

An Overlooked Asset in Law Practice Risk Management: Legal Counsel

Consider the following scenario. A for-profit business specializes in servicing a particular niche market. The business has a proven track record over the past five years, turning a profit and growing steadily. This year, the business has identified an opportunity to save costs and also enhance its competitive advantage: hire an in-house counsel.

The in-house counsel provides a valuable resource for the business in areas such as corporate governance, regulatory compliance and business strategy, among other internal professional activities. The in-house counsel also provides a beneficial conduit for privileged communications with officers of the company about potential risks and liabilities facing the business, both internally and externally.

This scenario seems typical in today's commercial business practices. Now, consider that the same for-profit commercial business is a law firm.

For a variety of reasons, law firms often fail to self-identify as for-profit enterprises similar to many of the clients that the firm services. In today's legal market, solo practitioners and small firms customarily resist hiring outside counsel for general business needs. While mid-size and large firms may recognize the benefit of hiring an outside counsel, they often resist developing an in-house counsel or part-time in-house counsel position. The most likely reason for this enigma is that law firms, big and small, have a stranglehold on external overhead expenses and thus resist hiring staff that do not generate income. From a practical perspective, however, most industries operate within these same financial constraints. If commercial businesses have committed to embracing the value of legal services as vital to their success, then law firms also should consider its benefit.

The Lawyer's Lawyer: A Risk Management Strategy

Lawyers are confident that their legal services provide value to the clients whom they serve. However, with respect to their own solo or small law firms, lawyers may be challenged in identifying vendors or professional service providers that provide value to their own firm. Those service providers also may help the firm to build efficiencies, identify risks, and ultimately contribute to the firm's overall competitive advantage in today's legal marketplace.

Accordingly, solo practitioners and lawyers in small firms would be well advised to identify an outside counsel in the event that a legal issue arises in law firm management. Examples of matters for which an outside counsel may benefit a law firm include the following:

- Reviewing vendor contracts;
- Advising on the management of client funds;
- Resolving billing/collection issues;
- Advising on conflicts of interest issues;
- Counseling in general commercial disputes;
- Identifying risk trends; and
- Developing internal risk control policies and procedures.

In addition, outside counsel may serve as a valuable resource to mitigate a potential liability claim by assisting with early intervention before a claim arises.¹ *ABA Model Rule 1.6(b)(4)* authorizes lawyers to seek confidential advice from other lawyers about their ethical duties. In addition, *ABA Model Rule 1.6(b)(5)* provides an exception to the lawyer's duty of confidentiality "to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, . . ."

A collateral benefit of proactively managing law firm risks through the use of outside counsel includes better client relationship management. For example, outside counsel would have the ability to provide an objective view in matters such as contentious billing disputes. Outside counsel also may help to clarify internal law firm staff duties in such areas as the creation of reporting hierarchies for internal disputes, as well as development of better client intake procedures and conflict resolution practices. Benefits will, of course, vary from practice to practice. However, it is difficult to imagine a scenario in which outside legal counsel could not positively contribute to a firm's overall risk management program.

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¹ It should be noted that potential claims may be reportable under a professional liability policy and lawyers should consult their policy, their broker, or their carrier regarding their reporting requirements.

Recent Developments Regarding In-House Legal Counsel for Law Firms

Law firms that staff a general counsel role typically incur \$1 million less on defense costs and indemnity payments with respect to malpractice claims than firms without a general counsel.² These savings represent an example of Benjamin Franklin's proverb that, "an ounce of prevention is worth a pound of cure."

The role of general counsel, including a part-time general counsel, creates many advantages for mid-size and large law firms, including but not limited to the following:

- Active management of client intake disputes and related issues including outside counsel guidelines;
- Active management of conflicts of interest checks;
- Management of vendor contracts and liabilities;
- Management of internal risk controls, including risk transfer strategies;
- Identify and foster business development opportunities for the firm; and
- Manage corporate or partnership related issues.

In other words, a general counsel performs activities apart from client servicing and the attendant demands of specialization, rather than fulfilling these roles on an *ad hoc* basis. However, an in-house counsel does not represent a panacea for all law firm internal issues. One area of recent litigation involves the ability of a law firm to invoke the attorney-client privilege with its general counsel when the subject involves a potential or actual claim of legal malpractice by a current firm client.

Historically, national trial and appellate courts that have addressed the issue have recognized two exceptions to the intra-firm attorney-client privilege: the fiduciary exception and the conflicts rationale. The fiduciary exception provides that where an attorney seeks advice concerning client representation, the attorney is acting in the interest of the client. Therefore, the client should share in that advice.³ The conflicts rationale provides that where an attorney seeks in-house advice concerning a potential malpractice action by the client, the firm is representing adverse parties in that action (the client and the firm itself). As a result, the firm's right to claim privilege is superseded by the interest in protecting current clients who may be harmed by the conflict.⁴

² Rotunda, Ronald D. Law Firms *Creating In-House Ethics Counsel*, VERDICT, Legal Analysis and Commentary From Justitia, Nov. 3 2014, citing *The Professional Lawyer*, v.20, no.2, 2010 Summer, p.1.

³ Cf. *Bank Brussels Lambert v. Credit Lyonnais (Suisse)*, 220 F. Supp. 2d 283 (S.D.N.Y. 2002); *Koen Book Distrib. V. Powell, Trachtman, Logan, Carrie, Bowman & Lombardo*, 212 F.R.D. 283 (E.D. Pa. 2002); *VersusLaw, Inc. v. Stoel Rives, LLP*, 111 P.3d 866 (Wash. 2005).

⁴ *In re Sunrise Securities Litigation*, 130 F.R.D. 560 (E.D. Pa. 1989); *E-Pass Technologies, Inc. v. Moses & Singer*, 2011 U.S. Dist. LEXIS 96231 (N.D. Ca. 2011).

Recently, however, a number of courts of last resort across the country have addressed this question and have reversed course.⁵ These courts have generally held that the attorney-client privilege does apply to communications between a law firm and its general counsel regarding a potential malpractice claim by a current client, providing certain conditions are met (see recommended strategies in the “Risk Control Strategies” section below).

Subsequent to these more recent state high court decisions upholding the privilege, the American Bar Association adopted Resolution 103, which declared that the attorney-client privilege shields a lawyer’s consultation with an in-house counsel even if the discussion creates a conflict.⁶ Resolution 103 goes on to declare that the fiduciary exception to the privilege does not apply where the lawyer seeks legal advice about the firm’s responsibilities to a client. Several lower state courts have followed this trend as well as a recent federal court decision applying federal law to the question.⁷

These recent opinions upholding the attorney-client privilege between a law firm and its in-house counsel are consistent with the *Restatement (Third) of the Law Governing Lawyers § 46, Comment c (2000)*, which states as follows:

A lawyer may refuse to disclose to the client certain law-firm documents reasonably intended only for internal review, such as a memorandum discussing which lawyers in the firm should be assigned to a case, whether a lawyer must withdraw because of the client’s misconduct or the firm’s possible malpractice liability to the client. The need for lawyers to be able to set down their thoughts privately in order to assure effective and appropriate representation warrants keeping such documents secret from the client involved.

Clearly, the momentum has shifted. Law firms that have considered utilizing an in-house general counsel role should be encouraged to develop that role in today’s competitive market. However, due diligence should be performed in order to understand the obligations and limitations on such a role in their jurisdiction.

Risk Control Strategies

An important risk management tool that law firms often overlook is hiring legal counsel. Both external and internal legal counsel provide a great value to law firms, especially in helping to develop risk management strategies to avoid or mitigate potential liabilities. If the firm has the ability to designate an in-house counsel or part-time in-house counsel, the firm should review state-specific laws, regulations and ethical guidance regarding any limitations to the general counsel’s function and should consider the following recommendations, at a minimum:

1. Formally appoint one or more lawyers in the firm to serve as the firm’s general counsel or part-time general counsel, or hire an objective, experienced counsel to fill this role.
2. When discussing firm-specific matters with the general counsel, follow these steps, at a minimum:
 - a. Ensure that the general counsel has not worked on the matter being discussed or on a substantially related matter, and if so, seek assistance of outside counsel;
 - b. Create a separate internal file on the matter;
 - c. Do not bill any client file for the time spent on the “in-house” consultation;
 - d. Treat the communications between the firm and its counsel as confidential and privileged; and
 - e. Keep written documentation to a minimum.
3. Include language in the firm’s engagement letter advising the client that attorneys may be required to seek confidential internal legal advice concerning the firm’s legal and ethical obligations to the client and that such consultations are subject to the attorney-client privilege between the law firm and its in-house counsel.
4. Educate the firm about the role of in-house counsel and/or its outside counsel.
5. Create a firm culture in the firm to consistently utilize in-house counsel within firm guidelines.

Establishing the role of general counsel at your law firm will enable you to derive numerous benefits, through supporting the firm in the resolution of complex internal issues and thereby permitting attorneys to focus on the ultimate goal of optimal client servicing.

⁵ *RFF Family Partnership, LP v. Burnes & Levinson, LLP*, 991 N.E.2d 1066 (Mass. 2013); *St. Simons Waterfront, LLC v. Hunter, Maclean, Exley & Dunn, P.C.*, 746 S.E.2d 98 (Ga. 2013); *Crimson Trace Corp. v. Davis, Wright, Tremaine, LLP*, (Ore. 2013).

⁶ American Bar Association Resolution 103 (2013); See Also American Bar Association Formal Ethics Opinion 08-453, *In House Consulting on Ethical Issues*, (Oct. 17, 2008).

⁷ *Moore v. Grau*, 2014 N.H. Super. LEXIS 20 (N.H. Super. Ct. 2014); *Edwards, Wildman, Palmer v. Superior Court (Mireskandari)*, 180 Cal Rptr. 3d 620 (2014); *Loop AI Labs, Inc. v. Gatti*, 2016 BL 53774 (N.D. Cal. 2016) (this is a limited opinion finding that the fiduciary exception does not apply where the communication did not involve a claim against the law firm and the firm withdrew within two weeks of learning about the conflict).

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