attorney-client privilege tests.

The first test, which was based primarily on Southern District of New York (S.D.N.Y.) precedent, required that the attorney be "a member of the bar of a court." The lawyer was an inactive member of the California bar, and the court made clear that the attorney's status as an inactive member of the Bar did not meet this standard. In reaching this conclusion, the court stated that it did not matter whether the attorney's inactive status was voluntary or involuntary (i.e., resulting from disciplinary sanctions). The court focused on the fact that in California the practice of law is explicitly limited to active bar members. Further, although the lawyer had been admitted in two California federal districts, Judge Cott noted that such admissions required a present license to practice. Thus the attorney was constructively suspended from practice in both districts when the lawyer failed to maintain active law licensure in California.

The second test was based on U.S. Supreme Court Standard 503, which requires that a client reasonably believe the attorney to be authorized to practice law for the privilege to apply. Judge Cott relied on a factually similar S.D.N.Y. opinion written by U.S. Magistrate Judge Ronald L. Ellis and held that the lawyer's employer, plaintiff Gucci, did not have a reasonable basis to believe that the lawyer was authorized to practice law because Gucci never investigated the attorney's qualifications. At a minimum, Judge Cott opined, the employer must at some point confirm the attorney's licensure to practice law in some jurisdiction without suspension or pending disciplinary sanctions.

In-House Counsel – Admission to the Bar, continued on page 2

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Risk Management Solution: In-house counsel departments should institute the same kinds of controls that are customary in law firms to ensure that all those who are held out as lawyers within the entity are in fact licensed and duly admitted in each jurisdiction where they practice. Such procedures will protect the attorneys individually and collectively and also demonstrate the corporate employer-client's interest in ensuring that all in-house counsel retain licensure.

Ensuring proper licensure may be complicated when in-house legal staff are required to travel to and advise in multiple jurisdictions on behalf of their employer or, as occurred in this case, the lawyer moves between legal and non-legal roles. A detailed understanding of the adoption (or not) of ABA Model Rule 5.5 (multijurisdictional practice) wherever in-house counsel regularly operate, and of the registration procedures for in-house lawyers now available in many states, are now essential for all general counsel.

Fee-Sharing Agreements Between Law Firms – Client Consent and Notification Requirements

Eng v. Cummings, McClorey, Davis & Acho, PLC, 611 F.3d 427 (8th Cir. July 9, 2010)

Risk Management Issue: What are the implications of failing to obtain a required written client consent for a fee-sharing agreement between law firms?

The Case: The law firm of Cummings, McClorey, Davis & Acho, PLC (CMDA) referred a wrongful death case to the law firm Eng & Wood (E&W). The firms exchanged letters confirming their agreement that CMDA would receive one-third of whatever E&W received in fees on the wrongful death case referred. E&W then entered a fee agreement with two of the decedent's family members who would serve as plaintiffs in the wrongful death case. E&W's fee agreements with the two family members were silent regarding any fee sharing with CMDA. CMDA sent one of the two family members a letter notifying them of the fee-sharing arrangement between CMDA and E&W, but neither family member client consented in writing to CMDA receiving part of any fee that E&W received.

E&W ultimately recovered more than $1.1 million total for the two clients, and collected attorney fees totaling $375,000. E&W then sent CMDA a check for $18,562.50, approximately five percent of the total fees that E&W had received. CMDA demanded more, and E&W filed a declaratory judgment action, seeking a declaration that CMDA had no right to any portion of the attorney fees that E&W earned on the wrongful death case referred to E&W by CMDA. CMDA responded with counterclaims including fraud, misrepresentation and unjust enrichment.

The trial court entered judgment for E&W. On appeal, the U.S. Court of Appeals for the Eighth Circuit affirmed. CMDA lacked the written consent from the clients to share in the fee, although such consent was required by the then-effective version of Missouri Supreme Court Rule 4-1.5(e). A divided Eighth Circuit panel also affirmed the trial court's dismissal of fraud and unjust enrichment claims, stating that such claims could not be used to circumvent the Rule's requirement for written client consent to a fee-sharing agreement and enforce an unenforceable agreement.

Comment: State rules differ regarding what information clients must receive and what form the client's consent must take before law firms will have an enforceable fee-sharing arrangement. State courts also differ regarding when a firm may avoid sharing fees based upon inadequate client consent. Yet this case serves as a powerful reminder that if a firm wants to share in a fee, it should take care to comply with all client consent requirements for such fee sharing. An agreement between firms without adequately memorialized client consent may result in a fee-sharing arrangement that is not enforceable.

Risk Management Solution: When a law firm seeks to refer work to nonfirm lawyers and share in those lawyers' fees, the referring firm should independently ensure that all necessary prerequisites for the fee sharing are satisfied. The referring firm is also wise to obtain written client consent from all affected clients and firms involved in the arrangement at the outset of the matter. Law firms should never enter into these arrangements without an explicit writing between them that each will comply with applicable ethical requirements, and each will give notice or verification to the other that it has complied.

Attorney-Client Privilege – Inadvertent Waiver

Leader Technologies, Inc. v. Facebook, Inc., 2010 WL 2545960 (D. Del. June 24, 2010)

Risk Management Issue: What must law firms do to protect client confidences when the client wishes to disclose confidential information to a third-party financing company?

The Case: U.S. District Judge Joseph Farnan was asked to review a pre-trial order by U.S. Magistrate Judge Leonard Stark compelling Leader Technologies, plaintiff in a patent matter, to produce to defendant Facebook certain documents, which Leader had previously shared with third-party financing companies. In seeking review, Leader argued that the documents were privileged and only exchanged with the third-party financing companies after establishing a "common legal interest," because the companies were interested in financing the litigation.

In the prior decision, the magistrate judge had recognized that the common interest doctrine is an exception to the general rule that attorney-client privilege is waived following disclosure of privileged information to a third party because "it is reasonable to expect that parties pursuing common legal interests intended resultant disclosures to be 'insulated from exposure beyond the confines of the group.'" Yet the magistrate judge determined Leader had not established that an adequate common interest existed. Moreover, ethics opinions from Pennsylvania and New Jersey both indicated that privilege might be waived for documents shared with litigation financing companies. Finally, Magistrate Judge Stark concluded that no common legal interest protecting attorney-client or work product privileged information could exist because a deal was never actually consummated between Leader and the litigation financing companies.

Taking up Leader's request for review, District Judge Farnan found Magistrate Judge Stark's analysis was not clearly erroneous or contrary to law and directed Leader to produce the documents at issue.

Risk Management Solution: Law firms should advise their clients that information they share with others, such as third-party vendors or service providers, will not be privileged. Clients should be informed, in writing if appropriate, that they need to take care when making disclosures about confidential or proprietary information. Likewise, lawyers should not simply rely on the "common interest doctrine" without ensuring that it applies to the proposed communication or disclosure. After all, if the protection does not apply, a court may determine that the attorney-client privilege has been waived.

Disqualification – Patent Litigation Counsel Not Per Se Subject to Patent Prosecution Bar

In re Deutsche Bank Trust Company Americas LLC, 2010 WL 21069757 (Fed. Cir. May 27, 2010)

Risk Management Issue: What can law firms, especially intellectual property firms, do to limit their risk of disqualification because of subject matter conflicts of interest?

The Case: Patent infringement litigation was commenced by plaintiffs Island Intellectual Property LLC, LIDS Capital LLC, Double Rock Corporation, and Intrasweep LLC (collectively "Island") against defendants Deutsche Bank Trust Company and Total Bank Solutions, LLC (collectively "Deutsche Bank"), over three patents relating to financial sweep services. The patents at issue stemmed from a common parent patent application. When the infringement suit was filed, Island had multiple other patent applications pending that also related to deposit sweep services.

Deutsche Bank applied to the court for a "patent application bar," that would disqualify Island's litigation attorneys from participating in the patent application process for this particular set of related patents. The patent application bar would prevent "anyone who gains access in the litigation to documents marked 'confidential-patent prosecution bar' from any involvement in prosecuting any patent in the area of 'deposit sweep services' during and for a limited period after the conclusion of this litigation." After a short hearing, the magistrate judge granted Deutsche Bank's request but, without comment, exempted Island's lead trial counsel from the patent application bar. The district court adopted the order that exempted Island's lead trial counsel from the patent application bar, and Deutsche Bank sought a writ of mandamus.

The U.S. Court of Appeals for the Federal Circuit found that the district court had "properly refused to adopt a rule amounting to a per se prohibition on the use of litigation counsel who also prosecutes patents." Nevertheless, the Federal Circuit reversed the district court order. The Federal Circuit held that opponents moving for such a patent bar are required to demonstrate that the information designed to trigger the bar and the duration and subject matter of the bar "[reflect] the risk presented by the disclosure of proprietary competitive information." An attorney seeking to be exempted from the bar must show that the lawyer's representation of the client before the U.S. Patent & Trademark Office and the subject matter of the litigation are such that there is little risk that counsel will inadvertently use sensitive information to the opponent's competitive disadvantage.

Comment: This patent law case has implications for law firms that regularly represent multiple clients in the same industry, where those clients may compete with one another. Moreover, on remand, the scope of Island's attorney-client relationship with counsel will be directly at issue. To avoid the bar, counsel will need to show that the scope of representation does not extend to involvement in the client's "competitive decision making," such that the risk of its use of confidential information from the case would be enough to bar counsel from prosecuting patent applications related to the infringement case. This highlights the need for attorneys and clients to have a clear and explicit understanding of the scope of the lawyer's engagement and what limitations exist, if any, on counsel's role as legal advisor.

Risk Management Solution: The scope of an attorney's representation should be clearly defined in an initial engagement letter or agreement. It should also be reviewed periodically, especially during long-term relationships. Engagement letters ought also to contain clear language identifying how the law firm will deal with subject matter conflicts involving multiple clients in the same industry in order to minimize the risk that a lawyer will be disqualified from representing any such clients when subject matter conflicts arise. The temptation to define the scope of representation broadly and generically needs to be avoided in order to protect the lawyer and the clients against unnecessary disqualifications.

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