Indemnity & Contribution: The Law Giveth and the Law Taketh Away

Materials for this panel include:

- Presentation Slides
- Case Summaries
- "The Multifaceted General Counsel," Lawrence S. Spiegel, *2015 Insights*, Skadden
- Speaker Biographies

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Speakers: Matthew R. Henderson,
Lawrence S. Spiegel & John K. Villa

Contribution

Requirements for Contribution

- "A defending party may, as third-party plaintiff, serve a summons and complaint on a nonparty who is or may be liable to it for all or part of the claim against it." Fed.R.Civ.P. 14(a)
- Right to contribution determined by state law

- General requirements:
  - Joint tortfeasors; and
  - Liable for same injury
- Joint tortfeasors
  - Distinction between the client's original injury and impaired cause of action
- Same injury
  - Could plaintiff have sued the potential third party defendant

- Different scenarios where contribution can be sought in a legal malpractice action:
  - Prior counsel
  - Successor counsel
  - The negligent attorney
  - Opposing counsel
  - Other parties

Day v. Robbins, 79 F.Supp.3d 538 (D. Md. 2016)

- Law firm ("Seeger") was sued for malpractice and filed cross-claim for contribution from former attorney ("Robbins")
- Seeger argued that Robbins acted outside the scope of his employment in his representation of plaintiff
- Law firm stated valid claim for contribution and indemnification against its former employee
- Seeger did not plead itself out of court for by arguing that it was not negligent or liable to plaintiff

McCalla v. E.C. Kenyon Const. Co.,
183 So. 3d 1192 (Fla. Dist. Ct. App. 2016)

- Judgment creditor of contractor brought fraudulent conveyance action against principals
- Principals were not entitled to set-off for amount judgment creditor received from prior settlement with lawyer
- The Court reasoned that the attorney was not a joint tortfeasor with the party he was hired to sue

Nilazra, Inc. v Karakus, Inc.,
136 A.D.3d 994, 25 N.Y.S.3d 650 (2016)

- Corporate purchaser of restaurant ("Nilazra") brought legal malpractice claim alleging attorney ("Levitis") was responsible for a sales tax lien
- Attorney asserted third-party claim against seller's attorney ("Ikhilov") on the basis that he had assumed duty to file notification of lien
- Court ruled that Levitis had stated a valid contribution claim

Recurring Issues

- Contribution or direct action
- Aggravation of existing injury
- Effect of settlement with plaintiff
- Can negligence of client's agent (successor counsel) be imputed to the plaintiff as comparative negligence

Recurring Issues (cont.)

- Can intentional tortfeasor (*e.g.*, fraud, breach of fiduciary duty) seek contribution
- Impact of adding plaintiff's current attorney as a third-party defendant
- Public policy considerations

Indemnification

Indemnity Provisions in Outside Counsel Agreements/Guidelines

- History
  - Worldwide recession in 2008
  - Attorneys treated like other vendors
- Broad indemnification provisions
  - Requiring the attorney to indemnify the client for anything that goes wrong in the engagement
  - Regardless of whether the lawyer was in any way responsible for what went wrong

- Contractual obligation
  - Without any reference to error or omission
  - Usually not covered by insurance
- Impact
  - Professional independence of attorneys
  - Risk that lawyers would favor course of action that reduces own exposure rather than what is best for client

Sample Language

- **Indemnification**. In the event there is ever any allegation that Law Firm committed malpractice in providing services to Client or that Client suffered any harm arising from the Client's relationship with Law Firm, Law Firm shall defend, indemnify and hold harmless Client against any and all claims, demands, losses, costs, expenses and liabilities arising out of or relating to any such allegation.

Sephora USA, Inc. v. Palmer, Reifler & Associates, P.A.,

2016 WL 2770534, (N.D. Cal. May 13, 2016)

- Attorney/Client Service Agreement provided that law firm would pursue civil damages for theft offenses, *i.e.*, shoplifting
- Sephora was sued in class action for fraudulent business practices in pursuing claims against shoplifters
- Sephora made written demand upon law firm to pay defense costs, and law firm refused

- Underlying case was dismissed on basis that law firm's demand letters to alleged shoplifters were settlement communications
- Sephora sued the law firm for breach of the indemnity clause.
- The court ruled that Sephora's complaint stated a valid claim that law firm breached its duty to defend

Recurring Issues

- What factors do lawyers fail to consider
- What are the "tradeoffs" of indemnity provisions
- Are indemnity provisions enforceable
- Can a client obtain indemnification for its own negligence

Recurring Issues (cont.)

- Can a client obtain indemnification if it wins underlying case
- Unanticipated risks embedded in outside counsel agreements
- Disconnect between what law firms are doing and what indemnity provisions mean
- What is "back door" indemnity

Questions?

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Case Summaries

Day v. Robbins, No. JKB-15-2023, 2016 WL 1536254 (D. Md. April 15, 2016)

The plaintiff, a former client of defendants, brought a single-count action for legal malpractice against defendants, Attorney Seth A. Robbins ("Robbins") and a law firm known as Quagliano & Seeger, P.C. ("Seeger"), alleging that they "breached the duties that they owed to their client…in violation of the standards reasonably to be expected of a reasonably competent practitioner. Seeger brought a Cross-Claim against Robbins for indemnity and contribution. Robbins brought a Motion to Dismiss Cross-Claim.

Seeger argued that Robbins "seeks to impose liability upon Seeger based upon the alleged wrongful acts of Robbins and under *respondeat superior* and/or agency principles. Seeger denied the allegation and argued that Robbins's actions were "undertaken for [his] personal gain, were not among the services provided by Seeger, and were performed without the knowledge, information or consent of Seeger." Therefore, Seeger concluded, Robbins's actions were outside of the scope of his employment or agency with Seeger, and to the extent that Seeger was found liable to Robbins, Seeger claimed that Robbins should indemnify it or contribute to the damages.

Robbins construed these statements as fatal to Seeger's cross claim: taking the statements as true, Seeger was not a joint tortfeasor with Robbins, as is necessary for an indemnification or contribution claim. Accordingly, Robbins argued Seeger pleaded itself out of its Cross-Claim.

The Court disagreed and held that Robbins has not pleaded itself out of its Cross-Claim, and therefore, Robbins's Motion to Dismiss Cross-Claim was denied. The mere fact that Seeger advanced multiple, inconsistent legal theories was not a legitimate reason for the Court to dismiss the Cross-Claim. Contrarily, "alternative pleading is permitted, just as is inconsistent pleading." As a matter of pleading policy—absent controlling authority dictating a contrary result—the Court was disinclined to embrace a theory that would hamstring employer-defendants like Seeger, forcing them to choose at the outset of litigation between denying liability and attempting to shift or apportion liability.

Nilazra, Inc. v. Karakus, Inc., 25 N.Y.S.3d 650 (App. Div. 2d Dep't 2016)

The plaintiff, a corporate buyer of restaurant, brought a claim against its attorney for legal malpractice, alleging that a sales tax lien accrued after purchase of restaurant. The defendant third-party plaintiff, Nelly Levitis ("Levitis") represented the plaintiff as the purchaser, and the defendant third-party defendant, Erik Ikhilov ("Iklihov"), represented the seller. Tax Law § 1141(c) required that at least 10 days prior to the transfer of a business, the purchaser must file a notification of sale, transfer, or assignment in bulk with the New York State Department of Taxation and Finance. The failure to timely file the notification results in the seller's sales tax liabilities attaching to the purchaser. Accordingly, the plaintiff commenced the legal malpractice action arising from Levitis failure to verify that the notification had been timely filed by Ikhilov.

Levitis, in turn, commenced a third-party action seeking contribution and indemnification against Ikhilov alleging, among other things, that he voluntarily assumed a duty to timely file the notification. Ikhilov

moved to dismiss the third-party complaint for failure to state a cause of action. The Court denied the motion. Ikhilov, the seller's attorney, appealed.

The reviewing Court held that Levitis's third-party complaint sufficiently plead a cause of action to recover damages for negligence, as it alleged that Ikhilov voluntarily assumed Levitis's duty, as the attorney for the purchaser, to timely file the notification with the Department, and breached that duty.

Sephora USA, Inc. v. Palmer, Reifler & Associates, P.A.,

Sephora contracted with its lawyers for "Loss Recovery Services" through an "Attorney/Client Service Agreement". The contract provided that the firm would pursue "damages and/or civil penalties for theft offenses"—i.e., shoplifting—on behalf of Sephora, and would remit proceeds of those recovery efforts to Sephora, less attorneys' fees structured a percentage of the amount recovered. The contract also contained an indemnification clause:

> **Indemnification**. Each party agrees to defend and indemnify the other party from and against any and all suits, judgments, or liabilities directly arising from the negligence or other improper conduct of such party.

Sephora was subsequently sued in a class action. The complaint alleged that Sephora, and the law firm acting on Sephora's behalf, engaged in unfair, unlawful, and fraudulent business practices, intentional misrepresentation, and fraud. Many of the allegations related to the law firm's conduct on behalf of Sephora, particularly sending demand letters and making telephone calls to alleged shoplifters (or parents of minors alleged to have shoplifted). After receiving the complaint, Sephora made a written demand on the firm that it bear the cost of defense and otherwise indemnify Sephora from and against the asserted claims. The law firm refused to reimburse Sephora for defense costs. The underlying class action suit was dismissed on the basis that the "settlement offers" were protected writings in anticipation of litigation.

Sephora subsequently sued the law firm and alleged that it breached its obligations under the contract, specifically the indemnity clause. The court determined that the complaint did not alleged facts giving rise to Defendants' duty to indemnify, and that the harm was better viewed through the lens of the duty to defend. In determining whether the complaint stated a cause of action for breach of duty to defend, the court looked toward whether the complaint could be fairly read to support a claim based on vicarious liability for Defendants' conduct. The court determined that although the Complaint was not formally divided into separate claims for direct and vicarious liability. The complaint gave rise to a duty to defend, and therefore, Defendants' motion was denied.

McCalla v. E.C. Kenyon Construction Co., 183 So.3d 1192 (Fla. 1st 2016)

In a separate and previously filed lawsuit, McCalla sued Kenyon for breach of the construction contract, breach of express and implied warranties, and violation of the Florida Deceptive and Unfair Trade Practices Act, and obtained a judgment against Kenyon for $627,657.48.

In the instant suit, McCallas allege that, before final judgment was entered against it in the first case, Kenyon transferred all or most of its assets to Messrs. Herring and Young (who knew of the McCallas' pending claims), without receiving reasonably equivalent value in exchange. The complaint alleged fraudulent transfers which rendered Kenyon unable to satisfy the judgment entered against it.

The lower court concluded the McCallas were not the proper claimants because the Florida statute under which the complaint was filed does not provide for an award of legal fees. The reviewing court disagreed and found that the statute authorizes such awards against both fraudulent transferor and transferee, jointly and severally.

The McCallas also filed suit against Amerisure Insurance Company (Amerisure), Kenyon's certified general liability policy carrier, alleging Amerisure wrongfully denied coverage intended for their benefit. On October 29, 2012, the McCallas settled with Amerisure for $65,000.00. As part of the settlement, the McCallas agreed to credit and deduct the sum of $158,558.17 from the judgment entered in their favor against Kenyon in the original action. The trial judge ruled that this credit or offset should inure to the benefit of Messrs. Herring and Young, no less than to Kenyon. The reviewing court disagreed with the trial court when it determined the appellees were entitled to set off the amount the McCallas received in settlement of malpractice claims they made against Christopher Greene, the first lawyer they retained to represent them in the original lawsuit against Kenyon, and his employers. The defendants in the professional malpractice action were never jointly and severally liable for the damages awarded in the original action against Kenyon. The court ultimately ruled that the principals were not entitled to setoff against damages award for the amount the judgment creditor received in settlement of legal malpractice claims against lawyer who first represent creditor in original lawsuit against contractor.

The Multifaceted General Counsel

Skadden

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From legal adviser to business strategist to compliance officer, an in-house counsel typically finds herself playing multiple roles in her organization. Each role requires knowing the organization's business, understanding its goals, and at all times demonstrating a commitment to its success. Yet these functions risk creating a tension with an in-house counsel's ultimate risk management responsibility. Protecting the organization's interests requires an in-house counsel to be clear about who the client is and what role the in-house counsel is undertaking, all while fostering a culture of compliance.

Identifying the Client

To provide timely, relevant, effective advice, an in-house counsel must have an in-depth understanding of the organization's business, needs, goals and risk tolerance profile. Equally important is clarity about who is the client. Rule 1.13 of the ABA Model Rules of Professional Conduct (Organization as Client) states that the organization is the client of an in-house lawyer; the in-house lawyer does not represent the organization's constituents, e.g., its directors, officers, employees, members, shareholders or others.

As compared to outside counsel, a lawyer working in-house spends every day as a colleague of the organization's business people. This informality of relationships is useful as it furthers information flow, allowing an in-house counsel to stay up-to-date on business as well as legal issues. In such discussions, she must remain mindful of Model Rule 1.13(f), which provides that, when the lawyer knows or reasonably should know that the organization's interests are adverse to those of the individual, the lawyer must explain to the individual that the organization is the lawyer's client. That is, an in-house lawyer must ensure employees understand that she does not represent them individually, and any discussion with her may not be kept confidential or privileged. (Model Rule 13(g) provides that the in-house lawyer may represent an individual jointly with the organization when doing so does not present a current client conflict under Model Rule 1.7.)

The duty of confidentiality runs to the organization, and the organization owns the privilege. Any lack of clarity on this point may create an impermissible conflict of interest and compromise an in-house counsel's ability to continue to represent the organization effectively, including due to the organization potentially forfeiting control of its otherwise privileged information to personnel claiming to be her clients. Consequences may include disqualification from the matter and possible malpractice claims. An in-house counsel also may find herself named as a witness in a matter.

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The Potential for Conflicts of Interest and Inadvertent Employee-Clients Necessitates the Use of So-Called *Upjohn* Warnings.

Interviews and, where appropriate, other formal or informal conversations with employees about matters in which they may have distinct, personal interests should begin with a discussion of confidentiality and privilege, including reminders that an in-house does not represent the individual personally and that, while the communications are confidential and privileged, she may share anything said by the individual with others in or outside the organization because the privilege belongs to the organization.

Wearing Multiple Hats

Similarly, an in-house counsel must be clear as to whether she is advising on a legal or business matter. In-house counsel may be consulted on a wide variety of issues, including regulatory, compliance, personnel, public relations and business negotiations. Whether such communications constitute legal or business advice or some combination thereof can implicate privilege and ethics issues. Because an in-house lawyer's role often blurs these distinctions (or can later be claimed as such by an adversary), courts tend to scrutinize claims of privilege by an in-house lawyer more rigorously than those of an outside counsel. To preserve a later argument that the attorney-client privilege applies, an in-house counsel must indicate unambiguously where the advice sought or given is predominantly legal, or risk it being discovered by third parties.

To strengthen a later assertion of privilege, documents seeking or providing legal advice from in-house counsel should identify in-house counsel as such and contain an explicit reference to a request for legal advice. Consider using a header such as "Request for Legal Advice" in addition to "Privileged and Confidential." If nonlegal personnel are communicating among themselves regarding legal advice or to collect information at the request of counsel, they should reference the request for legal advice or the request from counsel, *e.g.*, "for the purpose of seeking legal advice" or "at the request of counsel."

In addition, an in-house counsel should consider that offering business advice may dilute the effectiveness of her legal function. Because business assessments are often subjective and generally open to discussion and judgment among non-lawyers, a lawyer providing business advice or advice that combines legal and business judgments may create the perception that her legal counsel is also founded on subjectivity and ultimately beholden to the bottom line. This risks undermining her authority, which can be particularly problematic when handling objective legal requirements that could impose a cost on the business. Maintaining the trust of the organization's business people is crucial to an in-house counsel's success, and delving into a business role may undermine her credibility when it is most needed.

Promoting a Culture of Compliance

Ultimately, an in-house counsel's function is that of risk manager. Success requires establishing clear standards that are appropriate and practical. She must ensure — through training and formal and informal discussions — that employees are aware of and can identify the relevant risk issues, including when to turn to the legal department for guidance. Not every risk issue requires legal counsel involvement, so an effective in-house counsel will provide colleagues with the knowledge and tools to address foreseeable issues before they rise to the level of requiring the legal department's assistance or intervention.

An in-house counsel should not be afraid to be a deal-breaker when necessary. Sometimes colleagues need a reminder that an in-house counsel's role is to manage risks to the business and to enable the business to operate with the utmost integrity. This becomes easier as she builds credibility by offering thoughtful, practical legal guidance and develops her colleagues' confidence in her judgment. The time spent cultivating the perception of an in-house counsel as a principled partner dedicated to the organization's best interests will contribute significantly to her effectiveness and her client's ongoing success.

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Matthew Henderson concentrates his practice in the representation of attorneys in legal malpractice cases and disciplinary proceedings. He has extensive experience litigating consumer class action cases, including actions brought under the Fair Debt Collection Practices Act. Mr. Henderson also regularly represents businesses in contract actions and other commercial disputes.

Mr. Henderson regularly speaks and writes on attorney malpractice, legal ethics, attorney discipline, and risk management. He serves on the Chicago Bar Association Committee on Attorney Malpractice and also on the Professional Responsibility Committee. Mr. Henderson is also a member of the Illinois State Bar Association.

Mr. Henderson was an author of the American Bar Association's Amicus Curiae Brief filed in the United States Supreme Court case, Williams-Yulee v. the FloridaBar,135 S.Ct. 1656 (2015). The brief, which argued the ABA Model Rule prohibiting judicial candidates from personally soliciting campaign contributions does not violate the First Amendment, was cited twice in the decision.

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Lawrence S. Spiegel has more than two decades of experience advising individuals and corporations in complex criminal and civil matters. He has represented corporations, their directors, officers and employees in cases involving allegations of mail and wire fraud, securities fraud, tax fraud, government program and procurement fraud, bank fraud, consumer fraud and money laundering. He represents clients in connection with federal and state grand jury investigations, in inquiries by regulatory agencies, including the Securities and Exchange Commission, and at trial. He has successfully defended many clients in high-profile criminal investigations and indictments and on appeal. Mr. Spiegel has particular experience advising clients in the context of concurrent criminal proceedings and civil litigation. In addition, he has led many corporate internal investigations, and has advised boards of directors and management of public and private companies on compliance issues and programs, including those related to the Foreign Corrupt Practices Act.

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The *Financial Times* writes, "John Villa, of Williams & Connolly in Washington, has a reputation for being the lawyer that law firms turn to when in a spot of bother." *The American Lawyer* has called him "perhaps the premier [legal] malpractice defense lawyer in the nation." The *Washington Post* reports "John Villa of . . . Williams & Connolly [is] the lawyer and firm that lawyers and law firms turn to when they're in trouble," and describes him as "a litigator who has gained national prominence with a somewhat rare specialty: defending top-flight law firms in trouble." John was named to The *National Law Journal*'s list of "100 Most Influential Lawyers in America" as "the first lawyer that other attorneys and law firms turn to when caught up in the S&L and banking scandals." In its 2014 list of "6 Firms to Have on Speed Dial if Malpractice Trouble Hits," *Law360* puts Williams & Connolly and John Villa first. He has represented a substantial number of the largest law firms in the United States, but does not disclose his clients.

John was listed as one of the top 100 trial lawyers in America by *Benchmark Litigation*. He has argued before every federal court of appeals and the highest courts of three states and appeared in the federal or state courts of more than twenty states.