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Beazley Brief

Risk management insights for law firms from Beazley

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Law firm observers watched carefully over the summer as the Chicago law firm of Kirkland & Ellis squared off against pharmaceutical giant and client Mylan after Mylan objected to Kirkland's role in the unsolicited offer to buy Mylan NV made by Kirkland client Teva Pharmaceutical Industries Ltd. In response, Kirkland argued that it had a waiver from Mylan that permitted it to take on the Teva representation but a magistrate judge disagreed in a June 9, 2015 opinion. Although the parties have since decided to stand down from the dispute by agreement, the ramifications and issues that it brought to the fore should prompt firms to look carefully at their waiver forms.

In a June 15, 2015 article entitled ***DealPolitik: Mylan-Kirkland Decision Should Give Big Law Firms Shivers***, the Wall Street Journal's Ronald Barusch observed that "large law firms view themselves as a business. If a client wants its services, the client should expect prescribed terms of engagement giving a law firm maximum freedom to act on other assignments." Barusch also noted, however, that "every once in a while a case has to remind the firms how explicit they need to be to get that permission and to make it stick."

With that admonition in mind, we thought that it would be useful to take a look at some case law regarding how advance conflict waivers have been analyzed by the courts. We aimed to identify some best practices that could increase the chances that firms' advance conflict waivers will be validated. We asked Robert Palmersheim of the Chicago office of Honigman Miller Schwartz and Cohn LLP to take a look at the issue for us. His colleague, Teresa Sullivan, assisted him in this project.

Robert is a partner at Honigman with 20 years of experience litigating professional liability and commercial litigation matters. Teresa is a Honigman associate with substantial litigation experience having served as both first and second chair at trial. Robert, Teresa and Honigman partner Anand Mathew are members of that firm's Professional Liability group which defends lawyers and other professionals against claims of professional malpractice and related matters. Their experience litigating complex business disputes renders them particularly well-equipped to handle the professional malpractice claims and the "case within the case" issues that that can arise from them. Robert, Anand and Teresa work together regularly representing law firms facing professional liability matters.

We appreciate Robert's and Teresa's assistance with this *Beazley Brief* and think that their article contains some helpful analysis and identifies some useful "best practices" that firms can consider when handling advance conflict waivers. We thank them very much for their efforts.

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Best Practices for Conflict-Free Advance Conflict Waivers

By Robert J. Palmersheim and Teresa A. Sullivan
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"Even a client who accepts his lawyer's toe across an ethical line need not later tolerate the lawyer's foot."

So said Magistrate Judge Lisa Lenihan in her ruling on Mylan's recent motion for a preliminary injunction in Mylan v. Kirkland & Ellis, Case No. 2:15- cv-00581, U.S. District Court, Western District of Pennsylvania. The opinion considered the viability of Kirkland's advance waiver with its client, Mylan, and concluded that the waiver was ineffective.

Judge Lenihan's opinion leaves law firms with a serious question: how can they ensure that their own advance conflict waivers are effective? Given the current trends in law firm consolidation, lawyer and practice group mobility and the recent wave of corporate consolidation, this question ought to be front and center on law firms' radar screens.

This article examines some recent cases which assessed advance conflict waivers and offers some lessons learned. It also provides tips for drafting advance conflict waivers that should help minimize the potential for future disqualification.

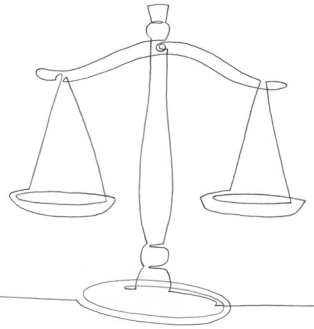
Conflicts Are An Increasingly Critical Concern For Law Firms

It is not just mega-firms like Kirkland that must anticipate future conflicts and carefully draft their conflict waivers. Firms of all sizes must be proactive. In 2014, there were 82 law firm mergers, which was just short of the 88 mergers reported in 2013[1]. Mergers and lawyer and practice group mobility increase the tension between a lawyer's duty to keep client information confidential (Model Rule 1.6) and a lawyer's duty to "adopt reasonable procedures" to detect conflicts of interest (Model Rule 1.7).[2] Increasing consolidation highlights the need for a comprehensive system for spotting and addressing potential conflicts. This is particularly true with respect to advance waivers.

The specific matter in which a conflict can arise varies substantially. Litigation and corporate takeover work are not the only areas where conflicts arise. As discussed below, the need for well-drafted advance conflict waivers and informed consent arise out of joint defense agreements, routine corporate transactions, and intellectual property representations (among others).

1 Available online at: http://www.altmanweil.com/index.cfm/fa/r.resource_detail/oid/a6f9708b-dc22-4f6b-a2c1-cce418852e60/resource/Another_Active_Year_for_US_Law_Firm_Combinations.cfm

2 For a broader discussion of that tension, see *Lawyer Mobility and Legal Ethics: Resolving the Tension Between Confidentiality Requirements and Contemporary Lawyers' Career Paths.* Available online at: http://www.law.ua.edu/resources/pubs/jlp_files/issues_files/vol31/vol31art08.pdf



Recent Cases Highlight The Importance Of A Thoughtful And Proactive Approach To Conflict Waiver Requests

Recent cases such as *Mylan* and others illustrate the potential for negative consequences and fallout from ineffective conflict waivers. Those consequences include (i) lost business and client relationships both present and future; (ii) reputational harm; (iii) the possibility of sanctions being levied against the firm and individual attorneys; and (iv) the risk of damages arising from potential client claims.

Mylan v. Kirkland & Ellis – Recommending Disqualification of Kirkland[3]

How did Kirkland get into the mess with Mylan to begin with? In 2013, Kirkland was retained by Mylan, the maker of the EpiPen, to provide services on a number of regulatory matters. At the time, Kirkland was representing Teva, another pharmaceutical company. That representation included active cases against Mylan. When Kirkland and Mylan began their relationship, Mylan signed an advance conflict waiver.

Originally, Kirkland had asked Mylan to waive conflicts as to any matters that were "substantially related" to the work Kirkland was doing for Mylan. However, the final draft of the waiver did not include the term "substantially" and only referred to "related" work. Kirkland went on to represent Mylan in a number of matters, giving Kirkland access to confidential information regarding the Mylan entities in general and Mylan's EpiPen injector. Subsequently, Kirkland agreed to represent Teva in a hostile takeover bid of Mylan. Mylan sued Kirkland over its representation of Teva in that takeover bid.

Using the hook of the ill-defined term "related," Magistrate Judge Lenihan criticized Kirkland's attorneys, saying, "[i]t would be hard to imagine a representation more opposed to a current client's interests, more in breach of a fiduciary duty toward those interests, than one in which the client's counsel sells his professional services to advance the interests of a competitor in a hostile takeover attempt of the client's entire corporate affiliate group." She went on to say that even if the takeover bid was not related to Kirkland's work for Mylan on its drug products, Kirkland's advance conflict waiver still failed because consent must be "informed," as required under Pennsylvania Rule 1.7 (and Model Rule 1.7). And because there was no specific reference to potential takeover bids in the waiver, the advance waiver was not informed as to that type of work. Although Magistrate Judge Lenihan's opinion was only an advisory opinion, the damage was done. Sullivan & Cromwell was chosen to replace Kirkland (thus costing Kirkland the potential[4] $40 billion takeover engagement), and this exposed Kirkland to the risks of continued litigation with Mylan.

Worldspan L.P. v. Sabre Group Holdings, Inc. – Disqualifying Alston & Bird[5]

In *Worldspan*, Alston & Bird, which had represented Worldspan in tax matters over a number of years, sought and obtained an advance conflict waiver from Worldspan. The waiver stated that the firm would not take on (i) matters substantially related to its work for Worldspan, or (ii) matters that would involve the use of confidential information against Worldspan. Six years later, Worldspan sued Sabre Group in a technology dispute, and Alston & Bird appeared to represent Sabre. The court held the advance waiver invalid because (i) it did not say anything about litigation and (ii) six years had passed since the waiver had been negotiated and when Alston & Bird appeared on behalf of Sabre. Thus, the court concluded, the consent could not have been "informed" and disqualified Alston & Bird.

Airgas Inc. v. Cravath – Settled Case in Which Airgas Sought Cravath's Disqualification

In 2010, Airgas Inc., Cravath's former client, sued Cravath over its representation of Air Products & Chemicals in a hostile takeover bid of Airgas. Airgas claimed that Cravath had access to its confidential information which helped Air Products prepare the (ultimately failed) hostile takeover bid. Cravath had represented Airgas in a number of financing deals between 2001 and 2009. In 2011, a federal judge in Philadelphia refused to grant Cravath judgment on the pleadings on Airgas' claims, and the parties later entered into a confidential settlement.[6] The court concluded that it was possible that Cravath's representation of Airgas was substantially related enough to the representation of Air Products in the hostile takeover attempt as to create an issue of fact regarding that potential conflict. The court's opinion did not discuss the conflict waiver between the parties. Yet, had there been a carefully crafted waiver (such as those discussed below), the court might have concluded that Airgas had given informed consent of the potential conflict so as to have waived any right to pursue a claim for breach of fiduciary duty.

Key Takeaways from Disqualification Cases

What can we learn from the cases in which the firms were disqualified (or, in Cravath's case, in which they failed to defeat disqualification on a Rule 12(c) motion)? First, the language used in an advance waiver must be as specific as possible. If the law firm wants a client to waive a conflict on a future takeover bid, the waiver should say so. Otherwise, the firm could face a situation like those faced in *Mylan* and *Airgas*. Don't just assume that if the waiver says that adverse litigation is permitted and the firm has set up ethical screens that a future takeover bid will be included. Secondly, firms should revisit conflict waivers periodically so that they do not become stale and so that the waiver takes into account (i) new clients, affiliates and/or matters that manifest themselves after the waiver is signed and (ii) other changed circumstances that evolve over time. Otherwise, firms risk a *Worldspan*-type scenario. Courts tend to scrutinize waivers that haven't been recently updated before they are used to try to avoid a potential conflict. Third, both *Mylan* and *Airgas* call into question whether a firm can ever represent a new client against a former or existing client in a hostile takeover bid if the representation of the former client gave the firm access to the kind of confidential information that would be helpful in pursuing the takeover bid.

Cases Rejecting Disqualification

Not all recent cases involving advance waivers have ended in disqualification. These cases illustrate the importance of a thoughtful, well-drafted, and proactive approach to conflicts and waiver requests and demonstrate that such advance conflict waivers can survive scrutiny.

Galderma Labs v. Actavis Mid Atlantic LLC – Rejecting Disqualification of Vinson & Elkins

In *Galderma*, the Court upheld an advance waiver.[7] Galderma had engaged Vinson & Elkins in one matter but later sued the firm when it began representing a different client in an unrelated matter. In response, Vinson & Elkins pointed to a waiver that it had agreed to with Galderma. The court considered a number of factors in deciding not to disqualify V&E. Those factors were that (i) the waiver included an agreement for a process by which the firm would determine when it would and when it would not handle matters for clients with adverse interests;

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3 Opinion Available online at: http://ia600309.us.archive.org/33/items/gov.uscourts.pawd.223479/gov.uscourts.pawd.223479.96.0.pdf

4 Teva ultimately dropped its bid to take over Mylan in late July 2015 when it acquired Allergan Plc's generic-drug business. Mylan stipulated to a dismissal of the case against Kirkland in August 2015.

5 Opinion Available online at: http://www.leagle.com/decision/199813615FSupp2d1356_11191.xml/WORLDSPAN,%20L.P.%20v.%20SABRE%20GROUP%20HOLDINGS,%20INC.

6 Opinion Available online at: http://blogs.reuters.com/alison-frankel/files/2015/05/airgas-vcravath-SJopinion.pdf

7 Opinion Available online at: http://www2.bloomberglaw.com/public/desktop/document/Galderma_Laboratories_LP_et_al_v_Actavis_Mid_Atlantic_LLC_Docket_/1

(ii) the waiver included an "explanation of the material risk of waiving future conflicts of interest" because it specified that the firm would be able to represent clients with adverse interests to Galderma; (iii) the waiver described "reasonably available alternatives to the proposed course of conduct" because it specified that Galderma was free to retain any counsel it wanted; and (iv) Galderma had been represented by counsel in the waiver negotiation.

Macy's, Inc. v. J.C. Penny [sic] Corp., Inc. – Rejecting Disqualification of Jones Day

In 2013, a New York state court upheld a waiver in *Macy's, Inc. v. J.C. Penny [sic] Corp*.[8] In business tort litigation between the two retail giants, J.C. Penney sought to disqualify Jones Day from representing Macy's because Jones Day represented J.C. Penney in various intellectual property matters in Asia. However, J.C. Penney had signed an advance conflict waiver in 2008, stating that Jones Day was allowed to take on matters adverse to J.C. Penney so long as they were "not substantially related to any of [Jones Day's] engagements on behalf of J.C. Penney."

In deciding that J.C. Penney had waived any objection to Jones Day's representation of Macy's, the court cited the language of the waiver which stated that Jones Day's future clients "may be direct competitors of [J.C. Penney] or otherwise may have business interests that are contrary to [J.C. Penney]'s interests" and that the future client "may seek to engage [Jones Day] in connection with an actual or potential transaction or potential litigation or other dispute resolution proceeding in which such client's interests are or potentially may become adverse to [J.C. Penney]'s interests."

The court also relied on the following language to conclude that J.C. Penney had waived the alleged conflict presented by the Macy's engagement: "[P]lease note that your instructing us or continuing to instruct us on this matter will constitute your full acceptance of the terms set out above and attached." The court stated that "[i]t is undisputed that Jones Day continued to represent defendant with respect to defendant's Asian trademark portfolio thereafter and, thus, defendant accepted the terms of the agreement, including waiver of the alleged conflict at issue." The specificity and acceptance of the agreement were important to the court, as was the fact that it found J.C. Penney's "intellectual property litigation and trademark registration" matters in Asia to be sufficiently distinct from the Macy's litigation.

GEM Holdco, LLC v. Changing World Technologies, L.P. – Rejecting Disqualification of Schalm Stone & Dolan LLP

In *GEM Holdco*, one party to a joint defense agreement sought to disqualify Schalm Stone & Dolan LLP (which had been representing all defendants) once a conflict arose between the defendants. All defendants had signed a retainer letter with Schalm Stone which contained a waiver.[9] In reviewing the waiver, the court upheld it and allowed Schalm Stone to continue to represent certain defendants. The court decided that traditional concerns about confidentiality were superseded by the waiver. Further, because the retainer letter discussed how the firm would handle future potential conflicts between the defendants, the court rejected the disqualification attempt based on the former clients' informed consent.

Key Takeaways from Cases Rejecting Disqualification

What are the key takeaways from these cases?

The factors cited in *Galderma* provide a guide for how to craft effective waivers: (i) include an agreement about the process for handling future potential conflicts; (ii) explain the material risks associated with signing the waiver; (iii) explain that the client has a choice in signing the waiver or not; and (iv) make sure the client is represented by counsel (inside or outside) when signing the waiver.

Additionally, firms should consider just how "related" the potential matter is to the former engagement, even if a conflict waiver is in place. In *Macy's*, the key, but not only, factor appeared to be that the Asian trademark work was substantially distinct from the J. C. Penney's business tort litigation. The court also cited favorable language in the waiver that allowed an inference of agreement even though J.C. Penney had not actually signed and returned the waiver document. A process for handling future conflicts is also important as demonstrated in both *Galderma* and *GEM Holdco*. For instance, in *GEM Holdco*, the waiver identified which of the parties would be represented if a conflict arose.

Best Practices For Advance Conflict Waivers

So, what's a law firm to do? How can a lawyer draft an advance conflict waiver that will best withstand scrutiny and the challenges highlighted in the cases discussed above?

It is impossible to predict the future and difficult at best to obtain informed consent prospectively for an unknown future contingency. Nonetheless, the lessons learned from these cases provide some guidelines that lawyers can use to draft advance conflict waivers successfully and to obtain the necessary informed consent so that they can better protect their clients and themselves:

1. Clearly specify what the firm wants the client to allow in terms of the type of potential future representation and what the client has agreed to allow, including the possibility that future clients could be direct competitors of the current client. This may have addressed the concerns in *Mylan* and *Airgas* if the clients had signed waivers that allowed for future takeover bids.
2. Clearly specify what the firm is *not* seeking in the waiver.
3. Specify an agreed course of conduct for addressing conflicts when they arise, which Vinson & Elkins did with Galderma and which helped save the firm from disqualification.
4. Document the client's agreement regarding the specific steps that the firm will take to safeguard confidential client information and specify that these are for the client's protection and are not evidence of a prohibited representation. Concerns about confidentiality and whether a firm could truly protect a client's confidential information -- and also represent that client's adversary -- was central to Judge Lenihan's *Mylan* decision.
5. State that the law firm and client have discussed the possible consequences and implications of the waiver and the important considerations for the client. In the *GEM Holdco* case, the firm accomplished this by including specific terms about what would happen if a conflict arose between the parties to the joint defense agreement.
6. Recognize that it is important to periodically revisit, update, and revise existing waivers as the nature of the client representation expands or changes over time. Six years was too long to wait, according to the *Worldspan* court.
7. Tailor the waiver according to client's legal and business sophistication. In the *Galderma* opinion, the court gave significant weight to the fact that Galderma had a great deal of experience with engaging law firms and signing conflict waivers as a part of those engagements in the past.

8 Opinion Available online at: http://www2.bloomberglaw.com/public/desktop/document/Galderma_Laboratories_LP_et_al_v_Actavis_Mid_Atlantic_LLC_Docket_/1
9 Opinion Available online at: http://www.hinshawlaw.com/assets/htmldocuments/Court%20Docs/GEM%20Holdco%20v%20Changing%20World%20Technologies.pdf

8. Ensure that the client is represented by counsel when signing a waiver. This was a factor in *Galderma* that militated in favor of rejecting disqualification; Galderma was represented by inside counsel who had significant experience engaging outside lawyers and signing similar conflict waivers.
9. Consider including the type of language that was important to the court in the *Macy's* case. Many clients never respond to the law firm's waiver letter. Including the sort of language Jones Day used (which acknowledged the client's acceptance by its continuing to instruct Jones Day on the engagement) may fix the "failure to respond" problem and avoid a swearing contest.
10. Don't bury the conflict waiver; make it conspicuous.
11. Understand and comply with applicable professional conduct rules in relevant jurisdictions. As many of the foregoing cases demonstrate (*Airgas*, in particular), courts take the ethical rules regarding conflicts and client confidentiality seriously.
12. Update conflict waivers when the firm merges or when hiring lateral attorneys whose clients present current or potential future conflicts with current firm clients.

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Beazley on the Podium

On **September 17, 2015**, lawyers' professional liability claims manager Brant Weidner joins two defense lawyers and a former California Superior Court judge on a panel at the 2015 ABA Fall National Legal Malpractice Conference in Scottsdale, Arizona. The panelists will discuss the following: **"Location, Location, Location: The Decisions Involved in Venue Selection."**

Contact Information

Email comments, feedback or suggestions for future *Beazley Brief* topics to Brant Weidner: brant.weidner@beazley.com.

A library containing all past issues of the Beazley Brief can be accessed at any time through Beazley's lawyers' risk management website: www.beazley.com/lawyersrisk/.

Inside the Box

Beazley Brief Confidential – Coming Soon Via Email!

We are delighted to announce a new Beazley publication which provides a detailed report of claims trends, benchmarking and risk management recommendations derived from a thorough analysis of our lawyers' professional liability claims data. We call it the Beazley Brief Confidential (BB:C). The inaugural edition of the BB:C was mailed to our insureds in hard copy format earlier this summer.

We have received much positive feedback about the BB:C. Some recipients have requested an electronic copy in order to make it easier to forward to other members of their firms. We're writing to let you know that we will be sending the first edition of the BB:C - via email – to all of our insureds by mid-September. We encourage recipients to share it with other members of their firms.

As we reported in our earlier mailing, we expect to prepare and distribute three BB:C "episodes" in which we comment on the trends we have observed in major claims affecting the legal profession before, during and after the financial crisis. Like our insureds, we, as underwriters, are always striving to understand the lessons learned from past claims. In addition to highlighting some of these in the BB:C, we also look to provide guidance as to what our claims tells us about where risk management focus might best be deployed.

The next edition of the BB:C will be published in early 2016. We have hinted at some of the subject matter to come in the conclusion of the first edition. To cater to our many global clients, we will also be looking to share our analysis of claims with international dimensions in future episodes.

Later in 2016, we will prepare a third BB:C episode based on your feedback. We are anxious to hear your thoughts on topics not addressed in the first two editions. Based on your feedback, we will "drill down" into our claims data, with the goal of mining further claims analysis and providing further loss prevention "nuggets."

You can forward any return comments to either Ian Rose or Brant Weidner at the contact details below. Please don't be shy in sharing your thoughts, opinions and suggestions with us.

All of our BB:C reports, our usual *Beazley Briefs*, Beazley claims scenarios and much more are available on our risk management website. The link is below. To access the site, you simply have to insert your own email address in the login details and the first six characters of your policy number. For your convenience, we will include the first six characters of your policy number when we send the BB:C via email to you later this month.

www.beazley.com/lawyersrisk/

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