Chapter 2: Governance of conflicts and new business intake

By Meg Block

Introduction
For many law firms, conflicts management is one of the most challenging elements of risk management. In the Risk Roundtable 2009 Law Firm Risk Management Survey, 41 percent of respondents ranked conflicts management as their top concern, and three-quarters of respondents included it in their overall list of concerns.1

Conflicts clearance can no longer be managed as a hub-and-spoke process with clerical staff and lawyers. This traditional model’s clerical core produces – because of lack of training and authority – over-inclusive and under-analyzed reports. The distributed recipients of these reports are time-constrained lawyers who are strongly incentivized not to look at conflicts issues too closely; they want the work. Involvement in conflicts clearance by an ethics lawyer or general counsel is by invitation only.

The risks associated with this model are simply too high to continue: party relationships in a global economy are too complex; competition for business and legal talent is too fierce; practicing lawyers are not specialists in ethics; and the consequences of a mistake in terms of expense and professional reputation are catastrophic.

The new governance model is a pyramid with a skilled research team that provides nuanced research to a centralized decision maker – be it an individual lawyer or a tight-knit clearance committee. This team has no personal stake in the outcome of the clearance decision; it places the interests of the firm above the special interests of the practitioner. This team also assesses business ethical conflicts; it analyzes the quality of the work, considers client relationships, and weighs the associated business risks as well as ethical ones.

The following discussion describes the distributed hub-and-spoke and centralized pyramid models in absolute terms. The truth is more complex: these two models are the endpoints of a spectrum of solutions. I find the contrast illuminating, not just simplistic, and hope you do too.

Background
The need for changes to the governance of conflicts clearance has been growing for 65 years. First, there has been an unrelenting drive towards corporate globalization since World War II, resulting in complexly structured multi-national corporations. The breadth of these corporate families makes the ethical duty of loyalty a complicated one to navigate.

Second, in the past twenty years there have been an unprecedented number of law firm mergers, which has increased law firm size, the breadth of their client base, and the likelihood of conflicting business relationships.

Third, in the wake of major corporate and accounting scandals at the turn of the
century, the relationship of lawyers and their clients was changed by new laws and revised ABA and state ethics rules. Section 307 of the Sarbanes-Oxley Act of 2002, modifications to the ABA Model Rules 1.6 and 1.13, and associated state ethics rules set up a fundamental tension between lawyers’ duties of loyalty and confidentiality to their clients and public expectation that upstanding lawyers will ‘blow the whistle’ on wayward ones. Law firm management has recognized the safest way to avoid the issue is to avoid problem clients. Hence the need for a new business and conflicts decision-making body that stands apart from lawyer and practice group interests and focuses on the greater good of the firm.

Fourth, in the years just preceding and following the 9/11 terrorist attacks, the US, UK, and EU passed a number of anti-money laundering laws to ensure that professional service firms ‘know their clients.’ The laws require due diligence to:

- Verify the identity of a client or service beneficiary;
- Verify the purpose and intended nature of the business relationship before it is established; and
- Actively monitor the business relationship.

To prove compliance, these tasks also add a record-keeping requirement to new client acceptance and conflict clearance.

Finally, lawyers are opportunistic and, consequently, mobile. Their success in changing firms depends on the clearance of conflicts. It cuts two ways. Laterals must be able to bring their most profitable clients with them, and the recruiting law firm must be sure that the lateral’s prior experience will not jeopardize its existing representations. As top legal talent is in high demand, these complex clearances must happen quickly.

In February 2009, the ABA House of Delegates approved changes to Model Rule 1.10, ‘Imputation of Conflicts Of Interest: General Rule,’ that make it easier for law firms to resolve conflicts of interest by screening a lateral from participation in a conflicting matter. Now that the model rule has been revised, practice standards will now evolve via state adoption of the change and case law, especially in the areas of client notification and consent. Other likely areas of interest include: documentation of firm policy and ability to prove compliance; and application of technology to ensure enforcement of a screen.

What’s needed?
The new model for conflicts clearance is based on the following irrefutable truths:

- Clearance must be based on all the facts.
- Clearance must be fast.
- Clearance must consider business as well as ethical issues.
- Clearance (or non-clearance) must benefit the firm, not the individual.

Following is a discussion on how these truths translate into governance.

_clearance must be based on all the facts_

Regardless of the governance model, conflicts and intake clearance must be based on all the facts, and those facts are increasingly complicated. There is a spectrum of clearance and intake services based on research, analysis, quality assurance, and documentation. The following sections show how the governance models stack up.
Throw it over the fence (hub-and-spoke model)
The most basic (and risky) governance model is the hub-and-spoke model, where clerical personnel simply search the party names provided by originating lawyers. No research is done to confirm whether the names are correct or if all pertinent names have been provided. The resulting reports may not even be reviewed for false hits; they are ‘thrown over the fence’ as is for the requesting lawyer to analyze.

Clerical staff report through intermediary managers to the executive director and there is minimal to no involvement of ethics lawyers. Staffing is negligible as there is no research, the searches take minutes to run, and lawyers bear the full burden of analysis. With this level of staff competency, maintenance of the conflicts data is rare. Staffing ratios can be as low as one conflicts clerk (with part-time back up) to 300 lawyers.

Research, screen, maintain, throw it over the fence (specialization model)
The top end of the hub-and-spoke model is to have more highly skilled staff conduct conflicts searches. Typical research includes:

- Confirmation of the proper spelling of party names;
- Verification that all pertinent party names have been submitted (based on area of law);
- Identification of corporate families for new clients; less consistently researched for adverse parties and other related parties;
- Comparison of party names with the names found on the US Treasury’s Office of Foreign Assets Control (OFAC) Specially Designated National (SDN) list or in specialist databases (such as World-Check); and
- Recent ‘newsworthy’ stories for new clients.

In this top-end model, researchers are divided into levels of expertise and specialization. The job titles vary widely and include clerks, coordinators, searchers, researchers, specialists, analysts, leads, and resolvers. For illustration, the job responsibilities of three tiers have been described and named simply Level One, Level Two and Level Three.

Level One
Level One is the entry-level position. Personnel perform all conflicts searches (including the
OFAC SDN or specialist databases) and are trained to remove duplicate and clearly false hits from conflicts reports. They also perform straightforward confirmation (such as phone calls to verify ambiguous party names).

Level Two
After four to six months, Level One personnel begin to be promoted to Level Two positions and Level Ones are replaced. Level Twos are responsible for the quality assurance of Level One work. They are given more complicated tasks, such as analyzing and annotating new client-matter and lateral-hire reports to highlight potential issues, researching corporate family membership, and maintaining corporate family trees and ethical walls in the conflicts database.

Level Twos are also responsible for the unceasing maintenance of the conflicts database; a significant task when one considers constant mergers and acquisitions, the transience of corporate families, the inevitable enjoining of new parties, and the need to update the description of a matter as it progresses. Finally, they are responsible for the maintenance of anti-money laundering documentation, terms of engagement (firm letters and outside counsel guidelines), and waivers.

Level Three
Level Three personnel are usually former practicing lawyers or highly experienced administrative personnel who have been promoted from Level Two. They review the triaged work of Levels One and Two. They are subject matter specialists (for example, litigation, corporate transactions, bankruptcy, intellectual property prosecution, lateral hiring), have frequent contact with originating lawyers, and drive the conflicts resolution process. They have the authority to resolve straightforward issues. Issues they cannot resolve are laid out for resolution by the originating lawyer. Level Threes are sometimes authorized to draft engagement, waiver, declination, and disengagement letters. Their actions are guided by frequent, formal contact with the general counsel, members of an ethics or business intake committee, and members of a hiring committee.

With the increased level of service comes increased professionalism and staffing. The ratio goes from 1:300 to 1:50. Professional certifications include paralegal certification, Masters of Business Administration, Masters of Library Science, and Juris Doctor (JD). As these professional degrees indicate, conflicts analysis requires sound reasoning, investigative and analytical skills, and strong business judgment. To analyze potential conflicts, the team must have a working knowledge of legal ethics, international business, and firm-defined positions on the

Figure 2: The specialization model

Chapter 2
resolution of conflicts issues. In addition, they require significant on-the-job training; a six-month ramp up is not unusual. Consequently, in this top-end model, they are employees with a high retention value.

An added benefit of this hierarchical structure is that it keeps personnel motivated through the long period of on-the-job training. As law firms move from the low to top end of the hub-and-spoke model, the administrative manager of the department also moves from a professional administrator to a lawyer. The JD credential is critical for credibility; as much as they loathe conflicts clearance, lawyers are reluctant to turn it over to anyone who has not been similarly trained.

Give them the answer (pyramid model)
Because of the riskiness of conflicts clearance and new client acceptance, the largest and most progressive law firms have centralized the entire process, usually under the auspices of the general counsel. As with the top-end hub-and-spoke model, in-depth research is tiered. Additionally, it is also focused on the business aspects of the matter, for example, the identity and suitability of new clients and the nature of the proposed work. The model changes to a pyramid because at the apex is a team of specialized lawyers responsible for clearance. They are responsible for deciding (in concert with practice group leaders, members of the management committee, and the general counsel) whether new work and new clients should be accepted. In this model the role of the originating lawyer is to provide sufficient information for a clearance determination to be made.

Clearance must be fast
In the hub-and-spoke model, clearance decisions are distributed to the requesting lawyers. Consequently, they control the time it takes to clear conflicts, secure waivers, and establish the terms of engagement – unless the situation requires escalation to a higher authority, such as a general counsel or intake committee. Lawyers’ complaints with this model focus on the poor quality of the information, the unintelligibility of conflict reports, and the consequent amount of work they have to do to clear conflicts, not the duration of time.

Not so with the pyramid model. Once the originating lawyers have submitted the background information for conflicts checks and new business intake, elapsed time becomes paramount. Clearance is expected within at most two days, and preferably within hours. Centralized staffs – especially in global firms – provide coverage 24 hours a day, seven days a week. To meet these time requirements (which are realistic from a competitive perspective), the staffing ratio in the pyramid model goes from 1:50 to 1:20.
Clearance must consider business as well as ethical issues

Adapting the old adage, “You can win the battle, but lose the war,” a firm can clear the conflicts battle and lose a client. Both general practice firms and practice boutiques must be attentive to client sensitivities, be they corporate family relationships, patent or trademark prosecutions, or subtle cross-practice challenges to loyalty. These business perspectives can only be provided by the firm’s most experienced business leaders and are particularly difficult to harness in the hub-and-spoke model, where the involvement of senior firm members is by invitation from the originating lawyer.

In the centralized pyramid model, on the other hand, the conflicts lawyer has the judgment and authority to involve the senior members of the firm when needed. Moreover, the conflicts lawyer has the stature to get senior members’ attention on a timely basis.

An alternative technique to surface client sensitivities is to circulate a new business report. These reports come in two flavors: the first publishes the description and associated parties of matters before approval; the second publishes the description, parties, and client-matter identification (ID) of clients and matters after approval. From a clearance perspective, the report of business under consideration is much more useful than the one that reports the fait accompli. The technique is not really effective, however, as the communication of the information depends on busy lawyers actually opening and reading the report.

Clearance (or non-clearance) must benefit the firm, not the individual

Many, many law firms characterize themselves as assemblies of solo practitioners. In firms with this culture, partners do not judge the clients and proposed business of others – although they do frequently complain about the big cases that got away because of small matter conflicts.

Firms that look at their client base critically and strategically inevitably implement a centralized new business clearance process in manual, semi-automated, or fully automated form. The benefits of formal, firm management review include:

- Objective consideration of whether a new client is a good client for the firm.
- Insertion of a neutral third party into head-on-head disagreements between partners.
- Formal oversight of proposed business arrangements; no more ‘giving away the store’.
- Formal review of billing and payment history for new matters of existing clients: why take on more bad business?
- Oversight by practice areas for ‘fit’ of work and staffing.

The consistency with which decisions are made can diffuse personal tensions and prune and reshape a firm’s client base over time.

A centralized conflicts clearance and new business intake process also leads eventually to a structured matter close and client disengagement processes, which mark the end of an active representation or relationship. Increasingly recognized for their importance, client and matter closing change the ethical considerations for conflicts of interest. It is possible to be adverse to a former client (Client A) as long as the new work for Client B is not substantially related to the work done for Client A. Matter closing also starts the retention period of the representation’s files. From a data perspective, matter closing is a milestone that is used to
update matter descriptions and associated party names. The marketing department uses the milestone to secure case studies and promote additional services. In short, additional rigor in closing matters and disengaging, as a result of the centralized process, leads to better client information and more efficient conflict analysis.

Can automation help?
Although expensive (it takes ‘a village’ to program all the tendrils of the conflicts clearance and new business intake process), automation does bring additional benefits including:

- Intelligent routing of information; straightforward decisions are expedited and tough decisions are sent on to those who can make them.
- Improved data quality through validated data entry.
- Increased efficiency via pre-population of known data and synchronized updates of firmwide systems; type once, use many.
- Time-based triggers to move decisions through bottlenecks or solicit updated information.
- Consistent gathering of intake documentation for long-term reference.
- Application of ethical wall and confidential security at matter inception.

In conclusion
The risks associated with conflicts clearance and new business intake can no longer be managed as a hub-and-spoke process with clerical staff and lawyers. A skilled, centralized team – likely to be led by a lawyer – is needed to provide nuanced research to a centralized decision-making body. This team must also assess business ethical conflicts, evaluate the quality of work, consider client relationships, and weigh the associated business risks. Their responsibility is to the firm, not individual practitioners. Automation, although expensive, helps with accuracy, speed, and documentation.

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References
3. For example, in 1986, AmLaw 100 firms had 25,994 lawyers; in 2008, AmLaw 100 lawyers totaled 81,992 – a threefold increase.
5. The Model Rules’ definition of screened applies to “situations where screening of a personally disqualified lawyer is permitted to remove imputation of a conflict of interest under Rules 1.10, 1.11, 1.12 or 1.18.”