INTRODUCTION

1 Lawyers typically act for more than one client. They owe duties to each client. Each client has its own interests which the lawyers must advance. At times the duties owed to, or the interests of, one client may conflict with those of another client or the interests of the lawyers.

2 “Conflict of interest” questions commonly arise where a law firm endeavours to act for different parties in a commercial or property transaction, acts in court proceedings against a former client, or acts for more than one party in litigation as occurs where a firm acts for both insurer and insured to defend or prosecute a claim. My paper deals with a number of Western Australian cases where conflict of interest questions have arisen.

In addition, following the collapse of HIH Insurance Ltd and its associated
companies questions of conflict in the insurance litigation context have been brought into the spotlight. I will discuss some of the cases that are relevant to this context.

LEGAL BACKGROUND

3 The Professional Conduct Rules of the Law Society of Western Australia include a number of rules that preclude a legal practitioner from giving advice or acting in litigation or a legal matter where to do so would conflict with the interests of a client. These rules (7.1 to 7.9) reflect obligations that arise in equity by reason of the fiduciary nature of the relationship between lawyer and client or because the lawyer often possesses information that is confidential to the client.

4 A lawyer who gives advice or acts in circumstances where there is or might be a conflict of interest may be exposed to being sued by the client for an injunction or equitable compensation for breach of fiduciary duty.

5 The principal fiduciary duties are (1) to act in the client’s interests (and hence not to prefer the interests of another party to those of the client) (2) to disclose material information and (3) not to divulge to some other party information that is confidential to the client. Occasions may arise where conflicting duties are or may be owed to different clients. These are the common “conflict of interest” situations where the firm cannot continue to act.
However conduct that conflicts with the interests of the client might also amount to a breach of a duty of care owed to the client or breach of the contract of retainer. There may be misleading conduct. In addition to equitable remedies breaches of duty or the conduct of the lawyer may give rise to a claim for damages.

Conflict of interest cases therefore raise issues not only of breach of fiduciary duty, but also breach of a general duty of care or the contract of retainer. In addition even in a case where there is no potential for breach of a duty of one of those kinds a court may grant a remedy against a lawyer to restrain possible misuse of confidential information or to control the conduct of officers of the court so as to maintain public confidence in the judicial system.

A law firm can act in circumstances that otherwise would be viewed as amounting to a conflict of interest where each party to whom a fiduciary duty is owed is fully aware of the relevant facts and freely consents to the firm continuing to act. The party is said to have given “informed consent”. The lawyer should make full and candid disclosure of the relevant facts and interests and generally should advise and facilitate the provision to the client of independent legal advice: *O’Reilly v Law Society of New South Wales* (1988) 24 NSWLR 204.

**WESTERN AUSTRALIAN CASES**
There is a number of comparatively recent Western Australian cases where these conflict of interest issues have been discussed. They include *Mallesons Stephen Jaques -v- KPMG Peat Marwick* (1991) 4 WAR 357, *Unioil International Pty Ltd -v- Deloitte Touche Tohmatsu* (1997) 17 WAR 98 and *Newman -v- Phillips Fox* (1999) 21 WAR 309. They are relevant in cases where:

9.1 A firm attempts to act against a former client who disclosed information that is relevant to interests of the new client;

9.2 A firm prefers its own interests (or those of another, possibly related, firm) to those of its client; and

9.3 Solicitors for one party in litigation become part of the firm that acts for the opposing party.


*Mallesons* concerned possession by the law firm of information that was confidential to the former client of the firm. The firm sought to act for a new client against its former client. A team of lawyers including three partners was instructed by the Commissioner of Corporate Affairs to assist to prepare briefs to counsel for the prosecution of a partner of the accounting firm KPMG Peat Marwick. There was a number of charges connected with the representation of the financial position of a company called Rothwells Limited. The law firm had previously been instructed by and had given advice to the accounting firm concerning audits of Rothwells and Mr
Carter’s involvement in those audits. The accounting firm obtained an injunction restraining the law firm from representing the Commissioner. This was so despite the agreement of the Commissioner not to seek information from any partner or employee of the law firm that would involve disclosure of information obtained from the accounting firm.

11 The following important propositions may be found in the reasons of the Court (Ipp J):

11.1 There mere fact that a solicitor has acted for a client in a particular matter will not, without more, entitle the client to restrain the solicitor from acting against him in the same matter: 360;

11.2 Solicitors may be restrained from acting against a former client on grounds involving disclosure of information subject to legal professional privilege and conflict of interest: 360;

11.3 The conflict of interest is between the continuing duty of a solicitor, owed to the former client, not to disclose, or use to the latter’s prejudice, that which he learned confidentially, and the interest which he has in advancing the case of his new client: 360;

11.4 If there is a real and sensible possibility that by acting for a new client the interest of the solicitor in advancing the case of that client might conflict with his duty to keep confidential information given to him by a former client, or to refrain from using that information to the
11.5 When a solicitor acts for a client he cannot withhold from the client any relevant knowledge that he has: 370;

11.6 The general rule is that in a partnership the knowledge of one partner is to be imputed as knowledge of the other partners: 374;

11.7 In a trial involving serious charges there could be an incalculable and prejudicial effect upon the state of mind, and therefore the demeanour, of a defendant who knows the prosecuting counsel has been briefed by the very firm of solicitors whom he previously consulted to advise him on several of the very issues that form the subject matter of the prosecution: 368;

11.8 It is of extreme public interest that no conduct should be permitted which is likely to prevent a litigant in a Court of Justice from having his case tried free from all matters or prejudice: 368.

12 The Law Society’s Professional Conduct Rules make it clear that a legal practitioner has an overriding duty to the Court. The duty of fidelity to the client’s interests is subject to this overriding duty. In conflict of interest cases it is important always to bear in mind that not only will the Court consider whether duties or interests conflict but will also evaluate the conduct or proposed conduct of lawyers in the context of ensuring that public confidence in the judicial system is maintained.
Unioil International Pty Ltd -v- Deloitte Touche Tohmatsu (1997) 17 WAR 98

13 Unioil concerned a law firm not acting in the best interests of the client by refraining from making enquiries that may give rise to information relevant to those interests. The national law firm Corrs had offices in different States that were asserted to be separate partnerships although they all traded under the same name. The Perth office of Corrs and the accounting firm Deloitte Touche Tohmatsu gave advice to the plaintiffs that led to them making a failed investment in a group of companies. By the time of trial the investment was worthless.

14 The plaintiffs sued both firms for damages for negligence, breach of contract and misleading and deceptive conduct. In addition Corrs were sued for breach of fiduciary duty. Two kinds of breach were alleged. The first was preferring the interests of the Sydney office of Corrs to the interests of the client. Secondly it was alleged that Corrs’ Perth office should have disclosed to the plaintiffs information possessed by the Sydney office that was relevant to the plaintiff’s decision whether to invest in the group of companies.

15 Both the accounting firm and Corrs were held liable to pay damages to the plaintiffs. The Court (Ipp J) held that there was a conflict between the fiduciary obligation of a solicitor in Corrs’ Perth office to take appropriate measures to protect the interests of the plaintiffs and his interest in protecting Corrs Sydney by refraining from making direct and vigorous
enquiries of a client of Corrs Sydney. That client had information that was relevant to the plaintiff’s proposed investment. However the Court held that Corrs was not under a fiduciary duty to disclose to the plaintiffs information that had been received by a partner of the Sydney office and was relevant to the plaintiffs’ decision whether to invest in the companies.

16 The following propositions emerge from the reasons of the Court:

16.1 A solicitor was in breach of the fiduciary duty owed to the client where there was a real and sensible possibility that he would be tempted either consciously or unconsciously to deal with a matter relevant to his client’s interests in a way that was least embarrassing to another party: 105-106;

16.2 There was a rebuttable presumption that the knowledge of one partner is to be regarded as the knowledge of other partners: 108. (On this issue the Ipp J qualified his previous decision in Mallesons);

16.3 It is an implied term of a solicitor’s contract of retainer that he keep his clients’ affairs secret and not disclose them to anyone except under the most special and exceptional circumstances: 108;

16.4 The nature of fiduciary duties is determined by the exigencies of particular circumstances, and no fixed or absolute rule applies: 110;

16.5 In a large firm of many partners it may be impracticable and even absurd to say that they are under a duty to reveal to each client, and use
for his benefit, any knowledge possessed by any one of their partners or staff: 110.

*Newman v Phillips Fox (1999) 21 WAR 309*

17 This was a case about lawyers seemingly changing sides in the course of litigation. Lawyers who had acted for a client in an arbitration ceased to do so and then became part of the law firm that acted for the other party. The Court granted an injunction restraining the second law firm from continuing to act in the arbitration. The injunction was in favour of a party who was not a former client of the firm.

18 Hely Edgar and Phillips Fox represented the opposite parties in an arbitration. Hely Edgar dissolved and ceased to act for the plaintiff. One of the partners and a number of employees joined Phillips Fox who endeavoured to continue to act in the arbitration. The former partner of Hely Edgar did not become a partner of Phillips Fox and any knowledge that had been obtained through acting for the plaintiff was not possessed by any partner of Phillips Fox. However the intention of Phillips Fox was that he would become a partner once the arbitration was at an end.

19 This was not a case where Phillips Fox owed any fiduciary duty to the plaintiff. Neither the firm nor any partner of the firm had acted for the plaintiff. Nevertheless the firm was restrained by injunction from continuing to act in the arbitration.
20 Confidential information was given by the plaintiff to an employee of Hely Edgar who became an employee of Phillips Fox. It included information about evidence, strategies, and strengths and weaknesses of the plaintiff’s case.

21 Phillips Fox had 20 partners and employed more than 80 professional staff. The former staff of Hely Edgar who had relevant knowledge worked in the insolvency group that was located on the 18th floor of the building where the firm was located. The partner who had acted for the other party in the arbitration worked in a different group, the corporate resources and construction group, that was located on a different floor. The two groups did not share secretaries and did not have day to day contact. Phillips Fox was prepared to move the relevant personnel in the corporate resources and construction group to premises that were physically separate from the firm’s ordinary premises. The relevant partner was prepared to undertake not to communicate with any solicitor at Phillips Fox about the arbitration proceedings other than one solicitor. Despite these facts an injunction was granted that prevented the firm from continuing to act for its client.

22 The following important propositions emerge from the case:

22.1 The justification for the grant of an injunction against a law firm may be founded upon one or more of three bases - namely, protection of confidential information, restraint from a breach of fiduciary duty in
the context of a conflict of interest, and the court’s control over the conduct of solicitors as its officers: 314;

22.2 The court can intervene if a solicitor possesses confidential information of a former client that is or might be relevant to a matter on which the solicitor is instructed by a second client: 314;

22.3 The court may intervene where a solicitor possessing confidential information is employed by or becomes a partner in a second firm that is acting in proceedings against the solicitor’s former client and there is a risk that information will be disclosed to those having the conduct of the proceedings against the former client: 314;

22.4 The exercise of jurisdiction cannot be based on a duty to advance the interests of the former client once the retainer has been terminated: 315;

22.5 The duty to preserve confidentiality of information imparted during the subsistence of the retainer continues notwithstanding the termination of the retainer: 315;

22.6 The court has jurisdiction to exercise authority over officers of the court as to the propriety of their behaviour: 315;

22.7 The duty to the court tends to be expressed in such a way as to emphasise the public interest in preserving confidence in the administration of justice and therefore in the appearance as well as the reality of independence: 316;
22.8 The notion that a lawyer can readily change sides undermines the appearance that justice is being done: 319;

22.9 There is a competing policy issue of the right of a client to have the services of a solicitor of choice and the need to preserve mobility of solicitors: 320;

22.10 Where there is evidence of a real and sensible possibility of misuse of confidential information the evidential burden shifts to the defendant firm to show that there is no risk of misuse: 322-323;

22.11 A “chinese wall” (or “cone of silence”) would not be sufficient to discharge the evidential burden if arrangements that were made were established *ad hoc* and did not involve some combination of the following:

22.11.1 Physical separation of various departments in order to insulate them from each other;

22.11.2 An educational program to emphasise the importance of not improperly or inadvertently divulging confidential information;

22.11.3 Strict and carefully defined procedures for dealing with a situation where it is felt the walls should be crossed and the maintaining of proper records where this occurs;

22.11.4 Monitoring by compliance officers of the effectiveness of the wall;
22.11.5 Disciplinary sanctions where there has been a breach of the wall.

ACTING FOR INSURERS

23 The law firm that is instructed by an insurer to act in litigation for an insured usually does so by virtue of the exercise by the insurer of its contractual rights to conduct the defence of or to settle any claim. A recovery action once a loss has been paid may be pursuant to true subrogation or a corresponding express contractual right. In all of these cases both the insurer and the insured are clients of the law firm.

24 The law firm owes to both duties in tort and fiduciary duties. It might owe contractual duties to both; a retainer with the insured being implied: *Pegrum -v- Fatharly* (1996) 14 WAR 92. There may be potential for the duties owed to, or the interests of, the insurer and the insured to conflict.

25 It is possible for the law firm to act under an express arrangement that falls outside the contract of insurance. For example in *CE Heath Underwriting and Insurance (Australia) Pty Ltd -v- Campbell Wallis Moule & Co Pty Ltd* [1992] 1 VR 386 the insured accountants’ professional indemnity policy empowered the insurer to take over and conduct the defence or settlement of any claim. After the writ was served the insurers' solicitors wrote to one of the insureds and advised that they would arrange for an appearance to be entered and attend on the return of a summons for directions on the strict understanding that by doing so they had not waived the underwriters'
reservation of rights and they required confirmation that they were to act on the basis outlined. They added that the alternative was for other representation to be sought. The insured agreed. A little over a week before trial the insurer’s solicitors advised that in reliance upon an exclusion clause in the policy the insurers denied liability. Nevertheless the insurer was held not liable to indemnify the insured accountants.

26 That is not always the result. In *Nigel Watts Fashion Agencies Pty Ltd v* *GIO General Limited* (1995) 8 ANZIC 61-235 an injured employee sued a landlord for damages at common law for negligence. The landlord in turn issued a third party notice against the employer claiming an indemnity pursuant to a clause in the lease of the premises from the landlord to the employer. The employee was injured when he entered a lift in the employer’s office premises.

27 The landlord’s third party claim for indemnity succeeded. The employer in turn sought indemnity against that liability from its employer’s indemnity insurer. This claim was not covered by the express terms of the contract of insurance. It was not a claim for damages.

28 The insurer had conducted the defence of the claim to judgment. The insured was not told about a settlement offer that was made to and rejected by its insurer. The New South Wales Court of Appeal appears to have accepted that if the insured had been told about the settlement offer it may well have agreed to contribute to the settlement which would have resulted
in a liability that was substantially less than the amount of the judgment that
was ultimately obtained against it. This was a loss of a "real chance" which
was held to be sufficient detriment to preclude the insurer from later denying
that the claim was not covered by the policy.

29 If a law firm acts against the interests of the insured it may find itself liable
to pay damages. In Groom -v- Crocker [1938] 3 All ER 394 on the insurer's
instructions its solicitors admitted negligence on the part of the insured as
part of a scheme whereby the insurer without the consent of the insured
attempted to obtain a commercial advantage pursuant to an agreement it had
with another insurer. The plaintiff's car was damaged by a motor lorry in a
collision caused solely by the negligence of the lorry driver. The insured
sued for and recovered damages from the insurer's solicitors.

30 A recent decision on the role of the law firm that acts for the insured on the
insurer’s instructions is Verson Clearing International -v- Ward &
Partners (1997) 9 ANZ Ins.Cas. 61-352. The defendant law firm Ward &
Partners received instructions from the SGIC to defend a claim for damages
brought against the SGIC’s insured by an injured worker. The services of
the worker had been provided by an employment agency. An appearance
and defence were filed. Subsequently the law firm formed the view that the
insured was not entitled to indemnity and gave that advice to the SGIC.
They were at the time still acting as the solicitors in the action for both the
insured and the SGIC. The insured engaged new solicitors and obtained an
order that the law firm deliver their file. The law firm appealed and submitted that advice given and steps taken by it from the time it was first instructed by the insurer were for the purposes of the insurer alone to the exclusion of the insured. The appeal was dismissed.

31 The court held that although the law firm effectively ceased to act for the insured after it had advised the SGIC that the insured was not entitled to indemnity it should have ceased acting earlier than that. Once it was apparent that a question arose as to the liability of the insured to indemnify the insured the law firm should have intimated to the insurer that it was not in a position to offer any advice as to that and the insurer would have to engage other solicitors if it wanted advice or legal representation on that aspect of the matter.

32 The court confirmed that a solicitor acting for an insurer exercising a “right of subrogation” in conducting the defence of proceedings in the name of the insured cannot continue to act for both where the interests of the insurer may not coincide with those of the insured. The law firm in that case was under a duty to act in the interests of both the SGIC and the insured and was not entitled to prefer one client to the other.

33 It is important to make reference to a recent unreported decision of the Victorian Supreme Court that concerns the issues of handing over the insurance law firm’s file, who is responsible for paying fees, and taxation of costs.
In *McKenzie -v- Director-General of Conversation and Natural Resources* [2001] VSC 220 (BC 2001, 04173) Gillard J of the Victorian Supreme Court had before him a summons for solicitors acting for insured seeking an order that their former solicitors who had been instructed by HIH Insurance hand over their litigation files. The plaintiff suffered from quadriplegia following a diving accident. He brought a claim for damages against a number of defendants who were insured by HIH. It instructed its solicitors. There was very little contact between the insurance law firm and the insureds. After the collapse of HIH Insurance the insureds employed their own firm of lawyers to act. They asked the insurance law firm to hand over its file. It agreed to do so if certain undertakings were given. The undertakings were not forthcoming. It held on to its file and stated that it proposed to enforce a lien for its costs.

Gillard J said that it was clear that a solicitor had a lien over documents in respect of unpaid costs and was not obliged to hand over documents to a client unless the lien was satisfied. The contract of insurance was not before the court but the parties agreed that it contained a term to the effect that the insurer had the right to take over the defence of any proceeding and conduct it on behalf of the insured. Gillard J held that where an insurer retained solicitors with the permission of the insured, pursuant to a contract, a solicitor client relationship was created between the insured and the
solicitors. There was a retainer between the insurance law firm and the insurer and between the insurance law firm and the insured.

36 Gillard J held that the costs incurred by the solicitor were in fact costs incurred on behalf of the insured. The retainer between the solicitor and the insured, unless there was a provision to the contrary, obliged the insured to pay the legal costs incurred on its behalf. Gillard J held that the insurance law firm was entitled to look to the defendants for the costs incurred to the point where its services were terminated. The entitlement to costs established the right of lien over the documents in its possession. He acknowledged however that the defendants were entitled to exercise their rights concerning the preparation of a proper bill of costs and compliance with statutory provisions concerning the payment of costs.

CONCLUSION

37 “Conflict of interest” cases include but extend beyond cases of breach of fiduciary duty. Where conflict occurs remedies against the offending law firm may not be confined to equitable remedies of injunction or equitable compensation. Other remedies may include damages for breach of a general duty of care, or breach of contract, or the remedy of damages for misleading conduct.

38 The decided cases reveal many unsuccessful outcomes for lawyers. These outcomes may suggest that in cases of doubt lawyers should cease to act. Failing to do so may lead to a situation of conflict of interest and exposure
to one or more of an array of equitable and common law remedies. In addition breach of the Professional Conduct Rules may amount to professional misconduct.

The title of this seminar “Terms of Engagement” with its military connotation may be an appropriate reference to the choice faced by a solicitor in many cases. Soldiers are not lawyers and lawyers are not soldiers. If there appears to be a conflict looming on the horizon it may be preferable to view it as a potential minefield rather than a battlefield.

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26 June 2002