

The Lawyers' *LAWYER* Newsletter

Recent Developments in Risk Management

Multiple Client Representation – Aggregate Settlements – Required Disclosure for Valid Client Consent

Waggoner v. Williamson, 8 So. 3d 147 (Miss. 2009)

Risk Management Issue: What is the scope of a lawyer's disclosure obligations when representing multiple clients in related matters that may result in an aggregate settlement?

The Case: After opting out of class action litigation, Mississippi plaintiffs Mr. and Mrs. Waggoner retained attorney Edward A. Williamson to pursue their claim against a drug manufacturer for injuries Mr. Waggoner sustained after taking diet drugs. Attorney Williamson represented 30 other plaintiffs against the same defendant; he also associated and signed a fee-sharing agreement with co-defendant attorney Miller, who represented 14 claimants in other states. Williamson and Miller negotiated a combined settlement of \$73.5 million, \$55 million of which was for Williamson's Mississippi clients. The defendant manufacturer refused to allocate the settlement to individual claimants. Instead, the defendant required in the settlement agreement that the lawyers comply with Rule 1.8, Model Rules of Professional Conduct or its state counterpart regarding conflicts of interest generally, and aggregate settlements in particular. The plaintiffs' attorneys themselves determined how to allocate the \$55 million among the Mississippi claimants.

The Waggoners claimed that Williamson telephoned them and directed them to meet him at a nearby airport where they learned, for the first time, that the case had settled. They said that when they arrived, they were presented with a disbursement statement showing their gross settlement to be slightly more than \$3 million, less a 45 percent attorney's fee, less another approximately \$90,000 for attorneys' fees for multi-district litigation, less a \$30,000 contribution to the Mississippi Trial Lawyers Association and another \$62,516.74 taken for expenses. They approved the disbursement sheet, which showed a "net to client" of \$1,472,100.50.

The Waggoners later sued Williamson and Miller in a multi-count complaint, including: that they did not know Williamson was not representing them individually; they were not told that their disbursement was part of an aggregate settlement; and they were told that if they did not agree to the settlement immediately, they could lose the right to any of the settlement funds. Because they were not fully informed, and on account of the other alleged breaches, they claimed that they did not legally consent to the settlement. Williamson and Miller disputed many of the Waggoner's factual allegations and legal arguments, but both of them admitted in deposition testimony that they "purposefully did not disclose information to the Waggoners regarding the aggregate settlement with [the defendant]."

The trial court dismissed the Waggoners' claims on summary judgment (except it permitted them to contest certain expenses), finding they knowingly consented to the settlement as a matter of law and were therefore barred from suing over it. The Mississippi Supreme Court reinstated the claims on the basis that disputed material issues of fact existed which precluded summary judgment. The Court focused on whether Williamson provided enough information to his clients such that their consent could be "knowing" as a matter of law. The Court noted that while a breach of the ethical rules does not normally provide the basis for a malpractice lawsuit, Williamson's own engagement agreement stated "[t]he lawyer shall not compromise or settle said right of action without the knowledge and consent of said clients(s)." In addition, the settlement agreement with the drug manufacturer required the lawyers to comply with Model Rule 1.8 or its state counterpart.

Multiple Client Representation, continued on page 2

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Comment: Even without the clause inserted here by the drug manufacturer in the aggregate settlement agreement, all jurisdictions impose special rules that lawyers must comply with when participating in aggregate settlements. Model Rule 1.8 (g) provides that “[a] lawyer who represents two or more clients shall not participate in making an aggregate settlement of the claims of or against the clients, . . . unless each client gives informed consent, in a writing signed by the client. The Lawyer’s disclosure shall include the existence and nature of all the claims or pleas involved and of the participation of each person in the settlement.”

Risk Management Solution: When law firms undertake multiple representation, that fact – and the conflicts of interest that necessarily result, including that the case might result in an aggregate settlement – should be clearly disclosed and discussed in the engagement letter sent at the outset of the relationship. Then, when a settlement is being offered, the terms should be explained to each client in sufficient detail – including the aggregate nature of the settlement and how each individual client’s share was arrived at – in advance of the lawyer entering into and binding the individual clients to the proposed terms.

Duty to Protect Confidential Information – Duty to Keep Client Informed of Developments Relating to Representation – Resolution of Conflict Between Duties Owed to Different Clients Regarding the Same Information

Romano v. Ficchi, 2009 WL 1460781 (N.Y. Sup. Ct. 2009)

Risk Management Issue: What are the duties of a lawyer when he learns a fact in connection with the representation of a client that, although confidential in connection with that engagement, may be material to the lawyer’s representation of a second client in an entirely separate and distinct matter?

The Case: Attorney Ficchi represented Plaintiff Romano, who purchased a residential condominium unit. During the purchase, Romano expressly told Ficchi that she wanted to buy this particular condominium because of the view the unit offered. In a separate engagement, Ficchi represented the seller of an adjoining property, during which he learned that the buyer of that adjoining property intended to demolish it and build a new structure that would obstruct the view from Romano’s condominium unit. That buyer in fact tore down the adjoining unit and erected a structure that obstructed Romano’s view. Romano thereafter sued Ficchi for malpractice, breach of contract, and breach of fiduciary duty. Ficchi moved to dismiss the lawsuit for failure to state a claim.

The Court dismissed Romano’s claims for breach of contract and breach of fiduciary duty but allowed her claim for malpractice to go forward. In pertinent part, the Court held that “[The Lawyer’s] knowledge of the intention of an adjoining buyer to develop his property in a way that would obstruct the view of the condominium unit plaintiff was considering to purchase and [the Lawyer’s] failure to inform the [plaintiff] that she was going to lose the very view which induced her to purchase it may support a claim of legal malpractice.” The Court likened Plaintiff’s claim to medical malpractice actions based on lack of informed consent, and cited prior New York case law to support its conclusion that an attorney may be liable to a client for malpractice if he negligently or willfully withholds information material to a client’s decision to pursue a certain course of action.

Comment: The problems that arose here were first, whether the lawyer had a duty to tell his client (Romano) the information he gained in connection with his representation of another client (the adjoining property seller) regarding the future obstruction of Romano’s view. Second, did the lawyer’s duty of confidentiality owed to his other client (the adjoining property seller) preclude him from disclosing to Romano that the adjoining buyer intended to obstruct her view? This situation is by no means unique. For example, it frequently arises when firms regularly represent clients who bid on publicly financed projects, where several clients may wish to bid against one another.

The Court’s conclusion calls for some discussion of how the lawyer should have acted when the problem became apparent. Clearly, receipt of information that is confidential to one client, but that would be material to another client, even in a separate engagement, constitutes a conflict of interest under the applicable version of the Rules of Professional Conduct (“RPC”) 1.7. Accordingly, a lawyer in this situation is obligated to seek consent from the building seller client to reveal the confidence learned during the course of that engagement to the condo purchasing client. It is at least possible, if not likely, that such consent will be given – because the construction plans are likely to be public in short order, the problem may be easily resolved by obtaining the developer’s consent. If the building seller client declines to give consent to disclosure, however, the lawyer’s proper response is to withdraw from the representation of the condo buyer, explaining that a conflict has arisen in connection with another engagement which the lawyer is not permitted to disclose. In addition, if in continuing to represent the adjacent property owner the lawyer is likely to use confidences learned from the condo buyer, or the continued representation may involve a breach of the duty of loyalty owed to the condo buyer, the lawyer may also be required to withdraw from representing the adjacent owner.

Risk Management Solution: The solution that some firms routinely adopt in order to deal with these situations is to insert a provision in every client’s engagement letter that states that the firm’s lawyers have no obligation to share information, even information material to the representation, if that information was learned while representing other clients and is confidential to those other clients. In the example of clients intending to make competing bids, while that language would not permit the firm to represent multiple clients bidding against each other, it would permit the firm to accept the engagement of one client and decline the engagement of the other without having to tell the represented client that the other client intended to mount a competing bid. Absent such prior consent, a firm placed in this predicament, if it continued to represent any one client would be at risk of subsequent claims of malpractice in the same way as was the defendant lawyer in the *Romano* case.

Duties to Former Clients – Conflicts of Interest Between Current and Former Clients – Liability for Malpractice for Breach of Duties to Former Client

Shu v. Butensky, 2009 WL 417265 (N.J. Super. Ct. App. Div. 2009)

Risk Management Issue: If a lawyer represents a new client in a matter adverse to a former client, does the lawyer owe continuing duties of care to the former client during the engagement for the new client?

The Case: Plaintiff Shu had retained Butensky to represent him in the purchase of real property in 1986. Paragraph 26 of the sale contract gave Shu as the buyer a right of first refusal in connection with the future sale of the adjacent lot. Specifically, paragraph 26 read as follows: “Buyer shall have a 30-day right of first refusal to purchase the adjacent property being subdivided from the within lot. These terms shall survive the passage of time.”

In 2005, the owners of the adjacent property subject to this right of first refusal sought to sell, and engaged Butensky to represent them in connection with the sale. As a part of this new engagement, Butensky wrote to his former client Shu in order to try to clear an alleged encroachment from the property that Shu had purchased when Butensky had represented him. In the correspondence relating to the alleged encroachment, Butensky did not identify any conflict of interest or request a waiver of any conflict. He also failed to remind or advise Shu in any way of Shu’s contractual right of first refusal to the property that Butensky was assisting his new clients to sell. The sale proceeded without the resolution of the encroachment issue. Litigation followed when the new owner sought to clear the encroachment, and during that litigation, Shu raised the first refusal issue, which ultimately became the basis for Shu’s malpractice claim against Butensky.

The trial court dismissed Shu’s malpractice claim on the grounds that Butensky did not owe Shu any duty in connection with the new engagement for his new clients to sell the property that was subject to Shu’s right of first refusal. The Appellate Court reinstated the claim, finding that it could “readily ascertain the existence of the three elements necessary to make out a *prima facie* case of legal malpractice” from Shu’s complaint. The Court held that:

“First, there is no question of the existence of an attorney-client relationship between plaintiff and defendant; Butensky represented Shu in the purchase of the real property at issue; the purchase contract gave Shu a right of first refusal on the adjacent lot; by clear unambiguous language, the owner of the lot burdened by Shu’s right of first refusal intended for this right to ‘survive the passage of time.’ It can thus be argued that Butensky’s professional responsibility as Shu’s attorney included protecting Shu’s right of first refusal. Second, assuming the existence of this duty, it can be argued that Butensky breached the duty by failing to draft and record an appropriate instrument echoing the contractual language, thereby giving constructive notice of the encumbrance to any prospective purchaser of the adjacent lot. And third, from these facts, a rational jury can find that there is a causal link between Butensky’s breach of his professional duty and the damages sustained by Shu in the form of the: (1) lost opportunity to acquire the adjacent lot; (2) monetary damages paid to [the subsequent purchaser] to settle the encroachment action; and (3) counsel fees incurred in defense of that action.” Accordingly, the Court set aside the dismissal of Shu’s malpractice claim.

Comment: It appears that among the failures identified by the Appellate Court, the defendant lawyer failed to notice and deal with the conflict arising with his former client by virtue of his new engagement nearly 20 years later. It is easy to see how this might have happened – few lawyers’ conflict databases would have detected that the property being sold by the new client might be the subject of a duty owed to a former client in a transaction that was completed many years earlier. When it became clear that his new client had a dispute with his former client, however, the possibility of a conflict should have surfaced and should have been addressed, with both the former and the new client. Although it is debatable whether the lawyer’s communication regarding the existence of the conflict would have brought the former client’s right of first refusal to the surface in time for Shu to exercise the right, it is at least arguable that when the lawyer familiarized himself with the prior representation of Shu in order to make the necessary disclosures to both former and present clients, he may have discovered the existence of the right of first refusal – which would have in turn arguably made the conflict unwaivable.

Two things are troubling about this decision, however. First, the only reason that Shu’s claim exists is that the same lawyer who represented him chanced to represent the new seller. If any other lawyer had been involved, it would have been Shu’s failure to recall or timely assert the right of first refusal, and not the lawyer’s. Second, it is not certain that, even had the lawyer gone through the proper conflict resolution process, he would necessarily have noticed the right of first refusal that arose from the prior engagement, since that was not the crux of the controversy that had in fact surfaced between the new client and the former client. Accordingly, even though the trial court’s dismissal of the malpractice claims was set aside, presumably these questions of causation remain to be argued as the case proceeds.

Risk Management Solution: When a lawyer is engaged in a transaction that is or becomes adverse to a former client, the lawyer needs to review the nature of the former engagement in order to determine if the new engagement is “the same as or substantially related to” the former engagement. Only having made that assessment will the lawyer be in a position to determine if the conflict is one where the conflict is such that it is not in fact waivable, or one where no waiver is required, or one where, in order to proceed with the new engagement, he must make adequate disclosure to and obtain a waiver and consent from the former client before proceeding with the new engagement.

Duty to Non-Clients – Liability for Error in Advice to Prospective Clients Under Negligent Misrepresentation Theory

Steele v. Allen, 2009 WL 399992 (Colo. Ct. App. 2009)

Risk Management Issue: When communicating with prospective clients, what precautions are necessary if lawyers are to avoid incurring liability for preliminary advice given during the course of such communications if no attorney-client relationship is thereafter established?

The Case: Plaintiffs Mr. and Mrs. Steele consulted with Attorney Allen and her law firm after an automobile accident, but they never hired the firm. In a subsequent suit against the firm for professional negligence and negligent misrepresentation, Plaintiffs alleged that in their consultation with Allen, Allen mistakenly advised Plaintiffs there was a five-year statute of limitations, and that they could not commence a personal injury suit against the other driver until they had settled any workers' compensation claims. Plaintiffs further alleged that the statute of limitations was actually three years, and that their subsequent lawsuit against the other driver was barred due to its expiration. The trial court granted Allen's motion to dismiss, finding that no professional negligence action existed because there was no attorney-client relationship, and that any non-client suit required fraud or malicious conduct by the attorney, which did not exist in the case before it.

In reversing the trial court's dismissal of the negligent misrepresentation claim, the Colorado Court of Appeals held that a negligent misrepresentation claim is independent of the principles of contract law, and that privity – such as an existing attorney client relationship – is not required. The Court relied on Section 15 of the Restatement (Third) of the Law Governing Lawyers (2000), which states, "[w]hen a person discusses with a lawyer the possibility of their forming a client-lawyer relationship for a matter, and no such relationship ensues, the lawyer must . . . use reasonable care to the extent the lawyer provides the person legal services." The Court further referenced comment (e) of Section 15 of the Restatement, which states, "[w]hen a prospective client and a lawyer discuss the possibility of representation, the lawyer might comment on such matters as whether the person has a promising claim or defense, whether the lawyer is appropriate for the matter in question, whether conflicts of interest exist and if so how they might be dealt with, *the time within which action must be taken*, and, if the representation does not proceed, what other lawyer might represent the prospective client. *Prospective clients might rely on such advice, and lawyers therefore must use reasonable care in rendering it.*" (Emphasis in original.)

In addressing the concern about unlimited potential liability to third party non-clients, the Court noted that "the specter of potential liability . . . is alleviated by the requirement in a claim for negligent misrepresentation that the plaintiff show that the defendant supplied false information in the context of a business transaction regarding the representation of a potential clients." Excepting from this situation informal statements by an attorney in a social setting, the Court cited comment (d) of the Restatement (Second) of Torts §552, which states " . . .[b]ut when one who is engaged in a business or profession steps entirely outside of it, as when an attorney gives a casual and offhand opinion on a point of law to a friend whom he meets on the street, or what is commonly called a 'curbside opinion', it is not to be regarded as given in the course of his business or profession; and since he has no other interest in it, it is considered purely gratuitous. The recipient of the information is not justified in expecting that his informant will exercise the care and skill that is necessary to ensure a correct opinion and is only justified in expecting that the opinion will be an honest one."

Comment: While the Colorado Court of Appeals attempts in this case to make the circumstances of a communication – business vs. social – into a bright line distinction for liability purposes, in practice the line can be a blurry one and result in litigation over what constitutes "reasonable reliance" under the specific fact circumstances of an actual consultation on a case by case basis.

Risk Management Solution: The short answer is that attorneys should take care whenever offering any comments that might fall into the category of potential legal advice, regardless of the setting. When communicating with prospective clients regarding the possibility that an attorney-client relationship will follow, the lawyer should take great care during the course of all such communications to make clear that any statement of opinions should not be taken as formal advice, which can only be given after an engagement letter has been provided to and countersigned by the client, and after appropriate research has been undertaken. Additionally, when no attorney-client relationship is established for any reason, a non-engagement letter should be sent to the client, which should cover at least the following matters: (1) state unequivocally that the lawyer or firm is not accepting the engagement to represent the prospective client; (2) explicitly reiterate that any statements of opinion given during preceding communications should not be taken as formal legal advice; and (3) avoid giving any legal advice (including regarding possibly applicable statutes of limitation, except, perhaps, for a statement such as "because there may be applicable statutes of limitation that may run in the very near future, or may already have passed, it is urgent that you obtain other counsel willing to undertake representation in the matter").

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