



Monday, May 16
2:00–3:00 pm

301 Conflicts of Interest
New to In-house Track

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In-house Ethical Conflicts

Recognizing and Responding to Them

IMAGINE THAT you've just been hired as the new general counsel of Sky Securities. Although you're delighted to have the job, your first day becomes more of a learning experience than you had anticipated.

Your 9 A.M. meeting is with your new boss, the CEO. Both you and he are eager to discuss the areas that you should focus on first. Before your meeting, you reflect on the thought process that led to today. You had thought long and hard about accepting this job. It's your big chance—professionally and financially—since you missed the tech boom of the 1990s, bypassing the many opportunities that came your way to join a dotcom. You left a partnership at a nationally renowned law firm to take the job. Sky Securities is young (three years old), hungry (everyone works nonstop as a team), and aggressive (formed by investment professionals whose most significant experience was the tech boom). It seems like a great place to work, and you're looking forward to this meeting to prioritize your initial efforts.

**By Steven N. Machtinger
and Dana A. Welch**

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The CEO greets you and says, “We have a lot to get done here, but there are a few areas that I really want you to focus on initially. First, the credit committee. With your attention to detail and analytical mind, we really need you to help us evaluate who should get margin loans. Next, as you know, we’re in business generation mode. I know that you have ties with all of the major law firms in town, and because they no doubt have clients in need of investment banking services, we need you to go out and build our law firm relationships to get those introductions. And even though it’s not your first priority, when you get a chance, could I have your thoughts on my employment agreement? I trust your judgment implicitly.”

The meeting has lasted only three minutes, and you’ve been on the job barely an hour, but already, you’re facing issues that you had never foreseen when you decided to join Sky Securities. The CEO has just breezily invited you to put yourself into the middle of several potential ethical conflicts:

- **The credit committee:** he’s asked you to join this committee not to evaluate the legality of margin loans, but to perform the business function of evaluating the creditworthiness of clients. What happens if and when a client ultimately defaults on a loan and you as chief legal officer are forced to initiate a collection action? You will be litigating about a loan that you will have had a personal hand in approving.

- **Building relationships with law firms:** you’ve been asked to generate new business by using your legal contacts. Although not explicitly stated, the implicit message is that law firms who produce business for Sky Securities will be similarly rewarded with Sky Securities business. Instead of being asked to select outside counsel best equipped to handle the company’s legal problems, you are being asked to select on the basis of business sourcing. Is your role that of another business generator, not too different from that of the investment bankers, or of an adviser whose principal concern is the protection against legal risk?
- **The CEO’s employment contract:** you are smack dab in the middle of a particularly uncomfortable, if classic “who is the client?” conflict. You must make the assumption that your boss and the corporation have adverse interests that are reflected in the employment contract. You know that your client is the corporation, but the CEO might not. Or if he does, he might brush off any suggestion that there’s a conflict between the two.

The above conversation may be unlikely to be packed into your first three-minute meeting with your boss, but both of us in our capacity as in-house counsel (one current and one former), as well as our counterparts at other companies, have had conversations that contained elements similar to one or more of the elements above.

Professional responsibility class in law school did not prepare us for the number and scope of the ethical dilemmas and conflicts that we face every day as in-house lawyers. The Model Rules of Professional Conduct (and their state counterparts) are not much help, either; for example, nowhere do the rules specifically address whether lawyers may also serve in a business capacity, although the rules are free from doubt when identifying the organization as the client. And no one prepared any of us—nor could they have—for the intense discomfort of making an unpopular call when we’re part of a team.

This article is designed to give practical guidance on recognizing an ethical dilemma or conflict when you’re in the middle of it and gracefully navigating your way out of these potential traps in a manner that preserves the client’s interests and your own reputation.

THE BACKGROUND AND THE RULES

The Model Rules of Professional Conduct, on which most states base their ethical codes, provide the starting point for this discussion. The Preamble to the Model Rules recites that our duty is to represent our client zealously. Rule 1.13 tells us who our client is: the organization, not an individual employee, director, or officer. The newly amended Model Rule 1.13 (which is a minority rule, not having been adopted by most state bars) allows permis-

ETHICAL RULES THAT APPLY TO IN-HOUSE LAWYERS

- **Model Rule of Professional Conduct 1.1.**
Must represent the client competently.
- **Model Rule of Professional Conduct 1.2.**
Cannot assist in fraud.
- **Model Rule of Professional Conduct 1.6.**
Confidentiality of information; permissive disclosure of otherwise confidential information allowed in certain circumstances in which harm to third parties will result from crime or fraud and in which lawyer's services have been used in furtherance of the crime or a fraud.
- **Model Rule of Professional Conduct 1.7.**
Cannot represent client in instances in which there is a concurrent conflict of interest absent waiver.
- **Model Rule of Professional Conduct 1.13.**
Organization is client; may report out potential or actual violation of law that is reasonably likely to be imputed to the organization and that is reasonably certain to result in substantial injury to the organization if the highest authority within the organization fails to or refuses to act.
- **Model Rule of Professional Conduct 2.1.**
Must exercise independent professional judgment.
- **SEC Rule 205** ("Up-the-ladder" reporting rule for lawyers practicing in front of the U.S. Securities and Exchange Commission). Must report evidence of wrongdoing up the chain of command and receive "appropriate" response; may, but need not, report it out.

sive disclosure of certain bad acts by employees, officers, or others associated with the organization, if the lawyer reports all the way up the ladder within the organization, the highest authority refuses to rectify a problem, and the organization (not third parties) may be harmed. Rule 1.7 proscribes concurrent conflicted representation, absent a waiver. Rule 2.1 exhorts us to exercise independent professional judgment. And of course, we cannot use our legal expertise to assist a fraud, according to Rule 1.2. The newly amended Model Rule 1.6 (in conformity with the rules of 42 states) allows permissive disclosure of financial frauds in which the lawyer's services were unwittingly used and where there will be resulting financial harm to third parties. The sidebar on this page highlights the relevant rules.

Increasingly, in response to the latest wave of corporate scandals, regulators are insisting that lawyers, most particularly those of us in-house, serve as gatekeepers, with an obligation to protect the investing public and provide a first line of defense for the regulators. For example, with the enactment of the new "up-the-ladder" rules, the U.S. Securities and Exchange Commission ("SEC") is for the first time regulating attorney conduct for many public company lawyers.

Although the Model Rules and their state counterparts provide the parameters for much attorney conduct, no rule, guideline, or prescript informs the issue of in-house lawyers serving in a business, as well as a legal, capacity, a position that most of us inevitably find ourselves in at least some of the time. The sidebar on page 27 highlights certain frequently recurring situations in which this conflict arises.

BEING A TEAM PLAYER: BE CAREFUL WHAT YOU ASK FOR

Getting back to our opening hypothetical, after the three-minute meeting has ended, you begin to become aware that you have been confronted with some potential ethical conflicts, but equally pressingly, you realize how hard it's going to be to say no to your new boss. All kinds of pressures are bearing down: the pressure to be responsive, the desire to be a team player, to become a fully appreciated and totally connected member of the executive team.

But the pressure that you feel is more than the pressure to be part of the club. You want to make sure that your boss and other business people come to you often with their legal issues. You've been at the job exactly one day, and you know that it will take a while to establish credibility, and while you're establishing yourself as a member of the team, you don't want to appear to be "difficult." Even more importantly, you know that being part of the inner circle means that you'll get better assignments, have access to more important people, and be included when important decisions are being made, all of which will make your job more enjoyable and enable you to give better legal advice. And on top of all of that, you know—and the CEO knows—who signs your paycheck.

There is, however, a price to pay for being part of the inner circle. Constraining the client—sometimes, even getting the client to listen to you—becomes difficult. Maintaining objectivity becomes difficult. Giving objective advice—exactly what we are paid to do—becomes difficult.

Once we have become part of the inner circle, it becomes harder to challenge—indeed, even to see—fundamental assumptions about the way that a company operates. Biases to defend a course of action become even stronger when we have participated in the decision to embark on that course of action.¹ Of course, there is also a penalty to being outside the inner circle: we have less access; clients tell us less; and we have less opportunity to protect our clients (that is, to make sure that things are done the right way). If we are not part of the inner circle, we may have less interesting work and, in most cases, less compensation.² So the tension is this question: how can a well-integrated (and therefore presumptively subjective) member of corporate management, as in-house counsel must be to be effective, ever claim to provide what the Rules (Model Rule 2.1), our ethics, and our clients demand: "independent," candid legal advice?

Resolving this tension has proven enormously difficult, and the regulators have stepped into the breach. In the wake of corporate scandals over a long period of time—National Student Marketing,³ National Telephone Company,⁴ Lincoln Savings,⁵ Salomon Brothers,⁶ Enron, Tyco, and WorldCom, among others—the investing public, the SEC, and other government regulators have asked, "Where were the lawyers?"

The result, especially in light of § 307 of the Sarbanes-Oxley Act (15 U.S.C. § 7245) and new SEC Rule 205 (the "up-the-ladder" reporting requirements, discussed more fully below), has been to impose limits on the degree to which a lawyer can be part of the business team (as opposed to a gatekeeper, deputized regulator, or even a whistleblower) in those situations involving possible material violations of the law.

THE REGULATORS RESPOND AND MAKE CORRESPONDING CHANGES TO THE ETHICAL RULES

After the collapse of Enron, Congress joined in the chorus asking where the lawyers had been and in short adopted § 307 of Sarbanes-Oxley, in which it demanded that the SEC draft rules requiring that lawyers representing public companies report evidence of wrongdoing. The SEC responded in August 2003 with Rule 205 (17 C.F.R. Part 205), the "up-the-ladder" rule.

AREAS OF CONFLICTS AND ETHICAL DILEMMAS

You should be on the lookout for conflicts or ethical dilemmas in the following circumstances:

- You have served as a decision maker, and someone is challenging the validity or legality of the decision.
- You are asked by an individual employee or officer for legal advice about something that is personal to him or her.
- You are asked to take on a nonlegal, business role in addition to your legal role, so you are "wearing two hats."
- You are asked to serve on the board of directors of your company.
- You are told to generate new business, not control legal risk.
- You are a member of the executive team at a wholly owned subsidiary.
- You are asked by an employee or an officer to keep a problem confidential.
- You are asked for legal advice on something in which you have a personal stake.

Rule 205 requires lawyers practicing before the SEC to report material evidence of wrongdoing up the chain of command within a company and permits, although it does not require, outside disclosure of wrongdoing. This permissive disclosure provision, which the ABA also adopted in modifying Model Professional Rules 1.6 and 1.13,⁷ contrasts and conflicts starkly with many state bar ethics rules, most notably and extremely those of California,⁸ which strictly prohibit any breach of lawyer-client confidentiality. In its final release on the new “up-the-ladder” Rule 205, the SEC noted that “generalized concerns about impacting the attorney-client relationship must yield to the public interest where an issuer seeks to commit a material violation that will materially damage investors, seeks to perpetuate a fraud upon the Commission in enforcement proceedings, or has used the attorneys’ services to commit a material violation.”⁹

THE PERHAPS UNINTENDED CONSEQUENCE OF A RULE THAT TURNS A LAWYER INTO A GATEKEEPER/DEPUTY REGULATOR IS THAT WE NOW MUST BE CONCERNED ABOUT MORE THAN ADVISING AND PROTECTING OUR CLIENTS; WE MUST BE CONCERNED WITH PROTECTING OURSELVES.

SEC Rule 205 requires that all lawyers “appearing and practicing” before the SEC, which includes in-house lawyers at publicly traded companies or their wholly owned subsidiaries, must report possible securities law violations up the chain of command within the corporation. The original proposed rule contained a “noisy withdrawal” provision that would have required attorneys not receiving an “appropriate response,” despite having climbed up all of the rungs of the reporting ladder, to withdraw from representation and to notify the SEC and/or disavow any false or misleading document filed or submitted with the SEC.¹⁰

Responding to the uproar that this provision raised among practicing lawyers, the SEC extended the comment period to consider both the “noisy withdrawal” proposal and an alternative approach

that would require the issuer to disclose in a publicly filed document the withdrawal of an outside attorney or the receipt of notice from an in-house attorney that he or she believed that the issuer had not responded appropriately.¹¹

Some would argue that Rule 205 requires no more of lawyers than what most of us already do—that is, move issues up the chain of command within our organization and seek an appropriate remedial response. Although this interpretation of Rule 205 is plausible, it is also true that the trigger for the reporting obligation in the rule is inherently ambiguous. The standard in the rule is that lawyers must be “aware” of evidence of a material violation.¹² Although we could define when we know something to a definite certainty, how do we define that point in time when we become “aware” of something? And how much evidence of a “material violation” is required before we must act?

For example, if someone forwards us an email containing a rumor of bad acts, have we become “aware” of a material violation? How about when an employee known to be highly disgruntled and therefore of suspect credibility brings to our attention what could be a big problem? These questions are as yet unanswered, but may be answered with the benefit of 20-20 hindsight in the context of a disciplinary action against a lawyer who failed to recognize a “trigger” for his or her reporting obligations. Also, what sort of response is “appropriate” to satisfy reporting obligations? Despite these (and other) difficult ambiguities, the SEC has now enacted a behavioral rule aimed squarely at attorneys, the violation of which may result in civil penalties or other remedies, including being barred from securities law practice.¹³

All of us can agree that a competent lawyer is more than a mere scrivener: a lawyer’s role is to provide professional, independent advice so that the client can best follow the law. But with these new rules, the regulators want a lawyer to do and be more. They want us to be gatekeepers. The perhaps unintended consequence of a rule that turns a lawyer into a gatekeeper/deputy regulator is that we now must be concerned about more than advising and protecting our clients; we must be concerned with protecting ourselves. It is not necessarily the case that the best interests of the client follow in this scenario. Any time that a lawyer must worry

about protecting his or her license and livelihood first, the interests of the client inevitably suffer.

SOME DANGER AREAS AND WHAT TO DO ABOUT THEM

What are some common traps, and how do you know when you're approaching them? What do you need to think about when making a decision about what course of action to take? There are no "one size fits all" answers here, but there are common themes and considerations to think about when facing a tough call.

You Are Not My Client—the Company Is: The “Corporate Miranda” Warning

Returning to our opening hypothetical, one of your first tough conversations is the not-so-pleasant task of informing your boss that you can't review his employment agreement on his personal behalf because you are counsel to the company, not to him personally. Our status as lawyers for the corporation, not for individual employees, is so fundamental to us that we may forget that this concept can be highly abstract or even lost on the business people with whom we work. Or they may be aware of it on some level, but not understand why we can't represent both them and the organization. To them, the conflict may not be so obvious. And indeed, there may not be a highly visible present conflict.

The “who is my client?” conflict comes in many forms and recurs on a frequent basis—perhaps because, when we are effective as in-house lawyers, our colleagues see us as part of their team. Here are some permutations: “Can you tell me whether I can make this trade?” “Can you help me with (fill in the blank), but not tell anyone else? I don't want my job to be endangered.” “The (fill in the blank) is making sexually suggestive comments to that young, attractive secretary, but I'm afraid that, if you do anything about it, they'll know that I brought it to your attention because she confided in me.” “This is a privileged conversation, right?” “You're my lawyer, right?”

Wrong. As stated previously, Model Rule 1.13 and its counterparts in the states tell us that it is the organization, not its individual officers and directors, that is the client and that our duties and loyal-

ties are to the organization. Turning to the original conversation, the most prudent assumption is that the CEO's and Sky Securities' interests in the employment agreement are (or will at a future time be) adverse, and you are ethically obliged under Rule 1.13(d) to explain (firmly, but gently) to your boss who the client is. This conversation is not an easy one to have the first day of a new job or, for that matter, at any other time.

The consequences of failing to make clear up front whom you represent will be endless and unpleasant. You can't do the job that you were hired to do if you leave the impression that you are always able to represent not only the company but also its employees. The CEO may not like no as an answer to the question “Will you review my employment contract?” In the long run, however, he would probably prefer to employ an in-house lawyer who has a keen understanding of ethical conflicts and can avoid these dilemmas not only for herself but also for her company. The best solution is to say simply, “No matter how much I may personally want to review the contract, I just can't help you here. I am the company's counsel. But I know a really great lawyer who will represent your interests wholeheartedly and without conflict.”¹⁴

The consequences of cutting corners on ethical conflicts are even more dire in other circumstances (for example, a potential disqualification from representing the company because of failure to disclose a conflict before obtaining confidential information from an employee). “No” is an uncomfortable message to give, but saying no is far better than ignoring the issues raised by the conflict.

When Lawyers Wear Two or More Hats

Our opening hypothetical had you being asked to serve as a member of the credit committee, not solely or principally in a legal capacity, but to participate in the evaluation of loans (a business function). Whether as members of credit committees or in other business or managerial functions, in-house attorneys increasingly serve in more than a legal capacity and are asked to do so because they possess skills that are well suited to management. Many general counsel have dual titles, serving also as director of human resources, chief administrative officer, or risk management officer. And many in-house attorneys serving in that dual capacity report

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- ACC, *Ethics*, web page, available on ACCA OnlineSM at www.acca.com/practice/ethics.php.
- *Attorney-Client Privilege*, an ACC InfoPAKSM, available on ACCA OnlineSM at www.acca.com/infopaks/attclient.html.
- Chad R. Brown, "In-house Counsel Responsibilities in the Post-Enron Environment," *ACCA Docket* 21, no. 5 (May 2003): 92–107, available on ACCA OnlineSM at www.acca.com/protected/pubs/docket/mj03/inhouse1.php.
- *Conflicts and Waivers*, an ACC InfoPAKSM, available on ACCA OnlineSM at www.acca.com/infopaks/conflict.html.
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- *In-house Counsel Ethics*, an ACC InfoPAKSM, available on ACCA OnlineSM at www.acca.com/infopaks/ethics.html.
- *Leading Practices in Codes of Business Conduct and Ethics*, available on ACCA OnlineSM at www.acca.com/protected/article/ethics/lead_ethics.pdf.
- John K. Villa, "How Will Recent Changes in Corporate Governance, Public Auditing, and the Role of In-house Counsel Affect You?" *ACCA Docket* 20, no. 9 (October 2002): 124–129, available on ACCA OnlineSM at www.acca.com/protected/pubs/docket/on02/ethics1.php.
- John K. Villa, "Waiving the Attorney-Client Privilege by Placing Advice of Counsel in Issue," *ACCA Docket* 21, no. 8 (September 2003): 102–106, available on ACCA OnlineSM at www.acca.com/protected/pubs/docket/so03/ethics.pdf.

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that the business role is the most satisfying one in which they have served.

But a host of conflicts present themselves the moment that an attorney becomes attorney plus. No ready answers or quick solutions exist, nor does any ethical rule directly address this issue. The comments to Model Rule of Professional Conduct 1.7 come the closest and address only the instance in which an attorney is serving as a member of the board of directors: the comments state that an attorney should not serve "if the dual role will compromise the lawyer's independence or legal judgment."¹⁵

If you do accept a dual role, you should be aware of the troublesome conflicts and challenges that come with the territory. You may have difficulty

deciding when you are serving as an attorney and when you are serving as a business person. The conflict inherent in being both a "team player" and providing objective legal advice can only be exacerbated in this setting.

To make matters worse, you're not the only one having difficulty sorting out when you are performing in which capacity: the client will probably be more confused than you are. Do you introduce yourself by saying, "Hello, I'm Sally Springer, and I'll be your chief administrative officer today" or "Hello, I'm Sally Springer, and I'll be your general counsel today," to properly inform your client which hat you are wearing? No matter what you do, there is bound to be more than one instance of

confusion and even potential disaster if your client, for example, discusses legal matters with you when you're wearing your business hat.

Courts recognize communications between in-house counsel and employees as protected by the attorney-client privilege when the communication is for the purpose of obtaining or providing legal advice.¹⁶ No privilege applies when the lawyer is giving business advice.¹⁷ Courts have set aside assertions of privilege in cases in which in-house counsel provided business advice, even if the attorney had no other corporate role.¹⁸

BY IDENTIFYING THE POTENTIAL PITFALLS OF SERVING IN A DUAL BUSINESS AND LEGAL CAPACITY, WE ARE NOT SUGGESTING THAT IN-HOUSE COUNSEL SHOULD AVOID BUSINESS ROLES OR GIVE UP ONES ALREADY ASSUMED.

In cases in which an in-house lawyer also serves in a titled business role, the privilege becomes even more problematic and subject to challenge. A court may be disinclined to uphold the privilege if the in-house lawyer is self-professedly serving in a business capacity.¹⁹

Not only is the privilege subject to challenge, but also there is a significant conflict not far below the surface of a dual legal/business role: you may find yourself in the position of giving yourself legal advice. As the adage goes, a lawyer who represents himself has a fool for a client. If you do find yourself in that position because the benefits outweigh the costs, make sure that someone else is giving you and others legal advice, especially on issues in which you have a personal stake.

For example, in defending a shareholder suit, can you defend or even investigate the alleged securities violations if you were involved in making the decisions forming the basis of the allegations or if you share fiduciary duties alleged to have been violated by senior management? Or if you sit on the investment committee of an employee fund that plummets in value, can you defend against claims of negligence or, worse, fraud when you had partici-

pated in the investment decisions? If you are the director of compliance, can you ensure compliance and at the same time defend noncompliance when a regulator investigates?²⁰ Or if you are an executive at a wholly owned subsidiary, to whom do you owe duties: your management team or your parent?

The problem becomes even more acute when the in-house lawyer also serves as a member of the board of directors, the governing body of a corporation. It is hard enough, for all of the reasons that we have described, for in-house counsel to tell management something that it may not want to hear.²¹ Imagine how much harder it is for in-house counsel to be both part of the governing board with all of the attendant liabilities and to be an advisor to that board, particularly when in-house counsel has to have a very difficult conversation with board members.²² Will the in-house counsel/board member be able to handle the conflicting roles and responsibilities?²³ Could anyone?

By identifying the potential pitfalls of serving in a dual business and legal capacity, we are not suggesting that in-house counsel should avoid business roles or give up ones already assumed. But before you step into a business role, make sure that it will not impair your ability to fully serve your client as a lawyer. Make sure that you have great outside counsel who fully understand you and your company and who can provide both a sanity check and independent legal advice when you feel that you are or might be compromised. Make sure that businesspeople know when you are giving them legal advice and when you are giving them your business judgment. If you serve in a dual capacity, you may have to clearly (but gracefully) announce in which capacity you are serving at the moment, in order to protect the privilege, among other things. And don't ever be afraid to admit that you may have a conflict. Better to err on the side of providing your client the best and sometimes hard legal advice than to be asked, "Where were the lawyers (read, "You") when . . . ?"²⁴

The Employee-Attorney Dilemma: Is There a Conflict?

A difficult source of ethical dilemmas facing in-house counsel is their status as both lawyer and employee. Should in-house counsel be afforded the same rights as other employees, or can the client,

based on the presumption that the client is entitled to counsel of choice, fire them at any time and for any reason? Will affording in-house counsel the same rights as other employees to such causes of action as wrongful termination result in relegating corporate counsel to second-class citizenship in the legal profession? Will our clients feel that they cannot trust us if they are worried about the possibility that we will sue the company for wrongful termination? What about claims for gender, race, or age discrimination? Will recognizing employment-related rights of in-house counsel lead inevitably to ethical violations, including disclosure of client confidences or violating the duty of loyalty to the client? Again, these questions have no easy answers.

IN REALITY, IT IS UNLIKELY THAT MANY CORPORATE COUNSEL, EVEN IN STATES IN WHICH THE CLAIM IS RECOGNIZED OR IN INSTANCES IN WHICH THE ATTORNEY IS PROTECTED BY THE PROVISIONS IN SARBANES-OXLEY, WILL EXERCISE THE RIGHT TO SUE FOR RETALIATORY DISCHARGE.

ACC has taken the position that in-house counsel should be treated like outside counsel and that the duty of loyalty to a client supersedes any employment-related right.²⁵ Furthermore, ACC has stated that, if in-house lawyers are treated differently from the way that their outside counterparts are treated, their prestige will suffer, and their clients will not take them seriously.²⁶

ACC's position stands in stark contrast to that of the California Supreme Court, which upheld, in *General Dynamics v. Superior Court*,²⁷ a cause of action for retaliatory discharge brought by a former in-house counsel. The court distinguished between in-house and outside lawyers:

Out of this duality of allegiance—for the interests of the client on the one hand, but within the bounds of ethical norms on the other—a genuine moral dilemma may arise. This is especially so in the context of the large commercially driven corporation whose essential objectives are largely defined by the desire to

maximize profitability Of course, the potential for such a dilemma is common to outside counsel as well. But unlike their in-house counterparts, outside lawyers enjoy a measure of professional distance and economic independence that usually serves to lessen the pressure to bend or ignore professional norms. Here again, the distinguishing feature of the in-house attorney is a virtually complete dependence on the good will and confidence of a single employer to provide livelihood and career success.²⁸

On this basis, the California Supreme Court found that in-house lawyers—divided between complying with ethical rules and their employers' questionable demands—needed judicial protection even more than their nonprofessional fellow employees.²⁹ Implicit in the court's decision is the notion that providing to an in-house attorney the right to claim for retaliatory discharge is central to the maintenance of professional independence. Other state courts, including courts in Illinois and Texas, have disagreed and refused to allow an in-house attorney's claim for retaliatory discharge on many of the same grounds articulated by ACC.

With the enactment of Sarbanes-Oxley, whistleblowing in-house lawyers (as well as other employees) in certain instances are afforded statutory protection. For example, § 806 (18 U.S.C. § 1514A) gives all employees, including attorneys, a cause of action against their publicly traded employer for a retaliatory employment action in which the employee has assisted a governmental investigation. Relief may include reinstatement, back pay, and attorney's fees. Also, § 1107 of Sarbanes-Oxley (18 U.S.C. § 1512) imposes potential criminal penalties on the retaliator.

In reality, it is unlikely that many corporate counsel, even in states in which the claim is recognized or in instances in which the attorney is protected by the provisions in Sarbanes-Oxley, will exercise the right to sue for retaliatory discharge. The effect on one's career of asserting such a claim against a former employer is likely to be enormous. In most instances, an in-house lawyer will successfully negotiate his or her way out of an irretrievably broken employment relationship. The fact that these cases are notable for their infrequent appearance does not, however, diminish the importance of the issue.

CONCLUSION

This article has presented just a few of the types of conflicts that an in-house lawyer may face not only the first day on the job, but also every day. There are few certain and definite answers for the multitude of ethical dilemmas and conflicts that arise from being an integrated member of a management team. The first step in any situation is to identify that a conflict exists, a task that requires sharp eyes and ears. The next step is to determine whether a rule applies to the conflict. If no specific rule applies and you're in a tough situation, carefully consider your course of action. Take advantage of your relationships with other in-house counsel and with outside lawyers whose integrity and practice you respect to help you formulate an approach to any particularly difficult situation. And remember that these potential conflicts and ethical dilemmas are some of the most difficult calls that any practicing lawyer can make. ■

NOTES

1. See, Donald C. Langevoort, "The Epistemology of Corporate-Securities Lawyering: *Beliefs, Biases, and Organizational Behavior*," 63 BROOKLYN L. REV. 629, 647 (1997), for a full and thoughtful exposition of the underlying psychology of lawyers' decision-making.
2. *Id.* at 651.
3. See, SEC v. National Student Marketing Corporation, et al., 360 F. Supp. 284, 1973 U.S. Dist. LEXIS 14371 (D.D.C. 1973). Here, the U.S. Securities and Exchange Commission brought charges against the outside lawyers, claiming that they had been conspirators in a securities fraud scheme because they had issued a comfort letter with respect to a merger, knowing that it was based on false financial information.
4. See, In the Matter of William Carter, Charles J. Johnson, Jr., 1981 SEC LEXIS 1940, 47 S.E.C. 471 (Feb. 28, 1981). Carter and Johnson were attorneys to National Telephone Company, which egregiously misrepresented its financial condition to shareholders and ultimately filed for bankruptcy. The SEC brought an action against the two lawyers, claiming that they had aided and abetted the securities fraud. An administrative law judge found against them, but the U.S. Securities and Exchange Commission reversed, calling it a "close question" because, although the lawyers had been intimately involved with and knew of the failures to disclose (and had in fact advised disclosure), there was not adequate proof of intent to assist a fraud. *Id.* at 507.
5. After the failure of Lincoln Savings & Loan, lawyers and law firms, including Kaye, Scholer and Jones, Day, paid more than \$125 million to the government and \$54 million to bondholders to resolve claims against them. H. Weinstein and M. Socarras, "Lincoln Savings and Loan: An Engine of Professional Responsibility." Paper presented at the 13th Annual Ray Garrett Jr. Corporate and Securities Law Institute, Apr. 29, 1993, and reprinted in 2 BANK LAWYER LIABILITY No. 2 (Apr. 30, 1993). Famously, District Court Judge Stanley Sporkin, presiding over the early Lincoln Savings litigation, asked: "Where were these professionals . . . when these clearly improper transactions were being consummated? Why didn't any of them speak up or disassociate themselves from these transactions? . . . What is difficult to understand is that with all the professional talent involved (both accounting and legal), why at least one professional would not have blown the whistle. . . ." Lincoln Savings & Loan Association v. Wall, 743 F. Supp. 901, 919-20, 1990 U.S. Dist. LEXIS 11178 (D.D.C. 1990).
6. See, In the Matter of Gutfreund, et al., 1992 SEC LEXIS 2939, 51 S.E.C. 93 (Dec. 3, 1992). Donald Feuerstein, the general counsel of Salomon, was informed of the submission of false treasury bids; he advised senior management that the behavior was criminal, but took no further action. The U.S. Securities and Exchange Commission stated that "[g]iven the role and influence within the firm of a person in a position such as Feuerstein's . . . such a person shares in the responsibility to take appropriate action to respond to the misconduct." *Id.* at 113.
7. New ABA Rule 1.6, adopted after extensive debate in August 2003, provides that a lawyer "may reveal information relating to the representation of a client . . . to prevent the client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's services [or] to prevent, mitigate or rectify substantial injury to the financial interests or property of another that is reasonably certain to result or has resulted from the client's commission of a crime or fraud in furtherance of which the client has used the lawyer's services . . ." New ABA Rule 1.13 allows, but does not require, an attorney to report *out* a violation of the law that is a violation of a legal obligation to the organization or may reasonably be imputed to the organization and is reasonably certain to result in substantial injury to the organization. This reporting out may occur only after the attorney has referred the matter to the highest in-house authority and that authority has failed to act and only if the lawyer reasonably believes that outside disclosure is necessary "to prevent substantial injury to the organization."

8. "It is the duty of an attorney . . . [t]o maintain inviolate the confidence, and at every peril to himself to preserve the secrets, of his or her client." CAL. BUS. & PROF. CODE § 6068(e) (West 2003).
9. Final Rule: Implementation of Standards of Professional Conduct for Attorneys, 17 C.F.R. § 205, available at www.sec.gov/rules/final/33-8185.htm at 33.
10. Proposed Rule: Implementation of Standards of Professional Conduct for Attorneys, 17 C.F.R. § 205 [Release Nos. 33-8150; 34-46868; IC-25829; File No. S7-45-02].
11. Final Rule at 42–43.
12. 17 C.F.R. § 205.3(b).
13. 17 C.F.R. § 205.6.
14. Outside lawyers are subject to similar "who is my client" issues and are also likely to stumble over the same conflicts. For example, one prominent lawyer recently was the subject of not so pleasant publicity about his role in advising former New York Stock Exchange ("NYSE") chief Richard Grasso to seek expedited payment of his \$139.5 million deferred compensation. The problem was that the lawyer was also the NYSE Board's chief counsel. *See*, Landon Thomas Jr., *Grasso's Motive for Payment Put in Doubt*, N.Y. TIMES, Nov. 6, 2003.
15. Model Rules of Professional Conduct, Comment 35 to Rule 1.7.
16. *See, e.g.*, *Upjohn Co. v. United States*, 449 U.S. 383 (1981), *Ames v. Black Entertainment Television*, 1998 U.S. Dist. LEXIS 18053, *20-22 (S.D.N.Y. 1998).
17. *See, e.g.*, *E.I. duPont de Nemours & Co. v. Forma-Pak, Inc.*, 351 Md. 396, 718 A.2d 1129, 1998 Md. LEXIS 813 (1998) (assertion of privilege denied where in-house counsel performing a business function.) *Also see, e.g.*, *Georgia Pacific v. GAF Roofing Mfg. Corp.*, 1996 U.S. Dist. LEXIS 671 (S.D.N.Y. Jan. 24, 1996) (court reaches surprising (and questionable) result of denial of privilege where communications concerned in-house attorney's advice about negotiation of contractual provisions; finds that, because attorney was "acting in a business capacity," no privilege applied). *Id.* at *6 and *12.
18. *E.I. duPont*, 351 Md. at 420–422; *Georgia Pacific*, 1996 U.S. Dist. LEXIS 671 at *9 (day-to-day involvement of in-house lawyer in business of company "may blur the line between legal and nonlegal communications").
19. *See, e.g.*, *TVT Records et al. v. The Island Def Jam Music Group et al.*, 214 F.R.D. 143, 2003 Dist. LEXIS 3061 (S.D.N.Y. 2003) (based on job titles, where employees are not only lawyers but also high-ranking management employees, the privilege does not apply) *id.* at 145; *Borase v. M/A Com*, 171 F.R.D. 10, 1997 U.S. Dist. LEXIS 4773 (D. Mass. 1997) (where general counsel had other management responsibilities, "assumption cannot be made" that he was acting in the capacity of an attorney providing legal advice, and privilege held not to apply). *Id.* at 15.
20. This situation was the one that the ex-general counsel of Tenet Healthcare found herself in. Senator Charles Grassley (R. Iowa) criticized her for serving as both general counsel and chief compliance officer, "calling it a conflict of interest to ensure compliance while defending non-compliance" with a Medicare fraud settlement reached in 1994. Sue Reisinger, *Some Cheer Tenet General Counsel's Departure*, NAT'L L. J., vol. 26, no. 7, Oct. 13, 2003, at 9–10.
21. The then-general counsel of Allied Chemical, Brian Forrow, framed the question in this way: "Is the hallmark of a lawyer—independent judgment—blurred because the lawyer serves as inside counsel? Or is inside counsel better able to bring independent judgment to a corporation's problems, even perhaps to go beyond the law to activate the corporate conscience? Stated another way, is corporate or outside counsel more likely to have the independence to tell senior management or the board of directors what they may not want to hear?" Brian D. Forrow, *The Corporate Law Department Lawyer, Counsel to the Entity*, 34 BUS. LAW 1797 (1979).
22. The Comments to Model Rule of Professional Conduct 1.7 specifically note that, "[i]f there is material risk that the dual role will compromise the lawyer's independence of professional judgment, the lawyer should not serve as a director or should cease to act as the corporation's lawyer when conflicts of interest arise."
23. Professor Geoffrey Hazard has warned that "a lawyer who must give detached legal advice and at the same time be mindful of his or her own potential liability as a corporate officer-holder cannot blink at the possibility that the quality of the representation may suffer." GEOFFREY C. HAZARD JR. AND W. WILLIAM HODES, *THE LAW OF LAWYERING: A HANDBOOK ON THE MODEL RULES OF PROFESSIONAL CONDUCT*, 3d ed. (Aspen Publishers 2001), 1.13:110, at 402.
24. For a very thoughtful analysis of the difficulties of navigating these shoals, *see*, Sally R. Weaver, *The Randolph W. Throver Symposium: The Role of the General Counsel: Perspective: Ethical Dilemmas of Corporate Counsel: A Structural and Contextual Analysis*, 46 EMORY L.J. 1023 (1997).
25. *See*, *Amicus Brief of American Corporate Counsel Association in Santa Clara County Counsel Attorneys Ass'n v. Woodside*, SO31593, 7 Cal. 4th 525, 28 Cal. Rptr. 2d 617, 869 P.2d 1142, 1994 Cal. LEXIS 1215 (1994), *reh'g denied*, 1994 Cal. LEXIS 2768 (Cal. May 19, 1994). *Amicus brief available on ACCA OnlineSM at www.acca.com/public/amicus/santaclara/pdf.*
26. *Id.*
27. *General Dynamics v. Superior Court*, 7 Cal. 4th 1164, 32 Cal. Rptr. 2d 1, 87 P.2d 487, 1994 Cal. LEXIS 3522 (1994).
28. *Id.* at 1182.
29. *Id.*

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Conflicts and Waivers



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The purpose of this InfoPAKSM is to assist corporate counsel in understanding and making decisions about conflicts and waivers. Included is an overview of the rules relating to the three principal kinds of conflict of interest that result in conflicts waiver requests, as well as a discussion of the issues corporate counsel should consider when reviewing a request for a conflicts waiver. It should not be construed as legal advice or legal opinion on specific facts, or representative of the views of ACC or any of its lawyers, unless so stated. This is not intended as a definitive statement on the subject but a tool, providing practical information for the reader.

This information has been produced by

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at the direction of the Association of Corporate Counsel

Conflicts and Waivers

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I. Introduction

You are sitting in your office catching up on correspondence when you see The Letter. Perhaps it was preceded by a telephone or in-person conversation, but perhaps not. Perhaps it is a small part of a lengthy engagement letter, or perhaps it is a freestanding document. In any event, The Letter informs you that the outside firm you just hired wants something from you – a conflict waiver, or stated alternatively, a limitation on the traditional lawyer-to-client duty of undivided loyalty.

What are the basic conflict-of-interest rules? Should you agree? Should you bargain over the scope of the requested waiver? Will the requested waiver be enforceable? Just who do these lawyers think they are and why are they doing this to you? And what risks do you run if you say “yes”? The purpose of this electronic “paper” is to provide some background information and some rules of the road for this evolving but essential corner of legal practice. Although there is no one right or wrong answer for all companies in all circumstances, there are better or less well-informed decisions.

Section II provides an overview of the rules relating to the three principal kinds of conflict of interest that result in conflicts waiver requests—current-client conflicts, former-client conflicts, and personal or business conflicts. Section III discusses problems and opportunities caused by lateral law firm hires and the potential availability of screens in some jurisdictions. Section IV discusses conflicts waivers from the outside law firm’s point of view. Finally, Section V discusses the issues that corporate counsel typically do or, in our opinion, should generally consider when reviewing a request for a conflicts waiver.

Our goal is to assist corporate counsel in understanding and making decisions about conflicts waivers. If you have any questions or suggestions about how to make this paper better or more useful, please let us know. We hope that this document will evolve over time.

This InfoPAK contains citations to the American Bar Association Rules of Professional Conduct (the “RPCs”), to the Restatement (Third) of the Law Governing Lawyers (2000) (“Restatement”), and to selected cases and ethics opinions. No attempt is made, however, to provide a detailed look at the conflicts rules of all jurisdictions. For your convenience, copies of the RPCs cited in this paper are contained in the Appendix hereto.

II. The Basic Conflicts Rules

A. Attorneys as Fiduciaries

The relationship between client and attorney is a fiduciary relationship, and the duty of loyalty is at the heart of that relationship. Lawyers generally owe their clients a duty of “undivided loyalty.” Restatement § 121 cmt. b. To borrow from another time and another context, this duty requires more of lawyers than “morals of the marketplace.” *Meinhard v. Salmon*, 248 N.Y. 458, 464, 163 N.E. 548 (1928) (Cardozo, J.).

The principal purpose of formal conflict-of-interest rules such as the RPCs is to codify those aspects of the duty of loyalty whose violation can lead to attorney discipline. Moreover, it is difficult for attorneys to defend against breach-of-fiduciary claims when the conflicts rules have been violated. *See, e.g.*, Restatement §§ 49, 52; *Maritrons G.P., Inc. v. Perm Hamilton & Scheetz*, 602 A.2d 1277 (Pa. 1992). In addition, an increasing body of case law supports the view that attorneys who violate the conflicts rules may not only be prohibited from collecting their fees but may also have to disgorge fees already received. *See, e.g.*, Restatement § 37 (referencing a multi-factor test); *Burrow v. Arce*, 997 S.W.2d 229 (Tex. 1999) (same); *Kidney Ass’n of Or. v. Ferguson*, 843 P.2d 442 (Or. 1992) (same).

Although the conflicts rules are not identical in all American jurisdictions, they are similar in many respects. A fair one-sentence overview is provided in Restatement § 121:

A conflict of interest is involved if there is a substantial risk that the lawyer’s representation of [a] client would be materially and adversely affected by the lawyer’s own interests or by the lawyer’s duties to another current client, a former client, or a third person.

B. Current-Client Conflict

1. Simultaneous Adverse Relationships Are Generally Prohibited.

The core of the current-client conflicts rules can be simply stated: except as noted below, American lawyers and law firms may not represent one current client adversely to another current client on any matter unless, at a minimum, both clients consent to the conflict after full disclosure. *See, e.g.*, RPC 1.7; Restatement §§ 121-22, 128-31. In other words, current clients generally have veto power that allows them to prevent their current counsel from opposing them on any matter, whether it is related or unrelated to the work that is being done for that client. However, this veto power may be substantially limited if not eliminated if the client agrees to sign a prospective conflicts waiver, which purports to waive all future conflicts between a client and another potential or existing client. A potential conflicts waiver may negate the need to obtain an additional waiver once a situation between the identified parties ripens into an actual claim. *Visa U.S.A., Inc. v. First Data Corp.*, 241 F.Supp.2d 1100, 2003 WL 194490 (N.D.Cal.2003) (enforcing a fairly detailed future conflicts waiver signed by sophisticated client that consulted counsel before signing).

To the authors’ knowledge, the only other American exception to the general rule that lawyers and law firms may not represent one current client adverse to another current client in Texas. Pursuant

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to Texas RPC 1.06, a Texas lawyer may ethically represent one current client adversely to another current client without disclosure to or consent from either client if the matters are unrelated. Of course, this does not mean that the clients must accept such a dual relationship; the client is free, even in Texas, to terminate an attorney-client relationship at any time and for any reason. Tex. RPC 1.15. The effect of this Texas rule may also be limited if the work that a Texas lawyer is doing for one or both clients involves other jurisdictions. For example, a Texas firm that wanted to represent Current Client A adversely to Current Client B in litigation in State X would likely find that the State X conflicts rules applied to State X litigation and that out-of-state Texas lawyers who were appearing pro hac vice were therefore disqualified. The same would be true, of course, if the Texas firm appeared in the litigation through local members of its State X office.

Other countries may have other rules. Whether, or to what extent, American conflicts rules will apply to the multinational conflicts of multinational law firms remains to be seen.

2. *The Prohibition Generally Applies to Entire Firm*

The reference above to the disqualification of “lawyers and law firms” is, of course, intentional. Pursuant to what is sometimes called the “firm unit rule,” all lawyers presently at a firm are typically disqualified due to a current-client conflict if any lawyer is disqualified as the conflict of one attorney in a firm is generally imputed to all attorneys associated with the firm. *See, e.g.*, RPC 1.10(a); Restatement § 123. This includes not only partners and associates but also “of counsel” attorneys and even some contract attorneys who have regular relationships with particular firms. Restatement § 123 cmt. c(ii); ABA Formal Op. 00-420 (“of counsel” lawyers are not temporary lawyers but are part of firm); ABA Formal Op. 94-388; *Cinema 5, Ltd. v. Cinerama, Inc.*, 528 F.2d 1384 (2d Cir. 1976). On the other hand, an imputed conflict leading to the disqualification of one law firm may not require the disqualification of separate law firm serving as co-counsel on a matter so long as there is only a small actual risk of confidential client information spreading from the primarily conflicted law firm to the second firm. *Baybrook Homes, Inc. v. Banyan Construction & Development, Inc.* 991 F.Supp.1440 (M.D.Fla.1997); *First Small Business Inv. Co. of California v. Intercapital Corp. of Oregon*, 108 Wash.2d 324, 738 P.2d 263 (1987).

The only exception to the firm unit rule as applied to current-client conflicts exists in the context of lawyers who change jobs. In some jurisdictions, “screens” or “ethical walls” allow firms to avoid disqualification if, but only if, the conflict is a result of work done by a laterally hired lawyer before he or she joined his or her present firm. This subject is addressed further in Section III below.

3. *The “Hot-Potato” Rule*

The former-client conflicts rules are more generous to law firms than the current-client conflicts rules. This makes sense: the duty of undivided loyalty that lawyers owe to current clients should be broader than the duty owed to former clients.

On any number of occasions, law firms have attempted to fire current clients in the middle of handling a matter in an attempt to turn those clients into former clients for conflicts purposes. These attempts, which generally do and should fail, have given rise to what is called the “hot-potato” rule: a firm cannot drop a client like a hot potato simply because a more desirable client comes along. *See, e.g.*, Restatement § 132, Reporter’s notes to cmt. c; *In re Rite Aid Corp. Sec. Litig.*, 139 F. Supp. 2d 649, 658 n.15 (E.D. Pa. 2001); *Universal City Studios, Inc. v. Reimerdes*, 98 F Supp 2d 449, 452 (S.D.N.Y. 2000). This rule applies also when the conflict is a result of a merger of two previously independent law firms. *See, e.g.*, *Picker Int’l, Inc. v. Varian Assocs.*, 869 F.2d 578,

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581 (Fed. Cir. 1989). In fact, conflicts waivers are required once law firm merger negotiations reach an advanced stage. ABA Formal Op. 96-400.

The hot-potato rule has two potential exceptions and one limitation. One potential exception applies when a conflict is not a result of anything that a lawyer or firm may have done. Suppose, for example, that Adverse Party A in Matter A acquired a firm's client in Matter B and then sought to use that new client relationship to disqualify the firm from Matter A. Some courts, at least, will allow the firm to withdraw from either Matter A or Matter B (but not keep both) rather than giving the adverse party/acquiring company the right of control. *See, e.g.,* Restatement § 132 cmt. j; *Ex parte AmSouth Bank*, 589 So. 2d 715 (Ala. 1991).

The second possible exception is that lawyers with a clear primary client and an equally clear secondary or accommodation client may sometimes be allowed to fire the accommodation client and continue with the primary client. *See, e.g.,* Restatement § 132 cmt. i; *In re Rite Aid Corp. Sec. Litig.*, 139 F. Supp. 2d at 659-60. As a practical matter, however, the accommodation client is unlikely to be a business entity. It is more likely to be, say, a middle-level manager whose business entity-employer has allowed its counsel to defend the manager as well as the entity in a case in which both were accused of wrongdoing. In such circumstances, the business entity would also be very well advised not to rely solely on the accommodation client theory but to seek a formal conflicts waiver from the middle-level manager as well. *Cf. Home Care Indus. v. Murray*, 154 F. Supp. 2d 861 (D. N.J. 2001); *Universal City Studios*, 98 F. Supp. 2d at 453.

The limitation is that the hot-potato rule applies only to current-client relationships. If a client is already a former client at the time that the firm takes on an adverse matter, the hot-potato rule does not apply. Whether a client is a current or former client depends, *inter alia*, upon the client's subjective belief in or the reasonableness of that belief under the circumstances. *See, e.g., Oxford Systems, Inc. v. CellPro, Inc.*, 45 F. Supp. 2d 1055 (W.D. Wash. 1999). For the cases discussing the often difficult dividing line between current and former clients, see also Restatement § 14 and sources cited therein.

4. Some Current-Client Conflicts Cannot Be Waived

There are some conflicts between current clients that the law regards as so severe that they cannot be waived. Thus RPC 1.7(a)(2) prohibits simultaneous representation if "there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client... ." Similarly, RPC 1.7(b)(1) prohibits simultaneous representation if the lawyer cannot "reasonably believe[] that the lawyer will be able to provide competent and diligent representation to each affected client." *See also* Restatement § 122(2)(c) (simultaneous representation prohibited if, *inter alia*, "it is not reasonably likely that the lawyer will be able to provide adequate representation to one or more of the clients").

The nonwaivable-conflicts rules are not written or interpreted the same way in all jurisdictions. In some jurisdictions, for example, a lawyer or law firm cannot ethically represent both a buyer and a seller in a real estate transaction even if both clients consent after full disclosure. *See, e.g., In re Johnson*, 707 P.2d 573 (Or. 1985). In others, a lawyer can do so if, and only if, the transaction is not too complex. *See, e.g., Baldasarre v. Butler*, 625 A.2d 458 (N.J. 1993). In still others, such representations may be permissible if competent clients agree, if the differences between them are not too sharp, and if the work will not require extensive advice to the clients. *See* Restatement § 122 illus. 10, 11; *see also* Cal. RPC 3-310 (broadly allowing such representations upon informed

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written consent). Although some states have disciplinary decisions or ethics opinions on this subject, there is presently no general and universal agreement among American lawyers about how this set of lines should be drawn. *See, e.g.*, Peter R. Jarvis & Bradley F. Tellam, “Conflicts About Conflicts,” *Prof. Law.* 22, 23 (May 1996).

The buyer-seller, lender-borrower, or landlord-tenant kind of dichotomy presents fixed-sum games in which “more” for one client typically means “less” for the other. Suppose, however, that several current or would-be clients simultaneously ask a single lawyer or law firm to represent all of them in putting together a corporation or other business entity through which they will do business together. In this type of situation, the adversity that is present in a straight buy-sell situation may as a practical matter be reduced, if not overcome, by the joint interests that the would-be incorporators or partners will have in putting together a profitable business. It should come as no surprise, therefore, that the general answer to the question of whether a single lawyer or law firm may represent multiple would-be incorporators or partners is “yes, qualified.” If the interests are wholly consistent, simultaneous representation may in fact be permissible even without a formal conflicts waiver. If the interests of the proposed multiple clients are too adverse, a single lawyer or firm cannot represent them all even if all consent. And in all situations in between (which, in our view, is about all of them), simultaneous representation is permitted only on the basis of informed consent from all the clients. Comment 12 to RPC 1.7 puts the matter as follows:

For example, a lawyer may not represent multiple parties to a negotiation whose interests are fundamentally antagonistic to each other, but common representation is permissible where the clients are generally aligned in interest even though there is some difference of interest among them.

5. *Intermediation Is Not a Free Pass*

Although the latest version of the ABA Model Rules no longer includes a separate rule on intermediation and instead addresses that subject in a revised Model Rule 1.7 (quoted in full in the appendix hereto), the former RPC 2.2 is still in force in many states. By its terms, it allows a lawyer to act as an “intermediary” for multiple parties in ways that may seem at first to some lawyers to allow greater flexibility than the current-client conflicts limitations in RPC 1.7. In our opinion, however, there is less wiggle room here than meets the eye. By its terms, RPC 2.2 does not apply unless, *inter alia*, the lawyer-intermediary “reasonably believes that the matter can be resolved on terms compatible with the clients’ best interests” and that “the common representation can be undertaken impartially and without improper effect on other responsibilities the lawyer has to any of the clients.” For the most part, the circumstances in which the normal current-client conflicts rules such as RPC 1.7 do not allow a waiver will likely parallel those in which intermediation is not allowed under RPC 2.2. *See, e.g.*, D.C. Eth. Op. 243 (1993) (lawyers can neither represent both parties to divorce pursuant to RPC 1.7 nor intermediate divorce for both parties pursuant to RPC 2.2); *see also Furia v. Helm*, 111 Cal.App.4th 945, 4 Cal.Rptr.3d 357 (2003) (court questioned but did not decide whether an attorney for one party to a dispute may act as a neutral mediator in the dispute).

6. *Corporate Families*

Does a firm’s representation of one member of a corporate family constitute representation of all related or affiliated corporations or entities? The answer is “it depends.” *See, e.g.*, ABA Formal Op.

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95-390, Cal. Eth. Op. 1989-113, 1989 WL 253261. The deciding factors are such issues as whether the entities operate as one or different businesses, whether the entities share counsel, whether they have a unity of interests in the representation at issue and the like. . See, e.g., *Certain Underwriter's at Lloyds of London v. Argonaut Ins. Co.*, 264 F.Supp.2d 914 (N.D.Cal.2003).

7. Conclusion: Current Clients Generally Have Veto Power

As is noted in the first paragraph of this subsection, the general rule of current-client conflicts is that current clients typically have veto power. If they do not wish to allow “their” lawyers to oppose them on any matter, their lawyers cannot do so.

C. The Former-Client Conflicts Rules.

1. Former Clients Have More Limited Powers

Former clients also have veto power, but it is limited to two situations. In addition, former clients can always waive conflicts. See generally RPC 1.9; Restatement § 132. The two types of situations in which former-client conflicts waivers are required have sometimes been referred to as “matter-specific” and “information-specific.” See, e.g., Or. Eth. Op. Nos. 1991-11, 1991 WL 279152; 1991-17, 1991 WL 279158. In many cases, matter-specific and information-specific conflicts will both be present. In many other cases, neither one will be. The point for present purposes is only that the presence of either one requires a conflicts waiver from both the former client and the current client before a lawyer or law firm can proceed.

2. Matter-Specific Conflicts

A matter-specific conflict exists, and a conflicts waiver is required, if the transaction or litigation that a lawyer or law firm proposes to handle adversely to a former client is the same as or sufficiently related to the transaction or litigation that the lawyer previously handled for that client. For example, a lawyer who represents the seller in a real property transaction cannot subsequently represent the buyer in litigation against the seller relating to that contract even if it could be shown that the lawyer learned no pertinent confidences or secrets from the seller at the time of the former representation. See, e.g., *Collatt v. Collatt*, 782 P.2d 456 (Or. Ct. App. 1989).

Not surprisingly, there is some dispute in the case law concerning how closely two matters must be related before a conflicts waiver is required. See, e.g., *Portland Gen. Elec. Co. v. Duncan, Weinberg, Miller & Pembroke, P.C.*, 986 P.2d 35 (Or. Ct. App. 1999); *Am. Heritage Agency v. Gelinas*, 774 A.2d 220 (Conn. App. Ct. 2001). For other cases on this subject, see Restatement § 132.

3. Information-Specific Conflicts

An information-specific former-client conflict exists if, during the course of work on a prior matter, a lawyer or firm learned confidential client information that could be used adversely to the former client in the present matter. See, e.g., *In re Brandsness*, 702 P.2d 1098 (Or. 1985) (identifying information-specific category); *Jessen v. Hartford Casualty Insurance Co.*, 111 Cal.App.4th 698, 3 Cal.Rptr.3d 877 (2003) (court applied the “substantial relationship” test to determine if information material to the evaluation, prosecution, settlement, or accomplishment of the prior representation was also material to the evaluation, prosecution, settlement, or accomplishment of the current representation for purposes of determining whether insured's lawyer must be disqualified

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because he was previously an associate in a law firm that frequently represented the opposing party); Or. Eth. Op. No. 1991-17, 1991 WL 279158 (giving examples). Not surprisingly, there is also disagreement within the case law on this issue regarding how clear the proof must be.

4. The Firm Unit Rule Applies to Former-Client Conflicts

There is no general distinction between current- and former-client conflicts when it comes to the firm unit rule. The need to disqualify a single lawyer will result in the need to disqualify an entire firm. *See, e.g.*, RPC 1.9, 1.10(a); Restatement §§ 123, 132. In some cases, however, ethical screens or walls may help a firm avoid disqualification due to a former-client conflict of a laterally hired lawyer. Disqualification may also be avoided if all attorneys who have worked on the matter giving rise to the former-client conflict have left the firm. These points are discussed in Section III below.

5. Conclusion: Former Clients Are Not Without Potential Recourse

Even when a company must concede that it is a former and not a current client of a law firm, this does not mean that it is powerless to prevent that law firm from acting adversely to it. In at least some circumstances, for example, a careful review of the confidential client information communicated to the former law firm may permit the company to argue that that information could be used adversely to the company in the present matter and that the law firm must therefore be disqualified. *See, for example*, the cases and authorities cited in the two prior sections.

In other circumstances, the relationship between the present and former matters may be enough. However, at least some courts have held that disqualification may not be available even in a matter-specific context if the law firm can prove that it did not acquire any pertinent client confidences and secrets. *See, e.g., Christensen v. United States Dist. Court*, 844 F.2d 694 (9th Cir. 1988). Interestingly enough, this does not necessarily mean that the lawyers in that firm are not subject to discipline for proceeding in such circumstances even if they are not disqualified.

D. Personal or Business Conflicts

The duty of loyalty can be violated not only by conflicting obligations owed to multiple current or former clients but also by conflicts between a single client's interests and the lawyer's own personal or business interests. In some jurisdictions, all or nearly all such conflicts would appear to be waivable. In others, some conflicts of this type cannot be waived. These conflicts are generally dealt with in RPC 1.7(b) and RPC 1.8; *see also* Restatement §§ 125-27.

1. Stock or Warrants for Fees; Doing Business with Clients

Suppose, for example, that a corporate client wishes to compensate a lawyer through the issuance of stock to the lawyer. Subject to the applicable limitations on excessive or unreasonable fees, such an alternative payment relationship is generally permissible as long as the deal is fair and the lawyer provides a sufficient explanation of the pros and cons. RPC 1.8(a); *see also* ABA Formal Op. 00-418; Restatement § 126.

The same general standards apply to other forms of doing business with clients.

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2. *Lawyers on Client Boards*

Personal or business conflicts can also arise when a lawyer or member of a lawyer's firm also occupies a position on a client's board of directors. In this type of situation, the conflict arises because the lawyer's or firm's duties as lawyers may conflict with the individual lawyer-director's duties as director. Once again, such conflicts are likely to be waivable after full disclosure. *See, e.g.*, ABA Formal Op. 98-410.

3. *Other Personal Conflicts*

This is not an exhaustive list of personal or business conflicts. For example, personal conflicts can also occur when married or otherwise related lawyers are on both sides of a matter, when the lawyer is to be paid by someone other than the client, or when aggregate settlements are negotiated. *See generally* RPC 1.8. As a practical matter, however, these kinds of conflicts will not generally give rise to waiver requests that come before corporate counsel.

E. A Conflicts Rules Postscript

Four points are worth noting.

1. *Fiduciary Duties May Go Beyond Ethical Obligations*

First, the conflicts rules do not necessarily provide the full measure of a lawyer's duties to a client. A lawyer or firm could conceivably be held civilly liable for breach of fiduciary duty even though a violation of the formal ethical rules may not be present. Conversely, there are also times when a lawyer will be subject to discipline even though the client would have no private cause of action. *Cf. Owens v. McDermott, Will & Emery*, 736 N.E.2d 145 (Ill. App. Ct. 2000). Corporate counsel may therefore wish to keep an eye on more than just what the formal conflicts rules provide.

2. *Be Careful About Disciplinary Threats*

Although the RPCs as such no longer contain a specific "threatening prosecution" rule equivalent to former DR 7-105, extortion is still prohibited. In some jurisdictions, a threat to file a bar complaint may violate either the general law against extortion or a surviving variant of the "threatening prosecution" rule. *See, e.g.*, RCW 9A.56.110 ("Extortion means knowingly to obtain or attempt to obtain by threat property or services of the owner . . ."); Cal. RPC 5-100.

3. *There Are Other Types of Conflicts*

The discussion above is not an exclusive list of all types of conflicts or problems that can affect corporate representatives. Three others are briefly noted below.

a. *Joint-Defense Conflicts*

On a sheer numbers basis, the incidence of joint-defense conflicts waiver problems is far less than the incidence of current-client, former-client, and personal or business conflict problems. Nevertheless, the issue is important enough to deserve separate mention, because it can provide a trap for the unwary that ought to be considered as part of an overall conflicts waiver process.

Suppose that two unrelated corporations are named as defendants in litigation and that they decide to be separately represented but to share privileged information on the basis of a joint-defense

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agreement. Suppose that a great deal of information is shared on this basis but that the interests of the two corporations subsequently diverge. Can the lawyers for each of the corporate clients continue to represent “their” client even though they now have information subject to the joint-defense privilege? The answer is “perhaps not.” See, e.g., ABA Formal Op. 95-395; *City of Kalamazoo v. Mich. Disposal Serv.*, 151 F. Supp. 2d 913 (W.D. Mich. 2001); *United States v. Anderson*, 790 F. Supp. 231 (W.D. Wash. 1992). Clients who enter into joint-defense agreements should consider whether, for example, they want to include a provision that allows each party to the agreement to continue to be represented by its counsel in the event of a breakup. At least one court has found that joint defense agreements can be implied from the sharing of confidential information and the disclosure made under the implied joint defense agreement could become the basis to disqualify one of the attorneys who participated in the joint defense. *In re Skiles*, 102 S.W.3d 323 (Tex.App.2003). *But cf. United States v. Stepney*, 246 F. Supp. 2d 1069, 1079-80 (N.D. Cal. 2003) (“Joint defense agreements...cannot extend greater protections than the legal privileges on which they rest.”).

b. Issue Conflicts.

So-called issue or positional conflicts are a sort of hybrid between personal conflicts and multiple-client conflicts. They arise when a single legal issue is present in two cases that a firm is handling in which the outcome of one of the cases is likely to adversely affect the outcome in the other. See, e.g., ABA Formal Op. 93-377; Restatement § 128 cmt. f. There is little actual law here, and thus it is not entirely clear whether or to what extent “hardcore” and obvious issue conflicts are waivable. *Cf. Or. DR 5-105(A)(3)* (expressly making all issue conflicts waivable); ABA Formal Op. 93-377 (dual representation prohibited if there is substantial risk that decision in favor of one client in one case will materially undercut other client’s position in other case).

A clarification may also be appropriate. An issue conflict is not present merely because a law firm may, on behalf of one client, advance legal positions that another client may, in the abstract, dislike. On the other hand, law firms that advance legal positions on behalf of one client that are very much to the dislike of other clients may find themselves in a personal or business conflict situation pursuant to RPC 1.7(a) or equivalent rules.

c. Attorney-Witness Conflicts

Corporate counsel who are hiring a firm to represent them in litigation may wish to consider whether there is any attorney at the firm they are hiring who may need to be a witness in the case. This is an issue on which the rules from state to state are not uniform. Some states allow lawyer A at a firm to try a case in which lawyer B will be a witness on behalf of the firm’s client as long as lawyer B does not participate in the trial. See RPC 3.7. Even in these states, however, it generally is the case that a firm must withdraw if a lawyer has testimony to give that is adverse to the firm’s client.

In other jurisdictions, a lawyer at a firm generally may not try a case even when the other lawyer’s testimony is favorable to the firm’s client. See, e.g., Wash. RPC 3.7 (significantly different than ABA RPC 3.7).

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4. *Circumstances Change*

Finally, and because the nature or degree of a conflict of interest may change over time as circumstances or client interests may change, conflicts waivers will sometimes need to be repeated or renewed. It is also possible that what was once a waivable situation will become one in which the conflict cannot be waived. *See, e.g., In re Johnson*, 707 P.2d 573; *cf.* Restatement § 121 cmt. 9; N.Y.C.L.A. Op. 724, 1998 WL 39561. Both corporate counsel and outside counsel must therefore remain alert as events unfold.

III. Ethical Screens and Walls

The subject matter of this heading is what used to be called “Chinese walls” and is now typically called “ethical screens” or “ethical walls.”

Suppose that a law firm wishes to recruit a government lawyer but that government lawyer is then working for the government adversely to the law firm’s corporate client. In most if not all American jurisdictions, the law firm can hire the government lawyer and even make him or her a partner without disqualification, as long as he or she is appropriately screened from any involvement in the matter. *See, e.g.*, RPC 1.11.

In some American jurisdictions, there are also black-letter rules that allow screening when a lawyer moves from one private place of employment to another. *See, e.g.*, Wash. RPC 1.10(b); Or. DR 5-105(H), (I); Pa. RPC 1.10(b). In addition, some other states may allow screening for private-lawyer moves by case law. *See, e.g.*, *Clinard v. Blackwood*, 46 S.W. 3d 177 (Tenn. 2001). Others, however, do not.

When, on the other hand, all lawyers at a firm who have worked on a matter or acquired confidences and secrets about a matter have left the firm, screening is unnecessary and the lawyers remaining at the firm will not be disqualified. *See, e.g.*, RPC 1.10(b); Restatement § 124.

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IV. What Outside Counsel Think About Waivers

This section reviews some of the thought processes of lawyers and law firms when they ask current, former, or prospective clients for conflicts waivers. We believe that if corporate counsel are better informed about the thought processes of their outside lawyers, they may be better able to respond effectively to the positions taken by those lawyers.

Of course, the principal motivator behind most law firm conflicts waiver requests, like the principal motivator behind most corporate behavior, is the profit motive. On the other hand, lawyers do not think solely, or necessarily logically, about short- or long-term profit maximization per se any more than businesses do. In addition, law firms, like many other organizations, have their bureaucratic sides. The result is that the typical law firm approach to conflicts waivers is a combination of perceived self-interested business judgment, legitimate concern for client welfare, attorney disciplinary rules, other perceived rules of thumb, and the all-too-human tendency on some occasions to act without thinking things all the way through.

To begin with, lawyers who request conflicts waivers typically do not view the making of those requests as acts of disloyalty, and they typically believe as well that in the circumstances in which they are asking for waivers, their clients will not be unduly prejudiced and may in fact be benefited by saying “yes.”

Consider, for example, the following more or less standard unrelated-matter current-client conflicts waiver: Mega-Law Firm Tax Partner does tax work for Tax Client. Potential Litigation Client now wishes to be defended by Mega-Law Firm Litigation Partner in wholly unrelated litigation brought by Tax Client against Potential Litigation Client through other counsel. When Tax Partner and Litigation Partner decide to seek conflicts waivers from their respective clients, they will probably note the lack of factual and legal relationship between the tax and litigation matters as well as the different lawyers handling the two matters as reasons to believe that Mega-Law Firm will be able zealously to represent both clients in their respective matters without any undue harm or prejudice to either one. They may also think that this is clearly a case of “no harm, no foul” since if Mega-Law Firm is not allowed to represent Litigation Client, that company will simply hire other counsel who will handle the matter roughly as well as Mega-Law Firm would have handled it.

In fact, Tax Partner and Litigation Partner may take their thought process further and come to the conclusion that Tax Client really brought this problem on itself by not using Mega-Law Firm for all of its work. They may also believe that Tax Client is lucky to have access to highly skilled Tax Partner at all, given that Tax Client’s lack of loyalty to the firm is clear from its division of work. Finally, and depending upon the size of the various matters, they may conclude that if they cannot get consent to represent Potential Litigation Client, they will have to stop representing Tax Client as soon as the hot-potato rule allows. In part, this is a kind of “live and let live” approach: since clients want to split their work, they should allow their lawyers to do so as well.

Suppose, however, that there is a clear relationship between the work that a lawyer wishes to do for and against a client. Suppose, for example, that Mega-Firm Corporate Partner sees an opportunity to represent Buyer and Seller in a jurisdiction that allows such representations or to represent Joint Venturer A and Joint Venturer B in the formation and operation of Joint Venture under circumstances in which the conflict can be waived. In this case, the thought process will likely start with the sophistication of the clients and their ability to decide key deal and legal points for themselves, especially if they have corporate in-house counsel to assist them. Corporate Partner

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may then consider that it is the clients, and not Corporate Partner, who have asked for this joint relationship and that their reasons for doing so are to save legal costs while getting the deal done quickly. Whether correctly or incorrectly, Corporate Partner may also conclude that he or she is uniquely qualified to make his or her way through this particular transactional minefield while keeping everyone reasonably happy. Finally, Corporate Partner may conclude that if matters appear to be falling apart as work on the transaction continues, the parties can always retain new or additional counsel at that time.

These examples all involve specific matters for which a conflicts waiver is necessary at a particular point in time. The process may not be all that different, however, when a firm asks at the outset of its representation of a client for a blanket waiver of all conflicts on all unrelated matters. In this case, the firm may also believe that its has unique prestige or skills that it will not be able to maintain at the very highest skill levels if it cannot get most or all of the clients it wishes to have. Firms in this kind of situation may also feel that the rule of undivided loyalty is an unnecessarily and overly broad rule that is simply unworkable as applied to modern life.

We do not mean to suggest that most law firms give no little or no thought to the possible effects on their clients of seeking a conflicts waiver. In fact, our experience suggests that for every conflicts waiver request that is actually made to a client, there are several that could have been made but were not—whether due to the belief that it would sour one or more important client relationships or to a concern that the firm's work for one or more clients may in fact be compromised.

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V. *Conflicts Waiver Considerations*

When outside counsel decide whether to request a conflicts waiver, they should typically consider three things: whether it is ethical to do so, whether they are likely to get the consent that they seek, and whether the benefits of making the request outweigh the potential burdens. The questions that corporate counsel should ask when faced with a conflicts waiver request are essentially the same. For present purposes, however, we have broken down these questions into seven overlapping but distinguishable parts.

A. **Is the Waiver Likely To Be Enforceable?**

It goes without saying that an attempt to waive a nonwaivable conflict will likely be held ineffective. Even if a conflict is theoretically waivable, however, there are right ways and wrong ways for a law firm to obtain the waiver.

As should be clear by now, a conflicts waiver will be effective only if based upon sufficiently complete lawyer disclosure or, in other words, informed client consent. This means that there will be times when a too-cursory discussion by a lawyer of the downsides of a conflicts waiver may lead to the waiver being held ineffective. In addition, the effectiveness of a conflicts waiver may be undercut by a significant change in the pertinent facts. *See, e.g.*, ABA Formal Op. 93-372; *see also Hasco, Inc. v. Roche*, 700 N.E.2d 768 (Ill. App. Ct. 1998) (waiver construed more narrowly than law firm concluded); *Gen. Cigar Holdings, Inc. v. Altadis, S.A.*, 144 F. Supp. 2d 1334 (S.D. Fla. 2001) (upholding waiver); *Elonex I.P. Holdings, Ltd. v. Apple Computer, Inc.*, 142 F. Supp. 2d 579 (D. Del. 2001) (same).

We would not recommend that corporate counsel take a cynical approach and expressly agree to a conflicts waiver in the hope and expectation that a court will later throw it out. Among other things, this kind of cynicism could well backfire if it came to the court's attention. Nevertheless, the potential enforceability of a particular conflicts waiver should at least be a factor for consideration.

B. **What Kind of Work Is To Be Done?**

1. *Business Matters*

Conflicts waivers are much more readily given in business matters than in litigation. Presumably, this is because both sides to a potential deal begin by wanting to see the deal completed and neither side is likely to wish to impose extra burdens by making the other side change counsel unless there is some real reason to do so. This makes sense and is a legitimate tactical consideration.

Some parties to business deals push this to another level and assert that the devil they know may be better than the devil they don't know and that a lawyer on the opposite side of a matter who is beholden to them in some other way will be more likely to be fair to them than a total stranger. We are not sure that this analysis makes sense. In the transaction in question, the law firm's obligations will be to the opposing party. The lawyer who is working on that transaction may not even be aware of any other relationship.

2. *Litigation*

Unlike parties who hope to do business together, parties to litigation sometimes think that they can

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gain by placing as many obstacles in an opponent's path as possible. Whether this strategy works very often—whether the litigation opponent that is forced to get new counsel will really give up or even fight less hard, for example—is often open to question. In many cases, opponents just seem to dig in and fight harder.

There are valid strategic reasons why a client may wish to consent to being sued by its own lawyer in particular cases. If, for example, a client wishes to make use of Lawyer X at Firm X, it may be the case that Firm X would be unwilling to let Lawyer X work for the client unless the client is willing to let Firm X represent opposing parties in certain kinds of litigation unrelated to the work of Lawyer X. Nor, of course, must all litigation be fought as “the war to end all wars.” If, for example, there is hope for an early settlement, it might be more appropriate to approach the matter as more in the nature of a business deal.

It may also be the case that the type of matter is as important as whether the matter does or does not involve litigation *per se*. For example, a client can reasonably conclude that it will allow a firm to represent opposing parties in small- or medium-sized breach-of-contract actions or actions for which the client is fully insured but not in dollar actions or in actions in which fraud is alleged.

3. *What Is Being Waived?*

A client should also bear in mind that it can determine how much consent to give. A client can, for example, allow a law firm to oppose it in attempting to negotiate a particular transaction or the resolution of an existing dispute but not allow the law firm to litigate against it if the transaction or negotiated resolution subsequently falls apart. Because consent need not be given, it can be given conditionally. In fact, in-house counsel may wish to look with greater favor upon conflicts waiver requests that are made with additional protections “built in” before a request is made for them. This point is addressed further below.

Similarly, a waiver might be given for work adverse to particular entities in the corporate enterprise but not others. *Cf.* ABA Formal Op. 95-390; Cal. Eth. Op. 1989-113, 1989 WL 253261. Most simply put, the client controls the scope of the waiver.

C. Who Will Do the Work?

Although a client's right to insist upon the disqualification of one lawyer at a firm typically allows the client to insist upon the disqualification of an entire firm, many clients are reasonably and understandably less concerned about conflicts waivers when the lawyers who will work for them and the lawyers who will work against them are not the same individuals. Moreover, a bright-line distinction of this type can save everyone from potential embarrassment or difficulties at a later time.

A client has a right to condition its consent on outside counsel's agreement to use different lawyers for and against that client or to take one or more particular steps to, for example, protect against the adverse use of the client's confidential information.

D. Is Confidential Information at Risk?

This question has two parts. One is simply whether the work that a lawyer or firm has done or is presently doing for a client has given the lawyer confidential client information (*i.e.*, client confidences and secrets) that the lawyer would be in a position to use adversely to that client in the matter for which the waiver is sought. *Cf.* RPC 1.6; ABA Formal Op. 93-372. The other is

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whether, if such a risk does theoretically exist, the client is nonetheless satisfied that protective measures can be taken, such as using different personnel or bringing in another firm to handle particular issues, to ensure that this risk will not become a reality. There are relatively few situations in which conflicts waivers should be given if corporate counsel cannot be satisfied here.

E. How Related or Unrelated Is the Work?

This question is implicit in several of the prior questions. Clients are understandably and quite properly more willing to grant conflicts waivers for work that is altogether unrelated to the work that a lawyer or firm is doing for them than for work that may be related in some way—whether because the same kinds of issues are involved, because the same lawyers or company personnel are involved, or because there is overlapping confidential client information.

F. How Broad Is the Consent?

Future or blanket conflicts waivers are permitted in some, if not necessarily all, jurisdictions. The two critical questions are whether the subsequent conflict is subject to waiver (in which case an advance waiver is no better than a present one) and whether the disclosure provided an adequate basis for the future consent. *See, e.g., Visa U.S.A., Inc. v. First Data Corp.*, 241 F.Supp.2d 1100 (N.D.Cal.2003) (enforcing fairly detailed future conflicts waiver against fairly sophisticated client that consulted counsel before signing); ABA Formal Op. 93-372; Cal. Eth. Op. 1989-115, 1989 WL 253263; N.C. Eth. Op. 8, 1999 WL 33262185; N.Y.C.L.A. Eth. Op. 724, 1998 WL 39561; Or Eth. Op. No. 1991-122, 1991 WL 279213. Although there are many circumstances in which a blanket conflicts waiver is both necessary and appropriate, there are others in which in-house counsel may at least wish to consider whether a more limited waiver would be more in keeping with client interests. At a minimum, raising this question with outside counsel may help flesh out what is and is not at stake in a particular conflicts waiver request.

G. How Good Is Outside Counsel's Disclosure?

Some states require written conflicts waivers. *See, e.g.,* Or. DR 10-101(B); Wash. RPC 1.7. Others do not. Even in those states in which no writing is required, however, the better practice from both outside counsel's and the client's point of view is for outside counsel to submit a written request for a waiver. *Cf.* ABA Formal Op. 93-372.

Corporate counsel who are asked to consider a waiver request should ask themselves whether the combined oral and written disclosures by outside counsel adequately explain the kind or kinds of conflict and the nature of the problem or problems that could result from them. We are concerned that an outside lawyer who does not explain a conflict in a manner that effectively brings home the essential points to in-house counsel may not fully understand the conflict at issue and why someone should care about it. We are also concerned that a lawyer who does not understand a conflict may be less likely to take the steps that are necessary to protect the client's interests.

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VI. Conclusion

Both corporate and outside counsel are human beings, and conflicts waivers often come down to a matter of personal relationships. That is as it should be. As we hope we have shown, however, more is at stake than the personalities of the particular individuals involved. Both client interests and the substantive rules of conflicts law should be considered before a decision is made.

VII. Appendix

Selected ABA Model Rules of Professional Conduct (2004). Please note: these are the ABA's present model rules and are not necessarily in force as written below in any particular jurisdictions. In addition, the interpretation of these rules can differ from jurisdiction to jurisdiction.

Rule 1.7 Conflict Of Interest: Current Clients

(a) Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:

- (1) the representation of one client will be directly adverse to another client; or
- (2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.

(b) Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:

- (1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;
- (2) the representation is not prohibited by law;
- (3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and
- (4) each affected client gives informed consent, confirmed in writing.

Rule 1.8 Conflict Of Interest: Current Clients: Specific Rules

(a) A lawyer shall not enter into a business transaction with a client or knowingly acquire an ownership, possessory, security or other pecuniary interest adverse to a client unless:

- (1) the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing in a manner that can be reasonably understood by the client;
- (2) the client is advised in writing of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent legal counsel on the transaction; and
- (3) the client gives informed consent, in a writing signed by the client, to the essential terms of the transaction and the lawyer's role in the transaction, including whether the lawyer is representing the client in the transaction.

(b) A lawyer shall not use information relating to representation of a client to the disadvantage of the client unless the client gives informed consent, except as permitted or required by these Rules.

(c) A lawyer shall not solicit any substantial gift from a client, including a testamentary gift, or prepare on behalf of a client an instrument giving the lawyer or a person related to the lawyer any substantial gift unless the lawyer or other recipient of the gift is related to the client. For purposes of this paragraph, related persons include a spouse, child, grandchild, parent, grandparent or other relative or individual with whom the lawyer or the client maintains a close, familial relationship.

(d) Prior to the conclusion of representation of a client, a lawyer shall not make or negotiate an agreement giving the lawyer literary or media rights to a portrayal or account based in substantial

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part on information relating to the representation.

(e) A lawyer shall not provide financial assistance to a client in connection with pending or contemplated litigation, except that:

- (1) a lawyer may advance court costs and expenses of litigation, the repayment of which may be contingent on the outcome of the matter; and
- (2) a lawyer representing an indigent client may pay court costs and expenses of litigation on behalf of the client.

(f) A lawyer shall not accept compensation for representing a client from one other than the client unless:

- (1) the client gives informed consent;
- (2) there is no interference with the lawyer's independence of professional judgment or with the client-lawyer relationship; and
- (3) information relating to representation of a client is protected as required by Rule 1.6.

(g) A lawyer who represents two or more clients shall not participate in making an aggregate settlement of the claims of or against the clients, or in a criminal case an aggregated agreement as to guilty or nolo contendere pleas, unless each client gives informed consent, in a writing signed by the client. The lawyer's disclosure shall include the existence and nature of all the claims or pleas involved and of the participation of each person in the settlement.

(h) A lawyer shall not:

- (1) make an agreement prospectively limiting the lawyer's liability to a client for malpractice unless the client is independently represented in making the agreement; or
- (2) settle a claim or potential claim for such liability with an unrepresented client or former client unless that person is advised in writing of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent legal counsel in connection therewith.

(i) A lawyer shall not acquire a proprietary interest in the cause of action or subject matter of litigation the lawyer is conducting for a client, except that the lawyer may:

- (1) acquire a lien authorized by law to secure the lawyer's fee or expenses; and
- (2) contract with a client for a reasonable contingent fee in a civil case.

(j) A lawyer shall not have sexual relations with a client unless a consensual sexual relationship existed between them when the client-lawyer relationship commenced.

(k) While lawyers are associated in a firm, a prohibition in the foregoing paragraphs (a) through (i) that applies to any one of them shall apply to all of them.

Rule 1.9 Duties To Former Clients

(a) A lawyer who has formerly represented a client in a matter shall not thereafter represent another person in the same or a substantially related matter in which that person's interests are materially adverse to the interests of the former client unless the former client gives informed consent, confirmed in writing.

(b) A lawyer shall not knowingly represent a person in the same or a substantially related matter in which a firm with which the lawyer formerly was associated had previously represented a client

- (1) whose interests are materially adverse to that person; and
- (2) about whom the lawyer had acquired information protected by Rules 1.6 and 1.9(c) that is material to the matter;

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unless the former client gives informed consent, confirmed in writing.

(c) A lawyer who has formerly represented a client in a matter or whose present or former firm has formerly represented a client in a matter shall not thereafter:

- (1) use information relating to the representation to the disadvantage of the former client except as these Rules would permit or require with respect to a client, or when the information has become generally known; or
- (2) reveal information relating to the representation except as these Rules would permit or require with respect to a client.

Rule 1.10 Imputation Of Conflicts Of Interest: General Rule

(a) While lawyers are associated in a firm, none of them shall knowingly represent a client when any one of them practicing alone would be prohibited from doing so by Rules 1.7 or 1.9, unless the prohibition is based on a personal interest of the prohibited lawyer and does not present a significant risk of materially limiting the representation of the client by the remaining lawyers in the firm.

(b) When a lawyer has terminated an association with a firm, the firm is not prohibited from thereafter representing a person with interests materially adverse to those of a client represented by the formerly associated lawyer and not currently represented by the firm, unless:

- (1) the matter is the same or substantially related to that in which the formerly associated lawyer represented the client; and
- (2) any lawyer remaining in the firm has information protected by Rules 1.6 and 1.9(c) that is material to the matter.

(c) A disqualification prescribed by this rule may be waived by the affected client under the conditions stated in Rule 1.7.

(d) The disqualification of lawyers associated in a firm with former or current government lawyers is governed by Rule 1.11.

Rule 1.11 Special Conflicts Of Interest For Former And Current Government Officers And Employees

(a) Except as law may otherwise expressly permit, a lawyer who has formerly served as a public officer or employee of the government:

- (1) is subject to Rule 1.9(c); and
- (2) shall not otherwise represent a client in connection with a matter in which the lawyer participated personally and substantially as a public officer or employee, unless the appropriate government agency gives its informed consent, confirmed in writing, to the representation.

(b) When a lawyer is disqualified from representation under paragraph (a), no lawyer in a firm with which that lawyer is associated may knowingly undertake or continue representation in such a matter unless:

- (1) the disqualified lawyer is timely screened from any participation in the matter and is apportioned no part of the fee therefrom; and
- (2) written notice is promptly given to the appropriate government agency to enable it to ascertain compliance with the provisions of this rule.

(c) Except as law may otherwise expressly permit, a lawyer having information that the lawyer knows is confidential government information about a person acquired when the lawyer was a public officer

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or employee, may not represent a private client whose interests are adverse to that person in a matter in which the information could be used to the material disadvantage of that person. As used in this Rule, the term "confidential government information" means information that has been obtained under governmental authority and which, at the time this Rule is applied, the government is prohibited by law from disclosing to the public or has a legal privilege not to disclose and which is not otherwise available to the public. A firm with which that lawyer is associated may undertake or continue representation in the matter only if the disqualified lawyer is timely screened from any participation in the matter and is apportioned no part of the fee therefrom.

(d) Except as law may otherwise expressly permit, a lawyer currently serving as a public officer or employee:

(1) is subject to Rules 1.7 and 1.9; and

(2) shall not:

(i) participate in a matter in which the lawyer participated personally and substantially while in private practice or nongovernmental employment, unless the appropriate government agency gives its informed consent, confirmed in writing; or

(ii) negotiate for private employment with any person who is involved as a party or as lawyer for a party in a matter in which the lawyer is participating personally and substantially, except that a lawyer serving as a law clerk to a judge, other adjudicative officer or arbitrator may negotiate for private employment as permitted by Rule 1.12(b) and subject to the conditions stated in Rule 1.12(b).

(e) As used in this Rule, the term "matter" includes:

(1) any judicial or other proceeding, application, request for a ruling or other determination, contract, claim, controversy, investigation, charge, accusation, arrest or other particular matter involving a specific party or parties, and

(2) any other matter covered by the conflict of interest rules of the appropriate government agency.

Rule 1.12 Former Judge, Arbitrator, Mediator Or Other Third-Party Neutral

(a) Except as stated in paragraph (d), a lawyer shall not represent anyone in connection with a matter in which the lawyer participated personally and substantially as a judge or other adjudicative officer or law clerk to such a person or as an arbitrator, mediator or other third-party neutral, unless all parties to the proceeding give informed consent, confirmed in writing.

(b) A lawyer shall not negotiate for employment with any person who is involved as a party or as lawyer for a party in a matter in which the lawyer is participating personally and substantially as a judge or other adjudicative officer or as an arbitrator, mediator or other third-party neutral. A lawyer serving as a law clerk to a judge or other adjudicative officer may negotiate for employment with a party or lawyer involved in a matter in which the clerk is participating personally and substantially, but only after the lawyer has notified the judge or other adjudicative officer.

(c) If a lawyer is disqualified by paragraph (a), no lawyer in a firm with which that lawyer is associated may knowingly undertake or continue representation in the matter unless:

(1) the disqualified lawyer is timely screened from any participation in the matter and is apportioned no part of the fee therefrom; and

(2) written notice is promptly given to the parties and any appropriate tribunal to enable them to ascertain compliance with the provisions of this rule.

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(d) An arbitrator selected as a partisan of a party in a multimember arbitration panel is not prohibited from subsequently representing that party.

Rule 3.7 Lawyer As Witness

(a) A lawyer shall not act as advocate at a trial in which the lawyer is likely to be a necessary witness unless:

- (1) the testimony relates to an uncontested issue;
- (2) the testimony relates to the nature and value of legal services rendered in the case; or
- (3) disqualification of the lawyer would work substantial hardship on the client.

(b) A lawyer may act as advocate in a trial in which another lawyer in the lawyer's firm is likely to be called as a witness unless precluded from doing so by Rule 1.7 or Rule 1.9.

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VIII. *Additional Resources*

Susan Hackett, *Conflicts of Interest: Do you understand how your outside counsel assess conflicts-or do you just trust them to act in your client's best interests? It's a growing crisis that needs your attention*, Vol.25 Legal Times No.3 January 21, 2002, available at <http://www.acca.com/protected/legres/conflicts/outsideconflict.html>

John R. Villa, *Conflicts of Interest Issues Involving Outside Counsel*, ACC Docket November/December 2001, available at <http://www.acca.com/protected/pubs/docket/nd01/conflict1.php>

Conflicts, Waivers, and Client Protection: A Mock Meeting of In-house and Outside Counsel Program Material ACC's 2001 Annual Meeting available at <http://www.acca.com/education2k1/am/cm/701CD.pdf>

Selecting Outside Counsel: Ask the Right Questions, Get the Right Results Program Material ACC's 2001 Annual Meeting available at <http://www.acca.com/education2k1/am/cm/031CD.pdf>

John K. Villa, *Corporate Counsel Guidelines*, by Co-published by ACC and West Group Copyright 2000 available at http://www.westgroup.com/store/product.asp?product_id=16761615&catalog_name=wgstore

Steven N. Machtinger and Dana A. Welch, *In-house Ethical Conflicts*, ACC Docket February 2004, available at <http://www.acca.com/protected/pubs/docket/feb04/conflict.pdf>

Leading Practices in Conflicts Management Programs: What Companies and Law Firms are Doing, available at http://www.acca.com/protected/article/conflicts/lead_conflict.pdf

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IX. Sample Forms and Policies

Sample Conflict Waiver Letter

[Date]

[Name of Lawyer Requesting Waiver]

[Outside Law Firm Name]

[Address]

Re: [name of case or transaction for which waiver is requested]

Dear [outside lawyer]:

This letter is in response to your request for a waiver of a [potential or actual] conflict of interest in connection with [law firm]'s representation of [other client's name] in the above referenced matter. We have no objection to such representation subject to the following conditions:

1. [Other client name] agrees not to object to [law firm]'s continued ability to represent XYZ COMPANY or its affiliates on existing and future matters; [and]
2. [Law firm]'s representation of [other client] will not involve the assertion against XYZ COMPANY or any of its affiliates of a claim of fraud, misrepresentation, or other dishonest conduct .[; and]
3. [Law firm] is representing [other client] for the sole purpose of [describe limited engagement to which XYZ COMPANY is consenting]and it is understood that XYZ COMPANY reserves the right to claim a potential or actual conflict of interest and take appropriate action regarding any other matters including broader representation of [other client] with reference to this matter.[; and]
4. [(Law firm) personnel providing services to (other client) in connection with this matter will not be among those concurrently providing services to XYZ COMPANY or a XYZ COMPANY affiliate. ;and]
5. [(Other client) has been informed of the conditions set forth in this letter and has agreed to these conditions.]

[Please sign this letter and have it signed by a representative of [other client] and return it to me if it is acceptable to you.]

Very truly yours,

XYZ COMPANY Attorney

Received and agreed to:

[Attorney at law firm]

[Other client representative]

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In-House Counsel Responsibilities in the Post-Enron Environment

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The Enron debacle has changed the current legal landscape, particularly the role of in-house counsel in the corporate environment. Enron, Arthur Andersen, and other corporations recently in the news employed numerous in-house attorneys, and many feel that the in-house attorneys should have served as the watchdog and the gatekeeper to report wrongdoing, fraud, and corruption in order to protect the corporation.

As a result of Enron and other corporate scandals, we lawyers are often the target of criticism. Recent regulations and future proposed changes likely will encourage in-house and outside counsel to be involved in the financial affairs of the corporation and to aggressively address and report improper conduct. Consequently, we in-house counsel will need to have heightened awareness of corporate conduct and properly investigate any reports of misconduct. This article will discuss the broad responsibilities of in-house counsel and will provide an overview of the post-Enron environment from the in-house perspective. In addition, the article will discuss how the attorney-client privilege may be affected by the dual business and legal responsibilities of in-house counsel.

The number of in-house counsel employed by corporations has been increasing. In 1991, the top 10 Fortune 500 companies employed an average of 287 in-house attorneys; by 2000, that average had increased by more than 40 percent to 407.2 The increasing number of attorneys being employed by corporations is the direct result of the tangible benefits that in-house attorneys provide for the corporate client. These benefits include the cost savings, the familiarity with the business of the corporation, the working relationship with employees and executives of the corporation, and the accessibility of the in-house lawyer.³ Perhaps the most significant benefit and the hardest to quantify is the fact that in-house counsel can intervene early and prevent the company from being involved in litigation by managing the legal risks of the corporate client.⁴

Prelitigation resolution is a reality when in-house counsel troubleshoot and solve problems. For example, I have been involved in a number of disputes that were resolved before litigation because all parties came together early, evaluated proportionate fault, and reached an amicable resolution of a dispute. The early involvement of in-house counsel is valuable because it can help a company avoid costly, time-consuming litigation. I have found, particularly in the engineering industry, that, if all interested parties discuss problems and identify solutions, a great number of matters can be solved short of litigation. To this end, in-house counsel may consider including a predispute resolution or mediation clause in their contracts with vendors, suppliers, and others.

In this post-Enron environment, many have questioned why the in-house attorneys of failing corporations did not stop the destruction before it became overwhelming. One response with significant merit is that the in-house attorneys were unaware of the misconduct. In this period of new scrutiny and sweeping legislative reform, however,

such answers may not be sufficient. Additionally, ignorance of misconduct may not protect in-house counsel from personal liability in certain situations.

New Reforms Are upon Us

New legislation and its soon to become effective regulations encourage the in-house lawyer to serve as the corporate gatekeeper. The Sarbanes-Oxley Act of 2002, which was the federal government's first response to the post-Enron corporate climate and an attempt to prevent another massive corporate failure, establishes broad new oversight of accountants, new corporate governance rules, and new reporting requirements for in-house counsel of public companies.⁵ For several detailed discussions of the broad scope of the Sarbanes-Oxley Act that have appeared in the ACCA Docket and elsewhere, see the value added sidebar.

The Sarbanes-Oxley Act will primarily affect lawyers of publicly traded companies; however, the American Bar Association ("ABA") is preparing to make significant changes to the Model Rules of Professional Conduct that will directly affect in-house counsel of all companies.

On March 28, 2002, the Task Force on Corporate Responsibility ("Task Force") was appointed by the ABA and directed to analyze corporate responsibility and strengthen corporate governance by creating new ethical standards for lawyers. The Task Force was charged as follows:

The Task Force on Corporate Responsibility shall examine systemic issues relating to corporate responsibility arising out of the unexpected and traumatic bankruptcy of Enron, and other Enron-like situations which have shaken confidence in the effectiveness of the governance and disclosure systems applicable to public companies in the United States. The Task Force will examine the framework of laws and regulations and ethical principals governing the roles of lawyers, executive officers, directors, and other key participants.⁶

The initial recommendations presented by the Task Force have been examined in previous ACCA Docket articles, and a new report should be released soon. In advance of that report, this article will focus on the practical, valuable, post-Enron lessons that our profession has already learned and the steps that we can take immediately to serve our clients.

Response of In-house Counsel to Corporate Scandals

ACCA recently conducted a survey of 1,216 members for their opinions about the recent corporate financial and accounting problems, as well as methods to prevent future disasters. Of the participants, 308 were general counsel, and 908 were other in-house counsel. The overwhelming results of the survey showed that "[i]n-house counsel want an expanded role in preventing and reporting fraud and believe that greater access to the

CEO and Board of Directors on their part will reduce fraud. A prevailing view is that in-house counsel are too often left 'out of the loop' on financial and accounting issues."⁷

The survey represents a cross-section of in-house counsel in the United States, and 48 of the participants polled were located outside the United States. The responses directly affecting in-house attorneys are summarized below:

- * 72 percent of those polled felt that ethics and corporate responsibility are taken very seriously, while 24 percent felt that ethics and corporate responsibility should be taken more seriously.

- * 64 percent of those polled felt that the company's corporate culture emphasizes the company as the client while, quite surprisingly, 20 percent felt that the corporation's culture emphasized that senior management was the client.

- * 78 percent of those polled felt that the general counsel or other in-house attorneys should report misconduct to appropriate corporate officials when they become aware of it.

- * Respondents were divided on whether the Model Rules of Professional Conduct, the Sarbanes-Oxley Act, or the new SEC disclosure requirements would best assist in preventing financial and accounting fraud. Of the respondents, 23 percent felt that the proposed changes to the Model Rules of Professional Conduct would best prevent the misconduct; 20 percent felt that the Sarbanes-Oxley Act would best prevent the misconduct; and 27 percent felt that the new SEC disclosure requirements would best prevent the misconduct.

- * 57 percent felt that in-house counsel should play a role as important as that of the CEO, COO, or CFO in preventing financial and accounting fraud, as well as other illegal and unethical behavior.

- * 71 percent felt that the law should be clearly defined and reporting illegal behavior made mandatory, regardless of the attorney-client privilege, to ensure the well being of the in-house counsel's company.

- * 48 percent believed that establishment of laws protecting attorney whistleblowers was required to ensure the well being of their company.

- * 44 percent believed that better access to the board of directors was needed to ensure the well-being of their company.

- * 49 percent of those polled would support establishing a new code or strengthening an existing business code of conduct; 42 percent felt that an employee hotline should be established; 76 percent felt that executives should implement a comprehensive education program for employees regarding their legal obligations; and 51 percent felt that there should be new or strengthened procedures for conducting independent investigations of possible misconduct.

- * 54 percent of those polled felt that the Sarbanes-Oxley Act was unnecessary because the Model Rules of Professional Conduct already set forth reporting requirements, while 46 percent felt that the law was necessary.

- * There was a split among those polled as to whether the proposed changes to the Model Rules, which concern the confidentiality of communications by encouraging disclosure of the threat of financial harm or material violations of the SEC rules, should have permissive or mandatory disclosure. Of the respondents, 35 percent felt that the

disclosure should be mandatory; 46 percent felt that disclosure should be permissive; and 19 percent were undecided.

* If the Model Rule revisions required mandatory reporting, 47 percent felt that such reporting would affect the attorney-client relationship because the client would be less candid; 30 percent felt that mandatory reporting would have no effect on the relationship; and 19 percent were undecided.

* 49 percent of those polled felt that in-house counsel were generally kept informed but were still kept "out of the loop" on important developments as they related to financial and accounting issues, while 39 percent felt that in-house counsel were kept well informed.⁸

The above summary represents the opinions from in-house counsel regarding the post-Enron landscape and, more important, the future role of in-house counsel. First and foremost, it is mandatory that we in-house lawyers consider the corporation, not individual officers and directors, as the client. Unfortunately, 20 percent of those polled felt that their corporations' culture emphasized that senior management was the client. Fortunately, 78 percent of those polled felt that the general counsel or other in-house attorney should report inappropriate conduct to corporate officials. Additionally, ACCA members are divided about which regulations (Sarbanes-Oxley, the Model Rules of Professional Conduct, or the new SEC disclosure requirements) would most likely prevent financial and accounting fraud.⁹

If the Model Rule changes on the horizon for the in-house lawyer are implemented, the requirements to report wrongdoing will likely increase. Therefore, it is significant that 48 percent of those polled felt that new laws should be established protecting attorney "whistleblowers" who take measures to protect the corporation as the client.

In the post-Enron environment, in-house counsel will need to be informed of the corporation's business affairs and will need to be cognizant of any potential misconduct. Significantly, 49 percent of those polled felt that in-house counsel were still kept "out of the loop" on financial and accounting issues. Thus, in order to fulfill our responsibilities, many of us may need to obtain the necessary training to comprehend basic accounting and to understand financial decisions.¹⁰

Who Is Our Client?

As in-house counsel, we must be constantly aware of the fact that we do not solely represent the board of directors, the principals, officers, or others individually. Instead, we represent the organization as a whole and are charged with representing our client, the organization, to the best of our ability. In fact, Model Rule 1.13 clearly defines the client of the in-house lawyer, noting in Rule 1.13(a) that "a lawyer employed or retained by an organization represents the organization acting through its duly authorized constituents."¹¹ Additionally, Model Rule 1.13 (b) currently provides that, if a lawyer for an organization knows that an officer, an employee, or other person associated with the organization is engaged in action, intends to act, or refuses to act in a matter related to the

representation that is a violation of a legal obligation to the organization or a violation of law that reasonably might be imputed to the organization and that is likely to result in substantial injury to the organization, the lawyer shall proceed as is reasonably necessary in the best interest of the organization.¹²

Consequently, although officers, directors, employees, and shareholders are stakeholders, we must be aware of the fact that we represent the entire organization, and we must take action against wrongdoing that will cause substantial injury to the organization.¹³

Protecting the Corporate Client

To comply with these new rules, we will apparently need to ensure that the conduct of directors and officers conforms to the law and that, if it does not, we report misconduct that violates any laws or regulations, particularly when such conduct can result in substantial harm or injury to the organization. See the value added sidebar for several articles that question whether such an arrangement is appropriate for in-house counsel, but until such time that some of these new rules evaporate, we need to be prepared to do exactly what the new rules require so that we do not become personally liable.

As general counsel, I attend all board meetings, and I frequently interact with the president, CEO, board of directors, and principal owners of all subsidiaries. Much of the interaction involves discussing our legal responsibility to the organization. For example, educating all directors and officers about their responsibilities and obligations to the organization is a must for me. Directors must be made aware of their fiduciary duties of loyalty and care to the organization, as well as other relevant laws, such as the corporate opportunity doctrine.

In addition, frequent contact and communication will help the in-house attorney discover misconduct and protect the corporation. A delicate balance must be maintained, however, to preserve the historical and valuable relationship between the in-house attorney and the organization. We should be viewed as trusted advisors, not investigators and prosecutors.

Our Role as Trusted Advisors

We have worked hard to become trusted members of our organizations, and we must maintain that position in order to be credible as people who can give legal and, at times, business advice. The current Model Rule 1.2 fosters this relationship:

A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent, but a lawyer may discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client to make a good faith effort to determine the validity, scope, meaning or application of the law.¹⁴

When we are kept informed of the company's affairs, we can advise the organization to avoid any legal pitfalls and misconduct before it occurs. We can then counsel our client

not to commit misconduct, and people in the organization will know that we can be trusted to protect the client's best interests, consistent with the law.

Maintaining Checks and Balances

Two of the proposals by the ABA Task Force in its July 16, 2002, Preliminary Report provide sound practical advice. First, the Task Force recommends that corporations "adopt a practice whereby the general counsel meets routinely and periodically, privately, with one or more independent directors, to facilitate board attention to potential violations of law by and breaches of duty to the corporation."¹⁵

This recommendation by the Task Force demonstrates the significance of the role of the general counsel and the need to have open lines of communication with independent directors and other senior-level officers of a corporation. The creation of established communication lines guards against acquiescence in wrongdoing by senior level management. Active involvement with independent directors and officers will allow the in-house attorney to be well informed and should encourage and promote ethical conduct.

The second recommendation by the Task Force is that "all engagements of outside counsel should establish at the outset a direct line of communication with General Counsel through which outside counsel should inform the general counsel of violations/potential violations of law, and duty to the corporation."¹⁶

The general counsel should have open communication with outside counsel, and outside counsel must be able to communicate concerns regarding violations of the law by directors or officers. The general counsel can in turn conduct investigations and take appropriate steps to correct problems.¹⁷ The post-Enron environment certainly underscores the importance of communication with outside counsel.

When I assumed the position of general counsel, I reassigned legal matters to local counsel, away from regional counsel, to foster and support communication with outside counsel. Busy in-house lawyers may often be tempted to use hasty communications via email or brief correspondence with outside counsel; however, person-to-person, face-to-face communication is extremely valuable.

My experience with outside counsel has been that they are honest and candid. Both of us identify issues and strategies, and the communication flow is open. If we have concerns about legal matters, we voice them and take action. We recognize that both of us contribute to the representation of the organization, and we often brainstorm ways to prevent problems before they develop. The general counsel should ensure that this relationship is preserved by frequently contacting outside counsel, and if this relationship is not mutually beneficial, a change may be required.

Dual Role: Keep the Trust by Protecting and Preserving the Attorney-Client Privilege

Another question that has arisen in the aftermath of corporate scandals is whether the in-house attorney in the post-Enron environment can preserve the attorney-client privilege as effectively as outside counsel. I believe that the answer is yes. The in-house attorney must, however, ensure that the privilege is protected and preserved, even when in-house counsel serve a dual role performing legal functions that are covered by the privilege and business functions that are not.

Today, in-house counsel perform a multitude of tasks besides serving as the corporate attorney. Corporations use in-house attorneys not only for their legal advice but also for their ability to provide counsel on day-to-day workplace problems and complex government regulations.¹⁸

A recent survey conducted by ACCA demonstrates that it is common for the in-house lawyer to serve as both a senior level manager of an organization and the legal advisor. The ACCA survey asked whether, in addition to serving as general counsel, the respondent also had a nonlegal function in the corporation, not including vice president or corporate secretary. The respondents-378 general counsel-answered as follows:

- * 8.7 percent (33) also serve as COO.
- * 7.4 percent (28) also serve as CFO.
- * 6.3 percent (24) also serve as CEO.
- * 13.5 percent (51) also serve as the head of a business unit, such as marketing, manufacturing, and so forth.
- * 24.9 percent (94) also serve as director of human resources.
- * 39.2 percent (148) also serve "other" business functions.¹⁹

Clearly, corporations rely on us to be a part of the business organization because the business advice and support provided by the in-house attorney is valuable to the organization. It is, however, important to note-and to make sure that the client knows-that if we are not providing legal advice, the attorney-client privilege does not apply. Consequently, in-house attorneys who serve dual roles will need to keep legal and business advice separate.

The key issue for courts when determining whether the attorney-client privilege applies to the in-house counsel's work is whether the attorney was acting in his or her legal capacity and whether the attorney was providing legal services for the corporation.²⁰

Generally, communications made for the purpose of obtaining and providing legal advice to the corporation are protected. The U.S. Supreme Court emphasized the importance of the attorney-client privilege in *Hunt v. Blackburn* (1888), a case in which the Court noted that the privilege is "founded upon the necessity, and the interest in administration of justice, of the aid of persons having knowledge of the law and skilled in its practice,

which assistance can only be safely and readily availed of when free from the consequences or the apprehension of disclosure."²¹

In *Upjohn Company v. United States*, *Upjohn* appealed a Sixth Circuit ruling that held that the attorney-client privilege did not apply to an Internal Revenue Service ("IRS") summons requesting production of questionnaires and notes of interviews prepared by *Upjohn's* general counsel, who was investigating payments to foreign government officials.²² The appeals court had held that the attorney-client privilege did not apply under the "control group" test, which, according to the appeals court, holds that the privilege "covers only those communications made by the so-called 'control groups of the corporation, namely those officers, usually top management, who play a substantial role in deciding and directing the corporation's response to the legal advice given."²³ The appeals court held that the privilege did not apply "[t]o the extent that the communications were made by officers and agents not responsible for directing *Upjohn's* actions in response to legal advice . . . for the simple reason that the communications were not the 'clients.'"²⁴

The U.S. Supreme Court declined to follow the narrow "control group" test by holding that it discouraged the sharing of relevant information by employees.²⁵ The Court noted that an attorney's advice should not be limited in that "the narrow scope given the attorney-client privilege by the court below not only makes it difficult for corporate attorneys to formulate sound advice when their client is faced with a specific legal problem, but also threatens to limit the valuable efforts of corporate counsel to ensure their client's compliance with the law."²⁶ Consequently, the Court held that the responses to the questionnaires were protected by the attorney-client privilege because "the communications concerned matters within the scope of the employees' corporate duties, and the employees themselves were sufficiently aware that they were being questioned in order that the corporation could obtain legal advice."²⁷

Although some states have adopted the control group test, others have adopted the subject matter test, which considers other factors, including the following: "1) the employee must be an employee of the corporation; 2) the communication must have been made by the employee at the direction of his supervisor; and 3) the subject matter of the communication must be within the employee's scope of employment."²⁸ In addition, the communication must have been made for legal purposes and remain confidential.²⁹

The U.S. Supreme Court in *Upjohn* did not adopt a definitive test but appears to have leaned toward the broader subject-matter test. The Court based its ruling on the fact that the information came from employees who had knowledge. Therefore, the *Upjohn* ruling corresponds to two of the three "subject matter" factors: (1) the communication was made by an employee, and (2) the subject matter was within the employee's scope of employment.³⁰

Upjohn addresses attorney-client privilege from the federal perspective, and the holding is relevant in many states. It is important to note, however, that individual states have varying perspectives and approaches. It is worth noting that ACCA recently submitted an

amicus brief in *Exxon Corp. v. Department of Conservation of Natural Resources*, in support of the in-house attorney-client privilege.³¹ The Exxon case is significant because it underscores the significance of the attorney-client privilege in the in-house context. In the Exxon case, the Supreme Court of Alabama reversed the judgment of the trial court and held that the admission at trial of a letter containing a legal opinion regarding mineral leases, which had been prepared at the request of the company's accounting manager by an Exxon in-house attorney, prejudiced Exxon and was reversible error. Exxon contended that the letter was prepared "for the purpose of facilitating the rendition of professional legal services."³² The court held that Exxon had met its burden of proving confidentiality of the document because all the recipients of the letter were "client representatives" who had duties closely related to the matter. The court also noted that the state had failed to present any evidence showing that the letter was not intended to be confidential or that the recipients of the letter were not client representatives.³³ See the value added for an article on the Exxon case and for documents relating to ACCA's amicus brief in the case.

As in-house counsel, you should take a number of practical steps to preserve the attorney-client privilege. For example, use legal titles, such as general counsel, chief legal officer, esquire, or attorney at law. Additionally, have procedures in place for separating legal files from corporate files and limit the number of people receiving legal information within an organization whenever possible.³⁴ The recipients of the legal advice or legal documents should be closely related to the matter at issue and should be representatives of the client. In addition, label information that is to be closely held as confidential but do not use the term "confidential" as a routine classification to be applied to all of your files. These strategies, coupled with your compliance with relevant state common law and evidentiary rules, will help to ensure preservation of the attorney-client privilege.

In my own practice, I keep all legal files separate from other files, and I am careful to distribute legal opinion and information only to those persons who are involved in the matter at hand and to the board of directors. I also appear as counsel and become actively involved in many legal proceedings. My active involvement in legal matters and appearance as counsel of record in pending matters adds an additional level of insurance for the privilege. Additionally, I work hard to make sure that recipients of legal information do not do something that will create a waiver of the attorney-client privilege—that is, I take the time to explain to them what would happen to their attorney-client privilege, for example, if we inadvertently began talking about some pending matter at, say, the company holiday party within earshot of a group of folks who were not involved with the matter at hand.

Document Retention Policies for the In-house Counsel Post-Enron

The recent obstruction of justice charges against corporations highlight the need for a corporation to design and implement an effective document retention program. If the document retention program is not properly administered, a corporation is exposed to civil and criminal liability, and in-house counsel may be violating Rule 3.4 of the Model Rules of Professional Conduct, which holds that a lawyer may not "destroy or conceal a document or other material having potential evidentiary value."³⁵ This rule has been in

the spotlight recently as allegations surfaced that an in-house lawyer for Arthur Andersen had authorized the shredding and deleting of documents related to Enron.³⁶

In-house lawyers and senior management must have oversight of the document retention program. A properly handled document retention system, in addition to protecting the corporation from subsequent liability for destroying documents, can be a cost saver by reducing storage expenses of unnecessary documents. In-house counsel can identify regulatory and legal retention requirements, as well as the various electronic and print forms of document retention programs being used within the corporation.³⁷ Additionally, you will need to determine which documents and records are required to be kept for life or for a limited period of time, such as tax records, medical records, records related to criminal or civil matters, and other documents required to be retained by federal law.

Obviously, the safe and responsible approach is to retain documents if there is any question about their future usefulness, and in-house lawyers are uniquely positioned to make such judgments. Of course, the document retention program should be implemented in the ordinary course of doing business because establishing such a program during a corporate crisis sends the wrong message to prosecutors, the opposition in a civil suit, jurors, employees, shareholders, customers, the public, and the media, among perhaps others, as well.

Your document retention policy should include specific methods for identifying documents eligible for destruction. In addition, the in-house lawyer should carefully analyze whether the policy permits destroying documents that could be beneficial to the corporation in the future because the policy is too broad in scope or time duration.³⁸ Finally, you should review the policy at least annually to incorporate any changes necessitated by laws or regulations. See the value added sidebar for ACCA's records retention resources.

Conclusion

The recent corporate scandals have caused many people to question whether the rules pertaining to lawyers, accountants, directors, officers, and others are strict enough to protect a corporation's employees and shareholders. As a result, new legislation and new rules will dramatically affect in-house counsel's professional responsibilities.

We will need not only to respond to the legal concerns of our client but also to ensure that officers, directors, and others keep the in-house attorney informed at all times. To protect the best interests of our client, we may also find ourselves writing and enforcing a corporate code of ethics for all employees. See the value added sidebar on page xx for ACCA Docket articles addressing corporate codes of conduct.

We are an asset to our clients because we are intimately familiar with and able to give advice on both the legal and business dealings of the corporation. It is, however, mandatory that we protect the attorney-client privilege by keeping legal and business advice separate and taking affirmative steps to preserve the attorney-client privilege.

All in-house counsel should consider implementing a document retention program that trains employees on the kinds of documents to retain and the length of time that these documents should be kept. Implementing a carefully designed document retention program during a time of normal business activity will help protect a corporate client from liability. Again, see the value added sidebar.

In-house counsel may have been under intense scrutiny during the recent corporate scandals, but a combination of increased attention to new legislation, rules of conduct, and professional judgment will help us fulfill our responsibilities to our clients and ourselves.

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NOTES

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3. A Company's First General Counsel, 1, 2-4 (2002), an ACCA InfoPAKSM available on ACCA OnlineSM at www.acca.com/infopaks/firstgc.html.
4. See id.
5. Corporate and Auditing Accountability, Responsibility and Transparency Act of 2002, Pub. L. No. 107-204 (2002).
6. Preliminary Report of the American Bar Association Task Force on Corporate Responsibility, at 1 (July 16, 2002).
7. ACCA Press Release, Summary of Findings: In-house Counsel Poll on Corporate Scandals, at 1 (Oct. 21, 2002), available on ACCA OnlineSM at www.acca.com/about/press/item.php.
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10. See id.
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12. MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.13(b) (2002).
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23. *Upjohn v. U.S.*, 600 F.2d 1223, 1226 (6th Cir. 1979).
24. *Id.* at 388, citing 600 F. 2d 1223 at 1225.
25. *Upjohn*, 499 U.S. at 392.
26. *Id.* at 392.
27. *Id.* at 394.
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29. *Id.*
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33. *Id.* at 7.
34. Scott R. Flucke: The Attorney-Client Privilege in the Corporate Setting: Counsel's Dual Role as Attorney and Executive, 62 U.M.K.C. L. REV. 549, 576-80 (1994).
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