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Beazley Brief

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Disaggregation: An Emerging Issue

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Large, complicated legal representations increasingly involve a team of service providers. The risks of these "disaggregated" legal representations—a concept that is identified and discussed at length below—might best be illustrated with an example.

Imagine this scenario (based loosely on the Qualcomm v. Broadcom case): in the middle of a major trial, a judge is conducting a sidebar conference during which one lawyer accuses the other of hiding key documents. The accused lawyer indignantly and confidently replies that all the documents have been produced and that her client knows of no other responsive documents.

In making her reply, the accused lawyer is necessarily relying upon not just the team of lawyers at her firm but also the cumulative work product of (i) her client's in-house counsel and in-house paralegals; (ii) the client's corporate IT department; (iii) the e-discovery vendor she hired; (iv) the law firm that her client hired to act as co-counsel for part of the case; and (v) the temporary lawyers she and the client hired to do document review.

As it happens, the lawyer's comments during the sidebar were literally false—even though they were made in good faith. The judge, angered at the failure to produce documents, decides to impose sanctions. The lawyer and her client, who are both disappointed and angry, now face each other antagonistically. Who's at fault? Who's to blame? And who pays? With so many people involved in the process, these questions aren't easy to answer. The lawyer and the firm's management committee hope that somewhere there is a document that details which service providers were responsible for which tasks. A desperate search for a helpful email ensues.

What is "Disaggregation?"

These days, sophisticated clients often break legal representations into pieces and assign responsibility for different tasks to an appropriate service provider. I call this a "disaggregated" representation because the tasks are broken apart and parceled out.

In some ways, disaggregation is similar to "unbundled" representations. An "unbundled" representation describes situations where a client, who cannot afford to pay a lawyer to handle an entire case, splits up various tasks between the lawyer and the client in an effort to save money. In contrast, disaggregation is driven by sophisticated clients who turn to other expensive service providers to handle various aspects of cases.

Many lawyers remember the old adage that "the client controls the objectives and the lawyer controls the tactics." While that is not quite what Model Rule 1.2 says (it says that clients control objectives and lawyers shall "consult" with the client as to tactics), sophisticated clients have taken control of case tactics for many years. Many of these clients are companies with general counsel who were themselves partners at large law firms, and who have managed relationships from both sides. We might date this trend to 1992, when the "DuPont Legal Model" (now in its fourth edition) was first introduced.

The DLM emphasizes the need to designate Primary Law Firms and Service Providers, and then to work collaboratively with Firms and Providers on strategic partnering—which should result in excellent and efficient service at reasonable prices. Through various means, the DLM and similar initiatives have revolutionized the way corporate clients manage outside law firms. And that trend will only accelerate.

The primary incentive for disaggregation is the high cost of outside counsel. In the last decade, the indicia of lawyers' incomes have continued to accelerate: profits per partner are up, first year salaries at large law firms now display a severely "bi-modal" distribution and the pressure to bill more hours continues unabated. These trends demand price competition, especially when, for example, those highly-paid first year associates are doing document review that could be competently done at much lower billing rates. At the same time, the practice of law has become more complex—a trend that demands specialization and division of labor. For example, large litigations that involve "electronically stored

information" (ESI) can require the help of various technical specialists.

These converging trends have led to a variety of disaggregation techniques. Clients may (i) regulate who at the firm works on the matter; (ii) retain for themselves certain tasks, such as discovery; (iii) ask the firm to partner with a familiar e-discovery vendor; (iv) ask the firm to partner with a boutique law firm that specializes in discovery; (v) assign the document review to temporary lawyers in the US or even abroad; (vi) assign a second firm to handle a portion of the case; or (vii) assign a second law firm to take the lead for the trial.

By engaging in disaggregation, in-house counsel are quite properly protecting the interests of their clients. That protection can be implemented through sophisticated contracting techniques such as a "request for proposal," terms and conditions or extensive policies and guidelines. Law firms, which are typically less innovative and more traditional than corporations, are lagging behind their clients on their initiatives to control the risks of this type of engagement.

Considering the Risks of Disaggregation

While disaggregation is perfectly appropriate[1], it does raise concerns.

What are the ethical limits of delegation? How tenuous can the firm's relationship be to the work that is done on the matter? In many of the cases where courts opine on the limits of delegation, the results aren't good for the lawyers. Indeed, the ethics rules require lawyers to adequately supervise and be responsible for subordinate lawyers and non-lawyers[2]. The rules also forbid lawyers from enabling non-lawyers to practice law[3]. While those rules have laudable goals and restrict the tasks that a lawyer can delegate, they also can require clients to pay large fees for tasks that can be competently done by non-lawyers.

What are the dangers? The most obvious danger of disaggregation is that balls will be dropped because no one knows who is responsible for a given task. One of the greatest risks for law firms is the failure to adequately document the existence and nature of the attorney- client relationship—to document who is, and who is *not*, the client, and to document what is, and what is *not*, in the scope of the representation. Disaggregation multiplies that problem.

Because lawyers are chronically pressed for time, they may overlook the importance of thoroughly documenting and tracking the disaggregation. There may not be a good record of who was doing which tasks. If the engagement ends successfully, that failure may never cost the lawyers anything. But, if the matter turns out poorly, the lawyer may be left holding the bag even if she has not performed beneath the standard of care.

Ethics rules and legal doctrines limit lawyers' ability to disclaim responsibility for the handling of a legal matter. The only good defense may be a contemporaneous document to or from the client showing that the client assigned a particular task to a service provider other than the law firm.

If there is a single take-away from this discussion, it is this: *law firms must counsel their client on the risks and advantages of disaggregated representations, must document the client's instructions, must document ongoing changes to those instructions and in general must create a written record to protect the client and the firm by detailing who was responsible for what tasks.*

What are the contractual issues? Lawyers must be careful not to inadvertently let the other service providers off the hook. E-discovery vendors often utilize contracts that limit their own liability—and in some cases actually ask the law firm to indemnify the vendor for the vendor's negligence! Obviously, law firms need to read those contracts carefully. It is for *the client* to decide whether or not it wishes to accept contract terms that may affect the client's ability to recover damages for negligence.

One way to manage that risk is to counsel the client on the risks of such clauses but to have the client's lawyers sign the vendor's contract. That solution may not always be possible. When it is not, the waiver of liability for the vendor's negligence is such an important decision that the firm should document that it counseled the client about the pros and cons of accepting a vendor's disclaimer of liability. If the vendor makes a costly mistake, the law firm will not want to rely upon memories of its oral advice to the client and the client's oral instructions to accept the vendor's contract.

What are the risks of a "hollowed out" representation? Taken to an extreme, disaggregation can result in the "hollowing out" of a representation to the point where the matter no longer makes economic sense. A matter that does not make economic sense for the law firm is a matter that raises the law firm's risk profile. This is an issue that requires the firm to communicate candidly with the client, and vice versa.

If there is a category of matters that do not make economic sense for the firm, it may be able to find a way to handle the matter with lower costs and still provide competent service. Firms are experimenting with innovative approaches such as the creation of tiers of staff lawyers who are not on partnership track, the outsourcing of certain tasks and the use of sophisticated paralegals. That is exactly the kind of "strategic partnering" that clients want, and it can help bind the firm and client to each other over the long run. If the disaggregated matter no longer fits the firm's cost structure, the firm can still provide a useful service in helping the client find the right way to manage the matter.

On occasion, the would-be rainmakers within a firm may push to undertake "hollowed out" representations. The rainmakers fear that, if the matter is sent to a different service provider, the client will leave the firm for all matters. The firm needs to work with its rainmakers so that they have the internal discipline to avoid this practice (firms should have some institutional checks on the process as well). Partners can be required to seek management approval for these sorts of arrangements and the

1 The ABA's Standing Committee on Ethics and Professional Responsibility issued its Formal Opinion 08-451 on August 25, 2008. The opinion addresses the outsourcing of legal work and notes that outsourcing "is a salutary trend in a global economy."
2 Model Rules 5.1 - 5.3
3 Model Rule 5.4

accounting and finance department can be instructed to alert the firm's general counsel to unusual terms in an engagement. No firm wants to undertake a legal representation where its only added value is the potential to be a source of recovery if the matter turns out poorly.

What does the law firm litigator need to think about? The lawyers' ability to meet their duty of candor to the court cannot be compromised by a disaggregation. Whether or not there is disaggregation, courts expect that each signed pleading and each oral representation are ones upon which the court can rely. Even if courts apprehend the disaggregated nature of the representation—and some do not—courts naturally (and reasonably) insist that lawyers who speak to the court have adequate support for what they say.

Mitigating the Risks of Disaggregation

What can lawyers do about the disaggregation risk? They can make sure that judges and magistrates understand how law is actually practiced. Also, where a client wishes to retain certain tasks in-house, lawyers can, and should, inform the client of the expectations of the judges. They should also work with the client to ensure that their litigators have sufficient understanding of the disaggregated representation to vouch for the process in court.

ABA Formal Opinion 08-451 notes that, when a lawyer outsources any work in the course of an attorney-client relationship, he retains the duty to ensure that the work is done competently and ethically and with the appropriate disclosures to the client. A lawyer also must ensure that the work is done without unauthorized disclosure of the client's confidences and in a reasonable way (Model Rule 1.5). Although Formal Opinion 08-451 offers helpful guidance about the lawyer's duty when delegating, it focuses mostly on lawyer-driven outsourcing rather than client-driven disaggregation. Hence, it offers little guidance on a law firm's management of the risks of disaggregation.

In the next few years, I predict that we will see opinions in which judges take in-house lawyers to task for failing to adequately perform some of the tasks they retain in-house. Law firm lawyers need to protect their clients by anticipating that danger and working with their clients to structure and monitor a disaggregation so as to avoid mistakes.

The risks of disaggregated representations are real and are only going to increase because it makes economic sense for clients to try to structure their engagements that way. We have seen sanctions awarded where the outside firm and the client have disagreed over who was responsible for which tasks and we have seen law firms sue their e-discovery vendors. Firms need to raise internal awareness of these risks, to meticulously document and monitor a disaggregation and to realize that at some point an extremely disaggregated representation may not make sense for the firm.

We welcome your feedback on this bulletin, and encourage you to email us with comments, observations or future topics for us to address, by contacting: straightanswers@beazley.com.

Please feel free to circulate this bulletin within your firm, and let us know if you are a reader who would like to be added to, or indeed removed from, the distribution list.

Inside the Box

Beazley expresses its gratitude to John Steele for his preparation and submission of this article on disaggregation. John is a frequent speaker and writer on topics related to the practice of law. He is a Lecturer in Legal Ethics at UC-Berkeley and Stanford Law School and is a member of the State Bar of California. We are pleased to be able to offer his insights here.

Beazley's LPL team has launched a risk management website for clients and brokers. The site is located in the lawyers section of the Beazley website at www.beazley.com/lawyers. It contains a wealth of information on risk management trends and tips to mitigate or avoid malpractice exposures. In particular, the site contains full details of Beazley's network of risk management service providers who are available to assist clients on preferential terms. We have assembled a 'best of breed' list of these providers, who are experts in issues ranging from records retention and e-discovery to reputation management.

Beazley policyholders can access the website by keying in the first six digits of the policy number (for Lloyd's policyholders, the Beazley policy number is located on the back page of the Lloyd's policy).

Update

As we reported in Issue 14 (entitled "Does Attorney-Client Privilege Protect Intra-Law Firm Communications?"), the attorney-client privilege may not protect a communication between a lawyer and his firm's in-house counsel about a current client representation particularly where there is or may be a conflict between the interests of the client and the law firm. We noted that many jurisdictions have adopted this premise as their standard (the most recent decision is Asset Funding Group LLC v. Adams and Reese LLP, (2008 WL 4948835, E.D. La., November 17, 2008) but we also suggested that there were other authorities and some recent case law that presented a more reasoned approach. One of the authorities we identified was New York State Bar Opinion 789 which suggested that no conflict existed when a law firm "investigates its legal and ethical obligations" in connection with an existing representation. On October 17, 2008, the ABA Standing Committee on Ethics and Professional Responsibility issued Formal Opinion 08-453 which appears to echo the New York State Bar (see 24 Law. Man. Prof. Conduct 616 (2008)). The Committee reasoned that an in-house ethics consultation about a current engagement does not give rise to a *per se* conflict between the firm and the client. Instead, it concluded that whether a conflict arises depends on the nature of the consultation and the respective interests of the firm and its client at the time. The Committee distinguished between a discussion geared to help a lawyer conform to ethics standards and a consultation the main purpose of which was to protect the interests of the consulting lawyer or the firm, typically for action already taken. Continued vigilance on this evolving issue is warranted.

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