CHAPTER 5

ETHICS AS THE DEVELOPMENT EVOLVES

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I. WHY CONFLICTS MATTER

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Both the current Washington Rules of Professional Conduct and the proposed amended version are prefaced with views on their role in the practice of law. The current set notes that the RPCs "point the way to the aspiring and provide standards" to judge lawyers' conduct in a disciplinary sense. The proposed amendments now under consideration echo that intent: "The Rules simply provide a framework for the ethical practice of law." Without diminishing either that aspiration or their role as a disciplinary code, the professional rules—particularly those relating to conflicts—also increasingly form the substantive law of legal malpractice, lawyer breach of fiduciary duty, disqualification, fee forfeiture and lawyer-related Consumer Protection Act claims. In short, conflicts matter today in a very practical way.

In this inaugural edition of the quarterly Ethics Page, we'll look at several Washington cases that underscore the practical importance of the conflict rules beyond the disciplinary setting. When the Ethics Page returns in the Fall, we'll then consider ways of managing conflicts to reduce risk.

Legal Malpractice. The Washington Supreme Court in *Hizey v. Carpenter*, 119 Wn.2d 251, 257-66, 830 P.2d 646 (1992), ruled that the RPCs themselves cannot be cited directly in establishing the standard of care for legal malpractice. At the same time, the Supreme Court in *Hizey* found that an expert could incorporate the concepts underlying the rules into an opinion on

the standard of care. Because the conflict rules are grounded in a lawyer's fiduciary duty of loyalty to a client, the practical import of *Hizey*'s distinction for conflict-based malpractice claims is not as significant as it might first appear—a violation of the conflict rules will simply be recast as a corresponding violation of the legal duty of an agent (the lawyer) to the principal (the client).

Breach of Fiduciary Duty. In a parallel decision issued within months of *Hizey*, the Washington Supreme Court made explicit the link between the conflict rules and a lawyer's fiduciary duty of loyalty. The Supreme Court in *Eriks v. Denver*, 118 Wn.2d 451, 457-61, 824 P.2d 1207 (1992), held that a lawyer with an unwaived multiple client conflict had violated both the conflict rules and the fiduciary duty of loyalty. In doing so, *Eriks* allows the RPCs to be considered directly in assessing whether a lawyer has breached a fiduciary duty to a client.

Disqualification. Although court decisions provide the procedural law of disqualification in terms of standing and the like, the RPCs effectively supply the substantive law. A recent case from the federal district court in Seattle, *Oxford Systems, Inc. v. CellPro, Inc.*, 45 F. Supp. 2d 1055 (W.D. Wash. 1999), is an excellent example of this trend. *Oxford* turned on whether the law firm involved had a current or former client conflict. The court looked directly to the corresponding RPCs—1.7 for current client conflicts and 1.9 for former client conflicts—in resolving those questions.

Fee Forfeiture. The Supreme Court in *Eriks* also held that a lawyer's breach of fiduciary duty may result in full or partial fee forfeiture: "Disgorgement of fees is a reasonable way to 'discipline specific breaches of professional responsibility, and to deter future misconduct of a similar type.'" 118 Wn.2d at 463 (citation omitted). The Court of Appeals recently reiterated that view in *Cotton v. Kronenberg*, 111 Wn. App. 258, 275, 44 P.3d 878 (2002), in affirming the

complete forfeiture of a lawyer's fee in the face of a conflict and an accompanying breach of fiduciary duty.

Consumer Protection Act. Under *Short v. Demopolis*, 103 Wn.2d 52, 61, 691 P.2d 163 (1984), the Washington Consumer Protection Act (CPA) applies to the "entrepreneurial aspects" of practicing law including "the way a law firm obtains, retains, and dismisses clients." In *Eriks*, the Supreme Court found that a lawyer's conflicts might constitute a violation of the CPA if they were triggered by "entrepreneurial purposes." 118 Wn.2d at 465. The Court of Appeals in *Cotton* took that same approach. 111 Wn. App. at 273-75. The practical dimension of the CPA is that it adds an attorney fee remedy for a successful claimant.

Although there are important professional reasons as reflected in the preamble to the RPCs to follow the rules on conflicts, there are also important practical reasons. Conflicts are no longer the exclusive province of bar discipline. As illustrated by the cases we've just examined, the professional rules on conflicts form the essential substantive law on a spectrum from legal malpractice to disqualification. Or, put simply, conflicts matter in a very practical way.

II. MANAGING CONFLICTS

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Note: Since this article was published, the Washington Supreme Court has adopted the new Washington Rules of Professional Conduct effective September 1, 2006. The new rules were under review by the WSBA and the Supreme Court at the time it was written and they are discussed in this column. The new RPCs, the accompanying commentary and the report of the WSBA special committee that recommended the new rules are all available on the WSBA's web site at www.wsba.org.

In the summer installment of Ethics & the Law, we looked at why conflicts matter. In this quarter's column, we'll examine two ways of managing conflicts to reduce civil and regulatory risk: (1) using conflict waivers effectively; and (2) structuring representations to eliminate conflicts in the first place.

Using Conflict Waivers Effectively

The recipe for an effective conflict waiver in Washington is drawn largely from the Rules of Professional Conduct. The WSBA and the Washington Supreme Court are considering proposed amendments to the RPCs—including those regulating conflict waivers. Although some terminology will change if the proposed amendments are adopted, the key practical ingredients for an effective conflict waiver will remain the same.

► *Confirm client consent in writing*. Both the present and the proposed versions of the current and former client conflict rules—respectively, RPCs 1.7 and 1.9—require that conflict waivers be confirmed in writing. With both, it is the client's consent that is being confirmed in writing. When documenting the client's consent, however, it is also wise to confirm *the disclosures* that led to consent. For the client, it sets out in one place the nature of the conflict to which the client consented. For the lawyer, it is an important record if there are ever any questions later about what the client was told before granting the waiver. Although

neither the current nor the proposed rules require that the client actually countersign the waiver to affirm consent, having the client do that is a good way to document consent. Oral disclosure and client consent are sufficient to start work on a matter. A written confirmation of the waiver, however, should follow shortly after that—both to meet the requirement of the rule and to document consent at the time it is granted.

► *Explain the nature of the conflict*. The current versions of RPCs 1.7 and 1.9 require that waivers be predicated on "consultation and a full disclosure of the material facts" and, in turn, define "consultation" as "communication of information reasonably sufficient to permit the client to appreciate the significance of the matter in question." The proposed amended versions (which are available on the WSBA's web site at www.wsba.org/lawyers/groups/ethics2003/default.htm) recast the predicate in terms of the client's "informed consent" and define that as "the agreement by a person to a proposed course of conduct after the lawyer has communicated adequate information and explanation about the material risks of and reasonably available alternatives to the proposed course of conduct." Whether framed as "full disclosure" or "informed consent," the goal remains the same: you need to tell the client in a way the client will understand what the risks of granting the waiver will be.

► *Remember that some conflicts can't be waived*. Not all conflicts can be waived—even if the clients involved want to. The classic example is that you can't be on both sides of the same litigation. Under the current version of RPC 1.7, multiple client conflicts are waivable only when "[t]he lawyer reasonably believes that the representation will not adversely affect the relationship with the other client[.]" Proposed amended RPC 1.7 retains this general limit and adds a specific prohibition against representing both sides in the same litigation.

The new WSBA Legal Ethics Deskbook contains sample conflict waivers covering a variety of situations. It's a great place to start when you are trying to blend the right ingredients into an effective waiver.

Eliminating Conflicts in the First Place

For there to be a conflict, there has to be *adversity* in the legal positions of the clients involved. If the adversity (or the potential for adversity) is eliminated, then the potential conflicts will likely be eliminated, too. Adversity can be eliminated by structuring a representation at the outset to handle only aspects of a matter where the positions of multiple clients are in concert.

Although this technique can be used in some instances to eliminate multiple client conflicts in different matters, it is most commonly employed in situations where the same lawyer is handling a matter jointly for multiple clients. For example, in products liability cases, it is common for dealers to tender the defense of a case to the manufacturer and for both to want to use the same lawyer to defend them. If the manufacturer and the dealer agree (without the defense lawyer acting as a broker between them) to reserve any claims and other liability-shifting issues between them to a later forum with other counsel, then the lawyer has no conflict in defending them in the primary action against the plaintiff because their interests in that case are fully aligned.

Structuring or limiting representations won't eliminate all conflicts and can have practical constraints if the resulting scope is too narrow to represent the clients effectively. In many situations, however, it can be a very useful tool for managing conflicts.

III. THE "WHO IS THE CLIENT?" QUESTION

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Note: Since this article was published, the Washington Supreme Court has adopted the new Washington Rules of Professional Conduct effective September 1, 2006. The new rules were under review by the Supreme Court at the time it was written and they are discussed in this column. The new RPCs, the accompanying commentary and the report of the WSBA special committee that recommended the new rules are all available on the WSBA's web site at www.wsba.org.

One of the key elements in analyzing conflicts is identifying who your client is in a given representation. Sometimes that task is easy: it's the single person sitting across the desk from you. But many times it's not. Physically or virtually there may be several people sitting across the desk from you—a family, business partners, a government agency or a corporate affiliate. The "who is the client?" question looms large in many situations because it tells us to whom we owe our duties of loyalty and confidentiality—and to whom we do not.

In this column we'll first look at the general rule for deciding whether an attorney-client relationship exists and then apply that rule in four contexts: corporations and their affiliates; partnerships; governmental entities; and insurance defense.

The General Rule. The general rule for determining whether an attorney-client relationship exists was set out in *Bohn v. Cody*, 119 Wn.2d 357, 363, 832 P.2d 71 (1992).[1] The Supreme Court in *Bohn* outlined a two-part test. The first element is subjective: does the client believe that an attorney-client relationship exists? Or, as the Supreme Court put it: "The existence of the relationship 'turns largely on the client's subjective belief that it exists.'"[2] The second element is objective: is the client's subjective belief objectively reasonable under the circumstances? Or, as the Supreme Court put it: "The client's subjective belief, however, does

not control the issue unless it is reasonably formed based on the attending circumstances, including the attorney's words or actions."[3]

The Supreme Court in *Bohn* and other courts that have subsequently applied *Bohn*'s two-part test have emphasized that whether an attorney-client relationship exists is ultimately a question of fact.[4] A written engagement agreement that sets out the nature and scope of the relationship in detail will likely be dispositive on this issue. But many situations either do not involve written agreements or, even if they do, the written agreements may not be sufficiently detailed to conclusively answer the question. In that event, the existence or absence of an attorney-client relationship will be inferred from the parties' conduct as viewed through the prism of *Bohn*'s two-part test.

Corporations and Their Affiliates. As I write this, the proposed amendments to the Rules of Professional Conduct are pending before the Supreme Court. If adopted, the new rules will offer a significant clarification to the "who is the client?" question in the corporate context. New RPC 1.13(a) adopts the "entity approach" to corporate representation: a lawyer representing a corporation is deemed to represent the corporation rather than its individual shareholders or officers. This is the same tact taken by Section 131 of the Restatement (Third) of the Law Governing Lawyers and the ABA's Model Rules of Professional Conduct. The "entity approach" doesn't preclude joint representation of both the corporation and one of its constituent members, such as an officer or director. But in those instances, any dual representation would be subject to RPC 1.7's multiple client conflict rules.

A related and often more difficult issue is whether representation of one corporate affiliate will be deemed representation of the entire "corporate family." There is no hard and fast rule. ABA Formal Ethics Opinion 95-390 (1995), which analyzes this issue in detail, suggests

two measures that will weigh on the side of considering all elements of a corporate family to be the same for conflict purposes. First, if the client has informed the lawyer that the corporate family should be considered a unified whole, then it will generally be treated as such. Second, even absent such an agreement, a corporate affiliate may be treated as a member of a broader corporate family when it shares common general and legal affairs management. At the same time, such affiliate relationships are most often found to constitute a single client when control is exercised through majority ownership of the affiliate by the corporate parent.[5]

Partnerships. Partnerships generally present the same "who is the client?" issues that corporations do. If approved, RPC 1.13(a) would adopt the "entity approach" in the partnership context, too, and would mirror the view taken in the ABA's Model Rules, ABA Formal Ethics Opinion 91-361 (1991) and Section 131 of the Restatement. Under that approach, the representation of a partnership will normally be limited to the entity and will not extend to the individual partners. A lawyer or law firm could jointly represent both a partnership and one of its individual partners, but the joint representation would be subject to RPC 1.7's multiple client conflict rules.

Governmental Entities. The Washington RPCs in both their current and proposed amended form differ from the ABA Model Rules in a significant way in the area of governmental representation. Current RPC 1.7(c) and proposed RPC 1.13(h) generally limit the "client" in governmental representation (absent some other arrangement in writing) to the specific agency for which the work is being handled rather than the broader governmental entity of which the agency is a part.

Insurance Defense. Although not an organizational conflict as such, insurance defense is an area where lawyers frequently encounter the "who is the client?" question: the insured who is

being defended, the insurer who is paying the bill for that defense, or both? States vary in their approach on this issue, with some saying that an insurance defense counsel represents both the insured and the insurer and some limiting representation to the insured only and treating the insurer as a third-party payor. Washington falls into the second group under *Tank v. State Farm Fire & Cas. Co.*, 105 Wn.2d 381, 388, 715 P.2d 1133 (1986), and WSBA Formal Ethics Opinion 195 (1999). In Washington, therefore, an insurance defense counsel has only one client—the insured whose interests the lawyer is directly defending in the matter involved.

Summing Up. In some areas, such as insurance defense, the RPCs or cases draw a bright line between who a lawyer does and does not represent. In many other contexts, notably corporate affiliate representation, the line is much less distinct. Even with the adoption of RPC 1.13(a), the "who is the client?" question will remain a very fact-specific exercise. With any of these areas, however, lawyers can help answer that question by carefully defining the client in a written engagement letter and then handling the representation consistent with the engagement agreement.

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[1] *See also Teja v. Saran*, 68 Wn. App. 793, 795-96, 846 P.2d 1375, *rev. denied*, 122 Wn.2d 1008 (1993) (applying *Bohn*); *accord Oxford Systems, Inc. v. CellPro, Inc.*, 45 F. Supp. 2d 1055, 1059 (W.D. Wash. 1999) (also applying *Bohn*).
[2] 119 Wn.2d at 363 (citation omitted).
[3] *Id.*
[4] *Id. accord Teja v. Seran*, *supra*, 68 Wn. App. at 795-96; *Oxford Systems, Inc. v. CellPro, Inc.*, *supra*, 45 F. Supp. 2d at 1059.
[5] *See also* Restatement, *supra*, § 131, comment d at 367.