

Conflicts of Interest: The UK Perspective

Regulation of lawyers in England is carried out by the Solicitors' Regulation Authority - commonly called the SRA. The SRA was set up by the Law Society in 2006 and the Law Society still sets the SRA's budget. Although not a government body, the members of the SRA are appointed (rather than elected) by an independent body and, from 2010 will be subject to oversight from the newly constituted Legal Services Board – whose members are appointed by the Lord Chancellor – a political post.

In a time of massive change in the regulation of the English legal system, the debate about a common code of practice for the legal professions of Europe is of particular importance. Some of you may have seen the consultation issued by the SRA concerning amendments to the rules on conflicts of interest. This is a very contentious issue in England and it is not the first time that the regulatory rules have been debated.

At this point, I should clarify that the issue under debate is the *regulatory regime* concerning conflicts of interest. The *law* in England, as it relates to conflicts of interest, can only be changed by legislation and can be expressed as follows:-

“A [lawyer] cannot act at the same time both for and against the same client, and his firm is in no better position. A man cannot without the consent of both clients act for one client while his partner is acting for another in the opposite interest. His disqualification has nothing to do with the confidentiality of client information. It is based on the inescapable conflict of interest which is inherent in the situation.”

Lord Millett – *Bolkiah –v- KPMG* [1999] 2 AC 222

Notwithstanding that this case was brought by a notorious playboy who allegedly treated an airline as his private plaything, it was heard by the House of Lords, the UK's highest court, and is therefore binding on all other courts and tribunals in the UK. Of course, the House of Lords would not be swayed by a bit of scandal!

There is, of course, a fundamental difference between the law and the regulatory regime. The regulatory regime allows the SRA to take action against solicitors for acting in breach of the rules whether or not the client has complained and provides a non-judicial avenue to make a complaint; the common law gives an individual client the right to challenge his solicitors in court and, if necessary, prevent them from acting for a third party.

The most recent (and high profile) example of this in the UK was the case of *Marks and Spencers Plc –v- Freshfields Bruckhaus Derringer*. The case concerned an attempted hostile takeover of Marks & Spencer by a consortium led by the entrepreneur Philip Green. Freshfields had acted for Marks and Spencer in some non-contentious transactions and it maintained that there was no conflict of interest if it acted for Mr Green's consortium, or, if there was, it could be managed so as not to risk client confidentiality. Marks and Spencer disagreed and sought an injunction preventing Freshfields from acting for Mr Green's consortium.

There are those who consider that the litigation was tactical, designed simply to delay the attempt at hostile takeover and that Marks and Spencer would not have objected but for the opportunity to derail the bid – which ultimately worked. In any event, the Court of Appeal upheld Marks and Spencer's position and refused an appeal against the injunction.

It is perhaps interesting that the case was brought by a sophisticated corporation with access to vast resources – including advice from one of the largest law firms in the UK - against another of the largest law firms in the UK and was strongly contested on both sides. It may be reasonable to assume therefore that the question “what is a conflict of interests?” is harder to determine in practice than it first appears. The Court of Appeal had no hesitation in finding that there was a conflict of interests however Freshfields and those advising them obviously felt that there was none at the time.

In this case, the SRA reviewed the finding of the Court and issued disciplinary proceedings against the solicitor involved. He was ultimately fined £9,000 and ordered to pay £50,000 in costs. But for the Court action, it is unlikely that the SRA would ever have identified an issue or taken any action in this particular case. That said the SRA does frequently investigate allegations of conflicts of interest. The more serious allegations usually relate to a conflict between the interests of the solicitor and their own client but such allegations can take many forms and often, the client may have been wholly unaware that the solicitor was acting improperly.

It is this general imbalance of power and knowledge between lawyers and their lay clients which has led the SRA to impose more restrictive rules in an effort to ensure that lawyers do not take unfair advantage of their clients.

These more restrictive rules are not without difficulty, notwithstanding that, in their current incarnation, they have only been in force for around four years and there is an ongoing debate, driven principally by “City”¹ firms (such as Freshfields) concerning whether our regulator’s conflict of interest rules should be relaxed – yet again. Some of you may have seen the SRA’s consultation on the subject. Indeed, at the beginning of September, the SRA published an analysis of responses confirming that the rules would be amended. We await with eager anticipation the SRA’s proposals for the amendments and the further consultation on the draft rules, due to be issued in autumn 2009.

It is perhaps helpful at this stage to sound a note of caution; lessons from the past have shown that there are real risks in relaxing rules relating to conflicts of interest. The two most striking examples are in relation to the sale and purchase of property and referral fees. You should be aware that the legal aspects of property transactions are usually handled by solicitors.

It has been permitted for a solicitor to act for both the buyer of a property and the mortgage lender for many years. There are a number of safeguards in place, including the

¹ large, mainly multinational firms which act for large corporate clients

requirement to comply with the requirements of a set of standardised instructions, called the Council of Mortgage Lenders' Handbook. The current recession (and indeed, the recession in the early 1990s) has thrown into sharp relief the problems of mortgage fraud. In many instances, mortgage fraud has been allowed to occur because a solicitor fails to recognise his obligations to disclose relevant information to lender clients. This failure is, of course, very bad news for the reputation of our profession when the issue of fraud hits the headlines.

It can be said that there are strong commercial reasons for permitting solicitors to act for both lender and purchaser because it ultimately reduces the cost to the purchaser by cutting out one set of legal fees. One must however ask whether the profession should yield to commercial pressure to waive, amend or reduce professional obligations. Is it not the case that our collective reputation suffers – and costs to the consumer are ultimately increased – by the opportunities for fraud or error? It is, of course, a regulator's invariable response to large scale issues of fraud, that regulation should be increased. There should be more oversight and more rules and the costs of compliance are thus increased – and passed on to the consumer.

The same sorry story is true of the relaxation of rules relating to the referral of clients and payment of referral fees. The rules were relaxed five years ago and already a massive referral industry has been created, covering many areas of law. Personal injury is by far the largest target and the so-called "claims farmers" have certainly done their bit for the reputation of the profession. Solicitors do, of course, have an interest in keeping the referral company happy; is this interest consistent with their duties to clients? Sometimes, the answer will be a resounding yes but there is a real and increasing risk that overreliance on referral companies will lead to a serious conflict of interest arising.

As I have already said, the regulator's rules as they currently stand are more stringent than the common law rules and it is a disciplinary matter if they are contravened. In the event that a client complains to the Legal Complaints Service, there is also a statutory power for the Legal Complaints Service to award some compensation. There is, of

course, the problem that many clients would not recognise a conflict of interest and would not know that they had a right to complain.

I have provided a copy of the current rules, in their entirety, as an attachment to this speech. I am quite sure that we have better things to discuss today than simply repeating the rules (which are likely to be amended soon in any event). You can see that the basic rule in respect of conflicts of interest is not to act where:-

- a) you are acting for another client with conflicting or potentially conflicting interests; and
- b) your interests (or those of your firm) are or may be in conflict with the interests of your client.

This basic rule is subject to several exceptions, all of which require that certain conditions are met and that the clients all consent in writing to you acting. The most common exception relied upon is where you are acting for two clients who have “substantially common interests.” This would cover situations where, for example, you are asked to advise both clients on a joint venture and its potential ramifications. It may also cover advising joint claimants or defendants in litigation in some circumstances.

It is important to note that, where a solicitor is relying on an exception to the duty not to act, it must be reasonable in all of the circumstances for him to act. The SRA will expect the solicitor to demonstrate that he can act for both clients properly, without fear or favour affecting his advice to either one. There is also a continuing requirement to ensure that it remains reasonable for the solicitor to act throughout the retainer.

The new rule is widely anticipated to have a broader exception, to permit firms to act where there is or may be a conflict of interest provided the clients are “sophisticated” and have consented to the firm so acting. There is likely to be substantial debate about the definition of “sophisticated client.” As matters stand, the definition of sophisticated client is likely to be limited to clients with their own in house legal departments or those who

have taken independent legal advice before confirming that they will waive the conflict. There is also clear scope for clients to argue about the consent that they have given. There may be difficulties regarding clients claiming, for tactical reasons that the consent was given based on a misunderstanding or mistaken information and should be withdrawn. It is my view that there is a potential minefield for solicitors here and it remains to be seen how the SRA will address the issues in the draft rules.

It is likely that the English authorities will continue to interpret any amendments to the rules in favour of the client. The courts take the view that the rules are there for the protection of clients and solicitors should not be able to get around the substance of the rules by focussing on a strict interpretation of the wording. The courts consistently emphasise that a solicitor's duty to act in the best interest of his client is second only to the solicitor's duty to the court and to maintaining the rule of law. Against this background then, it is likely that solicitors will have to demonstrate that they have explained, in some detail, the potential ramifications of their acting in a situation of conflict. I suspect that a failure to fully explain the nature and effect of a potential conflict of interest will lead to any written consent being set aside.

Turning now to the potential sanctions for acting where there is a conflict of interest, it is of note that most cases involving conflicts of interest referred to the Solicitors Disciplinary Tribunal fall into one of four main categories:-

1. The solicitor has acted for both purchaser and mortgage company in a property transaction and has failed to inform the mortgage company of a potential conflict of interest;
2. The solicitor has acted for a client where he (the solicitor) is the other party so, for example, a solicitor takes a loan from a client or buys a property from or sells a property to a client;
3. The solicitor has acted for a client where he has a personal relationship with a third party interested in the transaction in one way or another; for example,

referring a client to a family member who is perhaps a barrister, or acting for a client where a family member is the other party to the transaction;

4. The solicitor has entered into a referral arrangement with a third party which may compromise his ability to advise the client independently or put confidential information at risk.

It is uncommon for solicitors to be wholly prevented from practising, either permanently or temporarily, because they have acted in a situation of conflict of interest on a one off occasion, although such conduct is regarded as serious. That is not to say it is not possible, particularly where the conduct is deliberate or grossly improper. The position tends to be addressed by the imposition of a reprimand or fine, depending on circumstances and it is possible that a solicitor may have conditions imposed on his or her practising certificate. Repeated or deliberate infractions would be likely to lead to a more serious sanction.

I should mention at this stage that the SRA is going to be given new powers to publicly fine and rebuke solicitors for misconduct directly. At present, the SRA's disciplinary powers are limited to internal sanctions and all formal powers are exercised by the Solicitors Disciplinary Tribunal. The changes are designed to increase proportionality and reduce the cost of prosecuting misconduct at the lower end of the scale. It is likely that many of the less serious allegations of conflict of interest will be dealt with in this manner in the future.

The question of publicity is a thorny one. Any public rebukes or fines issued by the SRA – which will be issued without a formal hearing – will be published on the SRA's fully searchable database for a default period of three years unless the solicitor can demonstrate that they should not be published – no easy task, I assure you. Publicity is consistent with the SRA's new publicity policy. It is their view that transparency in regulation requires that disciplinary decisions be published, save in exceptional circumstances. I must confess that I do not share the SRA's view on this point, either in principle or in practice – but that is a debate for another day.

On a slightly separate point, the question of publicity is relevant to all lawyers wishing to practise in the UK. Any Registered European Lawyers or Registered Foreign Lawyers effectively submit to the jurisdiction of the SRA and, of course, the searchable database is online and is searchable from anywhere in the world. It may be the case therefore that foreign lawyers who work in England and are found to have breached the rules will be the subject of adverse publicity in their home bar notwithstanding that the rules of their home jurisdiction would not have been infringed. These are, I believe, serious issues facing the legal profession in the UK at present.

At this stage, I would like to say a few words about client confidentiality. In many ways, confidentiality is one of the overriding concerns when considering conflicts of interest and many of my earlier comments may be taken simply to include client confidentiality as an element to consider in the wider context of conflicts of interest.

It must be emphasised though that client confidentiality is a distinct duty owed by every solicitor to each of his clients. A solicitor also owes a duty to each client to inform them of relevant information which comes to that solicitor's personal attention, no matter the source. It is easy to see how these duties might conflict when advising clients in situations of an actual or potential conflict of interest. The current rules make it clear that the duty of confidentiality is paramount but it is likely that the solicitor affected would have to cease acting for one or both clients as he can no longer fulfil his competing duties to both.

In summary then, I think it is fair to say that a solicitor who acts where there is a conflict of interest is potentially in grave professional danger. Although there are situations where it is permissible to act in circumstances of a conflict of interest, there are numerous difficulties, particularly if matters become contentious.

There are calls for relaxation of the rules and these calls are likely to be followed. My perhaps somewhat cynical opinion is that this will only lead to more complex rules which

are more open to abuse. I am guessing that we will have to wait some time before the true effect of the changes becomes clear.