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N.J. SUPREME COURT YEAR IN REVIEW

LEGAL ETHICS & MALPRACTICE

Court Reaffirms American-Rule Exception To Enforce Fiduciary Duty

Other cases deal with duty of loyalty to clients in criminal defense contexts and the innocent-partner defense to malpractice-insurance fraud

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Perhaps most important among the several cases affecting legal ethics and legal malpractice this term was the Supreme Court's restatement of its faith in an exception to the "American Rule" that permits an award of attorneys' fees and costs to aggrieved parties injured by the tortious conduct of a fiduciary.

In *In Re Niles*, 176 N.J. 282, (2003), the errant fiduciary was the trustee of inter vivos trusts created by an 88-year-old single, demented multi-millionaire. The original trustee of the three trusts that Laura Niles created was a longtime neighbor, friend and professional investment counselor (Parkinson). The settlor's sister-in-law (Serena) and her son (Bono) managed to get her to change her will and trust to name Bono as her executor and trustee. The Court characterized Bono as a college graduate, who "had spent his...professional life collecting residential rent for a landlord/ pizzeria owner and attempting to get his insurance brokerage firm...off the ground."

Bono, with the help of his mother (Serena), prevailed upon the settlor to change her will and trust in such a way that they heavily favored the new trustee and his family. With his newfound power as Laura's fiduciary, Bono

embarked on a 16-month spending spree with her money. He and his mother used Laura's trust account, checkbook, signature stamp, cash and credit card to loot her assets. Included amongst their extravagant expenditures were a \$75,000 Mercedes Benz and a



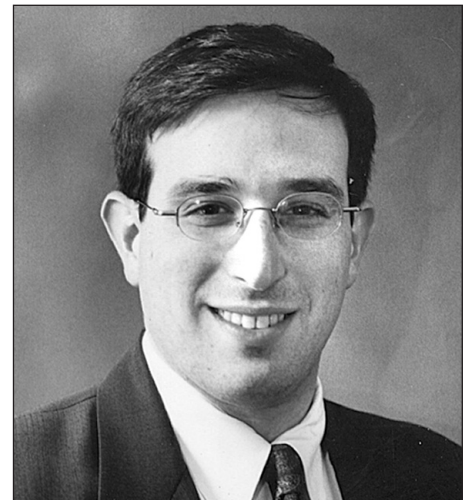
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\$20,000 Cartier wrist watch.

After Bono had served as fiduciary for about eight months, Parkinson, the original executor and trustee, filed a complaint seeking, amongst other relief, the appointment of a guardian ad litem for Laura, claiming that Bono and

his mother had "unduly influenced her into changing her will and trust agreements." The Court appointed a guardian ad litem who conducted an investigation as to the undue influence issue.

After a plenary hearing, the Judge sitting in Chancery Division, Probate Part, removed Bono as trustee, finding his conduct "inexcusable and reprehensible" because he had embezzled and misused the settlor's assets. The Court rejected Bono's accounting and directed him to pay surcharges to the estate in the sum of \$361,800 for his breach of fiduciary duty as trustee. At a second bench trial, the issues of undue influence were litigated. The trial court found "no clearer case of undue influ-



ence" than this one. The amendments to the will and trusts were declared null and void as having resulted from Bono and Serena's undue influence over Laura.

Following those two adjudications, the original fiduciary, Parkinson, sought

N.J. SUPREME COURT YEAR IN REVIEW

LEGAL ETHICS & MALPRACTICE

reimbursement of Laura's counsel fees in connection with the litigation to the tune of \$847,000. The Appellate Division affirmed the trial court's finding of undue influence but disallowed the request for counsel fees. The Supreme Court granted Parkinson's cross-petition for certification. In its decision, the Court made crystal clear its commitment to uphold and enforce the highest standards of fiduciary loyalty, whether that fiduciary is an attorney or an appointee under a will or trust, by requiring the errant fiduciary to pay the attorneys' fees and expenses of the prevailing party.

Seizing upon the egregious facts in *Niles*, the Supreme Court reaffirmed the principles in those cases where it had applied the exception to the "American Rule" in cases of lawyer malpractice. Specifically citing those cases that have caused a recent flurry in the law journals, *Saffer v. Willoughby*, 143 N.J. 256 (1996) and *Packard-Bamberger v. Collier*, 167 N.J. 427 (2001), the Supreme Court stated:

Like the attorney-client relationship, a trustee's fiduciary relationship is based on the utmost trust... Both the attorney and the trustee act as Officers of the court when acting on behalf of clients and beneficiaries. 176 N.J. at 297.

Like an attorney who commits malpractice in the form of exercising undue influence while representing a testator, settlor or an estate, a trustee of an estate who exercises undue influence over a testator intentionally has breached a fiduciary relationship in a manner at least as egregious as an attorney who has intentionally breached his fiduciary duty. 176 N.J. at 298.

Therefore, the court held that when the fiduciary commits the "pernicious tort of undue influence," an exception to the American Rule requires the estate to be made whole again by awarding the attorneys' fees and expenses against the

fiduciary that were incurred by the estate in attempting to right the fiduciary's wrong.

The holding has obvious implications for any attorney who, in addition to serving as the scrivener of a will or trust, also serves as a fiduciary under those instruments, an arrangement of dubious ethical propriety in some cases. Indeed, an attorney who serves in both those capacities has, according to the *Niles* decisions, two separate bases on which to be assessed attorneys' fees and expenses for negligent or intentional misconduct. The Court stated:

Undue influence committed by an executor or trustee to obtain a significant financial benefit for himself is especially pernicious, regardless of whether the fiduciary is an attorney. Undue influence by an attorney who becomes executor-beneficiary under a will and undue influence by a non-attorney who becomes trustee beneficiary, should be treated the same regarding the payment of counsel fees required to remove the person as a fiduciary... The only difference between the two is that the lawyer used his authorization to practice law as a license to steal and the trustee, having been named to that office, used the office to do the same. It is a difference with little meaning. 176 N.J. at 299.

The Court evidently rejected the parochial complaints which have recently appeared in the legal press that were critical of its rulings upholding the exception to the American Rule. Those critics claim that such holdings would open the "flood gates," spurring litigation that seeks assessment of attorneys' fees and costs against errant lawyers and other fiduciaries. Instead, the Court pointed out that the American Rule's exception is limited to those few cases of a fiduciary's misconduct such as undue influence where estate documents create or expand the fiduciary's

beneficial interest in the estate.

Consequently, the Court felt that such awards would necessarily be limited to a relatively few number of cases. More significant to the Court were the "important public policy concerns [that] are involved." The Court thus acknowledged that in a few cases, fee shifting is justified under the exception to the American Rule, where that shifting vindicates the more important public policies of upholding the fiduciary duty that attorneys or trustees owe their clients and/or beneficiaries.

While the Court expressly approved *Saffer* by relying on it so heavily in *Niles*, it did the very same thing by clear implication in yet another case. In *DiStefano v. Greenstone*, 357 N.J. Super. 352 cert. den. 176 N.J. 178 (2003), the Supreme Court denied certification of an Appellate Division decision that upheld *Saffer*, the seminal case of the American Rule exceptions. Indeed, the Court's refusal to grant certification in *DiStefano* is a clear and unequivocal reaffirmation of the principles it enunciated in *Saffer*:

1. That an attorney may not collect an attorneys' fee for negligently performed services; and
2. A negligent attorney is responsible for the legal expenses and attorneys' fees incurred by a former client in successfully prosecuting a legal malpractice action against him seeking to ameliorate the damage caused by that professional negligence.

The *DiStefano* case arose from an underlying personal injury claim, where the plaintiff's prior lawyer negligently allowed a foreign statute of limitations to expire before arranging for foreign counsel to timely file the claim. As a result, the client's claim became time barred. The client sued the former attorney and received a \$90,000 settlement in the malpractice action to compensate for the underlying injury case. At issue was whether the award should have been reduced by the negligent attorney's prospective one-third contingent fee. If that were done, then, in effect, the client would be penalized by reducing the award that would have fully compensated her for her injuries by sub-

N.J. SUPREME COURT YEAR IN REVIEW

LEGAL ETHICS & MALPRACTICE

tracting an amount in lieu of payment for the negligent attorney's services. A second issue was whether negligent attorneys are liable for attorneys fees and expenses incurred by the subsequent attorney who successfully represented the client against the negligent attorney.

The Appellate Division held that the client, under *Saffer*, could recover both the underlying settlement of \$90,000, without deduction or offset, plus the attorneys' fees of the subsequent attorney who successfully prosecutes the malpractice action.

While certain segments of the practicing bar and the liability insurance industry complain about the untoward ramifications of the exception to the American Rule as it applies to attorney malpractice cases, the Supreme Court, well aware of those concerns, nonetheless came out on the side of upholding the interests of those victimized by legal malpractice. The Court saw fit to uphold those interests, not only by disallowing a negligent attorney any fee for negligently performed services, but by holding that errant fiduciary (whether it is an attorney or otherwise) liable for the litigation expenses and attorneys' fees incurred by the damaged client in becoming whole once again as a result of the attorney's negligence.

That result and the important public policy statement it makes transcends the special interests of those who have recently complained about the exception to the American Rule. Thus, by denying certification in *DiStefano* and remaining silent in that case, the Supreme Court's message was loud and clear: the exception to the American Rule, which allows a prevailing client an award of attorneys' fees and expenses against a negligent attorney, is the rule in New Jersey and will likely remain so for some time to come.

The Fiduciary Duty: Conflicts of Interest

The lawyer's fiduciary duty also came before the Court in the context of the representation furnished by criminal defense attorneys. In *State in the Interest of S.G.*, 175 N.J. 132 (2003),

the Court reversed an Appellate Division decision, thus upholding a dissenting judge who would have disqualified a law firm that represented a defendant accused of shooting and killing another of the firm's client's. The Court held that in doing so, the representation offered by the law firm resulted in a prohibited conflict of interest and would not permit the firm to proceed with the representation, even though the client desired to waive the conflict and consent to the representation.

The decision emerges from the representation by two separate lawyers within the same firm of two separate criminal defendants. One lawyer, Steinberg, of Sufrin, Zucker, Steinberg, Waller & Wixted, entered his appearance on behalf of defendant S.G., who was charged with shooting Hilton. Steinberg had represented S.G.'s family in previous civil matters. Unbeknownst to Steinberg, however, Hilton had been represented by Steinberg's partner, Wixted, in an unrelated pending narcotics charge. That pending criminal matter was eventually dismissed, but not before Hilton had died as a result of the gunshot wounds inflicted by S.G.

The Sufrin firm had also represented Hilton in two other separate criminal matters over a period of five years. The firm was in the midst of representing him on one of those criminal charges at the time S.G. retained the firm to defend him against shooting Hilton. This dual representation continued for about three weeks until the pending charge against Hilton was dismissed, only because of his death.

The state made a motion to disqualify the firm from representing S.G., on the basis of its conflict of interest in representing the alleged assailant and his deceased victim. The trial court denied the motion, stating, "The representation clearly is over, [because] the victim, defense counsel's former client, is now obviously deceased." The State moved for leave to file an emergent interlocutory appeal, which was denied by the Appellate Division. The State then filed with the Supreme Court a motion for leave to appeal, which was granted. The

Supreme Court remanded the matter back to the Appellate Division for further consideration.

On remand, the majority of the Appellate Division panel viewed the case as one involving successive representation. It concluded that because of Hilton's death, the Sufrin law firm did not represent Hilton and S.G. simultaneously and therefore, no actual conflict existed. At most, the majority felt the facts presented only a potential for conflict, since there was no evidence that the law firm had obtained from Hilton any confidential information relating to S.G.'s representation. Thus, the risk of a potential conflict did not outweigh S.G.'s right to counsel.

Judge Newman, the lone dissenter on the Appellate Division, felt otherwise and would have disqualified the law firm because the representation would amount to a violation of RPC 1.7, the general conflict of interest rule. Judge Newman noted that an inherent risk of conflict was present when an attorney's representation of a defendant accused of committing a crime against another client of the firm, if the attorney might be required to cross-examine the victim/client. That now-deceased client's inability to either grant or deny consent to the dual representation should not alter the prohibition of the conflicting dual representation. Indeed, to permit the representation to go forward was a "disservice to the administration of criminal justice."

Faced with this scenario, the Supreme Court took the opportunity to return to its theme of the supreme importance of the fiduciary duty that the lawyer owes to his client:

One of the most basic responsibilities incumbent on a lawyer is the duty of loyalty to his or her clients...[citations omitted] Our Rules of Professional Conduct continue unabated that prohibition. A lawyer may not represent the client if the representation would be directly adverse to another client RPC 1.7, and that conflict is imputed to all members of a

N.J. SUPREME COURT YEAR IN REVIEW

LEGAL ETHICS & MALPRACTICE

law firm, disqualifying all, if anyone would be disqualified. RPC 1.10 The only exception to the rule's prohibition that might arise, subject to common law restrictions on disabling conflicts, is when an attorney: (1) reasonably believes that representation will not adversely affect that relationship with the other client; and (2) secures the consent of both clients, after full disclosure. RPC 1.7(a)(c)(1).

As the fiduciary duty pertains to criminal matters, "the trust between the attorney and client has enhanced importance [requiring] special vigilance because an attorney's divided loyalty can undermine a defendant's Sixth Amendment right to effective assistance of counsel." *Id.* at 39. In the *S.G.* case, the Court started its analysis by flatly rejecting the conclusion of the trial and appellate courts that the attorney's fiduciary duty ended with the death of one of the clients. The attorney's responsibility, said the Court "terminates upon expiration of the time in which to appeal from the final judgment or order," not when the client dies.

The only other way the duty to the client could come to an end is if the client would have given his consent to the termination. Without that consent, an attorney cannot withdraw from a criminal matter without leave of court. Since neither of those two events occurred here, the law firm's duty to continue to represent the decedent/victim's interests in connection with the final disposition of the charges for which it was obtained continued unabated. Therefore, "the firm owed a continuing duty of loyalty to Hilton throughout the duration of that representation. In fact, the charges against Hilton remained pending for three weeks after his death, during which time the firm undertook the defense of his alleged killer."

In the Court's view, this clearly was not a case, as the Appellate Division saw it, of successive representation of clients with adverse interests, where a

breach of client confidence might become the focus of a conflict analysis. Instead, the conflict of interest occurred simultaneously and on more than one level. First, as the victim who died as a result of the shooting, Hilton, the deceased client, had an interest in seeing his alleged attacker brought to justice. Had he survived, he would have been an obvious witness in a later criminal trial against the client/perpetrator. Simply because the client/victim died, does not mean that his interests were not adverse to those of the client/perpetrator during the few weeks of the firm's overlapping representation.

On yet another level, the firm's simultaneous representation of the client/perpetrator was adverse to the representation of the client/decedent. As a result of the assault, the client/decedent had an action for damages against the attacker. His interest in pursuing that action on his own prior to his death and later through his estate was directly adverse to the firm's representation of the alleged shooter. This patently adverse relationship is a conflict that the Rules of Professional Conduct clearly forbid.

The import of this decision may well be that the fiduciary duty, like the client's interests, survives even after the client has died. In so doing the Court reaffirmed the fundamental importance of the continuing fiduciary duty as an essential part of the attorney-client relationship.

Two other cases decided by the Court in the criminal defense context explore the lengths to which an attorney must go in representing a client, and whether strict adherence to the RPCs can ever take a back seat to the attorney's fiduciary duty to aggressively represent a client. In one case the answer was a resounding yes—finding that in an application for post-conviction relief ("PCR"), an attorney must advocate a client's claims even if he deems them to be utterly without merit.

By contrast, prior to conviction, the Court looked to the RPCs regarding conflicts of interest to determine whether a public defender should be precluded from representing a murder

suspect when that same attorney had represented a client questioned during the murder investigation.

In *State v. Rue*, 175 N.J. 1 (2002), the Court confronted the question of which takes precedence, Court Rule 3:22-6(d) or RPC 3.1. R. 3:22-6(d) requires an attorney representing a defendant on a post conviction relief (PCR) petition to "advance any grounds insisted upon by defendant notwithstanding that counsel deems them without merit." By contrast, RPC 3.1 prohibits an attorney from presenting to the court a frivolous action which has no good faith basis. When a court-appointed attorney advised the court in his client, Dudley Rue's, PCR petition that he deemed Rue's arguments for PCR to be without merit, a clash between R. 3:22-6(d) and RPC 3.1 required the Court's attention.

Holding that "post-conviction relief is New Jersey's analogue to the federal writ of habeas corpus," Justice Long writing for the Court found a "compelling judicial interest in sustaining only those convictions free from constitutional error." (Citing *State v. Afandor*, 151 N.J. 41, 49 (1997).) Moreover, the rule related to filing PCR petitions was enacted only after a long deliberation process. The Court briefly traces that process and found that when the Rule was finally enacted in 1964, it stated that an attorney advocating a PCR petition "should not be reluctant to advance any grounds insisted upon by the defendant notwithstanding he deems them without merit." This "should not be reluctant" language was bolstered in 1967 when the Rule was changed to read, as it does currently, "should advance any grounds insisted upon by defendant." The Rule was renumbered but unchanged in 1969.

RPC 3.1, on the other hand, was adopted in 1984. Subsequently, R. 3:22-6 was amended to make it gender neutral, but remained otherwise unchanged. Thus, when promulgating changes in the Rules' language, the Court was "cognizant of the existence of RPC 3.1, yet chose to maintain the stricture of the PCR rule requiring the advocacy of a defendant's claims, regardless of

N.J. SUPREME COURT YEAR IN REVIEW

LEGAL ETHICS & MALPRACTICE

merit.”

Although this holding renders RPC 3.1 effectively meaningless in the context of a PCR petition, the Court made it clear that the purpose of counsel’s representation of a defendant on a PCR petition is to advocate a position on behalf of a client. “In no event. . . is counsel empowered to denigrate or dismiss the client’s claims, to negatively evaluate them, or to render aid and support to the state’s opposition.” Basically, in light of R. 3:22-6(d), an attorney’s duty pursuant to the rule of Court is to represent his client to the fullest, even if in this instance it runs afoul of RPC 3.1.

Justice Verniero, in a concurrence joined by Justice Coleman, advocated considering a standard set forth in the United States Supreme Court case of *Anders v. California*, 386 U.S. 738, 744, 87A S.Ct. 1396, 1400, 18 L.Ed.2d 493, 498 (1967). The *Anders* decision set forth a procedure whereby counsel wishing to withdraw from an appeal due to what he believes to be meritless arguments by a client, must advise the court and request permission to withdraw, while in his brief advising the court of any arguments that might be reasonably argued on behalf of the client. The court then decides whether the claims are frivolous— if so, the appeal is dismissed; if not, the court will provide counsel to the defendant in order to argue the appeal.

Justice Verniero advocated considering an *Anders*-like approach because it “derives from the system’s need for candid, independent, and professional counsel,” while balancing “those needs alongside a defendant’s significant interests.” He also recommends that the possibility of adopting an *Anders*-like standard in New Jersey at least be considered by “an appropriate committee to review the rule for possible modification or revision.”

Rue underscored the lengths to which counsel must go in furtherance of its fiduciary duty. Even when a PCR petition is wholly without merit and amounts to a “fraud on the court,” the attorney must not only disregard RPC 3.1 and present the argument, but he

must advocate it in order to represent properly the criminal client seeking PCR.

State v. Jimenez, 175 N.J. 475 (2003), dealt with whether a conflict of interest arose when a public defender representing defendant Jimenez in a capital murder case should have been disqualified under RPCs 1.7(c) and 1.9 for also having represented someone who had been interviewed in connection with the murder.

Jimenez was implicated in the sexual assault and murder of a ten-year-old boy, Walter Contreras. Part of the evidence gathered during the investigation was a sweater with a distinctive pattern and stains which were presumably human blood. Ray Hughes was investigated as a possible suspect. Because a woman named Jolene Proctor had given Hughes’ name to investigators as a possible suspect, he threatened to kill her. He later pleaded guilty to harassment (downgraded from terroristic threats), and was sentenced to time served. A public defender was appointed to represent Hughes at his plea and sentence. That constituted the totality of Hughes’ representation by the public defender.

Meanwhile, this same public defender was one of two attorneys representing Jimenez, who had been arrested for Contreras’ murder. The State, which said nothing during Hughes’ plea and sentencing, sought to disqualify the public defender as having an RPC 1.7(c) conflict. Even though the State admitted that Hughes was not in any way implicated in the murder, it claimed that there was enough evidence of Hughes’ linkage to the suspect sweater that the public defender could not represent Jimenez. The State argued that because the option of Hughes’ third-party guilt was no longer available due to the public defender’s representation of Hughes, Jimenez’ defense was prejudiced and the public defender had an unwaivable conflict.

The trial court denied the State’s motion, stating that there was no linkage to Hughes’ involvement which would allow for a third-party guilt argument. The Appellate Division denied leave to appeal and the matter came to

the Supreme Court. The question presented was whether on the facts of this case the public defender had represented Hughes in a substantially related case in which his interests are materially adverse to Jimenez’, and in which information learned from representing Hughes would be used to defend Jimenez. Essentially, the Court questioned whether the public defender was able to represent Jimenez wholly independent of her prior representation of Hughes.

The Court found that the public defender could not have argued third-party guilt without some evidence of such guilt. In contrast to *Rue*, the Court cited the cases of *State v. Sturvidant*, 31 N.J. 165 (1959) and *State v. Koedatich*, 112 N.J. 225 (1988), to require some reasonable basis before third-party guilt can be presented as a defense. Here, the Court required defense counsel’s advocacy within the dictates of the RPC— implying that the failure to do so could result in grounds for reversing a conviction. On the facts of this case, the Court concluded that there was no basis for the third-party guilt defense because there was no link between Hughes and the murder. Moreover, the public defender waived that defense as a possibility early in the proceedings. Thus, on the facts of this case, it was not one “in which defense counsel will have to cross-examine a former client or call to the stand a former client who may incriminate himself and exculpate the present client.” Nor was there anything to suggest that the public defender learned anything in her representation of Hughes that would benefit Jimenez.

Thus, there was neither a conflict of interest nor an appearance of impropriety in the public defender’s representing Jimenez. Nothing in the public defender’s representing both Hughes and Jimenez would undermine the public’s confidence in the judicial system. However, the Court implied that the same would probably not hold true if the public defender’s representation of Hughes had been broader in scope and longer in time than it had been.

The Court cautioned, however, that it is advisable for counsel in a similar

N.J. SUPREME COURT YEAR IN REVIEW

LEGAL ETHICS & MALPRACTICE

situation to engage in a colloquy with the court, on the record, in which a defendant understands the scope and circumstances of the attorney's prior representation of the other client. "With a complete knowledge and understanding of the import of these facts, defendant may then voluntarily consent" to the attorney's representation.

Justice Long's dissent (joined by Justices LaVecchia and Coleman) felt that Hughes' terroristic threats may have been an acknowledgment of guilt of the murder, which could have been used against him in presenting a third-party guilt defense for Jimenez. Citing the *S.G.* decision, the Court was concerned about the public defender waiving the third-party guilt defense, thereby closing off a possible defense at an early stage of the proceeding. By having to choose between two possible avenues of defending Jimenez, she was in an unwaivable conflict. "At the very least, this case involves an appearance of impropriety" which must be avoided pursuant to RPC 1.7(c).

Although in *Jimenez* the Court looked to utmost candor and the dictates of RPCs 1.7(c) and 1.9 to determine whether a conflict existed which would have prevented a defense attorney from presenting a viable third-party guilt defense, the Court in *Rue* permitted frivolous claims once the defendant has been convicted and seeks post-conviction relief. The message of the Court's fiduciary duty cases this past term is that attorneys must comply scrupulously with that duty in all of its aspects, in some instances (i.e. on a PCR petition) even when it flies in the face of the RPCs. If they don't, then the Court has reserved to itself the now well established power to enforce compliance in at least two ways: by awarding counsel fees and expenses to clients damaged by the breach of that duty via the exception to the American Rule, and by disqualifying lawyers from representing clients in select cases of conflicts of interest.

The Case of the Innocent Partner

In an important case that had inno-

cent partners of dishonest lawyers sitting on the edge of their chairs for a while, the Supreme Court, in one of its last decisions this past term, helped those innocents breathe a collective sigh of relief. In *First Am. Title Ins. Co. v. Lawson*, 177 N.J. 125 (2003), the Supreme Court was confronted with a case of the collision of competing interests: the lawyer's expectation not to lose his insurance coverage for the misconduct of his dishonest partners on the one hand and the client's rights not to be deprived of that insurance coverage if resort to it becomes necessary. R. 1:21-C permits attorneys to practice law as a limited liability partnership. The rule also requires that law firms who do so must carry liability insurance to protect their clients from the professional negligence of any of its partners or employees.

Those interests came under attack when two dishonest partners of a limited liability partnership made material misrepresentations to their prospective insurer, which the Appellate Division had ruled were of such magnitude as to justify a complete rescission of all coverage. The Supreme Court had no difficulty affirming the rescission of the insurance policy as to the two dishonest partners. As to the innocent partner, however, the Court did a graceful balancing act in order to preserve his coverage and to protect his clients.

Here were the facts: Edward Lawson was licensed in New Jersey and Kenneth Wheeler was admitted in Connecticut and the District of Columbia. They formed a partnership in New Jersey in 1997. Later that year, Craig Snyder, a New York attorney, joined their practice. He drew up a limited liability partnership agreement and filed it with the New Jersey Secretary of State. Snyder maintained the firm's office in New York City. He did little or no work in the firm's New Jersey office. Wheeler served as the firm's managing partner and did most, if not all of the banking in New Jersey, although each of the partners did have signatory authority over the firm's checking accounts. Snyder, however, never transferred any funds to, from or between the

firm's New Jersey business or trust accounts.

About one year into their partnership, Lawson had discovered that Wheeler was improperly transferring money between client trust accounts and the firm's business accounts. Lawson confronted Wheeler and, instead of putting a stop to the practice, he joined in it. Snyder, however, knew nothing of this scheme.

Wheeler, as managing partner, applied for professional liability insurance for the firm. In response to questions on the application indicating whether any attorney in the firm had knowledge of any professional liability claims or any facts that would give rise to such a claim, Wheeler answered "no." Based on the application and a further statement of warranty made by Wheeler to the underwriter, the insurer issued a professional liability policy to the firm and its partners. The firm had missed payment of one of its premiums and was sent a notice of intent to cancel the policy, which was in fact canceled for nonpayment one month later. In order to reinstate the policy, Wheeler signed a new warranty affirming that there had been no claims during the prior five years against the firm or any member. Relying on that warranty, the insurer reinstated the policy. During the interim between the cancellation and Wheeler's executing a new warranty, the Office of Attorney Ethics notified the firm that it would be conducting an audit of the firm's books because of three grievances that it had received concerning the firm's handling of certain real estate transactions. As it turned out, Lawson had allegedly not paid \$339,012 to sellers of real property in a transaction the firm handled.

In addition, an outstanding mortgage of \$97,285 in another real estate closing had not been paid off by the firm. Once again, Snyder in New York knew nothing of this. The title insurer brought an action against the firm and the three individual partners. The professional liability insurer, however, evidently unaware of the firm's problems, notified Wheeler in February, 1999, that based on his renewed warranty, the

N.J. SUPREME COURT YEAR IN REVIEW

LEGAL ETHICS & MALPRACTICE

firm's policy had been reinstated.

When these facts came to light, the liability carrier then filed a declaratory judgment, seeking to cancel the reinstated policy, claiming it was void ab initio due to the material misrepresentations in the warranty furnished by the firm to reinstate the policy. The actions of the title insurers and the professional liability insurer were consolidated. The trial court concluded that the firm's policy did not insure against Lawson and Wheeler's "criminal and/or dishonest conduct," but did cover the firm's liability as a separate legal entity distinct from the individual partners. It therefore concluded that the firm's liability insurance was not void and it granted summary judgment in favor of the title insurers, but denied the motion as to the professional liability carrier. The Appellate Division reversed and held that these facts rendered the policy void for all purposes.

The Supreme Court's approach however, was not as sweeping as the Appellate Division's draconian solution. Instead, the Court did a fine dissection of the issues and interests involved. As to Wheeler's misrepresentation and Lawson's complicity in the misappropriation of client funds, the Court had no problem affirming the lower court's denial of coverage. The Court easily extended denial of coverage to the firm as a whole as well. It reasoned that Wheeler had occupied the position of managing partner and was responsible for the insurance application process. To allow coverage for the firm as an entity when it was the managing partner of the firm who made the misrepresentations to the carrier would, in the Court's opinion, condone the use of a partnership as a subterfuge for fraudulent conduct. Here, because it was the managing partner who was directly responsible for the misrepresentations and further, because two of the firm's three partners had engaged in misconduct, the carrier was entitled to rescind its coverage of the firm as an entity.

The more difficult question focused on coverage for Snyder, the innocent partner. He did not participate

in the fraudulent conduct of his partners, nor was he involved in any of the transactions which gave rise to the ethics investigations or damage claims. Snyder's work was limited to the New York office. He was not privy to any of his partners' misconduct. Those facts were crucial in the Court's analysis, since it furnished the factual foundation for its conclusion that Snyder was the innocent partner. The Court found it would be unfair to void Snyder's coverage on the basis of his dishonest partners' wrongful conduct because that might expose him to uninsured liability in a manner inconsistent with his expectation as a partner in a limited liability partnership, where a partner would not normally be held liable for the negligence of another partner in which he had no involvement.

Furthermore, to void the policy as to him would deny coverage to clients for any of his actions in matters that were totally unrelated to the misconduct of the two dishonest partners. Thus, if the professional liability carrier could deny coverage for Snyder's unrelated matters, that could leave members of the public who Snyder had honestly represented without the mandatory insurance coverage required by R. 1:21-(c), even though he was entirely uninvolved in the fraud of his other partners. Such a harsh result, the Court found, was contrary to public policy and it thus upheld coverage for Snyder and his clients in matters unrelated to the fraudulent conduct.

The Court however, was careful to remind us that rescission of insurance policies, given its draconian consequences of denying all coverage for all firm members, is not a rule that courts should apply with broad strokes. Instead, the policy of protecting innocent partners from the dishonesty of others within a limited liability partnership is compelling, especially if it affects coverage for the clients of those innocent partners. Those policies and the distinctions to be drawn between them are divisible in respect of each partner so that partial rescission, as opposed to voiding the entire policy ab initio, is the preferred remedy. After that

decision, a collective sigh of relief from the overwhelming majority of the practicing bar is surely in order.

Pro Hac Vice and the Lawyer's Duty of Candor

In another case, the topic of multi-jurisdictional practice came to the Court's agenda this past term. In *Boston University v. U.M.D.N.J.*, 176 N.J. 141 (2003), the Court held that a licensed New Jersey attorney who practices entirely outside of New Jersey must nonetheless be a member in good standing of the New Jersey Bar before he or she is entitled to appear in a New Jersey action pro hac vice. Smith was admitted in New Jersey in 1978 and practiced here for about three years. He then moved to Massachusetts, was admitted to the bar there and has practiced there continuously since that date. Since his relocation to Massachusetts, he had not paid his annual fees to the Client Protection Fund as required by R. 1:20-1(b) and 1:28-2. The Court had annually issued orders to him declaring him ineligible to practice in New Jersey. He owed the Client Protection Fund approximately \$2,500.00 in arrears since his departure from New Jersey.

Smith had been working as associate general counsel for Boston University and sought to be admitted pro hac vice to assist his employer's local counsel in a breach of contract action against U.M.D.N.J. In support of plaintiff's motion that Smith be admitted pro hac vice, Smith submitted a certification asserting that he was a member in good standing of the Massachusetts' bar and he sought to be admitted pro hac vice pursuant to R. 1:21-2. In his certification, however, Smith did not disclose that he was licensed as a New Jersey attorney, that he was ineligible to practice in New Jersey or that he had not paid his Client Protection Fund arrears.

U.M.D.N.J. opposed the motion for Smith's admission, arguing that he should not be permitted to appear until he brings current his arrears to the Client Protection Fund. The trial court nonetheless granted the motion, holding

N.J. SUPREME COURT YEAR IN REVIEW

LEGAL ETHICS & MALPRACTICE

that Smith's good standing as a member of the Massachusetts bar was sufficient to meet the pro hac vice requirement. When the motion was granted, Smith submitted payment to the Fund for one year, but did not pay the past due amount.

U.M.D.N.J. moved to reconsider and submitted the certification of Kenneth Bossong, the director and counsel to the Client Protection Fund. Bossong argued that the Fund's arrearages had to be paid in full before a licensed New Jersey attorney can become eligible to practice again. The trial court denied the motion for reconsideration and the Supreme Court took the matter on direct certification.

The pro hac vice rule, R. 1:21-2(a) provides:

An attorney of any other jurisdiction, of good standing there, whether practicing law in such other jurisdiction as an individual member or employee...authorized to practice law in such other jurisdiction or an attorney admitted in this state, of good standing, who does not maintain in this state a bona fide office for the practice of law may, at the discretion of the Court in which any matter is pending, be permitted, pro hac vice to speak in such matter in the same manner as an attorney of the state who maintains a bona fide office for the practice of law in this state and who is there-

fore, pursuant to R. 1:21-1(a) authorized to practice in this state. No attorney shall be admitted under this rule without annually complying with R. 1:20-1(b), R. 1:28-2 and R. 1:28B-1(e) during the period of admission.

Plaintiff argued that the rule is written in the disjunctive and that Smith has a right to rely solely on his good standing in Massachusetts to appear pro hac vice without consideration to the status of his admission in New Jersey. The Court, however, disagreed and instead required that he first pay all arrearages before being permitted to appear pro hac vice. To hold otherwise, the Court felt, would allow Smith to avoid his financial obligation as a member of the New Jersey Bar. That, said the Court, would lead to an anomalous reading of the pro hac vice rule.

The Court was also concerned with the apparent ethical impropriety in Smith's failure to disclose to the Court his status as an attorney who was not in good standing by reason of his arrearages. In fact, he had not paid the Client Protection Fund assessment and that there were extant numerous orders sent to him indicating that he may not practice law in this state until he paid those fees. "Those orders [said the Court] are clear, admit of no exception, and must be enforced strictly by our Courts." The Court found particularly troubling Smith's failure to disclose these facts to the Court in his certification seeking admission, especially in light of RPC 3.3(a)5, that states: "A lawyer shall not

knowingly fail to disclose to the tribunal a material fact with knowledge that the tribunal may tend to be misled by such failure."

Fortunately, for Smith, the Court did not refer the matter to the ethics authorities. The Court, however, did hold that "A licensed New Jersey attorney must be a member in good standing of the New Jersey Bar before he or she may appear pro hac vice." If Smith remits full payment to the Client Protection Fund, including all arrears and thereafter obtained a certificate of good standing in New Jersey, then he would be entitled to appear pro hac vice. If not, the trial court was to revoke its order granting him pro hac vice status.

To clarify any further misunderstanding of the pro hac vice rule, the Court referred R. 1:21-2 to the Civil Practice Committee, suggesting that it modify its language so as to effectuate the Court's holding.

On balance, the Court's agenda in the area of legal malpractice and legal ethics this past term took some important steps. Most notably, it reminded us once again of how essential complete and faithful adherence to our fiduciary duty is and that the Court stands firm in the ways it has enforced, and presumably will continue to enforce that duty through its unique, but effective, exception to the American Rule and through disqualification in cases of conflicts of interest. In so doing, the Court came out squarely on the side of upholding the highest standards of the lawyer's ethical duties to their clients, the Court, and to the general public. ■