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ANDREWS KURTH

Superhuman Ethics: The Ethics of Industry and Issue Lawyering

Terminating Client Relationships to Solve Conflicts Problem – a/k/a the "Hot Potato" Doctrine[1]

Issue: This memorandum addresses the ethical issues associated with a lawyer's attempt to turn a current client into a past client for conflicts analysis purposes.

Summary of Most Pertinent Rules[2]:

- **1.2(c)[3]:** Allows lawyer to limit the scope of representation if the limitation is reasonable under the circumstances and the client gives informed consent.
- **1.3:** Requires lawyer to act with reasonable diligence and promptness in representing a client.
- **1.4(b):** Requires lawyer to explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation.
- **1.7**: "Current client" conflict rule prohibits representation (i) of one client directly adverse to another ***or*** (ii) when there is significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client, or a third person, or by the lawyer's personal interest.
- **1.9:** "Past client" conflict rule prohibits representation of client with interests materially adverse to the interests of a former client relative to a substantially related matter.
- **1.16(b):** Allows lawyer to withdraw from representing a client if withdrawal can be accomplished without material adverse effect on the interests of the client.

Discussion:

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[2] References to "Rule" means the ABA Rules of Professional Conduct unless otherwise noted.

[3] The District of Columbia, Florida, Georgia, New York, North Carolina, Tennessee, Texas and Virginia follow rules modeled after ABA Model Rules. California's Rules of Discipline follow neither the Model Code nor the Model Rules, but borrow considerable substance from each.

The hot potato rule and its potential exceptions will vary by jurisdiction. Accordingly, an attorney analyzing whether the a potential conflict of interest will be analyzed pursuant to current client or past client rules should consult the rules, case law, and legal ethics opinions applicable in the jurisdiction or jurisdictions that may govern the attorney's conduct (*e.g.*, where the attorney is licensed, in the forum where the attorney is appearing on behalf of the client). The attorney should be mindful of the potential distinction between whether an attorney's withdrawal from a client's representation will violate applicable professional rules and whether such withdrawal will result in liability to the client.

- **The Hot Potato Rule and Its Exceptions**

The conflict of interest rules are designed to avoid the situation in which an attorney may not be able to diligently represent a client due to a conflict of interest. *See, e.g.*, Model Rules of Prof'l Conduct R. 1.7 & 1.9. Rule 1.7 addresses a lawyer's obligation with respect to ***current*** clients, while Rule 1.9 addresses a lawyer's obligation with respect to ***past*** clients. Under Rule 1.7, a lawyer generally may not undertake representation of a new client that will be adverse to an existing client, whether the matter is related or unrelated to the representation of the existing client. Under Rule 1.9, a lawyer generally may undertake representation adverse to a past client if the matter is unrelated to any work the lawyer did for the past client (and subject to duties to protect confidential information). Although Rule 1.16 allows a lawyer to withdraw from representing a client as long as there will be no material adverse effect, a lawyer cannot withdraw under Rule 1.16's permissive withdrawal provision in order to turn a current client into a "past client" for conflicts analysis purposes. This is informally known as the "hot potato" rule.

The Restatement of the Law Governing Lawyers 3d § 132 seems to have adopted what has become known as the "hot potato" rule after the statement of the court in *Picker Int'l. v. Varian Assoc.*, 670 F. Supp. 1363, 1365 (N.D. Ohio 1987), that "a firm may not drop a client like

a hot potato, especially if it is in order to keep happy a far more lucrative client." Comment c to Restatement § 132 states that a client becomes a "former client" for disqualification purposes if the representation ends normally or if grounds for permissive withdrawal exist and the "lawyer is not motivated primarily by a desire to represent the **new client**." The comment further states that:

> If a lawyer is approached by a prospective client seeking representation in a matter adverse to an existing client, the present-client conflict may not be transformed into a former-client conflict by the lawyer's withdrawal from the representation of the existing client. A premature withdrawal violates the lawyer's obligation of loyalty to the existing client and can constitute a breach of the client-lawyer contract of employment [reference omitted].

Accord, e.g., International Longshoreman's Ass'n Local Union 1332 v. International Longshoreman's Ass'n, 909 F. Supp. 287, 293 (E.D. Pa. 1995) (when a conflict situation arises, the general rule is that attorneys cannot pick and chose to retain the more remunerative client).

The so-called "hot potato" doctrine has been addressed in reported cases from 16 states (including reported federal court cases in Arizona, California, Florida, Georgia, Kansas, Illinois, Nevada, New Jersey, New York, Ohio, Oregon, and Pennsylvania; and reported state court cases in Alabama, California, Delaware, Indiana, Massachusetts, and Montana). *See* Attachment A (table of reported cases addressing the "hot potato" doctrine). Legal ethics opinions from at least four states, moreover, have also addressed the hot potato rule or its exceptions.[4] The duty of

[4] Alabama State Bar Disciplinary Commission Op. 92-21 (1992) (law firm may not represent one client against another even if subject matters of suits are unrelated, and withdrawal from representation of one client will not make the situation of a conflict with former client); Connecticut Bar Association, Committee on Professional Ethics, Informal Opinion 98-24 (Oct. 28, 1998) (termination of existing client is an ineffective way to end a conflict with another existing client under hot potato rule, because the "duty of loyalty to an existing client cannot be evaded by withdrawing from the attorney-client relationship"); District of Columbia Bar, Legal Ethics Committee, Legal Ethics Opinion 317 (Nov. 19, 2002) (in considering the extent to which a client's revocation of consent to a conflict requires an attorney's withdrawal, the opinion cites Comment j to Restatement of the Law Governing Lawyers § 132, which is the comment embodying the "exception" to the "hot potato" rule); District of Columbia Bar, Legal Ethics Committee, Legal Ethics Opinion 272 (May 21, 1997) (rejecting broadest statement of the so-called "hot potato rule" as inconsistent with recognition of "thrust upon" conflicts as addressed in D.C.'s Rule 1.7(d), which allows an attorney to remain in a matter after an unforeseeable conflict has arisen); Massachusetts

loyalty and concerns for protecting confidential client information are most commonly cited in support of the hot potato doctrine.

Court consideration of the "hot potato" doctrine arises in the context of a motion to disqualify counsel, with the moving party asserting that there is a concurrent conflict and the counsel defending against disqualification typically asserting that the moving party is a "past client" on an unrelated matter. Courts considering disqualification commonly employ a flexible application of the "hot potato" rule that will consider:

- **prejudice** to both the moving and non-moving parties (including, cost, inconvenience, and risk that confidential information may be compromised);
- **origin of the conflict** -- that is, the extent to which concurrent adverse representation was foreseen versus "thrust upon" (e.g., the result of corporate merger) or the lawyer had a hand in creating the conflict (e.g., existing client uses other counsel to sue another existing client);
- **prompt withdrawal** by the lawyer upon discovery of the conflict.[5]

For example, courts have found that when a law firm has two clients and one of the clients sues the other, thus creating a conflict of interest, the lawyer may choose to represent the client that has been sued. *See, e.g., Tipton v. Canadian Imperial Bank of Commerce*, 872 F.2d 1491, 1498-99 (11th Cir. 1989); *Florida Ins. Guar. Ass'n v. Carey Canada, Inc.*, 749 F. Supp. 255, 261 (S.D. Fla. 1990). In an article titled, "Conflicts of Interest in Corporate Litigation," Samuel Miller phrased this situation in the following manner:

Opinion No. 2002-2 (June 26, 2002) (recognizing possible exception to hot potato rule stated in Opinion 92-2 when representation was permissible when undertaken and the objection by one client to the other client representation was not reasonably foreseeable at that time); Massachusetts Opinion No. 2002-1 (January 24, 2002) (recognizing and applying the hot potato rule to conclude that lawyer could not withdraw from ongoing representation of husband in order to represent wife in divorce against him); Massachusetts State Bar Op. 92-3 (1992) (law firm may not represent long-term client in a matter which is detrimental to another client's interests when the firm withdrew from the other client's ongoing and unrelated representation); Rhode Island Supreme Court Ethics Advisory Panel, Opinion No. 2000-1 (Feb. 10, 2000) (recognizing and applying the hot potato rule to conclude that lawyer could not withdraw from representation of agency and then sue agency on unrelated matter absent the consent required under the current client rule).

[5] *See generally* cases listed on Attachment A.

> Client A is suing Client B, but in this model the law firm chooses to represent Client B, causing Client A (who initiated the suit with other counsel) to move for disqualification. In this case, the movant has "created" the conflict, and thus the courts seem to favor the right of Client B to keep its preferred counsel. Some courts have disregarded the "time of filing" rule in such cases, thereby allowing a lawyer to terminate Client A after the complaint has been filed, so long as the withdrawal is done immediately upon the lawyer's discovery of the conflict. By permitting the firm to convert Client A into a former client, the courts can avoid disqualifying the lawyer by finding that the two representations are not substantially related.

48 Bus. Law 141, 195-96 (1992). The same is not true if the law firm attempts to represent Client A in suing Client B. In this situation, the courts usually disqualify the firm from representing the client who initiated the action against the other client. *See id.* at 194. One apparent rationale behind this rule is that the client "creating" the conflict should be the one to lose its preferred lawyer when both clients have equal claims to the loyalty of their lawyers. *See id.* Perhaps in recognition of the flexible approach widely recognized in case law, the Restatement of the Law Governing Lawyers 3d § 132, comment j, notes that a lawyer may withdraw in circumstances attributable to the client's actions:

> A lawyer may withdraw in order to continue an adverse representation against a theretofore existing client when the matter giving rise to the conflict and requiring withdrawal comes about through initiative of the clients. An example is a client's acquisition of an interest in an enterprise against which the lawyer is proceeding on behalf of another client. However, if the client's acquisition of the other enterprise was reasonably foreseeable by the lawyer when the lawyer undertook representation of the client, withdrawal will not cure the conflict. In any event, continuing the representation must be otherwise consistent with the former-client conflict rules.

Accord Geoffrey C. Hazard, Jr. & W. William Hodes, The Law of Lawyering, A Handbook on the Model Rules of Professional Conduct (2d ed. 1998) § 1.16:302 (Vol. 1, p. 484) (the hot potato rule "will not wash if applied uncritically, *whenever* a lawyer drops a client for the purpose of suing that client on behalf of someone else").

In *Florida Insurance*, the United States District Court for the Southern District of Florida discussed the applicability of Florida Rules of Professional Conduct 4-1.7 (dealing with

concurrent representation of clients with adverse interests) and 4-1.9 (dealing with representation of interests adverse to former clients).[6] *See Florida Insurance Guaranty Ass'n v. Carey Canada*, 749 F. Supp. 255 (S.D. Fla. 1990). The court noted that "Rule 4-1.9 mandates a lesser disqualification standard than does the concurrent representation rule as it does not prohibit the representation of *any* party with an interest adverse to a non-consenting client. Rather, the rule precludes representation of only those parties with interests adverse to former clients in substantially related matters or where the former client's confidences would be compromised." *Id.* at 260 (*emphasis in original).* In effect, if, upon learning of the conflict, the law firm immediately ceases to represent the client that created the conflict, then the conflict should be analyzed under the lesser standard of Rule 1.9 governing former clients. In discussing whether a law firm can convert a current client to a former client and thus qualify for the lesser standard, the court stated that it could be accomplished under the following conditions:

> When counsel, upon discovery and absent consent, immediately withdraws from a concurrent adverse representation, the proper disqualification standard is expressed in the former representation rule. Otherwise to require disqualification for the mere happenstance of an unforeseen concurrent adverse representation - where the representations are not substantially related and client confidences are not endangered - would unfairly prevent a client from retaining counsel of choice and would penalize an attorney who had done no wrong.

Id. at 261.

The United States Court of Appeals for the Eleventh Circuit seemingly endorsed this analysis. In *Tipton*, the court denied the plaintiff's motion to disqualify counsel despite a period of simultaneous representation where the defendant's counsel withdrew from representing the plaintiff when plaintiff sued defendant and counsel learned of the conflict. *See Tipton*, 872 F.2d at 1499. Without specifically addressing the issue, the court applied the former representation

[6] Rules 4-1.7 and 4-1.9 of the Florida Rules of Professional Conduct are patterned after the ABA's model rules.

standard of Rule 1.9 in refusing to disqualify counsel. *See id.* at 1499; *see also Carlyle Towers Condominium v. Crossland Sav., FSB,* 944 F. Supp. 341, 352 (D.N.J. 1996) (finding that disqualification of firm that previously represented subsidiary was not mandated where conflict arose when defendant merged with parent corporation of subsidiary); *Gould, Inc. v. Mitsui Mining & Smelting Co.,* 738 F. Supp. 1121, 1127 (N.D. Ohio 1990) (finding that where client created conflict of interest through merger and acquired subsidiary that was involved in litigation against another client of law firm, firm would be allowed to choose which client it would continue to represent); *Ex Parte AmSouth Bank*, N.A., 589 So.2d 715, 722 (Ala. 1991) ("[A] law firm may avoid disqualification by moving swiftly to withdraw from its representation of a client, so as to minimize the prejudice to each client concerned, provided that the law firm did not play a role originally in creating the conflict of interest.").

- **When Is a Client a Past Client?**

In circumstances in which a lawyer has no active matter for a client, the lawyer may wonder whether the client is a current or past one. If the lawyer completed the single discrete task for which the lawyer was retained, the client is a former one. *See generally* Model Rules 1.2(c) (allowing lawyer to reasonably limit the scope of representation with client consent), 1.3, Comment [4] (if lawyer's employment is limited to a specific matter, relationship terminates when the matter has been resolved), and 1.16, Comment [1] (ordinarily a representation in a matter is completed when the agree-upon assistance has been concluded). On the other hand, if a lawyer has served a client over a "substantial period in a variety of matters, the client sometimes may assume that the lawyer will continue to serve on a continuing basis unless the lawyer gives notice of withdrawal." *See* Model Rule 1.3, Comment [4].

An attorney's duty of communication under Rule 1.4 and duty to protect a client's interests upon termination under Rule 1.16 combine to place the onus of clarity regarding the

beginning and the end of the representation on the attorney and not the client. If a client's belief that a representation is ongoing is reasonable under the circumstances, and the attorney does nothing to indicate that the relationship has terminated, an attorney may not be able to treat that client as a "former" client for conflicts of interest analysis. *See, e.g.*, Virginia LEO 1785 (November 13, 2003); District of Columbia Opinion No. 272 (May 21, 1997) (finding current client relationship when client consults lawyer from time to time indicating a "continuing relationship punctuated by periods of inactivity" when client has reasonable subjective belief that it continues to be a client of the firm). *Accord Westinghouse Elec. Corp. v. Kerr-McGee Corp.*, 580 F.2d 1311 (7th Cir. 1978) (finding that a reasonable subjective belief can be the basis for the formation of an attorney/client relationship). Accordingly, to be a clear line for conflicts analysis purposes and to prevent application of the hot potato rule, the attorney must be able to point to communications making it clear that the client would have no reasonable subjective basis for believing that a continuing attorney-client relationship exists. Model Rule 1.3, Comment [4] makes clear that "[d]oubt about whether a client-lawyer relationship still exists should be clarified by the lawyer, preferably in writing, so that the client will not mistakenly suppose the lawyer is looking after the client's affairs when the lawyer has ceased to do so."

- **Ethically Permissible Withdrawals May Not Preclude Liability for Failure to Complete Scope of Work**

If an attorney is retained to complete a defined scope of work, the attorney may nevertheless ethically withdraw from such representation prior to completion if consistent with Rule 1.16 and the hot potato rule. *See generally*, Geoffrey C. Hazard, Jr. & W. William Hodes, The Law of Lawyering, A Handbook on the Model Rules of Professional Conduct (2d ed. 1998) § 1.16:302 (Vol. 1, p. 485) ("A definition of loyalty broad enough to encompass the mere act of dropping a client would convert the client-lawyer relationship into one of continuing servitude."). Just because such withdrawal does not violate applicable professional rules,

however, does not mean that the lawyer is free from any liability for failure to complete the agreed scope of work. Such liability will be determined generally as a matter of contract law (*e.g.*, as to scope of contractual commitment, right to terminate, damages for breach, etc.). *See generally*, Geoffrey C. Hazard, Jr. & W. William Hodes, The Law of Lawyering, A Handbook on the Model Rules of Professional Conduct (2d ed. 1998) § 1.3:106 (Vol. 1, p. 75-76) (observing that the client-lawyer relationship is fundamentally a contractual relationship and pointing to the law of contract for evaluating an offer and acceptance of professional employment).

Absent clear communications defining the "contractual" obligations, a lawyer's acceptance of a representation implies an obligation to perform "competently, promptly, without improper conflict of interest and to completion." *See generally* Model Rule 1.16, Comment 1. *Accord* Geoffrey C. Hazard, Jr. & W. William Hodes, The Law of Lawyering A Handbook on the Model Rules of Professional Conduct (2d ed. 1998) § 1.16:101 (Vol. 1, p. 466-67) ("until withdrawal is accomplished, the client is still a client and has a corresponding claim to the unstinting loyalty of his lawyer.")