

# The Rules of Professional Conduct as Public Policy

Pennsylvania courts rarely reference the Rules of Professional Conduct (RPC) as a statement of public policy. When they do, it most often involves claims for wrongful termination of an at-will employee where some facet of public policy is threatened. See, e.g., *Paralegal v. Lawyer*, 783 F.Supp. 230 (E.D. Pa. 1992). The rules have also been applied in Pennsylvania cases voiding fee-sharing agreements not made in compliance with the RPC.

In a recent decision, the Supreme Court of Washington considered the issue of whether its version of the RPC can be referenced as a statement of public policy and concluded that it can. As a result, the Supreme Court affirmed the finding of the trial court that a joint-venture agreement was unenforceable as violative of public policy because two attorneys, who were parties to an agreement with non-lawyers, had entered into the agreement in violation of one of the rules.

In *LK Operating, LLC v. The Collection Group, LLC*, \_\_\_ P.3d \_\_\_, 2014 WL 3765499 (Wash.), defendant lawyers formed and represented a limited liability company that was essentially owned by their adult children through trusts they controlled that were the LLC's members. The defendant lawyers were approached by one of their clients, an accountant, with a proposal for the lawyers to get involved in a debt-collection business that would be run as a joint venture. The lawyers would provide half of the money and legal services, and the accountant client would provide the management services and the other half of the money. Neither side would charge for their services. The lawyers would own half of the joint venture, and their accountant client would own the other half. The lawyers saw this as an investment for their children's LLC.

There were two unfortunate developments in the deal. First, the parties never entered into a formal joint-venture agreement. Instead, the accountant client relied upon an email exchange with one of the lawyers that made him believe that the lawyers had accepted the proposal. Second, neither lawyer complied with the requirements of Rule 1.7, which impose restrictions on lawyers going into business with clients. The version of that rule in Washington state at the time required that the lawyers procure the informed consent of both of their clients — the LLC owned by their children and the accountant client — before entering into the joint venture.

At some point the accountant client contacted both the lawyers' legal assistant and bookkeeper "to request half of the funds needed to purchase the Unifund debt portfolio." He eventually received a check for half of the needed funds, but, instead of it being from the law firm checking account, it was a bank cashier's check with a notation that it was issued on behalf of the LLC owned by the lawyers' children. Over the next two years the accountant client received subsequent payments equal to half of the funds needed to purchase each subsequent portfolio from the same source. One of the lawyers and one of their legal assistants provided legal services to the accountant client's LLC at no charge.

The arrangement soured when the accountant client wanted to renegotiate under terms more favorable to him. When the lawyers refused, the accountant client, through his counsel, announced that his LLC would engage in no further purchases of portfolios with the lawyers. In response, the lawyers took the legal position that they had no interest in the joint venture and that it was their children's LLC that was the only other party. The children's LLC alleged that thereafter the accountant client began transferring the joint venture's accounts to another debt-collection company wholly owned by the accountant client, causing the children's LLC to sustain damages.

Litigation ensued. The LLC owned by the children of the lawyers sued the accountant client and his LLC "for declaratory relief regarding the allocation of ownership interest in (the joint venture), breach of contract, and breach of fiduciary duty. ..." In response, the accountant client and his LLC sued the lawyers for legal malpractice. Although the accountant client denied the existence of a joint-venture agreement, he contended that, if one existed, it was void ab initio as contrary to public policy. Specifically, he contended that the lawyers had represented both the accountant client and their children's LLC without resolving this conflict under Rule 1.7.

The trial court rejected the lawyers' arguments that the only appropriate remedy for a violation of the disciplinary rules "would be limited to an attorney disciplinary action against [the lawyers]" and that no violation occurred because they were not parties to the deal. The trial court found that, based upon violation of the disciplinary rules, the agreement was voidable by the accountant client and his LLC and that they were also entitled to damages. Accordingly, the accountant client opted to rescind. The Court of Appeals, Washington state's intermediate appellate court, affirmed and the Supreme Court granted allowance of appeal.

The Supreme Court's majority opinion acknowledged the lower court's holdings that RPC violations "in the formation of a contract may render that contract unenforceable as violative of public policy." It reasoned that it had the "legal authority to set public policy in the context of attor-

## Avoiding Liability



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ney ethics" because of its inviolate power "to regulate the practice of law." In the majority's view, however, not every violation incurred in the making of a contract automatically makes it unenforceable. Instead, "[t]he underlying inquiry ... is whether the contract itself is injurious to the public. While all RPC violations are in some way injurious to the public, not all RPC violations will render any related contract injurious to the public." Instead of applying Rule 1.7, as had the trial court, the majority focused instead on Rule 1.8(a). It found that "a contract entered in violation of former Rule 1.8(a) is presumptively, but not necessarily, unenforceable." The Supreme Court of Washington ultimately affirmed the lower court.

One justice dissented, concluding that rescission should not have been granted. Quoting from the preamble to the RPC, the dissenting opinion contended that the rules "were never intended to serve as the basis for civil law actions or remedies." In the justice's view, there are "[s]trong policy justifications [to] support the Scope section's preference for separating the law of ethics codes from other civil law decisions." According to the dissent, granting rescission was a disservice to the children's LLC, which was an innocent party, because it prevented the LLC from enjoying the benefit of its bargain.

This case illustrates the importance of compliance with the RPC in all dealings. It also teaches that a violation of the rules may lead to civil liability and unintended adverse consequences.