Ethical Quandaries Associated With Franchise Representation

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I. INTRODUCTION

Franchisors and franchisees often seek counsel from lawyers in part due to their well-honed ability to problem solve and communicate. In the context of everyday life, lawyers are indeed oftentimes the most capable problem solvers, draftsmen, authors and speakers. Ethical considerations that arise in the context of representing franchisors and franchisees, however, can limit counsel’s ability to problem solve by jurisdiction, and can otherwise limit the parties to whom counsel are authorized to communicate as well as what kind of advice, if any, they can provide.

This paper reviews ethical limitations on franchise counsel’s ability to provide advice in the world of a continuously evolving multijurisdictional economy, and limitations on how counsel must communicate when engaging in multi-party representation. It next examines ethical considerations and potential pitfalls inherent in communicating with clients, officers, directors and employees in the context of internal investigations and further ethical limitations and pitfalls presented following the completion of a report on an internal investigation. Finally, the paper briefly highlights counsel’s ethical limitations with respect to communications with existing and former client employees, opposing counsel and the government.

Inasmuch as the foundation beneath the body of law governing these issues is long-established, the changes in the franchise economy, franchise regulatory environment and increasingly transient employment environment underscore the fact that the law also continues to evolve and develop. Yet, like the foundation of ethics jurisprudence, the importance of staying current on how developments impact the representation of franchisors and franchisees as well as vigilant on compliance remains unchanged.

II. MULTIJURISDICTIONAL PRACTICE

In the United States, the regulation of the legal profession has historically been a state prerogative. One facet of that regulation has been laws which prohibit the practice of law by any person within a state where the individual is not licensed. These unauthorized practice of law (UPL) provisions apply with equal force to lawyers licensed in other jurisdictions, as well as to nonlawyers.

The one clear line of demarcation is that an out-of-state lawyer may not practice before a court in a state where he or she is not licensed to practice. In these instances, the judiciary serves as the gatekeeper, passing on the fitness and competence of a lawyer to practice in a court where he or she has not been admitted, through motions for admission pro hac vice. This is a well-recognized practice which has grown over the years, and in 1979 received the explicit endorsement of the United States Supreme Court.

\[1\] The authors would like to thank Sara E. Kitaeff, an associate at Witmer, Karp, Warner & Ryan LLP, and Aaron Ginsburg, a summer associate at Bryan Cave LLP, for their tremendous assistance and support in preparing this paper.

\[2\] Leis v. Flynt, 439 U.S. 438 (1979) (allowing an out-of-state lawyer the privilege of appearing upon motion, especially when associated with a member of the local bar, given the high mobility of the bar, and also the trend toward specialization).
While many industries and sectors of our economy increasingly operate on a national basis, largely without consideration of state boundaries, franchising has been particularly affected by this trend. Many franchise systems operate in all or substantially all of the 50 states. They are represented by a mix of in-house lawyers and outside counsel, and sometimes by both, who may be admitted to practice in just one or two states. Similarly, independent associations of franchisees may have a principal office in one state, directors and outside counsel from a number of states, and franchisee members in as many as 50 states. Counsel who represent these kinds of national organizations must have guidance on to what extent they can render services, give advice or provide representation to a client in a state other than the one(s) in which he or she is licensed to practice law. However, in many cases state bar associations did not address this dilemma directly and, except in cases involving other ethical violations, courts also did not provide any specific guidance.

An alarm of sorts was sounded by the decision of the Supreme Court of California in *Birbrower, Montalbano, Condon & Frank, P.C. v. Superior Court of Santa Clara County.* The plaintiff law firm (“Birbrower”) had its principal place of business in New York City. Two of its attorneys, neither of whom had ever been licensed to practice law in the state of California, represented ESQ Business Services, Inc. (ESQ), a California business, which was then in a dispute with Tandem Computers, Inc. (Tandem). The underlying contract between ESQ and Tandem provided that California law would govern the validity, construction, interpretation and enforcement of the rights and duties of the parties.

The Birbrower attorneys traveled from New York to California on several occasions to confer with ESQ. They discussed the dispute, provided strategic advice and met with representatives of Tandem. On one trip to California, the Birbrower counsel interviewed potential arbitrators. They also filed a demand for arbitration against Tandem with the American Arbitration Association offices in San Francisco, California. On another trip, they met with ESQ and its counsel to discuss whether or not to accept a settlement offer that had been tendered by Tandem. The fee agreement between Birbrower and ESQ was amended from a contingent fee of one third of the recovery to a flat fee of $1 million. The dispute between ESQ and Tandem was eventually settled.

ESQ later sued Birbrower for malpractice. A counterclaim for attorney’s fees was filed by the law firm. ESQ alleged that by practicing law without a license in California and by failing to associate with California counsel, Birbrower counsel had violated Section 6125 of the California Business and Professions Code. The trial court granted summary judgment in favor of ESQ, holding that since the law firm was not admitted to practice in California, had not associated with

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3 According to Franchise Times, the top 10 franchise systems, measured by worldwide sales, have 88,900 domestic locations in the aggregate. See http://www.franchisetimes.com/pdf/Top-200-2013.pdf

4 These dilemmas are not confined to the legal profession. The Federation of State Medical Boards recently proposed a model law that would clear the path for doctors licensed in one state to treat patients in another state. The draft legislation would form an interstate compact, which the Federation described as “the biggest change in medical licensing in decades”. The New York Times, June 29, 2014, available at http://nyti.ms/1mwYVqX.

5 949 P.2d 1 (Cal. 1998).
California counsel, and had provided legal services in the state of California, it could not recover compensation for services as an attorney in California.\textsuperscript{6}

The Supreme Court of California stated that the definition of the practice of law did not necessarily depend on or require the unlicensed lawyer’s physical presence in California. Physical presence, the court indicated, was just one factor that would be considered in deciding whether the unlicensed lawyer had violated the UPL provisions. The court did reject the notion that a person automatically practices law in California when he or she “virtually” enters the state by telephone, fax, email or satellite. The court also rejected the notion that an arbitration exception should be created, stating that any such exception was the province of the Legislature. In doing so, the court distinguished \textit{Williamson, P.A. v. John D. Quinn Constr. Corp.}, where a New Jersey law firm was hired to defend a construction arbitration conducted in New York.\textsuperscript{7} The Williamson court noted that an arbitration tribunal is not a court of record, and it relied on a local state bar report which had concluded that representing a client in an arbitration was not the unauthorized practice of law. The California Supreme Court pointed out that the Birbrower firm had not actually conducted an arbitration proceeding, and that the legal fees they sought were for advice, consultation and settlement strategy.

Notwithstanding this forceful and alarming statement of law and policy by the California Supreme Court, in many other jurisdictions, guidance had remained conspicuously lacking. Indeed, one commentator noted in 2005 that the only boundaries that had been well-defined in Kansas were that an unlicensed lawyer cannot establish an office in a state, cannot hold himself or herself out as authorized to practice law in that state and could not appear in court or file papers with the court, without appearing \textit{pro hac vice}.\textsuperscript{8} This commentator observed that the Kansas Supreme Court’s “… broad brush strokes in these contexts… provide no real guidance on multijurisdictional practice and do little to define what it means to practice law in Kansas in the circumstances in which doing so violates the regulation of the legal profession in that jurisdiction.”\textsuperscript{9}

The Birbrower decision was published in January 1998. In July 2000, the President of the American Bar Association (ABA) appointed a Commission on Multijurisdictional Practice (the Commission) with a broad mandate to study the then-current state of the law on multijurisdictional practice, to study the impact of the current rules on in-house lawyers, transactional practitioners, litigators and arbitrators, as well as law firms which maintain offices and engage in the practice of law in multiple jurisdictions, and to make recommendations that would serve the public interest.

\textsuperscript{6} The court's decision resolved only the question of whether the Birbrower firm could recover legal fees against the plaintiff in the malpractice action. It left the underlying malpractice action for the trial court.

\textsuperscript{7} 537 Fed. Supp 613, 616 (S.D.N.Y. 1982); see also Superadio, L.P. v. Winstar Radio Prods., LLC, 844 N.E.2d 246 (2006) (finding Model Rule 5.5(c)(3), not then adopted by Massachusetts, to be persuasive in deciding that a New York lawyer not licensed to practice in Massachusetts did not engage in the unauthorized practice of law by representing a party in a Massachusetts arbitration).


\textsuperscript{9} Id.
Also in 2000, The Restatement (Third) of the Law Governing Lawyers was published.\(^{10}\) This was the first Restatement in this area. It was less an actual restatement of the patchwork of sometimes materially inconsistent state ethical rules on multijurisdictional practice, and more a statement of what the law could or should be. The Restatement included the authority of a lawyer not admitted to practice in a state to provide legal services to a client at a place within such state “... to the extent that the lawyer’s activities arise out of or are otherwise reasonably related to the lawyer's practice ...” within his or her home state, or before a tribunal or administrative agency or the federal government in compliance with requirements for temporary or regular admission to practice before that tribunal or agency.\(^ {11}\) The publication of this Restatement was a positive development for all stakeholders, which set the stage for the work of the Commission.

The Commission issued an Interim Report in November 2001 and a Final Report in June 2002.\(^ {12}\) Its recommendations, reviewed more extensively below, were adopted by the ABA House of Delegates on August 12, 2002.

The Commission described its guiding principle as follows:

… We searched for the proper balance between the interests of a state in protecting its residents and justice system, on the one hand; and the interests of clients in a national and international economy in the ability to employ and retain counsel of choice efficiently and economically.

Noting that the wisdom of UPL provisions had been questioned since the 1960s in light of the changing needs of clients and the evolving nature of law practice, the Commission found that the regulation of legal practice had not kept pace with these developments, as the California Court of Appeal stated in 1998,

In the real world of 1998, we do not live or do business in isolation within strict geopolitical boundaries. Social interaction and the conduct of business transcends state and national boundaries; it is truly global. A tension is thus created between the right of a party to have counsel of his or her choice and the right of each geopolitical entity to control the activities of those who practice law within its borders.\(^ {13}\)

\(^{10}\) Restatement (Third) Of The Law Governing Lawyers (2000).

\(^{11}\) Id. at § 3 (Jurisdictional Scope of the Practice of Law by a Lawyer).


\(^{13}\) Estate of Condon, 65 Cal. App. 4th 1138 (1998) (deciding 11 months after Birbrower that Colorado attorneys representing a Colorado resident who was co-executor of the estate of a California resident had not engaged in the unauthorized practice of law, despite the fact that the Colorado attorneys entered the state of California, both physically and virtually).
Thus, the rationale for the material changes in UPL provisions, embodied in a new Rule 5.5 of the ABA Model Rules for Professional Conduct (Model Rules)\textsuperscript{14} was expressed as follows:

Although client needs and legal practices have evolved, lawyer regulation has not yet responded effectively to that evolution. As the work of lawyers has become more varied, specialized and national in scope, it has become increasingly uncertain when a lawyer’s work (other than as a trial lawyer in court) implicates the UPL law of the jurisdiction in which the lawyer is not licensed. Lawyers recognize that the geographic scope of a lawyer’s practice must be adequate to enable the lawyer to serve the needs of clients in a national and global economy. They have expressed concern that if UPL restrictions are applied literally to United States lawyers who perform any legal work outside the jurisdictions in which they are admitted to practice, the laws will impede the lawyers’ ability to meet their clients’ multistate and interstate legal needs efficiently and effectively.

Of course, the Model Rules have no specific effect on any UPL state provision. However, in the wake of the adoption of new Model Rule 5.5, a number of states have adopted some form of the Model Rule 5.5.\textsuperscript{15} However, many states have tinkered with the language, in some cases, in material ways. Thus, any practitioner must not rely on the Model Rules, but must carefully investigate UPL provisions of any state in which he or she is not licensed.\textsuperscript{16}

A summary of Model Rule 5.5 follows.

\textbf{A. Unauthorized Practice of Law Prohibited}

Model Rule 5.5(a) reaffirms that a lawyer may not practice law in a jurisdiction in violation of the law of that jurisdiction, nor may the lawyer assist anyone else to do so. This Model Rule acknowledges that, based on varying state provisions, a lawyer may be authorized by court rule or order or by applicable law, to practice for a limited purpose on a restricted basis. See Comment 1. The definition of what constitutes the practice of law also varies by jurisdiction. Comment 1 states that the purpose of these provisions is to protect the public from an unqualified lawyer who may not be competent to render advice regarding the laws of a state in which he or she is not licensed.


\textsuperscript{15} The following states have adopted Model Rule 5.5 in its entirety: Arkansas, Arizona, Delaware, Illinois, Iowa, Massachusetts, Nebraska, New Hampshire, Rhode Island, Utah, Vermont, and Washington. Maryland adopted Model Rule 5.5, but made a minor change to the accompanying Comments. See State Implementation of Model Rule 5.5 (prior to the August 2012 and February 2013 Comm. on Ethics 20/20 Revisions), ABA Comm. on Multijurisdictional Practice, Report to the House of Delegates (August 29, 2014), available at http://www.americanbar.org/content/dam/aba/administrative/professional_responsibility/quick_guide_5_5.authcheckdam.pdf.

\textsuperscript{16} See id. (providing a chart tracking state implementation of Model Rule 5.5).
B. Other Prohibitions

Model Rule 5.5(b) recites two other prohibitions on lawyers not admitted to practice in a jurisdiction. First, such a lawyer may not establish an office or other systematic and continuous presence in the jurisdiction for the practice of law. Second, the lawyer may not hold out to the public or represent that he or she is admitted to practice in the jurisdiction. These two prohibitions do not apply to situations where a lawyer may be authorized by law, by order of the tribunal, or by an administrative agency to appear before that tribunal or agency. The Model Rule requires a lawyer to seek admission to a court pro hac vice, if that court’s rules or other applicable law require that he or she do so.

There is generally no specific guidance in the Model Rule or in the Comments as to what constitutes establishing an office or other systematic and continuous presence. However, Indiana, in adopting Model Rule 5.5, added the following sentence to Comment 4: “For example, advertising and media specifically targeted to Indiana residents or initiating contact with Indiana residents for solicitation purposes could be viewed as systematic and continuous presence.” While in clear cases, which often have egregious facts, courts have had little trouble making a determination, there is precious little in the way of specific guidance from other cases where the facts are not so clear or egregious.17

For example, in In the Matter of Towne, a lawyer admitted in Pennsylvania and in the District of Columbia, took the Delaware bar examination, but did not pass. The lawyer then proceeded to open a law office in her home in Delaware, practicing in the area of federal immigration law and personal injury cases. Over a four-year period, the lawyer represented more than 100 Delaware residents in Delaware matters. The lawyer had also been convicted of bribing a federal immigration official and had served 37 months in prison. The Supreme Court of Delaware had little trouble declaring that this attorney should be disbarred.18

In Matter of Scheer, the respondent was licensed to practice in California and Iowa.19 She entered into 28 fee agreements with residents of 12 states other than California and Iowa. She was not registered in any of those states, did not affiliate with any local attorneys in those states, and failed to state in the fee agreements that she was not licensed in states other than California and Iowa. The court found that she had held herself out as licensed to practice law in each of the states. The attorney also collected more than $120,000 in flat fees before fully performing legal services that she had contracted to provide. The case is interesting because the court came to different conclusions as to the attorney’s activities in different states, based on the differing rules in those states. For example, the court found that she had not engaged in the

17 One commentator wrote that “[e]ven if there were a common definition of the practice of law, and the Model Rule was adopted without change in the states, uniformity would still not be assured because the rule, as written, is both open-ended and vague. For example, the rule, identifies certain activities that are permissible and certain activities that are not. The comments expressly recognize, however, that ‘the fact that conduct is not so identified does not imply that the conduct is or is not authorized’. In this vast gray area, it is likely that variance will arise among the states as to what conduct is permissible.” Arthur F. Greenbaum, Multijurisdictional Practice and the Influence of Model Rule of Professional Conduct 5.5 – an Interim Assessment, 43 Akron L. Rev. 729 (2010).

18 929 A.2d 774 (Del. 2007); see also In the Matter of Nadel, 82 A.3d 716 (Del. 2013) (reasoning that an attorney licensed in New Jersey and Pennsylvania, but not in Delaware, established a continuous and systematic presence in Delaware, providing legal services to at least 75 Delaware residents from a Delaware medical office owned by a friend of the lawyer and constituting between 10% and 15% of his law practice).

unauthorized practice in Colorado because that state permitted out-of-state lawyers to provide transactional services, as long as they did not establish a domicile or place for the regular practice of law. However, these safe havens were not available in New Jersey and New York, which led the court to conclude that she had engaged in unauthorized practice of law in those states. The attorney was suspended from the practice of law for two years, and was to remain suspended thereafter until she, among other things, made restitution of all of the flat legal fees that she had charged.

C. Exceptions or Safe Harbors

The real reform in the Model Rule 5.5 is contained within four separate exceptions that are available to a lawyer who is admitted in a jurisdiction, who has not been disbarred or suspended from practice in any jurisdiction, and performs the following activities on a temporary basis. The words “temporary basis” are not defined in the Model Rule or in the comments, and some states have substituted the word “occasional.”

1. Association with Local Lawyer

Model Rule 5.5(c)(1) allows the temporary practice of law in the state, if undertaken in association with a lawyer who is admitted to practice in that jurisdiction and who actively participates in the matter. As Comment 8 makes clear, the lawyer admitted to practice in the jurisdiction must actively participate in and share responsibility for the representation of the client.

2. Reasonably Related to a Pending or Potential Proceeding

Model Rule 5.5(c)(2) permits a lawyer to engage in the temporary practice of law in a state, if the services are reasonably related to a pending or potential proceeding before a tribunal in that state, or in another state. In this instance, the lawyer, or the person assisting the lawyer, must be authorized by law or order to appear in such proceeding, or reasonably expect to be so authorized, typically by admission pro hac vice. Comment 10 specifically lists permissible conduct pursuant to this provision as including meetings with clients, interviews of witnesses, and review of documents. In addition, a lawyer from another jurisdiction can take a deposition in the jurisdiction in connection with a matter pending outside the jurisdiction.

On February 11, 2013, the ABA House of Delegates approved amendments to the ABA Model Rule on Pro Hac Vice Admission. The amendments added a requirement that the lawyer seeking such admission must make any required assessment to the lawyers’ fund for client protection in the state, and pay any application fee required by that state. In addition, the state tribunal considering the application for admission pro hac vice may consider the lawyer’s conduct no matter where the conduct occurs. Finally, the new Model Rule adds new and more


21 In the federal court system, the authority to approve a pro hac vice appearance is consigned to the discretion of the trial court. Accordingly, there is no cognizable property interest within the terms of the 14th Amendment and the United States Constitution does not obligate a court to provide a pro hac vice applicant with procedural due process in passing on an application for permission to appear: Leis, 439 U.S. at 438-45; see also United States District Court v. Ramirez, 320 F. Supp. 2d. 368 (D. Md. 2004) (denying pro hac vice admission where applicant acted with indifference to the licensure requirements of the state, and in numerous instances neglected to prosecute cases resulting in dismissal of the actions to the detriment of her clients).
specific criteria to be applied in assessing an application for admission pro hac vice by a foreign lawyer, including, the legal training, familiarity with the laws of the United States, English language ability of the lawyer and the like.  

3. ADR Proceedings

Model Rule 5.5(c)(3) provides the arbitration exception which the Supreme Court of California declined to create in Birbrower. It permits a lawyer to temporarily represent clients in pending or potential arbitration, mediation, or other alternative dispute resolution proceedings in the jurisdiction or in another jurisdiction. However, these services must arise out of or be reasonably related to the lawyer’s practice in a jurisdiction in which the lawyer is admitted to practice and must be services for which the forum does not require pro hac vice admission. Comment 12 points out that in the case of court-annexed arbitration or mediation, a lawyer may be required to obtain admission pro hac vice, if court rules or law require such admission.

As previously noted, not all states have adopted the Model Rule in its entirety. In the case of the ADR exception, Florida requires out-of-state lawyers to file a statement with the Florida Bar in all domestic arbitration proceedings and pay a $250 fee. Out-of-state lawyers are also limited to three domestic arbitrations in any 365 day period. However, lawyers appearing in international arbitrations are exempted from this provision.

4. Services Arising Out of or Reasonably Related to a Lawyer’s Practice

Model Rule 5.5(c)(4) provides an additional safe harbor for the temporary practice of law in a jurisdiction in which a lawyer is not licensed, if those services arise out of or are reasonably related to the lawyer’s practice in the jurisdiction in which he or she is admitted. The “arise out of a reasonably related to” standard, which appears in this subsection of the Model Rule, as well as in subsection 5.5(c)(3), is an elastic concept. However, Comment 14. lists a number of facts and circumstances that may illustrate the application of those standards. Examples provided include those in which the client may have been previously represented by the lawyer or the client is a resident of or has substantial contacts with the jurisdiction in which the lawyer is admitted. The lawyer’s work may also involve or have significant contacts with the jurisdiction in which the lawyer is admitted. Finally, Comment 14 notes that the services provided by the lawyer may draw on his or her recognized expertise developed with the regular


23 But see Colmar v. Fremantlemedia North America, Inc., 612 N.E.2d 1011 (Ill. Ct. App. 2003). In a matter of first impression, the court was confronted with the fact that the attorney for the successful party in an arbitration held in Illinois was licensed to practice law in California, but not in Illinois. The unsuccessful party sought to void the arbitration decision on that basis. The court, relying on the fact that AAA arbitration rules permit parties to be represented by non-lawyers, and in light of the fact that no Illinois court had ever found that an out-of-state attorney’s participation in arbitration proceedings constitutes the unauthorized practice of law in Illinois, affirmed the award. The court also noted the provisions of Model Rule 5.5, which it found persuasive, despite the fact that they had not been adopted by the state of Illinois.

practice of law on behalf of clients in matters involving a particular body of federal or nationally uniform law. This is standard that can certainly be applied to franchising.

5. **House Counsel Exception**

Model Rule 5.5(d)(1) states that a lawyer admitted in another jurisdiction, or in a foreign jurisdiction, and not disbarred or suspended from practice in any jurisdiction, may provide legal services through an office or other systematic and continuous presence in the jurisdiction to an employer or its organizational affiliates. These services must be those for which the forum does not require admission pro hac vice. Further, in the case of a foreign lawyer who seeks to provide advice based on the law of this jurisdiction or another, the advice must be based on the advice of a lawyer who is admitted to practice in such jurisdiction.25 26

According to one commentator, if in-house counsel to a franchisor travels to a state in which he or she is not admitted to practice, and addresses questions posed by independent contractors or owners of a franchise or other individuals or entities that are not under common control with his or her employer, then under Model Rule 5.5(d)(1) the lawyer would be engaged in the unauthorized practice of law and would not be protected by this exception.27

D. **Services Authorized by Law**

Model Rule 5.5(d)(2) permits a lawyer admitted in another jurisdiction, or in a foreign jurisdiction, and not disbarred or suspended from practice in any jurisdiction to provide services in the jurisdiction on a systematic and continuous basis if those services are authorized by federal or other law or rule. The authority may be derived from statute, court rule, executive regulation or judicial precedent. This portion of the model rule, which the Commission initially proposed relegating to a comment, simply makes clear that “in a jurisdiction that has adopted rules permitting established practice by foreign lawyers who serve as legal consultants, a lawyer may establish a law practice in the jurisdiction if permitted by such a rule.”28

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25 This requirement was added by vote of the ABA House of Delegates on February 11, 2013. See Report 107C, ABA Comm. on Ethics 20/20, Report to the House of Delegates (February 2014).

26 For avoidance of doubt, Comment 15 makes clear that, except as provided in Model Rule 5.5(d), a lawyer who is admitted to practice in another state or foreign jurisdiction and who establishes an office or other systematic continued presence in the jurisdiction, must be admitted to practice law generally in that jurisdiction.

27 Carol A. Needham, *Multijurisdictional Practice Regulations Governing Attorneys Conducting a Transactional Practice*, 2003 U. Ill. L. Rev. 1331 (2003). Professor Needham states as follows: “If one of the states Lawyer A visits, other than Michigan or Nevada, adopted the language of the 2002 amendments to Model Rule 5.5, then Lawyer A would be free to perform legal work for his employer in that state pursuant to the authority granted in Rule 5.5(d)(1). As long as all of the legal questions that he addressed came from managers or other employees at ABC Company, or employees of ABC’s affiliates, he is free to provide legal advice. Note, however, that if the lawyer addresses questions posed by independent contractors, customers, owners of an ABC franchise, or other individuals or entities that are not under common control with ABC, then the language of Rule 5.5(d)(1) would not protect Lawyer A from the charge that his advice to those persons or entities amounts to UPL.”

E. Foreign Lawyers

Model Rule 5.5(e) requires that a foreign lawyer practicing pursuant to the exceptions in Model Rule 5.5(d) “...must be in good standing of a recognized legal profession in a foreign jurisdiction, the members of which are admitted to practice as lawyers or counselors at law or the equivalent, and is subject to effective regulation and discipline by a duly constituted professional body or public authority.”

On February 11, 2013, the ABA House of Delegates approved an amendment to the ABA Model Rule for Registration of In-House Counsel. The amendments require that an application of a foreign lawyer must be accompanied by an English translation if not in English. It also requires any such foreign lawyer to pay any annual client protection fund assessment of the state.29

F. Other Requirements

Comment 19 points out that a lawyer who practices in a jurisdiction in which he or she is not licensed, taking advantage of the provisions of Model Rule 5.5(c) or (d), will be subject to the disciplinary authority of that jurisdiction.30

Some states, while adopting Model Rule 5.5, have added the additional requirement that the out-of-state lawyer must register with the state licensing authority. For example:

- In Connecticut, an out-of-state lawyer practicing under the exceptions set forth in Model Rule 5.5(c) and (d), must (a) notify statewide bar counsel as to each separate matter prior to such representation in the state of Connecticut, (b) notify statewide bar counsel upon termination of each such representation in Connecticut, and (c) pay the fees prescribed by the Judicial Branch.31

- Nevada has enacted a separate rule, which requires private lawyers not admitted to practice in the state who would engage in transactional or extrajudicial matters pending in or substantially related to Nevada, to file an annual report with the State Bar of Nevada and pay a $150 fee. The annual report requires the disclosure, among other things, of the nature of the clients, whether individuals or business entities, for whom the lawyer has provided services that are subject to the rule, and the number and general nature of the transactions performed for each such client during the previous 12 month period. However, the lawyer is expressly prohibited from disclosing

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30 See Model Rule 8.5(a).

the identity of any clients or any information that is
confidential or subject to the attorney-client privilege. 32

- New Jersey requires annual registration with the New
Jersey Lawyers’ Fund for Client Protection, as well as
compliance with other portions of the ethical rules, for any
out-of-state lawyer who engages in transactional
representation in New Jersey, provided the transaction
originated in or is otherwise related to a jurisdiction in
which the lawyer is admitted to practice. 33

- South Carolina requires an out-of-state lawyer practicing
pursuant to the exception in Model Rule 5.5(c)(3) to file a
verified statement with the South Carolina Supreme Court
Office of Bar Admissions with respect to each ADR
proceeding in the state, which must include a statement
that the lawyer has not filed more than three such
statements in a 365 day period. The statement must be
accompanied by a $250 filing fee and must be served on
opposing counsel. 34

Similarly, a lawyer who practices in such a jurisdiction may be required to inform the
client that he or she is not licensed to practice law in that jurisdiction. 35 This would be required
when the representation occurs primarily in the jurisdiction, and requires knowledge of the law
of the jurisdiction. See Comment 20. In Birbrower, the Supreme Court of California called
attention to one of the few disputed facts in the case, which was whether the California client
was aware that its New York lawyers were not licensed to practice law in California. The better
practice in these situations would have been to make that clear in the fee agreement.

G. Hypotheticals

Hypothetical: A lawyer in a private law firm, whose practice consists primarily of the
preparation and registration of Franchise Disclosure Documents, is licensed to practice in State
A. One of her clients is a franchisor with its principal place of business in State B. The principal
owner of the franchisor is a private equity firm with its principal place of business in State C. The
franchise system has a purchasing cooperative, which was incorporated in State D and which
has its principal place of business in State E. The franchisor has franchisees in all 50 states
and each franchise agreement states that the law of the state in which the franchised unit is
operated governs the franchise agreement. The lawyer visits her franchisor client at its offices in
State B three times per year, attends quarterly meetings held in a variety of states with the

32 Nev. Rules of Prof’l Conduct R. 5.5A (September 1, 2013).
33 N.J. Rules of Prof’l Conduct R. 5.5(c)(6)(June 1, 2012).
35 For example, in Arizona, an out-of-state attorney engaged in the authorized multijurisdictional practice of law in the
state of Arizona, must (a) advise the client that the lawyer is not admitted to practice in Arizona, and (b) obtain the
client’s informed consent to such representation. Ariz. Rules of Prof’l Conduct R. 5.5(e) (last visited June 17, 2014).
franchise advisory council established by the franchisor, and attends semiannual meetings of the purchasing cooperative, all of which are held in State E.

In this case, the lawyer’s work for the out-of-state client preparing and registering FDDs, and providing advice and counsel with respect to the Franchisor’s relationship with the advisory council and the purchasing co-op, are all arguably related to the lawyer’s practice in her home state. Thus, these activities fall within the exception afforded in Model Rule 5.5(c)(3).

The activities that are conducted at the franchisor’s place of business in State E and in other states would likely not qualify as having established an office or a systematic and continuous presence in any of those states, despite the fact that the lawyer visits State B three times per year and State E on an annual basis. These services would most likely be classified as having been provided on a “temporary” basis in the states in which the lawyer is not admitted to practice.

**Hypothetical:** A lawyer in a private law firm, whose practice consists primarily of the representation of independent franchise associations, is licensed to practice in State A. One of his clients is an independent association of franchisees, which is managed on a day-to-day basis by an independent management firm based in State B. The association is a nonprofit Corporation, which was formed in State C. The president of the association has a principal office in State D. The board of the association consists of 12 franchisees from 10 different states. The members of the association come from 25 different states. The lawyer attends four meetings each year of the association, one of which is always in Las Vegas.

Like the lawyer for the franchisor in the previous hypothetical, the lawyer representing the independent franchisee association and providing advice and consultation in states other than the one in which he is admitted to practice, is clearly providing services related to the lawyer’s practice in his home state. Virtual contact with the independent management firm in State B, as well as the office of the president of the association in State D would not constitute systematic and continuous presence in either jurisdiction. The fact that one of the meetings of the association is always in Nevada would not be seen as having established an office in Nevada or as a continuous and systematic presence there, despite its regularity.

**Hypothetical:** A lawyer in a private law firm whose practice is concentrated in the field of litigation, is licensed to practice in State A. He has been asked to defend a potential lawsuit brought by 50 franchisees against their franchisor, which is based in State B. Each franchise agreement contains a venue provision as well as a mandatory mediation clause, which require mediation and litigation in the home state of the franchisor. The franchisees in question have only provided notice of a dispute, which triggers the mediation provision. The notice of dispute does not specifically state that litigation will be filed if the mediation is unsuccessful. One of the first steps the lawyer wants to take is to interview two former employees of the franchisor, both of whom reside in State C. He may elect to take depositions to perpetuate testimony from one or both of them.

The threshold question is whether the notices of claim constitute a potential proceeding before a tribunal within the meaning of Model Rule 5.5(c)(2). Given that the notice of claim and the resulting mediation are conditions precedent to litigation, the exception would likely apply and the lawyer’s activities in the state would probably be protected by that subsection, provided the lawyer reasonably expected to be admitted pro hac vice in the litigation, which might eventually be filed in State B.
In addition, the ADR Exception would also likely apply because the notices of claim triggered a mediation within the meaning of Model Rule 5.5(c)(3). Thus, the activities involved in interviewing the two former employees in State C would be reasonably related to such mediation.

If the lawyer decides to take depositions to perpetuate testimony pursuant to Fed.R.Civ.P. 27, this will require the filing of a petition in State C, where the two former employees reside. This proceeding would be one that would be reasonably related to the potential proceeding in State B, and thus would fall within the exception in Model Rule 5.5(c)(2), provided the lawyer was admitted pro hac vice in State C. A recommended practice would be for the lawyer to associate with a lawyer in State C, who would be required to actively participate in the matter.

III. GROUP OR MULTIPARTY REPRESENTATION

A. Conflicts of Interest

Model Rule 1.7(a) provides that a lawyer cannot represent multiple clients 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.\(^{36}\) Thus, group representation by a lawyer requires careful evaluation of whether the interests of any individual group client may be adverse to the interests of any other members of the group.

The analysis should begin with a determination of whether a concurrent conflict of interest exists. Model Rule 1.7(a) provides that a conflict exists if the representation of one client is directly adverse to any other client, or 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…”\(^{37}\)

A concurrent conflict of interest may be waivable if the following conditions are satisfied:

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 proceedings before a tribunal; and
4. each affected client gives informed consent, confirmed in writing.

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\(^{36}\) Model Rule 1.7(a).

\(^{37}\) Id.
North Carolina State Bar v. Whitted involved an examination of the attorney conflict issues. The underlying facts concerned a vehicle collision in which an attorney agreed to represent both the driver of an automobile and the estate of a passenger killed in the accident in their claims against the driver of the other vehicle. The court held that the interests of the estate of the passenger and interests of the driver were directly adverse, in part, because the driver of the car could well have been negligent and have caused the death of the passenger. As the court directly stated, the interests of the estate of the passenger and the driver were inevitably adverse. The court's decision to disbar the attorney was no doubt influenced by the fact that a payment for medical expenses in the amount of $2,000 was never deposited in the lawyer's trust account and was appropriated to his own use, using a forged endorsement. The Court of Appeals of North Carolina affirmed the order of disbarment.

In the end, this case stands for the proposition that if a client has interests, which are adverse or could be adverse to the interest of another client, or if a client either has a claim or a potential claim against another client, there is a concurrent conflict of interest which is not waivable under Model Rule 1.7(a).

Whether future conflicts can be waived is a separate issue. The United States District Court for the District of Texas was called upon to examine this question in Galderma Laboratories, L.P. v. Actavis Mid Atlantic, LLC. The plaintiff, Galderma Laboratories, was a manufacturer of branded dermatological products. Galderma retained outside counsel to provide legal advice regarding employee benefit plans. The engagement agreement with counsel contained a broad waiver of future conflicts of interest. While outside counsel was providing the legal services, a different law firm representing Galderma filed an action against Actavis. It subsequently came to light that the outside counsel retained by Galderma to provide legal advice on employment benefit plans also represented Actavis. Counsel's decided to sever its relationship with Galderma and not Actavis. Galderma filed a motion to disqualify counsel from continuing to represent Actavis, which was denied. The court observed that "...a general and open-ended waiver is likely to be ineffective because the vast majority of clients are not in a position to understand the material risks from the open-ended language of the waiver itself." However, the court found that an experienced consumer of legal services, such as Galderma, would tend to be more reasonably informed regarding the risk that a conflict may arise, and therefore, the waiver in issue was effective. The court also pointed out that the February 2002 amendment to Model Rule 1.7 "permits a lawyer to obtain effective informed consent to a wider range of future conflicts than would have been possible under the Model Rules prior to their amendment."

Waiver of future conflicts presents a dilemma in part because neither the client nor the lawyer can reliably predict the nature of the future matter that may create the conflict. What is

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38 82 N.C.App. 531 (1986).
39 Id. at 538.
40 Id. at 540.
42 Id. at 397.
43 Id. See also ABA Formal Op. 05-436.
clear is that courts are more comfortable with waivers of future conflicts by experienced users of legal services, or if the client has been represented by independent counsel in relation to such consent.\textsuperscript{44}

### B. Preserving Client Confidences

The duty and obligation of an attorney to preserve the confidences of a client can be particularly challenging in the context of multiparty representation. Comment 30 to Model Rule 1.7 provides that in determining whether common representation is appropriate, one factor to be considered is the potential effect on lawyer-client confidentiality and the attorney-client privilege. As the stated in the Comment to Rule 1.7,

> With regard to the attorney-client privilege, the prevailing rule is that, as between commonly represented clients, the privilege does not attach. Hence, it must be assumed that if litigation eventuates between the clients, the privilege will not protect any such communications, and the client should be so advised.\textsuperscript{45}

A ethical dilemma can arise if one client in a multiparty representation discloses something to his attorney on the condition that the attorney not disclose that information to any of the other clients being represented by the attorney in the same matter. The attorney has a duty of loyalty to each of the clients on an equal basis.\textsuperscript{46} Each client has the right to be informed of any facts that could have any bearing on the outcome of the case and to expect that any information in the hands of the lawyer will be used for the benefit of all clients, without differentiation.\textsuperscript{47} Comment 31 to Model Rule 1.7 makes clear,

> The lawyer should, at the outset of the common representation, and as part of the process of obtaining each clients informed consent, a lawyer should advise each client that information will be shared and that the lawyer will have to withdraw if one client decides that some matter material to the representation should be kept from the other.\textsuperscript{48}

### C. Aggregate Settlement Rule

**Hypothetical:** A lawyer is retained by a group of 50 franchisees of the same franchisor. The claim involves the imposition of a fee payable by franchisees which they contend is not permitted by the terms of the franchise agreements, and was not disclosed in the FDD received by any franchisee before they invested. The relief sought is a declaratory judgment that the fee may not be imposed, and a money judgment for fees previously collected. The fee agreements signed by each of the franchisees with the lawyer state that they agree that they will resolve the

\textsuperscript{44} Id.

\textsuperscript{45} Model Rule 1.7. Comment 30.

\textsuperscript{46} Model Rule 1.7, Comment 31.

\textsuperscript{47} Id.

\textsuperscript{48} Id.
matter as to the declaratory judgment if the Franchisor agrees that it will not impose the fee in the future. With respect to the claim for a money judgment, the fee agreements provide that each franchisee plaintiff will agree to settle the matter provided at least 75% of the amount claimed is recovered. Each plaintiff’s recovery would be pro rata based on the amount of fees paid by the plaintiff. The agreements further state that with respect to any offer to settle that does not meet these two thresholds, each franchisee plaintiff will agree to settle, provided 75% of the franchisees vote in favor.

This hypothetical implicates the so-called aggregate judgment rule found in ABA Model Rule 1.8(g). This Rule states in relevant part, that,

A lawyer who represents two or more clients shall not participate in making an aggregate settlement of the claims of or against the clients… 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, and of the participation of each person in the settlement.  

Model Rule 1.2(a) states that “[a] lawyer shall abide by a client’s decision whether to settle a matter.”  

Comment 13 to Model Rule 1.8(g) states that each client has the right to have the final say in deciding whether to accept or reject an offer of settlement.  

Model Rule 1.0(e) defines “Informed consent” as the “agreement by a person to a proposed course of conduct after the lawyer has communicated adequate information and explanation about the material risks of and reasonably available alternatives to the proposed course of conduct.”

The Comment to Model Rule 1.8(g) cites Model Rule 1.2(a), and reaffirms that before any settlement offer is made or accepted on behalf of multiple clients, the lawyer must inform each of them about all material terms of the settlement, including what the other clients will receive or pay if the settlement is accepted.

As to the latter requirement, a number of cases have been decided which turn on the issue of how much disclosure was made by the attorney concerning the proposed apportionment of the settlement.

ABA Formal Opinion 06-438 explains that the central purpose of Model Rule 1.8(g) is

“… to deter lawyers for favoring one client over another in settlement negotiations. By requiring the lawyers appeal to all clients information relevant to the proposed settlement. That information empowers each client to withhold consent, and thus

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49 Model Rule 1.8(g).
50 Model Rule 1.2(a).
51 Model Rule 1.8(g), Comment 13.
prevent the lawyer from subordinating the interests of the client to those of another client, or to those of the lawyer.\textsuperscript{52}

Clearly, the more transparency, the better, as further illustrated by the cases which follow.

The heirs of two fishermen lost at sea found themselves in conflict with the attorney that represented them in \textit{In Re The Petition of Mal De Mer Fisheries Inc.}\textsuperscript{53} The owner of the vessel offered an aggregate settlement of $485,000. The attorney notified one of the claimants that the owner of the vessel had offered to settle her claim for $115,000, without disclosing that the offer was an aggregate one and covered both claimants. The claimant conceded that in a later meeting, her attorney told her that the offer for the other claimant was three times the offer on her claim. The claimant consented to the settlement, but then changed her mind. The court observed that her attorney’s conduct was an apparent misrepresentation because the owner of the vessel had left it to counsel for the claimants to decide how the aggregate amount would be divided. Despite this failure of the attorney to provide all the facts to the claimant, and further, despite the fact that the settlement had never been reduced to writing, the court held that the misrepresentation did not affect the authority of the attorney to bind the claimant after she had agreed to accept the $115,000. The attorney in this case probably would have been better served to inform the claimant of what the other client would receive.

A similar issue was examined in \textit{In re An Anonymous Member of the South Carolina Bar.}\textsuperscript{54} The respondent attorney represented numerous clients in an environmental tort case. The matter was settled on an aggregate basis, with each of his clients being advised of their share in the settlement, but not the share of each other member of the settlement group, as required by South Carolina DR 5-106(A). The court found that disciplinary action was not warranted in part because the amount awarded to each client was reviewed by a federal judge, by a guardian ad litem appointed by the court to represent the minor and incompetent clients and by an independent attorney appointed by the court. In addition, the plaintiffs had been classified into different groups based on their injuries, a process which had been explained to them at numerous meetings and hearings. Respondent stated that he did not believe that he was required to make a disclosure by name of the settlement amounts. The court said that this position was at least arguable in respect of this respondent, but it would be enforced in the future.

A tragic automobile accident in which a wife and mother was killed was the setting for a decision of the Court of Special Appeals of Maryland in \textit{Scamardella v. Illiano.}\textsuperscript{55} Here, the attorney brought a personal injury claim on behalf of the wife’s parents, the wife’s husband and child, and the wife’s estate. A settlement was achieved in the amount of $1.25 million, which was the full extent of the insurance coverage of the defendants. At the time that the settlement was agreed to, no apportionment of that amount was proposed or agreed upon. Instead, the attorney suggested, and the parties agreed, that if the parties could not agree on apportionment, the parties would obtain other counsel, and the court would have to apportion monies. The court

\textsuperscript{52} ABA Formal Opinion 06-438 (February 10, 2006).


\textsuperscript{54} 377 S.E.2d 567 (S.C. 1989).

\textsuperscript{55} 727 A.2d 421 (Md. 1999).
examined the aggregate settlement rule under the Maryland Lawyers Rules of the Professional Conduct. The court observed that if there was any deficiency of disclosure, it did not result from any withholding of information, but rather from the failure to formulate an apportionment in advance. The court stated, “[w]e stress… that the fullest disclosure is the best disclosure, and note that other courts have used an attorney’s failure of appropriate disclosure as the ground for setting aside the appointment of a settlement… as the ground for setting aside an entire settlement… and as partial grounds for disbarment in a disciplinary proceeding.”

In *Re Mal Der Mare Fisheries, In Re An Anonymous Member of the South Carolina Bar* and *Scamardella*, all illustrate that an attorney owes the highest level of loyalty and fidelity to all of his or her clients and that withholding information from one client and not another client, especially when it relates to division of settlement proceeds, will inevitably lead to disqualification or even more dire consequences. *Abbott v. Kidder Peabody & Co, Inc.* directly implicates the aggregate settlement rule. In *Abbott*, 200 plaintiffs brought a non-class-action lawsuit in a single complaint. A single law firm represented all of the plaintiffs pursuant to a Representation Contract signed by all the plaintiffs. The Representation Contract established a steering committee of the plaintiffs, who would be the primary contact with the law firm. The Representation Contract also authorized the attorneys to settle any individual client’s claims on the same terms as those applicable to the personal claims of the steering committee members. The court granted the defendant’s motion to disqualify counsel for the plaintiffs on the basis that the Representation Contract did not comply with Col.R.Prof.Conduct 1.7(g), which deals with client conflicts generally, and not specifically the aggregate settlement rule. The court compared the facts to those in *Hayes v. Eagle-Pitcher Industries, Inc.*, a Tenth Circuit decision which invalidated a provision in an attorney-client agreement, which provided that majority rule would govern acceptance of any settlement arrangement. In *Abbott*, the governing committee, as a distinct minority of the 200 plaintiffs, was given much more authority over the group than in *Hayes*, where a majority of all plaintiffs was required.

In *The Tax Authority, Inc. v. Jackson Hewitt, Inc.*, the Supreme Court of New Jersey was called upon to interpret the aggregate settlement rule in the context of the settlement of a lawsuit brought on behalf of 154 franchisees. The claims related to the Performance Incentive Rebates that had been distributed to franchisees in connection with Refund Anticipation Loans (RALs) in prior tax seasons. Each of the 154 plaintiffs entered into an identical attorney-client agreement, which provided, in relevant part that,

(t)he Client agrees that the Matter may be resolved by settlement as to any or all of the Matter upon a vote of a weighted majority of the Client and all of the Co-Plaintiffs. Each Plaintiff shall have one vote for each funded RAL for the 2002 Tax Season. The Client will be eligible to vote only if correct in all payments required under this agreement... A quorum for such vote shall be 60% of the votes eligible to be cast.

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56 Id. at 428.


58 898 A.2d 512 (N.J. 2006).

59 In conformity with the policies of the ABA Forum on Franchising, co-author Eric H. Karp was counsel of record for the 154 plaintiff franchisees in this matter.
The attorney-client agreement also stated that any settlement proceeds would be apportioned according to each plaintiff’s proportionate share of the RAL reserve. The agreement also included formulas on how net proceeds would be calculated. Each client was also given an opportunity to consult with outside counsel before signing the agreement. A four person steering committee was formed to act as the primary contact with the attorneys.

The matter was mediated on a collective basis with JAMS. Present at the mediation were the members of the steering committee, but none of the other plaintiffs. The mediation resulted in a two-page settlement document which was signed by all three members of the steering committee as well as by representatives of Jackson Hewitt. The agreement stated that it was subject to the approval of the plaintiffs, and by the Board of Directors of Jackson Hewitt, Inc.

Not long after the settlement in principle was arrived at, a spreadsheet was posted to a password-protected website showing the calculation of each plaintiff’s estimated net participation in the cash portion of the settlement. The spreadsheet included the names of every plaintiff and the amount each was to receive. Kenneth Leese, the principal owner of lead plaintiff, The Tax Authority, Inc. was a member of the steering committee and also assisted in creating and finalizing the spreadsheet that was disclosed to all plaintiffs. Thereafter, 18 of the 154 plaintiffs refused to sign the eventual formal settlement agreement with Jackson Hewitt, Inc. Jackson Hewitt, Inc. brought a motion to enforce the settlement agreement. At the hearing on the motion, 14 of the 18 plaintiffs were represented by new counsel, who took the position that the attorney-client agreement violated the aggregate settlement rule.

The trial court determined that the former Model Rule DR 5-106, issued in 1980, required disclosure of the total amount of the settlement prior to each plaintiff’s approval, while the then-current Rule 1.8(g) did not include that requirement. The court found that the weighted majority provision did not violate the aggregate settlement rule, and that invalidating the settlement agreement would be unfair to those plaintiffs who wished to proceed with a settlement.

The Tax Authority was the sole plaintiff to appeal. The New Jersey Appellate Division reversed, holding that the weighted majority provision of the attorney-client agreement violated the aggregate settlement rule. Not long after the settlement in principle was arrived at, a spreadsheet was posted to a password-protected website showing the calculation of each plaintiff’s estimated net participation in the cash portion of the settlement. The spreadsheet included the names of every plaintiff and the amount each was to receive. Kenneth Leese, the principal owner of lead plaintiff, The Tax Authority, Inc. was a member of the steering committee and also assisted in creating and finalizing the spreadsheet that was disclosed to all plaintiffs. Thereafter, 18 of the 154 plaintiffs refused to sign the eventual formal settlement agreement with Jackson Hewitt, Inc. Jackson Hewitt, Inc. brought a motion to enforce the settlement agreement. At the hearing on the motion, 14 of the 18 plaintiffs were represented by new counsel, who took the position that the attorney-client agreement violated the aggregate settlement rule.

The New Jersey Supreme Court, citing Hayes, found that the weighted majority rule provision was not enforceable. It called attention to the sharp distinction between class-action lawsuits and simple joinder actions. In the former situation, the settlement is reviewed for fairness by a court, while in the latter, it is not. The court also cited In Re Hoffmart, a case in which an attorney represented six plaintiffs in a contest of a will. Two of the six signed an

60 The court noted in its decision that the settlement agreement was signed by the three surviving members of the steering committee—one member passed away during the course of the proceedings.

61 Id. at 517.

62 Id.

63 883 So.2d 425 (20014).
affidavit indicating that they would settle for any amounts in excess of the legacy to which they were entitled under the will. The attorney then entered into an aggregate settlement on behalf of all six plaintiffs in excess of their legacies under the will. The Louisiana Supreme Court determined that the aggregate settlement rule had been violated.\textsuperscript{64}

The New Jersey Supreme Court’s ultimate decision contained two essential elements. First, while the court found that the aggregate settlement rule prohibited enforcement of the settlement, it decided to make the application of its holding prospective only and thus actually enforce the settlement agreement against The Tax Authority. The court stated that the effort of plaintiffs’ counsel to represent plaintiffs from many different states and to successfully seek to have all plaintiffs agree in advance to be bound by a weighted majority was a plausible, although incorrect interpretation of RPC 1.8(g).\textsuperscript{65} No doubt, the court was strongly influenced by the completely transparent disclosure to all plaintiffs of the aggregate settlement and the exact participation of each plaintiff in that settlement.

Second, the court took note of the fact that some commentators have questioned the wisdom of the aggregate settlement rule, citing an article by Professors Charles Silver and Lynn Baker.\textsuperscript{66} Professors Silver and Baker state that “(b)ecause the stakes are so large, and the issue so complex, settlement is both more urgent and more difficult in mass lawsuits than in other litigation, and the aggregate settlement rule is a complication that often gets in the way.” In their article, they cite four major respects in which the aggregate settlement rule can complicate settlement: “by invading plaintiffs’ privacy; by preventing plaintiffs from offering defendants finality; by generating expense and delay; and by encouraging strategic behavior within plaintiff groups that frustrate global deals.” The New Jersey Supreme Court concluded by stating that “in light of those and other concerns advanced in favor of permitting less than unanimous consent in multi-plaintiff mass litigation, we refer this issue to the Commission on Ethics Reform for its review and recommendations to the Court.”\textsuperscript{67}

To return to our hypothetical, it is abundantly clear that in presenting any aggregate settlement to a group of clients, in this case franchisees, the lawyer must provide detailed information regarding the participation of each franchisee in the proceeds. It is also clear based on established case law, that any franchisee, who does not agree with settlement, would not be bound by a 75% vote to the contrary. With respect to the declaratory judgment aspect, the result is less clear, but the weight of established authority would indicate that even if the client consented in advance to settle on the basis of an agreement by the franchisor never to charge the fee in question, a dissenting plaintiff could not be compelled to settle on that basis, especially if the negotiated scope of the future prohibition on the imposition of such fees was not to the franchisee’s liking.

What is ironic about these aggregate settlement rule cases is that they are arguably a direct result of the tendency of franchise agreements to prohibit class actions, and even more recently, aggregate or consolidated lawsuits. This increases the fragmentary nature of these

\textsuperscript{64} Id. at 520.

\textsuperscript{65} Id. at 523.


\textsuperscript{67} Id. at 523.
cases, and while it makes it more difficult and expensive to litigate them, it is even more challenging to resolve them on a global basis.

IV. Ethical Considerations For Internal Investigations

Because franchising is a highly regulated business, any number of issues may arise which trigger the need to conduct an internal investigation. The most readily apparent issues may involve, for example, compliance with the Federal Trade Commission’s Rule on Franchising and various state franchise investment or sales laws, or less common issues such as compliance with the Sherman Act or the Clayton Act and their state equivalents. Other issues may be specific to particular businesses, such as compliance with the Foreign Corrupt Practices Act or regulations promulgated by the Securities and Exchange Commission (SEC), or perhaps issues involving corporate governance or employment matters.

Once it is determined that there is a need for an internal investigation, the company must identify the individual(s) to supervise the investigation. An officer of the company? The General Counsel? The board of directors? A subcommittee of the board of directors? Primary outside counsel? A myriad of issues weigh on this decision including, without limitation, the level of seriousness and the materiality of the issue(s), whether individuals may have personal knowledge of or are otherwise involved in underlying facts, whether individuals maintain the requisite independence, whether individuals have the appropriate level of discretion and, finally, what will be the attendant actual or opportunity costs associated with the selected supervisor(s) of the investigation.

The selected individual, board or other committee also needs to retain a person, department or firm to be in charge of conducting the investigation. The supervising investigator need not be a trained lawyer. There are, in fact, limited circumstances where the subject matter of the investigation merits selecting a professional with more germane experience or, alternatively, the gravity of the matter is not significant enough to require counsel. Examples could include matters such as employee disputes or other HR issues. Where investigations are more serious in nature or could have a material impact on the business, however, lawyers are most often the best choice.

Appointing an attorney to conduct the investigation affords a number of otherwise unavailable benefits. Most notably, use of counsel affords protections associated with the attorney-client privilege and work-product doctrine. Equally important, selecting an attorney to conduct the investigation affords such designated counsel the opportunity to review and understand all of the relevant facts. This, in turn, better informs counsel’s analysis of the company’s legal rights, obligations, and potential liabilities at the conclusion of the investigation. Other professionals may not be adequately equipped to provide these benefits.

Internal investigations—whatever the impetus—are fraught with ethical issues that have the potential to wreak havoc on the company, its officers and possibly the in-house or investigating counsel. Issues arise at the outset of the investigation and continue through to its conclusion and beyond. Counsel (or other lead investigators and supervisors) must be able to recognize and assess each issue as they arise, if not well before.

This Section IV highlights ethical issues to be assessed during an internal investigation, including the preparation and dissemination of a final report of findings. A failure to identify and satisfactorily address these ethical issues can lead to waiver of the attorney-client privilege, a
determination of incompetence with respect to investigating counsel, breach of fiduciary duties, breach of duties of loyalty and possibly even obstruction of justice or perjury.

A. Identify Your Client

When an internal investigation is deemed necessary, the initial threshold issue requires identifying the client. In most instances, the client is the company. Model Rule 1.13(a) provides that “a lawyer employed or retained by an organization represents the organization acting through its duly authorized constituents.” In other words, the lawyer’s duty runs to the entity itself and not the individual constituent officers, directors and employees with whom the lawyer regular confers and meets. Model Rule 1.13(f) mandates:

In dealing with an organization’s directors, officers, employees, members, shareholders or other constituents, a lawyer shall 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.

In discharging this duty, the lawyer must be clear to all involved that his or her loyalty runs to the organization and not to any individual shareholder, director, officer or employee. The lawyer must not be persuaded by the personal interests of the company’s directors, officers or employees, and must always consider the best interests of the organization above any individual interest.

Adherence to this rule may seem simple in theory, but is far more complex in practice. Companies are fictitious legal entities which, while recognized by the law as distinct “individuals”, can in fact only act, correspond and make decisions through the individual officers, directors and employees working on its behalf. When these individuals’ interests are aligned with the company, the process can be fairly straightforward. The inherent nature of internal investigations, however, has the potential to turn that dynamic on its head, relegating anyone with potentially relevant information about the investigation’s subject matter equally likely to find himself or herself adverse to the company during the course of or at the conclusion of an investigation. Indeed, prioritizing the best interests of the company at the potential expense of its employees, officers or directors is a primary purpose of an internal investigation.

Equally challenging is recognizing and being mindful of a limited exception to the rule that the company is the client. Depending on the circumstances, the client may be the corporation, the board of directors or a special subcommittee. And, if counsel is not careful, almost any one of these parties, or portions thereof, can become adverse. For example, a board of directors may be concerned about its independence, or that of its members, and therefore establish a subcommittee (or an audit committee) to take responsibility for an internal investigation. Identifying the client and the potential factual and legal developments in advance of commencing an investigation will help to avoid complications and conflicting duties as matters proceed.

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68 See also Cal. Rules of Prof’l Conduct R. 3-600(A) (Jan. 1, 2014).

69 Considerations when addressing these potential conflicts of interest are set forth in Section IV.D.1 below.
**Hypothetical:** The General Counsel of a long-standing client advises outside counsel that the Board of Directors has determined a need to conduct an investigation into whether the company engages in a practice of making financial performance representations to sell non-exempt franchises notwithstanding the absence of any such disclosure in Item 19 of the registered Franchise Disclosure Document. There is a concern that such conduct may trigger delivery of an investigative demand from the Federal Trade Commission or a state regulator. The General Counsel advises that the Board has decided to retain the outside counsel to conduct the investigation.

Under the limited facts provided above, the general rule applies that the company is the outside counsel’s client. A minor change in the facts, however, can insert the company’s board of directors or a subcommittee of the board of directors as the client. For example, as mentioned above, it is not uncommon for a board of directors to form a subcommittee of non-interested board members to pursue an internal investigation. In such a case, the subcommittee may become the client instead of the company. The distinction is not just a formality.

Under normal circumstances, it may be natural for outside counsel to speak freely with board members and other constituents of the company about legal matters. Because outside counsel is handling an investigation on behalf of the subcommittee, however, it may violate ethical obligations to engage in conversations about the subject matter of the investigation. Indeed, disclosure of facts or legal issues to company constituents who are not part of the investigating subcommittee could amount to a waiver of the attorney-client privilege. This result may make sense, particularly where those officers and directors are potential subjects of the investigation and, therefore, may have their own interests to protect with respect to the outcome of the investigation. In addition, as discussed in greater detail below, counsel needs to be careful in communications with company constituents to ensure that all parties readily appreciate to whom investigating counsel owes a duty of loyalty.

These issues are discussed in greater detail below which highlight why investigating counsel must remain vigilant in his or her understanding of, and respect for, the identification of the client. If not, the results of the investigation may lead to issues far worse than those arising solely from the misconduct that was the subject of the internal investigation in the first place.

**B. Reporting to the Client and Confidentiality**

After determining the identity of the client, the next ethical issue involves establishing the chain of command with respect to whom counsel should communicate and to whom those individuals are required to report. Establishing a clear chain of command enables investigating counsel to understand the particular individuals who are within the sphere of privilege, and from whom to take instruction. Two Model Rules specifically relate to these matters. First, Model Rule 1.4 addresses communications with clients and requires:

(a) A lawyer shall:

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70 See Zapata Corp. v. Madanado, 430 A.2d 779 (Del. 1981) (delegating a board's authority to a subcommittee to act on behalf of corporation for all matters within scope of delegation).


72 See Sections IV.D.1 below.
(1) promptly inform the client of any decision or circumstance with respect to the client's informed consent;

(2) reasonably consult with the client about the means by which the client's objectives are to be accomplished;

(3) keep the client reasonably informed about the status of the matter;

(4) promptly comply with reasonable requests for information; and

(5) consult with the client about any relevant limitation on the lawyer’s conduct when the lawyer knows that the client expects assistance not permitted by the Rules of Professional Conduct or other law.

(b) A lawyer shall explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation.

In addition, Model Rule 1.6(a) provides that “[a] lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation or the disclosure is permitted under paragraph (b).” Paragraph (b) addresses instances where disclosure is necessary to prevent bodily harm, the commission of a crime or fraud and substantial injury to the financial interests of the client or another. It also authorizes disclosure to secure legal advice, to establish a claim or defense against a lawyer, to comply with a court order or to detect and resolve conflicts of interest.

Ordinarily, outside counsel reports to the General Counsel and the General Counsel, in turn, reports to either a Chief Executive Officer or other executive officer, or the board. But what happens if the executive officers and the General Counsel are all subject to being potentially implicated in wrongdoing during the course of the investigation? This is particularly relevant in franchising where the results of an investigation could become the basis for a criminal indictment of certain individuals under certain state franchise laws.

Assuming that the company has in fact been identified as the client, then it will be important to cordon off interested officers and directors from communications regarding developments in the investigation. Alternatively, as discussed in Sections IV.A and IV.B above, it may be better to establish a subcommittee of disinterested directors/officers which directly retains counsel to conduct the investigation. Whatever the decision, the investigating counsel has an ethical obligation to maintain the confidentiality of the investigation, even in the face of questions from officers and directors to whom counsel may regularly report (and to whom she may continue to report with respect to other matters). This is not easily accomplished, even

73 See Model Rule 1.6(a) (“A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation or the disclosure is permitted by paragraph (b).”).
under the best of circumstances, as management will want to be kept apprised of developments in the investigation. Thus, it is important to strike a balance between keeping management informed about the investigation and avoiding disclosure of too much information which may subsequently become a basis for others to make claims of witness tampering or a waiver of privilege.

Failure to adhere to these ethical obligations can expose the company and everyone involved to criticism or, in more severe cases, claims of breach of fiduciary duty and malpractice. For example, in *Ryan v. Gifford*, the Delaware Chancery Court underscored the importance of managing communications and maintaining confidentiality when conducting an internal investigation. In *Ryan*, a law firm was retained by a special subcommittee formed by the board of directors of Maxim Integrated products to conduct an internal investigation with respect to allegations of backdating on stock options granted to Maxim's founder, chairman and CEO. After the law firm completed the investigation and reported the results to the special subcommittee, its members shared the law firm's findings with the entire board of directors. In subsequent shareholder litigation where the matters investigated were at issue, the court granted the plaintiffs' motion to compel otherwise privileged communications between the law firm and the subcommittee, concluding that the presentation of the law firm's findings to the entire board of directors constituted a waiver of the subcommittee's attorney-client privilege. The court stated that "[t]he presentation of the report constitutes a waiver of privilege because the client, the Special Committee, disclosed its communications concerning the investigation and final report to third parties—the individual director defendants and their counsel—whose interests are not common with the client."75

Whatever the purpose of an investigation, the mere fact that an investigation was deemed necessary mandates that investigating counsel remain vigilant in honoring the duty of confidentiality, the duty to keep the client (and the appropriate client constituents) informed by understanding and compliance with the established chain of command.

**Hypothetical:** The General Counsel has retained outside counsel to conduct an investigation into whether the franchisor's sales team has engaged in making unauthorized financial performance representations to lift sales of franchised locations in particular markets. Outside counsel reports to the General Counsel all developments in the investigation. The Senior Vice President of Franchise Development, who is responsible for hiring the General Counsel at the company and who regularly confers with the General Counsel on legal matters, asks the General Counsel for an update on developments and findings in the investigation.

Although the General Counsel will likely experience substantial personal and professional pressure upon receiving the inquiry from his or her biggest supporter in the company, it is important to limit discussions about the investigation to members of the board. This is particularly so when the inquiry is made by an individual who may become a focus of the investigation. Potential adverse developments and ways to avoid this circumstance are discussed in greater detail below.

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75. *Id.* at "3.
C. Ensuring a Thorough Investigation

The designated lead investigator and investigating counsel have a duty to the company and its shareholders to ensure the subject matters are thoroughly reviewed in a manner designed to correct unlawful or criminal conduct and establish a monitoring system to prevent any reoccurrence. Failing to do so can mire the investigation supervisor and investigating counsel in allegations that they deliberately subverted the investigation to conceal misconduct. These types of allegations often surface when an investigation fails to uncover misconduct that, in hindsight, should have been known to, or discovered by, the board, the supervisor of the investigation supervisor or investigating counsel.

The need for a highly regimented investigation is reflected by the court decision of In re Caremark Int’l Derivative Litig. The In re Caremark court decision highlighted and refined the duties of oversight for board members, finding that corporate directors have a fiduciary duty to establish a monitoring system to prevent and, where necessary, correct misconduct. In re Caremark was a series of shareholder class actions which sought to impose liability on then-serving directors of Caremark International, Inc. for breaching their duty of care by failing to put in place adequate internal control systems. As the court described it, the shareholders sought to establish liability based on allegations that the board “allow[ed] a situation to develop and continue which exposed the corporation to enormous legal liability.” While the Delaware court did not find the Caremark board liable, the court’s decision rippled through the business community because it recognized that liability for losses may be imposed upon directors where a corporate loss results from not only affirmative misconduct by such member(s) but also from “unconsidered inaction.” The court noted that “[r]elevant and timely information is an essential predicate for satisfaction of the board’s supervisory and monitoring role.” This decision is widely recognized as a foundation for imposing a heightened general duty of oversight upon a director “to attempt in good faith to assure that a corporate information and reporting system. . . exists.”

It has also become increasingly common to initiate an internal investigation at the behest of the government, be it the Federal Trade Commission, the Department of Justice or sometimes even Congress. In these instances, there is a further heightened need for thoroughness. A comprehensive investigation enables the company to ensure its communications with the government are accurate which can oftentimes make the difference between an indictment or other charging violation and less severe results such as either non-prosecution or deferred prosecution. On the other hand, if the effectiveness of an internal investigation is somehow compromised, the resulting effect can be severe for all involved—sometimes leading to a result that is worse than if the company had conducted no investigation at all. Several examples of how less than thorough investigations can become high profile problems include a law firm’s investigation of employee whistleblower claim at Global Crossing, another law firm’s investigation of Sherron Watkins’ memo about accounting

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76 698 A.2d 959 (Del. Ch. 1996).
77 Id. at 967.
78 Id. at 970.
79 Id.
irregularities at Enron\textsuperscript{81}, and a third law firm's investigation about stock option grants at Mcafee.\textsuperscript{82}

For corporations operating in a highly regulated industry, such as franchising, violations of disclosure and registration laws that result in losses to the corporation may adversely affect the financial standing of the corporation. Internal investigations are but one tool to be implemented to protect the company from civil, and possibly criminal, liability.

D. Conflicts of Interest

Model Rule 1.7 addresses conflicts of interest and provides as follows:

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.

Internal investigations are virtual minefields for actual, potential, and threatened conflicts of interest. While a number of the potential issues to consider are addressed below, it is not possible to cover every iteration of how a potential conflict may surface in an internal investigation. Before agreeing to an engagement as investigating counsel, all parties are best served to take inventory of prior representations—formal and informal—and take stock of investigating counsel’s personal and professional relationships with any person affiliated with the company. Investigating counsel’s work will include flushing out misconduct (that may have been previously and deliberately concealed), ascribing blame and possibly turning over incriminating evidence regarding the blameworthy to the government. This is not the ideal recipe for maintaining long-term relationships with those being investigated.

1. Relational Conflicts of Interest

Part of any internal investigation involves interviewing company officers, directors and employees to develop the underlying facts. What is unusual under these circumstances, however, is that the company employees often voluntarily cooperate with the investigation even though some or all of them could ultimately become adverse to the company in concurrent or subsequent civil or government proceedings. Indeed, a company may decide to disclose the substance of the interviews with investigative or prosecutorial government agencies to obtain “cooperation credit” as part of an effort to mitigate or completely eliminate government action.\textsuperscript{83} Where employees answer questions candidly to investigating counsel and potentially admit to


\textsuperscript{83} See Sections IV.F and IV.G regarding dissemination of internal investigation reports.
certain of their own transgressions, they will likely be displeased to later learn that their efforts have been transformed into the basis for civil fines or criminal indictments against them individually.

Therefore, in conducting an internal investigation, counsel runs the risk that company personnel—particularly those with whom investigating counsel has previously worked on other company matters—may mistakenly believe company counsel represents the employees individually, in addition to the company. If this situation develops, disputes may ensue about whether the privilege attaches at all and, if so, who owns the privilege. This can become a real problem if the parties’ interests conflict in the future. For example, if an employee discloses during the interview that he or she has been bribing foreign government officials to expedite the company’s ability to conduct business in those countries, the company may wish to disclose that information to obtain cooperation credit with the Department of Justice when it starts to investigate the company for violations of the Foreign Corrupt Practices Act. If the employee is not expressly advised of this possibility at the outset of the interview, then he or she may object and fight disclosure. While the dispute with the employee ensues, the Department of Justice is under the impression that the company is not cooperating by failing to promptly turn over relevant information. Worse yet, investigating counsel (who may have worked with the employee, say for the past ten years) struggles with the decision whether to “uncover” the damaging facts and expose the employee to internal and government action.

This type of dilemma is often referred to as a “relational conflict of interest.” These typically arise when the investigating attorney has a longstanding relationship with the company, its in-house counsel or other officers, directors or employees of the company such that his interests are too closely aligned with those of the individual company constituents.

“In the event an independent investigation is reasonably likely to implicate company executives, the board—not management—should retain special counsel for this investigation. Special investigations of company activities that may implicate the conduct of company executives require independence from management. Typically, lawyers and law firms are in the best position to conduct investigations, and care must be taken that these investigations are conducted thoroughly, vigorously, and objectively. It is important, therefore, that investigative counsel be chosen by, and report directly to, the board. To ensure that special counsel’s interests are not aligned with, or influenced by, management, the Commission believes that special counsel should not be one of the corporation’s regular outside counsel or a firm that receives a material amount of revenue from the company.”

One set of circumstances arguably implicating a relational conflict of interest developed when primary outside counsel was retained to conduct an internal investigation to identify the

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84 See Section IV.G for a discussion about ethical issues involved in delivering final reports of internal investigations to law enforcement or other government authorities.

source of a press leak within Hewlett Packard's board of directors. The company's primary outside lawyer had been closely associated with the board for years and was called upon to investigate the very same people with whom he had worked. The result of outside counsel's investigation was inconclusive, failing to identify the source of the leak. Yet, the company's efforts to investigate did not conclude with outside counsel's report. Instead, a new Chairwoman continued to pursue the source of the leaks, this time appointing the in-house senior counsel and ethics director to conduct the investigation through a process called pretexting. This is a practice where an individual lies about his or her identity in order to obtain confidential or privileged information that he or she is not entitled to, and it was used to delve into the personal communications of the company's board members. Ultimately, it was uncovered that the source of the leak was in fact a member of the board. However, the fact that the outside counsel's initial investigation was inconclusive has since called into question the wisdom of using closely associated outside counsel to investigate matters involving people with whom they regularly interact.

Consider whether corporate officers or employees may have previously considered you to serve as their individual counsel or, more notably, whether you have represented the individual officers or employees jointly with the Company in connection with other litigation. Vetting for and preventing relational conflicts of interest are essential to effectively handling internal investigations. The failure to strictly adhere to this rule has resulted in a number of high profile incidents where outside counsel conducting an investigation may have failed to assess potential conflicts with the requisite level of circumspection. Examples of such incidents are discussed below.

a. The Upjohn Warning

To try to avoid any potential misunderstanding with witnesses, investigation counsel is best served to provide relevant directors, officers and employees with an Upjohn warning. An Upjohn warning clearly communicates to the employee that the investigating counsel is acting at the request of, and for the benefit of, the company and, as a result, the employee should understand and expect that counsel will operate to serve the company's best interests (and not the best interests of the employee). This warning has its origins in the United States Supreme Court ruling in Upjohn v. United States, a case involving an internal investigation into improper payments made by Upjohn management to foreign government officials. During the case, the General Counsel and outside counsel sent questionnaires to hundreds of company employees regarding practices relating to payments to foreign governments and their representatives. Only a small fraction of the questionnaires were completed and returned and company counsel proceeded to interview those who did in fact complete the questionnaires. In a subsequent proceeding, the Internal Revenue Service sought production of the questionnaires, to which Upjohn naturally objected on the grounds of attorney-client privilege. After conflicting rulings

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88 Waggoner v. Snow, Becker, Kroll, Klaris & Krauss, 991 F.2d 1501, 1505-06 (9th Cir. 1993) (warnings regarding duties to the company effectively prevent employee claims of attorney-client privilege with investigating attorney).

regarding the applicability of privilege in the district court and the Sixth Circuit, the Supreme Court held that the attorney-client privilege attached to communications that: (1) were made by company employees; (2) to counsel for the company acting as such; (3) at the direction of authorized company representatives; (4) to secure legal counsel; and (5) concerning matters within the scope of the employee’s duties. Additionally, the Supreme Court’s analysis required that the employees “were sufficiently aware that they were being questioned [for] the corporation [to] obtain legal advice.” By recognizing that the company’s attorney-client privilege extended to counsel communications under these circumstances, Upjohn also highlighted the need to make this dynamic clear in communicating with company employees.

Giving an Upjohn warning is technically not complicated and there is generally no good reason for counsel to not follow its guidance with a disclosure similar to that set forth below:

I have been asked by the company to meet with you as part of the company’s investigation into [insert subject of investigation]. The purpose of our discussions is for me to gather all relevant information relating to [the subject of the investigation] so the company has a comprehensive understanding of the relevant facts, and so it can obtain legal advice in connection with potential upcoming litigation and other legal proceedings.

While we have known each other and worked with one another for quite some time, it is important that I make clear to you that I am counsel for the company. As such counsel, you need to understand that I do not and cannot represent you or any other officer, director or employee of the company. The substance of our conversations are subject to the protections of the attorney-client privilege, but the privilege is owned and controlled by the company and not you individually. This means that you do not have the right to waive the privilege and disclose the substance of our conversations to anyone—irrespective of whether such individuals are currently employed by the company—unless authorized in writing to do so by the company. On the other hand, the company may choose to waive the attorney-client privilege at any time and for any purpose, even without your consent.

Do you have any questions for me?

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90 Id.

91 Id.

92 The required content of an Upjohn warning has historically varied by state. For example, in the District of Columbia, the District Bar’s former rules required counsel to notify unrepresented parties that they may wish to obtain independent representation. See D.C. Rules of Prof’l Conduct, Former Rule 1-28. It is worth noting that, except for California, every state and the District of Columbia have now adopted the Model Rules, albeit some with their own additional language. See State Adoption of the ABA Model Rules of Prof’l Conduct, ABA Center for Prof’l Responsibility, available at https://www.americanbar.org/groups/professional_responsibility/publications/model_rules_of_professional_conduct/alpha_list_state_adopting_model_rules.html (last visited June 17, 2014).
Based on the Model Rules and applicable law, the temptation will be to deliver an Upjohn warning as clearly as possible to ensure that the relevant officer, director or employee does not look to the investigating attorney for advice, counsel or protection. The mere delivery of the disclosure itself, however, is bound to result in responsive questions which ask for further legal advice (i.e. do I need a lawyer, etc.) potentially making the environment somewhat less comfortable for all.\(^93\) Perhaps more importantly though, the more stern the disclosure, the less likely the employee or officer will be to cooperate and answer questions. Part of investigating counsel’s responsibility is to research and uncover all of the relevant facts, which typically are obtained through employee interviews. Striking fear into employees at the outset of an interview is usually not the most effective approach to achieve a forthcoming and candid discussion.

Another complication involved in issuing an Upjohn warning involves deciding whether written confirmation is necessary. While a written confirmation is likely to afford counsel better protection from claims by employees regarding an attorney-client privilege, it can also serve as one more reason why an employee may be less inclined to be forthcoming about relevant information in an interview. Alternatives to written disclosures include simply making a written note in the file that the disclosure was made or maintaining a common disclosure routine in each interview which will give courts greater comfort in deciding against an employee’s assertion of privilege.

A good example where the delivery of an Upjohn warning became a central issue can be found in United States v. Nicholas\(^94\), where the underlying facts involve counsel for Broadcom Corporation being retained to conduct an investigation into allegations of backdating stock options. During the course of the investigation, investigating counsel interviewed Broadcom’s Chief Financial Officer and subsequently—without the CFO’s permission—turned over the substance of those discussions to Broadcom’s outside auditors, the SEC and the Department of Justice. When the interview materials later served as the basis for an indictment against the CFO, he moved to suppress the evidence by claiming that the company had breached the attorney-client privilege by disclosing his responses to questions to the government. In response, the government argued that the CFO had been given an Upjohn warning by company counsel and, therefore, had no expectation of confidentiality. While the trial court initially agreed with the CFO and threw out the indictment based on its finding that the investigating counsel had failed to give an Upjohn warning, the Ninth Circuit viewed the matter differently and reversed the district court’s suppression order. The reversal was not based on a disagreement between the courts regarding whether the Upjohn warning had in fact been given (the Ninth Circuit left that finding undisturbed), but the court instead based its decision on the record reflecting the CFO never had an expectation of confidentiality. The CFO was always aware the results of the investigation would be turned over to the company’s auditors.\(^95\)

\(^93\) Model Rule 4.1(a) prohibits counsel from knowingly making a false statement of fact. Where counsel is aware that the company has a statutory or other obligation to disclose information to the government, counsel needs to answer questions about use of the information accurately.

\(^94\) 606 F.3d 600 (9th Cir. 2009).

\(^95\) See United States v. Ruehle, 583 F.3d 600 (9th Cir. 2009) (overruling trial court decision finding in favor of Broadcom’s CFO with respect to his argument that he had established an independent attorney-client relationship with investigating counsel).
b. The Zar Warning

In addition to an Upjohn warning, internal investigations under certain circumstances may also require that counsel give a Zar warning to relevant officers, directors and employees at the outset of an interview. A Zar warning notifies the employee that providing false information to internal investigators may lead to criminal charges for obstruction of justice. The need for this warning can be troubling for investigating counsel in two material respects. First, if the Upjohn warning did not cause an employee to shut down and stop volunteering information, then the delivery of a Zar warning may, on its own, cause an employee to seek independent representation before participating in an interview. Second, some may find it objectionable that an officer, director or employee can be criminally charged for dishonesty to company counsel (as opposed to a law enforcement officer).

However fair or unfair it may be for an employee to be criminally charged for responses it provides to its employer, this is exactly what happened in United States v. Zar. In April 2004, the former CFO and two former executives of Computer Associates International, Inc. pled guilty to obstruction of justice, among other things. While not an entirely uncommon claim to be pursued by the SEC, the obstruction charges in Zar were different because their foundation was based exclusively on false statements made to internal investigators—and not on statements made to any government agency or enforcement officer. The SEC’s charging statement alleged that the three executives conspired in advance of their interviews with internal investigators to deny facts evidencing criminal conduct. The court further found that Zar actually encouraged the other officers to not disclose the true facts but, instead, substitute them with false statements.96

A Zar warning may not be necessary in every witness interview or even every investigation. Investigating counsel simply needs to consider the rights of the employees prior to and while conducting interviews with employees. Those rights may also include the Fifth Amendment right against self-incrimination, the Sixth Amendment right to representation and employee constitutional rights of privacy, contractual rights in employment manuals. Depending on the issue being investigated and the witness being interviewed, counsel needs to constantly weigh these factors to ensure the employee is fairly informed of the circumstances and counsel has positioned himself or herself to gather the most information and documents possible.

2. Subject Matter Conflict of Interest

Before conducting an investigation, counsel should also take a close look at the facts and legal issues presented to ensure that part of the review will not involve matters in which counsel previously provided advice to the company. This is called a subject matter conflict of interest and is specifically addressed in Comment 10 to Model Rule 1.7:

The lawyer’s own interests should not be permitted to have an adverse effect on representation of a client. For example, if the probity of a lawyer’s own conduct in a transaction is in serious question, it may be difficult or impossible for the lawyer to give a client detached advice. . .97

97 Model Rule 1.7.
For example, one high profile incident involved a law firm's investigation of claims asserted by Enron Vice-President Sherron Watkins about accounting improprieties at the firm. In 2001, Watkins submitted a detailed memo to then Enron CEO Ken Lay notifying him about accounting irregularities in the company’s relationship with a special purpose entity. Upon receipt of the memo and following a meeting with Watkins, Lay retained a law firm to conduct an investigation into potential financial misconduct.\footnote{See In re Enron Corp. Sec., Derivative & “ERISA” Litigation, 284 F. Supp. 2d 511 (S.D. Tex. 2003).} Watkins objected to retaining the particular law firm selected to conduct the investigation.\footnote{Id.} The law firm had served as counsel to Enron with respect to the very transactions the investigation was supposed to investigate. Notwithstanding Watkins’ objections, the law firm proceeded to conduct the investigation and concluded with a finding of no improprieties.\footnote{Id.} The rest of the story is well known history—the law firm was accused of “whitewashing” the Watkins’ memo to protect its own work, the firm’s biggest client and its executive officers. Because there was substantial overlap between the law firm’s prior work and the subject matter of the investigation (as well as the extensive relational conflicts of interest), compliance with Model Rule 1.7 arguably precluded the law firm’s acceptance of the project in the first instance.

E. Are You Qualified to Conduct a Competent Investigation?

Model Rule 1.1 provides that “a lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation.” Comment 1 to Model Rule 1.1 adds color to the requirement of competence:

In determining whether a lawyer employs the requisite knowledge and skill in particular matter, relevant factors include the relative complexity and specialized nature of the matter, the lawyer’s general experience, the lawyer’s training and experience in the field in question, the preparation and study the lawyer is able to give the matter and whether it is feasible to refer the matter to, or associate or consult with, a lawyer of established competence in the field in questions. In many instances, the required proficiency is that of a general practitioner. Expertise in a particular field of law may be required in some circumstances.

Under normal circumstances, a lawyer does not necessarily need to have specialized training or prior experience to handle a matter if he or she can acquire the necessary competence through research, study and preparation. If, notwithstanding such efforts, counsel still knows he or she is incapable of handling the matter, then it must be referred to another attorney or law firm to handle. The competency standard is never to be taken lightly, but particularly in the complex role as investigating counsel.

Where the subject matter of the investigation involves a highly regulated area of law, investigating counsel is well-served to consider retaining special counsel to advise. Franchise issues are a good example of where investigating counsel may need specialized legal expertise. For example, investigating counsel may review documents reflecting that the company

\footnote{Id.}
constantly made earnings claims outside the FDD. In a normal transaction, that may be permissible so long as the claims are truthful and substantiated. In franchising, however, such conduct may violate the FTC Rule on Franchising and virtually every franchise sale law in the country. If counsel is not familiar with franchise laws, however, the whole issue may be completely missed and subsequently subject the company to system-wide class actions.

Cross border investigations are another example where specialized counsel may be appropriate to ensure competency in conducting investigations. Without a firm understanding of local law, investigating counsel may be completely blind to the lawfulness of certain conduct by company employees in foreign jurisdictions.

F. What to Do With The Results?

If investigating counsel has reached the conclusion of an internal investigation, he or she has probably avoided conflicts of interest, conducted the process with independent judgment and maintained the confidentiality and privileges available for such a process. After successfully navigating through the ethics labyrinth of an internal investigation, clients generally expect delivery of a completed report along with a recommendation. Model Rule 1.4, which is discussed in Section III.B above, should be considered before complying with any such request. Further, irrespective of who requests the final report, counsel should consult Model Rule 1.6 addressing confidentiality of information shared in an attorney-client relationship, which provides:

(a) A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation or the disclosure is permitted by paragraph (b).

(b) A lawyer may reveal information relating to the representation of a client to the extent the lawyer reasonably believes necessary:

1. to prevent reasonably certain death or substantial bodily harm;

2. 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;

3. 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;

4. to secure legal advice about the lawyer's compliance with these Rules;
to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client;

(6) to comply with other law or a court order; or

(7) to detect and resolve conflicts of interest arising from the lawyer's change of employment or from changes in the composition or ownership of a firm, but only if the revealed information would not compromise the attorney-client privilege or otherwise prejudice the client.

c) A lawyer shall make reasonable efforts to prevent the inadvertent or unauthorized disclosure of, or unauthorized access to, information relating to the representation of a client.101

In accordance with Model Rule 1.4, the first step following the completion of an internal investigation is delivering the report to the designated client representatives. But that may not be where the story ends. Of course, in the context of internal investigations, almost any one of the exceptions set forth in subparagraph (b) may apply with respect to its findings. Civil litigants and government authorities may also demand copies of the final report or information contained therein and, in some cases, it may be to the company's benefit to turn such information over. Third party requests for information from an internal investigation can also place investigating counsel in an uncomfortable position, particularly when its findings include material civil or criminal misconduct by company officers, directors or employees. Even more so if the government is figuratively knocking on the door asking for information contained in counsel's final report.

Therefore, once the investigation supervisor(s) have been provided with investigating counsel's report and other material findings, the next step largely depends upon the decision of the client. If there is no civil action pending and no investigative demand pending, presumably the client representatives will consult with counsel on taking corrective steps and implementing prophylactic measures to prevent recurrences.

G. Sharing the Report and Findings with the Government

But what if there is a government investigation pending or a government authority has requested a copy of the final report? Ever since the increased regulatory pressure on companies following the enactment of the Sarbanes-Oxley Act in 2002, it has become more common for companies to share the results of internal investigations with law enforcement in response to, or in anticipation of, a formal inquiry.102 While the obligation to report the findings of

101 Model Rule 1.6.

an internal investigation may vary based on a number of factors, disclosing the findings of the report merits serious consideration if it will help the company obtain credit for cooperation, influence the imposition of sanctions or avoid indictment. In fact, the Washington Post reported only a few years ago that the Department of Justice ("DOJ") and SEC are relying on internal investigations rather than conducting their own investigations in an effort to "save money and claim relatively easy victories."\textsuperscript{103}

In recent history, disclosure of the findings of an internal investigation has, at times, been demanded by government entities such as the DOJ and the SEC. Indeed, a 2003 DOJ memorandum by then Deputy Attorney General Larry Thompson highlighted that a corporation's "timely and voluntary disclosure of wrongdoing and its willingness to cooperate in the investigation of its agents, including, if necessary, the waiver of corporate attorney-client and work product protection" is one of the nine factors prosecutors consider when determining whether to bring charges and negotiate plea arrangements.\textsuperscript{104} After much objection to the contents of the Thompson Memorandum, Deputy Attorney General Paul McNulty issued his own memorandum in 2006 (the "McNulty Memorandum") which scaled back some of the more overreaching aspects of the Thompson Memorandum, though it did not completely eliminate the DOJ's policy of demanding the waiver of privilege by corporations.\textsuperscript{105}

Given the government's increased reliance on these findings, it can sometimes be in the company's best interest to volunteer the results of those investigations conducted internally. However, there are challenging ethical issues that arise when determining whether to voluntarily disclose the findings to the government and, if so, which portions. On one hand, it is important to provide truthful and thorough information to the government; on the other hand, it is also important to try to mitigate the risk that such information will expose the company to significant liability in subsequent third-party litigation.

\section*{H. Risks of Voluntary Disclosure}

Although providing the results of an internal investigation to a government entity may help minimize regulatory, civil and criminal exposure to the company and its officers, such voluntary disclosure can lead to additional risks. To avoid disclosing potentially harmful information, counsel may seek to apply the attorney-client privilege or work-product doctrine to material gathered during the course of an investigation. These confidentiality requirements imposed on the lawyer are designed to instill a client's trust in his or her lawyer and to encourage candid communication to assist the client with legal compliance. However, distinguishing which information gathered during the course of an investigation is considered privileged or protected can be challenging when dealing with the government.


\textsuperscript{105} The Thompson Memorandum endorsed a more routine policy of demanding waiver of the attorney-client privilege, whereas the McNulty Memorandum now requires prosecutors to obtain prior senior supervisory approval before making any such demand for a waiver.
1. **Attorney-Client Privilege**

Normally communications between counsel and employees or officers of the company in the course of an internal investigation are covered by the attorney-client privilege. The attorney-client privilege provides the company and its officers and directors important benefits. By retaining the ability to use the privilege, counsel can determine the truth of the underlying allegations while still protecting shareholder interests and preventing the investigation from impairing the reputations of employees, officers, and directors of the company not found to have engaged in wrongdoing.

It is nevertheless important to be aware that recognition of the attorney-client privilege in the context of internal investigations is not as straightforward as it might appear on the surface. In 2014, the plaintiff in *In Re Kellogg Brown & Root, Inc.* challenged the applicability of the attorney-client privilege and work product doctrine when it was asserted to protect communications between in-house counsel and employees conducted as part of a routine corporate compliance investigation required by regulatory law and corporate policy. The underlying case is a False Claims Act *qui tam* action brought by a former employee of government contractor, Kellogg Brown & Root (KBR) who alleged that KBR had inflated the costs of construction services on military bases in Iraq. In pursuing *qui tam* claims, the former employee sought production of documents generated as party of an internal investigation required by KBR’s Code of Business Conduct and government procurement regulations. The plaintiff argued that the materials should not be afforded protection because they were prepared in the ordinary course of business, and because there was no prospect of litigation or other legal proceedings at the time of the investigation. The District Court of the District of Columbia agreed with the plaintiff and ordered production of the ostensibly protected materials. On June 27, 2014, the D.C. Circuit reversed the district court’s ruling holding that it was clearly erroneous under *Upjohn v. United States*, and explaining that “the District Court’s novel approach would eradicate the attorney-client privilege for internal investigations conducted by businesses that are required by law to maintain compliance programs, which is now the case in a significant swath of American industry.” While the D.C. Circuit may have addressed KBR’s concerns in that case, the proceedings serve as a reminder to investigating counsel to be vigilant in controlling the dynamics and documentation of privileged communications. The privilege may be subject to challenge again in the future and checking off all the boxes necessary to afford protection is the best way to ensure confidentiality.

Having briefly covered the privilege and its recent challenges, the following addresses voluntary caveats to disclosing privileged communications associated with internal investigations.

a. **Voluntary Disclosure Usually Waives Privilege**

As discussed previously, when working with the government, a company may be more inclined to share information that would typically be protected to gain credit for cooperation or to reduce the impact of future sanctions and criminal allegations. While government agencies

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107 *Id.*
generally respect and support the attorney-client privilege\textsuperscript{108}, it may be in the company’s best interest to share the otherwise privileged information. The Thompson Memorandum explained how the DOJ likely views the issue—namely that waiving the privileged information “permits the government to obtain statements of possible witnesses, subjects, and targets, without having to negotiate individual cooperation or immunity agreements” and is “critical in enabling the government to evaluate the completeness of a corporation’s voluntary disclosure and cooperation.”\textsuperscript{109}

This raises an ethical dilemma though: Should investigative counsel recommend providing privileged materials to the government if it may later implicate officers or directors of the company in third-party litigation? The answer may depend on how the court treats a voluntary disclosure of privileged information to the government and the seriousness of the likely repercussions for failing to disclose.

The majority of jurisdictions find that voluntarily disclosure of protected information in the course of a government investigation deems the privilege waived for subsequent or parallel proceedings.\textsuperscript{110}

b. Selective Waiver

The Eighth Circuit alone adopts a selective waiver of privilege – that a company may voluntarily disclose privileged information to an investigating government agency without waiving the privilege in a parallel proceeding. In \textit{Diversified Indus., Inc. v. Meredith},\textsuperscript{111} the defendant corporation provided privileged communications to the SEC. In subsequent litigation, an opponent argued that the SEC disclosure waived the attorney-client privilege. The court held that the waiver of privilege only applied to actions initiated by the SEC and that the corporation could assert the attorney-client privilege to protect those released documents in all litigation involving other parties. In a court applying the selective waiver of privilege (i.e. an Eighth Circuit court), counsel can consider providing information to the government with less concern of future exposure in third-party litigation.\textsuperscript{112}

c. Restrictive Confidentiality Agreements

By contrast, the Second Circuit appears to uphold limited waivers in limited circumstances, if and only if, the parties have agreed that the privileged material will remain


\textsuperscript{109} See Thompson Memorandum. Although the Thompson Memorandum has been superseded by the McNulty memo, it is not lost on anyone that the McNulty memo is, to some degree, simply formal cover while the Thompson memo still accurately portrays how the DOJ may view corporate conduct with respect to turning over a report following an internal investigation.

\textsuperscript{110} \textit{See In re Columbia/HCA Healthcare Corp. Billing Practices Litig.}, 293 F.3d 289, 295-302 (6th Cir. 2002) (Discussing cases where voluntary disclosure of otherwise protected information waived privilege).

\textsuperscript{111} 572 F.2d 596 (8th Cir. 1977).

confidential after disclosure. The Second Circuit emphasizes that the waiver of attorney-client privilege may be avoided if the company and the government agency sign a restrictive confidentiality agreement limiting the scope of the disclosure. This rule allows companies to fully cooperate with a government agency and receive all the benefits associated with such compliance while simultaneously protecting the company’s interests in future third-party litigation.

Even though courts may have recognized that these arrangements protect the interest of both the government and the company, some Second Circuit courts may not uphold these agreements if they are executed before the internal investigation has taken place. The concern here is based on the well-established principle that “communications between client and attorney for the purpose of relaying communication to a third party [are] not confidential and not protected by the attorney-client privilege.” In other words, if counsel initiates communication with a client with the anticipation of sending those notes to the government pursuant to a confidentiality agreement, that communication may no longer be privileged.

For example, in In re Mckesson, the court expressly held that the attorney-client privilege did not protect materials presented to a government agency from third-party discovery, even though the company signed a confidentiality agreement with the SEC and the United States Attorney’s Office (USAO). There, corporate counsel agreed to disclose the findings of their internal investigation prior to conducting any communications with their client. The court found that since the communication was made with the expectation that the results would be shown to a third-party, the attorney-client privileged was waived. Specifically, the court held,

Where, as here, there is an agreement by the client that provides for the disclosure to a third party of the communications between a client and attorney in advance of those communications being made, the communications disclosed pursuant to that agreement are not confidential and the goals of the attorney-client privilege are not in play.116

Presumably, if the counsel in In re Mckesson had made the agreement with the SEC and USAO after conducting an internal investigation, the privileged communications would be protected because they would not have been made with the expectation that the findings would be delivered to a third-party.

Thus, because of the potential power of restrictive confidentiality agreements, corporate counsel should consider delaying an agreement with a government agency until after all privileged communications have been made. Doing this may allow the affected employees,

113 See In re Steinhard Partners, L.P., 9 F.3d 230 (2d Cir. 1993).

114 United States v. Bergonzzi, 216 F.R.D. 487, 493 (N.D. Cal. 2003) (citing United States v. Sudikoff, 36 F. Supp. 2d 1196, 1204-05 (C.D. Cal. 1999)); see also United States v. Bump, 605 F.2d 548, 550–51 (10th Cir. 1979) (“When a matter is communicated to the lawyer with the intention or understanding it is to be repeated to another, the content of the statement is not within the privilege.”); United States v. Tellier, 255 F.2d 441, 447 (2d Cir. 1958) (“Thus it is well established that communications between an attorney and his client, though made privately, are not privileged if it was understood that the information communicated in the conversation was to be conveyed to others.”).


116 Id. at *4.
officers, and directors to be forthcoming while protecting the interests of the company to strike a deal with the government.

2. Work-Product Doctrine

It is critical for counsel to consider the interplay between the attorney-client privilege and work-product doctrine from the onset as well. There have been decisions where the attorney-client privilege was waived, but the information was still protected by the work-product doctrine. This is because work product protection generally protects interview notes, especially those interspersed with statements of counsel's mental impressions and strategies.

For instance, in In re Mckesson (discussed above), the Court held that although the attorney-client privilege did not protect the materials presented to the government, the same materials could be withheld under the work-product doctrine. Generally, if work-product protection is waived as to one adversary, it is waived as to all adversaries. Since the relationship with the government is considered adversarial at the onset of an investigation, the work product protection would likely be waived to all current and future opponents for information shared with the government.

However, the In re Mckesson court applied the doctrine of selective waiver, which fundamentally permits a party to disclose work product to one adversary, but not to others. The court reasoned that because “[t]he work product privilege rests on the belief that ... promotion of adversary preparation ultimately furthers the truth-finding process,” there is a “distinction between disclosure to a private entity (resulting in waiver) and disclosure to a government entity pursuant to a confidentiality agreement (maintaining work product protection).”

Interestingly, the court’s decision in regard to work product is founded on the same confidentiality agreement that was held unenforceable with regards to attorney-client privilege. This again underscores the importance of pursuing a restrictive confidentiality agreement when reporting findings of an investigation to a government entity.

Many government agencies support selective waiver because it encourages companies to disclose information without necessarily waiving privilege. Nevertheless, most jurisdictions


\[119\] In re Steinhardt Partners, L.P., 9 F.3d 230, 235 (2d Cir. 1993).

\[120\] See, e.g., Diversified Industries, Inc., 572 F.2d at 611 (applying the selective waiver theory in finding that work product disclosures made to SEC during a private investigation did not waive protection even without a confidentiality agreement in place).

\[121\] United States v. Am. Tel. & Tel. Co., 642 F.2d 1285, 1300 (D.C. Cir. 1980).

\[122\] Mckesson, 2005 WL 934331 at *9.

that have considered the issue fail to distinguish a difference between disclosing protected information to government agencies or to other third parties, essentially rejecting the selective waiver theory. While this may dis-incentivize cooperation in government investigations, it is likely more in line with the traditional standards for work-product doctrine.

Given the different treatment by courts and differing approaches by various government agencies, it is important for investigative counsel to document and identify all privileged and protected legal information from the onset of an investigation. Accordingly, all legal theories related to investigative facts, mental impressions and legal conclusions should be memorialized to attempt to preserve these protections from subsequent third-party litigation. This may provide counsel comfort with its submissions to the government, while still protecting its ethical obligations to the client.

V. Duties Contacting Current and Former Employees

During the course of a representation, counsel may be required to contact a client’s unrepresented current or former employees or those of a party opponent. In all such scenarios, three Rules of Professional Conduct should be considered: Model Rule 4.2 (Communication with Person represented by Counsel); Model Rule 4.3 (Dealing with Unrepresented Persons); and Model Rule 4.4 (Respect for Rights of Third Parties). Each of these rules is set forth below:

Model Rule 4.2: Communication with Person represented by Counsel

In representing a client, a lawyer shall not communicate about the subject of the representation with a person the lawyer knows to be represented by another lawyer in the matter, unless the lawyer has the consent of the other lawyer or is authorized to do so by law or a court order.

Model Rule 4.3: Dealing with Unrepresented Person

In dealing on behalf of a client with a person who is not represented by counsel, a lawyer shall not state or imply that the lawyer is disinterested. When the lawyer knows or reasonably should know that the unrepresented person misunderstands the lawyer’s role in the matter, the lawyer shall make reasonable efforts to correct the misunderstanding. The lawyer shall not give legal advice to an unrepresented person, other than the advice to secure counsel, if the lawyer knows or reasonably should know that the interests of such a person are or have a reasonable possibility of being in conflict with the interests of the client.

Model Rule 4.4: Respect for Rights of Third Persons

(a) In representing a client, a lawyer shall not use means that have no substantial purpose other than to embarrass, delay, or burden a third person, or use methods of obtaining evidence that violate the legal rights of such a person.

(b) A lawyer who receives a document or electronically stored information relating to the representation of the lawyer’s client and knows or reasonably should know that the document electronically stored information was inadvertently sent shall promptly notify the sender.

A. Communications with a Client’s Current and Former Employees

Contacting a client’s current employees is relatively straightforward and regularly occurs in the ordinary course of the representation of a company. While these communications are often taken for granted, counsel should give full consideration to the fact the employee may technically be unrepresented and also give deference, where appropriate, to the employee’s rights of privacy as discussed in Sections IV.D.1.a and IV.D.1b above. Compliance with the guidelines set forth in *Upjohn v. United States*\(^{125}\) can help to ensure counsel’s conduct conforms to applicable ethical standards. Specifically, counsel should clearly communicate that (1) he or she represents the company (unless, of course, the company extends counsel to the employee as well); (2) the communications between them shall be protected by the attorney-client privilege of the company, meaning that the employee cannot waive the confidential nature of the discussions but the company can; and (3) the company may choose, at its option, to waive the privilege at any time. Giving an *Upjohn* warning to every client employee may be viewed as overkill, and it may very well be. This is because *Upjohn* warnings may create tension in discussions with employees, cause them to question their relationship with their employer and inadvertently result in minimizing the employee’s efforts to support the employer in the legal proceedings. The downside to not giving some disclosure to a client’s employee, however, can result in the employee—deliberately or unwittingly—waiving the company’s privilege and sharing critical information and strategy with others. Outside of the internal investigation context, it is unlikely that there will be a need to give any current employees a *Zar* warning.\(^{126}\)

Communications with former employees of the client should not become any more complex. While the Supreme Court in *Upjohn* did not address whether a company’s attorney-client privilege extends to communications between company counsel and former employees, there is really no meaningful distinction between the two types of communications. Accordingly, the principal foundation of the *Upjohn* case applies here as well. Written confirmation of these facts can be delivered to former employees and, if drafted properly, can avoid having an adverse effect on the former employee’s willingness to cooperate. One factor to consider, however, is whether to obtain the consent from the General Counsel for the current employer of the former employee before doing so. This is perhaps less important with respect to lower level employees as opposed to managerial employees and above. Assuming the substance of the communications will not involve the affairs of the current employer, consent is not required though it may still make good business sense to obtain such consent. If a company’s General Counsel learns that a third party’s attorney is interviewing a company employee without prior authorization, one potential may response may be to intervene and instruct the third party’s counsel that all future communications must go through counsel. Because the third party counsel’s issue will probably not be a high priority, such an event may effectively cut off any future informal access to the employee.

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B. Contacting Current Employees of Party Opponent

Contacting a current employee of a represented party without opposing counsel’s consent is usually presumed to be prohibited. However, such prohibition is not as comprehensive as typically assumed. This is because Model Rule 4.2, commonly referred to as the “no contact” rule and printed in full in Section V above, prohibits communications with a represented party. While practitioners are often generally familiar with the bright line “no contact” rule, a closer examination of subtle distinctions in the rule is warranted when business entities or associations are involved. Historically, state courts have applied a broad spectrum of tests to determine whether counsel can ethically pursue ex parte communications with current employees of a party opponent.\(^{127}\) The tests varied so much by jurisdiction that it became difficult to achieve any level of comfort with efforts to investigate claims through ex parte interviews of a party opponent’s current employees. Because such ambiguity often stymied legitimate efforts to interview witnesses, it weighed heavily in favor of counsel representing companies but played poorly within the plaintiff bar.

The California Court of Appeal decision in \textit{Snider v. Superior Court}\(^ {128}\) reviewed the various approaches to the “no contact” rule taken by California courts, the Model Rules and out-of-state courts before reaching its conclusion. In \textit{Snider}, an event design and construction company named Quantum sued its former employee Snider and his newly-formed event design and construction company for misappropriation of trade secrets and unfair competition. After Quantum’s counsel identified percipient witnesses at the initial case management conference, Snider’s counsel proceeded to interview two current Quantum employees (a sales manager and a director of production) on Quantum’s witness list—neither of whom had consulted with Quantum’s counsel about the case. When Quantum’s counsel learned of the communications by Snider’s counsel, he filed a petition for writ of mandate seeking to disqualify Snider’s counsel for having ex parte communications with Quantum’s current employees without authorization. The trial court issued the writ finding that opposing counsel had violated the California equivalent of Model Rule 4.2.\(^ {129}\) The appellate court reversed, concluding that the two current employees were not “represented parties” within the scope of the California Rules of Professional Conduct. The court of appeal based its decision on California Rules of Professional Conduct 2-100 and its conclusion that the two employees “(1) were not ‘officer[s], director[s] or managing agent[s]’ of the organization; (2) the subject matter of the communications was not an act or omission of the employees that could be binding or imputed

\(^{127}\) See, e.g., \textit{Fair Automotive Repair, Inc. v. Car-X Service Systems, Inc.}, 471 N.E.2d 554, 560-61 (Ill.Ct.App. 1984) (only applying “no contact” rule to “top management persons who had the responsibility of making final decisions”); \textit{Apple Corps. Ltd. v. Int’l Collectors Soc.}, 15 F.Supp.2d 519, 526-27 (prohibiting contacts with “litigation control group” defined as those with significant involvement in determination of corporation’s legal position); \textit{Baisley v. Missisquoi Cemetery Assoc.}, 708 A.2d 924 (Vt. 1998) (refusing to allow contact because employee would be source of a party admission); \textit{In re Air Crash Disaster near Roselawn}, 909 F.Supp. 1116, 1121 (N.D. Ill. 1995) (imposing broad prohibition because “virtually every employee may conceivably make admissions binding on his or her employer”); \textit{Chambers v. Capital Cities/ABC}, 159 F.R.D. 441, 442-43 (S.D.N.Y. 1995) (endorsing magistrate decision to forbid communication with all current employees of opposing party); and \textit{Lang v. Reedy Creek Improvement Dist.}, 888 F.Supp. 1143 (M.D.Fla. 1995 (ex parte contact with opposing party’s current employees only permitted with prior court approval).


\(^{129}\) California Rules of Prof’l Conduct, Rule 2-100 limits the prohibition on ex parte communications to opposing party’s current “officer, director or managing agent” or if such person’s statement “may be binding upon or imputed to the organization for purposes of civil or criminal liability or whose statement may constitute an admission on the part of the organization.”
to the organization; and (3) they were not employees whose statements might constitute admissions on behalf of the organization.\textsuperscript{130} The court also issued guidance to counsel who desire to contact employees of a represented organization, stating that they “should endeavor to ensure, prior to the contact, that the employee, either because of his or her status within the organization or the subject matter of the proposed communication, does not come within the scope of rule 2-100.”\textsuperscript{131} The court further noted that “once contact is made, counsel should at the outset pose questions designed to elicit information that would determine whether the employee comes within 2-100’s scope and should not ask questions that could violate the attorney-client privilege.”\textsuperscript{132} The standard applied by the \textit{Snider} court accurately reflected the application of California law, but it also concurrently underscored the differences among the states regarding application of the “no contact” rule.

In 2002, the Comment to Model Rule 4.2 was amended as part of an effort to end confusion about the ethical limitations of contacting current employees of a party opponent. Under the revised guidance, the ability to engage in \textit{ex parte} communications with a party opponent’s employees is now governed by whether the current employee “supervises, directs or regularly consults with the organization’s lawyer concerning the matter” at issue. Specifically, Comment 7 to ABA Model Rule 4.2 provides:

\begin{quote}
In the case of a represented organization, the Rule prohibits communications with a constituent of the organization who supervises, directs or regularly consults with the organization’s lawyer concerning the matter or has authority to obligate the organization with respect to the matter or whose act or omission in connection with the matter may be imputed to the organization for purposes of civil or criminal liability.\textsuperscript{133}
\end{quote}

State law on this issue can still vary but almost all of the jurisdictions have adopted the Model Rules in substantial part. For example, Comment 4 to Massachusetts Rule of Professional Conduct 4.2 provides:

\begin{quote}
In the case of an organization, this Rule prohibits communications by a lawyer for another person or entity concerning the matter in representation only with those agents or employees who exercise managerial responsibility in the matter, who are alleged to have committed the wrongful acts at issue in the litigation, or who authority on behalf of the organization to make decisions about the course of the litigation.\textsuperscript{134}
\end{quote}

\textsuperscript{130} 7 Cal.Rptr.3d at 121-122.

\textsuperscript{131} Id. at 122.

\textsuperscript{132} Id.


\textsuperscript{134} See \textit{e.g.} New York Rules of Prof’l Conduct, Rule 4.2, cmt. 7.
It has yet to be determined whether the amendment to Comment 7 has successfully clarified the application of the “no contact” rule to current employees of a party opponent. Subsequent cases, however, reflect that courts are implementing the intent of the amendment—to narrow the scope of the “no contact” rule. For example, a number of jurisdictions have expressed approval of *ex parte* communications with an opposing party’s current employees.135

One published decision regarding improper *ex parte* communications in the franchise context is *Midwest Motor Sports v. Arctic Car Sales, Inc.*,136 where a franchisee sued its franchisor for wrongful termination and the improper sale of a franchise to a new franchisee for the same territory. The terminated franchisee also named the new franchisee as a defendant. To assess the franchisee’s claim for $1 million in damages, the franchisor’s counsel sent a private investigator to the showrooms of the new franchisee and the former franchisee to tape record their respective employees’ statements regarding sales volumes and practices, including the interview of the new franchisee’s president as opposed to lower level employees. Applying South Dakota Rules of Professional Responsibility (modeled on Rule 4.2), the Eighth Circuit upheld evidentiary sanctions against the franchisor’s counsel finding that the investigator’s inquiry about the new franchisee’s sales volume constituted impermissible *ex parte* communications about the subject of the representation. The sanctions included the exclusion from evidence at trial the recordings made by the private investigator and any evidence obtained as a result of those recordings. The court’s decision was likely driven by the fact that the private investigator interviewed the president of the franchisee. It is not clear if the district court or the Eighth Circuit would have reached the same decision had the investigator limited his surreptitious contacts to other rank and file salespersons and/or sought different information.

Outside of the changes addressed by the 2002 Amendment to Comment 7 of Model Rule 4.2, there still are other circumstances that continue to require a case-by-case analysis. For example, courts and state bar ethics decisions expressly authorize communication with a corporate opponent’s in-house counsel, even when outside counsel has been retained by the company.137 Contacting putative class members is also permitted.138 On the other hand, the mere fact that a licensed attorney is representing himself in litigation does not necessarily


136 347 F.3d 693 (8th Cir. 2003).


enable him to communicate with a party opponent’s officers and directors. For example, if a franchisee is also a licensed attorney and pursues a claim on behalf himself, the fact that he is also a “party” to the litigation does not necessarily open the lines of communication with a represented franchisor’s officers and directors while the litigation remains pending.139

Other circumstances that require a fact intensive analysis involve anonymous and transparent communications by counsel with an opponent’s current employees through social media, such as Facebook and LinkedIn. Efforts to “friend” or “link”, at a minimum, constitute indirect ex parte communications with a represented party for purposes of Model Rule 4.2. However, the initial social media communications are not necessarily about matters related to the litigation, they may still be wholly permissible. The ethical rules regarding social media communication are no different than those applied to other mediums. Therefore, a determination regarding whether such an effort complies with ethics rules mandates an evaluation of the intended purpose behind the communication through social media. If the intended purpose is unrelated to the litigation, then the communication is likely permissible. On the other hand, if the intended purpose is to obtain information related to the litigation, the standard set forth in Comment 7 to Model Rule 4.2 applies. Because counsel’s intent will likely never be clear cut, pursuing ex parte communications with party opponent’s current employees may help uncover facts, but it is not without risk of sanction by the presiding court or censure by the applicable state bar.

C. Contacting Former Employees of the Party Opponent

Interviews of a party opponent’s former employees are often the most fruitful and least expensive form of fact investigation. Contacting former employees of a party opponent does not typically require the consent of the party opponent’s lawyer. This is because, according to the American Bar Association, individuals who are no longer associated with the company are not covered by Model Rule 4.2.140 This is not, however, a blanket rule across all jurisdictions and it does not give counsel an unfettered ability to elicit information from former employees.

Similar to the application of the “no contact” rule with respect to a party opponent’s current employees, state courts have varied in the breadth of their application of the “no contact” to a party opponent’s former employees. Indeed, historically some courts have presumptively swept all former employees of an opposing party under the “no contact” rule.141 Today, however, the Comment to Model Rule 4.2 reflects an appreciation of the fact that a party opponent’s former employees are fair game to be interviewed. There are circumstances, however, where such communications may still be frowned upon and counsel should be circumspect in how to proceed. For example, if the former employee participated substantially in the legal representation of the organization in the matter, certain jurisdictions may preclude

139 See In re Knappenberger, 108 P.3d 1161 (Or.2005) (en banc) (lawyer sued by two employees violated “no contact” rule by speaking to his employees about the action); Fishelson v. Skorupa, 2001 WL 888369 (Mass.Super.Ct. July 31, 2001) (represented party still entitled to protection of “no contact” rule even when opposing party is a licensed attorney).


communicating with former employees without the permission of counsel. Similarly, in other jurisdictions, ex parte communications with former employees is permissible so long as he or she did not serve as a “principal decision maker” in the determination of the organization’s legal position in the pending matter. There also are a handful of jurisdictions which have held that ex parte interviews of all former employees of a party opponent’s “litigation control group” are prohibited unless the individual employee or party opponent subsequently disavows representation.

Further, when communicating with a party opponent’s former employee, certain safeguards must still be adhered to irrespective of which jurisdiction’s laws apply. First, counsel is required to disclose the identity of his or her client at the outset of any such communications. Second, counsel must make sure not to provide any such third parties with legal advice. Third, counsel should make sure not to solicit from the former employee the disclosure of information otherwise protected by the opposing party’s attorney client privilege. In fact, in the event there is a confidentiality agreement with provisions that remain intact, inducing the former employee to disclose confidential information may expose counsel to claims for interference with contract.

As with communications with any other third party, a lawyer should proceed cautiously in communicating with former employees of a party opponent and confer with counsel licensed to practice in the applicable jurisdiction. Of course, if the former employees are represented by their own counsel in the matter, the bar against communication without consent of that counsel applies unless that communication is otherwise authorized by law.

VI. Communicating with Other Third Parties

A. Duty Communicating with Court or Tribunal

Rule 3.3 of the Model Rules, entitled “Candor Towards the Tribunal,” states:

(a) A lawyer shall not knowingly:

142 See N.C. Rules of Prof’l Conduct R. 4.2, cmt. 9 (applying the “no contact” rule to individuals who had substantive discussions with company counsel about the matter at issue).

143 Iowa Rules of Prof’l Conduct, Rule 4.2, cmt 11.

144 The term “litigation control group” has been defined to include “current agents and employees responsible for, or significantly involved in, the determination of the organization’s legal position in the matter whether or not in litigation, provided, however, that ‘significant involvement’ requires involvement greater, and other than, the supplying of factual information or data respecting the matter.” New Jersey Rules Of Prof’l Conduct, Rule 1.13(a).

145 See New Jersey Rules of Prof’l Conduct, Rules 4.2 and 1.13 (stating that former agents and employees who were members of the litigation control group shall presumptively be deemed represented in the matter by the organization’s lawyer but may at any time disavow said representation).

146 For a comprehensive discussion regarding the guidelines for preliminary disclosures and discussion with former employees of a party opponent, see, e.g., Revere Transducers, Inc. v. Deere & Co., 595 N.W.2d 751, 762 (Iowa 1999); and Snider v. Superior Court, 113 Cal.App.4th 1187 (2003).

147 Model Rule 4.2.
(1) make a false statement of fact or law to a tribunal or fail to correct a false statement of material fact or law previously made to the tribunal by the lawyer;

(2) fail to disclose to the tribunal legal authority in the controlling jurisdiction known to the lawyer to be directly adverse to the position of the client and not disclosed by opposing counsel; or

(3) offer evidence that the lawyer knows to be false. If a lawyer, the lawyer's client, or a witness called by the lawyer, has offered material evidence and the lawyer comes to know of its falsity, the lawyer shall take reasonable remedial measures, including, if necessary, disclosure to the tribunal. A lawyer may refuse to offer evidence, other than the testimony of a defendant in a criminal matter, that the lawyer reasonably believes is false.

(b) A lawyer who represents a client in an adjudicative proceeding and who knows that a person intends to engage, is engaging or has engaged in criminal or fraudulent conduct related to the proceeding shall take reasonable remedial measures, including, if necessary, disclosure to the tribunal.

(c) The duties stated in paragraphs (a) and (b) continue to the conclusion of the proceeding, and apply even if compliance requires disclosure of information otherwise protected by Rule 1.6.\(^{149}\)

The Comments to this Model Rule sets forth the special duties of lawyers as officers of the court to avoid conduct that undermines the integrity of the adjudicative process, as follows:

A lawyer acting as an advocate in an adjudicative proceeding has an obligation to present the client's case with persuasive force. Performance of that duty while maintaining confidences of the client, however, is qualified by the advocate's duty of candor to the tribunal. Consequently, although a lawyer in an adversary proceeding is not required to present an impartial exposition of the law or to vouch for the evidence submitted in a cause, the lawyer must not allow the tribunal to be misled by false statements of law or fact or evidence that the lawyer knows to be false.\(^ {150}\)

For purposes of application of this Rule, the term “tribunal” has been defined to include “a court, an arbitrator in a binding arbitration proceeding or a legislative body, administrative

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\(^{149}\) Rule 3.3 (d) omitted (discussing the expectation of candor in ex-parte proceedings).

\(^{150}\) Model Rule 3.3, cmt. 2.
agency, or other body acting in an adjudicative capacity.

Courts have construed the phrase “acting in an adjudicative capacity” to mean “when a neutral official, after the presentation of evidence or legal argument, . . . will render a binding legal judgment directly affecting a party’s interests in a particular matter.” The duty not only applies when presenting or otherwise submitting materials to the tribunal, but also in proceedings that are ancillary to those before a tribunal, such as a deposition or other discovery-related proceeding.

Importantly, the rule applies irrespective of whether the statement is made orally or in writing, and whether in an affidavit, a pleading, or other document. Violations of this rule can occur not only by affirmatively misleading statements, but they can also occur as a result of omissions that result in misleading the tribunal through silence. It also may be immaterial whether the affirmative misrepresentation is substantive or merely procedural.

In the regular practice of law, compliance with this rule may not appear difficult. The rule, however, can place counsel in difficult positions where tensions between compliance with different rules occurs, such as when compliance with the duty of candor, on the hand, may require conduct that is different from compliance with the duty of confidentiality or the duty of loyalty, on the other hand. For example, consider the situation where counsel for a franchisor—being sued by a franchisee for making unlawful financial performance—appears before a district court judge to present a motion to compel the production of documents early in the case. At the hearing, the district judge puts aside the motion and asks counsel a rather pointed question—whether his client’s representative actually made the alleged financial representations. If counsel knows that representations were in fact made, counsel must decide whether to answer the judge’s question directly and truthfully to comply with the duty of candor, knowing full well that such a concession may irretrievably concede liability for the franchisor client. Model Rule 3.3(c) is designed to directly address that issue and require counsel to truthfully answer the court’s question, even at the expense of the duty of confidentiality. Another circumstance where the duty of candor can be the cause for discomfort may occur when a client provides knowingly false testimony in deposition. Arguably, and depending upon the materiality of the false testimony.
statement, the duty of candor may require counsel to correct the testimony, and a failure to do so may render counsel complicit with the deponent.  

Therefore, while practitioners may often simply assume that the duty of candor will never be an issue for them, the ability to comply may not always be as simple and straightforward as it may appear in the abstract.

**B. Duty Communicating with Opposing Counsel**

Model Rule 4.1 is entitled “Truthfulness in Statements to Others” and provides:

In the course of representing a client a lawyer shall not knowingly:

(a) make a false statement of material fact or law to a third person; or

(b) fail to disclose a material fact to a third person when disclosure is necessary to avoid assisting a criminal or fraudulent act by a client, unless disclosure is prohibited by Rule 1.6.

Generally, counsel have no affirmative duty to advise opposing counsel of relevant facts. The rule covers most communications. However, counsel can often get embroiled up when he or she inadvertently incorporates or otherwise adopts the false statements by a client or a third party.

One question practitioners may ask is whether their thoughts or recollection can constitute “knowledge” of a falsity such that it triggers the obligations under Rule 4.1. If counsel merely believes there is a probable falsity regarding a fact, such a belief would probably be insufficient to trigger an ethical violation. The ethical rules also make a distinction between actual knowledge of a falsity—which would trigger a violation—and what counsel should have known to be false—which would not trigger a violation.

A failure to understand the distinction between permissible advocacy and the false statement of a material fact can lead to serious issues under Model Rule 4.1. For example, during negotiations, it may be permissible for counsel to “exaggerate or emphasize strengths, and minimize or deemphasize the weaknesses, of its factual or legal position” because such comments are recognized as posturing or puffing. Such statements, however, must be distinguished from false statements of material facts, which counsel is prohibited from making to opposing counsel. Counsel’s false statement of a material fact in unprivileged settlement

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157 See Bruce A. Green, *Ethically Representing a Lying Cooperating: Disclosure as the Nuclear Deterrent*, 7 Ohio St. J. Crim. L. 639, 642 (Spring 2010).

158 Brown v. Genesee County, 872 F.2d 169 (6th Cir. 1989) (no legal or ethical duty to correct a statement which counsel "believed it probable" that her client was mistaken as to facts);

159 In re Tocco, 984 P.2d 539 (Az. 1999) (“mere showing that the attorney reasonably should have known her conduct was in violation of the rules, without more, is insufficient”).

negotiations can lead to claims for conspiracy to defraud against counsel and client, as well as reprimand by the relevant state bar associations.\footnote{161}

1. **Communications During Mediation**

Communications outside the scope of mediation certainly must comply with Rule 4.1. But what happens in the setting of a caucused mediation covered by the mediation privilege? And if Rule 4.1 is violated in mediation, does the mediation privilege have an exception for reporting or otherwise addressing violations of Rule 4.1?

The short answer is that while Rule 4.1 always applies, the ABA Standing Committee on Ethics and Professional Responsibility has expressly condoned “puffing” in mediation. Specifically, the Standing Committee noted:

Under the Model Rule 4.1, in the context of a negotiation, including a caucused mediation, a lawyer representing a client may not make a false statement of material fact to a third person. However, statements regarding a party’s negotiating goals or its willingness to compromise as well as statements that can be fairly characterized as negotiation ‘puffing’ ordinarily are not considered ‘false statements of material fact’ within the meaning of the Model Rules.\footnote{162}

The Standing Committee’s note begs the question, “what recourse exists if false statements are made at a mediation where a mediation privilege applies?”

Section 4(a) of the Uniform Mediation Act provides that “a mediation communication is privileged . . . and is not subject of discovery or admissible in evidence in a proceeding unless waived or precluded as provided by Section 5.”\footnote{163} Subsection (b) describes the scope of the privilege. A party to a mediation may refuse to disclose, and may prevent any other person from disclosing, a mediation communication of any participant. A mediator may refuse to disclose, and may prevent any other person from disclosing, a mediation communication of the mediator. A nonparty participant may refuse to disclose, and may prevent any other person from disclosing, a mediation communication of the nonparty participant. Subsection (c) contains an exception for “evidence or information that is otherwise admissible or subject to discovery.” In the Reporter’s Notes, the drafters explain that “it is the communication that is made in a mediation that is protected by the privilege, not the underlying evidence giving rise to the communication.”

Therefore, one party’s counsel cannot reveal to third parties or attempt to introduce as evidence statements made during the mediation by the adversary or its counsel, except with opposing counsel’s consent. It seems unlikely that opposing counsel would consent to a waiver of the mediation privilege so that the other party’s counsel can raise an objection regarding compliance with ABA Model Rule 4.1. So, while Model Rule 4.1 does in fact apply in the

\footnote{161}{For a detailed analysis of this issue, see Ausherman v. Bank of Am. Corp., 212 F.Supp.2d 435 (D.Md. 2002).}

\footnote{162}{See ABA Comm. on Ethics and Prof’l Responsibility, Formal Opn. No. 06-439 (2006).}

\footnote{163}{National Conference of Commissioners on Uniform State Laws, Uniform Mediation Act (Aug. 2001)(adopted by the ABA House of Delegates in February 2002).}
context of a caucused mediation—with qualification, it may be a rule with no teeth because enforcement might effectively never occur.

C. Duty Communicating with the Government

Similar to communications with opposing counsel in an ordinary setting, Model Rule 4.1 also applies in the context of communications with the government—both in and out of court. The only difference is that a failure to be candid with the government is a failure to do so with the same party that is responsible for enforcement, particularly when submissions must be made under penalty of perjury.

In their efforts to be forthcoming and complete in disclosure, corporate counsel may inadvertently provide information to the government that is either incorrect, incomplete or protected by the attorney-client privilege or work-product doctrine. In this situation, counsel has an ethical and legal responsibility to recant the improper information as quickly and as accurately as possible. Thus, lawyers engaged in communications with the government need to be aware of the federal criminal and evidentiary statutes to avoid potential criminal allegations and ethical violations.

1. Perjury

Perjury is addressed in sections 1621 and 1623 of the criminal code.\footnote{18 U.S.C. §§ 1621 and 1623.} Section 1621, the older and more broad perjury statute, forbids willful false testimony given under oath “in any case in which a law of the United States authorizes an oath to be administered.”\footnote{Id.} Section 1623 is more specific, applying only to false declarations made in proceedings before or ancillary to any court or grand jury. While these statutes are mainly triggered when testifying before a court, the Supreme Court has construed the term “ancillary proceeding” to apply to pretrial depositions in criminal cases.\footnote{Dunn v. United States, 442 U.S. 100, 107-13 (1979).}

2. False Statements to the Government

Counsel should be aware that willfully false statements made at any point during the investigative process may still implicate criminal perjury statutes, even if not made under oath. False statements made to the government are covered by 18 U.S.C. § 1001. This broad section generally prohibits knowingly and willfully making false or fraudulent statements, or concealing information, in “any matter within the jurisdiction” of the federal government of the United States.\footnote{18 U.S.C. § 1001.} This statute is used in many contexts by the government to prosecute concealment of other crimes and false statements made in criminal investigations, including those made in response to a government inquiry.\footnote{United States Attorneys’ Manual, Title 9, Criminal Resource Manual § 916 (last visited June 17, 2014).} Therefore, because of the broad reaching nature of this statute, even false statements that are voluntarily disclosed to government agencies can be criminally prosecuted.

\footnote{164 18 U.S.C. §§ 1621 and 1623.}
\footnote{165 Id.}
\footnote{166 Dunn v. United States, 442 U.S. 100, 107-13 (1979).}
\footnote{167 18 U.S.C. § 1001.}
\footnote{168 United States Attorneys’ Manual, Title 9, Criminal Resource Manual § 916 (last visited June 17, 2014).}
3. **Obstruction of Justice**

Although perjury statutes and the false statements statutes criminalize untrue statements made to a federal officer, the obstruction of justice statutes also cover a broader range of circumstances. For example, the main obstruction of justice statute, 18 U.S.C. § 1503, makes it unlawful to “corruptly … endeavor[ ] to influence, obstruct, or impede, the due administration of justice….” To be found guilty under § 1503, the government must prove, inter alia, that the defendant intended to impede the administration of a judicial proceeding. While courts have generally found that a law-enforcement investigation is not, by itself, a judicial proceeding, counsel should be aware that making false statements that end up in front of a grand jury or other court proceeding could be subject to criminal prosecution under § 1503.

4. **Doctrine of Recantation**

If incorrect information is submitted to the government during an investigation or inquiry, counsel must act quickly and efficiently to mitigate the problem. The steps that counsel need to take to fulfill their ethical and legal obligation to retract incorrect information may depend on what stage the government investigation or inquiry is in.

At first, it might be appropriate for counsel to communicate directly with the government agency that was given the incorrect information. This is especially true if the information was made pursuant to a government inquiry or a confidentiality agreement because the government may be more forgiving if the corporation has been cooperating with the investigation all along.

However, if the criminal charges are already being pursued, either against the corporation, its officers or directors, or even against counsel, the government will likely not be as willing to forgive a mistake. Depending on what criminal charges were brought, a defendant in that scenario may have the opportunity to recant the information during a formal proceeding. For example, one of the perjury statutes, Section 1623, explicitly makes recantation a defense. In order to trigger the defense, the recantation must occur in “the same continuous court or grand jury proceeding in which [the false] declaration is made,” and it must occur before the perjury has “substantially affected the proceeding” and before it “become[s] manifest [to the perjurer] that [the perjury] has been or will be exposed.” However, if the information is not immediate, the government will likely succeed in a claim that the original perjury was already manifest or had substantially affected the proceeding.

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171 Internal Corporate Investigations, Perjury and Obstruction of Justice, 131-32, (Barry F. McNeil & Brad D. Brian eds., ABA Section of Litigation 3d. ed. 2007).


173 18 U.S.C. § 1623(d); Internal Corporate Investigations, Perjury and Obstruction of Justice, 126, (Barry F. McNeil & Brad D. Brian eds., ABA Section of Litigation 3d. ed. 2007); see also United States v. Denison, 663 F.2d 611 (5th Cir. 1981); United States v. Moore, 613 F.2d 1029 (D.C. Cir. 1979), cert. denied, 446 U.S. 954 (1980).

174 See United States v. McAfee, 8 F.3d 1010, 1016 (5th Cir. 1993) (finding that recantation by a witness during a second deposition of testimony provided during a prior deposition held not to satisfy Section 1623(d)).
This again underscores the significance of providing truthful information to the government upfront. The ethical balance between representing the best interests of the client while avoiding misleading statements to the government can be tricky. Thus, careful evaluation is necessary to ensure both the client and the attorney avoid any additional problems in the future.

5. Attorney-Client Privileged or Work Product Protected Information

In the process of the investigation, counsel may inadvertently disclose information to the government that is attorney-client privileged or work product protected. In this case, it might be in the company's best interest to try to retract such information to avoid many of the problems discussed above with regards to the waiver of these protections in subsequent third-party litigation.

Fortunately, Federal Rules of Evidence, Rule 502\textsuperscript{175}—enacted in 2008—provides counsel and the privilege with some additional protections from inadvertent disclosure. FRE 502(b) provides that when an inadvertent disclosure of privileged materials is made in a federal proceeding, it does not operate as a waiver if "(1) the disclosure is inadvertent; (2) the holder of the privilege or protection took reasonable steps to prevent disclosure; and (3) the holder promptly took steps to rectify the error."\textsuperscript{176}

a. Practical Withdrawal

If it is discovered that privileged information was disclosed to the government, the first step is to try to recover that information by contacting the government agency. In a discussion on how counsel should withdraw submissions to a government agency once an inadvertent disclosure of privileged information is made, an SEC investigator commented:

We do not adjudicate whether or not a record is privileged. This is true even when you accidentally give us something that you later say is privileged. We have a procedure for that. If you timely contact us and say "we accidentally gave you something, can we have it back," we will generally ask you to give us a letter explaining why you still believe it is still privileged, and we will ask you to sign a letter agreement. It is a standard letter that basically says we are giving it back to you and in return you will not assert any fruit of the poisonous tree against us. And we've actually done that several times. We have also said no. Usually the reason we say no is somebody waits five or six months before they call up and say "we gave you something by accident and we want it back." At that point, we say, we cannot unscramble the omelet.\textsuperscript{177}

\textsuperscript{175} FRE 502 specifically sanctions "clawback" agreements in which parties agree that inadvertent production of privileged materials can be cured and waiver avoided by a demand for return of the inadvertently produced materials.

\textsuperscript{176} For a greater discussion regarding the implications of FRE 502, please see Eric H. Karp and Les Wharton, \textit{Hot Button Privilege Issues For Franchise Counsel}, ABA Forum on Franchising (October 14-16, 2009).

Similarly, information that is work product protected should be recalled as soon as possible. However, since that information includes legal conclusions and mental impressions, it might be more harmful to the client if it is evaluated by the government agency before it is withdrawn.

Notwithstanding the safe harbor provisions of FRE 502, counsel should recognize that if too much time passes after disclosure or if the government agency rejects a proposal to recant the privileged information, it might be in the corporation's best interest for counsel to withdraw as the attorney for the investigation. If not, the attorney risks violating his duty of confidentiality to his or her client and exposes himself or herself to a wide range of litigious consequences. Hiring additional outside counsel in this situation preserves the ability for the corporation to recant the information and to retain the conflicted attorney for other non-related corporate matters.

VII. Conclusion

As the 45th anniversary of the enactment of the first state franchise law approaches, franchise and distribution law continues to develop. To be effective practitioners in the area, counsel are expected to maintain a heightened focus on the differences among jurisdictions, to understand the evolving nuances in sub-areas of the law and to advocate for changes in the balance of franchise legislation. While it makes the practice more challenging and enjoyable for all, it also requires a continued dedication to remaining current with each new piece of proposed or enacted legislation and published decision.

As reflected in this paper, ethical considerations involved in the practice of franchise law also demand continued attention. This demand exists irrespective of whether you are counsel to a franchise association or group of aggrieved franchisees and you need to afford all of your clients the appropriate level of communication and consideration, or you are counsel to a franchisor who has requested that you conduct an internal investigation into the activities of its operations personnel. In a practice area where counsel are often asked to advocate with respect to conflicting interests between franchisors and franchisees, a comprehensive understanding of the implicated ethical considerations can help counsel navigate through the potential conflicts and pitfalls that inevitably exist. This paper is not intended to be a one-stop update on ethical considerations, but instead it has only sought to highlight some of the many circumstances where ethical issues must be considered. Keeping these ethical considerations front of mind in practice will help to alert counsel to new issues and help to avoid those embedded into the issues they are asked to address.
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Mr. Karp served on the Board of Directors of the American Franchisee Association for ten years. He also served as Chair of the AFA Model Responsible Franchise Practices Act Committee, was the principal author of the Model Act and served as the Program Chair of the 1999 AFA Franchisee Legal Symposium. He was Co-Chair of the 2009 Annual Meeting of the American Association of Franchisees & Dealers and served on the AAFD’s Fair Franchising Standards Committee.

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