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A Bad Economy Increases Risks for Lawyers

Experts may disagree as to whether we are in a recession, but there is no question that our economy has been in a weakened state for a lengthy time period, which may impact professional liability claims for lawyers. For example, virtually all areas of practice for lawyers showed an increase in claims as a result of the 2008-09 recession. As a result, lawyers should be keenly aware of liability exposure as professional liability claims tend to increase during bad economies. Financial concerns may tempt lawyers to engage in precarious behaviors—curtailing risk control procedures, accepting riskier clients, or taking cases in practice areas outside of customary course of business. Similarly, clients who may more easily forgive an error or perceived bad outcome to a matter may now consider their law firms as a deep pocket that can ease their economic woes.

In this challenging economic environment, law firms must remember the fiduciary duties owed to clients, the ethical duties imposed upon them by the Rules of Professional Conduct, and best practices for avoiding claims. Monitoring and responding appropriately to the following issues will help to minimize a law firm's claim exposure.

[While] law firms may have to expand their risk appetite in order to expand their law practices and revenues…some risks are so severe that law firms must reject them.

Avoid the Risky Client

Financial pressures may force some law firms to consider potential clients that they would probably decline in better economic times. Such law firms need to balance the need for increased revenue against the liability risks of accepting a marginal client. Client intake represents a critical component in endeavoring to avoid legal malpractice claims. Attorneys seeking to expand their client base should institute strong risk control protocols pertaining to their client intake process and trust their instincts when meeting with prospective clients. Some of the client intake procedures that law firms should consider implementing include:

- Establishing an independent client intake review committee for law firms of a certain size;
- Screening out the high risk or incompatible client. Such clients may have fired or sued previous law firms, have a history of fraudulent or criminal behavior, have unrealistic expectations about the merits of their case, or delay or fail to respond to the law firm's requests for information;
- Conducting a comprehensive review of any lateral hire candidates for conflicts of interest and assessing any clients they bring with them for compatibility with the law firm's existing clients[1]; and
- Training support staff on consistency and documentation in the client intake process.[2]

1 See CNA's *From Here to There: Elements of an Effective Screen When Onboarding a Lateral Hire*.
2 See ABA MRPC Rules 5.1: Responsibilities of Partners, Managers, and Supervisory Lawyers and 5.3: Responsibilities Regarding Nonlawyer Assistance.

During the consultation phase, the law firm should ensure that the client's case has merit, is within one of the law firm's areas of concentration, and that the potential client has the ability to pay any anticipated legal fees and expenses. If the law firm decides that the potential client is not worth the risk, it should send a declination letter to the potential client. Some cyber criminals also may pose as prospective clients in order to deceive the law firm into providing them with funds held by the law firm. To help CNA insured attorneys navigate the client intake process and avoid falling victim to a cybercrime, you may refer to *Are You Ready to Commit? Client Intake and Proper Client Selection*; *Scammers Targeting Attorneys*; *Alert: New Scam Targeting Lawyers Wiring Funds*; *The Remote-Ready Law Firm: Managing the Long-Distance Relationships*; and, *For Your Eyes Only: Securing Lawyer-Client Communications*.

Decline to Dabble

During tough economic times, some lawyers may be tempted to dabble in practice areas in which they have no experience in order to earn more law firm revenues. However, the risks may outweigh the rewards for lawyers who deviate from their traditional areas of practice. "Failing to Know/Properly Apply the Law" is one of the most common types of error that leads to professional liability claims for lawyers.[3] Lawyers dabbling in unfamiliar practice areas, where they are not well-versed in the substantive law and procedural requirements, face an increased vulnerability to committing this type of error. Unless lawyers are willing and able to devote the necessary time and resources to learning a new area of practice, and possibly having another lawyer who is experienced in the relevant practice area serve as co-counsel, such representations should be declined.[4] Look for CNA's upcoming risk control article that discusses the dangers of dabbling.

Think Twice Before Suing a Client for Fees

Another tactic firms often employ to boost their accounts receivable is to bring collection actions against clients who have not paid their invoices for legal fees and expenses. Notably, such collection lawsuits often result in counterclaims for legal malpractice. Law firms may have ample justification for bringing a collection action and strong defenses to any professional liability claim. Nevertheless, law firms may have to expend time, energy, and resources defending a legal malpractice counterclaim. Therefore, the decision to bring a collection action against a client should be made with careful forethought and only after all other avenues have been exhausted.

Having a direct discussion with the client, instead of sending another invoice, may resolve the issue. In other instances, such a discussion can cause a client to consider compromise options, such as agreeing to pay a discounted amount or entering into a payment plan to pay off the outstanding balance over time. These types of agreements avoid the need to bring a collection action and also reduce the risk of a legal malpractice claim.

If discussions with the client prove unfruitful in resolving the outstanding legal fees and expenses, weigh the following factors in deciding whether or not to bring a collection lawsuit:

- if the client were to bring a counterclaim, does the deductible on your lawyers professional liability policy equal or supersede the amount that you are seeking to recover from the client;
- are any of the fees and expenses excessive or difficult to justify;[5]
- is your client judgment proof or likely to file for bankruptcy as a result of a collection action; and
- did your legal representation of the client meet the standard of care.

See *Billing Blues: Best Business Practices for Fee Collection* for further information on best practices for billing clients and collection actions.

Guard Against Conflicts of Interest

Conflicts of interest constitute a leading cause of professional liability claims against lawyers and law firms. Financial concerns may lead law firms to slash expenses related to their risk control protocols, such as the personnel and resources devoted to conflict of interest checking systems. Bad economy or not, law firms owe a fiduciary duty of loyalty to their clients. If law firms can make cost reductions without sacrificing the capability and effectiveness of their conflict of interest checking system, such a money-saving move may be a sound law practice management decision. But saving a little money upfront in exchange for a weaker conflict of interest system and later expending money, time, and resources due to a professional liability claim arising from a missed conflict of interest issue becomes penny wise and pound foolish.

3 American Bar Association's *Profile of Legal Malpractice Claims: 2016-2019*, p. 24.
4 See ABA MRPC Rule 1.1: Competence.
5 See ABA MRPC Rule 1.5(a)(1-8), which cites factors to consider when deciding whether a fee is reasonable.

Law firms must not ignore conflicts of interest in order to obtain a more lucrative engagement at the expense of an existing client. Many conflicts can be waived if the law firms secures the informed consent to waive the conflict from each affected client and such consent is documented in writing.[6] In some cases, however, either a client will decline to waive the conflict or the conflict itself is so severe that it cannot be waived. In these instances, lawyers must abide by their duty of loyalty to clients and refrain from taking on the new client. The consequences for lawyers who betray their duty of loyalty to clients include not only the possibility of legal malpractice lawsuits but may also encompass disqualification motions, bar disciplinary complaints, sanctions, disgorgement of legal fees, and loss of reputation. See *Conflicts of Interest* for further information on common conflict of interest issues and risk control tips on how to avoid them.

Communicate Regularly with Clients and Discuss the Impact of a Bad Economy on Their Matters

During tough economic times, clients may require more reassurance from their lawyers than usual, which may lead to an increased need for communication between lawyers and clients. In addition to promptly complying with reasonable requests for information, lawyers also must keep clients reasonably informed about the status of their matters.[7]

Discussions with clients as to whether the changed economic landscape has altered their perspectives on their own matters also should be pursued. For example, if a client cannot afford a key expert witness' fee in a litigation matter, it may affect the value of the case and serve as an incentive to settle the matter early in the discovery process. Perhaps some clients will be more amenable to a lower settlement offer or conversely, will set a higher minimum settlement amount in order to offset losses elsewhere. Lawyers should be cognizant of their clients' objectives, offer advice on whether such objectives are reasonable, and how to best achieve their clients' goals. In extreme cases, lawyers may want to consider withdrawal or declining representation if a client's financial constraints will adversely affect the ability to competently and diligently represent the client.

Documenting your client file strengthens client communications and may protect lawyers against professional liability claims. A well drafted engagement letter with a narrowly tailored "Scope of Representation" provision will help set expectations at the outset of the attorney-client relationship. Throughout the course of the representation, lawyers should have a paper (or electronic) trail of correspondence with the client referencing any legal advice provided, summaries of discussions on the benefits and risks of a particular litigation or transaction strategy, and client decisions regarding settlement negotiations, among other issues. Memorializing these interactions is critical in the event that the client decides to act contrary to your advice, sets time or financial constraints upon your representation, or tells you not to pursue certain causes of actions, defenses, or other important issues.

See CNA's *Lawyers' Toolkit: 4.0*, *Giving Business Advice Versus Legal Advice—The Pitfalls*, and *Plan Your Route Before Getting Out: Attorney Withdrawal* for further information on this subject.

Address Errors Promptly

Lawyers may commit errors at any point in their careers, but as noted earlier, claims typically rise in a bad economy and financial pressures may increase the likelihood of an error that leads to a professional liability claim. Errors can run the gamut from minor and correctible to substantial and damaging.

If a lawyer makes a substantial error that would likely result in prejudice to a client's rights or claims, then the error must be disclosed to the client. The attorney should inform the client of the following:

- any steps that may be taken to attempt to mitigate the loss and whether the client consents to the attorney taking such steps;
- the client's right to terminate the representation; and
- the client's right to consult with independent counsel regarding the attorney's error.[8]

It is important for the lawyer to disclose the error without admitting any liability. A lawyer who admits liability presents the risk of waiving insurance coverage and assuming the burden of undue liability where extenuating circumstances may exist.

6 See ABA MRPC Rules 1.7: Conflict of Interest: Current Clients et al.
7 See ABA MRPC Rule 1.4: Communication.

8 Some jurisdictions require the lawyer to affirmatively state that the client may have a viable legal malpractice claim against the attorney due to the error. Attorneys should refer to their local rules on what they must disclose to clients regarding their own potential liability.

Lawyers should inform their law firm of the error. In addition, they must follow any law firm protocols providing guidance as to whom and how such a disclosure should be made in order to preserve attorney-client privilege. Notice of the error also should be conveyed to the law firm's insurer. In some instances, the insurer may assign counsel to assist in ways to minimize damage to the client and advising the lawyer on communications to the client when disclosing the error. Any discussion with a client regarding an error should be followed up by a letter highlighting the subject matter of the discussion, the disclosures made by the lawyer to the client, any instructions from the client, and the date that the discussion occurred. See *To Err is Human—A Guide for Attorneys on How to Manage Errors* for further information on this subject.

Conclusion

Although it is impossible to eliminate all risks in managing a law practice, the guidance noted above will assist law firms endeavoring to minimize their liability risks during turbulent economic times. On occasion, law firms may have to expand their risk appetite in order to expand their law practice and revenues. Such growth risks require sound risk control practices as noted in this article. And some risks are so severe that law firms must reject them. While it is impossible to predict with certainty when economic conditions will stabilize, law firms should periodically engage in an internal audit and work to eliminate all unnecessary or excessive risks in order to remain on solid financial footing.

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