Ethical Coffee Break no. 8 (October 2011)

NATIONAL

ABA Ethics 20/20 Commission proposals to remove some more barriers to cross-border practice

The ABA Commission on Ethics 20/20,[1] in a way picking up where the Commission on Multijurisdictional Practice left off in 2002[2] issued its latest series of draft proposals for comment. The proposals[3] largely focus on how ethics rules should be amended to make it easier for US lawyers to engage in cross-border practice. The Commission will produce final versions of the draft proposals prior to submitting them to the ABA's policy-making House of Delegates for consideration in August at the association's 2012 ABA Annual Meeting in Chicago.

In particular, the proposals of modification of the Model Rules are: (1) Amendment to Rule 5.5 of extending the possibility to practice outside their jurisdiction to foreign lawyers; (2) Amendment of Model Rule 1.6 to permit a lawyer moving to a new firm to disclose – subject to a number of restrictions -- confidential information about current and former clients to a reasonably necessary extent to determine if a conflict of interest would arise if the lawyer associates with the firm; (3) Addition of a new comment to Model Rule 1.7 describing circumstances under which a client and lawyer may, in cases involving more than one jurisdiction, choose which jurisdiction's conflict of interest rules will apply.

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[1] The commission was created in 2009 to consider the impact of technology and globalization on professional conduct rules for lawyers and to develop recommendations to modify those rules where appropriate.

[2] The House of Delegates adopted many of the Commission on Multijurisdictional Practice's recommendations. The measures -- largely incorporated into the Model Rules and widely adopted at the state level -- allowed lawyers to temporarily practice in jurisdictions in which they are not licensed, and to seek admission by motion and identified circumstances under which foreign lawyers may practice temporarily in the United States.

[3] Texts available at www.americanbar.org/groups/professional responsibility/aba_commission_on_ethics_20_20/initial_proposals.html

The proposal for modification of the Model Rule on Admission by Motion modifies the rule by decreasing from five to three years the time in which the lawyer must have engaged in active practice of law.

The Ethics 20/20 Commission plans to issue one further draft recommendation on the subject of alternative business structures for law firms. The proposal would contain a permission for nonlawyers to have very limited ownership interests in law firms in the way in which the District of Columbia has allowed for more than 20 years (but with more restrictions aimed at ensuring lawyer's control and client's protection.)

SOUTH CAROLINA

The SC Supreme Court reaffirms that whether a fiduciary relationship exists between two classes of persons is a question of law. The Court also held that fiduciary duties created by an attorney-client relationship may be breached even though the formal representation has ended.

On October 18, 2011, the SC Supreme Court while reaffirming that whether a fiduciary relationship exists between two classes of persons is a question of law, held that a lawyer owes a fiduciary duty also to former clients and not only to current clients.

These are the (somewhat simplified) facts of the case: On August 2001, when her husband (Congressman Floyd D. Spence) was hospitalized and was not expected to survive, Mrs. Spence sought legal counsel with regards to her husband's assets, to her inheritance rights, and to her rights in his estate. Wingate undertook representation of Mrs. Spence and advised her that, notwithstanding a codicil that her husband had executed bequeathing her several properties, she was entitled to nothing from her husband's estate and that she was barred from receiving an elective share by a prenuptial agreement. Wingate advised Mrs. Spence to enter into an agreement with Mr. Spence's four adult children to create a trust for her benefit. Wingate negotiated the agreement, and the parties formally entered into an agreement on or around August 15, 2001. The agreement provided for a trust to be created and funded from one-third of the value of Mr. Spence's probate estate. On August 16, 2001, Congressman Spence died. Sometime between August 23, 2001 and the start of September 2001, Wingate informed Mrs. Spence that Wingate

had agreed to represent the estate and that she no longer needed an attorney. He never informed her of any potential conflict of interest that he had in representing the estate, nor did he seek her consent to, or a waiver of, any conflict of interest. Some time later, Mrs. Spence came to believe that the amount she had received under the agreement was much less than what she was entitled to under the will and codicil or if she had opted for an elective share.

She met with her late husband's children and Wingate to find a solution and to talk about the $500,000 benefits from a Federal Group Life Insurance Policy held by her late husband that she claimed her husband wanted to devise to her alone. She tried to hire again Wingate to protect her interest but he refused. Mrs. Spence brought a lawsuit to set aside the agreement creating the trust. Wingate withdrew as counsel for the estate in August 2002, around the time of this lawsuit. The trust agreement was eventually set aside.

Mrs. Spence brought a lawsuit against Wingate alleging several causes of action, among which breach of fiduciary duty for failing to disclose any potential conflict of interest and failure to either obtain her waiver of this conflict or to protect her interests in general and with particular regard to the insurance policy (Wingate never advised her that she needed to take any action to protect her rights with regard to the policy or said that she needed to hire a different lawyer.)[4]

The circuit court granted partial summary judgment to Wingate, finding as a matter of law that Wingate did not owe any fiduciary duties in regard to the insurance issue.[5] Mrs. Spence appealed. The Court of Appeals reversed and remanded, holding that summary judgment was inappropriate because a genuine issue of material fact existed as to what, if any, fiduciary duties were owed and whether those duties were breached.[6] The South Carolina Supreme Court granted Wingate's petition for a writ of certiorari. The Supreme Court, first

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[4] Mrs. Spence claimed that she was the only beneficiary of the proceeds of the $500,000 life insurance policy and that Wingate breached a fiduciary duty towards her on this issue because they discussed the insurance issue with her during the course of the representation.

[5] The court relied upon section 62-1-109 of the South Carolina Code and found Wingate owed no fiduciary duty to Mrs. Spence as a mere beneficiary of the estate, obviously ignoring that Mrs. Spence was a former client and not only a beneficiary of the estate.

[6] "Duties to a former client on a related matter are separate and distinct from any duties arising from Wingate's representation of the estate; therefore, the circuit court erred in finding section 62-1-109 of the South Carolina Code absolved Wingate of any duty he owed to [Mrs. Spence]"

noted that Section 62-1-109 of the South Carolina Code was not applicable.[7] Second, in deciding the issue of the existence of a fiduciary duty, held that "[a] fiduciary relationship exists when one reposes special confidence in another, so that the latter, in equity and good conscience, is bound to act in good faith and with due regard to the interests of the one reposing confidence" (*O'Shea v. Lesser,* 416 S.E.2d 629, 631 (1992)) and that an attorney-client relationship is, by its very nature, a fiduciary relationship.[8] Third, the Supreme Court found that the Court of Appeals had wrongly relied on *Hotz v. Minyard*, 403 S.E.2d 634 (1991) to hold that the existence of a fiduciary duty is a question of fact[9] and reversed the Court of Appeals on this point. The Supreme Court affirmed the reversal of the summary judgment "because a question of fact exists as to whether Wingate *breached* a fiduciary duty to Mrs. Spence." The Court held that it was undisputed that attorneys owe fiduciary duties to existing clients and that fiduciary duties created by an attorney-client relationship may be breached even though the formal representation has ended.[10] The Supreme Court concluded that "Wingate owed a fiduciary duty to his former client, Mrs. Spence" and that "[t]his duty included, among other obligations, the obligation

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[7] In the decision the Court dismissed the relevance of Section 62-1-109 because (1) Section 62-1-109 was not applicable because the benefits from insurance are not a part of the estate and (2) Section 62-1-109 … "is not determinative of whether Mrs. Spence is owed a fiduciary duty as a former client."

[8] The Court cited to *Hendricks v. Clemson Univ.,* 578 S.E.2d 711 (2003); *Hotz v. Minyard,* 403 S.E.2d 634 (1991); *In re Green*, 354 S.E.2d 557 (1987); *Royal Crown Bottling Co. v. Chandler,* 83 S.E.2d 745 (1954); *Wise v. Hardin*, 5 S.C. 325 (1874); *Weatherford v. Price*, 532 S.E.2d 310 (Ct. App. 2000).

[9] In fact, *Hotz* "did not state that whether a fiduciary duty is owed is a question of fact." The Supreme Court specified that the issue had already been clarified in *Hendricks v. Clemson Univ.,* 578 S.E.2d 711 (2003): "The determination of the existence of a duty is solely the responsibility of the court. Whether the law recognizes a particular duty is an issue of law to be decided by the Court."

[10] The Court refused Wingate's argument that an attorney's duty to a former client is limited to the requirements of Rule 1.9. The Court cited to its own precedent to state that "[a]n affirmative legal duty exists only if created by statute, contract, relationship, status, property interest, or some other special circumstance." (*Hendricks*, 578 S.E.2d at 714 (emphasis added).

not to act in a manner adverse to her interests in matters substantially related to the prior representation."[11]

A large disproportion between legal fees paid by the client and the settlement amount that the client actually receives may be the basis of a malpractice action.

On October 20, 2011 a U.S. District Judge ruled against a Charleston attorney ("Attorney") finding actual damages of $782,714 and $1 million in punitive damages.

The underlying dispute dates to February 2006 when Florida businessman Jack Tuttle of Tuttle Dozer Works bought a mobile piece of forestry equipment from a South Carolina company. Tuttle contended that the tree cutter did not work properly and sued Gyro-Trac. Tuttle hired Attorney to represent him. Exorbitant bills from Attorney started to pile up ($665,000 in litigation costs) and Tuttle was forced to accept a settlement that was not profitable. In addition, of the total agreed settlement of $700,000, Tuttle received only approximately $198,000.

Tuttle sued Attorney and the jury agreed that legal malpractice and negligent misrepresentation were involved.

NEW YORK

When law firms are the victims of wire transfer frauds, they must bear the loss.

On October 13, 2011 in Greenberg, Trager & Herbst, LLP. v. HSBC Bank, the NY Court of Appeals decided a new scam case involving lawyers.

In September 2007 a partner of Greenberg, Trager and Herbst, LLP ("Law Firm") received an e-mail from a representative of Northlink Industrial Limited ("Northlink"), a Hong Kong company. The e-mail stated that Northlink was looking for legal representation to assist in the collection of debts owed by American customers. When Law Firm requested a $10,000 retainer, NorthLink

[11] The Court affirmed the decision of the Court of Appeals for the part that held that "whether Wingate breached a duty regarding the congressional life insurance policy is a question of fact for a jury to determine".

informed Law Firm that a Northlink's customer had sent a payment to Law Firm and that Law Firm could take its retainer from it. A Citibank check for $197,500 was in fact received and Law Firm was instructed, via e-mail, to keep $10,000 as a retainer and to remit the balance to Northlink. On Friday, September 21, 2007, Law Firm deposited the check into its attorney trust account at HSBC. The next business day, Monday, September 24th, HSBC account reconciliation department processed the check and provisionally credited Law Firm's account for $197,750. HSBC presented the check for payment through the Federal Reserve Bank. The check was "administratively returned" to HSBC, i.e. returned for reasons other than dishonor, such as a damaged or illegible routing number. Because HSBC assumed there was a problem with the routing number, HSBC repaired it by utilizing the partial routing number located on the top right hand corner of the check and on September 26, 2007 resubmitted the check electronically for reprocessing. HSBC never informed Law Firm of the "administrative return" of the check. On September 27, 2007, a Law Firm partner called a representative of HSBC inquiring as to whether the check had "cleared" and if the funds were available for disbursement. Because Law Firm was informed that the funds were available, Law Firm took its retainer and wired $187,500 from its account to Hong Kong. On September 28, 2007, HSBC confirmed to Law Firm that the wire transfer had been consummated. On October 2, 2007, after HSBC received notice from Citibank that the check was being dishonored as "RTM [return to maker] Suspect Counterfeit", HSBC informed Law Firm that the check had been dishonored. HSBC then revoked its provisional settlement and charged back Law Firm's account.

On October 17, 2007, Law Firm brought suit against HSBC and Citibank.[12] The Supreme Court dismissed the complaint in its entirety and held that HSBC had no duty under the UCC to inform Law Firm that the check had been "administratively returned" on September 25th. The Appellate Division affirmed on the same ground. The Court of Appeals affirms (6-1).

The Court rejected the claim in negligence against Citibank because no duty was owed to Law Firm by Citibank being Law Firm not a Citibank's

[12] Law Firm sued in conversion and conspiracy, negligence and negligent misrepresentation by HSBC for failure to inform Law Firm that the check had been returned and dishonored on September 25, and for informing Law Firm over the phone that the funds had "cleared" and were available for disbursement; and negligence by Citibank for failing to detect that the check was counterfeit when it was presented the first time.

customer[13] and rejected also the two claims of negligent misrepresentation and of negligence against HSBC.

> [L]iability for negligent misrepresentation has been imposed only on those persons who possess unique or specialized expertise, or who are in a special position of confidence and trust with the injured party such that reliance on the negligent misrepresentation is justified . . [T]he relationship between a bank and its depositor is one of debtor and creditor" . . . and an arms length borrower-lender relationship . . . does not support a cause of action for negligent misrepresentation.

While the Court did not exclude that negligent misrepresentation might rely different aspects,[14] the Court categorically excluded that the conversation with the employee ("the check has cleared") gave rise to a right to recover from HSBC,

> [Law Firm]'s claim is based on the alleged oral statement by the HSBC representative that the check had "cleared" — an ambiguous remark that may have been intended to mean only that the amount of the check was available (as indeed it was) in [Law Firm]'s account. Reliance on this statement as assurance that final settlement had occurred was, under the circumstances here, unreasonable as a matter of law.

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[13] The court held:

> The duty of a payor bank (in this case Citibank) to a non-customer depositor of a check is derived solely from UCC 4-301 and 4-302. . . . In short, the only duty Citibank owed GTH was to pay the check, return the check or send notice of dishonor of the check by midnight of the next banking day after receiving the check. It is uncontroverted that Citibank returned the check within its midnight deadline.

[14] To resolve this case, we do not need to decide whether the relationship between GTH and

> HSBC would preclude all possible claims for negligent misrepresentation, but it is clear that the claim GTH asserts here cannot succeed, even accepting as true, as we must at this stage of the litigation, GTH's version of the conversation with the representative at HSBC.

The Court also rejected Law Firm's contention that "pursuant to UCC 4-201, HSBC was an agent of GTH during the period that HSBC was acting as a collecting bank for plaintiff."[15]

As for Law Firm's claim of negligence against HSBC based on HSBC's alleged duty to inform its customer when the check was first returned marked "sent wrong" on September 25th, the Court held that

> [T]he duty a collecting bank owes to a depositor is that of ordinary care in handling the item (*see* UCC 4-202). The UCC does not define "ordinary care," but it should be read as to have its normal tort meaning . . . The record demonstrates that HSBC acted with ordinary care . . . By showing that it acted in accordance with general banking rules or practices, a bank can ensure that its conduct at least prima facie meets an ordinary care standard.

Law Firm did not have better luck in equity. The Court refused to grant an equitable estoppel because in its view Law Firm "was in the best position to guard against the risk of a counterfeit check by knowing its 'client'.'

We will not comment on the correctness of the decision under a UCC perspective (let's only say that the mechanical application of the UCC provision to the facts of this case, reminds us a lot of the old Latin brocard "vigilantibus non dormientibus jura subveniunt" - law will help those who are vigilant not those who sleep-). We will comment instead on the proper ethical conduct that a lawyer must keep regarding the trust account.

It is the lawyer's responsibility to make sure that the funds are available before disbursing them from its trust account.

On one hand, a lawyer should be able to rely upon representation by his

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15 Although an agent owes a duty to its principal to disclose all material facts that come to its knowledge regarding the scope of the agency (*see Kirschner v KPMG LLP*, 15 NY3d 446, 480 [2010]), the purpose of UCC 4-201 is not to impose a fiduciary duty on a collecting bank. We have interpreted the statute such that the use of the term "agent" means that the item and any inherent risk in that item remains with the depositor and not the collecting bank (*see Hanna v First Natl. Bank of Rochester*, 87 NY2d 107, 119 [1995].

bank that the funds are available in its account. But probably a lawyer should not accept a vague statement as "the check has cleared" as a green light to the disbursement.

On the other hand, it is probably not a good practice for lawyers to take their retainer from a larger check that has nothing to do with the transaction that they are conducting for their clients. A lawyer should not accept to transit a check in his or her trust account to "cash" the check and keep part of it as a retainer. This conduct exposes the law firm to collection risks and it is not practice of law to begin with.

AROUND THE COUNTRY

Again on civility. This time we talk about judicial civility.

We have already spoken a couple of times of civility in the profession. While some courts have recently been sanctioning lawyers for having been uncivil[16] and the U.S. Supreme Court Justice Stephen G. Breyer's speech at the Opening Assembly of the ABA Annual Meeting in Toronto called for civility, better education and respect for the Rule of Law,[17] a U.S. District Judge of Texas was recently criticized by the Chief Judge Edith Jones of the 5th U.S. Circuit Court of Appeals. The District Judge in question had written a series of orders that condemned the conducts and even the competency of lawyers appearing before him. First, he had invited two quarrelling lawyers to go to a "kindergarten party" to learn discovery skills. Then, he had called another lawyer "anything but competent".

In an email to this District Judge, Judge Jones said that "this kind of rhetoric is not funny" and that "[i]n fact, it is so caustic, demeaning and gratuitous that it casts more disrespect on the judiciary than on the now-besmirched reputation of the counsel."

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[16] See Ethical Coffee Break no. 3. The South Carolina Supreme Court has recently sanctioned two lawyers for being uncivil. *In the matter of Anonymous Member of the South Carolina Bar*, Opinion No. 26964, filed on April 25, 2011; *In the Matter of William Garry White, III*, No. 26939 filed March 7, 2011.

[17] See Ethical Coffee Break no. 3 and 5.

We think that Judge Jones' s was a collegial and appropriate way for an appellate judge to express concern for the conduct of a district judge without instituting any kind of formal inquiry. Unfortunately Judge Jones' email was somehow leaked and it became public.

We do not disagree with Judge Jones but we have a somewhat different concern. One can understand how a judge like the above District Judge can become annoyed, angry and impatient with motions that they believe border on the frivolous. Especially when the judges feel that those motions have a media attention purpose. And we can understand also why a judge does not want to institute formal disciplinary proceedings because they are time consuming and detract from the important judicial functions of deciding the merits of cases. However, court orders that are in substance a public reprimand of attorneys should be used sparingly, as ever, because they amount to discipline of lawyers without opportunity to respond.