LEGAL PRACTITIONERS' LIABILITY COMMITTEE

Keeping out of the line of fire: managing conflicts of interest

Acknowledgements

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Introduction

This presenter's workbook is designed to help facilitate a training session for lawyers focusing on professional indemnity claims involving conflicts of interest and how to avoid them.

This video will challenge participants to assess whether they are doing enough to manage conflicts exposure. They will have the opportunity to:

- refresh their understanding of conflicts obligations and consequences
- learn more about conflicts risk in the context of indemnity claims
- reflect on their conflicts risk factors, processes and habits
- identify steps they might take to reduce their conflicts exposure such as:
    - identifying areas of conflicts risk and their policy on risk taking
    - screening new work to identify conflicts issues for consideration
    - deciding what is an acceptable conflict risk in a matter and implementing appropriate safeguards
    - recognising and resolving emerging conflicts of interest
    - dealing with conflicts claims and allegations appropriately
    - embracing a culture and approach to practice that maintains high standards of ethical conduct in relation to conflicts risk.

Conflict of interest

In representing a client, a lawyer has a duty to be unaffected by other interests.

However, conflict of interest is an inherent risk in legal practice. Limiting representation to a singular interest is not as easy as it sounds, especially in today's interconnected world. People can have different ideas about what constitutes a conflict and whether a lawyer has remained unaffected.

You may not be able to avoid the risk altogether but you can exercise a degree of control over your exposure and how you handle the 'heat' of actual conflict.

If you play with fire, or unexpectedly confront fire, there is a risk of being burned. Whether you end up charred, singed or hot and sweaty depends on how well you assess the danger, take precautions and behave in the heat of the moment.

Managing conflict risk effectively, whether at the outset of a matter or as a matter progresses, requires that you:

- recognise and show sound reasoning about conflicts risk and risk factors
- adopt practice processes and routines aimed at reducing conflicts risk
- avoid behaviour that increases conflict risk.

Raising awareness of conflicts – Are you claims-prone?

Discussion: Many ways to burn (DVD)

Law practice Better & Best Legal includes the following people:

Fiona Better	Principal
Richard Best	Principal
Malcolm Middleton	Special counsel, recent lateral hire
Amy Avago	Employed lawyer
Susie Sondheim	Personal assistant

While waiting for the others to arrive for a practice meeting about conflicts of interest, Fiona observes that:

> *'Richard is on the warpath about our conflicts management. He says we're a negligence claim waiting to happen.'*

She wonders what might be prompting Richard to hold such a view and reflects that the conflicts of interest principles are clear enough but maybe not so easy to apply in practice. She mentions principles such as *'no personal gain', 'don't act for one client against another'* and *'no divided loyalties'*.

Questions

1. Are you in a law practice that is high risk or low risk of a conflicts claim? Why?
2. What are the sources of conflicts obligations and consequences of breach?

Conflicts categories

The expression 'conflict of interest' covers the potential for a lawyer's representation of a client to be inappropriately affected by the interests of other clients, the lawyer or people associated with the lawyer, and anyone else.

There are several problem areas.

Related parties and intermediaries – Who is the client?

Lawyers often fail to appreciate they are acting for more than one interest when parties are closely related or when the lawyer is instructed via an intermediary. The person giving instructions or paying the bill is treated as the client and the lawyer fails to consider the interests of other parties or the lawyer assumes the parties have a common interest when they have separate interests. Conflicts risk factors include family groups, companies and directors, and intermediary accountants, agents and brokers, especially in matters related to financial borrowings and wills and estates.

Multiple, opposing interests

The classic conflict is acting for more than one party in the same or related matters where the parties have adverse interests. Acting for buyer and seller,

landlord and tenant, borrower and lender are examples where incompatible interests can give rise to allegations of conflicting duties and divided loyalties.

Conflicting duties rather than interests

Acting for a client against a former client is a conflict of duties not interests as the lawyer is not representing the interests of the former client. The lawyer has a duty of disclosure to one and a duty of confidentiality to the other. Such conflict of duties can also arise in representing one client against another in unrelated matters and when lawyers change firms. These situations are more likely to give rise to applications to a court to restrain lawyers from acting than liability claims.

Emerging conflict

Parties may start out with common or compatible interests but the interests of co-parties, such as co-owners or co-accuseds, can diverge. Potential conflicts between opposing parties such as buyer and seller can become actual conflicts as matters progress. Claims arise when lawyers continue acting instead of advising a party to seek independent advice or withdrawing from the matter.

Self-interest and personal relationship conflicts

Lawyers can find themselves in positions of conflict between their own self-interest and duties to act in the best interests of a client. Classic examples are borrowing money from a client, being a beneficiary under a will of a client testator or doing business with a client.

Self-interest can take other forms like being a witness in proceedings, seeking to protect fees and seeking to avoid liability for mistakes or criticism of conduct.

The existence of relationships with opposing or related parties can also be perceived as a threat to the lawyer's independence or objectivity in representing the client.

Sources of conflicts obligations and consequences of breach

Sources

Fiduciary duties of trust, confidence and loyalty

- Protect or advance the client's interests.
- No divided loyalty or double employment without consent.
- Keep confidences not to disclose or misuse.
- Make relevant knowledge available.
- No self-interest conflict.
- No unauthorised profit other than a reasonable fee.

Legal profession regulation and professional standards

- Legal Profession Uniform Law Australian Solicitors' Conduct Rules 2015 (Rules).

Contractual obligations relating to conflict

- Terms of client retainer confirming or modifying fiduciary duty.
- Professional indemnity insurance policy.

Duty of care/liability in tort for harm done by acting in a position of conflict

- Standard of care of truly independent representation.

Consequences

Professional indemnity claims

- Penalty excess.
- Higher premium.

Conduct complaints and disciplinary action

- Strike off, fine and/or reprimand.

Restraining orders

- Disqualified from representing one or more clients.
- Adverse personal costs order.

Client relationship and reputational damage

- Loss of future work and opportunities.

Productivity drain

- Fee refunds and write-offs.
- Investigation and defence time.

Personal stress

- Worry, inconvenience and aggravation.

Conflicts checking – How robust and reliable?

Discussion: Holes in the fire screens (DVD)

Managing conflict risk starts with recognising the potential for a conflicts situation to exist. This means every law practice, small or large, needs a conflicts checking system.

At Better & Best Legal, we hear Fiona ask employed lawyer Amy to explain how she opened a file that created an actual conflict of interest in a litigation matter. Amy says:

> '*Simple. Richard asked me to open a file for the defendant so I did. I had no idea Malcolm had already opened a file for the plaintiff in the very same matter*'.

Fiona asks how the system allowed the opening of opposing files. Amy says:

> *'Easy. We said the conflict check on our matter was done when it wasn't. We forgot. Richard delegated the check to me. I delegated the check to Susie. Susie forgot to do it. I forgot to check it was done. Richard forgot to ask about the results'*.

Fiona and Amy then discuss Better & Best Legal's conflicts screening processes, the limitations of the system and opportunities for improvement.

Questions

1. Do you know enough about your conflicts checking system, how it works and the system limits?
2. In what ways is your conflicts-checking system vulnerable? What conflicts won't the system pick up and why? How is the system vulnerable to being ignored or bypassed?
3. Who should do what to strengthen the reliability and robustness of your conflicts checking system?

Checking for relevant relationships and retainers

Whether the conflicts checking system is simple or sophisticated, it needs to be robust and reliable enough to inform decisions about whether to:

- act or not act
- use or not use conflicts safeguards
- continue acting (with or without safeguards) or withdraw from acting for one or more interests.

Any effective system must require lawyers to update their conflict searches whenever a new party becomes involved in a matter or a material asset is identified.

A poor checking system that fails to identify actual or potential conflicts puts the law practice in the line of fire when the conflict comes to light.

A good conflict checking system will also be comprehensive enough to throw up not only potential legal conflicts but also so called commercial conflicts, where clients of the firm expect a higher degree of loyalty or exclusivity from the law practice than is legally required. This includes expecting that the law practice will not act for commercial competitors of the client or there is a relationship with an opposing party that the law practice does not want to put at risk such as using a good referral source.

Ineffective checking – claim example

A law practice was instructed to act for the purchaser of management rights of a development. The agreement was subject to registration of the plan of subdivision, failing which the purchaser could terminate the agreement and be entitled to reimbursement of fit-out costs.

The partner responsible for the matter undertook a conflict search which showed nothing, despite another of the practice's partners already acting for one of the development's financiers. The conflict search or the record of the existing matter, or both, failed to include full and correct names of all relevant parties and details of the development such as its name and address that would have enabled the relevant partner to identify the connection between the two mandates.

The purchaser later claimed it wanted to terminate the contract but the law practice took active steps to ensure the plan of subdivision would be registered in time pursuant to the financier's interests.

Question

What are the vulnerabilities of your conflicts checking system and what can you do to strengthen your checking processes?

Accepting conflicts risk – Do you make good decisions?

Discussion: Fire drills (DVD)

At Better & Best Legal we see Richard, Fiona, Malcolm and Amy considering their appetite for conflict risk and whether there is a shared view about:

- acting for more than one party in the same or related matter
- acting for and against a client in unrelated matters
- triggers for withdrawal in the face of emerging conflict
- use of conflicts safeguards.

Safeguards mentioned are:

- disclosure
- consent
- limited scope retainers
- information barrier (also known as Chinese Wall)
- independent advice
- waiver clauses (limiting disclosure obligations)
- bump off clauses (who will go elsewhere if conflict emerges).

Question

Why and under what conditions/safeguards, if any, might a law practice accept the following matters?

Transaction – Can you act for vendor and purchaser of a business?

A vendor is selling a small business to a purchaser. Both the vendor and purchaser approach you about acting on the transaction. They tell you they have already discussed the terms of sale and the landlord has met the purchaser and consents to the transfer of the lease.

Litigation – Can you act for A in A vs B, and for B in B ats O?

Client A is a building supplies company. From time to time your firm provides legal services to the business. At present you are instructed in debt recovery against Customer B for an overdue account. So far, Customer B is self-represented.

Customer B, is a builder and approaches your law practice to defend them against a contractual claim by O, a property owner.

If a law practice accepts both mandates, what might constitute an emerging conflict and how should the conflict be handled?

Further training resource

Acting for the vendor and the purchaser of a business is the subject of LPLC's short training video, *Risky Business*. The video can be found in the training resources section of LPLC's website.

Conflict of interest – Says who?

Judicial attitudes

Judges take a keen interest in cases involving allegations of breach of fiduciary duty by officers of the court so expect your conduct to come under close scrutiny if you are ever involved in a conflicts case.

Even where conduct was not found to be improper, courts have been critical of lawyers for their imprudence in acting or continuing to act in matters where there are conflict issues.

In *Pyramid Building Society (in liq) v Rick Nominees Pty Ltd* and *Pyramid Building Society (in liq) v Meeral Pty Ltd*, unreported SCV (2162 & 2231 of 1992), Justice Byrne said:

> *How many cases like this need to come before the courts before solicitors appreciate the folly of acting for more than one party in the most innocent appearing of transactions? Judges for nearly a century have inveighed against the practice … I am entirely unimpressed with the argument that in a friendly and uncomplicated conveyancing transaction of whatever kind, it is proper for a solicitor to act for more than one party because no conflict is apprehended. Lawyers are in a better position than others to know that in the friendliest of partnerships, commercial dealings and marriages there is always the prospect of discord and conflict …*

As stated in Full Court of the Federal Court in *Commonwealth Bank of Australia & Anor v Smith & Anor* (1991) 102 ALR 453 at 477:

> *Not only must the fiduciary avoid, without informed consent, placing himself in a position of conflict between duty and personal interest, but he must eschew conflicting engagements. The reason is that, by reason of multiple engagements, the fiduciary may be unable to discharge adequately the one without conflicting with his obligation in the other. Thus, it has been said, after ample citation of authority, that where an adviser in a sale is also the undisclosed adviser of the purchaser, an actual conflict of duties arises … In such a case, it is not to the point that the fiduciary himself may not stand to profit from the transaction he brings about between the parties. The prohibition is not against the making of a profit ... but of the avoidance of conflict of duties*

As stated in *Trade Practices Commission v CC (NSW) Pty Ltd (No 3)* (1994) 125 ALR 94, per Hill J at 105:

> *[T]he conflict is so acute that mere disclosure to the parties of the conflict and authorisation that the conflict continue even where the parties are given the opportunity to seek independent legal advice on the question of authorisation, cannot solve the problem. Mere consent of the parties to the*

> *continuation of a conflict is not enough. There must be informed consent in the real sense of those words ...*

In *Law Society of NSW v Harvey* [1976] 2 NSWLR 154 at [171], Street CJ expanded on the nature and extent of the disclosure required to be made in the following terms:

> *It must be a conscientious disclosure of all material circumstances, and everything known to him relating to the proposed transaction which might influence the conduct of the client or anybody from whom he might seek advice. To disclose less than all that is material may positively mislead.*

In a negligence claim for breach of the duty of care, a whiff of conflict of interest can complicate the defence of the claim. A client can point to the conflict and argue its interests were subordinated to another's interests. The conflict may not be material to the acts of negligence alleged but will be closely considered against professional standards. If the conduct is serious enough, the judge may refer the conduct to the Victorian Legal Services Board and Commissioner.

In conflicts cases where restraining orders are sought or challenges made to information barriers, the courts seek to balance the public interest in the administration of justice and the client's interests in their choice of lawyer. Courts are alive to allegations of conflict being made against an opponent for tactical reasons and there have been mixed outcomes for the allegedly conflicted lawyers in these kinds of cases.

Courts are invariably unsympathetic to lawyers who show loyalty to their own self-interest.

Conduct rules

Compliance with the spirit and letter of the Rules materially reduces the risk of a conflicts claim. However, LPLC often becomes aware of lawyers overlooking or ignoring the requirements of the Rules.

Standards and rules change. How well do you know the current Rules? Are you confident you always comply with them?

Current clients

For various reasons discussed throughout this workbook, lawyers and law practices should avoid acting for more than one client in a matter. Under Rule 11, if a lawyer or law practice chooses to act for multiple parties in a matter, they must first formally advise all clients of the arrangements and all clients must give their informed consent. If a conflict arises between the duties owed to different clients, the lawyer or law practice must cease acting for one or both clients immediately.

An actual conflict cannot be cured by consent no matter how willing the clients may be to agree to the representation.

Rule 11 prevents a lawyer or law practice acting for a client in a matter where another client's confidential information could be material and disclosure of the information detrimental to the other client's interests, unless:

- both clients have given informed consent to the lawyer or law practice or
- an effective information barrier has been established.

While informed consent is not defined, it likely means being specific about the (name of the) client and the services to be provided to the other client. It is generally regarded as including the nature and consequences of the conflict, the right to alternative representation, how confidential information will be protected, triggers for actual conflict and consequences such as withdrawal. Lawyers need to be mindful of the client's capacity to consent at all. Undue influence and mental capacity may mean that consent cannot be given.

The requirement for an information barrier would seem to rule out an individual acting for both parties to a transaction unless the parties agreed to a no secrets engagement in which case there would be no confidential information requiring the protection of an information barrier.

Any Victorian law practice considering using an information barrier should consult the Law Institute of Victoria's Information Barrier Guidelines at https://www.liv.asn.au/PDF/Practising/Ethics/2006GuideInfoBarrier.aspx.

Former clients

Lawyers need to be aware of their ongoing duties to former clients, particularly the duties of confidentiality and loyalty. Under Rule 10, lawyers and law practices have an obligation to avoid conflicts between the interests of their current clients and the interests of their former clients. A lawyers or law practice cannot act in a matter where a former client's confidential information could be material and detrimental to the former client's interests if disclosed, unless:

- the former client has given informed consent to the lawyer or law practice or
- an effective information barrier has been established.

Note the discussion in 'Current clients' above regarding informed consent and information barriers.

The definition of former client includes clients of the lawyer in their present and past law practices, and clients of the lawyer's colleagues in the present law practice and their past law practices.

How would you ever know this information unless you routinely ask new clients and all your colleagues and how do you ask without tainting yourself with confidential information? And how do you obtain consent to the services from the former client while maintaining the confidentiality of the proposed new client?

Lawyer's own interests

Lawyers also have a duty to avoid a conflict between their own interests and the client's interests. Interests that must not conflict with the client's interests include those of the law practice and affiliates as defined in the Rules and including business partners, friends and relatives. Rule 12 states lawyers are not permitted to exercise any undue influence to benefit from their relationship with their client, other than the usual payment for the legal services they have provided. Rule 12 also contains specific provisions about:

- borrowing money from clients and former clients
- drawing a will appointing the lawyer or an associate as executor
- drawing a will or other instrument under which the lawyer, their law practice or an associate could receive a substantial benefit other than any proper entitlement to executor's commission and proper fees
- receiving a financial benefit from a third party in relation to any dealing where the lawyer represents a client or from another service provider to whom a client has been referred by the lawyer
- acting for a client in any dealing in which a financial benefit may be payable to a third party for referring the client.

LPLC policy

Under LPLC's professional indemnity insurance policy with defence costs exclusive excess, an insured law practice pays a double excess where it has represented more than one party or interest in respect of any matter or transaction.

There can be indemnity issues if the conduct of the lawyer prejudices the interests of underwriters. This can happen when a lawyer continues acting for a client after discovering a mistake that may lead to a claim. Is the lawyer creating a conflict by, in effect acting, for themselves in the matter?

Think of examples such as missing a limitation period or failing to comply with a self-executing order which can give rise to a claim. Lawyers can be tempted to fix the problem themselves such as by making an application to extend the limitation period or to set aside judgment.

They may see the interests of clients, underwriters and themselves in fixing the problem as being aligned when in fact they are not.

Continuing to act is fraught with danger. Instead of just facing one claim in relation to the original mistake, the lawyer and law practice may be exposed to:

- further allegations of negligence, for example that the lawyer failed to advance the client's interests by downplaying their role in the mistake or by rushing a matter to settlement
- claims for breach of fiduciary duty for acting in a self-interest conflict situation
- penalty excess for acting in a position of conflict

- potential indemnity issues, for example over unauthorised admissions.

Continuing to act also risks:

- a complaint and disciplinary action for lack of professional independence and breaches of duties to the court and the administration of justice
- an order of the court restraining you from continuing to act, with probable costs consequences.

Law practice policy

A conflicts policy sets out the approach a law practice takes to choices about conflicts issues. Good policy aids good decision-making on a case-by-case basis and aids consistency of decision-making across the practice and over time.

The policy embodies the appetite and tolerance of the law practice for conflict risk and compliance. For example, law practices and conflicts policies may vary regarding:

- types of legal services offered as some practice areas and segments within practice areas are more conflicts-prone than others
- criteria for acceptance of new clients including loyalty-sensitive clients that insist on exclusivity
- criteria for accepting new matters, especially if multiple interests are involved
- who can approve new clients and matters
- resources deployed (the higher the risk, the higher the safeguards and the more resources will be required for conflicts screening, safeguards and checking compliance)
- implementation of safeguards such as consents, terms of engagement, information barriers, independent advice and whether to adopt minimum compliance or best practice
- approaches to emerging conflict, such as whether in the case of diverging client interests the firm will continue to act for one party if possible
- writing non-engagement letters to unrepresented parties.

Policy embodies the 'rules' a law practice makes for itself or a sole practitioner makes for himself or herself. When a conflict claim arises the lawyer sometimes says

> *Usually I would not have acted but this time I broke my own rules.*

or

> *We have a policy that written consent is required but the policy wasn't followed.*

The larger the practice, the more important it is that policy is documented, communicated and backed up with resources for monitoring and troubleshooting.

Personal values

Lawyers can find themselves in uncomfortable positions when their personal values or preferences are at odds with the values of their profession, clients or the law practice. Also, lawyers are not always insightful when it comes to understanding the impact of conflicts of interest on their professional judgment.

A lawyer with a conservative approach may be uncomfortable in a law practice that takes big risks acting for multiple parties with minimum safeguards or when faced with an important client who doesn't understand the conflicts problem.

A law practice with a conservative approach may face tensions when individual lawyers do not agree with law practice policy and see the firm turning away good work unnecessarily and adversely impacting on the firm's bottom line.

Studies about how people think show that there are good reasons to take a conservative approach to conflicts of interest because people underestimate the impact of conflict of interest on their judgment.

Professionals believe they are capable of being objective and independent but they may be more influenced by unconscious biases in their thinking than they realise. For example, in some multi-party matters there will be a party who is more dominant than another. A lawyer may not even realise they are showing bias towards the interests of the more dominant client. Or the opposite may occur and the consciousness of the need to be seen as unbiased may cause the lawyer to unconsciously favour the weaker party.

This unconscious bias is most apparent in cases of self-interest conflict. Protection of self-interest is a natural survival instinct and a very powerful force. For example, a lawyer may rationalise that continuing to act for a client at no charge to fix a mistake is in the client's best interests. A truly independent lawyer may come to a different conclusion as there may be options the lawyer does not consider.

There is some interesting work on disclosure of conflicts of interest that says people feel pressured into taking advice from advisers who disclosure their own self-interest conflicts. By disclosing the conflict, the advisor seems to be trustworthy and people feel it would be rude not to return the trust.

People will discount the advice but they may not discount it enough. Somewhat disconcertingly, advisers who disclose their conflict often give more biased advice than if the conflict had not been disclosed. Disclosure seems to give some lawyers an unconscious moral licence to pursue self-advantage.

Client expectations

Lack of a shared understanding between lawyer and client as to the lawyer's undivided loyalty will increase the risk of a conflicts claim or complaint.

To the layperson, conflict of interest means self-interest conflict so there is often a gap from the start in the client's expectations and understanding of a lawyer's professional obligations in dealing with potential and actual conflicts.

Lawyers need to make sure they understand the expectations of particular clients in particular matters as expectations can vary between clients and for the same client at different times or in different matters.

Some clients have low expectations of loyalty from their lawyer. They accept that lawyers may act for them in some matters and against them in others. The lawyer needs to gauge whether this attitude stems from the informed pragmatism of a sophisticated client or from a client who doesn't know their rights.

On the other hand, some clients demand a level of loyalty that goes beyond the lawyer's professional obligations. Again, the lawyer needs to gauge the root cause of the sensitivity. It could be a genuine sensitivity or tactic to restrict the access of others to the lawyer's services such as a commercial rival or opponent in a dispute.

Either way, a lawyer needs to be careful not to be the one to create the expectation gap by over-promising undivided loyalty.

The key to fulfilling obligations and meeting client expectations is good communication. Don't make assumptions about the client's views of loyalty and don't treat disclosure and consent as a form-signing exercise. Ask clients about their expectations, listen to their answers and fully explain your obligations and the client's options.

Emerging conflict of interest – Continue or withdraw?

Discussion: Pardon my arson (DVD)

Fiona observes clients having a heated discussion. They look familiar but she can't place them. It turns out they are husband and wife, Tim and Tina Smith, who are clients of Better & Best Legal in relation to estate planning and a commercial dispute involving their landscaping business.

Richard breaks the bad news there could be conflicts problems. The good news, he says, is that if they navigate the conflicts issues of the Smith matters then they can handle any conflict in any area of practice.

Questions

Matter 1: Husband and wife mirror/mutual wills

1. Is there a conflict of interest inherent in husband and wife wills? In this particular matter?
2. How should any conflict or potential conflict be handled to demonstrate good risk management and compliance with professional obligations?

Mirror wills: Identical terms but not irrevocable. Can be changed after death of a testator (or before). Relies on mutual trust and moral responsibility of surviving spouse to not revoke or alter. However, a mirror will allows the surviving spouse flexibility in the conduct of their affairs if circumstances change.

Mutual wills: May or may not be identical. Formal agreement that neither party will revoke or alter the will without the knowledge and approval of the other. Gives certainty about how assets will be dealt with but surviving spouse can be locked in to arrangements that are inappropriate. If the surviving spouse does act contrary to the terms of the will, the courts will usually recognise the rights of an intended beneficiary to enforce the agreement.

Matter 2: Litigation by the business against the football club

3. Does the challenge by the client's opponent to the interpretation of the agreement drafted by Better & Best Legal give rise to a conflict of interest? If not why not? If so, what are the implications and how should the situation be handled to demonstrate good risk management and compliance with obligations? Is obtaining counsel's advice sufficient?
4. Does Malcolm's relationship with the defendant give rise to a conflict of interest? If not why not? If so, what are the implications and how should the situation be handled to demonstrate good risk management and compliance with obligations?
5. What are the lessons for you and your practice?

Duty to cease acting?

When conflicts of interests or duties emerge in a matter lawyers face the difficult decision of deciding whether to continue to act in the matter for or cease to act for one or all of the parties to the conflict.

Lawyers need to determine if continuing to act is simply unwise and imprudent or improper and a breach of professional obligations.

Some lawyers don't want to take any risks and cease acting immediately a conflict of interest emerges.

Other lawyers stay in the line of fire and believe they can act and maybe even should continue to act because it is in the best interests of the client for them to do so. The lawyers may rationalise that they:

- are obliged to finish what they started and become a mediator to help clients resolve their differences
- can vary the scope of the retainer to finesse a continuing role for themselves that is not conflicted
- establish an information barrier at this late stage
- get another lawyer in the firm to act or provide independent advice
- have a responsibility to fix a problem they may have created.

However, these courses of action increase the risk of a conflicts claim.

As a general rule, a lawyer must finish an engagement and can terminate only in certain circumstances (Rule 13). However, lawyers often overlook that termination may be required by law or other conduct rules. Conflict of interest is one of those times where termination is likely to be required.

What courts have said

If the lawyer does not terminate the engagement then a court may do it for them whether on its own motion or the application of a (former) client or even a third party. Anticipating how a court may view your conduct in continuing to act will aid decision making in managing emerging conflict.

The test applied by many courts to determine whether to restrain a lawyer from acting was stated in *Grimwade v Meagher* [1995] 1 VR 446 as follows.

> *The objective test to be applied ... is whether a fair-minded reasonably informed member of the public would conclude that the proper administration of justice required that [the lawyer] be […] prevented from acting, at all times giving due weight to the public interest that a litigant should not be deprived of his or her choice of [lawyer] without good cause.*

Circumstances where the courts have exercised their powers over lawyers as officers of the court include:

- to protect the confidential information of a former client (see guidelines for effective information barriers)
- where the lawyer's client has a conflict of interest in one of the capacities in which the lawyer is representing the client
- the lawyer will be a material witness
- the lawyer has a personal interest in the outcome
- the lawyer has a relationship that compromises independence.

In *Clay v Karlson* (1997) 17 WAR 493, Templeman J said:

> *I emphasise that Seaman refers to the fact that it is generally unwise for a practitioner who is likely to be called as a witness to continue to represent his client in those proceedings. It must follow, I think, that the case is even stronger against the solicitor acting who has a personal interest in the outcome of the action: he is more than simply a witness.*

Mr Justice Ipp said in 'Lawyers Duties to the Court', (1998) 114 *Law Quarterly Review* 63 at 132:

> *(A) lawyer might have a personal interest in the outcome of proceedings or be likely to be called as a witness, and is consequently unable to give the court the independent and uninvolved assistance expected from officers of the court. The duty to the court arises from the court's concern that it should have the assistance of independent legal representatives. The integrity of the adversarial system in England and Australia is dependent on lawyers acting in perfect good faith, untainted by divided loyalties of any kind.*

A contention by an opposing party that the lawyers drafting or advice is wrong does not necessarily give the lawyer a personal interest in the outcome. In *Premier Capital (China) Ltd v Sandhurst Trustees Ltd* [2012] VSC 611, Pagone J said:

> *14. .... A contention that an agreement is void for uncertainty (…) does not create a separate interest comparable to that considered in Clay v Karlson (…). Templeman J appeared to accept, and I respectfully agree, that there may be situations in which a solicitor's involvement in giving evidence cannot reasonably be avoided. The matters pleaded (in relation to the drafting and interpretation of the agreement) do not make allegations of a kind comparable to those in Clay v Karlson in which the propriety of the conduct of the practitioners was in issue. A reasonably informed fair-minded member of the public might consider it prudent for (the solicitors) not to act in the proceeding (…) but would not conclude that the*

administration of justice required that they should be prevented from continuing to act for (their client).

In the same case, Pagone J warned that applications for a restraining order must be for proper purpose not simply to cause inconvenience to the opponent and a forensic advantage to the moving party.

Other relevant duties

- General duties to the courts and of independence – Rules 3 and 4.
- Lawyers acting in matters before the court must exercise the forensic judgments called for during the case independently after appropriate consideration of instructions – Rule 17.
- Prohibition on appearing as an advocate in a hearing where it becomes apparent the lawyer will be required to give evidence material to the determination of contested issues – Rule 27.

Managing a 'flaming mistake'

From time to time you may need to face up to the uncomfortable truth that when your own self-interest becomes involved in a matter, you may not be objective even if you think you are.

Whether it is improper for you to continue acting or merely imprudent will depend on the facts of the case. You would be well advised to seek out the experience of others and obtain your own advice as to whether arrangements short of withdrawal will suffice or whether continuing to act will expose you to a claim or other adverse consequences.

Here are a few final thoughts on managing mistakes.

Do not assume an allegation of negligence is tactical and do not attempt a do-it-yourself fix without taking advice.

Experience shows that lawyers who dismiss allegations of negligence as purely tactical or who try to fix mistakes themselves, generally make things worse for the client and themselves. There may be substance to the allegation of negligence that the lawyer cannot see. The so-called solution the lawyer adopts may be a bad solution or badly executed and give rise to a further claim.

Protect your indemnity and notify circumstance to LPLC early.

Don't jeopardise your indemnity by late notification or unauthorised admissions. There is no penalty for early notification but there may be a double excess if you act in a position of conflict.

LPLC will very likely have experience you can draw on to help decide the best course of action to get the problem fixed.

Don't risk elevating negligence to a conduct issue. Consider your professional obligations and take professional advice.

Don't compound a mistake by acting in a position of conflict. If continuing to act puts you in a position of being unable to act in the best interests of the client, of having an interest in the outcome, of being a material witness or in some other way compromising your independence and other duties, you should not do so.

The performance of professional obligations is ultimately a matter for you, not your insurer. LPLC cannot advise you about your conduct position but can provide information about resources and sources of advice.

Don't assume client consent, independent advice or briefing counsel will douse the flames of conflict.

Client consent, even informed consent, does not mean that the lawyer can continue to act. The client cannot consent to the lawyer breaching the lawyer's duty to the court or the administration of justice, such as acting where the lawyer lacks independence because of their exposure to civil liability.

Use of counsel is not a panacea to conflict problems. Counsel still must be briefed by the lawyer acting for the client and the contents of the brief are likely to be affected by the lawyer's personal interest in the matter. Furthermore, use of counsel does not address the fundamental issue of the lawyer's lack of independence, even if it does address the need for independent advice to the client, although that is not a given.

Where to from here?

What matters most is not what you have learned today but what you are going to **do** with what you have learnt.

Where are you most exposed to the risks raised by today's content and what are you going to **do** differently to reduce the risk?

Conflict claims examples
Property and finance

Intra-family matters

A grandmother who had a falling out with all her children agreed to gift $300,000 to her favourite granddaughter to buy a new property.

The conditions of the gift were that the grandmother be allowed to build her own granny flat on the property and have a right to live there, close to her granddaughter.

The lawyer met with the granddaughter and her husband. The couple explained that the property they intended to buy would be funded by the sale of their current home, a mortgage and the gift from the wife's grandmother.

They asked for a document that clearly stated the money was a gift and did not need to be repaid. They also said the granny flat would be built on the property.

The lawyer then met with the grandmother who explained she wanted to gift the money to remove it from her estate as she did not want her children to have it when she died. While she seemed very capable and sure of what she wanted, she was 89, partially deaf and blind and had suffered three strokes.

The lawyer prepared an agreement that provided:

- the $300,000 was a gift to the granddaughter and her husband
- the grandmother could build a granny flat on the property and have access to it and the rest of the property save for her granddaughter's house
- the granny flat was to be removed on the grandmother's death and form part of her estate
- the grandmother would have an equitable interest in the property and could lodge a caveat accordingly
- the agreement ended on the grandmother's death.

Minor amendments were made under instruction from the grandmother and agreed by the granddaughter and her husband.

After the agreement was executed, the property was purchased and the parties moved into the house pending construction of the granny flat. Before long, they had a falling out and the grandmother moved out and demanded her gift back.

The grandmother issued proceedings against the couple. After the matter failed to settle at mediation, the lawyer was joined.

The allegations against the lawyer were that he:

- failed to advise the grandmother to seek independent advice about the agreement

- failed to properly explain the agreement and its consequences to the grandmother
- knew or should have known there was a conflict of interest and the grandmother was vulnerable.

Another pattern of conflicts claims involves borrowings by related parties such as families, corporations and business partners, secured by the real property assets of members of the group, who are vulnerable in some way yet do not receive any or proper independent advice. The vulnerable parties are then left liable to lenders in circumstances they did not expect. Some of these claims are very large and exceed the sum insured at the compulsory level.

Emerging conflict

The lawyer was instructed to just prepare a section 32 statement as the selling agent was instructed to prepare the contract of sale. The selling agent inserted a special condition at the request of the purchaser making the contract subject to the purchaser obtaining a planning permit. After the contract was signed the lawyer commenced acting for the purchaser and continued to act for the vendor.

When the purchaser tried to end the contract relying on the special condition, the vendor argued that on their interpretation of the special condition the purchaser was not entitled to end the contract. The vendor alleged that if the lawyer had properly advised the vendor on the effect of the special condition the dispute may have been avoided. They also alleged that by failing to properly advise the vendor, the lawyer had favoured the purchaser's interests over the vendor's.

Although the parties agreed to cancel the contract, the vendor's loss was the commission payable to the agent and the vendor sought payment from the lawyer.

Self-interest conflict

The lawyer acted for a company owned by a friend of the lawyer and the friend's business partner. The company was developing a multi-unit property.

The company came under financial pressure and engaged a company owned by the lawyer's wife to sell the units. She had connections with spruikers who marketed properties to investors. The lawyer's friend set the price for each of the units and the wife added commission for her company and the spruikers to arrive at the sale price.

Each of the units was sold and the proceeds were directed to the wife's company. The lawyer's role was limited to preparing the sale documents, including settlement statements that were provided to his friend prior to settlement.

The lawyer's friend subsequently had a falling out with his business partner who took control of the company. The business partner disputed the payments made to the wife's company, alleging she acted as an estate agent under the *Estate*

Agents Act 1980 (Vic) without a licence and was not entitled to commission. The business partner sued the lawyer for breach of trust, arguing payment was made to the lawyer's wife's company without instructions and was not required to be made under the Estate Agents Act.

The lawyer was in a position of conflict because of his wife's interest and should not have acted in the matter. He was exposed to a claim in circumstances where payments were made to his wife's company without the knowledge of his friend's business partner.

Wills and estates

Mutually binding wills

The lawyer was asked by a friend to prepare wills for the friend's mother and stepfather. While this was the mother's second marriage, the couple had actually been married for more than 30 years. Their only children were from the wife's first marriage. The lawyer was instructed by the wife that she and her husband wished to leave the matrimonial home (the major asset) to her three children, even if she died first. The property was held as joint tenants.

The lawyer advised the couple to sign identical wills and then execute a deed agreeing to leave the property to the children, and to provide for a caveat to be lodged on the property on behalf of the children. The lawyer prepared the wills and deed, and attended the wife in hospital to execute the documents.

The husband, who was in his 70's and almost blind, went to the lawyer's office. The lawyer said he spent about half an hour going through the documents with the husband to ensure he was satisfied that he understood their meaning before signing.

The wife died two months later. The husband, who was an executor with the three stepchildren, instructed the lawyer to act in the estate, requesting all correspondence be sent to the stepdaughter due to his eyesight. A caveat was lodged on behalf of the stepchildren.

Several years later the stepfather said he discovered the caveat over his property and had it removed to allow him to make arrangements for his care and to give effect to a new will he had made. He had formed a new relationship.

The stepfather's recollection about the will was that he was taken to the lawyer's office, he was in the office for 15 to 20 minutes, just did what he was told and signed.

This example illustrates some of the pitfalls for lawyers, especially where they are asked to make irrevocable for both parties. Did the husband consider that he may need to sell the property in order to enter an aged care facility or that he might commence a new relationship that would affect how he wanted to deal with relevant property? Each party needs independent advice on the pros and cons

of them. Mutually binding wills are in some respects similar to family law financial agreements, where independent advice is required.

Family disputes

The lawyer acted on a deceased estate where the deceased's son and daughter were her executors. The son was a longstanding client of the lawyer's firm in other matters. Before obtaining probate, the daughter alleged the son had misappropriated money from their mother's bank account during her lifetime. The mother had authorised her son to operate her bank account and he said the money was a gift for being his mother's primary caregiver.

The daughter was reluctant to sign the probate application without the money being included in the inventory of assets and liabilities. She claimed the lawyer offered to assist the siblings resolve their dispute and when he advised that the alleged debt did not need to be specified in the inventory, she agreed to proceed with probate.

The dispute continued and prior to distributing the assets the lawyer referred the siblings to independent lawyers. The son and daughter subsequently instructed the lawyer to hold an amount in a controlled money account pending resolution of their dispute and to distribute the rest of the estate.

The daughter then alleged the lawyer favoured her brother and gave negligent advice about the inventory and amount claimed by the son as a gift. She argued that signing the probate application was in effect an agreement that the estate had no claim on the alleged debt. She sued the lawyer claiming damages comprising 50 per cent of the alleged debt plus fees paid to another law firm for advice.

The lawyer eventually had the proceedings dismissed as the daughter had not brought proceedings against her brother.

Although the siblings received independent advice resulting in the lawyer holding money on trust pending resolution of the dispute, the lawyer should have recognised the potential conflict earlier when the daughter raised concerns. The daughter should have been referred for independent advice at that stage, with the lawyer staying clear of the dispute.

Commercial transactions

Acting for vendor and purchaser

The lawyer acted for both the vendor and purchaser of a shop. The lawyer said she was retained only to document what the parties agreed but this limited retainer was not confirmed in writing.

The purchaser was subsequently unhappy with the performance of the business and sued the vendor for misrepresentation as to takings, breach of undertakings to maintain the goodwill of the business until settlement and to provide assistance

in the management of the business as well as for breach of a restraint of trade clause.

The disappointed purchaser also sued the lawyer alleging that she preferred the other side's interests. The purchaser alleged the lawyer should have advised on differences between the draft contract and the executed version, particularly amendment of the restraint of trade clause to reduce the radial limitation from 25km to 5km. The purchaser also alleged the lawyer failed to warn of the risks associated with the execution of the contract where there was no 25km restraint of trade clause and no warranty or guarantee from the vendor regarding the takings and profits of the business.

Who is the client

The lawyer acted for a lender on instructions from a broker regarding a loan. He was instructed to register an interest on the Personal Property Securities Register (PPSR) over a boat owned by the guarantor, a director of the borrower company.

The lawyer registered an interest on the PPSR that was defective as the registration referred to an incorrect serial number for the boat and was lodged in favour of the broker rather than the lender. The guarantor subsequently sold the boat without needing to discharge the registered security.

The lawyer said the broker had orally instructed him to make the security over the boat in favour of the broker rather than the lender. This was done to secure the guarantor's obligations to pay the broker an ongoing management fee in the event of default in repayment of the loan. However, the lender was not aware of the instruction and was not advised by the lawyer that part of the proposed security would not be available for the loan. The broker's instructions to register security given by the guarantor in the broker's favour were potentially adverse to the lender's interests and should have been confirmed directly with the client.

Litigation

Emerging conflict

The lawyer originally acted for a husband and wife in a regulatory investigation of a business they owned jointly. The couple and their company were then sued by a man who alleged the couple represented he would receive a half share of the business and that their actions were misleading and deceptive. He sought orders for repayment of money he had paid or alternatively a half share of the business.

The husband asked the lawyer to act for him personally in the proceedings, and also for his wife and the company which were co-defendants. During the matter it became clear the allegations against the wife were confined to her role in signing two letters acknowledging receipt of payments from the plaintiff to the business. The plaintiff never intended to give evidence against the wife regarding any oral misrepresentations. The wife maintained she merely signed the letters on behalf of the company and did not personally make any representations.

More than a year after the proceedings were commenced, the parties settled with the husband and wife jointly and severally liable for the settlement amount. The husband and wife subsequently defaulted in meeting the instalment payments under the settlement agreement and the plaintiff made a successful summary judgment application.

The wife then sued the lawyer, alleging that when she signed the settlement she wasn't aware of advice from counsel that raised the possibility of her bringing a strike out application. She also said the lawyer did not properly discuss the proposed settlement with her before signing.

The lawyer had sought instructions only from the husband whose interests were not wholly aligned with his wife's interests. The plaintiff's claim against the wife was weaker and she alleged her husband was not authorised to give instructions on her behalf.

Self-interest

When a commercial or property transaction drifts into dispute and the matter is transferred to the firm's litigation lawyer, the litigation lawyer may fail to adequately consider the possibility of negligence by the transactional lawyer. Litigation can be well advanced before the issue gets raised and notified to LPLC. These cases can be very large, very complex and very costly.