

Conflicts of Interest Under New DR 1-106

BY ROY SIMON

Conflict of interest issues are likely to be the most frequent and difficult issues under New York's new MDP rules, which take effect on November 1, 2001. Last month, I asked how the rule on personal conflicts of interest (DR 5-101) applies to the contractual relationships with nonlegal professionals envisioned by DR 1-107. This month I focus on conflicts of interest under DR 1-106.

What does DR 1-106 cover?

New DR 1-106 covers nonlegal services that a law firm provides, directly or indirectly, to its clients or to others. The rule refers to three types of providers:

- a law firm (*i.e.*, the law firm's own nonlawyer employees)
- a lawyer who also provides nonlegal services (*i.e.*, a dual-profession lawyer)
- an entity that a lawyer or law firm owns, controls, is an agent of, or is otherwise affiliated with (*i.e.*, an entity legally separate from the law firm itself).

The MacCrate Committee (which proposed the new rules last year) gave the following examples of nonlegal services provided by nonlawyer employees of a law firm:

[P]atent lawyers routinely hire scientists and nonlawyer patent agents to work with them on client projects. Antitrust lawyers frequently employ economists to assist them in dealing with the economic issues and working with expert witnesses and other outside consultants. Many law firms have professional lobbyists on staff to assist them in governmental relations. Practitioners in the real estate tax certiorari or condemnation fields often employ appraisers who assist them in advocacy as to the values for specific properties. Elder law attorneys often employ social workers who serve their clients in conjunction with the legal services provided....

Report of the New York State Bar Association Special Committee on the Law Governing Firm Structure & Operation 98-99 (April 2000).

Regarding lawyers who personally provide both legal and non-legal services, the MacCrate Committee noted that "lawyers often practice ... a wide variety of other professions and callings, including real estate brokerage, insurance brokerage, financial planning, medicine, nursing, social work, and so on." The Committee specifically mentioned the American Association of Attorney-Certified Public Accountants, formed by lawyer-accountants back in 1964. *Id.* at 99.

My question is: When do the conflict of interest rules — especially DR's 5-105 and 5-108 — apply to these nonlegal services?

When either the law firm itself or a dual-practice lawyer within the firm directly provides the nonlegal services, the new rule divides up the nonlegal services into two categories — “distinct” and “not distinct” — to which I now turn.

Nonlegal services that “are not distinct”: DR 1-106(A)(1)

Under DR 1-106(A)(1), if a law firm simultaneously provides a client with legal and nonlegal services that “are not distinct” from each other, then the Disciplinary Rules — including the conflict rules — apply to both the nonlegal services (as well as the legal services, of course). New EC 1-9, which refers specifically to “prohibitions against representation of persons with conflicting interests,” states: “[W]here the legal and non-legal services are not distinct, DR 1-106(A)(1) requires that the lawyer providing nonlegal services adhere to all of the requirements of the Code of Professional Responsibility with respect to the nonlegal services.” Nothing in DR 1-106 allows a client to waive this protection.

To use an example, suppose a law firm represents Major Corp. in a merger transaction, and an economist on the law firm’s staff provides Major with a prediction of its post-merger market share. Because the legal and economic services in this example are “not distinct,” the economist’s services are governed by the conflict rules. Thus, the economist cannot offer his services to anyone else (whether or not that person is a client of the law firm) if the Disciplinary Rules would prohibit the law firm itself from providing legal services to that person.

As long as the economist is working on the merger for Major Corp., he may not simultaneously do any work for a litigation opponent or transactional adversary of Major Corp., even in a wholly unrelated matter, unless he satisfies the twin prongs of DR 5-105(C) — “a disinterested lawyer would believe that the lawyer can competently represent the interests of each [client]” and “each consents to the representation after full disclosure....” Moreover, if Major becomes a former client, DR 5-108 will prohibit the economist from providing his nonlegal services to any adversary of

Major in a matter substantially related to the merger (e.g., an antitrust challenge to the merger) absent Major’s consent after full disclosure.

As a corollary, under DR 5-105(E), the economist must keep contemporaneous records of all of his engagements, and must check each proposed new engagement against those engagements for conflicts. If the conflict of interest rules would prohibit the law firm from representing or advising a given client, then the same rules will prohibit the economist from serving that client.

Finally, as new EC 1-9 explains: “DR 1-106(A)(1) applies to the provision of nonlegal services by a lawyer even when the lawyer is not personally providing any legal services ... if the person is also receiving legal services from another lawyer in the firm that are not distinct from the nonlegal services.” Needless to say, when a lawyer is personally providing both legal and nonlegal services to the same client, the lawyer must adhere to the Disciplinary Rules not only when providing the legal services but also when providing the nonlegal services.

Nonlegal services that “are distinct”: DR 1-106(A)(2)

On the other hand, under DR 1-106(A)(2), if the law firm itself provides nonlegal services to a client that “are distinct” from the legal services the law firm is providing to that client, then the Disciplinary Rules do not apply to the nonlegal services unless the client “could reasonably believe that the nonlegal services are the subject of an attorney-client relationship.” Even that risk can be reduced or eliminated if the law firm, pursuant to DR 1-106(A)(4), “has advised the person receiving the services in writing that the services are not legal services and that the protection of an attorney-client relationship does not exist with respect to the nonlegal services” (Of course, the disclaimer is effective only if the nonlegal services really are nonlegal services. The services must be neither the unauthorized practice of law by a nonlawyer nor the authorized practice of law by a lawyer who is also capable of providing nonlegal services. A disclaimer cannot transform legal services into nonlegal services; it can only dispel client confusion about nonlegal services.)

New EC 1-11 elaborates on the disclaimer option as follows:

... Such a communication should be made before entering into an agreement for the provision of nonlegal services, in a manner sufficient to assure that the person understands the significance of the communication. In certain circumstances, however, additional steps may be required to communicate the desired understanding. For example, while the written disclaimer set forth in DR 1-106(A)(4) will be adequate for a sophisticated user of legal and nonlegal services, a more detailed explanation may be required for someone unaccustomed to making distinctions between legal services and nonlegal services....

Unfortunately, DR 1-106 (A)(2) does not expressly cover the situation in which a law firm, through a nonlawyer employee, provides nonlegal services to a person who is not a client of the law firm. The rule refers only to nonlegal services distinct from “*legal services being provided to that person by the lawyer or law firm.*” In my view, when nonclients obtain services from a law firm’s staff employees, the services should be subject to the Disciplinary Rules if the person receiving the services “could reasonably believe that the nonlegal services are the subject of an attorney-client relationship.” Accordingly, if a law firm allows its nonlawyer employees to serve the public, the law firm should always provide the nonclient with a disclaimer, pursuant to DR 1-106(A)(4), stating that “the services are not legal services and that the protection of an attorney-client relationship does not exist with respect to the nonlegal services”

Nonlegal services provided by affiliated entities: DR 1-106(A)(3)

The MacCrate Committee listed the following examples of nonlegal services provided by law firm affiliates:

- San Francisco’s Littler-Mendelsohn, which concentrates its practice in management-side labor relations, established a subsidiary called Employment Law Training, Inc. to train clients on how to minimize employment discrimination.
- Washington, D.C.’s Howrey & Simon has formed three subsidiaries: (1) Capital Environmental employs scientists and other specialists who provide risk analysis regarding environmental cleanup costs; (2) Capital Accounting employs accountants to assist the law firm’s litigation clients in measuring their damages and exposure; and (3) Capital Economics employs economists and accountants who perform market analysis for mergers and acquisitions.

- Detroit's Dickinson Wright, using computer technicians that it had hired to meet the law firm's internal needs, created a company called Technology Consulting Partners that helps businesses such as Chrysler Financial and Dollar Rent-a-Car manage their operations more efficiently.
- New York's Anderson Kill & Olick, which represents clients in insurance coverage disputes, formed a company named Anderson Kill Insurance Services to advise companies on such subjects as choosing appropriate policies and securing maximum recoveries in policy disputes without litigation.
- Long Island's Ruskin, Moscou, Evans & Faltischek formed an investment banking firm named Island Star Capital to advise Long Island companies regarding mergers and acquisitions, to help them raise capital, and to lend management expertise to early stage companies.

When law firm subsidiaries or other affiliates provide nonlegal services, the services are governed by DR 1-106(A)(3), which parallels DR 1-106(A)(2). Thus, exactly as under DR 1-106(A)(2), the law firm is subject to the Disciplinary Rules with respect to the nonlegal services provided by the affiliated entity "if the person receiving the services could reasonably believe that the nonlegal services are the subject of an attorney-client relationship." (However, there is an exception "if the interest of the lawyer or law firm in the entity providing the nonlegal services is *de minimis*.")

When a nonlegal entity (rather than a law firm) provides nonlegal services, the risk that the recipient will confuse the nonlegal services with legal services is reduced. But some nonlegal services look confusingly like legal services. Consider advice about how to minimize employment discrimination, or advice about mergers and acquisitions, or advice about securing maximum recoveries in insurance disputes. If the nonlegal subsidiary uses an affiliated law firm's name as part of its own name, or shares office space with a law firm, or engages in joint marketing efforts with the law firm, then the risks significantly increase that the recipient "could reasonably believe that the nonlegal services are the subject of an attorney-client relationship." Therefore, whenever possible, the law firm should provide the consumer of the nonlegal services with a disclaimer pursuant to DR 1-106(A)(4).

Conclusion

Despite its cloudy language, the message of DR 1-106 is simple. When a law firm directly provides a client with both legal and nonlegal services that are "so closely entwined that they cannot be distinguished from each other" (EC 1-9), then the nonlegal services are always subject to the Disciplinary Rules, including the conflict of interest rules. When either a law firm itself or an affiliated entity provides a person with nonlegal services that the law firm considers distinct from any legal services offered by the law firm, the law firm should always explain to the recipient that the services "are not legal services and that the protection of an attorney-client relationship does not exist with respect to the nonlegal services...." A law firm that does not issue such a disclaimer regarding nonlegal services must either scrupulously abide by the Disciplinary Rules or bear the risk of a reasonable recipient's confusion.

Roy Simon is a Professor of Law and Director of the Institute for the Study of Legal Ethics at Hofstra University School of Law and the author of Simon's New York Code of Professional Responsibility Annotated, published annually by West. The 2001 edition is now available.