

Loss Prevention – It Begins at the Front Door

By Peter A. Giuliani

Several New York-based law firms are member of Attorneys' Liability Assurance Society, Inc., the captive mutual professional liability insurer of hundreds of law firms across the country. Familiarly known as "ALAS", the Chicago-based Society regularly publishes updates to its first-rate law firm loss prevention manual. For member firms, the manual is a valuable guide for managing and administering law practices to minimize exposure to malpractice claims and suits. New York's smaller firms, and non-member firms, can benefit from what ALAS has to say about client intake.

Often, ALAS' updates are provocative, and the latest one, "Identifying Good Clients and Avoiding Bad Ones: A Business Intake Management Guide" is no exception. ALAS has always asserted that the best loss prevention tool is the front door. Extensive research bears witness to the fact that, in most claims, the insured firm would not be involved if it had simply not accepted the "unworthy client" in the first place. Most often there are "yellow flags" that should have alerted the law firm about problem clients early enough in the intake process to have avoided taking on the client.

"Unworthy clients" are not simply those who are dishonest and unscrupulous. They may have flawed or misdirected business plans. They may be financially unstable and unable to pay for legal services. Then, there are those who are never satisfied with any lawyer or outcome and frequently skip from firm to firm, leaving behind unpaid bills and chagrined partners.

Too many partners in too many firms are so hungry to bring in new business, that they lose objectivity during the client intake process. If the intake processes lack rigor and discipline, it is too easy for "unworthy clients" to get in the door. Once retained, the firm may have difficulty detaching itself from the client. Too often, the firm doesn't recognize the problem until after the client has run up a big tab and the originating partner is loath to cut bait and move on, because of the significant fee losses involved.

For ALAS, "The first line of defense against unworthy clients is a sound business intake system." This is true for clients who are new to the firm, but may also apply to repeat clients who have experienced financial adversity, key personnel changes, discontinued operations, and/or significant changes basic business structure. For that reason, ALAS recommends conducting a periodic review of existing clients, especially public companies and those privately-held clients who are seeking raise third-party financing or who are acting in some kind of fiduciary capacity.

What is involved in a sound intake process? Here's an outline based on ALAS' advice:

1. Conflict Search and Resolution – Every intake process should begin with a thorough conflict search, not just for possible adverse parties, but for possible

- adverse positions the firm may have taken in prior cases. Patent firms need an additional conflict check into adverse or competing technologies.
2. Creditworthiness Review – Telling a prospective client that you want permission to conduct a credit check is probably not going to win any points with the client. There is, however, a wealth of information available on the internet through a wide range of sources. The obvious starting points might be Dunn & Bradstreet and Moodys. Other on-line sources of company and individual credit information include CRIBIS, Experian, Thomson West and Equifax, Inc.
 3. Independent Review of Client/Matter Intake Decisions – In handling client intake, perhaps the most effective procedure is to require a separate review by an independent and disinterested party. That person could be the Managing Partner, the firm's Loss Prevention Partner, or any other partner not immediately involved with the originating partner's practice. This review should include a thorough and dispassionate review of all information gathered through the conflict and creditworthiness checks. All of this counts for nothing, however, if the independent reviewer lacks the authority or courage to turn down the client.
 4. Further Due Diligence – If the initial credit check turns up anything questionable, and the firm still wants to pursue the matter, the next step should be a personal background check on the individual client or, in the case of a company, on owners, officer, directors and key shareholders. Here again there are ample resources available on-line. Alternatively, the firm may elect to engage a private investigator to do a background check.

Law firms that want to get really serious about managing the quality of their client bases should also consider linking client intake to partner compensation. Part of the intake process should be to keep a continuing record as to prospect and client quality by originating partner. Consider, for example, two partners each having \$1 million in originations. One partner's clients pass creditworthiness and due diligence reviews with flying colors. The other partner exhibits a history of introducing clients of questionable creditworthiness or whose background checks raise "yellow flags". Clearly, the former partner is worth more to the firm than the latter.

Though these procedures may irritate partners who originate business, the best advice is: Just say, "Know." If what you find out raises too many cautionary flags, have the courage to say "No." before a risky situation turns into an intractable situation.