A Lawyer’s Duty to Inform a Current or Former Client of the Lawyer’s Material Error

Model Rule of Professional Conduct 1.4 requires a lawyer to inform a current client if the lawyer believes that he or she may have materially erred in the client’s representation. Recognizing that errors occur along a continuum, an error is material if a disinterested lawyer would conclude that it is (a) reasonably likely to harm or prejudice a client; or (b) of such a nature that it would reasonably cause a client to consider terminating the representation even in the absence of harm or prejudice. No similar obligation exists under the Model Rules to a former client where the lawyer discovers after the attorney-client relationship has ended that the lawyer made a material error in the former client’s representation.

Introduction

Even the best lawyers may err in the course of clients’ representations. If a lawyer errs and the error is material, the lawyer must inform a current client of the error.1 Recognizing that errors

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1 A lawyer’s duty to inform a current client of a material error has been variously explained or grounded. For malpractice and breach of fiduciary decisions, see, e.g., Leonard v. Dorsey & Whitney LLP, 553 F.3d 609, 629 (8th Cir. 2009) (predicting Minnesota law and concluding that “the lawyer must know that there is a non-frivolous malpractice claim against him such that there is a substantial risk that [his] representation of the client would be materially and adversely affected by his own interest in avoiding malpractice liability” (internal quotation marks omitted)); Beal Bank, SSB v. Arter & Hadden, LLP, 167 P.3d 666, 673 (Cal. 2007) (stating that “attorneys have a fiduciary obligation to disclose material facts to their clients, an obligation that includes disclosure of acts of malpractice”); RFF Family P’ship, LP v. Burns & Levinson, LP, 991 N.E.2d 1066, 1076 (Mass. 2013) (discussing the fiduciary exception to the attorney-client privilege and stating that “a client is entitled to full and fair disclosure of facts that are relevant to the representation, including any bad news”); In re Tallon, 447 N.Y.S.2d 50, 51 (App. Div. 1982) (“An attorney has a professional duty to promptly notify his client of his failure to act and of the possible claim his client may thus have against him.”).

For disciplinary decisions, see, e.g., Fla. Bar v. Morse, 587 So. 2d 1120, 1120–21 (Fla. 1991) (suspending a lawyer who conspired with his partner to conceal the partner’s malpractice from the client); In re Hoffman, 700 N.E.2d 1138, 1139 (Ind. 1998) (applying Rule 1.4(b)). See also Ill. State Bar Ass’n Mut. Ins. Co. v. Frank M. Greenfield & Assocs., P.C., 980 N.E.2d 1120, 1129 (Ill. App. Ct. 2012) (finding that a voluntary payments provision in a professional liability insurance policy was “against public policy, since it may operate to limit an attorney’s disclosure [of his potential malpractice] to his clients”).

For ethics opinions, see, e.g., Cal. State Bar Comm. on Prof’l Responsibility & Conduct Op. 2009-178, 2009 WL 3270875, at *4 (2009) [hereinafter Cal. Eth. Op. 2009-178] (“A lawyer has an ethical obligation to keep a client informed of significant developments relating to the representation. . . . Where the lawyer believes that he or she has committed legal malpractice, the lawyer must promptly notify the client of the significant developments . . . .” (citation omitted)); Colo. Bar Ass’n, Ethics Comm., Formal Op. 113, at 3 (2005) [hereinafter Colo. Op. 113] (“Whether a particular error gives rise to an ethical duty to disclose [under Rule 1.4] depends on whether a disinterested lawyer would conclude that the error will likely result in prejudice to the client’s right or claim and that the lawyer, therefore, has an ethical responsibility to disclose the error.”); Minn. Lawyers Prof’l Responsibility Bd. Op. 21, 2009 WL 8396588, at *1 (2009) (imposing a duty to disclose under Rule 1.4 where “the lawyer knows the lawyer’s conduct may reasonably be the basis for a non-frivolous malpractice claim by a current client that materially affects the client’s
occur along a continuum, an error is material if a disinterested lawyer would conclude that it is (a) reasonably likely to harm or prejudice a client; or (b) of such a nature that it would reasonably cause a client to consider terminating the representation even in the absence of harm or prejudice.

If a material error relates to a former client’s representation and the lawyer does not discover the error until after the representation has been terminated, the lawyer has no obligation under the Model Rules to inform the former client of the error. To illustrate, assume that a lawyer prepared a contract for a client in 2015. The matter is concluded, the representation has ended, and the person for whom the contract was prepared is not a client of the lawyer or law firm in any other matter. In 2018, while using that agreement as a template to prepare an agreement for a different client, the lawyer discovers a material error in the agreement. On those facts, the Model Rules do not require the lawyer to inform the former client of the error. Good business and risk management reasons may exist for lawyers to inform former clients of their material errors when they can do so in time to avoid or mitigate any potential harm or prejudice to the former client. Indeed, many lawyers would likely choose to do so for those or other individual reasons. Those are, however, personal decisions for lawyers rather than obligations imposed under the Model Rules.

The Duty to Inform a Current Client of a Material Error

A lawyer’s responsibility to communicate with a client is governed by Model Rule 1.4. Several parts of Model Rule 1.4(a) potentially apply where a lawyer may have erred in the course of a current client’s representation. For example, Model Rule 1.4(a)(1) requires a lawyer to promptly inform a client of any decision or circumstance with respect to which the client’s informed consent may be required. Model Rule 1.4(a)(2) requires a lawyer to “reasonably consult with the client about the means by which the client’s objectives are to be accomplished.” Model Rule 1.4(a)(3) obligates a lawyer to “keep a client reasonably informed about the status of a matter.” Model Rule 1.4(a)(4), which obliges a lawyer to promptly comply with reasonable requests for information, may be implicated if the client asks about the lawyer’s conduct or performance of the representation. In addition, Model Rule 1.4(b) requires a lawyer to “explain a
matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation.” More broadly, the “guiding principle” undergirding Model Rule 1.4 is that “the lawyer should fulfill reasonable client expectations for information consistent with the duty to act in the client’s best interests, and the client’s overall requirements as to the character of representation.” A lawyer may not withhold information from a client to serve the lawyer’s own interests or convenience.

Determining whether and when a lawyer must inform a client of an error can sometimes be difficult because errors exist along a continuum. An error may be sufficiently serious that it creates a conflict of interest between the lawyer and the client. Model Rule 1.7(a)(2) provides that a concurrent conflict of interest exists if “there is a significant risk that the representation of one or more clients will be materially limited by . . . a personal interest of the lawyer.” Where a lawyer’s error creates a Rule 1.7(a)(2) conflict, the client needs to know this fact to make informed decisions regarding the representation, including whether to discharge the lawyer or to consent to the conflict of interest. At the other extreme, an error may be minor or easily correctable with no risk of harm or prejudice to the client.

Several state bars have addressed lawyers’ duty to disclose errors to clients. For example, in discussing the spectrum of errors that may arise in clients’ representations, the North Carolina State Bar observed that “material errors that prejudice the client’s rights or claims are at one end. These include errors that effectively undermine the achievement of the client’s primary objective for the representation, such as failing to file the complaint before the statute of limitations runs.” At the other end of the spectrum are “nonsubstantive typographical errors” or “missing a deadline that causes nothing more than delay.” “Between the two ends of the spectrum are a range of errors that may or may not materially prejudice the client’s interests.” With respect to the middle ground:

Errors that fall between the two extremes of the spectrum must be analyzed under the duty to keep the client reasonably informed about his legal matter. If the error will result in financial loss to the client, substantial delay in achieving the client’s objectives for the representation, or material disadvantage to the client’s legal position, the error must be disclosed to the client. Similarly, if disclosure of the error is necessary for the client to make an informed decision about the representation or for the lawyer to advise the client of significant changes in strategy, timing, or direction of the representation, the lawyer may not withhold information about the error.

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3 Id. cmt. 5.
4 Id. cmt. 7.
5 See supra note 1 (listing authorities).
7 Id.
8 Id.
9 Id.
Another example is contained in the Colorado Bar Association’s Ethics Committee in Formal Opinion 113, which discusses the spectrum of errors that may implicate a lawyer’s duty of disclosure. In doing so, it identified errors ranging from those plainly requiring disclosure (a missed statute of limitations or a failure to file a timely appeal) to those “that may never cause harm to the client, either because any resulting harm is not reasonably foreseeable, there is no prejudice to a client’s right or claim, or the lawyer takes corrective measures that are reasonably likely to avoid any such prejudice.” Errors by lawyers between these two extremes must be analyzed individually. For example, disclosure is not required where the law on an issue is unsettled and a lawyer makes a tactical decision among “equally viable alternatives.” On the other hand, “potential errors that may give rise to an ethical duty to disclose include the failure to request a jury in a pleading (or pay the jury fee), the failure to include an acceleration provision in a promissory note, and the failure to give timely notice under a contract or statute.” Ultimately, the Colorado Bar concluded that whether a particular error gives rise to an ethical obligation to disclose depends on whether the error is “material,” which further “depends on whether a disinterested lawyer would conclude that the error will likely result in prejudice to the client’s right or claim.”

These opinions provide helpful guidance to lawyers, but they do not—just as we do not—purport to precisely define the scope of a lawyer’s disclosure obligations. Still, the Committee believes that lawyers deserve more specific guidance in evaluating their duty to disclose errors to current clients than has previously been available.

In attempting to define the boundaries of this obligation under Model Rule 1.4, it is unreasonable to conclude that a lawyer must inform a current client of an error only if that error may support a colorable legal malpractice claim, because a lawyer’s error may impair a client’s representation even if the client will never be able to prove all of the elements of malpractice. At the same time, a lawyer should not necessarily be able to avoid disclosure of an error absent apparent harm to the client because the lawyer’s error may be of such a nature that it would cause a reasonable client to lose confidence in the lawyer’s ability to perform the representation competently, diligently, or loyally despite the absence of clear harm. Finally, client protection and the purposes of legal representation dictate that the standard for imposing an obligation to disclose must be objective.

With these considerations in mind, the Committee concludes that a lawyer must inform a current client of a material error committed by the lawyer in the representation. An error is material if a disinterested lawyer would conclude that it is (a) reasonably likely to harm or prejudice a client; or (b) of such a nature that it would reasonably cause a client to consider terminating the representation even in the absence of harm or prejudice.

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10 Colo. Op. 113, supra note 1, at 3.
11 Id.
12 Id.
13 Id. at 1, 3.
A lawyer must notify a current client of a material error promptly under the circumstances.\textsuperscript{14} Whether notification is prompt will be a case- and fact-specific inquiry. Greater urgency is required where the client could be harmed by any delay in notification. The lawyer may consult with his or her law firm’s general counsel, another lawyer, or the lawyer’s professional liability insurer before informing the client of the material error.\textsuperscript{15} Such consultation should also be prompt. When it is reasonable to do so, the lawyer may attempt to correct the error before informing the client. Whether it is reasonable for the lawyer to attempt to correct the error before informing the client will depend on the facts and should take into account the time needed to correct the error and the lawyer’s obligation to keep the client reasonably informed about the status of the matter.

When a Current Client Becomes a Former Client

As indicated earlier, whether a lawyer must reveal a material error depends on whether the affected person or entity is a current or former client. Substantive law, rather than rules of professional conduct, controls whether an attorney-client relationship exists, or once established, whether it is ongoing or has been concluded.\textsuperscript{16} Generally speaking, a current client becomes a former client (a) at the time specified by the lawyer for the conclusion of the representation, and acknowledged by the client, such as where the lawyer’s engagement letter states that the representation will conclude upon the lawyer sending a final invoice, or the lawyer sends a disengagement letter upon the completion of the matter (and thereafter acts consistently with the letter);\textsuperscript{17} (b) when the lawyer withdraws from the representation pursuant to Model Rule of Professional Conduct 1.16; (c) when the client terminates the representation;\textsuperscript{18} or (d) when overt acts inconsistent with the continuation of the attorney-client relationship indicate that the

\textsuperscript{14} See N.J. Eth. Op. 684, supra note 1, 1998 WL 35985928, at *1 (“Clearly, RPC 1.4 requires prompt disclosure in the interest of allowing the client to make informed decisions. Disclosure should therefore occur when the attorney ascertains malpractice may have occurred, even though no damage may yet have resulted.”); 2015 N.C. Eth. Op. 4, supra note 1, 2015 WL 5927498, at *4 (“The error should be disclosed to the client as soon as possible after the lawyer determines that disclosure of the error to the client is required.”); Tex. Eth. Op. 593, supra note 1, 2010 WL 1026287, at *1 (requiring disclosure “as promptly as reasonably possible”).

\textsuperscript{15} See MODEL RULES R. 1.6(b)(4) (2018) (permitting a lawyer to reveal information related to a client’s representation “to secure legal advice about the lawyer’s compliance with these Rules”).

\textsuperscript{16} United States v. Williams, 720 F.3d 674, 686 (8th Cir. 2013); Rozmus v. West, 13 Vet. App. 386, 387 (U.S. App. Vet. Cl. 2000); see also MODEL RULES Scope cmt. 17 (2018) (explaining that “for purposes of determining the lawyer’s authority and responsibility, principles of substantive law external to these Rules determine whether a client-lawyer relationship exists”).

\textsuperscript{17} See Artromick Int’l, Inc. v. Drustar Inc., 134 F.R.D. 226, 229 (S.D. Ohio 1991) (observing that “the simplest way for either the attorney or client to end the relationship is by expressly saying so”); see also, e.g., Rusk v. Harstad, 393 P.3d 341, 344 (Utah Ct. App. 2017) (concluding that a would-be client could not have reasonably believed that the law firm represented him where the lawyer had clearly stated in multiple e-mails that the law firm would not represent him).

\textsuperscript{18} A client may discharge a lawyer at any time for any reason, or for no reason. White Pearl Inversiones S.A. (Uruguay) v. Cemusa, Inc., 647 F.3d 684, 689 (7th Cir. 2011); Nabi v. Sells, 892 N.Y.S.2d 41, 43 (App. Div. 2009); MODEL RULES R. 1.16 cmt. 4; see also STEPHEN GILLERS, REGULATION OF LAWYERS: PROBLEMS OF LAW AND ETHICS 77 (11th ed. 2018) (“Clients, it is said, may fire their lawyers for any reason or no reason.”) (citations omitted).
relationship has ended. If a lawyer represents a client in more than one matter, the client is a current client if any of those matters is active or open; in other words, the termination of representation in one or more matters does not transform a client into a former client if the lawyer still represents the client in other matters.

Absent express statements or overt acts by either party, an attorney-client relationship also may be terminated when it would be objectively unreasonable to continue to bind the parties to each other. In such cases, the parties’ reasonable expectations often hinge on the scope of the lawyer’s representation. In that regard, the court in *National Medical Care, Inc. v. Home Medical of America, Inc.*, suggested that the scope of a lawyer’s representation loosely falls into one of three categories: (1) the lawyer is retained as general counsel to handle all of the client’s legal matters; (2) the lawyer is retained for all matters in a specific practice area; or (3) the lawyer is retained to represent the client in a discrete matter.

For all three categories identified by the *National Medical Care* court, unless the client or lawyer terminates the representation, the attorney-client relationship continues as long as the lawyer is responsible for a pending matter. With respect to categories one and two above, an attorney-client relationship continues even when the lawyer has no pending matter for the client because the parties reasonably expect that the lawyer will handle all matters for the client in the future as they arise. In the third category, where a lawyer agrees to undertake a specific matter, the attorney-client relationship ends once the matter is concluded.

Although not identified by the *National Medical Care* court, another type of client is what might be called an episodic client, meaning a client who engages the lawyer whenever the client requires legal representation, but whose legal needs are not constant or continuous. In many such

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19 See, e.g., Artromick Int’l, Inc., 134 F.R.D. at 230–31 (determining that a man was a former client because he refused to pay the lawyer’s bill and then retained other lawyers to replace the first lawyer); Waterbury Garment Corp. v. Strata Prods., 554 F. Supp. 63, 66 (S.D.N.Y. 1982) (concluding that a person was a former client because the law firm represented him only in discrete transactions that had concluded and the person had subsequently retained different counsel).


21 Id. at 229–30.


23 Id. at *4.

24 Id.; see also MODEL RULES R. 1.3 cmt. 4 (2018) (stating that unless the relationship is terminated under Model Rule 1.16, the lawyer “should carry through to conclusion all matters undertaken for a client”).

25 See Berry v. McFarland, 278 P.3d 407, 411 (Idaho 2012) (explaining that “[i]f the attorney agrees to handle any matters the client may have, the relationship continues until the attorney or client terminates the relationship”); see also MODEL RULES R. 1.3 cmt. 4 (2018) (advising that “[i]f a lawyer has served a client over a substantial period in a variety of matters, the client sometimes may assume that the lawyer will continue to serve on a continuing basis unless the lawyer gives notice of withdrawal”).

26 Simpson v. James, 903 F.2d 372, 376 (5th Cir. 1990); Berry, 278 P.3d at 411; see also Revise Clothing, Inc. v. Joe’s Jeans Subsidiary, Inc., 687 F. Supp. 2d 381, 389–90 (S.D.N.Y. 2010) (noting that an attorney-client relationship is ordinarily terminated by the accomplishment of the purpose for which it was formed); Thayer v. Fuller & Henry Ltd., 503 F. Supp. 2d 887, 892 (N.D. Ohio 2007) (observing that an attorney-client relationship may terminate when the underlying action has concluded or when the attorney has exhausted all remedies and declined to provide additional legal services); MODEL RULES R. 1.16 cmt. 1 (“Ordinarily, a representation in a matter is completed when the agreed-upon assistance has been concluded.”).
instances, the client reasonably expects that the professional relationship will span any intervals and that the lawyer will be available when the client next needs representation.\textsuperscript{27} If so, the client should be considered a current client. In other instances, it is possible that the attorney-client relationship ended when the most recent matter concluded.\textsuperscript{28} Whether an episodic client is a current or former client will thus depend on the facts of the case.

**The Former Client Analysis Under the Model Rules**

As explained above, a lawyer must inform a current client of a material error under Model Rule 1.4. Rule 1.4 imposes no similar duty to former clients.

Four of the five subparts in Model Rule 1.4(a) expressly refer to “the client” and the one that does not—Model Rule 1.4(a), governing lawyers’ duty to respond to reasonable requests for information—is aimed at responding to requests from a current client. Model Rule 1.4(b) refers to “the client” when describing a lawyer’s obligations. Nowhere does Model Rule 1.4 impose on lawyers a duty to communicate with former clients. The comments to Model Rule 1.4 are likewise focused on current clients and are silent with respect to communications with former clients. There is nothing in the legislative history of Model Rule 1.4 to suggest that the drafters meant the duties expressed there to apply to former clients.\textsuperscript{29} Had the drafters of the Model Rules intended Rule 1.4 to apply to former clients, they presumably would have referred to former clients in the language of the rule or in the comments to the rule. They did neither despite knowing how to distinguish duties owed to current clients from duties owed to former clients when appropriate, as reflected in the Model Rules regulating conflicts of interest.\textsuperscript{30}

\textsuperscript{27} See, e.g., Parallel Iron, LLC v. Adobe Sys. Inc., C.A. No. 12-874-RGA, 2013 WL 789207, at *2–3 (D. Del. Mar. 4, 2013) (concluding that Adobe was a current client in July 2012 when the law firm was doing no work for it; the firm had served as patent counsel to Adobe intermittently between 2006 and February 2012, and had not made clear to Adobe that its representation was terminated); Jones v. Rabanco, Ltd., No. C03-3195P, 2006 WL 2237708, at *3 (W.D. Wash. Aug. 3, 2006) (reasoning that the law firm’s inclusion as a contact under a contract, the law firm’s work for the client after the contract was finalized, and the fact that the client matter was still open in the law firm’s files all indicated an existing attorney-client relationship); STEPHEN GILLERS, REGULATION OF LAWYERS: PROBLEMS OF LAW AND ETHICS 78-79 (11th ed. 2018) (“Lawyers might believe that a client is no longer a client if they are doing no work for it at the moment and haven’t for a while. . . . [A] firm may have done work for a client two or three times a year for the past five years, creating a reasonable client expectation that the professional relationship continues during the intervals and that the lawyer will be available the next time the client needs her.”).

\textsuperscript{28} See, e.g., Calamar Enters., Inc. v. Blue Forest Land Grp., Inc., 222 F. Supp. 3d 257, 264–65 (W.D.N.Y. 2016) (rejecting the client’s claim of an attorney-client relationship where the relationship between the law firm and the client had been dormant for three years; despite the fact that the attorney-client relationship had not been formally terminated, it ended when the purpose of the parties’ retainer agreement had been completed).


\textsuperscript{30} Compare MODEL RULES R. 1.7 (2018) (addressing current client conflicts of interest), with MODEL RULES R. 1.9 (2018) (governing former client conflicts of interest).
Because Model Rule 1.4 does not impose on lawyers a duty to communicate with former clients,\(^3\) it is no basis for requiring lawyers to disclose material errors to former clients.

The California State Bar’s Committee on Professional Responsibility and Conduct reached a similar conclusion with respect to California Rule of Professional Conduct 3-500, which states that “[a] member [of the State Bar of California] shall keep a client reasonably informed about significant developments relating to the employment or representation, including promptly complying with reasonable requests for information and copies of significant documents when necessary to keep the client so informed.” In concluding that a lawyer had no duty to keep a former client informed of significant developments in the representation, and specifically the former client’s possible malpractice claim against the lawyer, the Committee focused on the fact that the lawyer and the former client had “terminated their attorney-client relationship” and on Rule 3-500’s reference to a “client,” meaning a current client.\(^2\)

Finally, in terms of possible sources of an obligation to disclose material errors to former clients, Model Rule 1.16(d) provides in pertinent part that, upon termination of a representation, “a lawyer shall take steps to the extent reasonably practicable to protect a client’s interests, such as giving reasonable notice to the client, allowing time for employment of other counsel, surrendering papers and property to which the client is entitled and refunding any advance payment of fee[s] or expense[s] that has not been earned or incurred.” This provision does not create a duty to inform former clients of material errors for at least two reasons. First, the wording of the rule demonstrates that the error would have to be discovered while the client was a current client, thereby pushing any duty to disclose back into the current client communication regime. Second, Model Rule 1.16(d) is by its terms limited to actions that may be taken upon termination of the representation or soon thereafter; it cannot reasonably be construed to apply to material errors discovered months or years after termination of the representation.

**Conclusion**

The Model Rules require a lawyer to inform a current client if the lawyer believes that he or she may have materially erred in the client’s representation. Recognizing that errors occur along a continuum, an error is material if a disinterested lawyer would conclude that it is (a) reasonably likely to harm or prejudice a client; or (b) of such a nature that it would reasonably cause a client to consider terminating the representation even in the absence of harm or prejudice. The lawyer

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must so inform the client promptly under the circumstances. Whether notification is prompt is a case- and fact-specific inquiry.

No similar duty of disclosure exists under the Model Rules where the lawyer discovers after the termination of the attorney-client relationship that the lawyer made a material error in the former client’s representation.
Rule 1.2. Scope of Representation.

(c) A lawyer may limit the objectives of the representation if the limitation is reasonable under the circumstances and the client gives informed consent.

COMMENT

[6] Rule 1.5 (b) requires a lawyer to communicate in writing the scope of the lawyer's representation when the lawyer has not regularly represented a client. In all matters involving limited scope representation, it is generally prudent for a lawyer to state in writing any limitation on representation, provide the client with a written summary of considerations discussed, and to receive a written informed consent from the client to the lawyer's limited representation. The term "informed consent" is defined in Rule 1.0 (c) and is discussed in Comment 28 to Rule 1.7. Lawyers also should recognize that information and discussion sufficient for informed consent by more sophisticated business clients may not be sufficient to permit less sophisticated clients to provide informed consent. See Comment 28 to Rule 1.7.

Criminal, Fraudulent, and Prohibited Transactions

[76] A lawyer is required to give an honest opinion about the actual consequences that appear likely to result from a client's conduct. The fact that a client uses advice in a course of action that is criminal or fraudulent does not, of itself, make a lawyer a party to the course of action. However, a lawyer may not knowingly assist a client in criminal or fraudulent conduct. There is a critical distinction between presenting an analysis of legal aspects of questionable conduct and recommending the means by which a crime or fraud might be committed with impunity.

[87] When the client's course of action has already begun and is continuing, the lawyer's responsibility is especially delicate. The lawyer is required to avoid assisting the client, for example, by drafting or delivering documents that the lawyer knows are fraudulent or by suggesting how the wrongdoing might be concealed. A lawyer may not continue assisting a client in conduct that the lawyer originally supposed was legally proper but then discovers is criminal or fraudulent. The lawyer must, therefore, withdraw from the representation of the client in the matter. See Rule 1.16 (a). In some cases, withdrawal alone might be insufficient. It may be necessary for the lawyer to give notice of the fact of withdrawal and to disaffirm any opinion, document, affirmation or the like. See Rule 4.1.

[98] Where the client is a fiduciary, the lawyer may be charged with special obligations in dealings with a beneficiary.

[109] Paragraph (d) applies whether or not the defrauded party is a party to the transaction. Hence, a lawyer should not participate in a sham transaction; for example, a transaction to effectuate criminal or fraudulent escape of tax liability. Paragraph (d) does not preclude undertaking a criminal defense incident to a general retainer for legal services to a lawful enterprise. The last
clause of paragraph (d) recognizes that determining the validity or interpretation of a statute or regulation may require a course of action involving disobedience of the statute or regulation or of the interpretation placed upon it by governmental authorities.
Loss Prevention Services

Quality Assurance Review

A timely review of practice management issues affecting the legal profession

The Aon Claims Experience
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The Aon Claims Experience

By Douglas R. Richmond, Managing Director,
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I. Introduction

We have long tracked publicly-reported verdicts against, and settlements by, law firms with the goal of educating our clients about the nature of claims being asserted against them, including the size, cause of loss, noticeable trends, and associated risks. This is a valuable but imperfect endeavor because publicly-reported matters represent but a small percentage of the cases or claims against law firms. Many cases are kept confidential through arbitration. And, even when lawsuits against firms receive substantial media attention at the outset or during the course of the litigation, they often settle confidentially. Analyzing the conduct which gives rise to publicly-reported matters is also challenging because complaints typically include a potpourri of allegations and theories that impede a true understanding or meaningful study of what factors prompted the claim against the attorney or law firm, and press reports of verdicts or settlements rarely provide the level of detail that we'd like to see.

Realizing the risk management value to be gained from better understanding law firms’ claims experience, we embarked on the arduous task of analyzing in detail the claims history of our approximately 275 firms over the past 10 years. On the whole, our clients may reasonably be classified as large law firms, but we also serve numerous midsized firms, as well as some boutique firms. We began our study by reviewing the claims and circumstances described in clients’ annual submissions to insurers. We also examined claims bordereaux prepared by monitoring counsel when available. Ultimately, each notification, whether it was a circumstance or claim, was categorized by both practice area and the conduct which most directly lead to the allegations of misconduct made against the lawyer or firm. Finally, we calculated the amounts paid in defense costs, settlements, or judgments for each matter. We recorded defense costs and indemnity payments “ground up,” meaning that we captured sums paid by firms within their self-insured retentions as well as funds paid by insurers.

In our review, we analyzed 5,941 notifications. Again, a notification could be either a claim or a circumstance. Out of these notifications, firms and their insurers paid 805 settlements or judgments totaling $1,258,209,413. Because these indemnity payments do not include any disgorgements of fees or fees written off by firms in resolving claims, the total loss experienced by our firms may be slightly higher than the reported figure.

All told, firms and their insurers paid $590,313,095 in defense costs. We believe this figure to be materially underreported. In their submissions to insurers, firms often described settlements or judgments without reporting the defense costs associated with the matters. The expense incurred when a firm self-defended a dispute was also rarely, if ever, reported. And when it was obvious that a firm would not meet its retention amount in a policy year, it often said nothing in its submission about legal fees incurred in the defense of reported matters.

Our analysis of our firms’ data confirms many of our beliefs about the nature of the risks facing law firms today. For example, the data reinforced our concerns about the severity of third-party claims against firms arising out the representation of dishonest or unworthy clients. But we were also surprised by a few of our discoveries. In any event, we present the key results of our study here in the hope that they will help firms better understand the liability environment and focus their risk management efforts accordingly. If nothing else, our data point to the need for good practice management; a culture of collaboration that minimizes the opportunity for error and increases the chance of detection and opportunity for timely correction or mitigation of mistakes; continued attention to careful business intake; and, in some instances, the development or implementation of systems to reduce risk.
II. Notifications and Payments – A Macro View

Figure A below reflects a varying number of notifications being reported by our firms over the past ten years. The gray bar represents the total number of notifications by policy year, while the green bar reflects the number of open claims remaining as of year-end 2013. The blue line in Figure A reflects the number of notifications in which some form of payment was made, whether in the form of attorneys’ fees, settlements, or judgments, or some combination of the three.

The increase in the number of notifications since 2007 does not necessarily reflect a more active claims environment, or a decline in practice quality or attorneys’ adherence to their professional obligations. Rather, the increase is just as likely a result of the growing number of lawyers in our client population, whether through the addition of new law firm clients or as a result of existing clients’ growth, and firms’ increasing sensitivity to the need to report to their insurers circumstances that could lead to claims. The widely-reported insurance industry sentiment that the frequency of claims against lawyers would grow exponentially as a result of the economic crisis beginning in 2007-2008 is simply not borne out in our data. Even if there has been some related increase, it has been comparatively modest and certainly nowhere close to the scale predicted or feared. Whether the insurance industry’s concern over the severity of claims in certain practice areas arising during the same time is meritorious is as yet unclear. Figure A reflects a number of matters from the 2007-2010 policy years that remain open. Many of these claims are in the real estate or corporate practice areas, which seem to have been most affected by the recession. A number of these claims involve significant alleged damages.

2004-2013 Lawyers Professional Liability Claims Summary
Notice Counts and Ground Up Payments

Figure A

<table>
<thead>
<tr>
<th>Year</th>
<th>Notices</th>
<th>Open Matters</th>
<th>Ground Up Paid</th>
<th>Notices with Ground Up Payment</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>359</td>
<td>504</td>
<td>$482.0M</td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td>100</td>
<td>135</td>
<td>$191.4M</td>
<td></td>
</tr>
<tr>
<td>2006</td>
<td>20</td>
<td>132</td>
<td>$257.1M</td>
<td></td>
</tr>
<tr>
<td>2007</td>
<td>26</td>
<td>136</td>
<td>$194.8M</td>
<td></td>
</tr>
<tr>
<td>2008</td>
<td>58</td>
<td>147</td>
<td>$238.8M</td>
<td></td>
</tr>
<tr>
<td>2009</td>
<td>84</td>
<td>139</td>
<td>$256.0M</td>
<td></td>
</tr>
<tr>
<td>2010</td>
<td>120</td>
<td>120</td>
<td>$88.9M</td>
<td></td>
</tr>
<tr>
<td>2011</td>
<td>160</td>
<td>98</td>
<td>$79.9M</td>
<td></td>
</tr>
<tr>
<td>2012</td>
<td>84</td>
<td>46</td>
<td>$49.1M</td>
<td></td>
</tr>
<tr>
<td>2013</td>
<td>689</td>
<td>231</td>
<td>$21.1M</td>
<td></td>
</tr>
</tbody>
</table>
The red line on Figure A illustrates the total amount of ground up payments by policy year made through year-end 2013. Payments are recorded in the policy year in which the claim was reported, regardless of when it was settled or went to judgment. Thus, and by way of example, if a claim was reported in 2009 but settled for $5 million in 2012, that $5 million payment is reflected in the 2009 policy year total. Again, the gray part of each column represents all notifications and the green portion of each column represents the number of claims that remain open for that policy year.

This data deserves additional comment. First, even in years where significant defense and indemnity payments have been made (e.g., 2004-2008), a number of open claims remain. Second, claims that were notified several years ago and which remain open will likely not be resolved without some, or possibly significant, payments made in the form of fees or settlements. Third, we know of recent settlements of claims arising out of the 2007 and 2008 policy years that will bring total payments in those years close to the amounts thus far paid for 2006 matters. Finally, the relatively small payment figures for 2010 and the years after are not yet cause for celebration. Most of these claims are not developed; as most readers well know, claims against law firms are typically long-tail events. One or more significant claims arising from those policy years could cause the total for the affected years to approach or exceed the figures found in some of the years in the mid-2000s.

III. Practice Areas

The chart set forth in Figure B analyzes the Aon claims experience from the standpoint of the twenty-one practice areas we assigned to notifications. The first four columns from left to right address the frequency of notifications in each practice area, while the final three columns focus on the severity of the losses by each practice area.

Figure B

<table>
<thead>
<tr>
<th>Area of Practice</th>
<th>Notice Count</th>
<th>% of Total Notices</th>
<th>GU Matters</th>
<th>% of GU Matters</th>
<th>GU Paid</th>
<th>% of GU Paid</th>
<th>Median GU Paid</th>
</tr>
</thead>
<tbody>
<tr>
<td>Administrative Law</td>
<td>76</td>
<td>1.28%</td>
<td>12</td>
<td>1.03%</td>
<td>$25.5M</td>
<td>1.38%</td>
<td>$100.0k</td>
</tr>
<tr>
<td>Banking</td>
<td>100</td>
<td>1.68%</td>
<td>16</td>
<td>1.37%</td>
<td>$26.3M</td>
<td>1.42%</td>
<td>$849.5k</td>
</tr>
<tr>
<td>Bankruptcy</td>
<td>207</td>
<td>3.48%</td>
<td>36</td>
<td>3.08%</td>
<td>$30.5M</td>
<td>1.65%</td>
<td>$252.6k</td>
</tr>
<tr>
<td>Bond</td>
<td>62</td>
<td>1.04%</td>
<td>14</td>
<td>1.20%</td>
<td>$4.7M</td>
<td>0.25%</td>
<td>$137.0k</td>
</tr>
<tr>
<td>Corporate/Transactional</td>
<td>1,111</td>
<td>18.70%</td>
<td>250</td>
<td>21.37%</td>
<td>$695.6M</td>
<td>37.63%</td>
<td>$334.7k</td>
</tr>
<tr>
<td>Employee Benefits &amp; ERISA</td>
<td>47</td>
<td>0.79%</td>
<td>11</td>
<td>0.94%</td>
<td>$29.1M</td>
<td>1.57%</td>
<td>$300.0k</td>
</tr>
<tr>
<td>Employment &amp; Labor</td>
<td>290</td>
<td>4.88%</td>
<td>35</td>
<td>2.99%</td>
<td>$23.3M</td>
<td>1.26%</td>
<td>$100.0k</td>
</tr>
<tr>
<td>Energy (e.g., oil and gas)</td>
<td>25</td>
<td>0.42%</td>
<td>3</td>
<td>0.26%</td>
<td>$28.3M</td>
<td>1.53%</td>
<td>$4,000.0k</td>
</tr>
<tr>
<td>Environmental</td>
<td>39</td>
<td>0.66%</td>
<td>8</td>
<td>0.68%</td>
<td>$26.4M</td>
<td>1.43%</td>
<td>$888.0k</td>
</tr>
<tr>
<td>Family Law</td>
<td>125</td>
<td>2.10%</td>
<td>15</td>
<td>1.28%</td>
<td>$4.2M</td>
<td>0.23%</td>
<td>$63.6k</td>
</tr>
<tr>
<td>Governmental Affairs/Lobbying</td>
<td>30</td>
<td>0.50%</td>
<td>19</td>
<td>1.62%</td>
<td>$77.1M</td>
<td>4.17%</td>
<td>$1,500.0k</td>
</tr>
<tr>
<td>Health Care</td>
<td>37</td>
<td>0.62%</td>
<td>14</td>
<td>1.20%</td>
<td>$5.3M</td>
<td>0.29%</td>
<td>$104.9k</td>
</tr>
<tr>
<td>Intellectual Property</td>
<td>667</td>
<td>11.23%</td>
<td>74</td>
<td>6.32%</td>
<td>$68.0M</td>
<td>3.68%</td>
<td>$177.5k</td>
</tr>
<tr>
<td>Litigation (Commercial)</td>
<td>1,468</td>
<td>24.71%</td>
<td>292</td>
<td>24.96%</td>
<td>$272.1M</td>
<td>14.72%</td>
<td>$99.3k</td>
</tr>
<tr>
<td>Litigation (Criminal)</td>
<td>29</td>
<td>0.49%</td>
<td>1</td>
<td>0.09%</td>
<td>$1.8M</td>
<td>0.10%</td>
<td>$1,800.0k</td>
</tr>
<tr>
<td>Litigation (IP)</td>
<td>162</td>
<td>2.73%</td>
<td>33</td>
<td>2.82%</td>
<td>$39.3M</td>
<td>2.12%</td>
<td>$196.6k</td>
</tr>
<tr>
<td>Litigation (Personal Injury)</td>
<td>253</td>
<td>4.26%</td>
<td>39</td>
<td>3.33%</td>
<td>$9.3M</td>
<td>0.50%</td>
<td>$50.0k</td>
</tr>
<tr>
<td>Real Estate</td>
<td>515</td>
<td>8.67%</td>
<td>131</td>
<td>11.20%</td>
<td>$151.5M</td>
<td>8.19%</td>
<td>$187.5k</td>
</tr>
<tr>
<td>Securities</td>
<td>139</td>
<td>2.34%</td>
<td>40</td>
<td>3.42%</td>
<td>$109.7M</td>
<td>5.94%</td>
<td>$652.3k</td>
</tr>
<tr>
<td>Tax</td>
<td>142</td>
<td>2.39%</td>
<td>46</td>
<td>3.93%</td>
<td>$123.8M</td>
<td>6.70%</td>
<td>$667.8k</td>
</tr>
<tr>
<td>Trusts &amp; Estates</td>
<td>417</td>
<td>7.02%</td>
<td>81</td>
<td>6.92%</td>
<td>$96.8M</td>
<td>5.24%</td>
<td>$158.8k</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>5,941</strong></td>
<td><strong>1,170</strong></td>
<td><strong>1,848.5M</strong></td>
<td></td>
<td><strong>$190.8k</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

GU = Ground Up
A. Frequency by Practice Area

Figures C, D, and E are graphic depictions of the data accumulated in Figure B. Figure C illustrates claim frequency by practice area. Not surprisingly, litigation generated the greatest number of notifications. The corporate/transactional practice area was second, followed by intellectual property, real estate, trust and estates, and employment practice. Our claims frequency is very similar to that reported by the Attorneys’ Liability Assurance Society, better known as ALAS. ALAS likewise reports litigation as the leading producer of claims, followed by corporate practice. Our claims data differs from ALAS’s in terms of frequency primarily from the standpoint of the number of intellectual property notifications. This is undoubtedly a result of our representation of a number of IP firms, whereas ALAS only began insuring IP firms in 2005 or so and still has very few on its roster. In addition, we represent a number of full-service firms with large IP practices.

### Practice Area | Notice Count

<table>
<thead>
<tr>
<th>Practice Area</th>
<th>Notice Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>Litigation</td>
<td>32%</td>
</tr>
<tr>
<td>Corporate/Transaction</td>
<td>19%</td>
</tr>
<tr>
<td>Intellectual Property</td>
<td>11%</td>
</tr>
<tr>
<td>Real Estate</td>
<td>9%</td>
</tr>
<tr>
<td>Trusts &amp; Estates</td>
<td>7%</td>
</tr>
<tr>
<td>Employment &amp; Labor</td>
<td>5%</td>
</tr>
<tr>
<td>Other</td>
<td>17%</td>
</tr>
</tbody>
</table>

The ABA’s Standing Committee on Lawyers’ Professional Liability also periodically publishes its Profile of Legal Malpractice Claims, which attempts to categorize claims against lawyers by practice area and cause of loss. The ABA data, in contrast to both the Aon and ALAS data, is driven almost entirely driven by small firms and sole proprietorships. The most recent profile data released in September 2012 and covering claims between 2008 and 2011 reveals the top 10 areas of practice from a claims frequency perspective as: (1) real estate; (2) plaintiffs’ personal injury litigation; (3) family law; (4) trusts and estates; (5) bankruptcy and collection; (6) criminal law; (7) corporate/ business organization; (8) business transaction/ commercial law; (9) personal injury defense litigation; and (10) international law.

B. Severity by Practice Area

Figures D and E graphically depict claim severity by practice area. We expected to find corporate lawyers to be at greater risk for significant claims and the data proved our thesis to be correct. The corporate/transactional practice area accounted for 36% of all ground up payments. Besides commercial litigation, no other practice area accounted for even 10% of the total ground up payments. There are numerous reasons for this disproportionate risk, including, but not limited to, the size of projects being handled by our clients’ transactional lawyers; a continuing series of unworthy client matters exposing firms to liability for aiding and abetting the unworthy clients’ misconduct, as well as to liability for fraud and negligent misrepresentation; and the fact that corporate practice errors were often detected long after the transaction was completed and the ability to remedy or mitigate a mistake was lost.

In reviewing the results found in Figures D and E, please understand that the energy and governmental affairs practice areas are outliers. The energy category encompasses very few claims, albeit collectively very costly ones, which easily could have been classified as corporate/transactional matters. In addition, the significant losses in the governmental affairs practice area were primarily the result of a single rogue lobbyist.
Admittedly, classifying notifications by practice area is sometimes as much art as it is science. A number of notifications that we classified as corporate/transactional matters could have equally fit in the securities, real estate, or banking areas. Thus, the data must be interpreted with some flexibility. Even so, the fact remains that transactional practices are exponentially more susceptible to severe claims than is litigation practice.

There is one final noteworthy point. When it comes to litigation practice, awards of monetary sanctions will typically not be included in the data. Probably because of exclusions for fines and penalties in lawyers’ professional liability insurance policies that generally absolve insurers of related indemnity obligations, firms often did not report sanctions against their lawyers in their renewal applications. Even so, we are aware of numerous significant sanction awards entered against trial lawyers in the past few years.

2004-2013 Lawyers Professional Liability Claims Summary
Total and Average Ground Up Paid by Practice Area

<table>
<thead>
<tr>
<th>Practice Area</th>
<th>Total Ground Up Paid</th>
<th>Average Ground Up Paid (Paid Claims Only)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Administrative Law</td>
<td>$2,125,195</td>
<td>$2,125,195</td>
</tr>
<tr>
<td>Banking</td>
<td>$1,645,760</td>
<td>$1,645,760</td>
</tr>
<tr>
<td>Bankruptcy</td>
<td>$847,249</td>
<td>$847,249</td>
</tr>
<tr>
<td>Bond</td>
<td>$336,648</td>
<td>$336,648</td>
</tr>
<tr>
<td>Corporate/Transactional</td>
<td>$2,782,460</td>
<td>$2,782,460</td>
</tr>
<tr>
<td>Employee Benefits &amp; ERISA</td>
<td>$2,646,424</td>
<td>$2,646,424</td>
</tr>
<tr>
<td>Employment &amp; Labor</td>
<td>$665,450</td>
<td>$665,450</td>
</tr>
<tr>
<td>Energy (e.g., oil and gas)</td>
<td>$9,420,919</td>
<td>$9,420,919</td>
</tr>
<tr>
<td>Environmental</td>
<td>$3,294,161</td>
<td>$3,294,161</td>
</tr>
<tr>
<td>Family Law</td>
<td>$280,962</td>
<td>$280,962</td>
</tr>
<tr>
<td>Governmental Affairs/Lobbying</td>
<td>$4,056,789</td>
<td>$4,056,789</td>
</tr>
<tr>
<td>Health Care</td>
<td>$379,598</td>
<td>$379,598</td>
</tr>
<tr>
<td>Intellectual Property</td>
<td>$919,045</td>
<td>$919,045</td>
</tr>
<tr>
<td>Litigation (Commercial)</td>
<td>$931,778</td>
<td>$931,778</td>
</tr>
<tr>
<td>Litigation (Criminal)</td>
<td>$1,800,000</td>
<td>$1,800,000</td>
</tr>
<tr>
<td>Litigation (IP)</td>
<td>$1,190,111</td>
<td>$1,190,111</td>
</tr>
<tr>
<td>Litigation (Personal Injury)</td>
<td>$238,347</td>
<td>$238,347</td>
</tr>
<tr>
<td>Real Estate</td>
<td>$1,156,342</td>
<td>$1,156,342</td>
</tr>
<tr>
<td>Securities</td>
<td>$2,742,995</td>
<td>$2,742,995</td>
</tr>
<tr>
<td>Tax</td>
<td>$2,690,565</td>
<td>$2,690,565</td>
</tr>
<tr>
<td>Trusts &amp; Estates</td>
<td>$1,195,179</td>
<td>$1,195,179</td>
</tr>
</tbody>
</table>
IV. Causes of Claims

In addition to tracking notifications by practice area, we categorized each notification by the conduct that primarily caused the circumstance or loss. Although some factual instances could be placed in two or more categories, we attempted to identify the root cause leading to the notification or the ultimate loss. This was occasionally difficult when the information provided was scarce. At the opposite end of the spectrum, the task also was challenging if the notification encompassed many, if not most, of the theories of recovery we utilized in our analysis. For example, claims against lawyers for aiding and abetting clients’ misconduct were in some cases just as easily classified as fraud or negligent misrepresentation claims, since plaintiffs often alleged all three theories. Despite these inherent limitations, we believe this data is both informative as to the type of conduct which leads to claims being made against lawyers and instructive as to the expected consequences of such conduct.

Figure F is the numerical data in table form classifying all notifications by cause of loss. The first four columns reading from left to right address frequency, while the final three columns address the severity for each category of loss.

A. Frequency by Conduct Causing the Claim

We were surprised by the number of notifications attributable to mistakes; after all, we are privileged to represent many of the finest firms in the profession. Figure G illustrates the frequency of notifications for each cause of loss category. Although many firms report circumstances that describe possible mistakes out of an abundance of caution, and many of those matters never lead to losses of any sort, 20 percent of the mistake notifications still resulted in some form of payment by the law firm or its insurers. The mistakes came in a wide variety of forms, but some common themes did emerge.

Many of the mistakes were simple administrative errors. Missed deadlines were the leading problem in litigation practice. Failing to timely file expert witness disclosures, Rule 26 disclosures, pre-trial and post-trial motions, and notices of appeal are just a few examples. The intellectual property area was plagued by docketing errors in the form of delinquent responses to office actions and failures to file
or timely file maintenance fees for clients. Administrative errors in the corporate/transactional practice area also found their roots in poor docketing or task management, especially in the failure to perfect security interests for clients upon the completion of transactions.

Other recurring themes in the area of mistakes include poor communications between national and local counsel in litigation. Far too often each firm assumed the other was performing certain tasks when, in fact, nothing was done. A number of transactional practice notifications also arose out of cut and paste errors. For example, purchase agreements would contain two choice of law provisions with each paragraph referencing a different controlling jurisdiction. Similarly, a contract would incorporate illogical indemnity or escrow language which was clearly a remnant from the template used by the drafting attorney.

Substantive errors ranged from allegedly faulty tax opinions to poor trial strategies. Some of these notifications were generated by unhappy clients with unrealistic expectations, but others arose because the lawyer failed to comprehend and apply the law properly. And many of these substantive errors resulted in significant settlements. One trend that emerged with respect to alleged substantive errors was the absence of collaboration between lawyers or of partner oversight. Even though clients often demand efficiency and lean staffing, the risks associated with lawyers working in isolation or laboring under workloads or deadlines that overwhelm them are too great to discount or ignore. To the extent that supervision is an issue, senior lawyers need to remember their supervisory obligations under their states’ equivalents of Model Rule 5.1. This is an area in which lawyers’ recognition of their ethical obligations unquestionably reduces professional risk.

Dabbling by lawyers is also a recurring source of mistake claims. During the recent economic downturn the number of mistake notifications arising from dabbling increased, but dabbling claims are as old as law practice itself. Even when the economy is generally good a particular practice area within a firm may be slow or an individual lawyer may have an unfortunate amount of billable time to fill. A firm culture that encourages collaboration, discourages lawyers from experimenting in unfamiliar practice areas, and supports a well-managed new matter intake system will minimize both the frequency and severity of dabbling claims.

Although our data does not reflect it, we are also concerned that a number of mistakes are attributable to impaired lawyers. There is reliable evidence that lawyers suffer from depression at a disproportionate rate as compared to the general population and are similarly afflicted by substance abuse. Depression and chemical dependency obviously foster misjudgments and negatively affect lawyers’ diligence. The degree to which the mistake figures are attributable to impaired lawyers is, however, very difficult to determine because firms in their applications seldom identify lawyers’ alleged errors as being rooted in some form of impairment. In some cases they may not be aware of the impairment and in other cases they may not describe it out of compassion or respect for the lawyers. In any event, because we are gathering a majority of our information from firms’ applications, our ability to precisely track the frequency or severity of notifications resulting from impaired lawyers is limited.

The number of fraud and misrepresentation notifications was higher than expected. Most of the notifications in this category concerned allegations made by third parties against the lawyer or law firm. Examples include assertions against lawyers in the litigation practice area for knowingly misrepresenting material facts during discovery or in negotiations. In the transactional area, claims were often based on lawyers’ alleged false statements or failure to disclose information during the due diligence phase of a transaction. In these cases the adversary typically claimed that it would not have consummated the transaction, or would have valued it differently, had the lawyer made appropriate disclosures. A few notifications involved clients’ assertions of billing fraud or lawyers’ misrepresentations regarding the progress or status of matters.

Notifications based on conflicts of interest were relatively lower than expected. Firms have unquestionably devoted substantial resources to checking and clearing conflicts over the past ten years, and their efforts have paid off. But some common themes remain. The representation of multiple parties in transactional matters—or at least the alleged representation of multiple parties—is a common source of conflict of interest allegations, with the end game being a claim for breach of fiduciary duty. Consider this only slightly hypothetical scenario: Joel Frye and his son, Joel II (“Deuce” to his friends), are real estate investors and long-time clients of your partner, Derek Hines. The Fryes ask Hines to prepare all the documents necessary for their joint venture with another real estate investor, Mike Look. Hines does so and, in the course of the project, meets several times with the Fryes and Look to discuss the joint venture, the purchase and development of the commercial property that is its subject, and the like.
Over time, Look becomes disenchanted with the joint venture and the Fryes agree to buy out his interest. Hines represents the Fryes in the buy-out; Look is represented by separate counsel. During those negotiations, two potential buyers approach Deuce about the property. Hines either advises the Fryes not to share that information with Look, or he acquiesces in the Fryes’ decision not to do so.

Three days before the buy-out closes—on favorable terms to Look, by the way—the Fryes receive an offer for the property from one of the prospective buyers that is nearly three times the price the joint venture paid for it. Hines is comfortable with the Fryes’ decision not to disclose the offer to Look. After the buy-out closes, the Fryes accept the offer for the property and sell the property that once belonged to the joint venture.

Upon learning of the sale, Look sues both the Fryes and Hines for their alleged breach of fiduciary duties to the joint venture. With respect to Hines, Look alleges that Hines represented the joint venture rather than any of the individual venturers and, by favoring the Fryes over him, Hines breached his fiduciary duty to the joint venture.

We saw this scenario over and over again with relatively slight variations. Other conflict-related notifications centered on the enforceability of a conflict waiver previously executed by the client, with the recurring issue of whether the client had received sufficient factual information from the lawyer to give truly informed consent to the conflict.

B. Severity by Conduct Causing the Loss

*Figure H* illustrates the aggregate amount of ground up dollars paid in each category of conduct causing loss. Mistakes again led the way with almost $830 million in paid loss, which represents nearly 47 percent of the total amount paid. In light of the number of mistake-related notifications during the 10 years of our study, the sheer amount of claim payments in this category is perhaps predictable. The more conspicuous figures, however, are linked to the dishonest client and fraud and misrepresentation categories. Dishonest client issues represented only 9.88 percent of the total notifications, but accounted for over 23 percent of the total dollars paid. Fraud and misrepresentation claims, which are frequently (but certainly not always) made in conjunction with aiding and abetting allegations, accounted for almost 12 percent of the total amount paid.

2004-2013 Lawyers Professional Liability Claims Summary
Total Ground Up Paid by Conduct Causing the Loss

*Figure H*
The severity associated with dishonest client and fraud claims is best illustrated by the average amount paid for each category of conduct causing the loss. Figure I includes only those notifications where some monies were paid, whether they went to defense costs, settlement, satisfaction of a judgment, or some combination of the three. In other words, when a firm is forced to defend itself against allegations arising out of its representation of a dishonest client, our data indicate that an average of $3.5 million will be spent on the dispute. Although rare, claims originating from the conduct of dishonest lawyers are also expensive to resolve. Indeed, injecting a dishonesty element into a claim almost always intensifies the litigation, increasing defense costs and frequently inflating any settlement or verdict. Conflicts of interest likewise aggravate litigation and its corresponding costs. Many of the most serious matters involved alleged misconduct that combined some type of dishonesty and a conflict of interest.

Because of a concern that a few bad claims might skew the analysis, we also analyzed the median amount paid for each type of conduct causing the loss. Figure J depicts the median amount paid for each category of loss when at least some payment was made on the claim. Again, the severity of dishonest client and dishonest lawyer claims is evident from the median amounts that well exceed other categories of loss. Figures I and J corroborate the perverse proposition that “dishonesty pays.” Of course, it is the target firm and its insurance carriers that ultimately pay for any dishonesty, and those payments go to adversaries.

2004-2013 Lawyers Professional Liability Claims Summary
Average and Median Ground Up Paid by Conduct Causing the Loss

<table>
<thead>
<tr>
<th>Conduct</th>
<th>Average Ground Up Paid (Paid Claims Only)</th>
<th>Median Ground Up Paid (Paid Claims Only)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Conflicts of Interest</td>
<td>$1,138,783</td>
<td>$199,349</td>
</tr>
<tr>
<td>Dishonest Clients</td>
<td>$3,915,582</td>
<td>$348,530</td>
</tr>
<tr>
<td>Dishonest Lawyer</td>
<td>$2,632,784</td>
<td>$396,715</td>
</tr>
<tr>
<td>Fraud and Misrepresentation</td>
<td>$1,289,695</td>
<td>$124,600</td>
</tr>
<tr>
<td>Impaired Lawyer</td>
<td>$19,131</td>
<td>$19,131</td>
</tr>
<tr>
<td>Malicious Prosecution/Abuse of Process</td>
<td>$1,131,417</td>
<td>$25,000</td>
</tr>
<tr>
<td>Mistakes</td>
<td>$1,297,346</td>
<td>$195,000</td>
</tr>
</tbody>
</table>
C. Conduct Causing the Loss by Practice Area

One enlightening aspect of our data is the ability to analyze losses by practice area. For example, Figure K reflects the number of notifications, and Figure L illustrates the dollars paid, for each category of conduct which caused losses in the commercial litigation practice area.

As in every other area of practice, mistakes were the source of the greatest number of notifications in commercial litigation practice. A significant number of these notifications were generated by allegations of trial strategy error. But, because the claimant was required to prove both the negligence of the lawyer and that but for the breach the claimant would have prevailed in the litigation, a majority of these matters were either dismissed or settled for nuisance value. Even mistakes in the form of missed deadlines were often relatively inconsequential because they were identified at a time when effective corrective steps could be taken.

With respect to severity, dishonest clients played a significant role even in commercial litigation practice. A common claim falling into this category featured a client that concealed relevant documents or information from its lawyer during discovery, which later provided the basis for sanctions against both the client and the lawyer.

Commercial Litigation Claims

<table>
<thead>
<tr>
<th>Category</th>
<th>Notices</th>
<th>Matters with Ground Up Paid</th>
<th>Ground Up Paid</th>
</tr>
</thead>
<tbody>
<tr>
<td>Conflicts of Interest</td>
<td>27</td>
<td>120 (8.17%)</td>
<td>$34.1M (12.52%)</td>
</tr>
<tr>
<td>Dishonest Clients</td>
<td>44</td>
<td>273 (18.60%)</td>
<td>$68.9M (25.32%)</td>
</tr>
<tr>
<td>Dishonest Lawyer</td>
<td>2</td>
<td>9 (0.61%)</td>
<td>$0.5M (0.19%)</td>
</tr>
<tr>
<td>Fraud and Misrepresentation</td>
<td>38</td>
<td>221 (15.05%)</td>
<td>$36.3M (13.35%)</td>
</tr>
<tr>
<td>Impaired Lawyer</td>
<td>0</td>
<td>0 (0.00%)</td>
<td>$0.0M (0.00%)</td>
</tr>
<tr>
<td>Malicious Prosecution/Abuse of Process</td>
<td>54</td>
<td>268 (18.26%)</td>
<td>$58.1M (21.34%)</td>
</tr>
<tr>
<td>Mistakes</td>
<td>127</td>
<td>577 (39.31%)</td>
<td>$74.2M (27.28%)</td>
</tr>
</tbody>
</table>
Turning to the corporate/transactional practice area data, the frequency analysis reflected in Figure M is once again dominated by mistakes. Besides failing to perfect security interests, many notifications arose from allegations that a lawyer failed to properly document a transaction or provided poor advice regarding the transaction. For example, a client might allege that a lawyer failed to document the transaction so as to minimize any tax consequences, or failed to properly interpret a statute or regulation. Fraud and misrepresentation notifications were also numerous and often involved a counter-party’s claim that the lawyer misrepresented or concealed material facts during the negotiation of the transaction.

The costs associated with dishonest clients were most obvious in the corporate/transactional practice area. Figure N reflects that almost 50 percent of all amounts paid in this practice area were a result of firms’ representation of dishonest clients. Fraud and misrepresentation claims accounted for nearly 15 percent of the dollars spent in this practice area. As noted earlier, plaintiffs who sue firms for aiding and abetting clients’ alleged misconduct often allege fraud and negligent misrepresentation as well, although plaintiffs assert stand alone fraud and negligent misrepresentation claims with unfortunate regularity. Regardless, the data brightly highlight the risk associated with the representation of unworthy clients in corporate and transactional matters.
Figures O and P reflect the average and median amounts paid by conduct causing the loss in the corporate/transactional category and similarly highlight the risks associated with claims involving unworthy clients. The potential for a catastrophic loss due to a dishonest client exists almost exclusively in the corporate and transactional realm. The malicious prosecution/abuse of process category relates to claims arising out of the erroneous assertion of liens and security interests. As you can see, associated losses were insignificant.
As for intellectual property practice, mistakes account for over 82 percent of all notifications. Most mistake allegations are attributable to missed deadlines, but a few claims arose from patent lawyers’ failure to understand the art involved and the consequential filing of an application that failed to adequately cover the client’s invention. Other substantive claims included drafting errors that resulted in the rejection of the patent claims at the USPTO or subsequent invalidation of the claims by courts. With respect to severity, a substantial percentage of the payments are likewise a result of mistakes. Other major claims involved lawyers who allegedly engaged in inequitable conduct before the patent office. These claims included malpractice actions brought by clients whose patents were invalidated because of lawyers’ misconduct and third-party claims for fraud by the offending lawyers. The intellectual property frequency and severity data are set forth in Figures Q and R, respectively.

**Intellectual Property Claims**

<table>
<thead>
<tr>
<th>Category</th>
<th>Notices</th>
<th>Matters with Ground Up Paid</th>
<th>Ground Up Paid</th>
</tr>
</thead>
<tbody>
<tr>
<td>Conflicts of Interest</td>
<td>6</td>
<td>25 (3.75%)</td>
<td></td>
</tr>
<tr>
<td>Dishonest Clients</td>
<td>3</td>
<td>34 (5.10%)</td>
<td></td>
</tr>
<tr>
<td>Dishonest Lawyer</td>
<td>2</td>
<td>4 (0.60%)</td>
<td></td>
</tr>
<tr>
<td>Fraud and Misrepresentation</td>
<td>4</td>
<td>46 (6.90%)</td>
<td>$32.5M (47.79%)</td>
</tr>
<tr>
<td>Impaired Lawyer</td>
<td>0</td>
<td>1 (0.15%)</td>
<td>$0.0M (0.00%)</td>
</tr>
<tr>
<td>Malicious Prosecution/</td>
<td>2</td>
<td>6 (0.90%)</td>
<td>$0.4M (0.52%)</td>
</tr>
<tr>
<td>Abuse of Process</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mistakes</td>
<td>57</td>
<td>551 (82.61%)</td>
<td>$31.7M (46.68%)</td>
</tr>
</tbody>
</table>
The real estate practice figures are depicted in Figures S (frequency) and T (severity). The mistakes in this practice area varied considerably. Alleged drafting errors were common. A significant number of notices involved assertions by clients that the lawyers simply provided poor advice on a real estate investment. Fraud claims were particularly prevalent in this area as third parties sued lawyers hoping to void a purchase agreement or forestall a foreclosure. In many of these matters, the actual driving force appears to have been the drop in property values during the economic slowdown. For clients who suffered as a result, their lawyers and other professional advisors frequently become scapegoats. The severity chart for the real estate practice area is relatively benign, although it is worth noting that there are a number of open matters in this area and insurers have allocated significant reserves to some of them.

### Real Estate Claims

![Figure S](image1)

<table>
<thead>
<tr>
<th>Mistakes</th>
<th>Notices</th>
<th>Matters with Ground Up Paid</th>
<th>Ground Up Paid</th>
</tr>
</thead>
<tbody>
<tr>
<td>Conflicts of Interest</td>
<td>14</td>
<td>43 (8.35%)</td>
<td></td>
</tr>
<tr>
<td>Dishonest Clients</td>
<td>10</td>
<td>54 (10.49%)</td>
<td></td>
</tr>
<tr>
<td>Dishonest Lawyer</td>
<td>4</td>
<td>4 (0.78%)</td>
<td></td>
</tr>
<tr>
<td>Fraud and Misrepresentation</td>
<td>11</td>
<td>95 (18.45%)</td>
<td></td>
</tr>
<tr>
<td>Impaired Lawyer</td>
<td>0</td>
<td>0 (0.00%)</td>
<td></td>
</tr>
<tr>
<td>Malicious Prosecution/Abuse of Process</td>
<td>0</td>
<td>15 (2.91%)</td>
<td></td>
</tr>
</tbody>
</table>

![Figure T](image2)

- **Figure S**
  - $6.2M (4.07%)

- **Figure T**
  - $132.1M (87.21%)
The frequency of notices in securities practice, illustrated in Figure U, reflects a more equal split between mistakes, fraud, and dishonest client matters than in any other practice area. The most common mistake involved a substantive error in a registration statement. The remaining notices often included claims by investors or other third parties that the lawyer aided and abetted the client’s fraud. Distinguishing between whether the claim was prompted by misrepresentations made by the lawyer or the result of a dishonest client channeling false information through the lawyer was often difficult. Thus, when analyzing the severity chart, Figure V, it is reasonable to combine the fraud and dishonest client and dishonest lawyer categories. The combination of these categories results in over $41.5 million in paid loss representing over 38 percent of the total dollars paid. In a nutshell, securities lawyers appear to be especially vulnerable to liability arising out of the representation of unworthy clients.

Securities Claims

![Figure U and Figure V diagrams showing the frequency and severity of notices in securities practice.]

<table>
<thead>
<tr>
<th>Category</th>
<th>Notices</th>
<th>Matters with Ground Up Paid</th>
<th>Ground Up Paid</th>
</tr>
</thead>
<tbody>
<tr>
<td>Conflicts of Interest</td>
<td>1</td>
<td>3 (2.16%)</td>
<td></td>
</tr>
<tr>
<td>Dishonest Clients</td>
<td>9</td>
<td>32 (23.02%)</td>
<td>$5.7M (5.19%)</td>
</tr>
<tr>
<td>Dishonest Lawyer</td>
<td>6</td>
<td>6 (4.32%)</td>
<td>$2.5M (2.30%)</td>
</tr>
<tr>
<td>Fraud and Misrepresentation</td>
<td>14</td>
<td>41 (29.50%)</td>
<td>$12.6M (11.47%)</td>
</tr>
<tr>
<td>Impaired Lawyer</td>
<td>0</td>
<td>0 (0.00%)</td>
<td>$0.0M (0.00%)</td>
</tr>
<tr>
<td>Malicious Prosecution/Abuse of Process</td>
<td>0</td>
<td>0 (0.00%)</td>
<td>$0.0M (0.00%)</td>
</tr>
<tr>
<td>Mistakes</td>
<td>14</td>
<td>57 (41.01%)</td>
<td>$59.5M (54.21%)</td>
</tr>
</tbody>
</table>
Next are the statistics for the trust and estate practice area (*Figures W and X*). Once again, the majority of both notices and dollars paid were mistake-related. Allegations of substantive errors in the creation of estate plans came standard. Lawyers were also sued for alleged dishonesty in their capacities as trustees. Some claims by non-clients proved to be significant. Although conflict of interest issues in this practice area are often quite thorny, at least as of the end of 2013, our clients have seen few significant losses as a result of breach of fiduciary duty claims arising out of conflicts of interest. Of course, when it comes to tort liability, it is in the area of fiduciary duty that conflicts come to the fore.
V. Loss by Firm Size

We also studied the frequency of notifications and the severity of loss by type of conduct in combination with firm size. We categorized firms by the number of practicing lawyers: 1-100 lawyers, 101-500 lawyers, 501-1000 lawyers, 1001-1500 lawyers, and over 1501 lawyers. The figures below reflect for each category the frequency of notifications (left side pie chart) and severity of losses (right side pie chart) for each type of conduct causing the loss. What stands out from these graphs is that mistakes continue to be prevalent in terms of both frequency and total amount of dollars paid regardless of firm size.

Cause of Loss by Firm Size

<table>
<thead>
<tr>
<th>Notices</th>
<th>Ground Up Paid</th>
</tr>
</thead>
<tbody>
<tr>
<td>With 1 to 100 Attorneys</td>
<td>With 1,001 to 1,500 Attorneys</td>
</tr>
<tr>
<td>With 101 to 500 Attorneys</td>
<td>With Greater than 1,500 Attorneys</td>
</tr>
<tr>
<td>With 501 to 1,000 Attorneys</td>
<td></td>
</tr>
</tbody>
</table>

- Conflicts of Interest
- Dishonest Clients
- Dishonest Lawyer
- Fraud and Misrepresentation
- Impaired Lawyer
- Malicious Prosecution/Abuse of Process
- Mistakes
VI. Summary and Recommendations

After reviewing the data, the obvious next step is calculating what firms might learn from it in terms of evaluating professional risk and how best to manage it. The severity of the claims attributable to dishonest clients highlights firms’ continuing need to pay careful attention to client quality. Doug Richmond’s article, Dishonest or Unworthy Clients: Pink Flags, in the Summer 2010 issue of the Quality Assurance Review remains a good starting point for learning to recognize potentially unworthy clients. Firms are also well advised to evaluate lateral partner candidates’ clients for worthiness with the same rigor that potential new clients are scrutinized as part of their intake processes. Otherwise, an unworthy client that would never come into the firm through the front door may slip in through the side door. Several very fine law firms have suffered significant losses as a result of unworthy clients who were unknowingly brought to them by partners who were recruited laterally.

With respect to conflicts of interest, two things stand out. First, lawyers need to do a better job of explaining matters to clients or prospective clients with the thoroughness required to obtain informed consent to conflicts. These can be uncomfortable conversations for lawyers because of the understandable but exaggerated concern that they may in trying to obtain informed consent actually persuade clients or prospective clients not to engage them in the matter under discussion. But they are necessary conversations because experience teaches that uninformed consent to a conflict is valueless or something close to it. In any event, many related problems are avoidable if firms educate their lawyers on the importance of informed consent and, where necessary, coach them in obtaining it. Second, firms need to be very sensitive to conflicts in the formation of entities (e.g., partnerships, LLCs, and close corporations) and joint ventures. For example, when long-time entrepreneurial Client A comes to one of your partners with his intended partners B and C and asks you to form a partnership, who does—or should—the firm represent? The easy answer is A and, after the partnership is formed, perhaps the partnership and A or just one or the other; the harder part is ensuring that B and C do not become accidental clients of the firm. Furthermore, lawyers with some frequency knowingly represent multiple clients (e.g., A, B and C) in forming new businesses because they do not foresee any conflicts; all three entrepreneurs appear to be united in interest and the prospect of their interests diverging (or in some cases already being divergent at least to some extent) is lost in the enthusiasm for the new venture. Suffice it to say that conflicts of interest arising out of joint representations are often challenging and in this context they are a recurring source of claims and circumstances.

The frequency of fraud and misrepresentation claims surprised us, although we knew these theories regularly imperil lawyers as perhaps best evidenced by our publication of a related white paper in December 2014. Some of these claims are understandable as desperate efforts by third parties to avoid the privity requirement for legal malpractice liability. Some other percentage is to be expected as ancillary to the aiding and abetting claims that characterize suits by third-parties against law firms that have had the misfortune of representing unworthy clients. Many fraud and misrepresentation claims arising out of transactional practices involve omissions or non-disclosures of allegedly material information that a buyer or other counter-party later claims would have caused a deal to be differently priced or structured. As Harry Bryans pointed out in his 2008 article, Transactional Lawyers and Client Disclosures—A Modest Proposal, these claims often illustrate that a transactional lawyer best serves the client when she helps ensure that deal-related disclosures are construed on thorough due diligence (regardless of who is responsible for performing it), sufficient time is built into the process so that disclosures may be carefully prepared, and the draft disclosures are reviewed by all knowledgeable client representatives (regardless of whether, in the case of representations qualified as to the client’s “knowledge,” the knowledge of such persons is attributable to the client under the express terms of the agreement). As Harry further counseled, transactional lawyers should generally urge the client to make full disclosure whenever known facts are arguably responsive to a counter-party’s request because it is invariably in the client’s interest to do so. If a client resists disclosing a matter potentially material to a transaction when there is no rational basis to do so, the lawyers involved are well advised to consult internally. In such circumstances, a firm may have to seriously consider resigning from the representation.

In litigation, lawyers must recognize the difference between matters of opinion or puffery and material facts. For example, the existence of insurance coverage and the amount of insurance coverage are material facts. Lawyers who misrepresent the existence or amount of available coverage in negotiations or discovery thinking that they are gaining some sort of adversarial advantage for the
client are, in fact, digging themselves deep professional holes. The same is true with respect to misrepresentations of clients’ financial condition rather than their insurance coverage.

Now we come to the difficult subject of mistakes. To the extent that firms can implement software systems to help avoid administrative errors they should do so. Docketing programs and proofreading systems are vastly improved from their initial versions. But the inherent limitations of automated software programs remain. If the information entered is poor, or the output is not timely viewed by the right people, the system is of no real value. The lawyer responsible for a representation must ensure that proper information is entered into the system. More than one person in a firm should get notice when a system indicates an action and should be prepared to assume responsibility for seeing that there is an appropriate response. And, to the extent reasonably possible, any docketing or proofreading system should be integrated with the other firm systems such as Outlook or word-processing programs.

The best means of minimizing substantive errors is the development or preservation of a firm culture that promotes collaboration. Effective collaboration on projects requires each lawyer to take ownership of the representation. This means that junior lawyers must feel comfortable in the ability to ask questions and offer comments or observations when they believe something is askew. Partners must be willing to accept others’ inquiries and observations without feeling unfairly second-guessed. Partners should also be encouraged to check their judgment with fellow partners. Of course, there are forces conspiring against collaborative practice in many representations, most notably client pressure to avoid duplication and unnecessary time and expense through lean staffing and restrictions on lawyers’ activities. Ultimately, each firm must balance the risk of mistakes and the associated costs in not collaborating when it would be wise to do so, such as antagonizing a client, with the fact that some collaborative activity and time spent on supervision cannot be billed.

Finally, a firm should cultivate a culture that encourages lawyers who realize that they may have erred to promptly seek advice about how to correct the error, and to make full disclosure to the consulted attorney about what was done or not done, so that the advice may stand some chance of allowing the mistake to be rectified or at least mitigated. Far too often mistakes are aggravated by lawyers’ refusal to accept responsibility or unwillingness to seek help, and errant lawyers’ attempts to secretly correct their own errors can be downright incendiary. Lawyers working in teams too often remain silent when they should voice concerns out of the belief that someone else will spot or correct a possible error, or remain quiet out of the belief that they must not have truly spotted a possible problem because otherwise a colleague would have said or done something about the issue. In fact, the Homeland Security maxim of “if you see something, say something,” applies with equal force to lawyers working together on client matters. And the obligation to act should be incumbent upon both the lawyer who committed the error as well as anyone within the firm who notices the mistake.

What is not reflected in our claims data (or anyone else’s for that matter) are the uninsurable harms flowing from claims against lawyers. For example, a lawyer’s misconduct may have significant personal consequences, ranging from professional stigma to professional discipline to criminal prosecution. Lawyers’ misconduct may seriously impair client relationships and cost their firms business. And any claim against a firm necessarily forces lawyers within the firm to devote time and energy to its resolution – time that could be more productively spent on billable matters, business development, or other positive activities intended to advance the firm’s interests.

We hope the information presented here is both thought provoking and educational. We plan on updating our claims data annually and you can expect to see more reports like this one. Over the past six months we have presented this information at numerous regional programs and subsequently to many of our firms at their annual retreats or in-house CLE programs. Each presentation often takes on firm-specific characteristics. If you would like for us to present our claims information, or some aspect of it to your firm, please let us know.
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CHRIS E. MALING vs. FINNEGAN, HENDERSON, FARABOW, GARRETT & DUNNER, LLP, & others. [Note 1]

473 Mass. 336

September 8, 2015 - December 23, 2015

Court Below: Superior Court, Suffolk County

Present: Gants, C.J., Spina, Cordy, Botsford, Duffly, Lenk, & Hines, JJ.

Records And Briefs:

(1) SJC-11800 01 Appellant Maling Brief
(2) SJC-11800 02 Appellee Henerson Brief
(3) SJC-11800 03 Appellee Henderson Supplemental Brief
(4) SJC-11800 04 Appellant Maling Supplemental Brief
(5) SJC-11800 06 Amicus Knobbe Martens Olson Bear LLP Brief
(6) SJC-11800 07 Amicus Boston Patent Law Brief

Oral Arguments


In a civil action, in which the plaintiff alleged harm under various legal theories resulting from the failure of the defendant law firm and attorneys (who represented him in connection with the prosecution of patents for his inventions before the United States Patent and Trademark Office [USPTO]) to disclose an alleged conflict of interest in violation of Mass. R. Prof. C. 1.7 (i.e., the defendants' simultaneous representation of a commercial competitor of the plaintiff in a separate proceeding before the USPTO to seek a different patent for a similar device), a Superior Court judge did not err in granting the defendants' motion to dismiss, where the plaintiff failed to allege adequately that the defendants' representation of his competitor either was directly adverse to him [339-345] or materially limited their ability to obtain patents for his inventions. [345-348]

Discussion of the rules of professional conduct requiring law firms to implement procedures to identify and remedy actual and potential conflicts of interest. [348-349]

CIVIL ACTION commenced in the Superior Court Department on April 25, 2013.
A motion to dismiss was heard by Janet L. Sanders, J.

The Supreme Judicial Court on its own initiative transferred the case from the Appeals Court.

Thomas M. Bond for the plaintiff.

Erin K. Higgins (Christopher K. Sweeney with her) for the defendants.

Paul A. Stewart, of California, & Sara E. Hirshon, for Knobbe, Martens, Olson & Bear, LLP, & others, amici curiae, submitted a brief.


CORDY, J. In this case we consider whether an actionable conflict of interest arises under Mass. R. Prof. C. 1.7, as appearing in

471 Mass. 1335 (2015), when attorneys in different offices of the same law firm simultaneously represent business competitors in prosecuting patents on similar inventions, without informing them or obtaining their consent to the simultaneous representation. [Note 2]

The plaintiff, Chris E. Maling, engaged the defendant law firm Finnegan, Henderson, Farabow, Garrett & Dunner, LLP (Finnegan), including the three individual attorneys named in this suit, to represent him in connection with the prosecution of patents for Maling's inventions for a new screwless eyeglass. After obtaining his patents, Maling learned that Finnegan had been simultaneously representing another client that competed with Maling in the screwless eyeglass market. Maling then commenced this action, alleging harm under various legal theories resulting from Finnegan's failure to disclose the alleged conflict of interest. A judge in the Superior Court dismissed Maling's complaint for failure to state a claim under Mass. R. Civ. P. 12 (b) (6), 365 Mass. 754 (1974). Maling appealed, and we transferred the case to this court on our own motion. We conclude that the simultaneous representation by a law firm in the prosecution of patents for two clients competing in the same technology area for similar inventions is not a per se violation of Mass. R. Prof. C. 1.7. We further conclude that based on the facts alleged in his complaint, Maling failed to state a claim for relief. Accordingly, we affirm the judgment of dismissal.
1. Background. In 2003, Maling engaged Finnegan to perform legal services in connection with the filing and prosecution of patents for Maling's inventions for a new screwless eyeglass, including a screwless eyeglass hinge block design. Finnegan prepared patent applications for Maling's inventions after ordering prior art searches. Over the next several years, Finnegan successfully obtained four separate patents for Maling.

Attorneys in Finnegan's Boston office represented Maling from approximately April, 2003, to May, 2009. [Note 3] During this period of time, attorneys in Finnegan's Washington, D.C., office represented

Masunaga Optical Manufacturing Co., Ltd. (Masunaga), a Japanese corporation that also sought patents for its screwless eyeglass technology. Upon learning of Finnegan's representation of Masunaga, Maling brought suit, asserting claims stemming from the alleged conflict of interest that arose from Finnegan's simultaneous representation of both clients. [Note 4] We describe the allegations in Maling's complaint germane to our decision.

Maling alleges that he engaged Finnegan to file and prosecute a patent for [his] inventions for a new screw-less eyeglass, including without limitation, his invention of a screwless eyeglasses hinge block design, and that in September, 2003, Finnegan ordered prior art searches relating to Maling's inventions. [Note 5] Maling alleges that Finnegan belatedly commenced preparation of a patent application for his inventions in or about May, 2004, and that it inexplicably took [fourteen] months to do so. Maling also alleges that Finnegan filed patent applications for Masunaga more quickly than it did for him. At the same time, Maling acknowledges that Finnegan successfully obtained patents for his inventions. Maling further claims that he paid Finnegan in excess of $100,000 for its services, and that he invested millions of dollars to develop his product. He claims he would not have made this investment had Finnegan disclosed its conflict of interest and/or its work on the competing Masunaga patent. He further alleges that the Masunaga applications are very similar to the Maling applications, and that Finnegan knew it was performing work in the same patent space for both clients. Maling also alleges that he was harmed when Finnegan,
in 2008, declined to provide him with a legal opinion addressing similarities between the Masunaga patents and the Maling patents. Because Finnegan did not provide the legal opinion Maling claims, he was unable to obtain funding for his invention, and his product was otherwise unmarketable on account of its similarities to the Masunaga device; as a result, his patents and inventions have diminished in value. In sum, Maling contends, Finnegan's simultaneous representation of both clients, as well as its failure to disclose the alleged conflict, resulted in great harm and tremendous financial hardship for Maling.

Finnegan moved to dismiss Maling's complaint for failure to state a claim under Mass. R. Civ. P. 12 (b) (6). The motion was granted in October, 2013, and Maling appealed. We then transferred the case to this court on our own motion.


Maling's complaint sets forth four bases for relief: (1) breach of fiduciary duty; (2) legal malpractice; (3) unfair or deceptive practices in violation of G. L. c. 93A; and (4) inequitable conduct before the United States Patent and Trademark Office (USPTO). Because each count hinges on the existence of an undisclosed conflict of interest arising from Finnegan's representation of both Maling and Masunaga, we focus our inquiry on whether, under the facts alleged, an actionable conflict arose in violation of the Massachusetts Rules of Professional Conduct.

Rule 1.7 of the Massachusetts Rules of Professional Conduct, which applies to conflicts of interests between current clients, governs the issues in this case. [Note 6] By its terms, rule 1.7, with limited exceptions, provides that a lawyer shall not represent a client if the representation is directly adverse to another client, Mass. R. Prof. C. 1.7 (a) (1), or where there is a significant risk that the
representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer,\[Mass. R. Prof. C. 1.7 (a) (2). The purpose of rule 1.7 is twofold. It serves as a \[prophylactic [measure] to protect confidences that a client may have shared with his or her attorney \[and] safeguard[s] loyalty as a feature of the lawyer-client relationship.\[SWS Fin. Fund A v. Salomon Bros. Inc., 790 F. Supp. 1392, 1401 (N.D. Ill. 1992). [Note 7]

In the practice of patent law, the simultaneous representation of clients competing for patents in the same technology area is

sometimes referred to as a \[subject matter conflict.\[See, e.g., Dolak, Recognizing and Resolving Conflicts of Interest in Intellectual Property Matters, 42 IDEA 453, 463 (2002); Hricik, Trouble Waiting to Happen: Malpractice and Ethical Issues in Patent Prosecution, 31 AIPLA Q.J. 385, 412 (2003) (Hricik). Subject matter conflicts do not fit neatly into the traditional conflict analysis. Maling advocates for a broad interpretation of rule 1.7 that would render all subject matter conflicts actionable, per se violations. We disagree. Rather, we conclude that although subject matter conflicts in patent prosecutions often may present a number of potential legal, ethical, and practical problems for lawyers and their clients, they do not, standing alone, constitute an actionable conflict of interest that violates rule 1.7.

a. Adverse representation under rule 1.7 (a) (1). Representation is \[directly adverse\[ in violation of rule 1.7 (a) (1) when a lawyer \[act[s] as an advocate in one matter against a person the lawyer represents in some other matter, even when the matters are wholly unrelated.\[Mass. R. Prof. C. 1.7 comment 6. In other words, \[a\[ law firm that represents client A in the defense of an action may not, at the same time, be counsel for a plaintiff in an action brought against client A, at least without the consent of both clients.\[McCourt Co. v. FPC Props., Inc., 386 Mass. 145 , 145 (1982).

In the instant case, Maling and Masunaga were not adversaries in the traditional sense, as they did not appear on opposite sides of litigation. Rather, they each
appeared before the USPTO in separate proceedings to seek patents for their respective screwless eyeglass devices.

Maling contends, however, that he and Masunaga were directly adverse within the meaning of rule 1.7 (a) (1) because they were competing in the same patent space. We disagree that the meaning of directly adverse stretches so far. The rules of professional conduct make clear that simultaneous representation in unrelated matters of clients whose interests are only economically adverse, such as representation of competing economic enterprises in unrelated litigation, does not ordinarily constitute a conflict of interest and thus may not require consent of the respective clients.


Curtis v. Radio Representatives, Inc., 696 F. Supp. 729 (D.D.C. 1988), a case involving broadcast licenses, offers a useful example. In Curtis, the United States District Court for the District of Columbia found that no actionable conflict of interest existed where a law firm simultaneously represented clients in the preparation and prosecution of applications for radio broadcast licenses from the Federal Communications Commission (FCC). Id. at 731-32, 737. [Note 8] The court reasoned that the fact that an attorney is simultaneously representing two companies that are competitors in the same industry does not itself establish an actionable breach of an attorney's fiduciary duty. Id. at 736, quoting D.J. Horan & G.W. Spellmire, Jr., Attorney Malpractice: Prevention and Defense 17-1 (1987). It went on to explain that a conflict of interest could develop between clients seeking broadcast licenses under circumstances where objectionable electrical interference existed between two stations. Curtis, supra. However, because the defendant failed to assert such interference, or even the potential for such interference, the
court could not conclude that a conflict of interest existed in violation of the rules of professional conduct adopted by the District of Columbia. Id. at 736-37.

The analysis undertaken by the court in Curtis is instructive in our evaluation of Maling's claims. Finnegans representation of Maling and Masunaga is analogous to that undertaken by the law firm in Curtis. Finnegans represented two clients competing in the screwless eyeglass device market in proceedings before the USPTO. As Maling acknowledges, Finnegans was able successfully to obtain patents from the USPTO for both his device and Masunagas, in the same way that the law firm in Curtis was able to obtain radio broadcast licenses for each of its clients from the FCC. Maling and Masunaga were not competing for the same patent, but rather different patents for similar devices.

Like the court in Curtis, we acknowledge that an actionable conflict of interest could arise under different factual circumstances. For example, where claims in two patent applications filed prior to March 16, 2013, are identical or obvious variants of

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each other, the USPTO can institute an interference proceeding to determine which inventor would be awarded the claims contained in the patent applications. 35 U.S.C. § 135(a) (2002). [Note 9], [Note 10] If the USPTO had called an interference proceeding to resolve conflicting claims in the Maling and Masunaga patent applications, or if Finnegans, acting as a reasonable patent attorney, believed such a proceeding was likely, the legal rights of the parties would have been in conflict, as only one inventor can prevail in an interference proceeding. In such a case, rule 1.7 would have obliged Finnegans to disclose the conflict and obtain consent from both clients or withdraw from representation. See Mass. R. Prof. C. 1.7 comments 3, 4.

Maling's conclusory allegations as to the high degree of similarity between his device and the Masunaga device are contradicted by his acknowledgment elsewhere in the complaint that

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patents issued for both his applications and the Masunaga applications. Although Maling alleges that the Masunaga and Maling applications are similar in many important respects, he does not allege that the claims are identical or obvious variants of each other such that the claims in one application would necessarily preclude claims contained in the other. Additionally, we appreciate that the claims comprising a patent application may be sufficiently distinct so as to permit the issuance of multiple patents for similar inventions, or components of an invention, as was the case here. Accordingly, Maling's allegations do not permit any inference as to whether the similarities between the inventions at the time Finnegan was retained to prepare and prosecute Maling's patent applications were of such a degree that Finnegan should have reasonably foreseen the potential for an interference proceeding. [Note 11] Maling's conclusory statement that the inventions were very similar is precisely the type of legal conclusion that we do not credit. See Iannacchino, 451 Mass. at 636. Moreover, Maling makes no allegations that an interference proceeding was instituted, nor has he alleged facts supporting the inference that Finnegan took positions adverse to Maling and favorable to Masunaga in the prosecution of their respective patents.

We also recognize that subject matter conflicts can give rise to conflicts of interest under rule 1.7 (a) (1) in nonlitigation contexts. Comment 7 to rule 1.7 explains that directly adverse conflicts may also arise in the course of transactional matters. For example, a lawyer would be precluded from advising a client as to his rights under a contract with another client of the lawyer. Such conflict involves the legal rights and duties of the two clients vis-à-vis one another. ABA Op. 05-434, supra at 140.

Here, such a conflict likely arose in 2008 when Maling sought a legal opinion from Finnegan regarding the likelihood that he might be exposed to claims by Masunaga for patent infringement. Finnegan declined to provide the opinion, and Maling alleges that he lost financing as a result. Providing the opinion arguably would have rendered the interests of Maling and Masunaga directly adverse within the meaning of rule 1.7 (a) (1), and either declining representation or disclosing the conflict and
obtaining consent would have been the proper course of action. [Note 12] But there is no allegation that Finnegan had agreed to provide such opinions in its engagement to prosecute Maling’s patents. Without such a claim, we cannot conclude that a conflict based on direct adversity has been adequately alleged.

b. Material limitation under rule 1.7 (a) (2). We turn next to the question whether Finnegan's representation of Masunaga materially limited its representation of Maling in contravention of rule 1.7 (a) (2), which prohibits representation where there is no direct adverseness [but] there is a significant risk that a lawyer's ability to consider, recommend or carry out an appropriate course of action for the client will be materially limited as a result of the lawyer's other responsibilities or interests. Matter of Driscoll, 447 Mass. 678, 686 (2006) (quoting comment 4 to previous version of Mass. R. Prof. C. 1.7 [b], which contained language now in rule 1.7 [a] [2]).

In his complaint, Maling alleges in conclusory terms that Finnegan was unable to protect both his interests and Masunaga's and ultimately chose to protect Masunaga at his expense in the patent prosecution process. In Maling’s view, Finnegan pulled its punches and got more for Masunaga than for Maling before the USPTO. He has failed, however, to allege sufficient facts to support such a proposition.

The case of Sentinel Prods. Corp. vs. Platt, U.S. Dist. Ct., No. 98-11143-GAO (D. Mass. July 22, 2002) (Sentinel), illustrates how a subject matter conflict resulting from the prosecution of patents for competing clients could give rise to a conflict of interest under rule 1.7 (a) (2). In the Sentinel case, a law firm prosecuted patents for two clients, a company (Sentinel), and one of Sentinel's former employees. Id. at 1. Sentinel brought suit, claiming that because of the simultaneous representation, its patent applications were denied, delayed, or otherwise impeded and that it suffered economic losses as a result. Id. at 5. On a
motion for summary judgment, the court concluded that the law firm filed applications with the USPTO for Sentinel, and then two weeks later for the former employee. Id. at 1-2. The firm's attorneys testified that they thought the applications overlapped and that they were unable to discern a patentable difference between the applications. Id. at 5. A patent for the employee's application was issued first, and Sentinel's application was rejected after the USPTO found it conflicted with claims contained in the employee's patents. Id. at 2-3. The firm subsequently narrowed the claims in Sentinel's application to avoid conflict with the former employee's application, and the USPTO issued Sentinel patents containing the narrower claims. Id. at 3, 6-7.

The so-called claim shaving, see Hricik, supra at 415, that occurred in Sentinel clearly implicates rule 1.7(a)(2). Altering the claims in one client's application because of information contained in a different client's application at least creates a question of fact whether courses of action that reasonably should be pursued on behalf of the client were foreclosed. Mass. R. Prof. C. 1.7 comment 8.

Unlike the facts in Sentinel, Maling's complaint provides little more than speculation that Finnegan's judgment was impaired or that he obtained a less robust patent than if he had been represented by other, conflict-free counsel. Maling does not allege that the claims contained in his applications were altered or narrowed in light of the Masunaga applications, as the plaintiffs demonstrated in Sentinel, or, importantly, that his client confidences were disclosed or used in any way to Masunaga's advantage. [Note 13] Nor does he allege that Finnegan delayed filing his patent application to ensure the success of Masunaga's application over his own. Ultimately, Maling's bare assertions that Masunaga was given preferential treatment and was enrich[ed] to his detriment as a consequence do not support an inference that Finnegan was materially limited in its ability to obtain patents for Maling's inventions.

Finnegan's subsequent inability or unwillingness to provide a legal opinion regarding the similarities between the Maling and

Masunaga inventions also raises a question whether the simultaneous representation [a] course[ ] of action that should have been
Pursued on Maling's behalf. Mass. R. Prof. C. 1.7 comment 8. As previously discussed, rendering such an opinion would likely have created a direct conflict between Maling and Masunaga in violation of rule 1.7 (a) (1). To the extent that such a conflict was foreseeable, because, as Maling alleges, the Masunaga and Maling inventions were so similar, it is possible that Finnegan should have declined to represent Maling from the outset of his case so as to also avoid a violation of rule 1.7(a)(2). This, however, depends in large measure on the nature of Finnegan's engagement by Maling in 2003.

Before engaging a client, a lawyer must determine whether the potential for conflict counsels against undertaking representation. Comment 8 to rule 1.7 elaborates:

- The mere possibility of subsequent harm does not itself require disclosure and consent. The critical questions are the likelihood that a difference in interests will eventuate and, if it does, whether it will materially interfere with the lawyer's independent professional judgment in considering alternatives or foreclose courses of action that reasonably should be pursued on behalf of the client.

Maling's complaint does not contain any allegations as to the services or scope of representation agreed upon by Maling and Finnegan other than that Finnegan agreed to file and prosecute a patent for Maling's inventions. Nor is it adequately alleged that Finnegan should have reasonably anticipated that Maling would need a legal opinion that would create a conflict of interest. There are simply too few facts from which to infer that Finnegan reasonably should have foreseen the potential conflict in the first place. See, e.g., Vaxiion Therapeutics, Inc. v. Foley & Lardner LLP, 593 F. Supp. 2d 1153, 1173 (S.D. Cal. 2008) (deciding that expert testimony created question of fact as to likelihood that conflict of interest would develop from firm's simultaneous representation of competitor clients in patent prosecution).

Based on these inadequacies, we agree with the motion judge that the complaint does not sufficiently allege that Finnegan violated its duties under rule 1.7 (a) (2) by undertaking representation of both Maling and Masunaga.

Because Maling's claims hinge on the existence of a conflict of interest, and because we conclude there was none adequately alleged in this case, he fails to state a claim on each of the counts.
in his complaint. [Note 14], [Note 15]

c. Identifying conflicts of interest. This case also raises important considerations under Mass. R. Prof. C. 1.10, as appearing in 471 Mass. 1363 (2015), which prohibits lawyers associated in a firm from knowingly represent[ing] a client when any one of them practicing alone would be prohibited from doing so by Rule[ ]

1.7. □ Mass. R. Prof. C. 1.10 (a). [Note 16] To ensure compliance with both rules 1.7 and 1.10, firms must implement procedures to identify and remedy actual and potential conflicts of interest. See Mass. R. Prof. C. 5.1 comment 2, as appearing in 471 Mass. 1445 (2015) (requiring firms to make reasonable efforts to establish internal policies designed to detect and resolve conflicts of interest).

What constitutes an adequate conflict check is a complex question. As a member of this court observed, □[a]gainst a backdrop of increasing law firm reorganizations and mergers, lateral transfers, and the rise of large-scale firms that transcend State and national borders, the issue of dual representation is one of multifaceted overtones and novel complexity. □ Coke v. Equity Residential Props. Trust, 440 Mass. 511, 518 (2003) (Cowin, J., concurring). Nothing we say here today, however, should be construed to absolve law firms from the obligation to implement robust processes that will detect potential conflicts.

This court has not defined a minimum protocol for carrying out a conflict check in the area of patent practice, or in any other area of law. However, no matter how complex such a protocol might be, law firms run significant risks, financial and reputational, if they do not avail themselves of a robust conflict system adequate to the nature of their practice. Although Maling's complaint does not plead an actionable violation of rule 1.7 sufficiently, the misuse of client confidences and the preferential treatment of the interests of one client, to the detriment of nearly identical interests of another, are serious matters that cannot be reconciled with the ethical obligations of our profession.

3. Conclusion. As noted throughout this opinion, there are various factual scenarios in the context of patent practice in which a subject matter conflict may give rise to an actionable violation of rule 1.7. On the facts alleged in Maling's complaint,
however, we find that no actionable conflict of interest existed. The dismissal of the complaint is affirmed.

So ordered.

FOOTNOTES


[Note 2] We acknowledge the amicus briefs submitted by the Boston Patent Law Association and by Knobbe, Martens, Olson & Bear, LLP; Honigman Miller Schwartz and Cohn LLP; Nixon & Vanderhye P.C.; Lewis Roca Rothgerber LLP; Schiff Hardin LLP; Steptoe & Johnson LLP; Snell & Wilmer LLP; Barnes & Thornburg LLP; Pillsbury Winthrop Shaw Pittman LLP; Verrill Dana LLP; and Morrison & Foerster LLP.

[Note 3] Finnegan, Henderson, Farabow, Garrett & Dunner, LLP (Finnegan), withdrew its representation of Chris E. Maling before the United States Patent and Trademark Office (USPTO) on May 20, 2009; however, it is not clear from the record when the firm and Maling terminated their relationship.

[Note 4] The original complaint was filed by Maling and his company, The Formula, LLC, in the United States District Court for the District of Massachusetts in April, 2012. It was dismissed following the United States Supreme Court's decision in Gunn v. Minton, 133 S. Ct. 1059, 1068 (2013), which held that legal malpractice claims arising from representation in patent proceedings are not within the exclusive subject matter jurisdiction of the Federal courts. Maling refiled his case in the business litigation section of the Superior Court in April, 2013. After judgment entered dismissing the complaint on October 29, 2013, notices of appeal were filed by both plaintiffs, but no filing fee was paid in the Appeals Court on behalf of The Formula, LLC. Therefore, Maling is the sole appellant.


[Note 6] Since Maling's complaint was filed in 2012, the Massachusetts Rules of Professional Conduct have been revised and updated. Because the substance of rule 1.7 remains unchanged, we analyze Maling's claims against the most recent version of the rules, published in 2015. See Mass. R. Prof. C. 1.7, as appearing in 471 Mass. 1335 (2015).


At the time this action was brought, concurrent conflicts of interest were governed by 37 C.F.R. § 10.66 (2012) (entitled, § Refusing to accept or continue employment if the interests of another client may impair the independent professional judgment of the practitioner)), which provided:

• (a) A practitioner shall decline proffered employment if the exercise of the practitioner's independent professional judgment in behalf of a client will be or is likely to be adversely affected by the acceptance of the proffered employment, or if it would be likely to involve the practitioner in representing differing interests, except to the extent permitted under paragraph (c) of this section.

• (b) A practitioner shall not continue multiple employment if the exercise of the practitioner's independent professional judgment in behalf of a client will be or is likely to be adversely affected by the practitioner's representation of another client, or if it would be likely to involve the practitioner in representing differing interests, except to the extent permitted under paragraph (c) of this section.

• (c) In the situations covered by paragraphs (a) and (b) of this section a practitioner may represent multiple clients if it is obvious that the practitioner can adequately represent the interest of each and if each consents to the representation after full disclosure of the possible effect of such representation on the exercise of the practitioner's independent professional judgment on behalf of each.

• (d) If a practitioner is required to decline employment or to withdraw from employment under a Disciplinary Rule, no partner, or associate, or any other practitioner affiliated with the practitioner or the practitioner's firm, may accept or continue such employment unless otherwise ordered by the Director or Commissioner.

[Note 8] There are very few appellate court decisions that deal with the issues raised in this case. The most instructive cases are those decided by judges in the Federal District Courts. See generally Gunn v. Minton, 133 S. Ct. 1059, discussed in note 4, supra.

application derived from those in the true inventor's patent application. 35 U.S.C. § 135.

Because the Maling and Masunaga Optical Manufacturing Co., Ltd. (Masunaga), patents were filed prior to the effective date of the relevant provisions of 35 U.S.C. § 135, the applications would have been subject to an interference proceeding had a question arisen as to whether the patent applications contained conflicting claims. 

[Note 10] Interference proceedings are meant to assist the director of the USPTO in determining priority, that is, which party first invented the commonly claimed invention. See MPEP, supra at § 2301 (rev. Oct. 2015) at http://www.uspto.gov/web/offices/pac/mep/mep-2300.pdf [http://perma.cc/T2D9-G52D ]. This first-to-invent system was supplanted by the enactment of the America Invents Act, which updated various provisions of the patent code, and which gives priority to the first party to file an application. See 35 U.S.C. § 135 (2012). Prior to the American Invents Act, 35 U.S.C. § 135(a) (2006) provided, in relevant part:

Whenever an application is made for a patent which, in the opinion of the Director [of the USPTO], would interfere with any pending application, or with any unexpired patent, an interference may be declared and the Director shall give notice of such declaration to the applicants, or applicant and patentee, as the case may be. The Board of Patent Appeals and Interferences shall determine questions of priority of the inventions and may determine questions of patentability.

[Note 11] Maling's allegation that he and Masunaga competed in the same patent space, without more, fails to demonstrate entitlement to relief. Maling cites no authority, and we have found none, that gives this term special meaning in the context of patent jurisprudence.

[Note 12] The record does not reflect Finnegan's rationale for declining to provide the opinion.

[Note 13] Contrast Tethys Bioscience, Inc. vs. Mintz, Levin, Cohn, Ferris, Glovsky & Popeo, P.C., No. C09-5115 CW, slip op. at 4, 10 (N.D. Cal. June 4, 2010) (allegations that defendant law firm's use of nearly identical language in patent applications for plaintiff and plaintiff's competitor were sufficient to plead actionable conflict of interest because court could draw inference of the improper disclosure of client information).

[Note 14] At oral argument, Maling's counsel implied that Finnegan's failure to discover and disclose Masunaga's patents in the course of its prior art searches constituted malpractice or negligence. Because Maling's complaint contains no allegations to this effect, we do not decide the question whether an attorney has an ongoing obligation to discover prior art.

[Note 15] Maling also alleges that Finnegan failed to disclose information to the USPTO such that it engaged in inequitable conduct. Inequitable conduct in the USPTO occurs when a party withholds information material to patentability, or material
misinformation is provided to the USPTO, with the intent to deceive or mislead the patent examiner into granting the patent. Outside the Box Innovations, LLC v. Travel Caddy, Inc., 695 F.3d 1285, 1290 (Fed. Cir. 2012)

Even if this claim arises from conduct unrelated to the alleged conflict of interest, Maling nonetheless fails to state a claim. First, it is unsettled whether the inequitable conduct doctrine is merely a defense or whether it provides an independent cause of action against counsel. See ShieldMark, Inc. vs. Creative Safety Supply, LLC, No. 1:12-CV-221, slip op. at 12-13 (N.D. Ohio Oct. 9, 2012), report and recommendation adopted, No. 1:12-CV-221 (N.D. Ohio Jan. 9, 2013) (describing the dearth of case law on the issue). We need not decide the issue, however, as Maling failed to plead sufficient facts to state a claim for inequitable conduct. To successfully prove inequitable conduct, the accused infringer must provide evidence that the applicant (1) made an affirmative misrepresentation of material fact, failed to disclose material information, or submitted false material information, and (2) did so with intent to deceive the [USPTO]. Cancer Research Tech. Ltd. v. Barr Labs., Inc., 625 F.3d 724, 732 (Fed. Cir. 2010), cert. denied, 132 S. Ct. 499 (2011). At a minimum, Maling makes no allegations as to Finnegan's intent to deceive the USPTO, and therefore fails to state a claim of inequitable conduct.

[Note 16] The lawyers working on Masunaga's patent prosecution worked out of a different office than the lawyers working on the prosecution of Maling's patents. Although the risks of inadvertent confidential client information disclosure or misuse may be reduced in such circumstances, this makes little difference from a disciplinary rules standpoint as conflicts are generally imputed to all members of the firm regardless of their geographical location or work assignments.
NOT FOR PUBLICATION

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

NASDAQ, INC, et al.,
Plaintiffs,

v.

MIAMI INTERNATIONAL HOLDINGS,
INC., et al.,
Defendants.

Civil Action No. 17-6664-BRM-DEA

OPINION

MARTINOTTI, DISTRICT JUDGE

Before this Court is an appeal by Fish & Richardson, PC ("Fish") (ECF No. 107) of
Magistrate Judge Douglas E. Arpert's September 6, 2018 Memorandum and Order (ECF No. 105)
granting Nasdaq, Inc. ("Nasdaq"), Nasdaq ISE, LLC ("ISE"), and Ften, Inc.'s ("FTEN")
(collectively, "Plaintiffs") Motion to Disqualify Fish as Miami International Holdings, Inc, Miami
International Securities Exchange, LLC, MIAX Peral, LLC, and Miami International
Technologies, LLC's (collectively, "MIAX") counsel. (ECF No. 54.) Plaintiffs opposed the
appeal. (ECF No. 109.) Having reviewed the parties' submissions filed in connection with the
appeal and having declined to hold oral argument pursuant to Federal Rule of Civil Procedure
78(b), for the reasons set forth below and for good cause having been shown, Fish's Appeal (ECF
No. 107) is DENIED and Judge Arpert's September 6, 2018 Memorandum and Order (ECF No.
105) is AFFIRMED.
I. BACKGROUND

Fish does not dispute Judge Arpert’s recitation of facts to Nasdaq’s Motion to Disqualify. See (ECF No. 107-1 at 9 (“[T]he core facts on Plaintiff’s Motion to Disqualify Fish were not in dispute. Rather, the dispute was the legal conclusions to be drawn based on those facts, i.e., whether disqualification under RPCs 1.9 and 1.10 was appropriate.”)). Indeed, Judge Arpert noted “[t]he relevant facts [were] generally not contested.” (ECF No. 105 at 6.) As such, the Court incorporates Judge Arpert’s comprehensive recitation of the background, in relevant part:

Plaintiffs [Nasdaq], [ISE] and [FTEN] bring this action alleging patent infringement and misappropriation of trade secrets against four entities collectively referred to by the parties as MIAX. The Complaint contains ten counts. Counts I and II of the Complaint allege that MIAX has infringed two separate patents owned by ISE. Counts III, IV, V and VI allege that MIAX has infringed four separate patents owned by Nasdaq. Count VII alleges that MIAX infringed a patent owned by FTEN. The final three counts, Counts VIII through X, allege that MIAX misappropriated certain of Nasdaq’s trade secrets.

The seven patents-in-suit relate generally to electronic trading technology. More specifically, ISE’s patents are directed to how an automated exchange allocates trades between traders. FTEN’s patent relates to automatically cancelling orders by monitoring market data from a plurality of exchanges. Nasdaq’s patents are directed to displaying quotes in a particular way, monitoring whether a trader’s trading terminal is online, and assigning orders to designated securities processors. ECF No. 69-6 at ¶ 22. All of the patents-in-suit are alleged to be infringed by the same accused products and services relating to electronic trading platforms.

MIAX is represented in this action by [Fish] and Reed Smith LLP (“Reed Smith”). Plaintiff Nasdaq is a former client of Fish. Fish represented Nasdaq with respect to intellectual property matters from 1998 until 2011, during which time Fish prosecuted many patents on behalf of Nasdaq, including the four patents that Nasdaq is asserting in the present case (the “Nasdaq Patents”). The Nasdaq Patents were filed between 1998 and 2002, and the patents issued between 2009 and 2011. ECF No. 54-1 at 3.

In 2011, Fish’s representation of Nasdaq was terminated. ECF No. 69-1 at ¶ 6. Fish transferred Nasdaq’s patent portfolio to another law firm, Nixon & Vanderhye, P.C. Id. Fish did not retain
any copies of the physical files from Nasdaq after the representation was terminated. *Id.* at ¶ 8. Most of the Fish attorneys that worked on prosecuting the Nasdaq Patents still practice with Fish today, and all reside in the firm's Boston office. *Id.* ¶ 5.

When approached about representing MIAx in the instant case, Fish apparently recognized that there was a conflict -- it could not be adverse to its former client, Nasdaq, in any matter substantially related to Fish's prior representation. As such, Fish and MIAx entered into a "limited-scope engagement agreement" with respect to the present action. *Id.* ¶ 9. Under this agreement, MIAx would be required to retain an additional law firm as "conflicts counsel" to handle all matters where Fish would have a conflict with Nasdaq. *Id.* MIAx retained Reed Smith as conflicts counsel. Consequently, according to Fish, Fish is lead counsel for aspects of the case pertaining to ISE, FTEN and the trade secret claims, but Fish will have no input into the defense of the four Nasdaq Patents. ECF No. 69 at 7. Reed Smith, on the other hand, is lead counsel for issues relating to the Nasdaq Patents. *Id.*

When challenged by Nasdaq regarding its appearance in this matter, Fish asserted that its appearance on behalf of MIAx presents no conflict because its representation excludes the Counts in the Complaint involving the Nasdaq Patents. ECF No. 54-1 at 4. Fish advised Plaintiffs that in order to meet its ethical obligations to Nasdaq, Fish screened every lawyer who previously represented Nasdaq and has "walled off" its entire Boston office from participation in this case (the Fish attorneys working on this case are located in the firm's New York, Texas, California and Washington D.C. offices). *Id.*

(ECF No. 105 at 1-3.)

Nevertheless, on March 2, 2018, Plaintiffs moved to disqualify Fish, arguing Fish's efforts to avoid a conflict were "woefully deficient." (ECF No. 54 at 4.) In their Motion to Disqualify, they argued Fish's participation in this matter will prejudice Nasdaq because "(1) Fish prosecuted four of the seven patents that are asserted of this action; (2) the remaining three patents involve the same field of technology for which Fish provided IP counseling to and prosecuted patents for Nasdaq; and (3) the trade secret claims similarly involve the same technological field and may implicate confidential information that Nasdaq provided to Fish during its previous relationship." (ECF No. 105 at 3.) On September 6, 2018, Judge Arpert granted Plaintiffs' Motion to Disqualify
Fish, finding in part, “[a]s opposing parties, and given the fact that the other Plaintiffs, IFE and FTEn, are wholly-owned subsidiaries of Nasdaq, there can be no dispute that Nasdaq and MIAIX have adverse interest with respect to this litigation.” (ECF No. 105 at 7.) Now, Fish appeals Judge Arpert’s decision. (ECF No. 107.)

II. LEGAL STANDARD

With respect to a district judge’s review of a magistrate judge’s decision, Federal Rule of Civil Procedure 72(a) states: “The district judge . . . must consider timely objections and modify or set aside any part of the order that is clearly erroneous or is contrary to law.” Id. Similarly, this Court’s Local Rules provide that “[a]ny party may appeal from a Magistrate Judge’s determination of a non-dispositive matter within 14 days” and the District Court “shall consider the appeal and/or cross-appeal and set aside any portion of the Magistrate Judge’s order found to be clearly erroneous or contrary to law.” L.Civ.R. 72.1(c)(1)(A).

A district judge may reverse a magistrate judge’s order if the order is shown to be “clearly erroneous or contrary to law” on the record before the magistrate judge. 28 U.S.C. 636(b)(1)(A) (“A judge of the court may reconsider any pretrial matter [properly referred to the magistrate judge] where it has been shown that the magistrate judge’s order is clearly erroneous or contrary to law.”); Fed. R. Civ. P. 72(a); L.Civ.R. 72.1(c)(1)(A); Haines v. Ligget Grp., Inc., 975 F.2d 81, 93 (3d Cir. 1992) (describing the district court as having a “clearly erroneous review function,” permitted only to review the record that was before the magistrate judge). The burden of showing that a ruling is “clearly erroneous or contrary to law rests with the party filing the appeal.” Marks v. Struble, 347 F. Supp. 2d 136, 149 (D.N.J. 2004). A district judge may find a magistrate judge’s decision “clearly erroneous” when it is “left with the definite and firm conviction that a mistake has been committed.” Dome Petroleum Ltd. v. Employers Mut. Liab. Ins. Co., 131 F.R.D. 63, 65

III. DECISION

A. Limiting the Scope of Representation

Fish argues the threshold legal issue to be determined prior to deciding whether Fish is averse to a “former client” in a “substantially related” matter under RPC 1.9(a) is whether Fish was permitted to limit the scope of its representation of IMAX. (ECF No. 107-1 at 9-10.) Plaintiffs argue Fish’s limited scope representation does not work to immunize the conflict of interest at hand. (ECF No. 109 at 7-8.)

Rule of Professional Conduct 1.2(c) states, “A lawyer may limit the scope of the representation if the limitation is reasonable under the circumstances and the client gives informed consent.” The Restatement (Third) of the Law of Lawyering, Section 121, comment c(iii), notes “[s]ome conflicts can be eliminated by an agreement limiting the scope of the lawyer’s representation if the limitation can be given effect without rendering the remaining representations objectively inadequate.” Illustration 4 of the Restatement is instructive:

Lawyer has been retained by Client to represent Client in general business matters. Client has a distribution contract with Manufacturer, and there is a chance that disputes could arise under the contract. Lawyer represents Manufacturer in local real estate matters completely unrelated to Client’s business. An agreement between Lawyer and Client that the scope of Lawyer’s
representation of Client will not extend to dealing with disputes with Manufacturer would eliminate the conflict posed by the chance otherwise of representing Client in matters adverse to Manufacturer (see § 128). Such an agreement would not require the consent of Manufacturer.

Id. § 121 ill. 4. To eliminate the conflict, the Lawyer was required to craft a representation agreement that avoided all disputes involving the Client and Manufacturer to avoid the chance of the Lawyer having to represent the Client in matters adverse to the Manufacturer. Id.

Although a lawyer may limit the scope of its representation, Judge Arpert was correct in finding that the limitation here was unreasonable under the circumstances of this matter. (ECF No. 105 at 7.) It is undisputed that Fish is representing MIAIX in this case and that Nasdaq is an opposing party to the matter. An attorney-client relationship existed between Fish and Nasdaq for over a decade, which means Fish has familiarity with Nasdaq’s strategic approaches to managing its technology and inventions. In fact, Fish prosecuted Nasdaq Patents asserted in this case, and, as such, there is no doubt that during the course of that relationship Fish obtained confidential information that is likely to bear upon the current dispute between Nasdaq and MIAIX whether as to the patents or misappropriate on trade secrets claims. See Essex Chem. Corp. v. Hartford Acc. & Indem. Co., 993 F. Supp. 241, 246 (D.N.J. 1998) (finding that, where the matters are substantially related, “the court will presume that the attorney has acquired confidential information from the former client”); see also Audio MPEG, Inc. v. Dell, Inc., 219 F. Supp. 3d 563, 569 (E.D. Va. 2016) (“It is well settled that once an attorney-client relationship has been established, an irrebuttable presumption arises that confidential information was conveyed to the attorney in the prior matter.”).

As opposing parties and given that IFE and FTEN are wholly-owned subsidiaries of Nasdaq, Nasdaq and MIAIX clearly have adverse interests in this litigation. Despite MIAIX’s
attempt to parcel individual claims in this case for conflict purposes, this is one lawsuit, all claims are contained in a single Complaint, and IMAX elected to file a single motion to dismiss in response to the Complaint. The single brief on the motion to dismiss filed by Fish and Reed Smith attacked all the patents in the case on practically identical grounds, including those that Fish had previously prosecuted and won for Nasdaq. In addition, the brief contained a joint introduction, fact section, and joint exhibits. This demonstrates a collaborative effort in representing MIAX against Nasdaq, irrespective of their limited scope representation agreement. As such, Judge Arpert’s conclusion that Fish and MIAX’s limited-scope agreement was not appropriate under the circumstances is not “clearly erroneous or contrary to law.” L.Civ.R. 72.1(c)(1)(A). Unlike the Illustration 4 in the Restatement, Fish is representing IMAX in a matter adverse to Nasdaq and the limited scope agreement did not avoid all disputes between Nasdaq and IMAX. Accordingly, Fish’s Appeal is DENIED for this reason alone. Nevertheless, the Court will briefly address Fish’s RPC 1.9 and 1.10 arguments.

B. RPC 1.9

Fish argues Plaintiffs did not carry their burden to justify disqualification. (ECF No. 107-1 at 19.) Plaintiffs argue Judge Arpert correctly disqualified Fish under City of Atl. City v. Trupos, 992 A.2d 762 (N.J. 2010). (ECF No. 109 at 19.)

A motion for disqualification calls for the Court to “balance competing interests, weighing the need to maintain the highest standards of the profession against a client’s right freely to choose his counsel.” Dewey v. R.J. Reynolds Tobacco Co., 536 A.2d 243, 251 (N.J. 1988) (citation omitted). However, “a person’s right to retain counsel of his or her choice is limited in that there is no right to demand to be represented by an attorney disqualified because of an ethical requirement.” Id. The burden of production is borne by the party seeking disqualification. Trupos,
992 A.2d at 771. If the burden is met, the burden shifts to the attorney sought to be disqualified to demonstrate the matter in which they represented the former client is not the “same or substantially related” to the matter in which the disqualification motion is brought. *Id.* Therefore, the burden of persuasion on all elements under *RPC 1.9(a)* remains with the moving party, it “bears the burden of proving that disqualification is justified.” *Id.* (citation omitted). Lastly, “a determination of whether counsel should be disqualified is, an issue of law, subject to de novo plenary appellate review.” *Id.*

The Rule of Professional Conduct 1.9(a) states, “[a] lawyer who has represented a client in a matter shall not thereafter represent another client in the same or a substantially related matter in which that client’s interests are materially adverse to the interests of the former client unless the former client gives informed consent confirmed in writing.” There are “three necessary predicates to the application of R.P.C. 1.9(a)’s disqualification bar.” *Trupos*, 992 A.2d at 772. First, the law firm must have “formerly represented” the plaintiff asserting disqualification. *Id.* Second, the subsequent matter must be “materially adverse” to the interests of the former client. *Id.* Third, the two matters must be “the same or substantially related.” *Id.*

As to the first element, Fish’s argument that this Court should only evaluate whether ISE and FTEN are former clients of Fish is erroneous. Although neither ISE nor FTEN were ever clients of Fish, Nasdaq was indisputably a “former client” of Fish and is an adverse party to IMAX in this action. In fact, Fish is representing IMAX against Nasdaq in Counts VIII through X, alleging that MIAX misappropriated certain of Nasdaq’s trade secrets. Therefore, the former client element is met. The fact that neither ISE nor FTEN were ever clients of Fish is not an issue germane to disqualification.
As to the second element, Fish does not contest the “materially adverse” finding. It does not discuss this requirement in its brief. Nevertheless, this matter is clearly “materially adverse” to the interests of the Nasdaq. Fish prosecuted four of the seven patents that are asserted in this action, the remaining three patents involve the same field of technology for which Fish allegedly provided intellectual property counseling to and prosecuted patents for Nasdaq, and the trade secret claims involve the same technological field and may implicate confidential information that Nasdaq provided to Fish during its prior relationship. (ECF No. 105 at 3.)

As to the third element, Fish claims the matters are not “substantially related.” Specifically, it contends that just because it represented Nasdaq years ago and the matters share similar subject matter, is not enough to call the matters “substantially related.” (ECF No. 107-1 at 26.) Pursuant to RPC 1.9,

matters are deemed to be “substantially related” if (1) the lawyer for whom disqualification is sought received confidential information from the former client that can be used against that client in the subsequent representation of parties adverse to the former client, or (2) facts relevant to the prior representation are both relevant and material to the subsequent representation.

Trupos, 992 A.2d at 764. The Court finds Fish received confidential information from Nasdaq that can be used against Nasdaq in this matter and facts relevant to Fish’s representation of Nasdaq are relevant and material to this matter.

Through a decade long relationship with Nasdaq, Fish possessed information relating generally to Nasdaq’s patent prosecution strategy and approach to defending the validity of its patents, and knowledge of what Nasdaq protected as trade secrets apart from its patented inventions in the electronic trading technology field. (ECF No. 109 at 23.) Fish’s prior intellectual property counseling and prosecution work for Nasdaq unquestionably allowed Fish to gain access to confidential information that can be used to Nasdaq’s detriment in this case. In fact, “[t]he seven
asserted patents and the alleged trade secrets involve the same general field of technology, and the accused instrumentalities are the same for all the patent infringement claims.” (ECF No. 105 at 7.) Moreover, Fish unquestionably possesses direct knowledge of four of the seven patents in this matter and has chosen to jointly participate in this matter with Reed Smith by filing a single motion to dismiss. Kaselaan & D’Angelo Associates, Inc. v. D’Angelo, 144 F.R.D. 235, 239 (D.N.J. 1992) (“Recognizing that plaintiff’s attorney’s longstanding relationship with Commercial Union would necessarily have made him privy to confidential and proprietary information of Commercial Union, including its claims and litigation philosophy, its methods and procedures for defending claims and litigation, and its information regarding the administration of various business operations, the court held that plaintiff’s attorney could use such information to the substantial disadvantage of his former client Commercial Union.”); Essex Chem. Corp., Co., 993 F. Supp. at 246 (finding that, where the matters are substantially related, “the court will presume that the attorney has acquired confidential information from the former client”). Furthermore, the Fish attorneys involved in Nasdaq’s past representation are still members of Fish in the Boston office.

Although approximately seven years have passed since Fish’s representation of Nasdaq, the passage of time does not dilute the significance of the confidences provided and the overwhelming substantial relationship between the issues here and the past relationship. Accordingly, the matters are substantially related, and Fish’s Appeal is DENIED.

C. RPC 1.10

Fish argues in the alternative that even if there was a conflict, disqualification is inappropriate. (ECF No. 107-1 at 31.) Plaintiffs argues disqualification was appropriate because “whatever alleged prejudice that befalls MIAX is mitigated by the fact that ‘MIAX has been
represented by two sets of attorneys form the outset of this litigation,’ and ‘Reed Smith’s representation of MIAX can continue uninterrupted.” (ECF No. 109 at 32.)

While disqualification typically is the “result of finding that a disciplinary rule prohibits an attorney’s appearance in a case, disqualification never is automatic.” United States v. Miller, 624 F.2d 1198, 1201 (3d Cir. 1980). In fact, “[m]otions to disqualify are viewed with ‘disfavor’ and disqualification is considered a drastic measure which courts should hesitate to impose except when absolutely necessary.” Alexander v. Primerica Holdings, Inc., 822 F. Supp. 1099, 1114 (D.N.J. 1993) (citation omitted). A court “should disqualify an attorney only when it determines, on the facts of the particular case, that disqualification is an appropriate means of enforcing the applicable disciplinary rule.” Id. In doing so, “[i]t should consider the ends that the disciplinary rule is designed to serve and any countervailing policies, such as permitting a litigant to retain the counsel of his choice and enabling attorneys to practice without excessive restrictions.” Id. The question of whether disqualification is appropriate is essentially a balancing test, with the “client’s right to freely choose his counsel” on one side of the scale, and “the need to maintain the highest standards of the legal profession” on the other. Strategic Envtl. Partners, LLC v. Bucco, No. 13-5032 CCC, 2014 WL 6065816, at *2 (D.N.J. Nov. 12, 2014).

In Wyeth v. Abbott Labs., 692 F. Supp. 2d 453, 459 (D.N.J. 2010), the court provided several factors this Court should consider in determining whether disqualification is warranted: (1) prejudice to the former client; (2) prejudice to the new client; (3) whether the law firms representation of the former client in the former matter has allowed the new client to gain access to any confidential information relevant to this case; (4) “the cost—in terms of both time and money—“for the new client to retain new counsel; (5) “the complexity of the issues in the case
and the time it would take new counsel to acquaint themselves with the facts and issues”; (6) “which party, if either, was responsible for creating the conflict.”

Weighing these factors, the Court finds disqualification was appropriate. “Indeed, finding otherwise would allow the same law firm that argued for the patentability of Nasdaq’s inventions to represent parties adverse to Nasdaq in this suit who are arguing those very same patents are invalid.” (ECF No. 105 at 9.) On balance, Nasdaq would suffer more prejudice and hardship if Fish’s representation of MIAAX was allowed, being that Fish has access to confidential information and is familiar with Nasdaq’s strategic approaches to managing its technology and inventions. By contrast, prejudice to MIAAX would be minimal because: (1) this case is still at the pleading stage, (2) MIAAX has also voluntarily hired Reed Smith to represent it in this matter on several issue and Reed Smith is already familiar with this case; and (3) Fish is responsible for creating its own conflict in this case by choosing to represent MIAAX in a litigation where it previously prosecuted the same patents for Nasdaq. Accordingly, disqualification was proper.

IV. CONCLUSION

For the reasons set forth above, Fish’s Appeal (ECF No. 107) is DENIED and Judge Arpert’s September 6, 2018 Memorandum and Order (ECF No. 105) is AFFIRMED.

Date: November 26, 2018

/s/ Brian R. Martinotti
HON. BRIAN R. MARTINOTTI
UNITED STATES DISTRICT JUDGE
United States Court of Appeals for the Federal Circuit

DR. FALK PHARMA GMBH,
Appellant

AND

SALIX PHARMACEUTICALS, INC., VALEANT PHARMACEUTICALS INTERNATIONAL, INC.,
Intervenors

v.

GENERICO, LLC, FLAT LINE CAPITAL LLC,
MYLAN PHARMACEUTICALS INC.,
Appellees

2017-2312


SALIX PHARMACEUTICALS, INC., DR. FALK PHARMA GMBH,
Plaintiffs-Appellants

v.
MYLAN PHARMACEUTICALS INC., MYLAN INC.,
Defendants-Appellees

2017-2636, 2018-1320

Appeals from the United States District Court for the
Northern District of West Virginia in No. 1:15-cv-00109-
IMK, Judge Irene M. Keeley.

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VALEANT PHARMACEUTICALS
INTERNATIONAL, INC., SALIX
PHARMACEUTICALS, INC., PROGENICS
PHARMACEUTICALS, INC., WYETH LLC, FKA
WYETH,
Plaintiffs-Appellees

v.

MYLAN PHARMACEUTICALS INC., MYLAN INC.,
MYLAN LABORATORIES LIMITED,
Defendants-Appellants

ACTAVIS LLC,
Defendant

2018-2097

Appeal from the United States District Court for the
District of New Jersey in Nos. 2:15-cv-08180-SRC-CLW,
2:15-cv-08353-SRC-CLW, 2:16-cv-00035-SRC-CLW, 2:16-
cv-00889-SRC-CLW, 2:17-cv-06714-SRC-CLW, Judge
Stanley R. Chesler.
ON MOTIONS

SEALED ORDER FILED: February 8, 2019
PUBLIC ORDER FILED: February 20, 2019*

MARY W. BOURKE, Womble Bond Dickinson (US) LLP, Wilmington, DE, argued for appellant and intervenors in 17-2312 and plaintiffs-appellants in 17-2636. Also represented by KRISTEN HEALEY CRAMER, DANA KATHRYN SEVERANCE, DANIEL M. ATTAWAY; JOHN W. COX, Atlanta, GA.


MICHAEL ISIDORO VERDE, Katten Muchin Rosenman LLP, New York, NY, argued for appellee Mylan Pharmaceuticals Inc. in 17-2312, for defendants-appellees in 17-2636, and for defendants-appellants in 18-2097. Also represented by DEEPRO Mukerjee, LANCE SODERSTROM, JONATHAN ROTENBERG, STEPHANIE MAE ROBERTS; HOWARD ROBERT RUBIN, RAJESH RAM SRINIVASAN, ERIC THOMAS WEILINGER, Washington, DC; ROBERT FLORENCE, SHARAD KOTAGIRI BIJANKI, MICHEAL L. BINNS, KAREN L. CARROLL,

* This order was originally filed under seal and has been unsealed in full.
At issue are three motions to disqualify Katten Muchin Rosenman LLP as counsel for Mylan Pharmaceuticals Inc. (“Mylan”) in three appeals before this court. Valeant Pharmaceuticals International, Inc. (“Valeant-CA”) and Salix Pharmaceuticals, Inc. (“Salix”) move to disqualify in Valeant Pharmaceuticals International, Inc. v. Mylan Pharmaceuticals Inc., No. 2018-2097 (“Valeant II”), Salix moves to disqualify in Salix Pharmaceuticals, Inc. v. Mylan Pharmaceuticals Inc., No. 2017-2636, 2018-1320 (“Salix II”), and Valeant-CA and Salix move to disqualify in Dr. Falk Pharma GmbH v. Generico, LLC, No. 2017-2312 (“Dr. Falk II”). Because we find that Katten has an ongoing attorney-client relationship with Valeant-CA and its subsidiaries, including Salix, we conclude that Katten’s representation of Mylan in these appeals presents concurrent conflicts of interest. Therefore, we grant the motions to disqualify.

I. BACKGROUND

The motions to disqualify stem from Katten’s representation of Bausch & Lomb Inc. (“Bausch & Lomb”), a corporate affiliate of Valeant-CA and Salix (collectively, “movants”), in a trademark litigation and its concurrent representation of Mylan, adverse to movants, in the pending appeals. Specifically, Katten signed an engagement letter with Bausch & Lomb that broadly defined Katten’s client as any Valeant entity. Attorneys Deepro Mukerjee and Lance Soderstrom represented Mylan during various stages of the Valeant, Salix, and Dr. Falk proceedings—first, as attorneys from Alston & Bird LLP, but later, as
attorneys from Katten. The parties agree that Mukerjee and Soderstrom moved to Katten as of May 3, 2018. The parties, the engagement letter, and the procedural history are detailed below.

A. The Parties

The parties relevant to the motions to disqualify include, Valeant-CA, Valeant Pharmaceuticals International (“Valeant-DE”), Salix, and Bausch & Lomb. Valeant-CA, a Canadian corporation and the movant in Valeant II and Dr. Falk II, is the ultimate parent of these entities. Specifically, Salix—a movant in all three appeals—is a wholly-owned subsidiary of Salix Pharmaceuticals, Limited, which is a wholly-owned subsidiary of Valeant-DE, which is an indirect, wholly-owned subsidiary of Valeant-CA. Bausch & Lomb is also an indirect subsidiary of Valeant-CA and an affiliate of the above-listed entities.

Valeant-CA contends that it has been a longstanding client of Katten, both directly and through its subsidiaries. Specifically, movants allege that a concurrent conflict arises in all three appeals from Katten's ongoing representation of Bausch & Lomb in a trademark matter regarding the mark MOISTURE EYES. A partner in Katten's

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1 On July 26, 2018, counsel for Valeant-CA filed a notice of appearance in which it indicated that Valeant-CA had changed its name to “Bausch Health Companies Inc.” Valeant II, ECF No. 30. All filings pertaining to the present motions refer to Bausch Health Companies Inc. by its former name of “Valeant Pharmaceuticals International, Inc.” To avoid any confusion, we will also refer to Bausch Health Companies Inc. by its former name of Valeant Pharmaceuticals International, Inc.” or, as abbreviated herein, “Valeant-CA” for purposes of this order.

2 Movants also contend that a conflict arises from Katten’s representation of another Valeant-CA subsidiary,
Chicago office has been representing Bausch & Lomb since 2001. Verde Decl. at ¶ 8 (“The only affiliate that Katten identified as a current client was Bausch & Lomb, Inc. . . . [A] partner in Katten's Chicago office[] has been representing Bausch & Lomb on trademark, copyright and advertising issues since 2001.”). Mukerjee admits that he was aware that Katten represents Bausch & Lomb when he moved to the firm. Mukerjee Decl. at ¶ 17 (“During my discussions with Katten in late 2017, I was informed that Katten represents Bausch & Lomb, Inc.”).

B. The Engagement Letter & OC Guidelines


Section 1.1 of the OC Guidelines states that “[t]hese guidelines will govern the relationship between Valeant Pharmaceuticals International[, i.e. Valeant-DE], its subsidiaries and affiliates. . . and outside counsel.” Gorman Decl. Ex. A, at § 1.1. The terms of the OC Guidelines also require that Katten complete a conflict check “before representation of [Valeant-DE and its subsidiaries and affiliates] commences.” Gorman Decl. Ex. A, at § 1.2. The terms further state that “[a]ny conflict of interest that is discovered in such a check or that develops during an ongoing counseling matter. The parties dispute whether this matter is truly ongoing. Because we find that a conflict arises from the Bausch & Lomb litigation, which is undisputedly ongoing, we need not decide whether this counseling matter involving VPNA also presents a conflict.
representation can only be approved, waived or otherwise cleared by the written agreement of the Valeant General Counsel.” Gorman Decl. Ex. A, at § 1.2. The OC Guidelines do not define “conflict of interest,” but state that “Valeant expects its firms to adhere to local rules and ethics rules relating to conflict of interest and client representation.” Gorman Decl. Ex. A, at § 1.2.

The OC Guidelines also specify that “Valeant expects a significant degree of loyalty from its key external firms,” defined as “firms with 12 month billings exceeding one million dollars.” Gorman Decl. Ex. A, at § 1.2. These key firms should “not represent any party in any matters where such party’s interests conflict with the interests of any Valeant entity.” Gorman Decl. Ex. A, at § 1.2. Finally, the OC Guidelines state that they “will continue to apply unless revoked in writing by either party or modified by a subsequent letter signed by Valeant General Counsel and outside counsel.” Gorman Decl. Ex. A, at § 1.5. Salix and Valeant-CA contend, and Mylan does not dispute, that the engagement letter, including the OC Guidelines, remains active under this provision.

B. The Procedural History

1. Valeant proceedings

granted the motion on May 1, 2018. Valeant I, ECF No. 300.

Mukerjee and Soderstrom, then at Alston & Bird, represented Mylan throughout the district court litigation. On May 3, 2018, Mylan notified the district court that Mukerjee and Soderstrom had left Alston & Bird to join Katten. On May 25, 2018, Valeant-CA filed a motion to disqualify Katten in the district court action. Mylan timely appealed the district court’s summary judgment on June 22, 2018. Valeant-CA then filed a motion to disqualify Katten in this court on July 9, 2018, and the district court stayed a decision on the motion to disqualify pending before it. We stayed the parties’ briefing on the merits in this appeal pending our decision on the motion. Valeant II, ECF No. 24.

2. Salix & Dr. Falk proceedings


In Salix I—the district court proceeding—Salix and Dr. Falk sued Mylan on June 26, 2015, alleging that Mylan’s submission of an abbreviated new drug application constituted an act of infringement under § 271(e) of the ’688 patent, which is listed in the Orange Book. Attorneys from Parker Poe represented Mylan throughout the district court litigation in Salix I. On April 22, 2017, a month after trial was complete, Mukerjee and Soderstrom, then of Alston & Bird, entered appearances in the district court action. After entering an appearance, Mukerjee took part in negotiating the stipulation to dismiss Mylan’s
counterclaims. The district court entered judgment on September 12, 2017, finding that Dr. Falk and Salix had failed to demonstrate by a preponderance of the evidence that Mylan’s proposed product would infringe claim 1 of the ’688 patent.

Salix appealed the judgment on September 27, 2017. Mukerjee and Soderstrom, who were still at Alston & Bird at that time, and five attorneys from Parker Poe all entered appearances before this court. The parties completed briefing in February 2018. On June 5, 2018, after Mukerjee and Soderstrom moved to Katten, Salix filed the present motion to disqualify.

In Dr. Falk I—the parallel Board proceeding—Mylan petitioned for inter partes review of claims 1 and 16 of the ’688 patent. Dr. Falk identified Salix as a real party in interest. The Board granted institution and, in a final written decision dated May 19, 2017, found claims 1 and 16 of the ’688 patent unpatentable as obvious. Dr. Falk timely appealed that decision on July 18, 2017. On appeal, Mukerjee and Soderstrom, then of Alston & Bird, entered appearances in that case for the first time. The parties completed briefing in February 2018. On June 5, 2018, after Mukerjee and Soderstrom moved to Katten, Salix and Valeant-CA moved to intervene and filed the present motion to disqualify. On September 12, 2018, we granted the motion to intervene in an oral order just prior to commencing oral argument on the motions to disqualify. See Oral Arg. at 0:39, available at http://oralarguments.capecourts.gov/default.aspx?fl=2018-2097.mp3.

Movants contend that Katten’s representation of Bausch & Lomb presents a concurrent conflict with Katten’s representation of Mylan against Valeant-CA and Salix in either of two ways—first, they contend that the engagement letter creates an ongoing relationship between Katten and Valeant-CA, including all of its subsidiaries; and second, they contend that all Valeant-CA subsidiaries
are so interrelated that representation of one constitutes representation of all. Accordingly, Valeant-CA and Salix move to disqualify Katten as counsel in these appeals. Mylan opposes. We have jurisdiction over these appeals pursuant to 28 U.S.C. § 1295(a)(1), (4).

II. DISCUSSION

We apply regional circuit law to disqualification matters. Celgard, LLC v. LG Chem, Ltd., 594 F. App’x 669, 671 (Fed. Cir. 2014); accord Atasi Corp. v. Seagate Tech., 847 F.2d 826, 829 (Fed. Cir. 1988). The relevant regional circuits in all three appeals apply the Model Rules of Professional Conduct. Thus, all three motions allege violations of the same rule—Rule 1.7(a) of the Model Rules of Professional Conduct—which states:

a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:

(1) the representation of one client will be directly adverse to another client . . . .

3 In Valeant, the relevant regional circuit is the Third Circuit, which applies the professional conduct rules of the forum state. See United States v. Miller, 624 F.2d 1198, 1200 (3d Cir. 1980). The forum state, New Jersey, has adopted the Model Rules of Professional Conduct. N.J. Rule of Prof'l Conduct 1.7(a). In Salix, the relevant regional circuit is the Fourth Circuit, which applies the rules of professional conduct of the forum state. See Shaffer v. Farm Fresh, Inc., 966 F.2d 142, 145 (4th Cir. 1992). The forum state, West Virginia, has also adopted the Model Rules. W. Va. Rule of Prof'l Conduct 1.7(a). Finally, in Dr. Falk, the U.S. Patent and Trademark Office is the relevant forum and it has also adopted the Model Rules. 37 C.F.R. § 11.107(a).
When applying this rule, we look to “the total context, and not whether a party is named in a lawsuit,” to assess “whether the adversity is sufficient to warrant disqualification.” *Celgard*, 594 F. App’x at 672; *see also Freedom Wireless, Inc. v. Bos. Commc’ns Grp., Inc.*, No. 2006-1020, 2006 WL 8071423, at *2 (Fed. Cir. Mar. 20, 2006) (“The parties debate whether Freedom Wireless and Nextel are ‘directly adverse’ in these circumstances, where Nextel was not a named party to the initial lawsuit. We conclude, on the facts of the case, that the parties are directly adverse for purposes of analyzing a conflict of interest and determining the need for disqualification.”). Indeed, Comment 34 to Rule 1.7, which addresses “organizational clients,” states:

A lawyer who represents a corporation or other organization does not, by virtue of that representation, necessarily represent any constituent or affiliated organization, such as a parent or subsidiary. *See* Rule 1.13(a). Thus, the lawyer for an organization is not barred from accepting representation adverse to an affiliate in an unrelated matter, *unless the circumstances are such that the affiliate should also be considered a client of the lawyer*, there is an understanding between the lawyer and the organizational client that the lawyer will avoid representation adverse to the client’s affiliates, or the lawyer’s obligations to either the organizational client or the new client are likely to limit materially the lawyer’s representation of the other client.

Model Rules of Prof’l Conduct r. 1.7 cmt. 34 (Am. Bar Ass’n 2018) (emphasis added). Circumstances in which an affiliate is considered a client of a lawyer can arise by express agreement or when affiliates are so interrelated that representation of one constitutes representation of all. *GSI Commerce Sols., Inc. v. BabyCenter, LLC*, 618 F.3d 204, 210–12 (2d Cir. 2010) (finding that...
corporate affiliate were so interrelated such that “representation adverse to a client’s corporate affiliate implicate[d] the duty of loyalty owed to the client”).

For the reasons stated below, Katten’s representation of Mylan in *Valeant II, Salix II,* and *Dr. Falk II* adverse to the movants presents concurrent conflicts of interest with its representation of Bausch & Lomb in the ongoing trademark litigation under Rule 1.7.

A. Katten’s Representation of Mylan in *Valeant II*

Katten’s representation of Mylan adverse to Valeant-CA and Salix in *Valeant II* and its ongoing representation of Bausch & Lomb, an affiliate of movants, presents a concurrent conflict of interest in violation of Rule 1.7. This is true even though movants are affiliates of Bausch & Lomb because the terms of the engagement letter and movants’ demonstration of interrelatedness between the various Valeant affiliates presents circumstances such that movants should also be considered a client of Katten.

1. The Engagement Letter

Because the engagement letter creates an ongoing attorney-client relationship between the law firm, Katten, and its organizational clients, Valeant-CA and Salix, Katten’s representation of Mylan adverse to movants in *Valeant II* gives rise to a concurrent conflict of interest under Rule 1.7. The express terms of the engagement letter and accompanying OC Guidelines indicate that Katten formed such a relationship with the movants when it signed the engagement letter for the Bausch & Lomb trademark litigation. Specifically, the engagement letter states that it “represents the general terms of engagement governing the overall relationship between [Katten] and Valeant Pharmaceuticals International, Inc.,” i.e. Valeant-CA. Gorman Decl. Ex. A, at 1. This sentence, on its face, demonstrates that Katten’s relationship extends beyond just Bausch & Lomb to at least Valeant-CA.
The OC Guidelines, which are expressly incorporated into the engagement letter, further extend the relationship to include any Valeant entity. Section 1.1 of the OC Guidelines states that the guidelines “will govern the relationship between Valeant-[DE], its subsidiaries and affiliates, . . . and outside counsel.” Gorman Decl. Ex. A, at § 1.1. And section 1.2 of the OC Guidelines requires that Katten complete a conflict check “before representation of [Valeant-DE and its subsidiaries and affiliates] commences.” Gorman Decl. Ex. A, at § 1.2. While these sections reference Valeant-DE and not Valeant-CA, the phrase “its subsidiaries and affiliates” encompasses Valeant-CA because Valeant-CA is the parent company, i.e. affiliate, of Valeant-DE. That same phrase also encompasses another movant in Valeant II, Salix, because Salix is a subsidiary of Valeant-DE. For these reasons, the engagement letter creates an ongoing relationship between Katten and both Valeant-CA and Salix.

Mylan argues that the engagement letter and OC Guidelines do not prevent Katten from representing a party that is adverse to Valeant-CA or Salix and that the terms of the letter actually authorize Katten to do so. In support of its position, Katten points to section 1.2 of the OC Guidelines, which provides that:

Valeant expects a significant degree of loyalty from its key external firms (key firms being firms with 12 month billings exceeding one million dollars ($1,000,000)). Such firms should therefore not represent any party in any matters where such party’s interests conflict with the interests of any Valeant entity.

Gorman Decl. Ex. A, at § 1.2 (emphases added).

Mylan contends that, “[t]he clear converse of this provision is that firms that are not ‘key external firms,’ may take on matters adverse to a Valeant entity as long as they otherwise comply with the [Rules of Professional
Conduct].” Valeant II, Mylan’s Opp. at 11. Because it is undisputed that, despite having represented various Valeant-related entities in certain matters over the years, Katten is not a key firm, Mylan argues that Katten is not bound by the provisions of the engagement letter that broadly define the client as any Valeant entity.

We find this reading of the engagement letter to be irrational. Section 1.2 does not indirectly authorize Katten to represent parties adverse to Valeant-CA and Salix so long as Katten remains a non-key firm. Rather, section 1.2 expects a heightened degree of loyalty from key firms, requiring something more than mere adherence to the ethical rules. It states that key firms should not represent “any party” in “any matters” that would conflict with “any Valeant entity.” Gorman Decl. Ex. A, at § 1.2. This reference to “any matters” encompasses, as Valeant-CA stated at oral argument, a “blunderbuss” limitation on key firms to avoid, not only matters that give rise to ethical conflicts, but also those that give rise to other types of conflicts. See Oral Arg. at 9:36. Other types of conflicts could include, for example, a matter involving the filing of an amicus brief that presents no ethical conflict under the rules of professional conduct, but that espouses a legal position contrary to one taken by a Valeant entity in another case. Thus, section 1.2 broadens the degree and type of loyalty expected from key firms.

But for firms generally, the OC Guidelines state that “Valeant expects its firms to adhere to local rules and ethics rules relating to conflict of interest and client representation.” Gorman Decl. Ex. A, at § 1.2. This in no way narrows the definition of Katten’s client to only Bausch & Lomb. Such a reading would be contrary to the various other provisions that define the client generally to include Valeant-CA and Salix. Mylan’s argument fails.

Mylan also argues that the engagement letter creates a relationship between only Katten and Bausch & Lomb
because both Valeant-CA and Bausch & Lomb appear on the letterhead of the engagement letter and because Denis A. Polyn, who Mylan contends was a Bausch & Lomb attorney with a Bausch & Lomb email address, signed the engagement letter. But Mylan ignores the fact that Polyn was also the Vice President and Assistant General Counsel of Intellectual Property at Valeant-CA at that time. Gorman Decl. Ex. A, at 3. The fact that Polyn had a Bausch & Lomb email address and, according to Katten, was also a Bausch & Lomb attorney, does not mean that this engagement governed only the relationship between Katten and Bausch & Lomb. Rather, that the two entities appear to share a common letterhead and common employees only further underscores that Valeant-CA is a client of Katten because it demonstrates, as detailed below, that the two affiliates are interrelated. Thus, because the engagement letter creates an ongoing attorney-client relationship between Katten and Valeant-CA and its subsidiary Salix, Katten’s representation of Mylan adverse to movants in Valeant II gives rise to a concurrent conflict of interest under Rule 1.7.

2. Interrelated Affiliates

Even if there were any plausible ambiguity in the engagement letter, Mylan’s arguments would still fail because Valeant-CA, Salix, and Bausch & Lomb have demonstrated that the three entities are sufficiently interrelated to give rise to a corporate affiliate conflict.

The relevant regional circuits have not previously set out factors governing corporate interrelatedness in this context. In GSI Commerce Solutions, Inc. v. BabyCenter, L.L.C., 618 F.3d 204, 211–12 (2d Cir. 2010), the Second Circuit considered the circumstances in which “representation adverse to a client’s corporate affiliate implicates the duty of loyalty owed to the client.” Id. at 210. It found that the factors relevant to this inquiry include “(i) the degree of operational commonality between affiliated entities, and (ii)
the extent to which one depends financially on the other.” *Id.* Regarding the first factor, it noted that “courts have considered the extent to which entities rely on a common infrastructure,” focusing “on shared or dependent control over legal and management issues,” which “reflects the view that neither management nor in-house legal counsel should, without their consent, have to place their trust in outside counsel in one matter while opposing the same counsel in another.” *Id.* Regarding the second factor, it noted that, “several courts have considered the extent to which an adverse outcome in the matter at issue would result in substantial and measurable loss to the client or its affiliate.” *Id.* at 211. The Second Circuit applied these factors to find that a parent and its subsidiary were sufficiently interrelated to give rise to a corporate affiliate conflict.

In the absence of evidence to the contrary, we conclude that the relevant regional circuits would likely find the Second Circuit’s reasoning persuasive and would therefore adopt its factors here. In particular, we find that they would agree that shared or dependent control over operational and legal matters between the affiliates is significant to the inquiry. Accordingly, we apply the Second Circuit’s interrelatedness test to the facts in this case, and find that Valeant-CA, Salix, and Bausch & Lomb all share a high degree of operational commonality and are financially interdependent. Gorman Suppl. Decl. at ¶¶ 5, 6, 7, 10, 11, 12.

Valeant-CA and Bausch & Lomb “have a common infrastructure whereby [Valeant-CA] provides administrative and general support services to Bausch & Lomb. This includes “accounting, cash management, employee benefits, finance, human resources, travel, computer systems, insurance, and payroll services.” Gorman Suppl. Decl. at ¶ 5. The two also “share the same in-house Valeant legal department.” Gorman Suppl. Decl. at ¶ 6. Robert Gorman, the Vice President and Head of Global Intellectual
Property at Valeant-CA, is a member of the shared legal department and is “responsible for managing and controlling all of their IP related matters and disputes.” Gorman Suppl. Decl. at ¶ 6. The current Vice President and Assistant General Counsel at Valeant-CA and former Vice President and Assistant General Counsel at Bausch & Lomb, John F. Lafave, states that, since his “transition to the current position at [Valeant-CA] in 2013, [he] still use[s his] email address at bausch.com.” Lafave Suppl. Decl. at ¶¶ 1–2. Finally, Valeant-CA’s public filings to the U.S. Securities and Exchange Commission (“SEC”) from May 8, 2018 show that Bausch & Lomb contributed over $1 billion to Valeant-CA’s reported revenues for the first quarter of 2018. Gorman Suppl. Decl. at ¶ 7. This all demonstrates that Valeant-CA and Bausch & Lomb share a high degree of operational commonality and are financially interdependent.

The same is true with regard to Salix and Valeant-CA. Salix and Valeant-CA also share an in-house legal department; indeed, Salix does not have its own legal department. Gorman Decl. at ¶ 6. Valeant-CA and Salix share a common infrastructure whereby Valeant-CA provides administrative and general support services to Salix, such as accounting, cash management, employee benefits, finance, human resources, travel, computer systems, insurance, and payroll services. Gorman Decl. at ¶ 5. The two entities are also financially interdependent because Salix’s sales directly affect Valeant-CA’s bottom line. Specifically, Valeant-CA’s SEC filings demonstrate that its “revenue depends on Salix’s gastrointestinal product sales,” the sales of Salix products in the U.S. totaled $593 million of Valeant-CA’s revenue from branded prescription products for the first quarter of 2018, and Salix’s drug Apriso® is the second-highest revenue producer of Valeant-CA’s branded prescription drugs. Gorman Decl. at ¶¶ 9–10. All of this demonstrates that Valeant-CA and Salix share a high degree of operational commonality and are financially interdependent.
interdependent. For these reasons, we find that Valeant-CA, Bausch & Lomb, and Salix are sufficiently interrelated to give rise to a corporate affiliate conflict.

B. Katten’s Representation of Mylan in *Salix II* & *Dr. Falk II*

Katten’s representation of Mylan in *Salix II* and in *Dr. Falk II* also gives rise to a concurrent conflict interest under Rule 1.7. As noted above, the engagement letter and accompanying OC Guidelines create an ongoing relationship between Katten and Salix. Specifically, section 1.1 of the OC Guidelines states that “[t]hese guidelines will govern the relationship between Valeant Pharmaceuticals International[,] i.e. Valeant-DE], its subsidiaries and affiliates. . . and outside counsel.” Gorman Decl. Ex. A, at § 1.1. Section 1.2 of the OC Guidelines requires that Katten complete a conflict check “before representation of [Valeant-DE and its subsidiaries and affiliates] commences.” Gorman Decl. Ex. A, at § 1.2. Because Salix is a subsidiary of Valeant-DE, the term “subsidiaries” in sections 1.1 and 1.2 reasonably encompasses Salix. For these reasons, the engagement letter creates an ongoing relationship between Katten and Salix.

Again, even if there were an ambiguity in the engagement letter, which there is not, Katten’s representation of Mylan adverse to Salix would still give rise to a conflict of interest. This is because Katten and Bausch & Lomb undisputedly have an attorney-client relationship and Bausch & Lomb, Salix, and Valeant-CA are sufficiently interrelated to give rise to a corporate affiliate conflict. *See supra* II.A.2. For the reasons stated above, Katten’s representation of Mylan in *Salix II* and *Dr. Falk II* present conflicts of interest in violation of Rule 1.7.

C. Additional Considerations

Mylan contends that, even if Katten has violated Rule 1.7, disqualification is not warranted under the
circumstances. Some district courts have held that disqualification is mandatory for violation of Rule 1.7. See, e.g., Manoir-Electroalloys Corp. v. Amalloy Corp., 711 F. Supp. 188, 195 (D.N.J. 1989) (finding that disqualification should be mandatory for violation of Rule 1.7)). But other district courts have considered whether the totality of the circumstances—including the impact, nature, and degree of a conflict, the prejudice or hardship to either party, and which party was responsible for creating the conflict—warrants disqualification. Wyeth v. Abbott Labs., 692 F. Supp. 2d 53, 457–59 (D.N.J. 2010) (citing Bos. Scientific Corp. v. Johnson & Johnson Inc., 647 F. Supp. 2d 369, 374 (D. Del. 2009); Elonex I.P. Holdings, Ltd. v. Apple Computer, Inc., 142 F. Supp. 2d 579, 583–84 (D. Del. 2001) (balancing factors to find disqualification unwarranted)). We have previously disqualified counsel without consideration of any factor, other than the fact of the ethical violation, but did so in a nonprecedential decision. Freedom Wireless, 2006 WL 8071423, at *3 (“Having concluded that a conflict of interest exists, we further conclude that disqualification . . . is warranted.”). Here, we need not decide which approach is preferable because we find that, even if additional considerations were necessary, they all weigh in favor of disqualification.

Mylan will not face any prejudice or undue hardship as a result of disqualification. Indeed, because movants seek only prospective relief, Mylan will not need to submit new briefs in Salix II or in Dr. Falk II. And, Parker Poe, who represented Mylan in Salix I all the way through trial, remains counsel of record along with Katten in that appeal. In Valeant II, we stayed briefing on the merits, so Mylan now has the opportunity to seek new counsel to draft its briefs. Finally, we conclude that Katten’s erection of an ethical wall is insufficient to resolve its violation of Rule 1.7. Katten claims that this wall cordons off Mukerjee and Soderstrom from Katten attorneys who have worked on matters for Bausch & Lomb, Valeant-CA, or affiliates in
the 18 months preceding May 7, 2018. But this wall does nothing to address the concerns stemming from Katten’s violation because it was created after Mukerjee and Soderstrom joined Katten, it applies only partially to work conducted within 18 months before May 7, 2018, and Katten never previously informed movants of any potential conflict. We find that disqualification is warranted here, whether or not disqualification is mandatory under Rule 1.7.

IV. CONCLUSION

For the reasons stated above, we find that Katten’s representation of Bausch & Lomb in the trademark litigation presents a concurrent conflict of interest with its representation of Mylan in Valeant II, Salix II, and Dr. Falk II. Under Rule 1.7, Katten may not represent Mylan in these appeals unless it previously obtained informed and written consent from both clients. Katten has failed to do that here, and therefore has violated Rule 1.7.

Accordingly,

It Is Ordered That:

The motions to disqualify are granted.

FOR THE COURT

February 8, 2019
Date

/s/ Peter R. Marksteiner
Peter R. Marksteiner
Clerk of Court