# Special Report

Corporate Counsel

## Client Identity

A lawyer retained or employed by a corporation or other organization represents the entity itself, not any of its constituents. This "entity theory" of representation is recognized in Model Rule 1.13(a) and in Section 96(1)(a) of the *Restatement (Third) of the Law Governing Lawyers*.

Although the entity theory sounds straightforward, and is firmly established and accepted by all U.S. courts, the application of this principle is often complicated and unpredictable in the real world of corporate legal practice. Disputes frequently arise because:

- constituents of a corporate client can get the wrong idea about whom the lawyer represents—especially in small companies—due to the fact that counsel can interact with the client only through its agents and officials;
- corporate lawyers and their clients often disagree whether the representation extends to corporate affiliates;
- the very identity of a corporate client sometimes mutates when assets or the company itself is sold; or
- intracorporate disputes can make it unclear who really speaks for the client.

This Special Report examines these troublesome issues, which crop up time and again in disqualification disputes, malpractice actions and disciplinary proceedings.

## Corporate Lawyers Must Take Steps to Minimize Client Identity Problems

Under the entity theory, the lawyer for a corporation or other organization owes her ethical and professional obligations to her client—the organization—and not to the organization's constituents. *Murray v. Metro. Life Ins. Co.*, 583 F.3d 173, 25 Law. Man. Prof. Conduct 552 (2d Cir. 2009).

See also *Kirschner v. K&L Gates*, 46 A.3d 737 (Pa. Super. Ct. 2012) (firm retained by committee of independent directors to investigate internal misconduct represented and owed duties to entire corporation, not just committee, despite express statement to the contrary in retainer agreement); ABA Formal Ethics Op. 08-453 (2008) (law firm's ethics counsel represents firm as a whole, and not individual firm lawyers, although simultaneous representation of individual firm member is permitted where no conflict exists between firm and individual lawyer).

Therefore, a constituent generally will not be able to recover against the lawyer for malpractice, even though the legal advice rendered to the corporation affects the constituent. *Palmer v. Fox Software, Inc.*, 107 F.3d 415 (6th Cir. 1997).

Along the same lines, the constituents of an organization usually find themselves unable to convince the court that the entity's counsel owed a fiduciary duty to anyone other than the organization. E.g., *Lane v. Chowning*, 610 F.2d 1385 (8th Cir. 1979) (no fiduciary duty to former chairman and CEO of bank).

In addition, most courts have rejected claims by corporate constituents that they were the intended beneficiaries of the services provided by corporate counsel. E.g., *Murray v. Metro. Life Ins. Co.*, supra.

Model Rule 1.13(a) means only that the lawyer for a corporation does not thereby *automatically* or *necessarily* represent the organization's constituents. The en-


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tity theory does not preclude the possibility, however, that the corporate lawyer may inadvertently end up representing *both* the corporation *and* a constituent.

Therefore, the lawyer for an organization must take care to avoid the creation of an attorney-client relationship with individual constituents or owners unless the lawyer intends to do so and concludes that it is ethical to do so. A constituent who inadvertently becomes a client may be able to sue the lawyer for malpractice, to prevent the lawyer from representing the corporation in a matter adverse to the constituent or to cause a waiver of the organization's attorney-client privilege and obtain documents that otherwise might be shielded. In addition, work product protection for the corporate lawyer's work could be lost.

One author stated in the 1990s that "it is extremely rare for courts to find an attorney-client relationship between an entity lawyer and an individual constituent." Moore, *Expanding Duties of Attorneys to "Non-Clients": Reconceptualizing the Attorney-Client Relationship in Entity Representation and Other Inherently Ambiguous Situations*, 45 S.C. L. Rev. 659, 679 (1994).

Nevertheless, the large volume of case law on point shows that, whether or not they ultimately win, lawyers for corporations are frequently sued by constituents who claim an attorney-client relationship.

## Many Executives Don't Get It

Many corporate executives apparently do not realize that corporate counsel represents the corporation only, and not them as individuals. See Weaver, *Ethical Dilemmas of Corporate Counsel: A Structural and Contextual Analysis*, 46 Emory L.J. 1023, 1028 (1997).

The typical problem arises when officers or directors ask corporate counsel for advice or information about how a particular transaction will affect them. Unless the lawyer embarked on an individual attorney-client relationship with the constituent, the advice is generally regarded as being for the corporate client's benefit and the attorney is held not to have assumed a duty to the individual. *Innes v. Howell Corp.*, 76 F.3d 702 (6th Cir. 1996); *Cole v. Ruidoso Mun. Sch.*, 43 F.3d 1373 (10th Cir. 1994); *Waggoner v. Snow, Becker, Kroll, Klaris & Krauss*, 991 F.2d 1501 (9th Cir. 1993); *Hile v. Firmin, Sprague & Huffman Co.*, 595 N.E.2d 1023 (Ohio Ct. App. 1991).

The problem facing the corporate lawyer is that an attorney-client relationship may develop without any formality. See *Restatement (Third) of the Law Governing Lawyers* § 14 (2000), which provides that an attorney-client relationship arises whenever a person manifests an intent for the lawyer to provide legal services for the person, the lawyer either manifests consent or fails to manifest lack of consent, and the lawyer knows or reasonably should know that the person is reasonably relying on the lawyer to provide the services.

The evolving test for an implied attorney-client relationship looks to the reasonable expectations of the constituent. See Restatement § 14 cmt. f (question is one of fact based on reasonable and apparent expectation of person or entity whose status as client is in question); Moore, *Expanding Duties of Attorneys to "Non-Clients": Reconceptualizing the Attorney-Client Relationship in Entity Representation and Other Inherently Ambiguous Situations*, 45 S.C. L. Rev. 659 (1994) (proposing tort-based "reasonable expectation" test in malpractice cases involving entity representation); South Carolina Ethics Op. 91-24 (1991) (expectation of would-be client, not form of entity, determines identity of client).

Precisely when an attorney-client relationship will be found is difficult, if not impossible, to predict. Some courts seem to apply general rules, while others explore a laundry list of factors. Hazard, *Triangular Lawyer Relationships: An Exploratory Analysis*, 1 Geo. J. Legal Ethics 15, 30 (1987) (describing case law as "baffled and baffling"); see, e.g., *First Republic Bank v. Brand*, 51 Pa. D.&C.4th 167 (Pa. C.P. 2001) (setting out 10-factor test for determining whether corporation's lawyer has entered into attorney-client relationship with corporation's shareholder).

In general, a constituent's conclusory assertion that he believed the lawyer represented him is insufficient to raise a factual issue; there must be additional facts or circumstances showing that it was reasonable for the constituent to entertain this belief. *Rice v. Strunk*, 670 N.E.2d 1280 (Ind. 1996); *Bowen v. Smith*, 838 P.2d 186 (Wyo. 1992).

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When courts attempt to reconstruct whether an attorney-client relationship was implied in the dealings between corporate lawyer and constituent, the following themes frequently surface as focal points of concern or disagreement:

***Adversity of interest.*** An obvious and substantial conflict of interest between the constituent and the organization weighs against finding that corporate counsel also represented the constituent. E.g., *TJD Dissolution Corp. v. Savoie Supply Co.*, 460 N.W.2d 59 (Minn. Ct. App. 1990) (unreasonable for major shareholder to rely on advice of corporation's lawyer during negotiations to sell corporation to third party where shareholder knew that lawyer represented corporation, that his interests were adverse to company, and that he had been requested to obtain his own attorney). See generally Restatement § 14 cmt. f.

***Receipt of confidential information.*** A lawyer does not become counsel for a constituent merely because the constituent imparts confidential communications to the lawyer for the organization on a matter of interest to the organization. *Nilavar v. Mercy Health Sys.*, 143 F. Supp.2d 909 (S.D. Ohio 2001); *Kubin v. Miller*, 801 F. Supp. 1101 (S.D.N.Y. 1992); *Ferranti Int'l PLC v. Clark*, 767 F. Supp. 670 (E.D. Pa. 1991); *Talvy v. Am. Red Cross in Greater New York*, 618 N.Y.S.2d 25 (N.Y. App. Div. 1994), aff'd, 661 N.E.2d 159 (N.Y. 1995); see also *United States v. Teamsters*, 120 F.3d 341 (2d Cir. 1997) (rejecting reasonable belief standard in context of claim that employee's communications to organization's lawyer were protected by attorney-client privilege).

***Knowledge that constituent's livelihood depends on advice.*** The lawyer's awareness that the constituent's livelihood depends on the lawyer's advice generally does

not warrant implying an attorney-client relationship. *Robertson v. Gaston Snow & Ely Bartlett*, 536 N.E.2d 344 (Mass. 1989); *Delta Automatic Sys., Inc. v. Bingham*, 974 P.2d 1174 (N.M. Ct. App. 1998). But see *Good Old Days Tavern, Inc. v. Zwirn*, 686 N.Y.S.2d 414 (N.Y. App. Div. 1999) (president and sole shareholder, whose livelihood depended on corporation, could sue corporate counsel as third-party beneficiary of contract between corporation and lawyer for legal services).

***Purpose of consultation.*** When the constituent consulted the lawyer to carry out his responsibilities for the corporation, it is generally not reasonable for the constituent to believe that the lawyer represents him personally. *Cole v. Ruidoso Mun. Sch.*, 43 F.3d 1373 (10th Cir. 1994).

***Prior relationship between constituent and lawyer.*** The existence of a personal relationship between the corporate lawyer and the constituent generally does not by itself justify finding an individual attorney-client relationship. *Ferranti Int'l PLC v. Clark*, 767 F. Supp. 670 (E.D. Pa. 1991); *Egan v. McNamara*, 467 A.2d 733 (D.C. 1983); *Doe v. Poe*, 595 N.Y.S.2d 503 (N.Y. App. Div. 1993).

***Prior representation of individual.*** Prior individual representation of the constituent by corporate counsel is usually not enough by itself to imply an attorney-client relationship. *Palmer v. Fox Software, Inc.*, 107 F.3d 415 (6th Cir. 1997); *Waggoner v. Snow, Becker, Kroll, Klaris & Krauss*, 991 F.2d 1501 (9th Cir. 1993); *Zimmerman v. Dan Kamphausen Co.*, 971 P.2d 236 (Colo. Ct. App. 1998); *Robertson v. Gaston Snow & Ely Bartlett*, 536 N.E.2d 344 (Mass. 1989); *Delta Automatic Sys., Inc. v. Bingham*, 974 P.2d 1174 (N.M. Ct. App. 1998).

But prior representation may be considered as one factor bearing on the reasonableness of the putative client's belief. *In re Brown*, 956 P.2d 188 (Or. 1998).

***Payment of fees.*** The fact that the organization, not the constituent, paid the lawyer's fees sometimes undercuts the claim that the constituent had an attorney-client relationship with the lawyer. E.g., *Robertson v. Gaston Snow & Ely Bartlett*, 536 N.E.2d 344 (Mass. 1989). The payment of attorneys' fees by the constituent can be a factor—*Atlas Partners II v. Brumberg, Mackey & Wall*, No. 4:05-cv-00001, 2006 BL 19215 (W.D. Va. Jan. 6, 2006); *Admiral Merchs. Motor Freight, Inc. v. O'Connor & Hannan*, 494 N.W.2d 261 (Minn. 1992)—but does not by itself create an attorney-client relationship. *Turkey Creek, LLC v. Rosania*, 953 P.2d 1306 (Colo. Ct. App. 1998).

***Description of lawyer's role.*** Courts take into consideration whom the lawyer was described as representing at the time. E.g., *Palmer v. Fox Software, Inc.*, 107 F.3d 415 (6th Cir. 1997) (offering circular identified lawyer as counsel for corporation); *Waggoner v. Snow, Becker, Kroll, Klaris & Krauss*, 991 F.2d 1501 (9th Cir. 1993) (chief executive officer had described lawyer at meeting, in court, and in testimony as attorney for corporation and not for him personally); *Nilavar v. Mercy Health Sys.*, 143 F. Supp.2d 909 (S.D. Ohio 2001) (correspondence referred to lawyer as counsel for corporation); *Ahan v. Grammas*, No. 02-09937, 2004 WL 2724111, 21 Law. Man. Prof. Conduct 4 (Md. Cir. Ct. Nov. 19, 2004) (engagement letter identified corporation as client), cert. denied, 914 A.2d 768 (Md. 2007).

***Nature of entity.*** The greater the overlap between ownership and management, the more likely it is that an individual attorney-client relationship with the constituent will be found. E.g., *Rosman v. Shapiro*, 653 F. Supp. 1441, 1445 (S.D.N.Y. 1987) ("where, as here, the corporation is a close corporation consisting of only two shareholders with equal interests in the corporation, it is indeed reasonable for each shareholder to believe that the corporate counsel is in effect his own individual attorney"). See Restatement § 14 cmt. f (implied attorney-client relationship more likely to be found when "organization is small and characterized by extensive common ownership and management").

***Failure to clarify role.*** The lawyer's failure to clarify the nature of her role in representing the organization may contribute to a reasonable belief that the lawyer represents the individual as well as the organization. E.g., *Home Care Indus., Inc. v. Murray*, 154 F. Supp.2d 861 (D.N.J. 2001); *Wick v. Eismann*, 838 P.2d 301 (Idaho 1992); see Restatement § 14 cmt. f (failure to clarify whom lawyer represents may lead to representation not intended by lawyer).

## Obligation to Clarify Role

Because the entity usually is the client, a corporate director or officer in theory understands that the lawyer represents the corporation and that anything he tells the corporation's counsel is known to the corporation. But in reality constituents may come to expect personal loyalty from the lawyer and believe they may safely confide in her.

**Rule 1.13 requires corporate counsel to explain whom she represents when the lawyer should know that the constituent's interests conflict with those of the organization.**

Therefore, to protect the individuals as well as the organization, Model Rule 1.13(f) requires a lawyer to "explain the identity of the client when the lawyer knows or reasonably should know that the organization's interests are adverse to those of the constituents with whom the lawyer is dealing." See, e.g., *In re Harding*, 223 P.3d 303, 26 Law. Man. Prof. Conduct 102 (Kan. 2010) (city attorney who was feuding with city officials over his pension benefits violated rule by failing to advise them that his representation of city might be adverse to them); see also *Kentucky Bar Ass'n v. Hines*, 399 S.W.3d 750, 29 Law. Man. Prof. Conduct 411 (Ky. 2013) (no proof that corporate counsel who assisted dissident shareholders violated rule).

A lawyer representing an organization must also keep in mind Model Rule 4.3 (communications with unrepresented persons). Under that rule, if the lawyer realizes or should realize that a constituent without separate counsel misunderstands the lawyer's role, the lawyer must make reasonable efforts to correct the misunderstanding.

Unlike Rule 4.3, Rule 1.13(f) does not expressly condition the clarification duty on the constituent's misunderstanding of the lawyer's role. Rather, the black-letter language of Rule 1.13(f) requires a warning whenever the lawyer reasonably should know that the interests of

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the constituent and the organization are adverse. Comment [10] suggests in broader terms that clarification should be provided when the interest of the organization "may be or become adverse."

The Restatement takes the position that a warning is required only when the lawyer should realize that the constituent mistakenly assumes either that the lawyer represents him, that the lawyer will keep their discussions secret within the organization, or that the interests of the constituent and the organization are basically the same. Even then the duty to warn does not apply unless failure to do so would materially prejudice the constituent. *Restatement (Third) of the Law Governing Lawyers* § 103 cmt. e (2000).

## Content of Warning

Opinions vary about what a lawyer may or must say by way of clarification or warning. See Moore, *Conflicts of Interest for In-House Counsel: Issues Emerging From the Expanding Role of the Attorney-Employee*, 39 S. Tex. L. Rev. 497 (1998) (describing variety of viewpoints among lawyers).

Model Rule 1.13(d) itself requires only that the lawyer "explain the identity of the client." Comment [10] goes significantly further, suggesting that counsel advise that the lawyer cannot represent the individual, that the individual may wish to obtain independent representation, and that discussions between the lawyer for the organization and the individual may not be privileged. See also Colorado Ethics Op. 120 (2008) (lawyer should inform constituent that organization is lawyer's client, that conflict of interest may exist between organization and constituent, that lawyer does not represent constituent, that constituent may wish to obtain independent counsel, and that constituent cannot claim attorney-client privilege for communications with lawyer); District of Columbia Ethics Op. 269 (1997) (counsel should make clear that attorney represents corporation and that corporation may waive attorney-client privilege).

The Restatement disputes the suggestions in the comment to Rule 1.13 and maintains that the lawyer need only clarify her role. *Restatement (Third) of the Law Governing Lawyers* § 103 cmt. e (2000).

Lawyers who are conducting internal investigations for a client routinely caution employees that they represent only the corporation and disclaim any attorney-client relationship with the individual. See District of

### Lawyers Usually Are Permitted to Represent Corporate Clients in Actions by or Against Constituents

One of the areas in which the client-identity issue arises most often is litigation brought by the corporation against one or a few of its constituents, or by constituents against the corporation.

A director, officer or shareholder in such an action often seeks the disqualification of the company's counsel on grounds of conflict of interest or use of confidential information imparted to the lawyer by the constituent. Citing the rule that corporate counsel represents the corporation itself rather than the individuals who own and manage it, courts traditionally have held that the company's lawyer is not disqualified from representing the corporation in such a suit, because the constituent is not recognized as a client or former client of the corporate lawyer. E.g., *Cole v. Ruidoso Mun. Sch.*, 43 F.3d 1373 (10th Cir. 1994); *McKinney v. McMeans*, 147 F. Supp.2d 898 (W.D. Tenn. 2001); *Kubin v. Miller*, 801 F. Supp. 1101 (S.D.N.Y. 1992); *Prof'l Serv. Indus., Inc. v. Kimbrell*, 758 F. Supp. 676 (D. Kan. 1991); *Ex parte Tiffin*, 879 So. 2d 1160, 19 Law. Man. Prof. Conduct 582 (Ala. 2003); *Havasu Lakeshore Inv., LLC v. Fleming*, 158 Cal. Rptr.3d 311, 29 Law. Man. Prof. Conduct 392 (Cal. Ct. App. 2013); *Meehan v. Hopps*, 301 P.2d 10 (Cal. Ct. App. 1956); *Talvy v. Am. Red Cross in Greater New York*, 618 N.Y.S.2d 25 (N.Y. App. Div. 1994), aff'd, 661 N.E.2d 159 (N.Y. 1995); *Stanley v. Bobeck*, No. 92630, 25 Law. Man. Prof. Conduct 613 (Ohio Ct. App. Oct. 29, 2009); see also Pennsylvania Ethics Op. 97-12 (1997) (lawyer who represented one of two stockholders of closely held corporation and may have represented corporation as well may represent stockholder and corporation against other stockholder); cf. *Ferranti Int'l PLC v. Clark*, 767 F. Supp. 670 (E.D. Pa. 1991) (law firm is not disqualified from representing corporation in action against corporation's former corporate counsel, who originally hired firm).

For the same reason, an organization's counsel generally is not disqualified from representing a third person who is adverse to a constituent of the organization. Where no express or implied attorney-client relationship exists between the lawyer and the constituent, the constituent is not a client or former client for conflict of interest purposes. *Havasu Lakeshore Inv., LLC v. Fleming*, supra; *Responsible Citizens v. Superior Court*, 20 Cal. Rtpr.2d 756 (Cal. Ct. App. 1993); *Greate Bay Hotel & Casino, Inc. v. City of Atlantic City*, 624 A.2d 102 (N.J. Super. Ct. Law Div. 1993).

A lawyer is not disqualified from representing someone in a lawsuit against a corporation merely because it has the same officers and/or directors as another corporation represented by the lawyer. See *McCarthy v. John T. Henderson, Inc.*, 587 A.2d 280 (N.J. Super. Ct. App. Div. 1991) (law firm not disqualified from representing plaintiffs in action against close corporation that had same officers and shareholders as another close corporation that law firm previously represented); Arkansas Ethics Op. 97-2 (1997) (law firm that represents corporate client may represent another client against second corporation whose officer is also member of corporate client's board).

The distinction between the corporate entity and its owners and managers takes on special significance in shareholders' derivative actions. The potential for conflicts of interest in that scenario is beyond the scope of this article.

Columbia Ethics Op. 269 (1997) (warning required in internal investigations whenever possible adversity exists, as when individual was more than passive observer of some act or omission that may be attributable to corporation and may have been responsible for questioned conduct).

Lawyers conducting internal investigations also routinely inform employees that the corporation, not the employee, controls the attorney-client privilege for the statements made in the interview and that the corporation may choose to waive the privilege and disclose the communications. These cautions—often called "*Upjohn* warnings" for the seminal case on the corporate attorney-client privilege, *Upjohn Co. v. United States*, 449 U.S. 383 (1981)—are essential to prevent the employee from later asserting that the lawyer may not disclose confidences imparted during the interview. The *Upjohn* advisories should be documented in writing to avoid any doubt about whether they were actually given. See *United States v. Ruehle*, 583 F.3d 600, 25 Law. Man. Prof. Conduct 550 (9th Cir. 2009) (court apparently assumed that warnings were not given in absence of documentation; however, officer could not claim privilege because he knew anyway that all factual information would be communicated to third parties).

See ABA WCC Working Group, *Upjohn Warnings: Recommended Best Practices When Corporate Counsel Interacts With Corporate Employees* (July 17, 2009); G. Collins & D. Seide, *Warning the Witness: A Guide to Internal Investigations and the Attorney-Client Privilege* (2011); Brewer, *Ethics of Internal Investigations in Kentucky and Ohio*, 27 N. Ky. L. Rev. 721 (2000).

For an argument that *Upjohn* does not adequately address constituents' interests when they may not be aligned with those of the company during an internal investigation, see Green & Podgor, *Unregulated Internal Investigations: Achieving Fairness for Corporate Constituents*, 54 B.C. L. Rev. 73 (2013) ("Courts need to expand upon the current attorney-client privilege jurisprudence to take account of a corporation's duty to treat its employees fairly and not to exploit them").


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