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*Lawyer-Client Relationship*

## Panelists Explore Ins and Outs Of Well-Drafted Engagement Letters

CHICAGO—Although lawyers may think of engagement letters as boring paperwork that is potentially off-putting to clients, these documents are vital for managing client expectations, preventing complaints, and defending claims, according to a panel discussion held here Feb. 17 at the 10th Annual Legal Malpractice & Risk Management Conference.

Lawyers often see themselves as victims but ''we are almost always the masters of our own fate,'' and engagement letters are one way for lawyers to control the risk of malpractice claims, moderator Peter R. Jarvis said in launching the program on ''Don't Ignore the 'Basics'—Engagement, Disengagement and End-of-Representation Letters.'' Jarvis is a partner in the Portland, Ore., office of Hinshaw & Culbertson, the primary sponsor of the conference.

Panelist Bruce D. Elliot noted that drawing up a retention letter gives lawyers and clients the opportunity to have a ''coming to reality'' discussion that sets clear expectations for the representation. Getting sued is really not about substantive issues, it's about the failure to manage expectations, said Elliot, a vice president in professional liability claims at the Travelers Cos. in St. Paul, Minn.

Engagement letters are the first thing that lawyers and courts look at in malpractice cases, panelist Lauren B. Shy noted. She is assistant general counsel of Fragomen, Del Rey, Bernsen & Loewy, a large immigration law firm in New York.

**Reasons for Engagement Letters.** Lawyers offer a range of reasons for not bothering with engagement letters, according to the program materials. Excuses include ''I hate bureaucracy,'' ''if it ain't broke. . .,'' ''my clients will be offended,'' ''other partners don't do it,'' and ''it's boring.''

But there are plenty of reasons for making the effort, the materials make clear. Engagement letters may be required by statute or professional conduct rules; they are ''Exhibit A'' in defending subsequent civil litigation and bar complaints; they can reduce conflicts risks; and they can make the difference between summary judgment and triable issues of fact. Moreover, if Dr. House of TV fame is correct in saying ''Everybody lies,'' engagement agreements can help disprove a client's falsehoods about the lawyer-client arrangement.

The materials also identify some positive reasons for engagement letters: they're consistent with ethics requirements for competence, diligence, and communication; they avoid good-faith misunderstandings; they can generate additional work authorized by the client; they can address file retention and destruction; and they offer potential control of the forum for malpractice claims.

**Manage Client Expectations.** Every one of the panelists made the point that engagement letters, and the process of doing them, can help frame the client's expectations.

You can say to the client, ''We need to make sure we have the same expectations,'' Jarvis suggested.

### Checklist for Engagement Letter

*Materials accompanying a panel discussion on ''Don't Ignore the 'Basics'—Engagement, Disengagement and End-of-Representation Letters,'' at the 10th Annual Legal Malpractice & Risk Management Conference provided this list of 16 components for an engagement letter:*

- Who is and is not a client.
- Scope of work/duty, as well as exclusions and limitations.
- Who is and is not liable to the firm, and for what.
- Rate or basis of the fee, including potential changes of hourly rates.
- Basis for acceptance of additional work.
- Advance deposits or retainers for fees and/or costs and expenses.
- Reporting obligations to and from firm.
- When/how representation will end.
- File retention or destruction.
- ADR and forum/law choice.
- Client signature or e-mail approval.
- Timing of invoices.
- When payment is due.
- Interest issues.
- Withdrawal issues.
- Conflicts issues.

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Shy recommended that the attorney call the prospective client, explain why an engagement letter is important, and set up a time to answer questions. ''Use it as another valuable point of contact with the client'' as a matter of improving client relations, she said.

Elliot pointed out that lawyers dealing with institutional clients often fail to use engagement letters because they like to present themselves as the client's fireman, who can be called at any time for any reason. Lawyers need to set reasonable expectations, and retainer letters can help do that, in his view.

If there is no engagement letter and a claim is made against the lawyer years later, it's not so much that people will lie as that no one will really know for sure what the agreement was, Elliot said.

Jarvis said that he uses e-mail for engagement letters because it's easier to get them back. If the client doesn't return the message with an agreement to its terms, that's a red flag, Jarvis said. He suggested saying to the client, ''If there's a term you don't like, tell me.''

Jarvis noted that in a malpractice action against Davis Polk & Wardwell, a single sentence in the engagement agreement about the scope of work made all the difference, resulting in a dismissal of the plaintiff's case. See *AmBase Corp. v. Davis Polk & Wardwell*, 834 N.Y.S.2d 705, 23 Law. Man. Prof. Conduct 243 (N.Y. 2007).

Under ABA Model Rule 1.2, Jarvis pointed out, any limitations on the scope of representation have to be in writing and agreed to.

Shy added that if events after the engagement letter change the scope of representation or who the lawyer represents, the change needs to be documented in an e-mail or other written communication to the client(s).

**Form Engagement Letters.** The panelists were not keen about the idea of putting terms and conditions on a firm's website and referencing those terms for an engagement agreement.

Rather than just having a standard agreement, a firm should tailor it to the particular situation, Shy commented.

In Elliot's view, the website approach may be acceptable when lawyers are certain they understand their niche. But if there's variety in your practice, you're starting out on the wrong foot, he said.

Jarvis noted that it can be difficult to vary a standard agreement. And if the standard agreement is really long, he asked, do you really need all that?

From the audience, Ronald Ryland of Sheppard, Mullin, Richter & Hampton in San Francisco commented that in litigation matters lawyers really need the engagement letter, and so any term of consequence should be in the letter. But if the engagement letter is too long to read to the client, think about revising it, he added.

**Heading Off Conflicts.** Clear identification of clients in an engagement letter can help lessen the assertion of claims alleging disloyalty and breach of fiduciary duty, the speakers remarked.

''When the engagement letter is nonexistent or unclear, we may not know for sure if there's a client for conflict purposes,'' Elliot pointed out.

Shy observed that lawyers need to be clear who they represent whenever they will be working with more than one person, such as an employer and employee.

From the audience, an attendee asked the panel how successful it is for the engagement letter to say ''We are not representing your affiliates.''

It works, Jarvis responded, unless you've done something inconsistent with that statement. It's important for the engagement agreement to state ''We represent X and only X,'' he suggested, but he added that sometimes the firm has to come back during the representation and say ''Remember we don't represent Y.''

**Fee Provisions.** The engagement letter should clearly set out the firm's fees and explain what the firm usually does to collect them, Elliot said. He noted that a large percentage of malpractice claims come when law firms are chasing fees.

Malpractice claims are cooked up in a stew that includes disappointing results, substantive errors, and poor client communication, he said, and when this volatile situation exists a huge bill from the law firm serves as a trigger. Accordingly, Elliott advised, the engagement letter needs to set clear expectations about fees—and the firm must follow them.

Shy noted that law firms are facing increasing pressure to charge flat fees. A flat-fee retainer agreement can be drafted, she said, to leave a window to revise the fee arrangement if the law or regulations materially change, or if the client wants additional services.

**Components of End-of-Representation Letter**

*Materials accompanying a panel discussion at the 10th Annual Legal Malpractice & Risk Management Conference suggested several components for an end-of-representation letter:*

- We think we are done.
- Anything else you'd like us to do at this time?
- Identify client monitoring or other responsibilities.
- Offer to be hired on additional matters?

Jarvis emphasized the need for clarity about fees, and who will pay them. If there are multiple clients, the engagement agreement can specify joint and several liability for fees, he suggested. And if no deposit is being charged, he added, the retainer letter may say that the firm reserves the right to charge a deposit if the client falls behind on payment.

Jarvis suggested not including a provision that states the firm will contemplate the possibility of altering or amending its fees depending on results. If the results are negative, that clause can backfire, he pointed out.

**What Else to Include (or Not).** The engagement letter is a useful place to address the eventual disposition of client files and property, Shy told the audience. In particular, she mentioned New York City Ethics Op. 2010-1, 26 Law. Man. Prof. Conduct 100, which advised that lawyers may agree with clients in advance which items in their file the lawyer will return, discard, or save once the representation concludes. The opinion provides a sample engagement letter that specifies how file

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documents will be handled once the representation is over.

Almost all ethics opinions in recent years conclude that the lawyer is much better off to address this issue in engagement agreements, Jarvis commented.

On the wisdom of specifying the forum for lawyer-client disputes, Elliot said this issue is not amenable to a one-size-fits-all solution. ''It's good to be in control of the forum, but it's hard to know what's the best forum,'' he said.

He pointed out that the defense of malpractice claims is rich in issues and lends itself to motion practice. Agreeing to arbitrate all disputes is frustrating if the arbiter turns out to have a ''split the baby'' mentality, he said. Reacting to that point, Jarvis speculated that lawyers may want clients to agree to arbitrate fee disputes but not malpractice claims.

Jarvis noted that an engagement letter may specify the basis for the firm's acceptance of additional work; for example, it could state that additional work will only come from a particular individual.

Jarvis questioned the value of having the engagement agreement say that the firm can withdraw ''for any reason or no reason.'' You usually can't withdraw for any reason or no reason, so why say that, he commented.

Jarvis also cautioned against using superlatives in engagement agreements, because they could end up raising the duty of care. Any guarantee of success should also be avoided, Shy noted.

**Clients Push Back.** The panel noted that firms are increasingly being confronted with client pushback regarding retainer agreements, resulting in a ''battle of the forms.'' Examples include RFP (request for proposals) boilerplate, master service agreements, and comprehensive outside counsel guidelines, which are being used even for nonlitigation matters.

Jarvis noted that some of these documents even say the law firm assumes all liability without regard to fault. Shy confirmed that she has seen such clauses. Outside guidelines or form agreements for engagements should be reviewed closely to see whether the law firm is being asked to agree to something it shouldn't, she urged.

Even when a firm goes along with a client's agreement, Jarvis commented, it may still want to clarify some points, such as confirming its understanding about whom the firm does and does not represent.

**End-of-Representation Letters.** The panelists also emphasized the value of end-of-representation letters for avoiding misunderstandings, heading off conflicts of interest, and starting the clock running on many claims. An end-of-representation letter can also be useful to document aspects of the representation, even for the first time, Jarvis pointed out.

He noted that an end-of-representation letter doesn't have to be negative or a high act of ''CYA.'' You don't have to say ''You have 87 days to sue me,'' or even ''you're not our client anymore.'' Instead, you can say ''We've completed this matter and we're closing our file.'' Or you can write to the client and say ''I'm think I'm done. Is there anything else?'' The client may say yes, Jarvis remarked.

Not infrequently, a conflict dispute arises because a representation remains ongoing without the lawyer's realizing it, the speakers said. There are a growing number of cases, Jarvis stated, where failure to have a disengagement letter is the biggest factor in finding a continuing attorney-client relationship.

Jarvis also noted that it is almost always a benefit to a law firm to get the limitation period started on any claim the client may assert against the firm. Elliot agreed, pointing out that when a jurisdiction has a short statute of limitations, as is often the case for malpractice claims, a month or even a day can make a big difference.

For a large client, should there be an end-of-representation letter for each matter? On this question, Jarvis noted that ''there are certain issues you may want to close out.'' Explain that you want to make sure you're on the same page and that there are no misunderstandings, he recommended.

At least send an end-of-representation letter to clients you never want to see again, he added.

**Disengagement, Nonengagement Letters.** The panelists also discussed disengagement letters when withdrawing from a representation, and ''nonengagement'' letters to prospective clients who did not actually hire the firm.

According to the program materials, reasons for these letters include: to confirm work done or not done, and what the client must then do; to avoid or at least reduce conflicts and the possibility of continuing duties; to start the statute of limitations; to address file retention or destruction; and perhaps to confirm the reason(s) for the disengagement.

Regarding disengagement letters, Jarvis posited that where the party is a former client, information about imminent deadlines should be provided.

Shy commented that a nonengagement letter is more difficult. What do you say when there's no attorney-client relationship, and to what extent do you identify what that person needs to do? she wondered.

### Disengagement/Nonengagement Letters

*Materials for a panel discussion at the 10th Annual Legal Malpractice & Risk Management Conference included a checklist of components for a disengagement or nonengagement letter:*

- We are done/we were never there.
- Suggest seeking other counsel?
- Possible time limits?
- Possible statement of reasons?
- Limitations on use of statements made?
- File or document retention/destruction?
- Billing issues.

Elliot suggested that a nonengagement letter should be sent if the discussion with the prospective client came close to establishing an attorney-client relationship. He cautioned against stating any specific time limits, and instead advised lawyers to ''err on the side of caution'' by just encouraging the not-quite client to look for other counsel, or seek immediate counsel for a time-sensitive matter.

If nothing confidential was discussed in a meeting with a prospective client, a nonengagement letter could so state, Jarvis noted. He suggested a different approach for situations in which confidences were dis-

cussed and the jurisdiction has a ''full version'' of Model Rule 1.18, which allows screening measures to avoid imputation of conflicts from a lawyer in the firm who has learned potentially harmful confidences from a prospective client.

In that situation, he said, the nonengagement letter could state that, as the lawyer and prospective client discussed at the time, confidences were shared but will not prevent others in the firm from representing clients adverse to the prospective client.

By Joan C. Rogers

*Private Firm*

## Panel Finds That Meaning of 'Partner' Varies According to Reason for Asking

CHICAGO—When a lawyer has no ownership interest in a law firm, doesn't share in the firm's profit, doesn't vote on its management, and can be fired at will, there can be a variety of consequences if the firm chooses to call that lawyer a ''partner.''

So said panelists at a program on ''The Meaning of 'Partner' in the Changing Law Firm,'' presented Feb. 17 at the 10th Annual Legal Malpractice & Risk Management Conference in Chicago.

Examples they discussed are whether a nonequity ''partner'' has the right to examine the law firm's books, the circumstances in which a nonpartner lawyer may be expelled, the extent to which the firm and its true owners are responsible for the nontraditional partner's actions, and the potential disconnect between nonequity partners and obligations that ethics rules impose on ''partners.''

In explaining the impact of using the ''partner'' title, the speakers distinguished between jurisdictions that have adopted the Revised Uniform Partnership Act (RUPA)—which is most of them—and a small group of states—Delaware and two others—that don't require partners to have an economic interest. Nonequity partners are not even mentioned in RUPA but are specifically allowed in the Delaware model, according to panelist Robert W. Hillman, a law professor at the University of California, Davis.

Hillman and his fellow panelists discussed four contexts in which the meaning of ''nonequity partner'' may become an issue:

- figuring out rights and duties among lawyers in a law firm;
- understanding employment law protections;
- analyzing relationships with third parties; and
- figuring out ethical responsibilities.

The chameleonic concept of ''partner'' plays out differently in each one, the speakers explained.

**RUPA Has No Bananas.** Because RUPA doesn't refer to nonequity partners, ''we could call them 'bananas,' '' Hillman joked. The name stuck and his fellow speakers used it in their comments too.

Hillman emphasized that RUPA does not even define the term ''partner,'' much less nonequity partner. He explained that Section 101(6) of RUPA defines ''partnership'' as an association of two or more persons to carry on as co-owners a business for profit, and Section 202(a) states that a partnership is formed by the association of two or more persons to carry on as co-owners a business for profit.

From these sections, Hillman suggested, it can be inferred that a ''partner'' is one of these people populating a partnership. But ''not a nanosecond of thought'' was given to the subject of nonequity partners during the development of RUPA, he said.

''Law firms have moved away from the traditional view of partner,'' he noted, and now use the ''nonequity partner'' label for a variety of situations, such as lawyers who are permanent associates, older partners who are reducing their practices, and lawyers in transition to becoming partners.

Nonequity partners are an important part of law practice, but ''partnership law is behind the curve'' in not recognizing this status, said Hillman, author of *Hillman on Lawyer Mobility* (2d ed. 2010) and *Law, Culture and the Lore of Partnership: Of Entrepreneurs, Accountability, and the Evolving Status of Partners*, 40 Wake Forest L. Rev. 793 (2005). He also is co-author of *The Revised Uniform Partnership Act* (2010-2011 ed.)

**Delaware Model.** Delaware takes a different approach, as does Colorado, and Texas ''sort of'' follows it, according to panelist Allen Sparkman of Sparkman + Foote in Denver, who is also of counsel to Houston-based Bond & Smyser.

According to materials accompanying the panel discussion, the key part of the Delaware model is Delaware Code Section 15-205, which addresses admission to a partnership without contribution or partnership interest. It defines ''partner'' as ''a person who is admitted to a partnership as a partner of the partnership,'' and allows admission as a partner ''without acquiring an economic interest in the partnership.''

In other words, a partnership is specifically allowed to have partners who are ''bananas,'' Sparkman remarked.

### Nonequity Partners—Risk Management

Materials accompanying a program on ''The Meaning of 'Partner' in the Changing Law Firm,'' presented at the Legal Malpractice and Risk Management Conference, offered these pointers for law firms that have nontraditional types of partners:

- Draft clear agreements that define rights and duties.
- Detail the expulsion process for all types of partners.
- Consider how lawyers are designated on website biographies.
- Where possible, organize in states that expressly permit nonequity status.

According to Sparkman, Colorado's partnership statute likewise provides for partners who have no economic interest in the partnership. See Colo. Rev. Stat. § 7-64-101(18) (defining partner as ''a person who is admitted to a partnership as a partner of the partnership''); Colo. Rev. Stat. § 7-64-205 (allowing partner to be admitted without making contribution or acquiring transferable interest). Colorado's change to the Revised Uniform Partnership Act was driven by the view that

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law firm practice had outstripped existing law, he said. The Texas statute is ''more subtle'' in that it lacks any express language about a partner's economic interest, he added.

Use of the term ''partner'' is common even in limited liability companies and professional corporations because no one wants to be called a ''member,'' Sparkman noted.

**Partnership, Employment Agreements.** Hillman commented that RUPA is supportive of partnership agreements and contracts, and those agreements ''can give bananas partner-like rights.''

He noted that it is common for firms to have nonequity partners sign both the partnership agreement and an employment agreement, but ''that's not necessarily appropriate,'' he said.

''I've never understood the logic of getting permanent nonequity partners to sign a partnership agreement saying you're not a partner,'' he said. In Hillman's view, it is preferable to have the partnership agreement define ''nonequity partner,'' and have the nonequity partners sign an employment agreement.

Sparkman pointed out, however, that in the few jurisdictions adopting Delaware's approach, the nonequity partner is a partner and should sign the partnership agreement.

But in that situation, the partnership agreement will have extensive provisions on nonequity partners, Hillman noted.

**Internal Partnership Rights.** According to the panelists, key issues relating to the rights of nonequity partners within law firms are access to information and expulsion/discharge. The governing approach—RUPA or the Delaware model—makes a big difference on these issues, the speakers made clear.

**''Law firms have moved away from the traditional view of partner.''**

ROBERT W. HILLMAN
UNIVERSITY OF CALIFORNIA, DAVIS

Hillman explained that RUPA provides broad information rights and does not allow agreements that unreasonably restrict those rights. A nonequity partner does not have information rights under RUPA, but a contract can give a nonequity partner these rights, he said.

According to Hillman, the Delaware model grants greater authority for firms to restrict information rights. Many law firms formed under Delaware law can be expected to restrict information rights for nonequity partners, he suggested.

Regarding expulsion and discharge, Hillman explained that under RUPA it is difficult to expel a partner but an employee can be fired. So nonequity partners in RUPA jurisdictions can be expelled from a law firm, he said.

Panel moderator Allison Rhodes, a self-described ''banana'' who is a nonequity partner in Hinshaw & Culbertson in Portland, Ore., commented that if a firm has a large stable of nonequity lawyers, it may want to consider whether the firm is underinsured for claims by employees and look into additional employment practices liability insurance, or EPLI.

**Employment Law Protections.** Rhodes asked the panel about nonequity partners and employment laws, such as the Age Discrimination in Employment Act.

''Partnership law isn't the last word on the status of people who are partners,'' Hillman said. ''Whatever your label or status is under RUPA, federal statutes have an entirely different definition of 'partner,' '' he explained.

Under cases interpreting federal discrimination statutes, he said, the real question is the extent of an individual's control and influence in the organization, not that person's title or status under state law. See *Clackamas Gastroenterology Assocs. v. Wells*, 538 U.S. 440, 19 Law. Man. Prof. Conduct 251 (2003), which held that the principal guidepost for deciding whether shareholders and directors of professional corporations count as ''employees'' under the federal employment discrimination laws is the extent of the corporation's control over them.

Courts are likely to conclude that in large firms even full partners can still be employees, Hillman said, explaining that the issue goes beyond whether the partnership agreement limits the lawyer's rights, extending to the degree of the lawyer's control in the partnership. The large size of a firm may mean that even a full partner has no control, he explained.

Sparkman noted that in a Colorado case not involving a law firm, sale of interests in limited liability partnerships were held to be the sale of securities under state law. The people who bought interests in the LLPs had extremely limited rights, he noted. (See *Toothman v. Freeborn & Peters*, 80 P.3d 804 (Colo. Ct. App. 2002).)

**Effect on Others.** Regarding law firms' relationships with those outside the firm, Hillman explained that under the traditional concept of partnership by estoppel a partnership can be deemed to exist for all purposes when a person holds himself out as a partner, even without a formal partnership agreement.

That concept is not relevant to nonequity partners, Hillman remarked, because RUPA replaced it with the more limited idea of ''purported partner,'' which refers to a person who is held out as a partner with authority to bind the partnership only as to specific third parties.

Hillman pointed out that on this subject agency law and partnership law overlap. Every lawyer is a firm's agent and can bind the law firm in certain ordinary matters, he said. Sparkman agreed that labels are not determinative of a lawyer's authority. A firm can authorize a lawyer to take actions regardless of the lawyer's label or status, he noted.

Law firms also are vicariously liable for an associate's malpractice, Hillman added. On the other hand, he noted, RUPA now allows limited liability partnerships in which partners themselves are not jointly responsible for each other's malpractice or the malpractice of other lawyers in the firm.

Hillman noted that if a firm is extremely risk-adverse, it could identify nonequity partners as such to prevent any possible misunderstandings. But if a firm is worried about a lawyer's conduct, there are probably bigger concerns, he observed, presumably referring to potential malpractice claims.

The panel noted that the issue of who is a ''partner'' in a firm can crop up in unexpected contexts. As an example, they cited *Morson v. Kreinlander*, 616 F. Supp.3d 171 (D. Mass. 2009), which involved the issue of diversity jurisdiction.

The court in that case held that complete diversity existed even though the law firm had a contract partner in the same state as the plaintiff, because the contract partner was effectively an employee despite his title. The opinion quotes the First Circuit in *Serapion v. Martinez*, 119 F.3d 982, 988 (1st Cir. 1997), as stating that the determination of whether an attorney is a partner or mere employee ''cannot be decided solely on the basis that a partnership calls—or declines to call—a person a partner.''

**Responsibilities of 'Partners.'** As for the ethical implications of ''partner'' labels, Rhodes noted that ABA Model Rule 1.0(g) defines a ''partner'' as ''a member of a partnership.'' A member of a partnership might include a nonequity partner, or even the firm's head dishwasher, she quipped.

The definition of ''partner'' matters, Rhodes said, because Model Rule 5.1(a) requires a ''partner'' in a law firm to make reasonable efforts to ensure that all lawyers in the firm conform to the professional conduct rules.

Together, she said, these two provisions create a ''circular, confusing'' reference. A nonequity partner probably has little control over the firm's docketing system and conflicts checks, particularly in other offices of the firm, she pointed out.

Hillman noted that the same problem can apply to equity partners when they lack any meaningful control over the firm's policies and systems. Rule 5.1 is a throwback to the old view of partnerships, he asserted.

Sparkman said there is a need to invoke a ''rule of reason'' in applying the two rules. He also noted that Colorado's version of RUPA allows partnerships to file statements limiting partners' authority.

Are law firms filing these documents? Rhodes asked. She speculated that Rule 5.1(a) is an attempt to hold someone in law firms accountable for ensuring professional conduct by lawyers in firms, given that law firms themselves cannot be disciplined in most jurisdictions.

The only way Rule 5.1(a) makes sense, Hillman suggested, is to make sure that a management structure is in place, get the right people, and ensure that they have systems for monitoring compliance with the rules. Partners can't absolve themselves completely but can do some delegation, he said.

**Misrepresentation Issue.** Rhodes also wondered about misrepresentation and reliance in the use of partnerships terms. She asked whether she could be viewed as misrepresenting her status, in violation of ethics rules, by calling herself a ''partner'' when she's really a ''banana''—a nonequity partner.

Rules potentially bearing on this issue include Model Rule 8.4(c) (conduct involving deceit, dishonesty, and misrepresentation), Model Rule 7.1 (false or misleading communication about lawyer or lawyer's services), and Model Rule 7.5(d) (forbidden to imply practice as partnership if not true), according to materials accompanying the panel discussion.

Rhodes noted that in New York County Ethics Op. 740 (2008), the ethics committee concluded that a lawyer who, according to the law of New York, is not a partner would violate ethics rules by calling herself a partner. The committee did not address whether a nonequity partner is a partner under New York law, she pointed out.

There's no such thing under New York law as a nonequity partner, Hillman said.

By Joan C. Rogers

*Malpractice*

## Panelists Review Practicality of Inserting Breach of Fiduciary Duty Counts Into Suit

CHICAGO—During a Feb. 16 session on ''Establishing a Fiduciary Breach,'' speakers at the 10th Legal Malpractice & Risk Management Conference addressed the practical impact of introducing a breach of fiduciary duty claim into a garden-variety malpractice action.

Traditional breaches, the panelists noted, include revealing a confidence, not disclosing a conflict, failing to turn over client funds, misrepresentation, and engaging in self-dealing—including transactions with clients.

Adding a breach of fiduciary count may be appealing from the plaintiff's perspective because the claim can extend the statute of limitations, lead to disgorgement of fees, and modify the burden of proof. The panelists cautioned, however, that those allures don't mean that plaintiff's counsel can take shortcuts in proving that a breach actually occurred and caused damage.

**Advantages Cited.** What are the practical consequences of injecting a breach of fiduciary claim into a malpractice action? asked moderator John W. Sheller, of Hinshaw & Culbertson's Los Angeles office. Are there advantages to tacking on a fiduciary duty claim?

There are some notable benefits to the plaintiff, replied panelist Murray J. Fogler, of Beck, Redden & Secrest, Houston. For example in Texas, he said, courtesy of *Burrow v. Arce*, 997 S.W.2d 229, 15 Law. Man. Prof. Conduct 300 (Tex. 1999), clients who establish that their lawyers violated a fiduciary duty may be entitled to a remedy of at least partial fee forfeiture without having to prove that the breach actually caused them any financial loss.

''Plaintiffs in breach of fiduciary actions sometimes get a more forgiving statute of limitations,'' added panelist Nancy Jane Marshall, who practices in New Orleans with Deutsch Kerrigan & Stiles. That's not the case in Louisiana, she said, but it is true in a number of other jurisdictions.

That is certainly true in Texas, Fogler noted, where breach of fiduciary duty claims have a four-year limitation period, as compared to the two-year window for standard malpractice claims.

Plaintiffs in Texas also benefit from ''pattern jury instructions that are so broad that it makes it difficult for a lawyer to defend,'' Fogler added.

The availability of disgorgement and punitive damages can make adding a fiduciary duty count appealing, the panelists also noted. In California, Sheller observed, a breach of fiduciary duty arising out of a conflict of interest will lead the court to look at disgorgement as a matter of equity.

In Texas, Fogler chimed in, it can affect the burden of proof. Texas courts apply a rebuttable presumption

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of unfairness to transactions between fiduciaries and those to whom a duty of disclosure is owed, he said.

**Still Must Prove Link.** The panelists emphasized that plaintiffs seeking to prevail in a breach of fiduciary duty case still must prove not only that there was a breach of a duty but also that there is a causal link between the breach and an injury. They focused on *Brown v. Green*, 302 S.W.3d 1 (Tex. App. 2009), to highlight this obligation.

In *Brown*, the former client sued his lawyer for breach of fiduciary duty after the lawyer began representing the former client's wife in their divorce. The husband had also sued to remove the lawyer and the husband's sister from their director positions in a charitable foundation.

In the breach of fiduciary duty litigation, the husband argued that the lawyer misused confidential information he had gained during the dozen years that he represented the husband in his business affairs. Specifically, he asserted that the lawyer abused his knowledge of the disparity in the parties' financial position and his knowledge of family dissension to wear the husband down emotionally and financially in both the divorce and the foundation litigation.

The trial court granted the lawyer's motion for summary judgment, ruling that the husband failed to establish that any protected information was passed on, let alone used in either matter, Fogler noted. Affirming, the appellate court ruled that even assuming the husband told the lawyer in confidence about the discrepancy in financial conditions, there was no evidence that the lawyer used the information that way.

What I found most instructive in this case, said Sheller, is that the husband tried to bootstrap a breach of fiduciary duty argument by arguing that the divorce and the foundation matters were so ''inextricably intertwined'' given the lawyer's close association with the family that the lawyer must have used the confidential information against his client.

But the court didn't buy the ''inextricably intertwined'' analysis, the panel observed. The allegation that confidential information ''must have'' been imparted ''does not logically flow from the evidence or arguments,'' the court said. It noted that the original petition in the foundation lawsuit mentioned ''irreconcilable differences'' but made no reference to any family dissension.

By Lance J. Rogers

*Malpractice*

## Panelists Review Recent Developments On Duty to Nonclients, Patent Malpractice

CHICAGO—Who can sue you, where can they sue you, and how will they prove their case?

At a Feb. 16 panel on ''Significant Developments in Litigating Legal Malpractice Claims,'' presented at the 10th Legal Malpractice & Risk Management Conference, speakers discussed attorneys' duties to nonclients and offered tips on predicting when a malpractice matter will land in federal court, particularly when the representation at issue dealt with intellectual property rights.

**Spot the Client.** Pamela A. Bresnahan of Vorys, Sater, Seymour and Pease, Washington, D.C., focused attention on an issue that crops up in almost every malpractice conference: what is the duty to nonclients and how are courts expanding that duty?

As an example of case law that has steadily expanded duties to third parties, Bresnahan pointed to *Branham v. Stewart*, 307 S.W.3d 94, 23 Law. Man. Prof. Conduct 134 (Ky. 2010), which held that an attorney retained by the next friend and guardian of an injured minor had an attorney-client relationship with the minor that allowed the minor to sue the attorney for malpractice.

The court reasoned that the minor was at all times the true party in interest, Bresnahan noted, even though the underlying action the attorney was retained to pursue was brought in the name of the child's mother as next friend and guardian.

Bresnahan's view is that the case essentially says lawyers have two clients and ''puts lawyers in an unbelievable conflict.'' Panel moderator David E. Jones, of Hinshaw & Culbertson's office in Peoria, Ill., agreed. ''Finding an attorney-client relationship here really puts this decision outside the mainstream,'' he said.

**''The circuit courts of appeal don't want state malpractice claims cluttering up their docket.''**

Kevin S. Rosen
Gibson, Dunn & Crutcher

Another member of the panel mildly defended the ruling. ''The court is basically saying to the lawyer 'you walked into a situation where the client's sole function is to protect the minor, yet you didn't do anything','' said Kevin S. Rosen of Gibson, Dunn & Crutcher, Los Angeles.

The court had a choice, Rosen stated: declare the minor unrepresented or declare the lawyer accountable. Right, countered Bresnahan, and it chose the minor over the lawyer.

**Admission of Error.** On a ''good news'' front for lawyers, Bresnahan called attention to *Schmitz v. Rinke, Noonan, Smoley, Deter, Colombo, Wiant, Von Korff & Hobbs Ltd.*, 783 N.W.2d 733 (Minn. Ct. App. 2010), which held that a client cannot establish a lawyer's breach of the standard of care merely because the lawyer admitted he had made a mistake.

The lawyer in *Schmitz* testified under cross-examination that he believed he had a duty to advise his client not to send a letter that acted as a repudiation of a contract. The lawyer admitted that he ''felt it was a mistake to send the letter.'' The client claimed that this admission obviated the need for expert testimony as to what the standard of care was and whether the lawyer breached that standard.

The court disagreed. There was a range of actions the lawyer could have taken, the court said, including advising the client not to send the letter, but also editing the letter in such a way as to reduce the risks. The fact that more than one reasonable response was available is precisely why the client should have produced expert testimony explaining the standard of care, it reasoned.

**Uniformity or Docket Clutter?** On another topic, Rosen told the audience that predicting whether a malpractice matter involving an element of patent, trademark, or copyright law will land in state or federal court depends not only on the allegations of the complaint but also, to some extent, on geography.

Under 28 U.S.C. § 1338(a), he explained, federal courts retain exclusive subject matter jurisdiction over actions ''arising under'' federal law, including actions arising under any act of Congress relating to patents, copyrights, and trademarks.

If the jurisdiction question involves patents and winds up before the U.S. Court of Appeals for the Federal Circuit, Rosen said, the odds are good that the malpractice case will end up in federal court since the Federal Circuit has repeatedly expressed an expansive view of federal jurisdiction under Section 1338(a).

''That's because the Federal Circuit puts a priority on uniformity in patent law decisions,'' Rosen said.

On the other hand, he added, other federal jurisdictions take a more conservative approach. ''The circuit courts of appeal don't want state malpractice claims cluttering up their docket,'' he stated.

**Case Within Case.** As an example of the federal court's underlying philosophy, Rosen pointed to *Air Measurement Techs. Inc. v. Akin Gump Strauss Hauer & Feld LLP*, 504 F.3d 1262, 23 Law. Man. Prof. Conduct 547 (Fed. Cir. 2007), which found federal jurisdiction over a patent malpractice matter because, the court said, the plaintiff could not prevail without becoming enmeshed in federal patent law when trying to prove that it would have prevailed in the case-within-a-case.

The client's argument that the attorney's errors allowed patent infringers to raise defenses centering on the invalidity and unenforceability of patent, the court said, involved substantial issues of federal law that are best handled by a federal court. Federal courts have exclusive jurisdiction over state-law malpractice actions when the adjudication of the malpractice claim requires the trial court to address the merits of the plaintiff's underlying patent infringement matter, the court reasoned.

The Federal Circuit reiterated this stance in January, Rosen pointed out, when it released *Warrior Sports Inc. v. Dickinson Wright PLLC*, 2011 U.S. App. LEXIS 521, 27 Law. Man. Prof. Conduct 30 (Fed. Cir. Jan. 11, 2011). The court found that the district court should have assumed jurisdiction over a malpractice action against patent attorneys where at least one of the client's claims required resolution of a substantive issue of patent law. The client was claiming that but for its attorneys' alleged malpractice it would have recovered even more money from a competitor that it sued for infringing the client's patent.

**More Conservative Approach.** Exemplifying the more conservative approach taken by other courts that are less enthusiastic about invoking federal jurisdiction, Rosen said, is *Singh v. Duane Morris LLP*, 538 F.3d 334, 24 Law. Man. Prof. Conduct 406 (5th Cir. 2008). In *Singh*, he noted, the court concluded that the malpractice case did not ''arise under'' federal law even though proof of the malpractice claim would require delving into trademark law. Just because a case requires resolution of a federal question does not automatically confer jurisdiction, the court said.

The court acknowledged that the plaintiff would, as part of his case-within-a-case, try to prove that his trademark brand had a secondary meaning, but reasoned that this federal issue was not sufficiently ''substantial'' to invoke federal jurisdiction as it was predominantly a factual question.

Rosen suggested that this was a very ''loose interpretation of the term substantial.''

Also illustrative of this conservative approach, Rosen added, is *Eddings v. Glast*, 2008 U.S. Dist. LEXIS 48589 (N.D. Tex. June 24, 2008), where the court remanded a malpractice case to state court, ruling that the patent law issue was not essential to the resolution of the action because the malpractice case could be resolved without settling the patent law question.

According to Rosen, the court plucked the following language from *Air Measurement* to justify its refusal to accept removal of the case: ''If there is a theory upon which [plaintiffs] can prevail on their malpractice claim that does not involve a substantial patent law question, then patent law is not essential to the malpractice claim, and § 1338 jurisdiction is lacking.''

Rosen mused whether such a stance could ''swallow the rule'' and make it easy for a plaintiff to avoid federal court. Conceivably this could give plaintiffs ''a lot of power to frame removability by alleging multiple claims,'' he stated.

**Framing the Issue.** Picking up on this thread, the speakers said that the more a claim looks like a garden-variety malpractice suit, the less likely it will land in federal court.

For example, Rosen observed, in *Lockwood v. Sheppard, Mullin, Richter & Hampton*, 93 Cal. Rptr.3d 220 (Cal. Ct. App. 2009), the state court reasoned that a federal court possessed exclusive jurisdiction over the client's contention that he was injured by his lawyers' misrepresentations before the U.S. Patent and Trademark Office. The court stressed that the damage calculus would require evaluating whether the PTO would have granted a reexamination request in the absence of those misrepresentations.

By contrast, Rosen noted, a different California appellate court came to a contrary conclusion in *E-Pass Tech. Inc. v. Moses & Singer LLP*, 117 Cal. Rptr.3d 516, 26 Law. Man. Prof. Conduct 694 (Cal. Ct. App. 2010). That court found that federal jurisdiction was lacking because the issue was a fairly standard malpractice question: Did a law firm give negligent advice in counseling the client to pursue what the firm allegedly knew was a doomed strategy of filing patent infringement lawsuits?

According to the court, Rosen said, ''the legal question there was no different from that presented in other malpractice actions: whether a reasonable attorney would have pursued the underlying case, which is not a question of patent law.''

**Estoppel.** One argument that crops up occasionally, Rosen said, is the contention that there is no need to engage in a case-within-a-case dialogue because ''the case has already been decided, so we already know what the outcome was.'' I see this a lot, but courts should reject it, he remarked.

Illustrative of this issue, Rosen said, is *Byrne v. Wood, Herron & Evans LLP*, 2008 U.S. Dist. LEXIS 61962 (E.D. Ky. Aug. 13, 2008), where the plaintiff sued his lawyers claiming that his patent infringement action

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against Black & Decker for a weed control device would have been successful but for the lawyers' negligence. The court hearing the malpractice action found that federal jurisdiction was proper, rebuffing the defendants' claim that there was no need to engage in a case-within-a-case analysis since the court in the underlying patent action had already issued a summary judgment in favor of Black & Decker.

''The issue is not the ultimate resolution in the underlying case, but whether that resolution would have been different but for the attorneys' malpractice,'' the court explained.

By Lance J. Rogers

*Malpractice*

## Experts on Insurance Marketplace See Low Prices, but High Costs, Cuts in Limits

CHICAGO—The market for lawyers' professional liability insurance continues to be ''soft'' with low pricing levels, but defense costs are increasing and the ''severity'' of claims is on the rise too, according to speakers at the 10th Legal Malpractice & Risk Management Conference.

At a Feb. 17 panel discussion on ''The Insurance Marketplace and Considerations,'' moderator Victoria L. Orze of Hinshaw & Culbertson, Phoenix, and two insurance experts explored the current market concerning lawyers' professional liability (LPL) coverage, along with changes in the legal industry that are affecting the insurance market.

There's a developing trend in the LPL market for insurers to share coverage, and changes in the legal industry of interest to insurers include mass lateral movement between firms and the outsourcing of legal services, the panelists said.

The panel materials mention a ''noticeable uptick in frequency'' of claims in 2010. But in introductory comments at the conference, Ronald E. Mallen of Hinshaw's San Francisco office discussed claim trends and said that in 2000 the frequency of claims against lawyers peaked and has been going down, when adjusted for lawyer population. On the other hand, he noted, claims are becoming more severe, with defense costs alone in the seven-figure range.

**Low Prices, High Claims.** ''We are basically at very low historical pricing levels,'' panelist Anthony K. Greene commented, explaining that excess ''capacity'' in the LPL market has resulted in a long ''soft'' market. He is a broker and director with Herbert L. Jamison & Co. in West Orange, N.J.

Regarding insurers' investment income, Greene noted that with treasury rates in the cellar, low investment returns are locked in for a couple of years. This is starting to change the behavior of insurers, he observed.

Like Mallen, Greene emphasized the increasing ''severity''—that is, large size—of claims. Claims arising from large transactions that took place three to five years ago are just now being seen, and ''millions of dollars could be spent on a case just in defense costs alone,'' he said.

Panelist Matthew F. Probolus, a vice president and senior underwriting specialist at Chubb Specialty Insurance in Simsbury, Conn., likewise emphasized that clients' deals several years ago were huge, and now the malpractice claims from these deals are working their way through the system.

One consequence of the economic downturn, Probolus said, was a spike in dishonest clients—which is scary from an underwriting perspective, as he put it. Dishonest clients have led to major losses in the range of seven to eight figures, he said.

As for LPL market activity over the past year, the panel materials note that there is new movement into and out of the insurance market, and that carriers' ''appetites'' are evolving. Moreover, there have been some ''base rate increase'' filings, and rumblings of hardening in the market.

Greene noted that because carriers are trying not to raise their rates, they're cutting back on limits. But new carriers are making up for this cutback, he said.

Probolus commented that the marketplace has been a little more stable of late. We haven't seen a big influx of carriers, he said.

Conference materials indicate some new LPL products are coming to market, such as a ''starter policy'' for first-time buyers, price concessions for giving up choice of counsel, a ''value plan'' with low limits and streamlined underwriting, and a ''moonlighting policy'' for corporate or government lawyers who spend less than 26 percent of their time in private practice.

Some new policies are really more of a branding initiative than a new product, Greene commented.

**Laterals and Insurance.** Greene noted that firms are aggressively looking to bring in lawyers from other firms, even whole practice groups. In doing so, he said, they need to consider where they want to be in terms of coverage for laterals' prior acts, especially if the firm left behind is going under.

**''[M]illions of dollars could be spent on a case just in defense costs alone.''**

Anthony K. Greene
Herbert L. Jamison & Co.

Probolus pointed out that if a practice group comes into a firm, that development changes the firm, which means that underwriting is necessary for the risk. ''Why do you want to expose your limits to work done somewhere else?'' he asked.

Orze asked her fellow panelists whether their insured firms talk to them before adding laterals. Greene said that it varies according to the relationship the firm has with the broker, but that it's best to have a prospective discussion. A firm may have obligations under its policy to notify the insurer when there are certain changes, he commented.

Greene pointed out that laterals bring in a book of business to their new firm. ''There will be pressure to share that asset,'' he said. He also said there's a very limited market for ''tail'' coverage in which a lawyer seeks insurance for claims arising during a policy period but made afterward.

**Sharing Risks in Layers.** Greene said that when a firm needs a high limit of insurance—such as $50 million—an evolving trend is for carriers to share risk in the primary layer of coverage, rather than just stacking coverage.

Orze referred to the process of compiling high-limit coverage through layers in which insurers share risk as ''building a tower.'' The process of putting the coverage together is quite involved, Probolus said.

An audience member asked whether insurers who are sharing risk in layers of exposure enter into a participation agreement among themselves, as would occur when multiple lenders extend a loan.

Greene answered that the participating insurers may agree on monitoring counsel, but not other details. There is no contractual agreement that binds insurers in this situation on how they will deal with a claim, he said.

This comment drew murmurs and gasps from the audience. ''I'm sensing consternation from law firms that get their coverage in shared layers,'' Orze commented.

Probolus insisted that ''it does work.'' Insurers trade on the ability to be there when there's a hit, he said.

Greene brought up what he called the ''nuclear worst'' for insurers: the bad faith issue, which takes the cap off of policy limits. Clients sometimes raise this issue, he noted.

**On the Horizon.** Probolus predicted that the trend of law firms' outsourcing some of their services will start to play a role in the LPL market. There is a real exposure from confidential information getting out to the world in the course of outsourcing, he said.

Underwriters will react by coming up with a supplement that covers the protection of confidential information, Greene suggested.

By Joan C. Rogers

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