

Screens And Conflicts In The Second Circuit

BY ROY SIMON

Last month's column focused on a new Second Circuit case, *Hempstead Video, Inc. v. Incorporated Village Of Valley Stream*, 2005 WL 1274244 (2d Cir. May 31, 2005) (Leval, J.), which rejected the conventional wisdom that an "of counsel" lawyer's conflicts are automatically imputed to the firm to which the lawyer is "of counsel." This month's column focuses on another question revisited in *Hempstead Video*: Can screens (a/k/a "Chinese Walls") overcome an imputed disqualification?

To recap the *Hempstead Video* case briefly: in 1994 Hempstead Video (an "adult shop") sued the Village of Valley Stream to force the Village to grant Hempstead Video a permit to open its store. The case settled in 1996 when the Village agreed to grant Hempstead Video a permit on the condition (among others) that the store would not have any "enclosed viewing rooms, live peep shows or live performances" at the premises. In 2003, the Village received an anonymous tip that Hempstead Video had installed enclosed viewing rooms, and the Village returned to court to shut them down. The Village was represented by the Garden City law firm of Jaspán Schlesinger Hoffman.

During the litigation, a solo practitioner named William Englander became "of counsel" to the Jaspán firm. Englander had represented Hempstead Video in labor matters for twenty years. Englander was not involved in Hempstead Video's litigation against the Village about "enclosed viewing rooms," but he was helping to defend Hempstead Video against an employment discrimination complaint, so Hempstead Video was one of Englander's current clients. When Hempstead Video became aware that Englander had become "of counsel" to the Jaspán firm, it moved to disqualify the Jaspán firm.

Magistrate Judge Thomas Boyle, who was presiding over the litigation, denied Hempstead Video's motion to disqualify the Jaspán firm, concluding that Englander was affiliated only "loosely" with the Jaspán firm, and in a manner "too attenuated to merit imputation of the conflict of interest." The case then proceeded to final judgment on the merits in favor of the Village.

Hempstead Video appealed both the judgment on the merits and the denial of its motion to disqualify. The Second Circuit affirmed on both grounds. In analyzing the disqualification question, the Second Circuit divided the analysis into two steps:

The first step in that framework is to determine whether an attorney is "associated" with the firm. If he is, a rebuttable presumption arises that the attorney and the firm share client confidences, and the court then proceeds to the second step, which involves determining whether that presumption has been rebutted.

In last month's column, I quoted the essence of the court's holding on the first issue. Rejecting a per se rule that would automatically impute an "of counsel" lawyer's conflicts to the firm, the court said:

We believe the better approach for deciding whether to impute an “of counsel” attorney’s conflict to his firm for purposes of ordering disqualification in a suit in federal court is to examine the substance of the relationship under review and the procedures in place. The closer and broader the affiliation of an “of counsel” attorney with the firm, and the greater the likelihood that operating procedures adopted may permit one to become privy, whether intentionally or unintentionally, to the pertinent client confidences of the other, the more appropriate will be a rebuttable imputation of the conflict of one to the other. Conversely, the more narrowly limited the relationship between the “of counsel” attorney and the firm, and the more secure and effective the isolation of nonshared matters, the less appropriate imputation will be. ...

This month, I am focusing on the second issue: When an “of counsel” lawyer’s conflicts are imputed to the firm, can screening rebut the presumption that the “of counsel” lawyer has shared confidences and secrets with the firm? The Second Circuit’s answer is quite surprising.

Background: Screening in the New York Code of Professional Responsibility

The starting point for analyzing whether screens can avoid imputed disqualification is DR 5105 (D) of the New York Code of Professional Responsibility, which provides as follows:

While lawyers are associated in a law firm, none of them shall knowingly accept or continue employment when any one of them practicing alone would be prohibited from doing so under DR 5101(A), DR 5105(A) or (B), DR 5108(A) or (B), or DR 9101(B) except as otherwise provided therein.

According to a literal reading of DR 5105(D), if any lawyer in a firm is disqualified due to a conflict with another current client under DR 5105, then no lawyer associated with the firm may begin or continue employment in that matter. This rule of imputation is animated by policies of loyalty and confidentiality. If the interests of Client A conflict with the interests of Client B, then Client A may hesitate to share confidences and secrets with the firm, and may worry that the firm will not serve him with total loyalty.

When the conflict is with a former client rather than another current client, firms often try to avoid disqualification by setting up a screen between the disqualified lawyer and the rest of the firm. However, DR 5105(D) itself says nothing about screens. In contrast, DR 9101(B), which governs conflicts arising from a lawyer’s former work as a public officer or employee, expressly allows a law firm to avoid imputed disqualification if the former government lawyer is “effectively screened from any participation.” Moreover, the imputed disqualification rules of many jurisdictions expressly permit screens to cure conflicts with former clients in substantially related matters. For example, the imputed disqualification rules of Illinois, New Jersey, and Pennsylvania (among others) permit a law firm to oppose the former client of a laterally hired lawyer as long as the laterally hired lawyer is promptly and effectively screened.

Because New York’s imputed disqualification rule, DR 5105(D), does not mention screens, a law firm that wishes to avoid imputed disqualification in a New York state or federal court has to persuade a court to deny disqualification despite the literal language of DR 5105(D).

The Brief History of Screening in the Second Circuit

The Second Circuit has never definitively analyzed the efficacy of screens in curing conflicts of interest. However, the court has sometimes made cryptic remarks rejecting screens, and these remarks have proved highly influential.

In *Fund of Funds, Ltd. v. Arthur Andersen & Co.*, 567 F.2d 225 (2d Cir. 1977), the law firm of Morgan, Lewis & Bockius helped a lawyer named Robert Meister and his firm investigate and prepare a securities fraud suit against Arthur Andersen. Morgan Lewis lawyers sorted out documents relating to Andersen, gave legal opinions concerning possible Andersen defenses, attended meetings in which the suit against Andersen was discussed, and reviewed the Andersen complaint before it was filed. Because Andersen was a current client of Morgan Lewis in various matters unrelated to Fund of Funds, however, Morgan Lewis made it a policy that “no attorneys involved with Andersen matters would work on the Fund of Funds case.” When the suit was filed, Andersen moved to disqualify Meister and his firm on grounds that they were tainted by Morgan Lewis’s conflict. Morgan Lewis argued that it had built a “Chinese Wall” to isolate the lawyers in the firm who represented Andersen. The district court found Morgan Lewis’s involvement troublesome, but concluded that it was “highly unlikely” that any of Andersen’s confidential information could have been disclosed and therefore refused to disqualify Meister and his firm. On appeal, the Second Circuit reversed and ordered disqualification. Morgan Lewis did not pursue the Chinese Wall argument on appeal, but in a footnote the Second Circuit said:

Morgan Lewis argued below that it built a Chinese Wall within the firm and that no information passed between the two groups of attorneys and thus that no confidential information was disclosed. The court below found that no such “Chinese Wall” could be created in a single firm. We incline to agree.

Three years later, in *Cheng v. GAF Corp.*, 631 F.2d 1052 (2d Cir. 1980) (“*Cheng*”), *vacated on other grounds*, 450 U.S. 903 (1981), an attorney had essentially changed sides during the progress of a lawsuit. The side switching attorney’s former firm, which represented the plaintiff, was a “tiny office” with only four to six attorneys. His new firm, which represented the defendant, was also a “small office” with about twenty lawyers. When the plaintiff moved to disqualify the defense firm, the defense firm argued that disqualification was not warranted because the firm had set up a Chinese Wall. Specifically, the defense firm argued that the side switching lawyer had been assigned to the firm’s health law area, whereas the suit alleging employment discrimination was being handled by the firm’s employment law section. Other lawyers in the defense firm submitted affidavits swearing that the side switching attorney had not disclosed the plaintiff’s confidences or discussed the merits of the case, thus effectively rebutting any taint. The district court accepted the argument and denied disqualification, but the Second Circuit disagreed. Perceiving too high a risk that the moving lawyer would inadvertently disclose the plaintiff’s confidences and secrets, the Second Circuit said it was “not satisfied that under the facts of this case the screening will be effective.” Thus, based on DR 5105(D), the Second Circuit ordered the district court to disqualify the entire firm.

Reading Tea Leaves

For nearly a quarter of a century, *Fund of Funds* and *Cheng* were among the only Second Circuit decisions available to guide lawyers and lower courts regarding the efficacy of screens in conflict situations. The

dearth of decisions resulted from a trilogy of United States Supreme Court decisions in the early 1980s holding that rulings on motions to disqualify were not appealable. See *Firestone v. Risjord*, 449 U.S. 368 (1981) (an order *denying* a motion to disqualify in a civil case is not an appealable “final decision”); *Flanagan v. United States*, 465 U.S. 259 (1984) (an order *granting* a motion to disqualify opposing counsel in a criminal case was not an appealable “final order” and did not meet the conditions for an interlocutory appeal); and *RichardsonMerrell, Inc. v. Koller*, 472 U.S. 424 (1985) (an order *granting* a motion to disqualify opposing counsel in a civil case cannot be appealed until trial is over).

Consequently, the Second Circuit was silent about screening from the mid-1980s until it decided *Hempstead Video* in May of this year. But that is only one reason that the *Hempstead Video* opinion is so significant. The other reason is that the opinion marks a radical departure from conventional wisdom about screens.

The conventional wisdom about screens is reflected in various federal district court decisions that have rejected screens as an antidote to conflicts, especially in relatively small firms. The opinion in *Hempstead Video* cited four such cases: *Young v. Central Square Central School District*, 213 F. Supp. 2d 202, 217 (N.D.N.Y. 2002) (Second Circuit “has expressed consistent skepticism about screening as a remedy for conflicts of interest and declared that such procedures ultimately must be rejected if they are subject to doubt,” and the New York Code of Professional Responsibility “does not recognize the use of screening devices except in cases involving former government lawyers or judges.”); *Mitchell v. Metropolitan Life Insurance Co.*, 2002 WL 441194 (S.D.N.Y. 2002) (same); *Marshall v. State of N.Y. Division of State Police*, 952 F. Supp. 103, 112 (N.D.N.Y. 1997) (the relatively small size of the Ruberti Firm – approximately 15 lawyers – “raises doubts that even the most stringent screening mechanisms could have been effective”); *Baird v. Hilton Hotel Corp.*, 771 F. Supp. 24, 25, 27 (E.D.N.Y. 1991) (nine lawyer firm’s Chinese Wall around lateral lawyer was not effective because the firm was “smaller than the firm in the *Cheng* case and the measures taken to insulate her are no more stringent,” plus, “as in *Cheng*, this case is ongoing and accordingly the danger of disclosure continues,” and “in her daily contacts with plaintiffs’ counsel there remains a danger of inadvertent disclosure”).

But all of these cases granted motions to disqualify brought by *former* clients of the disqualified lawyer’s law firm, and all of these cases rejected arguments by the disqualified firm that a screen was sufficient to overcome the former client’s objection to the conflict. None of these cases considered whether screening could ever be sufficient to overcome a current client’s objection to being opposed by its own law firm. *Hempstead Video* is the first Second Circuit case to accept screening in the context of a concurrent conflict – and it thus raises questions about a bedrock principle of conflicts doctrine: a law firm may not oppose a current client without that client’s informed consent. That principle has been a fixture of conflicts analysis for nearly three decades, ever since *Cinema 5 Ltd. v. Cinerama, Inc.*, 528 F.2d 1384, 1386 (2d Cir. 1976) (cited in *Hempstead Video*), which held that it is “prima facie improper” for a law firm to oppose the firm’s own current client in any matter, even a totally unrelated matter.

The facts of *Cinema 5* are worth studying. In *Cinema 5*, a lawyer named Manly Fleischmann was a name partner in two different law firms – Jaeckle, Fleischmann and Mugel of Buffalo and Webster, Sheffield, Fleischmann, Hitchcock and Brookfield in New York City. When Fleischmann’s New York City firm brought suit against an “actively represented” current client of his Buffalo firm (Cinerama), Cinerama moved to disqualify the New York firm. The district court granted the motion and the Second Circuit affirmed, finding a breach of the firm’s fiduciary duty of “undivided loyalty” to its client. In a footnote

dismissing the utility of screening in such a situation, the court said it was “confident” that Mr. Fleischmann “would make every effort to disassociate himself from both lawsuits and would not divulge any information that came to him concerning either,” but the court “cannot impart this same confidence to the public by court order.”

Ever since *Cinema 5*, Second Circuit case law has set forth “a *per se* rule of disqualification when an attorney is representing one client in a litigation against another current client.” *Sumitomo v. J.P. Morgan & Co.*, 2000 WL 145747 (S.D.N.Y.2000).

In my view, what makes the decision in *Hempstead Video* remarkable is that – despite the Second Circuit’s consistent *per se* rule tracing back to *Cinema 5* – the court approved a screen as an antidote to a *concurrent* conflict. *Hempstead Video* was not a former client of Englander’s, but rather was one of his current clients. The Jaspan firm was opposing *Hempstead Video* in pending litigation against the Village of Valley Stream. Everyone understood that if *Hempstead Video* was a current client of the Jaspan firm, then the rule announced in *Cinema 5* would prohibit Jaspan Schlesinger from opposing its own current client. Yet the Second Circuit refused to disqualify the Jaspan firm. The primary holding, as discussed above, was that Englander’s limited “of counsel” affiliation with the Jaspan firm was “too attenuated to merit imputation of the conflict of interest.” But the Second Circuit went on to reach an alternative holding that is extraordinary. Even assuming that Englander’s potential conflict *was* imputed to the Jaspan firm, the Jaspan firm had rebutted the presumption of shared confidences and its disqualification was not warranted because (a) Englander’s association with the Jaspan firm was “limited,” (b) the Jaspan firm had put “screens” in place to protect *Hempstead Video*’s client confidences, and (c) both Englander and the lead lawyer from Jaspan Schlesinger had submitted “uncontroverted affidavits” swearing that they had not exchanged any confidential information about the Valley Stream case.

The Second Circuit reached its holding in *Hempstead Video* by focusing on first principles. The authority of the federal courts to disqualify attorneys derives from their inherent power to “preserve the integrity of the adversary process.” In analyzing disqualification motions, a court attempts to balance “a client’s right freely to choose his counsel” against “the need to maintain the highest standards of the profession.” Thus, although ethics rules like DR 5105 (D) provide guidance, disqualification is warranted only where an attorney’s conduct tends to “taint” the underlying trial.

The Second Circuit also had its eye on developments in other circuits. “Although some courts have treated the presumption that confidences are shared within a firm as irrebuttable,” Judge Leval wrote, “there is a ‘strong trend,’ which we join, toward allowing the presumption of confidence sharing within a firm to be rebutted.” Thus, the court concluded:

We see no reason why, in appropriate cases and on convincing facts, isolation—whether it results from the intentional construction of a “Chinese Wall,” or from *de facto* separation that effectively protects against any sharing of confidential information—cannot adequately protect against taint. ...

Thus, the court not only indicated that Chinese Walls might sometimes avoid disqualification when a law firm sued one current client on behalf of another; the court also stated squarely that it would sometimes approve “*de facto* separation” in the absence of a formal Chinese Wall.

Applying this approach to the particular facts of the *Hempstead Video* case, the Second Circuit was satisfied that disqualification of the Jaspan firm was unwarranted. The court stressed that Englander was “of counsel” to the Jaspan firm only with regard to a few specific cases, and that he remained “independent of the Jaspan firm” as to all other matters. Specifically, Englander “maintained separate files and shared no confidences relating to his representation of [Hempstead Video] with Jaspan.” Moreover, Englander and Jaspan had each adopted “measures” as soon as they learned of the potential conflict to “protect against any breach”

Thus, the court was “satisfied that any presumption of shared confidences that may arise by operation of law has been sufficiently rebutted,” and the court concluded that the Jaspan firm’s continued representation of Valley Stream was “free of disqualifying taint.”

Revolutionary Approach

The *Hempstead Video* approach is revolutionary. It is unlike any previous case decided by courts in the Second Circuit. New York courts have never approved screens to protect one current client from opposing another current client absent that client’s consent.

The policy reason for not allowing screens to cure conflicts with current clients is strong. When the client moving for disqualification is a current client of the firm, rather than a former client, the client is presumably continuing to communicate confidential information to the firm in order to obtain competent representation in ongoing matters. A current client therefore needs to have absolute trust that the information it communicates to the firm will not be passed on (whether deliberately or accidentally) to other lawyers in the firm who could use the information against the current client in another matter. Otherwise, the current client will clam up and withhold potentially important information out of fear that communicating that information will boomerang.

Moreover, even in situations where courts have been willing to consider screens, they have ordinarily insisted on formal screening measures, not merely a “*de facto*” separation. See, e.g., *Mitchell v. Metropolitan Life Insurance Co.*, *supra* (“to rebut the presumption, the screening measures must have been established from the first moment the conflicted attorney transferred to the firm or, at a minimum, when the firm first received actual notice of the conflict”). The Second Circuit’s apparent tolerance of “*de facto* separation” lowers the bar. A firm fighting disqualification can now argue that the lawyer linking two firms works in another office, or on a different floor, or in a different department of the firm, or has his own independent practice, or is otherwise physically separated from the confidences and secrets of the client moving to disqualify.

Is Cinema 5 Dead? Are Screens Alive?

What would happen if a case resembling *Cinema 5* came before the Second Circuit today? Would it come out the same way that it did in 1976, or would it come out as *Hempstead Video* did in May of this year? That is an interesting question, because in both cases the firm opposing a current client was linked to the firm representing the current client by a single lawyer – William Englander in the *Hempstead Video* case, and Manly Fleischman in *Cinema 5*.

If I were a law firm fighting disqualification on facts similar to *Cinema 5*, I would make three arguments. First, I would argue that the linking lawyer (the common partner or “of counsel” lawyer) has only a

“limited” relationship with our firm, working only on specified cases and playing no role in the case that is the subject of the disqualification motion. Next, I would argue that our firm built a solid Chinese Wall as soon as we discovered the conflict, and that even before the wall was built there was “*de facto* separation.” Finally, I would seek out affidavits from the lawyers representing our current client and from the lawyers opposing that same client swearing that they had not shared any confidential information about that client.

Will those arguments work? Frankly, I doubt it. *Hempstead Video* presented unusual facts, and ordering disqualification would have required the district court to go back to square one in the litigation, with little likelihood of a different outcome. (I have not discussed the underlying merits of *Hempstead Video*, but it was not a close case and the outcome would presumably have been the same no matter what law firm opposed *Hempstead Video*.)

But we can be sure those arguments will be made. Doors that we thought were closed now appear to be open, or at least unlocked. Large firms with offices in multiple cities will trot out *Hempstead Video* to overcome conflicts that are based on relatively minor representations by a partner in another city who has little or no contact with the office fighting disqualification. Small firms will cite *Hempstead Video* to fight disqualification based on an association with an “of counsel” lawyer whose relationship barely rises above a pure referral relationship. Firms that spot conflicts at the outset of a lucrative potential new matter will opt to build Chinese Walls rather than decline the representation. And firms that fail to detect conflicts will argue (when the opposing party moves to disqualify them) that the lack of a formal Chinese Wall is irrelevant because there is “*de facto* separation that effectively protects against any sharing of confidential information.”

Of course, opening these doors is not necessarily a tragedy. From time to time, it is healthy to reexamine the basic premises of legal ethics and either rejects them because they are flawed or embrace them with renewed vigor because they are sound. In any event, there is room for people of good faith to differ on issues relating to conflicts of interest. As Chief Judge Kaufman said in *Fund of Funds*, “Compliance or noncompliance with Canons of Ethics frequently do not involve morality or venality, but differences of opinions among honest men over the ethical propriety of conduct.” Indeed, in Texas and Alaska, the rules of professional conduct allow a law firm to oppose a current client without that client’s consent in any matter not substantially related to the matters in which the law firm represents the client.

But reexamining basic premises and arguing about the policies and factual assumptions undergirding our conflict of interest rules will take time. In the meantime, until another disqualification ruling satisfies the demanding criteria needed for an appeal to the Second Circuit, lawyers and district courts in the Second Circuit are going to be very busy remapping the conflicts terrain reshaped by *Hempstead Video*.

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