

CONFLICTS OF INTEREST

The Professional's perspective

Recap – The Essence of the Problem

1. For this section of the seminar we are considering the difficulties which conflicts create for the professional who
 - (i) is advising
 - (a) two sets of trustees
 - (b) the trustees and a beneficiaryor
 - (c) a number of beneficiaries;("the two clients situation")
 - (ii) has advised one of those individuals or bodies and now proceeds to be instructed by another, or perhaps another institution such as a bank which for example, wishes to take security for a loan. ("the former client situation");and
 - (iii) the situation in which the professional has an interest itself in the trust or in the transaction in question in some way; ("the professional/personal situation").

This note is intended only as a summary of the applicable principles and recent case law and should not be relied upon as a definitive statement on a detailed subject which has been considered recently at length, in the context of directors' duties.¹

2. The question of conflicts is likely to arise most often in the case of solicitors and most of the case law concerns the legal profession with a few variations relating to accountants acting in or with a view to litigation. However, you

¹ Ultraframe and Gadget Shop cases: Ultraframe (UK) Ltd Fielding [2005] EWHC 1638 and Wilkinson v West Coast Capital & Ors [2005] EWHC 3009 (Ch)

may also come across it possibly, in relation to actuaries or forensic accountants. I should mention at this stage, that the Solicitors' Practice Rules 1990 were amended on 5 May 2006 to include new provisions in relation to conflicts, confidentiality and disclosure to which I will refer below.

3. The essence of the problem as it applies to professionals is of course, their duty of "single-minded loyalty" to their client's best interests. The professional must be able to render his services without any inhibitions. He must be able to give it all his energy and what is more, use all the information, strategies and resources at his disposal, for his client. Accordingly, there can be no conflict of duty and interest, whether personal or that of the firm as a whole, or a situation in which there is a conflict of duties between one client and another. As Lord Millett put it:

"The fiduciary must take care not to find himself in a position where there is an **actual conflict** of duty so that he cannot fulfil his obligations to one principal without failing in his obligations to the other"

4. This will all seem relatively obvious. A fiduciary is subject to the "no conflicts" rule. Equally, the proposition that a fiduciary and therefore, a professional must not make a profit (other than his contractual fees), for his own benefit or those of a third party without the informed consent of his principal stems straight from "the no profits rule".
5. However, both these absolutes can in some circumstances, be qualified if the appropriate quality of consent can be obtained. The professional, for example, may in some circumstances act for principals with **potentially** conflicting interests if he can obtain their informed consent.

6. Where is the line to be drawn and how, if at all can the conflict be managed? These questions have troubled the solicitors' professional at least, for more than a century. It seems that other professions have only just realised the complexity of the position in which their work places them!

Two clients at the same time

7. A case with which you will all be familiar and which is perhaps the paradigm, is Moody v Cox & Hatt [1917] 2 Ch 71. It concerned an action for rescission of a contract of sale of a public house and four cottages, with a counterclaim for specific performance. The vendors were a solicitor and his clerk who were selling in their capacity as trustees of a will trust. The solicitor had also acted for the purchaser in the transaction. They were under a duty to obtain the best price for the beneficiaries of the trust but at the same time, the solicitor was required to use his skills and knowledge to further his client's best interests. Lord Cozens Hardy MR concluded at 81:

“A solicitor may have a duty on one side and duty on the other namely, a duty to his client as solicitor on the one side and duty to his beneficiaries on the other but if he chooses to put himself in that position it does not lie in his mouth to say to the client, “I have not discharged that which the law says is my duty towards you, my client, because I owe a duty to the beneficiaries on the other side”. The answer is that if a solicitor involves himself in that dilemma it is his own fault. He ought before putting himself in that position to inform the client of his conflicting duties, and either obtain from that client an agreement that he should not perform his full duties of disclosure or say - which would be much better – “I cannot accept this business”.

8. Not much sympathy there then! Lord Walker in the recent House of Lords decision of Hilton v Barker Booth & Eastwood [2005] 1 WLR 567 considered this case and concluded:

“Since Hatt and Cox were selling as trustees, they had a duty to their beneficiaries to obtain the best price reasonably obtainable. It was argued that this modified the extent of Hatt’s duty, as a solicitor to Moody as his client. That argument was decisively rejected.”

9. However, there had been some movement away from the absolute in all circumstances, in the case of Clarke Boyce v Mouat [1994] 1 AC 428. Lord Jauncey, giving the judgment of the Privy Council stated at 435,

“There is no general rule of law to the effect that a solicitor should never act for both parties in a transaction where their interests may conflict. Rather is the position that he may act provided that he has obtained the informed consent of both to his acting. Informed consent means consent given in the knowledge that there is a conflict between the parties and that as a result the solicitor may be disabled from disclosing to each party the full knowledge which he possesses as to the transaction or may be disabled from giving advice to one party which conflicts with the interests of the other.”

10. These issues have been explored more recently by the House of Lords both in the case of Prince Jefri Bolkiah v KMPG [1999] 2 AC 222 per Lord Millett, which in fact, was concerned with the protection of confidential information belonging to a former client and most recently, as I have already mentioned, in Hilton v Barker Booth & Eastwood, (supra), per Lord Walker. Lord Walker’s analysis of the position of a solicitor who acted for clients with conflicting interests, had confidential information from a previous dealing with one of them and managed also to obtain a personal interest in a transaction in which it was instructed for both clients, is instructive!
11. To summarise the relevant background, a firm of solicitors having previously acted for one client B, in proceedings which resulted in him being

imprisoned for offences of participating in the management of a company whilst an undischarged bankrupt, fraudulent trading and obtaining credit while an undischarged bankrupt, acted for a new client in a property development deal in which the new client would develop the site and sell it on to B. B at that stage had been released on licence. Without telling the second client about B, the solicitors acted for both the new client and B in the property transaction, negotiated a reduced deposit for B, obtained a bank loan and advanced cash to B. B refused to complete on the transaction or to vacate a caution. The first client decided to rescind the contract and it was at this stage that the solicitors informed him of the conflict and that he should take separate advice. The bank enforced its security and the business of the client collapsed. He sought contractual damages from the solicitors.

12. Lord Walker analysed the fiduciary and contractual nature of a solicitor's relationship with his client and concluded at 575, as follows:

“A solicitor's duty to his client is primarily contractual and its scope depends on the express and implied terms of his retainer. The relationship between a solicitor and his client is one in which the client reposes trust and confidence in the solicitor. It is a fiduciary relationship. But not every breach of duty by a fiduciary is a breach of fiduciary duty A solicitor's duty of single-minded loyalty to his client's interest, and his duty to respect his client's confidences, do have their roots in the fiduciary nature of the solicitor-client relationship. But they may have to be moulded and informed by the terms of the contractual relationship”.

He went on to quote the following passage from *Farrington v Roe McBride & Partners* [1985] 1 NZLR 83 at 90

“A solicitor's loyalty to his client must be undivided. He cannot properly discharge his duties to one whose interests are in opposition to those of

another client. If there is a conflict in his responsibilities to one or both he must ensure that he fully discloses the material facts to both clients and obtains their informed consent to his so acting. . . . And there will be some circumstances in which it is impossible, notwithstanding such disclosure, for any solicitor to act fairly and adequately for both.”

Lord Walker concluded that it was common ground that the solicitors could not properly act for both vendor and purchaser on the development contract. He went on to hold

“It is a solicitor’s duty to act in his client’s best interests and not to do anything likely to damage his client’s interests, so far as this is consistent with the solicitor’s professional duty. To disclose discreditable facts about a client, and to do so without the client’s informed consent, is likely to a breach of duty, even if the facts are in the public domain.”

13. The thrust of these authorities therefore, is that if a solicitor puts himself in a position of having two irreconcilable duties it is his own fault. If he has a person financial interest which conflicts with his duty, he is even more obviously at fault. However, if informed consent can be obtained and the circumstances are appropriate, the solicitor’s fiduciary duties may be moulded by his contractual retainer, at least while the conflict remains potential rather than actual.

14. As Lord Browne- Wilkinson emphasised in Henderson v Merrett Syndicates [1995] 2 AC 145 at 206A-D

“the extent and nature of the fiduciary duties owed in any particular case fall to be determined by reference to any underlying contractual relationship between the parties. This, in the case of an agent employed under a contract, the scope of his fiduciary duties is determined by the terms of the underlying contract. Although an agent is, in the absence of

contractual provision, in breach of his fiduciary duties if he acts for another who is in competition with his principal, if the contract under which he is acting authorises him to so to do, the normal fiduciary duties are modified accordingly: see *Kelly v Cooper* [1993] AC 205 The existence of a contract does not exclude the co-existence of concurrent fiduciary duties (indeed, the contract may well be their source); but the contract can and does modify the extent and nature of the general duty that would otherwise arise.”

Beware however, of too great an element of sculpture and of consent which may not be fully informed. Solicitors are not estate agents! Furthermore, take heed of the Solicitors’ Practice Rules 1990 as amended as from 5 May 2006 at rule 16D which make clear that there are circumstances in which consent cannot remedy the situation.

15. Putting aside the potential for contractual terms entered into from day one, it must also be borne in mind that in equity the conflicts rule applies where duties or duty and personal interest “**possibly may** conflict”: *Aberdeen Railway Co v Blaikie Bros* (1854) 1 Macq 461 at 471 and *Boardman v Phipps* [1967] 2 AC 46 per Lord Upjohn at 124². Would the reasonable man, looking at the relevant facts think that there was a real sensible possibility of conflict? This test may prove extremely difficult to apply in practice. The 1990 Solicitors’ Rules as now amended make reference to “significant risk” that duties may conflict. One is already in very difficult territory if the professional is attempting to make a judgment call as to the degree of significance of the risk.
16. Also bear in mind that although one thinks of the rule arising in relation to the same transaction, this is not necessarily the case. In *Marks & Spencer v Freshfields* [2004] 1 WLR 2331 at para 16 Lawrence Collins J held

² This was most recently quoted in *Wilkinson v West Coast Capital & Ors* [2005] EWHC 3009 (Ch) at (the Gadget Shop case)

“Most of the cases refer to the problem in the context of conflicting interests in the same transaction, but it seems to me clear that it goes somewhat beyond that. Although *Prince Jefri Bolkiah v KPMG* is not directly in point because it is a former client case and not, therefore (see *Hollander & Salzedo, Conflicts of Interests and Chinese Walls* (2000), p 27) an application of the double employment rule, the way in which Lord Millett expresses himself is wholly inconsistent with the double employment rule being limited to same matter conflicts. I accept there must be some reasonable relationship between the two matters, but they do not, in my judgment, have to be the same.

17 The principles are confirmed by the Guide to the Professional Conduct of Solicitors.”

In fact, Rule 16D(2)(c) of the Solicitors’ Rules deals with “related matter” for the purposes of Rule 16D(2)(b) in the following way:

“ a related matter will always include any other matter which involves the same asset or liability.”

Clearly, this is not exhaustive and each set of circumstances must be considered on their own terms.

Present and former client

17. The case of the present and former client concerns the risk of the use of confidential information gained during a previous retainer and usually arises therefore, when the previous client seeks an injunction. Such circumstances were considered by Lord Millet in the Prince Jefri case and in Bristol & West Building Society Mothew , by Clarke LJ in Koch v Richards Butler [2002] EWCA Civ 1280 and most recently by Mummery LJ in Gus Consulting GMBH v Leboeuf Lamb Greene & Macrae [2006] EWCA Civ 683. In many ways, the issues are clearer given that the jurisdiction of the court arises

purely as a result of the confidential information and the need for its protection.

18. Where consent is not forthcoming, a solicitor or other professional will be restrained from acting for the new client if such a restriction is necessary to avoid a significant risk of the disclosure or misuse of confidential information belonging to the former client: Prince Jefri case at 234. Therefore, there is no absolute rule that the professional may not act and in Rakusen v Ellis Munday & Clarke [1912] 1 Ch 831, a two man firm where the partners operated independently, did just that with the approval of the Court of Appeal. However, Lord Millett reformulated and strengthened the test to be applied in the favour of the former client. He stated that the duty to preserve confidentiality is unqualified and the former client is entitled to prevent the solicitor from exposing him to any avoidable risk of leakage of that information. He concluded at 237:

“ . . .the court should intervene unless it is satisfied that there is no risk of disclosure. It goes without saying that the risk must be a real one, and not merely fanciful or theoretical.”

19. As you will recall, he went on to state that there was no rule of law against Chinese walls but was extremely doubtful about ad hoc measures. Nevertheless, in the case of Young & Ors v Robson Rhodes [1999] 3 All ER 524 Laddie J refused an injunction preventing a merger of PKF and Robson Rhodes despite the fact that partners of Robson Rhodes were acting as forensic accountants in litigation against PKF. Laddie J determined that the crucial question was whether the barrier would work and concluded that it would do so.
20. In the most recent case of Gus Consulting GMBH v Leboeuf Lamb Greene & Macrae, heard on 26 May 2006, Mummery LJ held:

“30

The law is that there is no need for a restraining order against acting or advising in an adverse interest, if the court is “satisfied on the basis of clear and convincing evidence that all effective measures have been taken to ensure that no disclosure will occur. . . .” (per Clarke LJ in **Koch** at paragraph 24(8) .

31. Each case turns on a careful judicial analysis and assessment of the quality of the evidence about the effectiveness of the precautions taken to protect the confidentiality of the former client’s information from the risk of disclosure and misuse. If there is clear and convincing evidence that the precautions taken will provide effective protection, there will be no real risk to justify the grant of an injunction.”

He concluded that the Chinese wall set up and the undertakings given where not only had the firm acted for the opposing party in an arbitration on a previous occasion, but a number of the that party’s legal team had moved to the firm, were sufficient to avoid the risk.

21. The new Solicitors’ conflicts rule 16E(4) provides as follows:

“If you hold, or if your practice holds, confidential information in relation to a client or former client, you must not risk breaching confidentiality by acting, or continuing to act, for another client on a matter where:

(i) that information might reasonably be expected to be material;

and

(ii) that client has an interest adverse to the first-mentioned client or former client

except where proper arrangements can be made to protect that information in accordance with paragraph (5) below.”

Sub- rule (5) contains reference to informed consent but also puts the onus the professional to be able to show that he has a reasonable belief that both

clients understand the relevant issues, these having been brought to their attention and that in all the circumstances it is reasonable to act.

Actuaries

22. It would not be unfair to say that the actuarial profession has come late to the conflicts party and until recent times has been untroubled by such matters. However, in recent times the matter has become overcooked being considered by Lord Penrose and the Morris Review and addressed by Harvie Brown in his Presidential Address to the Faculty in October 2004. It was also the subject of specific advice to the Institute in a letter from Herbert Smith of April 2004.

23. PCS Rule 5.2 provides as follows:

“If there is or might appear to be a conflict of interest between two or more clients of a member or of the member’s firm, or a conflict between a client and the member or the member’s firm, the member must consider the nature and extent of the conflict and **whether it is such as to make it improper for the member to give advice to one or more of the clients involved in the conflict.**”

What wise or alternatively trusting chaps, actuaries must be.

Accountants

24. As you will appreciate, a number of the cases, including Prince Jefri itself, concerned accountants, usually fulfilling forensic or other duties akin to those which a solicitor might render in litigation. They were treated identically with solicitors. Of course, accountants fulfil numerous functions and for example, may give investment advice. There is insufficient time here to consider all possible ramifications.

25. However, what about accountants' auditing obligations? As you will know, they usually have very heavy documentation restricting the terms of their engagement and habitually audit clients with conflicting interests. PWC in particular, is quite aggressive about its stance. It argues that auditing is a public function and must not be curtailed and can be distinguished from all the circumstances in which the conflict rule has been applied which are litigation based. In Prince Jefri, Lord Millett concluded that audit clients impliedly consent to their dual or rather, multi-faceted employment.
26. The Chartered Accountants' Guide to Professional Ethics includes numerous statements relating to conflicts without referring to it directly and also includes a section on conflicts and confidential information which in many cases leaves the matter in the discretion of the individual. Unfortunately, it seems that the court will judge them more harshly than their professional body.

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