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By John W. Amberg and Jon L. Rewinski

Ethics Roundup 2003

Last year, California's rigorous system of attorney ethics was faced with continued pressure by forces within and outside the state, reflecting public unease about the role of lawyers in recent corporate scandals and the government's war against terrorism. Lawyers were pressured to abandon undivided loyalty to their clients and to become whistle-blowers in the service of a perceived greater public good. The California Legislature passed the first substantive amendment to the state's statutory duty of confidentiality in 131 years, and the American Bar Association and the Securities and Exchange Commission both published rules that, by inviting lawyers to reveal confidential information without their clients' consent,

conflict with California law. California lawyers may face a showdown between the traditional state regulation of attorneys and federal preemption in 2004.

The Duty of Confidentiality

A core value of the legal profession for centuries, and codified in California since 1872, the lawyer's duty of confidentiality received its first substantive change in 2003.¹ The fiduciary duty of confidentiality is not merely aspirational; it is a legal obligation set forth in Business and Professions Code Sections 6000 et seq. and the Rules of Professional Conduct. Breach of this duty may result in liability and professional discipline. Business and Professions Code Section 6068, titled "Duties

of Attorney," states: "It is the duty of an attorney... (e) To maintain inviolate the confidence, and at every peril to himself or herself to preserve the secrets, of his or her client." Under an amendment to Section 6068(e), which will

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go into effect on July 1, 2004, California lawyers will be permitted to reveal "confidential information relating to the representation of a client to the extent that the lawyer reasonably believes the disclosure is necessary to prevent a criminal act that the attorney reasonably believes is likely to result in death...or substantial bodily harm...."²

The sponsors of the amendment justified it on the grounds that 1) it would harmonize Section 6068(e) with Evidence Code Section 956.5, which contains a similar exception to the attorney-client privilege, and 2) it would "bring California in line with every other state in the nation and the ABA Model Rules of Professional Conduct."³ However, the duty of confidentiality is broader than the attorney-client privilege and protects all secrets, not just privileged communications. Also, exceptions to the privilege presume notice to the client, a hearing, and a court order before disclosure.

The American Bar Association also rewrote its Model Rules of Professional Conduct in response to criticism that lawyers

amended ABA Model Rule 1.13 would permit a lawyer for a corporation to reveal confidential information about a violation of a duty to the organization or the law, *without the client's consent*, if the corporation's highest authority failed to act on the information, and the lawyer "reasonably believes that the violation is reasonably certain to result in substantial injury to the organization...."⁶ In California, there is no attorney-client privilege if the lawyer's services are used to commit a crime or fraud, but California law contains no comparable exception to the duty of confidentiality and no counterpart to Model Rule 1.13.

Not by coincidence, the ABA's amendments to the Model Rules were adopted shortly after the effective date of new SEC Rules governing attorney conduct that threatened the legal profession's tradition of self-regulation. Promulgated by the SEC under the Sarbanes-Oxley Act of 2002, the SEC Rules purport to apply to every lawyer "appearing and practicing before the Commission"—a phrase that is defined

ports to shield a lawyer who complies in good faith with the new SEC Rules from liability or discipline by any state.⁹

The new SEC Rules conflict with California law governing the fiduciary duties of attorneys. Neither Section 6068(e) nor the Rules of Professional Conduct recognize an exception to the duty of confidentiality for alleged violations of the securities laws or harm to investors. Under Rule 3-600(A) of the Rules of Professional Conduct, the corporate lawyer's duty of confidentiality is owed to the corporation, not to its directors, officers, or shareholders.¹⁰ When the lawyer knows that an agent of the company is acting in a manner that violates the law or violating the law by refusing to act, Rule 3-600(B) states that the lawyer may take those actions that appear to be "in the best lawful interests of the organization," including urging reconsideration of the matter or referring the matter to higher authority within the organization. Whatever actions are taken, however, Rule 3-600 cautions that the lawyer "shall not violate his or her duty of protecting all confidential information as provided in Business & Professions Code section 6068, subdivision (e)...." If the company's highest authority persists in illegal conduct that is likely to result in substantial injury to the organization, a member of the California bar may not blow the whistle on the client. Under Rule 3-600(C), the lawyer's response "is limited to the member's right, and where appropriate, duty to resign...."

In a public letter to the SEC in August 2003,¹¹ the Corporations Committee of the State Bar's Business Law Section warned that any California lawyer who discloses client confidences in reliance on the new SEC Rules would violate California law and expose themselves and their clients to substantial risks. The SEC did not respond but took the position in a public comment to the Washington State Bar Association that state law is preempted by the SEC Rules.¹²

The Duty of Loyalty

Another core value of the legal profession is the duty of undivided loyalty to the client.¹³ As the California Supreme Court stated a decade ago, a client is entitled to a lawyer's undivided loyalty as the client's advocate and champion throughout the engagement.¹⁴ This past year, the Fourth District Court of Appeal reaffirmed the duty of undivided loyalty in a new context.

In *Hernandez v. Paicius*,¹⁵ the plaintiff sued his doctor for medical malpractice. The law firm defending the doctor also represented the plaintiff's medical expert in an ongoing disciplinary proceeding and previously had represented the expert in several malpractice

(Continued on page 34)

The challenge to traditional notions of loyalty and confidentiality continued unhaltingly in 2003

were complicit in recent corporate scandals by failing to blow the whistle at Enron, Worldcom, Tyco, and other companies. Although the ABA Model Rules are not binding in California, they may provide guidance.⁴ As amended, ABA Model Rule 1.6 would permit a lawyer to reveal confidential information *without the client's consent* if the lawyer reasonably believes disclosure is necessary "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 if the lawyer does not discover the crime or fraud until after the act was committed, "to prevent, mitigate, or rectify" the financial injury.⁵ Furthermore,

broadly,⁷ SEC Rule 205.3(d) (2) would permit a lawyer for a corporate issuer to reveal to the SEC, *without the client's consent*, confidential information under three circumstances in which the attorney reasonably believes disclosure is necessary: 1) to prevent the company from committing a material violation of the securities laws likely to cause substantial injury to the financial interest or property of the company or its investors, 2) to prevent the company from committing perjury, suborning perjury, or perpetrating a fraud on the SEC, or 3) to rectify a material violation that caused or may cause substantial injury to the finances or property of the company or investors, and in furtherance of this violation the lawyer's services were used.⁸ In an attempt to preempt state regulation, SEC Rule 205.6 pur-

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Marion County Superior Court
(Indianapolis)

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18th Judicial Circuit

MISSISSIPPI

4th Circuit Court

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105th District Court (Corpus Christi)
133rd District Court (Houston)
219th District Court (McKinney)
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The Los Angeles County Bar Association certifies that this activity has been approved for Minimum Continuing Legal Education legal ethics credit by the State Bar of California in the amount of 1 hour.

1. The duty of confidentiality, a core value of the legal profession, has been codified in California since 1872.

True.
False.

2. Under California law, a lawyer must "maintain inviolate the confidence, and at every peril to himself or herself to preserve the secrets, of his or her client."

True.
False.

3. The amendment to Code of Civil Procedure Section 6068(e) will require a lawyer to reveal confidential client information if the lawyer reasonably believes the disclosure is necessary to prevent a criminal act that the lawyer reasonably believes is likely to result in death or substantial bodily harm.

True.
False.

4. The attorney conduct rules promulgated by the Securities and Exchange Commission under the Sarbanes-Oxley Act are consistent with California's Rules of Professional Conduct.

True.
False.

5. The duty of loyalty prohibits lawyers from attacking their clients during cross-examination at trial, even if the examination is based on public information.

True.
False.

6. The duty of loyalty is codified in a California statute.

True.
False.

7. Ordinarily, a lawyer owes no professional duties to nonclients.

True.
False.

8. A communication between a lawyer and a non-client may give rise to a duty of confidentiality even if no attorney-client relationship is formed.

True.
False.

9. An attorney for an insurance carrier may not misrepresent the nature of the coverage of the carrier's insured to opposing parties.

True.

False.

10. A law firm may represent a party in a lawsuit brought against a current client of the firm if the client gave its informed written consent in advance to the conflict of interest.

True.
False.

11. Procedures put in place by a law firm to screen confidential client information from other lawyers in the firm may be effective to rebut the presumption that one lawyer's knowledge of confidential information is imputed to all lawyers within the firm.

True.
False.

12. A lawyer may not accept employment adverse to a former client, absent informed written consent by both clients, if the lawyer obtained confidential information in the prior engagement that is material to the new engagement.

True.
False.

13. Regarding successive engagements, an attorney's possession of confidential information is presumed if there is a substantial relationship between the former and the present representations, and the relationship of the attorney and the former client is such that confidential information material to the current representation normally would have been imparted to the attorney.

True.
False.

14. The award of an arbitration panel will not be disturbed if a party cannot point to any particular impact on the award as a result of the opposing lawyer's alleged conflict of interest.

True.
False.

15. A lawyer is prohibited from communicating with a party that the lawyer knows or should know is represented by another lawyer.

True.
False.

16. When a corporation is represented by counsel, officers, directors, and managing agents of the corporation are "represented parties" under Rule 2-100 of the Rules of Professional Conduct.

True.
False.

17. After a lawyer withdraws from representing a client, the lawyer may not recover his or her contingent fee.

True.
False.

18. A lawyer who is disqualified due to a conflict of interest in violation of the Rules of Professional Conduct may be paid for services actually rendered.

True.
False.

19. A lawyer who agrees to mediate a dispute between his or her client and another party may act as an advocate for the client.

True.
False.

20. An attorney may enter into a business transaction with a client if the terms are fair and reasonable to the client, even if the client does not consent in writing.

True.
False.

MCLE Answer Sheet #124

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| 17. | <input type="checkbox"/> True | <input type="checkbox"/> False |
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| 19. | <input type="checkbox"/> True | <input type="checkbox"/> False |
| 20. | <input type="checkbox"/> True | <input type="checkbox"/> False |

actions. During cross-examination at trial, the defendant's lawyer attacked the expert's competence, integrity, and reputation. In her closing argument, the defendant's lawyer described the plaintiff's expert as a "liar" who "had the guts to come in here and lie to you [the jury]."

The Fourth District Court of Appeal reversed judgment for the defendant. In a strongly worded opinion, the court of appeal concluded that the defendant's lawyer had "demonstrated a dulled sensitivity to professional ethics and engaged in an egregious and shocking breach of her duty of loyalty to [her firm's client, the plaintiff's expert]."¹⁶ The court reached this result even though much, if not all, of the lawyer's cross-examination was based on publicly available information. Nevertheless, the court declared that "[t]he spectacle of an attorney skewering her own client on the witness stand in the interest of defending another client demeans the integrity of the legal profession and undermines confidence in the attorney-client relationship."¹⁷

A lawyer facing this dilemma should find a remedy before trial—perhaps a written waiver by both clients, or the retention of separate counsel (with appropriate screening mechanisms in place to ensure the absence of any conflict) to examine the witness.¹⁸ If the dilemma is not resolved by the time the expert/client testifies, the trial court must declare a mistrial because of an insuperable obstacle to going forward: a lawyer with two clients in a situation in which the lawyer can be loyal only to one.¹⁹

Duties to Potential Clients and Nonclients

Under what circumstances does a lawyer's conduct create a duty of competence, loyalty, or confidentiality to nonclients? During 2003, three courts of appeal and the State Bar's Committee on Professional Responsibility and Conduct (COPRAC) analyzed these issues.

Generally, a lawyer has no professional obligation to nonclients for the consequences of the lawyer's professional negligence,²⁰ although this rule is subject to certain limited exceptions when a nonclient was the intended beneficiary of the lawyer's services.²¹ In *Moore v. Anderson Zeigler Disharoon Gallagher & Gray*,²² a lawyer prepared an amended estate plan that dramatically altered the distribution of the client's property among the client's nine children. The client executed the amended plan two days before his death. After expensive litigation among themselves, some of the children sued their deceased father's lawyer for legal malpractice, claiming that the lawyer had failed to evaluate their

father's testamentary capacity.

The First District Court of Appeal affirmed judgment on demurrer for the lawyer, holding that a lawyer preparing a will for the testator owes no duty to beneficiaries to ascertain and document the testamentary capacity of the client.²³ The court noted that the crux of the dispute was the testamentary capacity of the client rather than the draftsmanship of the amended estate plan itself.²⁴ The court expressed its reluctance to impose on the lawyer an obligation to evaluate his client's capacity, because that obligation would be inconsistent with the lawyer's existing duty of undivided loyalty to the client and would impose "an intolerable burden" on lawyers.

The Second District Court of Appeal considered whether a lawyer representing one spouse owed a duty to advise the other spouse of his rights arising from a wrongful death action involving the couple's child. In *Hall v. Superior Court*,²⁵ the couple's two-year-old daughter drowned in a swimming pool at the home of her paternal grandmother. The little girl's father was present at the time of the drowning, but the mother was not. The couple separated, and the mother sued her estranged husband's mother for wrongful death. The father demanded that his wife drop the lawsuit and threatened to file for divorce if his estranged wife continued with this "evil thing." The wife ultimately settled the wrongful death claim for \$210,000, and the judgment was paid by the grandmother's homeowner's insurance carrier.

When the estranged husband learned the insurer would pay the settlement, he sued his wife and her lawyer to get a portion of the settlement for himself. He contended that his wife's lawyer had a duty to advise him that the claim would likely be covered by his mother's homeowner's insurance and, as an heir, he would be entitled to a portion of any proceeds. The trial court denied the attorney's motion for summary judgment, but the Second District Court of Appeal reversed, concluding that under the circumstances of this case—the wife's lawyer never consulted with the husband, and the husband never contacted the wife's lawyer—the wife's lawyer owed no duty to the husband to discuss the husband's legal rights.²⁶

When representing an organization, a lawyer must communicate with the organization's employees. Whether the lawyer also represents the employees was addressed by the Fourth District Court of Appeal in *Koo v. Rubio's Restaurants, Inc.*²⁷ The plaintiffs in *Koo* filed a putative class action for overtime wages against Rubio's Restaurants on behalf of Rubio's salaried assistant and general managers. The plaintiffs' counsel sought to inter-

view the managers, and defense counsel filed declarations stating that he represented both the restaurant and its managers. Based on the declarations, the plaintiffs' counsel successfully moved to disqualify the defense attorney for purporting to represent both the plaintiffs and the defendant in the same litigation. The court of appeal reversed, holding that the defense attorney's unilateral declaration regarding representation could not, by itself, create an attorney-client relationship when none otherwise existed.²⁸ There was no evidence suggesting that any of the managers agreed to be represented by defense counsel in their individual capacities, and there is a distinction between communicating with corporate managers in their representative capacities and in their individual capacities.²⁹

In Formal Opinion 2003-161, COPRAC considered whether a lawyer owes professional duties to nonclients who ask legal questions in casual settings. The committee opined that even if a formal attorney-client relationship is not formed, the lawyer will be obligated to treat a communication as confidential if 1) the speaker was seeking representation or legal advice and, under the totality of the circumstances, the speaker had a reasonable belief that the attorney was willing to be consulted in his or her professional capacity, and 2) the speaker provided information to the attorney in confidence. Of critical importance in assessing the speaker's reasonable belief are the statements and conduct of the attorney. If the attorney explicitly tells the speaker, before the speaker discloses any private information, that the attorney will not represent the speaker, the duty of confidentiality should not attach, even if the speaker thereafter discloses confidential information. But if the attorney listens to the speaker's story without protest and the client discloses private information, the duty to maintain the information in confidence probably will attach.

Business Transactions with Clients and Collecting Fees

In *Rus, Miliband & Smith v. Conkle & Olesten*,³⁰ an accounting firm hired a law firm on a contingency fee basis to sue its malpractice insurer. After the accounting firm asked its lawyers for a written explanation of the basis for the lawsuit, the lawyers moved to withdraw over the objections of their client, citing a "breakdown in communications." The accounting firm retained new counsel and ultimately settled the claim against the carrier for a sizeable sum. When the original lawyers who had withdrawn demanded a portion of the settlement proceeds based on the services they had provided, the accounting firm filed a declaratory relief action against the lawyers. The trial court granted summary

judgment for the accounting firm.

The Fourth District Court of Appeal affirmed. The rules on recovery after a separation between client and lawyer in a contingency case depend on who wanted to terminate the relationship and why. If the lawyer withdraws from the engagement without the client's consent, recovery depends on whether the lawyer had "justifiable cause" for withdrawal. Under the circumstances, the court of appeal concluded that the lawyers had no reasonable justification for withdrawing and so were precluded from withdrawing *and* retaining a quantum meruit claim on any contingent recovery.³¹

Similarly, a lawyer disqualified due to a conflict of interest in violation of the Rules of Professional Conduct may not recover for services rendered. In *A. I. Credit Corporation, Inc. v. Aguillar & Sebastinelli*, the First District Court of Appeal held that when a lawyer does not appeal his or her disqualification, the order is collateral estoppel on the issue of ethical breach.³²

In *Fletcher v. Davis*,³³ a lawyer sued his former client, a corporation, and others to recover legal fees and expenses the lawyer incurred in representing the client in litigation with its landlord. To secure payment of the lawyer's fees and costs, the former client, through its president, had orally agreed to provide the lawyer with a lien on any judgment. There was no written retainer agreement. The client discharged the lawyer and retained new counsel, who ultimately obtained a \$500,000 judgment, which was distributed to the former client's new lawyer and other judgment creditors. The lawyer sued his former client, the new lawyer, and others who received proceeds from the judgment, alleging that all defendants were on notice of his lien. The trial court dismissed the action on demurrer, ruling that the plaintiff could not plead facts showing perfection of his lien or that the third parties had knowledge of the lien.

In an opinion that was subsequently depublished, the Second District Court of Appeal affirmed. The court of appeal held that the trial court had erred in ruling that the lawyer's lien had to be in writing. The California Supreme Court has granted review on this issue of first impression, which is, according to the court of appeal, "admittedly a close one [in which] reasonable justices, lawyers and scholars could, and do, arrive at different conclusions."³⁴

When a lawyer enters into a business transaction with a client, he or she must comply with Rule 3-300 of the Rules of Professional Conduct.³⁵ In *BGJ Associates, LLC v. Wilson*,³⁶ an individual retained a lawyer to file a declaratory relief action for a prescriptive easement over a parcel of property owned by a rail-

road. The railroad offered to settle by selling the parcel at issue as well as another parcel. The lawyer and a friend were interested in participating in this investment and, together with the client, the three formed an oral joint venture to acquire the property.

The client retained new counsel to evaluate his rights and ultimately purchased the property with different partners. His first lawyer sued the former client for breach of oral contract and other contractual and tort claims. The court concluded that the lawyer had violated Rule 3-300 and, therefore, the alleged joint venture was voidable at the election of the client.

The Second District Court of Appeal affirmed, holding that the lawyer had failed to disclose in writing all of the proposed transaction's terms (Rule 3-300(A)) and to obtain the client's informed written consent (Rule 3-300(C)). Furthermore, the oral joint venture was unfair to the client. The court rejected the lawyer's contention that Rule 3-300 should not be applied once the client retains independent counsel.

Conflicts of Interest

In *Visa U.S.A., Inc. v. First Data Corporation*,³⁷ the federal district court in San Francisco approved the use of both a prospective conflict waiver and an ethical screen by a law firm that concurrently represented the plaintiff in the lawsuit and the defendant in a separate matter. First Data moved to disqualify its lawyers from representing its adversary, Visa, under Rule 3-310(C) of the Rules of Professional Conduct, but the district court denied the motion because First Data had signed an advance waiver of all future conflicts of interest between the parties. Interestingly, the case involved Heller Ehrman White & McAuliffe LLP, the same law firm whose prospective waiver was approved in a seminal 1995 case, *Zador Corporation N.V. v. Kwan*.³⁸

In 2001, First Data sought to retain Heller Ehrman's Silicon Valley office to represent it in a patent infringement action. Heller Ehrman informed First Data that it had a longstanding relationship with Visa, and as a condition of the engagement, First Data agreed to permit Heller Ehrman to represent Visa in any future litigation between First Data and Visa. The firm promised it would not represent Visa if it possessed confidential information of First Data relating to the dispute and would use screening mechanisms to prevent its lawyers representing Visa from communicating with firm lawyers working with First Data about the separate engagements. In 2002, Visa retained Heller Ehrman's San Francisco office to sue First Data for trademark infringement and breach

of contract.

In support of its motion to disqualify Heller Ehrman, First Data argued that it did not knowingly consent to the waiver, but the court held that advance waivers are permitted under California law even if the waiver does not state the exact nature of the future conflict. First Data's claimed ignorance was not credible because it was a sophisticated user of legal services and had contemplated the possibility of litigation with Visa when it engaged Heller Ehrman. The language in the firm's advance waiver was more explicit than blanket waivers upheld in other cases, the court noted, and having received a valid prospective conflict waiver, the firm did not breach its duty of loyalty. The court also held that Heller Ehrman had rebutted the presumption that knowledge of First Data's confidential information is imputed to all lawyers in the firm by showing that screening procedures had been timely implemented.³⁹

The duty to avoid conflicts of interest in successive engagements was the subject of *Jessen v. Hartford Casualty Insurance Company*.⁴⁰ Rule 3-310(E) provides that, absent informed written consent by both clients, a lawyer may not accept employment adverse to a former client if the lawyer obtained confidential information in the prior engagement that is material to the new engagement. Jessen sued his insurer, Hartford Casualty Insurance Company, for bad faith denial of coverage, and Hartford moved to disqualify Jessen's lawyer on the ground the lawyer had represented Hartford in coverage matters at the lawyer's previous law firm. The trial court denied the motion, ruling it was barred by collateral estoppel because Hartford had unsuccessfully tried to disqualify the same lawyer in two prior cases. The Fifth District Court of Appeal reversed, noting that the lawyer had worked on 17 coverage opinions or lawsuits for Hartford at the former firm, and remanded the case for rehearing under the substantial relationship test.⁴¹

Citing *H. F. Ahmanson & Company v. Salomon Brothers, Inc.*,⁴² the *Jessen* court noted that the attorney's possession of confidential information will be presumed when a substantial relationship is shown to exist between the former and the present representations, and when the relationship of the lawyer to the former client is such that confidential information material to the current dispute normally would have been imparted to the attorney. Unfortunately, the court's definition of "substantial relationship" is cumbersome: "[S]uccessive representations will be 'substantially related' when the evidence before the trial court supports a rational conclusion that information material to the evaluation, prosecution, settlement or accom-

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plishment of the former representation given its factual and legal issues is also material to the evaluation, prosecution, settlement or accomplishment of the current representation given its factual and legal issues.⁷⁴³ As the court admitted, this "is anything but a 'bright line' standard."⁷⁴⁴

In *Pour Le Bebe, Inc. v. Guess, Inc.*,⁴⁵ the Second District Court of Appeal refused to vacate an arbitration award, even though it found that the appellant had been denied a full hearing before the arbitration panel on its claim that the attorneys for the opposing party had a conflict of interest and had breached their duty of loyalty. *Pour Le Bebe* (PLB) moved to disqualify the law firm of Mitchell, Silberberg & Knupp, arguing that Mitchell, Silberberg represented PLB in other matters at the same time it represented Guess, Inc., in violation of Rule 3-310(C), and that due to Mitchell, Silberberg's past representation of PLB, the lawyers also had obtained confidential information substantially related to the issues in the arbitration in violation of Rule 3-310(E). Indeed, Mitchell, Silberberg had requested a conflict waiver, but PLB refused to sign it.

The arbitrators summarily denied PLB's motion to disqualify based on insufficiency of evidence, denied a subsequent request for further evidence and a full evidentiary hearing, and denied a later motion for reconsideration based on newly discovered evidence that, according to PLB, contradicted the lawyers' representations to the panel. Although the court of appeal concluded that PLB never had an opportunity to discover and reveal the alleged conflict of interest in the arbitration, it affirmed the award because PLB failed to point to any particular impact Mitchell, Silberberg's continued representation of Guess had on the material issue or the arbitrator's award.

Fraud Against Third Parties

During 2003, courts also considered a lawyer's liability to nonclients for fraud. There is no mystery here. The decision in *Shafer v. Berger, Kahn, Shafon, Moss, Figler, Simon & Gladstone* confirms that a lawyer who commits actual fraud in his or her capacity as a lawyer when dealing with a third party is not relieved of liability.⁴⁶

In *Shafer*, the lawyers for the insurance carrier of the defendant in the underlying case represented to the plaintiffs that the insurance policy excluded coverage for willful acts and that the carrier had reserved a right to deny coverage when it accepted the defendant's tender of the defense of the underlying lawsuit. This was false. In fact, to avoid the expense of *Cumis* counsel, the carrier had amended the reservation of rights letter

to provide coverage for willful acts.

The plaintiffs sued the carrier's lawyers for fraud. The court of appeal reversed judgment for the defendant lawyers on demurrer, ruling that the reliability and trustworthiness of attorney representations constitute an important component of the efficient administration of justice. A lawyer's representations have long been invested with a particular expectation of honesty and trustworthiness.⁴⁷ The court observed that deceit undermines the administration of justice.

Similarly, a lawyer who serves as a mediator may not defraud the mediating parties even though he does not represent them as a lawyer. In *Furia v. Helm*,⁴⁸ a lawyer representing a couple in their dispute with a contractor over a remodeling project offered to mediate the dispute. To encourage the general contractor to use him as the mediator, the lawyer told the general contractor in writing that he would "attempt to fairly mediate" the dispute "rather than advocate" for his clients. At the same time, the lawyer wrote the homeowners that he was "not going to be truly neutral during our efforts to negotiate an agreement....[B]e assured that I will not disclose any communications between us that are expected to be confidential."

The mediation was unsuccessful. After litigation with the homeowners, the general contractor sued the lawyer for legal malpractice and misrepresentation, and the trial court sustained demurrers to the complaint without leave to amend. The First District Court of Appeal concluded that the general contractor had adequately alleged both the existence of a duty to act as a neutral mediator and a breach of that duty.⁴⁹ Reluctantly, however, the court affirmed the judgment because the general contractor's claim that he was "placed in a strategic disadvantage" in the litigation was too conclusory.⁵⁰ As noted in *Furia*, an offer by a lawyer for a party in a dispute to act as a neutral mediator is fraught with peril, if not ethically improper, because of conflicts of interest.⁵¹

Communication with a Represented Party

In *Snider v. Superior Court*,⁵² the plaintiff's lawyer was disqualified after contacting two of the defendant's employees. The trial court held that the lawyer violated Rule 2-100 of the Rules of Professional Conduct, which prohibits a member of the State Bar from communicating directly or indirectly with a party the member knows to be represented by another lawyer. The Fourth District Court of Appeal reversed, in a scholarly decision. The employees contacted by the lawyer—a sales manager and a director of production—were not "represented parties" under Rule 2-

100 because they were not officers, directors, or managing agents of the organization. Also, the subject matter of the communications did not consist of acts or omissions that could be binding on the company. Moreover, the persons contacted were not employees whose statements might constitute admissions by their employer. Finally, there was no evidence the employees had any privileged information.

Advice by Lawyers to Commit a Violation of Law

In *Hetos Investments, Ltd. v. Kurtin*,⁵³ the plaintiff borrowed money from the defendant to fund a real estate project. The parties negotiated the terms of the promissory note directly, without the involvement of their counsel. At the defendant's request, and after the parties completed their negotiation, the plaintiff's lawyers prepared a promissory note memorializing the terms of the loan. When the project failed, the plaintiff asserted a claim against the defendant for usury, based on the promissory note prepared by the plaintiff's counsel. The defendant moved to disqualify the plaintiff's lawyers, arguing that if the allegations were true, the lawyers had advised the plaintiff to commit a violation of law—specifically, the law against usury—in violation of Rule 3-210 of the Rules of Professional Conduct, which provides: "A member shall not advise the violation of any law...unless the member believes in good faith that such law...is invalid." The trial court denied the disqualification motion, and the Fourth District Court of Appeal affirmed.

The court reasoned that if there was a violation of the law in this case, the defendant, not the plaintiff, was the violator by charging interest at a usurious rate. The defendant conceded that the plaintiff's lawyers had not advised him in connection with the preparation of the note and, therefore, the court held, they did not violate Rule 3-210.⁵⁴ The court's reasoning assumes that Rule 3-210 is limited to advice rendered to clients, although the rule does not use the word "client."

Preemption of Ethical Standards

Last year, both state and federal district courts held that California's Ethics Standards for Neutral Arbitrators in Contractual Arbitration were preempted. The standards that 1) require appointed arbitrators to disclose potential conflicts of interest and 2) set forth procedures for disqualification⁵⁵ were challenged by NASD and the New York Stock Exchange—two "self-regulatory organizations" (SRO) that conduct securities arbitrations. In *Mayo v. Dean Witter Reynolds, Inc.*⁵⁶ and *Wilmot v. McNabb*,⁵⁷ the federal district courts held that the California standards are

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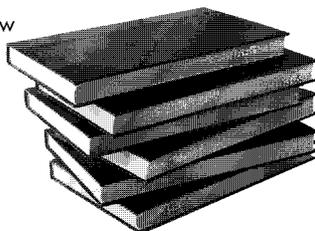
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preempted by the Securities and Exchange Act of 1934 and the Federal Arbitration Act. In *Jevne v. Superior Court*, the Second District Court of Appeal held that the California standards are preempted by SRO arbitration rules and procedures to the extent they were approved by the SEC.⁵⁸

During 2004, many of these 2003 ethics developments are likely to be reflected in the work of the State Bar's Commission for the Revision of the Rules of Professional Conduct. The commission is continuing its multiyear task of reviewing and, where necessary, rewriting California's ethics rules.⁵⁹ ■

¹ The duty was originally codified in 1872 as Code of Civil Procedure §282(5). It is currently codified as Business and Professions Code §6068(e), and this section was modified by AB 1101, which was signed by Governor Gray Davis on October 10, 2003.

² BUS. & PROF. CODE §6068(e)(2) (effective July 1, 2004).

³ Assembly Committee on Judiciary, Synopsis of Proposed Consent (AB 1101).

⁴ State Comp. Ins. Fund v. WPS, Inc., 70 Cal. App. 4th 644, 655-56 (1999).

⁵ MODEL RULES OF PROF'L CONDUCT R. 1.6(b)(2), (3).

⁶ MODEL RULES OF PROF'L CONDUCT R. 1.13(c)(1), (2).

⁷ 17 C.F.R. §205.2(a).

⁸ 17 C.F.R. §205.3(d)(2)(i), (ii), (iii).

⁹ 17 C.F.R. §205.6(c).

¹⁰ RULES OF PROF'L CONDUCT R. 3-600(A); Skarbrevik v. Cohen, England & Whitfield, 231 Cal. App. 3d 692 (1991).

¹¹ Letter from the State Bar of California, Business Law Section, Corporations Committee, to Giovanni P. Prezioso, General Counsel, Securities and Exchange Commission (Aug. 13, 2003).

¹² Public statement in Letter from Securities and Exchange Commission to Washington State Bar Association (July 23, 2003).

¹³ The duty of loyalty is codified in the phrase "[t]o maintain inviolate the confidence...of his or her client" in Business and Professions Code §6068(e).

¹⁴ Flatt v. Superior Court, 9 Cal. 4th 275 (1994).

¹⁵ Hernandez v. Paicius, 109 Cal. App. 4th 452 (2003).

¹⁶ *Id.* at 466.

¹⁷ *Id.* at 467.

¹⁸ The court of appeal stated that disqualification is not always the appropriate remedy. *Id.* at 467.

¹⁹ *Id.* at 468.

²⁰ Moore v. Anderson Zeigler Disharoon Gallagher & Gray, 109 Cal. App. 4th 1287, 1294 (2003).

²¹ See, e.g., Lucas v. Hamm, 56 Cal. 2d 583 (1961) (holding that intended beneficiaries of a will whose bequests were denied because of negligent drafting could assert a claim for malpractice against the drafting lawyer) and Heyer v. Flaig, 70 Cal. 2d 223 (1969) (holding that the daughters of the decedent, whose bequests were denied because of the lawyer's negligence in drafting the will, could assert a claim for malpractice against the lawyer).

²² Moore, 109 Cal. App. 4th 1287, 1294.

²³ *Id.* at 1298.

²⁴ *Id.* at 1299. The court also examined several *Bikania* factors, including 1) the extent to which the transaction was intended to affect the nonclient, 2) the foreseeability of harm to the nonclient, 3) the degree of certainty that the nonclient suffered injury, 4) the closeness of the connection between the lawyer's conduct and the injury suffered, 5) the moral blame attached to the lawyer's conduct, and 6) the policy of preventing future