

COPY

STATE BAR ASSOCIATION OF NORTH DAKOTA ETHICS COMMITTEE
Opinion No. 97 - 02
April 29, 1997

The Ethics Committee has been asked to give its opinion on whether a disqualifying conflict of interest exists between representation of a corporation and representation of one of the two shareholders of the corporation in a divorce from the other shareholder.

FACTS

A husband and wife, each of whom owns 50% of a corporation, are divorcing. One partner in a law firm (Partner A) represents the corporation; another partner in the firm (Partner B) represents the husband in the divorce. The husband had advised Partner A that the corporation had no assets and was "inoperative." There are judgments against the corporation, and the creditors who hold those judgments are said to be in the process of organizing to sue to pierce the corporate veil and to allege that the husband has engaged in fraudulent conveyancing. During the first day of the divorce trial, both partners learned of allegations that the husband had cashed checks made payable to the corporation without depositing those checks in any account of the corporation. The presiding judge recused himself, and the divorce trial was continued to a later date. The requesting attorney asks whether it would be improper for either Partner A or Partner B to continue the representation.

The facts presented to the Committee give no information about the directors, officers, or employees of the corporate client. Nor do the facts presented give information as to the type of work which Partner A did or does for the corporate client or about the contacts which Partner A had or has with the two shareholders during the course of

representing the corporation. The only information given about the corporation is that the two spouses are the only shareholders.

DISCUSSION

Under N.D.R. Prof. Conduct 1.10 (a), which governs imputed disqualification, two lawyers in the same firm cannot knowingly represent a client if either one of them would be prohibited from the representation if practicing alone. Therefore, the Committee considers whether the Rules of Professional Conduct would allow one lawyer to represent both the corporation and the husband in the fact situation presented.

N.D.R. Prof. Conduct 1.13(a) provides that a lawyer employed or retained by an organization represents the organization, "acting through its duly authorized constituents." In representing the corporation, Partner A's duty is to the interests of the corporation. Since a closely held corporation is involved, it is not sufficient simply to conclude that Partner A represents only the corporation and that the corporation is a client completely separate from its shareholders. In applying Rule 1.13 to a closely held corporation, the distinction between the corporate entity and the shareholders "begins to blur," C. Wolfram, Modern Legal Ethics at 42, and it is difficult to separate the interests of the corporation from the interests of its shareholders. Case law supports the general proposition that, when a close corporation is involved, the application of Rule 1.13 must be decided on a case by case basis. One court has noted:

Although, in the ordinary corporate situation, corporate counsel does not necessarily become counsel for the corporation's shareholders and directors, . . . 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 [sic] own individual attorney. Rosman v. Shapiro, 653 F. Supp. 1441 (S.D.N.Y. 1987) (citations omitted).

There must be consideration given to whether Partner A could be considered to represent, or to have represented, either of the spouses during the course of representation of the corporation.

Even if there were no possibility that representation of either the corporation or the husband would be adversely affected if the firm represents both of them, the requesting lawyer must also consider the interests of the wife, since she owns 50% of the corporation. Depending on the wife's position in the corporation (e.g., as officer, director, or employee), and on the contact between Partner A and the wife during the course of Partner A's representation of the corporation, it may be reasonable for the wife to believe that Partner A was, or is, in effect her own individual lawyer.

The rules of professional conduct allow for a lawyer to represent both a corporation and one of its shareholders in certain situations. Rule 1.13 (c) provides:

A lawyer representing an organization may also represent any of its directors, officers, employees, members, shareholders or other constituents, subject to the provisions of Rule 1.7. If the organization's consent to the dual representation is required by Rule 1.7, the consent shall be given by an appropriate official of the organization other than the individual who is to be represented.

Since Rule 1.13(c) allows for representation of both a corporation and a shareholder only if provisions of Rule 1.7 are met, the facts presented must be considered in light of Rule 1.7.

In applying Rule 1.7, one must first determine whether the interests of the corporation and the interests of the husband are adverse. A lawyer for a corporation has a duty to keep the interests of the corporation paramount and to remain neutral in disputes among the shareholders. Woods v. Superior Court of Tulare County, 149 Cal. App.3d 931, ___, 197 Cal. Rptr. 185, 189 (1983). In light of the allegations of misuse of corporate

property, it is the Committee's opinion that the interests of the corporation are adverse to the interests of the husband.

Since there are adverse interests between the corporation and the husband, the Committee next considers whether the adverse interests of the husband and of the corporation constitute a disqualifying conflict under N.D.R. Prof. Conduct 1.7. Both 1.7(a) and 1.7(c) are potentially applicable to the fact situation presented.¹ In determining whether a conflict of interest disqualifies a lawyer from representing a client, Rule 1.7 focuses on the likelihood that the representation will be adversely affected by the conflict.

Rule 1.7(a) prohibits a representation if the representation will be adversely affected by the lawyer's responsibilities to another client. Whether the situation presented rises to the certainty of adverse affect which triggers the application of Rule 1.7(a) cannot be determined from the facts presented to the Committee. If the requesting lawyer determines that representation of the corporation will adversely affect representation of the husband, or that representation of the husband will adversely affect representation of the corporation, Rule 1.7(a) mandates disqualification.

The Committee is of the opinion that if Rule 1.7(a) does not require disqualification, Rule 1.7(c) applies. Under Rule 1.7(c), if the conflict might adversely affect the representation, the representation can be undertaken only if 1) the lawyer reasonably believes the representation will not be adversely affected, and 2) the client gives informed consent to the representation. It is the Committee's opinion that the facts presented in the

¹ Based on the facts presented, Rule 1.7(b), which addresses situations where the lawyer's own interests are likely to adversely affect the representation, does not appear to apply.

request for opinion constitute a conflict which might adversely affect the representation of the corporation, and that client consent is required in order for the firm to represent both the corporation and the husband. Informed consent to that simultaneous representation must be given by the wife under Rule 1.13(c).

The Committee's opinion is supported by case law, and is consistent with ethics opinions of other states. Some courts have disqualified counsel from representing one spouse against the other when that counsel previously served as corporate counsel to the family corporation. See, e.g., Woods v. Superior Court of Tulare County, 149 Cal.App.3d 931, 197 Cal.Rptr.185 (1983) (absent consent, an attorney for a family-owned corporation should not represent one owner against the other in a divorce action); Ethics Advisory Comm., Kansas Bar Ass'n Op. 91-3 (lawyer who represented corporation and served on its board may not represent one shareholder in divorce from other shareholder where second shareholder was active participant in corporation and regarded the lawyer as her individual lawyer) (May 23, 1991); R.I. Sup. Ct., Ethics Advisory Panel, Op. 93-58 (1993) (lawyer who formed a corporation for its two shareholders and served as legal counsel for the corporation may not subsequently represent one shareholder, whom the lawyer has also previously represented in personal matters, in a dispute against the other shareholder regarding the corporation without the other shareholder's consent) ABA/BNA Law. Man. on Prof. Conduct 1001:7824.

The Committee concludes that consent of the wife is required for Partner B to continue to represent the husband. If that consent is not given, the law firm may be unable to continue to represent either the corporation or the husband. Where more than one client

is involved and the lawyer withdraws because a conflict arises after representation, whether the lawyer may continue to represent any of the clients is determined by Rule 1.9.

Comment to Rule 1.7. It is the opinion of the Committee that, under Rule 1.9(b) the law firm may not continue to represent either the corporation or the husband, unless the wife gives informed consent.

CONCLUSION

When one partner in a law firm represents a corporation in which two spouses are each 50% shareholders and there are allegations of misuse of corporate property by one of the spouses, another partner in the law firm cannot represent one of the spouses in their divorce absent consent of the other spouse. Absent consent of the other spouse, the law firm cannot continue to represent either the corporation or one of the shareholder/spouses.

This opinion is provided pursuant to N.D.R. Law. Discipline 1.2(B), which provides:

A lawyer who acts with good faith and reasonable reliance on a written opinion or advisory letter of the ethics committee of the association is not subject to sanction for violation of the North Dakota Rules of Professional Conduct as to the conduct that is the subject of the opinion or advisory letter.

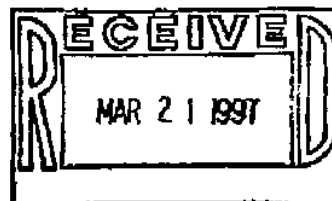
This opinion was drafted by Alice R. Senechal, and was unanimously adopted by the Committee on April 29, 1997.


Alice R. Senechal, Chair

97-02

March 20, 1997

Ms. Alice R. Senechal, Chair
Box 5576
Grand Forks, ND 58206-5576



RE: REQUEST FOR OPINION

Dear Ms. Senechal:

Our firm has a question regarding a hypothetical situation.
hypothetical fact situation is as follows:

The

Law firm represents husband in a divorce and corporation (closely held) in the corporate capacity. Husband and wife each own 50% of the corporation. Partner A represents corporation and partner B represents husband in the divorce. In the course of the litigation, wife has produced copies of checks written out to corporation but cashed by husband. The proceeds of the checks (in excess of \$100,000.00) were not deposited into any account for the corporation and the whereabouts of such money is unknown. Corporation has judgments against it from its creditors which it has failed to pay in excess of \$200,000.00. Partner B did not know of the existence of these checks until the divorce trial started and after one half day, was postponed until a later date. The judgments were entered by the creditors after proper service and upon default. Partner A was aware of the service of the various summons and complaints but was told by husband that the corporation had no assets and was inoperative. Partner A was unaware of the alleged

check cashing. The various creditors who hold judgments have or are in the process of organizing and suing to pierce the corporate veil and to allege fraudulent conveyancing by husband. The trial judge has recused himself after one half day of trial and another judge has been assigned. Trial is to continue in three months. The one half day of trial transcript will have to be prepared anyway for the successor judge.

Do either Partner A or Partner B have a conflict of interest or in any other manner would it be improper for either or both of them to continue representing husband and/or corporation? Thank you for your prompt response to this situation.

Sincerely yours,

