ENGAGING WITH THE REALITIES OF THE CORPORATE FAMILY

Kristen Salvatore DePalma and Emily V. Burton*

INTRODUCTION

An attorney owes his or her client a duty of undivided loyalty. When that client is a corporation, the question arises whether the firm owes a duty of loyalty to every member of that corporation's family and whether such a duty would be in any way shapeable by the attorney. Given the myriad of affiliate relationships and the ongoing developments in corporate structures, full attribution of every attorney-client relationship to every member of a corporate family would create serious difficulties for any large firm representing multiple corporate clients.

Thankfully, different factors winnow down conflict situations to those in which the law firm's representation raises genuine ethical concerns. Part I of this article discusses Comment 34 to Rule 1.7 of the Delaware Lawyers' Rules of Professional Conduct (the "Rules"), which clarifies the situations wherein affiliates of a corporate client must also be considered a client for conflict purposes.[1] Part II describes the ways in which advance waivers may permit attorneys to negotiate the scope of representation with a prospective client prior to litigation, as well as exceptions to the "hot potato" rule, which permits an attorney to terminate his representation of a client when the conflict is not attributable to the attorney's actions.

I. UNDER COMMENT 34 TO RULE 1.7, REPRESENTATION OF ONE MEMBER OF A CORPORATE FAMILY WILL NOT NECESSARILY CONFLICT THE ATTORNEY OUT OF REPRESENTATION ADVERSE TO OTHER MEMBERS OF THE CORPORATE FAMILY

The Rules provide somewhat limited guidance regarding when an attorney or firm that undisputedly has an attorney-client relationship with one entity, the client, also has an attorney-client relationship with an affiliate of that client. Rule 1.7(a), governing concurrent conflicts of interest, states:

> (a) Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:
>
> (1) the representation of one client will be directly adverse to another client; or
>
> (2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.[2]

---

* Ms. DePalma and Ms. Burton are attorneys at Young, Conaway, Stargatt & Taylor, LLP in Wilmington, Delaware. The authors would like to thank Alexander D. Thaler for his time and helpful comments on this article.

1. Delaware has adopted Rule 1.7, and its Comments, of the American Bar Association ("ABA") Model Rules of Professional Conduct ("Model Rules").

2. Del. Prof. Cond. R. 1.7(a).

Rule 1.7 is clarified by Comment 34, which states:

> A lawyer who represents a corporation or other organization does not, by virtue of that representation, necessarily represent any constituent or affiliated organization, such as a parent or subsidiary. See Rule 1.13(a).[3] Thus, the lawyer for an organization is not barred from accepting representation adverse to an affiliate in an unrelated matter, unless the circumstances are such that the affiliate should also be considered a client of the lawyer, there is an understanding between the lawyer and the organizational client that the lawyer will avoid representation adverse to the client's affiliates, or the lawyer's obligations to either the organizational client or the new client are likely to limit materially the lawyer's representation of the other client.[4]

"'[W]hether a lawyer represents a corporate affiliate of his client, for purposes of Rule 1.7, depends not upon any clear-cut *per se* rule but rather upon the particular circumstances[.]'"[5]

While few courts have explicitly interpreted Comment 34 since its adoption,[6] its meaning can be inferred from related sources. The ABA Reporter's Explanation of Changes for Comment 34 notes:

> The language is largely drawn from the conclusions of ABA Standing Committee on Ethics and Professional Responsibility Formal Opinion 95-390, although the Commission believes that there will be more situations in which the lawyer will be prohibited from undertaking representation than may have been reflected in that opinion.[7]

Furthermore, Formal Opinion 95-390 itself explicitly drew on preexisting case law.[8] Therefore, Comment 34 may be interpreted in light of both Formal Opinion 95-390 and prior case law. Although Delaware's case law on the topic is limited, authority from other jurisdictions that have adopted ABA Model Rule of Professional Conduct ("Model Rule") 1.7 and Comment 34 provides the best indication of a Delaware court's ruling.[9]

---

3. Rule 1.13(a) provides: "A lawyer employed or retained by an organization represents the organization acting through its duly authorized constituents." DEL. PROF. COND. R. 1.13(a).

4. DEL. PROF. COND. R. 1.7(a) cmt. 34.

5. Avocent Redmond Corp. v. Rose Elecs., 491 F. Supp. 2d 1000, 1006 (W.D. Wash. 2007) (quoting ABA Formal Ethics Opinion 95-390 (Jan. 25, 1995) (hereinafter "Formal Op. 95-390")).

6. Comment 34 was promulgated by the ABA in 2002 and adopted by Delaware on July 1, 2003. It has also been adopted by Arizona, Arkansas, Colorado, Connecticut, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Maine, Maryland, Minnesota, Missouri, Nebraska, New Hampshire, North Carolina, Oklahoma, Pennsylvania, Rhode Island, South Carolina, South Dakota, Utah, Vermont, Washington, Wisconsin, and Wyoming. *See* ABA chart listing jurisdictions that adopted Rule 1.7, Comment 34 as of October 28, 2009, *at* http://www.abanet.org/cpr/pic/1_7_34.pdf. Alaska, the District of Columbia, and New York have adopted modified versions of Comment 34. *Id. See also* Charles W. Wolfram, "*Ethics 2000 And Conflicts Of Interest: The More Things Change* …." 70 TENN. L. REV. 27, 49 (Fall 2002) (addressing the promulgation of Comment 34, noting an absence of clarity).

7. ABA Comm'n on Evaluation of the Model Rules of Prof. Conduct, Report 401 to the ABA House of Delegates, at 73 (Aug. 6, 2001), *at* http://www.abanet.org/cpr/e2k/e2k-rule17rem.html.

8. *See, e.g.*, Formal Op. 95-390, *supra* note *5,* at 1001:264 (citing Teradyne Inc. v. Hewlett-Packard Co., No. C-91-0344 MHP ENE, 1991 U.S. Dist. LEXIS 8363 (N.D. Cal. June 6, 1991); Hartford Accident & Indem. Co. v. RJR Nabisco, Inc., 721 F. Supp. 534, 540 (S.D.N.Y. 1989)).

9. *See, e.g.*, Jones v. State*,* 745 A.2d 856, 868 (Del. 1999); United Water Del., Inc. v. PSC, 723 A.2d 1172, 1176 (Del. 1999).

A. "A Lawyer Who Represents A Corporation Or Other Organization Does Not, By Virtue Of That Representation, Necessarily Represent Any Constituent Or Affiliated Organization, Such As A Parent Or Subsidiary"[10]

The first sentence in Comment 34 states, "A lawyer who represents a corporation or other organization does not, by virtue of that representation, necessarily represent any constituent or affiliated organization, such as a parent or subsidiary."[11] Prior to the enactment of Comment 34, a few courts held that suing an affiliate was equivalent to suing the client for conflict of interest purposes.[12] In contrast, the majority of courts, as well as Formal Opinion 95-390, adopted a fact-intensive, weighing approach to the question.[13] The opening sentence of Comment 34 clearly establishes the weighing approach as the governing rule of interpretation in jurisdictions that have adopted the Model Rules.[14] Furthermore, Comment 34's recognition of a legal distinction between members of a corporate family while tempering the effect of that distinction is consistent with other areas of corporate law.[15] Therefore, a court considering the issue as a matter of first impression should find no *per se* conflict where an attorney undertook representation adverse to an affiliate.

B. "The Lawyer For An Organization Is Not Barred From Accepting Representation Adverse To An Affiliate In An Unrelated Matter"[16]

The courts' struggle to establish principled guidelines for when an attorney may undertake representation adverse to an affiliate predates both Comment 34 and Formal Opinion 95-390. The protection of client confidences concerning the larger corporate family has consistently been a key concern in evaluating this question.[17] In order to protect client

---

10. Del. Prof. Cond. R. 1.7 cmt. 34.

11. *Id.*

12. *See* Carlyle Towers Condo. Ass'n v. Crossland Sav., FSB, 944 F. Supp. 341, 346 (D.N.J. 1996) (citing *Teradyne*, 1991 U.S. Dist. LEXIS 8363, at *6-7**;** Stratagem Dev. Corp. v. Heron Int'l N.V., 756 F. Supp. 789, 793 (S.D.N.Y. 1991); *Hartford Accident*, 721 F. Supp. at 540) (holding that under New Jersey law, suing an affiliate is the same as suing a client for conflict purposes).

13. *See, e.g.*, Westerly Capital, LLC v. Windmill Mgmt., LLC, CV086000954S, 2008 Conn. Super. LEXIS 2826, at *6-8 (Conn. Super. Ct. Oct. 30, 2008) (noting that Connecticut had adopted the substantial relationship test as a prerequisite to disqualification where an attorney undertakes representation adverse to an affiliate); Brooklyn Navy Yard Cogeneration Partners, L.P. v. PMNC, 663 N.Y.S.2d 499 (N.Y. Sup. Ct. 1997) (denying motion to disqualify under New York law).

14. Formal Op. 95-390, *supra* note 5, at 1001:258 ("A lawyer who represents a corporate client is not by that fact alone necessarily barred from a representation that is adverse to a corporate affiliate of that client….").

15. *See, e.g.*, Allied Capital Corp. v. GC-Sun Holdings, L.P., 910 A.2d 1020, 1040 (Del. Ch. 2006) (adopting a moderate approach to claims that a parent civilly conspired with its subsidiary on the grounds that the law must at once "recogni[ze] the presumptively separate legal dignities of parent and subsidiary" while also being responsive to the day to day interactions of related entities).

16. Del. Prof. Cond. R. 1.7 cmt. 34.

17. *See, e.g.*, Pennwalt Corp. v. Plough, 85 F.R.D. 264, 270 (D. Del. 1980) (granting motion to disqualify based on the "substantial relationship test," applying the Model Code of Professional Conduct, the predecessor to the Model Rules).

confidences in representation adverse to an affiliate, courts applied the substantial relationship test, borrowed from the "former client" analysis.[18]

In *Pennwalt Corp. v. Plough, Inc.*,[19] the United States District Court of Delaware applied the substantial relationship test when considering whether attorneys should be disqualified where, while representing the client in an antitrust matter, they brought suit against its affiliate for false advertising.[20]

> The … rule for disqualification where there is concurrent dual representation of sister corporations cannot be accepted for the simple factual reason that [the law firm] has never represented [the sister] or [the parent corporation]…. Similarly, [the law firm's] claim that the ethicality of its position is unassailable because it never represented [either affiliate] is overly broad. Representation under the Code has been prohibited in varied circumstances even though the attorney-client relationship never existed.[21]

The court then applied the substantial relationship test because, "[w]hile the case *sub judice* is not a 'prior representation' case, there would be no hesitation to find [the law firm] disqualified if that firm could not pass the widely adopted 'substantial relationship' test analogized to concurrent representation of sister corporations[.]"[22] "[T]he determination of whether there is a substantial relationship … involves a realistic appraisal of the possibility that confidences had been disclosed in the one matter which will be harmful to the client in the other."[23]

The court observed that the substantial relationship test is not the only criteria to be considered:

> In assessing whether this threat exists in circumstances such as those presented here, the court properly may [also] examine the relationship between the sister corporations. The object of this inquiry is not to determine whether [the affiliate] can be affixed with the label "client." Rather, it is to gauge the degree, if any, to which [the firm]'s representation [in either case] may be influenced by a regard for the alternate client's welfare.[24]

The court noted that until the corporations were organized into the same division, shared the same legal department, and reported to the same executive, there was not a conflict under Canon 5 of the New York Code of Professional

18. *See* Morrison Knudsen Corp. v. Hancock, 69 Cal. App. 4th 223, 233 (Cal. Ct. App. 1999) (quoting H. F. Ahmanson & Co. v. Salomon Bros., 229 Cal. App. 3d 1445, 1455 (Cal. Ct. App. 1991)) (granting motion to disqualify upon finding that multiple cases alleging negligent engineering were substantially related); *Pennwalt*, 85 F.R.D. at 270; Glueck v. Jonathan Logan, Inc., 653 F.2d 746, 749 (2d Cir. N.Y. 1981) (applying substantial relationship test where attorneys undertook representation adverse to members of an association represented by the attorneys). *See contra* Discotrade Ltd. v. Wyeth-Ayerst Int'l, 200 F. Supp. 2d 355, 360 (S.D.N.Y. 2002) (limiting *Glueck* to the association context without addressing subsequent case law applying *Glueck* in the corporate affiliate context). *See also* DEL. PROF. COND. R. 1.9 cmt. 3 (defining "substantially related" for the purposes of Rule 1.9).

19. 85 F.R.D. 264 (D. Del. 1980).

20. Although *Pennwalt* applied the Model Code of Professional Responsibility, rather than the Model Rules, it continues to be cited as an authority in this area, and its approach has been adopted by cases interpreting the Model Rules. *See, e.g.*, *Westerly*, 2008 Conn. Super. LEXIS 2826, at *5 (adopting *Pennwalt* approach while applying Model Rule 1.7).

21. *Pennwalt*, 85 F.R.D. at 268.

22. *Id.* at 270.

23. *Id.*

24. *Id.* at 271-72.

Responsibility.[25] But the court added, "It is difficult to perceive how there could be free, unfettered communications between [the firm] and [its client] after the merger of headquarters [when] a small staff of in-house attorneys located at the same physical site and under the active supervision of one attorney are handling both … matters."[26]

In *Brooklyn Navy Yard Cogeneration Partners, L.P. v. PMNC*,[27] the Supreme Court of New York considered a motion to disqualify attorneys based on their firm's concurrent representation of the opposing party's subsidiary.[28] The court "reject[ed], *ab initio,* the theory … that the two corporations should be treated as one entity for conflicts purposes since no evidence ha[d] been submitted to demonstrate that the '[d]omination [of the parent over the subsidiary is] so complete, [the] interference so obtrusive' as to rebut the presumption that they are separate and distinct legal entities,"[29] even though "they share common legal and accounting departments and have some officers in common."[30] Instead, the court held that "[t]he thorny question of attorney disqualification requires a response sensitive to each of the substantial interests implicated in the controversy."[31] Therefore, the court applied the substantial relationship test.[32] The court wrote:

> In deciding the question of whether the "possibility of disclosure" exists, two factors are relevant: (1) The nature of the law firm … insofar as it sheds light upon whether confidential information about the client would have been shared among the members of the firm … [and] (2) The type of legal work done for the client insofar as it may have put the firm in the position of acquiring confidential information that could be used in an adversarial manner.[33]

Ultimately, the court denied the motion to disqualify because

> the legal work done for defendant's subsidiary was of a highly specialized nature and had absolutely nothing in common with the subject matter of the present controversy. Moreover, … the work for the subsidiary was accomplished by a geographically isolated member of the firm.[34]

This approach has been applied by a court following Comment 34. In *Westerly Capital, LLC v. Windmill Management, LLC*,[35] a firm undertook representation adverse to the supermajority owner of two LLCs represented by the firm.[36] The Superior Court of Connecticut held that, in that context,

---

25. *Id.* at 272.

26. *Id.* at 273.

27. 663 N.Y.S.2d 499 (N.Y. Sup. Ct. 1997).

28. *Id.* at 500.

29. *Id.* (modification in quoted text in the original).

30. *Id.* at 500 n.1.

31. *Id.* at 500.

32. *Id.* at 501.

33. *Id.* (internal citations omitted).

34. *Id*.

35. CV086000954S, 2008 Conn. Super. LEXIS 2826 (Conn. Super. Ct. Oct. 30, 2008).

36. *Id.* at *5 (applying Conn. R. Prof. Conduct 1.7(a), which mirrors Model Rule 1.7(a) and incorporates Comment 34).

> the Second Circuit imposed a "substantial relationship test" to the effect that whenever a lawsuit is sufficiently related to the matters which the representation of the [client] covers so as to create a realistic risk that one of the parties will not be represented with vigor, or that unfair advantage will be taken of another party, there should be disqualification. The Second Circuit's concern was focused on whether a trial might be tainted or the free flow of information from a client to the law firm be inhibited.[37]

The court denied the motion to disqualify because "there [wa]s no evidence that [the attorney] obtained or had access to any confidential information of [the affiliate] held by [the client], and little possibility he would have such access in the future."[38] Therefore, ownership, even accompanied by a degree of control, is insufficient by itself to support disqualification under this rationale.[39]

The court in *Westerly* does not mention Comment 34 in its analysis or rationalize its application of case law interpreting the Model Code of Professional Conduct when applying the Model Rules. Nonetheless, the substantial relationship test appears to be incorporated into Comment 34, both because the word "unrelated" was already freighted with meaning when the ABA knowingly used it, and because Formal Opinion 95-390, which formed the basis for Comment 34, cited *Pennwalt* when describing the limitations on representation adverse to an affiliate.[40] Therefore, under Rule 1.7, an attorney would likely be conflicted out of representation adverse to an affiliate where the matter is substantially related to the attorney's work for the client.

C. "[When] The Circumstances Are Such That The Affiliate Should Also Be Considered A Client Of The Lawyer"[41]

While Comment 34 itself is rather elliptical as to what circumstances would require the affiliate to be also considered a client of the lawyer, Formal Opinion 95-390 addressed the question at length.[42] It began with the proposition that the answer depends on the particular facts and circumstances of the case, evaluated through the prism of the rules governing formation of an attorney-client relationship with a single client: "A client-lawyer relationship does not … require an explicit agreement, let alone a written letter of engagement: it may come into being as a result of reasonable expectations and a failure of the lawyer to dispel those expectations."[43] "Thus, the nature of the lawyer's dealings with [affiliates] may be such that they have become clients as well."[44] Or, "the lawyer's relationship with the [affiliate] may lead the affiliate

37. *Id.* at *6-8.

38. *Id.* at *9.

39. *See id.*; Whiting Corp. v. White Machinery Corp., 567 F.2d 713, 715-16 (7th Cir. 1977) (client's 20% ownership interest of defendant and client's officers' service on defendant's board did not create a conflict of interest disqualifying attorney from representing plaintiff).

40. Formal Op. 95-390, *supra* note *5,* at 1001:263.

41. Del. Prof. Cond. R. 1.7 cmt. 34.

42. Formal Op. 95-390, *supra* note *5,* at 1001:264.

43. *Id.* at 1001:263 (subsequently quoting Restatement (Third) of the Law Governing Lawyers § 26 (Tent. Draft No. 5, 1992)).

44. *Id.* at 1001:264.

reasonably to believe that it is a client of the lawyer."[45] Furthermore, "[a] client-lawyer relationship with the affiliate may also arise because the affiliate imparted confidential information to the lawyer with the expectation that the lawyer would use it in representing the affiliate."[46] "Finally, the relationship of the [client] to its affiliate may be such that the lawyer is required to regard the affiliate as his client."[47] "[S]ome of the key facts applicable to the analysis include (1) whether the [client] and the [affiliate] share a common legal department and management duties, (2) whether the lawyer's work for [the client] benefits [the affiliate], or (3) whether the lawyer's work for the [client] involves collecting confidential information."[48] From a broad perspective, "'the principal focus should be the practical consequences of the attorney's relationship with the corporate family. If that relationship may give the attorney a significant practical advantage in a case against an affiliate, then the attorney can be disqualified from taking the case.'"[49] These scenarios are discussed in more detail below.

1. An Affiliate Becomes Entitled To Be Treated As A Client Where "The Nature Of The Lawyer's Dealings With [The Affiliate Are] Such That [It Has] Become A Client"[50]

An affiliate may become a client when the lawyer performs legal services for the affiliate, possibly in the course of performing legal services for the client.[51] In *Hartford Accident & Indemnification Co. v. RJR Nabisco, Inc.*,[52] the United States District Court for the Southern District of New York

> [c]onclude[d] that [the affiliate], through its subsidiary [the client], was [also] a client … [where] the parent attached considerable importance to the product liability litigation against its subsidiary and, accordingly, supervised the subsidiary's litigation. [One attorney's affidavit stated,] "I have, for the most part, received assignments requesting legal representation from an officer or attorney of [the affiliate] even though the services were to be performed for [the client]." … If the parent and subsidiary were in

---

45. *Id.*

46. *Id.*

47. *Id.* at 1001:265.

48. Honeywell Int'l Inc. v. Philips Lumileds Lighting Co., Case No. 2:07-CV-463-CE, 2009 U.S. Dist. LEXIS 12496 (E.D. Tex. Jan. 6, 2009) (granting motion to disqualify under Model Rule 1.7 cmt. 34). California courts, which have not adopted the Model Rule, are directed to consider similar factors: "(1) whether the attorney received 'confidential information' from one entity 'substantially related to the present claim against' the other; (2) whether control of the two entities' legal affairs overlap; (3) whether the two entities have overlaps in other areas, such as operations, personnel, or insurance coverage." iSmart Int'l Ltd. v. I-Docsecure, LLC, No. C 04-03114 RMW, 2006 U.S. Dist. LEXIS 77323, at *11 (N.D. Cal. Oct. 12, 2006).

49. *iSmart*, 2006 U.S. Dist. LEXIS 77323, at *12 (quoting Morrison Knudsen Corp. v. Hancock, 69 Cal. App. 4th 223, 253 (Cal. Ct. App. 1999)) (although *iSmart* addressed California law, this observation was based in part on Formal Op. 95-390 and is accurate when applied to case law interpreting the Model Rule and Comment 34).

50. Formal Op. 95-390, *supra* note *5,* at 1001:264.

51. *See, e.g.*, GSI Commerce Solutions, Inc. v. BabyCenter, L.L.C., 644 F. Supp. 2d 333, 334-35 (S.D.N.Y. 2009) (although engagement letter stated that only parent corporation was a client, a subsidiary became a client when lawyers performed legal services for the subsidiary at the parent's request).

52. 721 F. Supp. 534 (S.D.N.Y. 1989).

> fact distinct and separate entities for representation purposes, then there would have been no need for the parent's general counsel to have retained this supervisory role.[53]

Despite concluding that the affiliate had become a client as a result of its participation in the litigation, the court denied the motion to disqualify on the grounds that the relationship had terminated when the firm terminated its relationship with the attorney representing the subsidiary.[54]

Control of litigation is only one possible factor supporting disqualification under this section. For example, one court noted the attorneys' use of the affiliate's name when describing their client, ultimately granting the motion to disqualify the firm.[55] Another court noted that the firm's work had benefited the affiliate.[56] In contrast, a court denied a motion to disqualify, where a firm filed a patent listing a company's CEO as the first inventor and failed to complete assignment of the patent to the client company, on the grounds that even though the work benefited the CEO, he could not have believed himself to be the firm's client because of the engagement letter.[57] Therefore, to the extent possible, interaction with affiliates should be minimized, and the relationship's scope should be clarified to limit conflicts on this basis.

2. An Affiliate Becomes Entitled To Be Treated As A Client Where "The Lawyer's Relationship With The Affiliate … Lead[s] The Affiliate Reasonably To Believe That It Is A Client Of The Lawyer"[58]

As is true generally, an attorney-client relationship can be formed where an affiliate reasonably believes that it is the attorney's client and the attorney fails to take steps to dispel that belief.[59] In *Avocent Redmond Corp. v. Rose Electronics*,[60] the United States District Court for the Western District of Washington noted that "[d]etermining the existence of an attorney-client relationship is a fact-based inquiry."[61] "'The existence of the relationship 'turns largely on the client's subjective belief that it exists. The client's subjective belief, however, does not control the issue unless it is reasonably formed based on the attending circumstances, including the attorney's words or actions.'"[62] The attorneys in that case as-

53. *Id.* at 540 (applying a cross section of federal case law).

54. *Id.* at 541.

55. Jones v. Rabanco, Ltd., No. C03-3195P, 2006 U.S. Dist. LEXIS 53766, at *12 (W.D. Wash. Aug. 3, 2006) (granting motion to disqualify under Washington law, one month prior to Washington's adoption of Comment 34: "Additionally, many of the internal memos of attorneys … who worked on the LRI matter referred to Rabanco as if it were their client.") (cited in *Avocent*, 491 F. Supp. 2d at 1008 (applying Model Rule 1.7)).

56. GSI Commerce Solutions, Inc. v. BabyCenter, L.L.C., 09 CV 2857 (JSP), 2009 U.S. Dist. LEXIS 65226, at *1-2 (S.D.N.Y. July 27, 2009) (applying New York law, which has not adopted Model Rule 1.7, Comment 34 verbatim).

57. Synergy Tech & Design, Inc. v. Terry, No. C 06-02073 JSW, 2007 U.S. Dist. LEXIS 34463, at *25-26 (N.D. Cal. May 2, 2007) (applying Washington law, which follows the Model Rule).

58. Formal Op. 95-390, *supra* note *5,* at 1001:264.

59. *See, e.g.*, Teradyne, Inc. v. Hewlett-Packard, Co., 20 U.S.P.Q. 2d (BNA) 1143, 1144-45 (N.D. Cal. 1991).

60. 491 F. Supp. 2d 1000 (W.D. Wash. 2007).

61. *Id.* at 1003 (applying Model Rule 1.7).

62. *Id.* (quoting Bohn v. Cody, 832 P.2d 71 (1992)).

serted that although they had represented a sister corporation of the plaintiff, OSA Technologies, Inc. ("OSA"), they had never represented the plaintiff itself, Avocent Redmound Corp. ("Redmound").[63] The court began its analysis with the engagement letter because "'[t]he engagement agreement is the basic contract with the client and its terms are accorded substantial weight in determining the scope of the relationship.'"[64]

The agreement in *Avocent* stated: "I am writing to confirm that this firm has been engaged to represent OSA Technologies, Inc., a wholly owned subsidiary of Avocent Corporation, and its affiliates ('you' or the 'Company'), in connection with its general corporate matters…."[65] The court stated, "In the first sentence of this agreement, the client is expressly identified as '*OSA Technologies, Inc*., a wholly owned subsidiary of Avocent Corporation, *and its affiliates*.' Further confirming this client identity, is the agreement's client-signature line, which states: SO AGREED. *OSA Technologies, Inc*., a wholly owned subsidiary of Avocent Corporation, *and it's [sic] affiliates.*'"[66] "Therefore, by agreeing to represent 'OSA … and its affiliates,' [the firm] represented Redmound."[67] Thus, because Redmound's belief that the firm represented it was reasonable, the court found Redmound to be a client under Comment 34.[68] In theory, any conduct traditionally creating a reasonable belief of an attorney-client relationship would create an attorney-client relationship under this rationale.[69]

3. An Affiliate Becomes Entitled To Be Treated As A Client Where "The Affiliate Imparted Confidential Information To The Lawyer With The Expectation That The Lawyer Would Use It In Representing The Affiliate"[70]

The classic case in which an affiliate became a client by way of imparting confidential information to a lawyer with the expectation that the lawyer would use the information in representing the affiliate is *Westinghouse Electric Corp. v. Kerr-McGee Corp*.,[71] which was cited in Formal Opinion 95-390.[72] In *Westinghouse*, Kirkland, Ellis & Rowe ("Kirkland") was hired by Westinghouse Electric Corporation ("Westinghouse") to bring claims that 17 of its long-term supply contracts had become commercially impractical as a result of antitrust violations by companies involved in the uranium industry.[73] Contemporaneously, the American Petroleum Institute ("API") hired Kirkland to prepare a report for Congress

63. *Id.* at 1002-03.

64. *Id.* at 1004 (quoting a docket entry).

65. *Id.*

66. *Id.* (emphasis in original).

67. *Id.*

68. *Id.* at 1006.

69. *See* Formal Op. 95-390, *supra* note *5,* at 1001:263.

70. *Id.* at 1001:264.

71. 580 F.2d 1311 (7th Cir. Ill. 1978).

72. Formal Op. 95-390, *supra* note *5,* at 1001:264 (citing *Westinghouse* as an example of a situation in which an affiliate might become a client by conveying confidential information).

73. *Westinghouse*, 580 F.2d at 1313.

demonstrating the absence of antitrust concerns raised by cross-ownership of alternative energy sources, including uranium.[74] To prepare the report, Kirkland sent

> 59 API member companies a survey questionnaire seeking data to be used … in connection with its engagement by API. In the introductory memorandum to the questionnaire, [Kirkland] advised the 59 companies that [it] had "ascertained that certain types of data pertinent to the pending anti-diversification legislation are not now publicly available" and the API "would appreciate your help in providing this information to Kirkland …." The memorandum included the following:
>
> "Kirkland, Ellis & Rowe is acting as an independent special counsel for API, and will hold any company information in strict confidence, not to be disclosed to any other company, or even to API, except in aggregated or such other form as will preclude identifying the source company with its data."[75]

Several of the companies providing data and interviews to Kirkland in connection with the report were parties to Westinghouse's litigation and moved to disqualify Kirkland from that litigation on the grounds that Kirkland represented them in the API efforts.[76]

The United States Court of Appeals for the Seventh Circuit noted, "The professional relationship for purposes of the privilege for attorney-client communications 'hinges upon the client's belief that he is consulting a lawyer in that capacity and his manifested intention to seek professional legal advice.'"[77] By affidavit, one movant testified that he "'was given to believe that the Kirkland firm was representing both API and Gulf;' … and Getty's vice president stated that in submitting data to Kirkland he 'acted upon the belief and expectation that such submission was made in order to enable [Kirkland] to render legal service to Getty in furtherance of Getty's interests.'"[78] Because "Gulf, Kerr-McGee and Getty each entertained a reasonable belief that it was submitting confidential information … to a law firm which had solicited the information upon a representation that the firm was acting in the undivided interest of each company," the court found that an attorney-client relationship had developed and disqualified Kirkland.[79]

Although inquiry into whether disqualification is proper because the attorneys represent the client in a related matter is facially similar to inquiry into whether the affiliate has become a client as a result of disclosing confidential information, the inquiries address separate concerns. The former inquiry, under the substantial relationship test, asks whether, in the course of the firm's interactions with the client, the firm may have acquired confidential information concerning the affiliate that is relevant to the lawsuit against the affiliate and that the client expected would be kept confidential.[80] Disqualification is proper in that context to protect the firm's relationship with the client. In contrast, the latter rule addresses

---

74. *Id.*

75. *Id.* at 1313-14 (emphasis in original, modifications to quoted material in original).

76. *Id.* at 1312.

77. *Id.* at 1319.

78. *Id.* at 1320 (modifications in nested quotations in original).

79. *Id.* at 1321.

80. *Westerly*, 2008 Conn. Super. LEXIS 2826, at *6-8.

the reasonable expectations of the affiliate.[81] Disqualification in that context is necessary because a second attorney-client relationship has developed and is subject to the full protection afforded by Rule 1.7.

Lamson & Sessions Co. v. Mundinger[82] demonstrates the distinction between the standards. In *Lamson*, Lamson & Sessions Co. ("Lamson") sued its former subsidiary, YSD Industries, Inc. ("YSD").[83] Jones Day was Lamson's customary outside counsel and had served in that capacity while Lamson owned YSD. Since YSD's spinoff, Jones Day had performed one limited project for YSD[84] and investigated YSD's financial situation for Lamson.[85] The United States District Court for the Northern District of Ohio first held that Jones Day's representation of YSD did not result in a conflict under the former client rules.[86] It then noted that, "[w]hile the affidavit alleges that [YSD was] involved with attorneys from Jones Day at various other times during the past twenty years, it is clear from the affidavit that at all other times Jones Day was acting as counsel for Lamson not YSD; thus, any information gained in those dealings was not confidential information gained in an attorney-client relationship with YSD."[87] Therefore, the court denied the motion to disqualify, despite the relevance of the information YSD provided to Jones Day in connection with Jones Day's investigation on behalf of Lamson.[88] The fact that Jones Day was representing Lamson in the litigation against YSD likely played an unstated role in the court's analysis. Nonetheless, it is clear that this inquiry turns not only on the possession of relevant information, but on the source of that information and the context in which it was acquired.

4. An Affiliate Becomes Entitled To Be Treated As A Client Where "The Relationship Of The [Client] To Its Affiliate [Is] Such That The Lawyer Is Required To Regard The Affiliate As His Client"[89]

The final criteria upon which an affiliate may be considered a client under Comment 34 to the Model Rules is the overlap in personnel and operations between the client and its affiliate.[90] Any overlap in the legal departments is

81. *Westinghouse*, 580 F.2d at 1321.

82. Case No. 4:08CV1226, 2009 U.S. Dist. LEXIS 37197 (N.D. Ohio May 1, 2009) (denying motion to disqualify).

83. *Id.* at *3.

84. *Id*. at *4-5 ("Cognizant of the ongoing relationship between its longtime client, Lamson, and YSD, Jones Day drafted and obtained … an engagement letter that limited the scope of the representation to the consequences of the demutualization, clarified that YSD alone was the client, attempted to waive potential future conflicts between YSD and Lamson as clients, and stated that the representation could only be expanded with Jones Day's consent.").

85. *Id.* at *18 n.4.

86. *Id.* at *16.

87. *Id*.

88. *Id.* at *19.

89. Formal Op. 95-390, *supra* note *5,* at 1001:265.

90. *See* Commonwealth Land Title Ins. Co. v. St. Johns Bank & Trust Co., No. 4:08-CV-1433 CAS, 2009 U.S. Dist. LEXIS 87151, at *20 (E.D. Mo. Sept. 22, 2009) (granting motion to disqualify based on overlap in personnel in case governed by Comment 34). *See also* JPMorgan Chase Bank *ex rel.* Mahonia Ltd. v. Liberty Mut. Ins. Co., 189 F. Supp. 2d 20, 23 (S.D.N.Y. 2002) (applying New York law: "[I]t is wholly artificial to separate [the affiliate] and [the client] for purposes of analyzing [the firm]'s responsibilities in this context. Just from the fact that [the client] accounts for more than 90% of [the affiliate]'s business and that [the affiliate] and [the client] share identical corporate headquarters, an identical board, and an identical general counsel, … it is obvious that the two share a wealth of common interests adversely impacted by the lawsuit in question.").

particularly problematic, not only because it suggests a close relationship under this test, but because it also obfuscates the bounds of the representation and is more likely to result in shared information, and because the "identity of process" of a single legal department addressing matters broadens the class of "substantially related" matters.[91]

For example, in *Honeywell Int'l Inc. v. Philips Lumileds Lighting Co.*,[92] Phillips Lumileds Lighting Co. ("Phillips Lumileds") moved to disqualify counsel for Honeywell International, Inc. ("Honeywell") on the grounds that the attorneys concurrently represented its parent, Phillips Electronics North American Corporation ("PENAC"), in numerous matters.[93] The United States District Court for the Eastern District of Texas reasoned that "[u]nder Model Rule 1.7, Philips Lumileds must establish two things: (1) that it is a current client of PHJW, counsel for Honeywell; and (2) that PHJW's representation of Honeywell is directly adverse to it."[94] The court further stated:

> Here, it is undisputed that (1) Philips Lumileds and the other Philips affiliates share a common legal department, Philips IP&S; (2) Philips and Philips Lumileds share common management, computer networks, and marketing designs; and (3) PHJW currently represents PENAC. As indicated above, Philips IP&S directs intellectual property litigation and licensing strategy for Philips subsidiaries worldwide, including Philips Lumileds. Additionally, … PHJW has had broad access to confidential information of various Philips entities, based on its representations of various Philips entities.[95]

Furthermore, "both the Philips Lumileds' website and marketing materials feature the Philips logo. The PENAC website also features the Philips logo. Considering all the facts, the court is persuaded that Philips Lumileds should be considered a current client of PHJW."[96]

Therefore, to avoid a disqualification on the grounds that an affiliate has become a client or is entitled to be treated as such, law firms should: (1) limit their interaction with affiliates that they do not intend to represent; (2) clarify the scope of their representation when dealing with both clients and affiliates, (3) avoid collecting confidential information from affiliates, and (4) carefully weigh the risk that a court will find an affiliate to be a client if its operations and personnel overlap substantially with those of the client.

---

91. *See Commonwealth Land Title Ins.*, 2009 U.S. Dist. LEXIS 87151, at *20 (noting that an "identity of process" in a legal department's defense of class action caused class action lawsuits addressing different vehicle malfunctions to be substantially related "regardless of the nature of the component involved").

92. Case No. 2:07-CV-463-CE, 2009 U.S. Dist. LEXIS 12496 (E.D. Tex. Jan. 6, 2009).

93. *Id.* at *3.

94. *Id.* at *5-6.

95. *Id.* at *7-8.

96. *Id.* at *8.

D. "There Is An Understanding Between The Lawyer And The Organizational Client That The Lawyer Will Avoid Representation Adverse To The Client's Affiliates"[97]

The fourth clause in Comment 34 to the Model Rules provides that an attorney may not undertake representation adverse to an affiliate if "there is an understanding between the lawyer and the [client] that the lawyer will avoid representation adverse to the client's affiliates." This understanding can be either implicit or it may be stated in the engagement letter.[98]

In *Commonwealth Land Title Insurance Co. v. St. Johns Bank & Trust Co.*, [99] the United States District Court for the Eastern District of Missouri granted a motion to disqualify because it found that the client had an "expectation and understanding that its outside counsel [would] avoid representation adverse to [its] affiliates unless a waiver [was] previously obtained."[100] St. Johns Bank & Trust Co. ("St. Johns") hired the law firm of Polsinelli Shalton Flanigan & Suelthaus PC (the "Polsinelli firm") to bring an action against Commonwealth Land Title Ins. Co. ("Commonwealth").[101] Although initially the Polsinelli firm had never represented Commonwealth or any of its affiliates, four months later the Polsinelli firm merged with Shughart Thomson & Kilroy, PC (the "Shughart firm"), which had represented Commonwealth and its related companies for many years and "[con]currently represent[ed] (1) one of Commonwealth's sister companies in an unrelated suit, and (2) insured policyholders of Commonwealth's sister companies in two unrelated suits."[102] "Commonwealth argue[d] that [the firm]'s representation of St. Johns [was] a concurrent conflict prohibited under [Model Rule 1.7,] but St. Johns argue[d] that the representation is permitted under … [Comment 34] to the rule."[103] The court first determined that "[i]f a concurrent conflict exists, it does not matter that the … lawyers in this case did not previously represent Commonwealth."[104]

The court then concluded:

> In the instant case, [the firm]'s concurrent representation of St. Johns in this action and Commonwealth's sister companies and their insureds in unrelated actions presents a conflict of interest. The conflict is based on the circumstances of Fidelity's [(Commonwealth's parent)] centralized oversight of litigation involving its affiliate companies according to a common set of established procedures and practices which apply to all litigation concerning the affiliated companies and their policyholders, Fidelity's retention of hands-on authority with respect to matters such as settlement, and its expectation and understanding that its outside counsel will avoid representation adverse to Fidelity's affiliates

97. DEL. PROF. COND. R. 1.7 cmt. 34.

98. *See, e.g.*, *Commonwealth Land Title Ins.*, 2009 U.S. Dist. LEXIS 87151, at *15 (implicit understanding); *Avocent*, 491 F. Supp. 2d at 1004 (understanding based on engagement letter).

99. No. 4:08-CV-1433 CAS, 2009 U.S. Dist. LEXIS 87151 (E.D. Mo. Sept. 22, 2009) (applying Missouri Supreme Court Rule 4-1.7, which mirrors Model Rule 1.7 and includes Comment 34).

100. *Id.* at *15 (applying Missouri Supreme Court Rule 4-1.7, which mirrors Model Rule 1.7 and includes Comment 34).

101. *Id.* at *3.

102. *Id.*

103. *Id.*

104. *Id.*

> unless a waiver is previously obtained. These circumstances establish that Fidelity, Commonwealth, and its sister companies should all be considered clients …, and are owed a duty of loyalty …. Because Commonwealth refuses to consent to the concurrent representation, [the firm] must be disqualified from representing St. Johns in this matter.[105]

This issue differs from the discussion in the preceding section because this inquiry focuses on the client's reasonable expectations concerning the scope of the relationship, whereas the previous section discussed the possibility that the affiliate should be considered a client due to the affiliate's reasonable expectations. Based on *Commonwealth* and *Avocent*, it appears as though any problems created by this rationale can be addressed through an engagement letter informing the client that the firm may undertake representation adverse to any affiliates.

E. "The Lawyer's Obligations To Either The Organizational Client Or The New Client Are Likely To Limit Materially The Lawyer's Representation Of The Other Client"[106]

Comment 34 to the Model Rules ends with a prohibition on representations in which "the lawyer's obligations to either the organizational client or the new client are likely to limit materially the lawyer's representation of the other client." This restates the general proposition contained in Rule 1.7(a) that "[a] concurrent conflict of interest exists 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, … or a third person …." Absent from this constraint is any consideration for the impact of the new attorney-client relationship on the lawyer's interactions with the Affiliate. That absence underlines the thrust of Comment 34, which is that an affiliate is not a client solely by virtue of its status as an affiliate of the client. On the other hand, this definition of a concurrent conflict of interest explicitly recognizes that even where the affiliate is not a client of the lawyer, the lawyer may in practice limit his or her representation of the new client as a result of the affiliate's relationship with the pre-existing client. As one commentator has observed, "it seems that courts will find representation adverse to a corporate affiliate objectionable in at least two paradigm situations-one involving impermissible disloyalty and the other involving a substantial level of understandable discomfort on the part of the entity client."[107]

CFTC v. Eustace[108] demonstrates such a material limitation of the lawyer's responsibility to the client in this context. *CFTC* did "not fit precisely under either Rule 1.7 or bankruptcy doctrine."[109] A court-appointed equity receiver "failed to disclose prior client relationships with various UBS entities knowing that another UBS entity, UBS Fund Services (Cayman) Limited ('UBS Cayman'), participated in various aspects of the transactions underlying [the] cases," which were a valuable asset of the estate.[110] The equity receiver had not named UBS Cayman as a defendant when bringing suit.[111]

---

105. *Id.* at *14-15.

106. Del. Prof. Cond. R. 1.7 cmt. 34.

107. Charles W. Wolfram, *Ethics 2000 and Conflicts of Interest: The More Things Change …* 70 Tenn. L. Rev. 27, 52 (Fall 2002).

108. C.A. Nos. 05-2973 & 06-1944, 2007 U.S. Dist. LEXIS 33137 (E.D. Pa. May 3, 2007).

109. *Id.* at *21.

110. *Id.* at *1.

111. *Id.* at *5.

Nonetheless, "UBS Cayman [was] mentioned throughout the Complaint, and its role in the overall business transaction was, according to the Complaint, a significant one. The complaint paint[ed] UBS Cayman as one of the victims of the wrongdoing by Man[, the defendant]."[112] The potential conflict was brought to the court's attention after a deposition of UBS Cayman employees suggested that they had been negligent in the challenged transactions.[113]

The receiver argued that under Rule 1.7, Comment 34, his firm was not barred from bringing suit against UBS because "the UBS entities they represent and those entities which are involved in this litigation are separate legal entities, and there is no reason they should be treated as the same client. Moreover, according to the Receiver … there was no expectation by UBS Financial Services that [the Receiver] would avoid representations adverse to UBS Cayman."[114]

The court wrote:

> If this dispute was merely an issue of whether a law firm could accept a representation adverse to a corporate affiliate of an entity when the firm has an ongoing client relationship with another unrelated affiliate of that entity, the court would [have] readily [found] that … the Receiver's arguments were correct and that no disabling conflict existed.[115]

Nonetheless, the United States District Court for the Eastern District of Pennsylvania granted the motion to disqualify partially on the grounds that if the receiver tried the case, the receiver might, "because of allegiances to other UBS entities … frame[] questions and arguments to the jury in such a way as to encourage the jury to impose liability only as to Man and to prejudice Man's third-party claim against UBS Cayman."[116] That result could lead to reversal on appeal.[117] The situation of this case in the bankruptcy context is helpful because, typically, the new client would not have required court intervention to discharge its own counsel.

Viewed as a whole, Comment 34 is a flexible rule that respects the expectations and practical constraints of the lawyers and entities it governs. Comment 34 protects client confidences by applying the substantial relationship test where the client may have imparted to the attorney confidential information concerning its affiliate.[118] The Comment recognizes that an attorney-client relationship with a client may expand to encompass a relationship with an affiliate or can give an affiliate a reasonable basis to believe that such a relationship has formed.[119] It also respects the client's reasonable expecta-

---

112. *Id*.

113. *Id.* at *9.

114. *Id.* at *15-17.

115. *Id.* at *18-19.

116. *Id.* at *35.

117. *Id*.

118. *Westerly*, 2008 Conn. Super. LEXIS 2826, at *5 (denying motion to disqualify where matters were not substantially related).

119. *See, e.g.*, *Hartford Accident*, 721 F. Supp. at 540 (granting motion to disqualify where attorneys formed attorney-client relationship with affiliate in the course of representing client).

tions concerning the relationship between its affiliate and its attorney.[120] Finally, Comment 34 reiterates the more general rule that an attorney must give each client his or her undivided loyalty, absent a waiver.[121]

F. This Standard Notably Omits Any Mention Of Disqualification Based On Adversity

Comment 34 to the Model Rule does not mention adversity, whether direct or indirect, as grounds for disqualification. This is a marked deviation from other authorities that have addressed the issue.[122] For example, disqualification based on direct adversity was the second issue discussed in Formal Opinion 95-390.[123] Furthermore, some courts, even those applying Comment 34, have granted motions to disqualify on the grounds that the representation against the affiliate was adverse to the client.[124] Finally, the *Restatement (Third) of the Law Governing Lawyers* (the "*Restatement*") includes two comments directing that attorneys be disqualified if representation adverse to the affiliate is derivatively adverse to the client.[125] Comment 34's omission of any mention of adversity

> prompted a dissent by Larry Fox, a member of the Commission [and] a member of the Standing Committee on Ethics and Professional Responsibility.… Fox argued that the ethics opinion has been criticized by the corporate community because of the view that any loss within a corporate family injures, and therefore is directly adverse to, the enterprise as whole. Fox also voiced his concern that although large, sophisticated clients have figured out how to protect themselves from such adverse representation, smaller, less sophisticated enterprises would be disadvantaged by this exception to the rules of loyalty. The motion to delete failed.[126]

Although Formal Opinion 95-390 included direct adversity as one of its three grounds for disqualification of an attorney undertaking representation adverse to an affiliate, Formal Opinion 95-390 defined direct adversity very narrowly.[127] Formal Opinion 95-390 reasoned that direct adversity under Rule 1.7(b) is not present where the client is derivatively harmed by the lawsuit, such as where a lawsuit against a subsidiary reduces its value to its parent, the client.[128] This interpretation of "direct" was based both on the distinction between "direct" and "indirect" established under Rules 1.7(a) and (b) and on the difficulty of drawing a line elsewhere.[129] Because Formal Opinion 95-390 held that derivative

120. *See Commonwealth Land Title Ins.*, 2009 U.S. Dist. LEXIS 87151, at *15 (granting motion to disqualify where, among other things, client expected that attorneys would not undertake representation adverse to its affiliates).

121. *See CFTC*, 2007 U.S. Dist. LEXIS 33137, at *21 (disqualifying where representation of trust possibly limited by loyalty to other client).

122. *See* Formal Op. 95-390, *supra* note *5,* at 1001:261; Restatement of the Law Governing Lawyers § 121 cmt.d (hereinafter "Restatement"); Cliffs Sales Co. v. Am. S.S. Co., Case No. 1:07-CV-485, 2007 U.S. Dist. LEXIS 74342 (N.D. Ohio Oct. 4, 2007).

123. Formal Op. 95-390, *supra* note *5,* at 1001:261.

124. *See, e.g.*, *Cliffs Sales*, 2007 U.S. Dist. LEXIS 74342 (applying Ohio Prof. Cond. R. 1.7, which mirrors Model Rule 1.7 and includes Comment 34, to grant a motion to disqualify where the affiliate was responsible for 80% of the client's income).

125. Restatement, *supra* note *122* § 121 cmt.d.

126. Carl A. Pierce, *Ethics 2000 and the Transactional Practitioner*, 3 Transactions 7, at 15-16 (Spring/Summer 2002).

127. Formal Op. 95-390, *supra* note *5,* at 1001:266.

128. *Id.* at 1001:265-66.

129. *Id.* at 1001:266-67.

adversity should not result in disqualification, and because direct adversity is always grounds for disqualification under Rule 1.7(a)(1), Formal Opinion 95-390 effectively limited disqualification based on adversity to those cases where disqualification would be proper whether the opposing party was an affiliate or not.

Courts considering disqualification have at times denied motions to disqualify based on indirect adversity. In *Cliffs Sales Co. v. American Steamship Co.*,[130] Cliffs Sales Co. ("Cliffs") moved to disqualify defendant's counsel on the grounds that the firm had previously represented Cleveland-Cliffs, Inc. ("CCI"), Cliffs' parent corporation, and was retained by CCI in a different matter during the initial two months of the litigation. Although the firm typically limited its representation to the intentional client through an engagement letter, it had failed to obtain such a letter in its most recent representation of CCI.[131] Therefore, the United States District Court for the Northern District of Ohio considered whether the lawsuit against the affiliate was also directly adverse to its parent, the client.[132]

> Logically any parent of a wholly owned subsidiary could argue that an action against the subsidiary, especially one involving millions of dollars, is necessarily adverse to the parent, making Rule 1.7 a *per se* prohibition against concurrent representation of a parent corporation and another client in opposition to the parent's subsidiary, even in an unrelated matter….
>
> A more reasoned interpretation of Rule 1.7 does not require a finding of a *per se* conflict of interest when a law firm accepts representation … against the subsidiary of a current corporate client. [An affiliate] is not a client of the firm just by virtue of the fact that it is wholly owned by the law firm's [client]. Instead, Rule 1.7 requires the court to examine the facts of each situation to determine if the representation is actually adverse to the [client] thus creating a conflict of interest.
>
> In this case Cliffs generates … about 80% of CCI's total revenue. Cliffs and CCI share a unity of personnel and location. The lawsuit currently before the court concerns a dispute over millions of dollars of overcharges for shipments of iron ore to Mittal Steel, CCI's largest customer, representing 45% of CCI's North American pellet sales, as well as the question of whether [the defendant] is obligated to make winter deliveries of iron ore to Mittal Steel. While the Plaintiff in this lawsuit is Cliffs, nevertheless, CCI, the parent, was obliged by SEC rules to disclose this litigation as material in its most recent Form 10-K filed in May 2007. Based upon these facts, this litigation is … adverse to CCI. Consequently, the court finds that [the firm]'s representation of [the defendant] in this lawsuit while CCI was a client was a conflict of interest and a violation of Rule 1.7(a)(1).[133]

Despite finding a violation of Rule 1.7, the court denied the motion to disqualify on the grounds that no further harm or prejudice would occur because the firm's unrelated representation of CCI had concluded two months into the litigation.[134]

Section 121, comment *d* of the Restatement presents two illustrations discussing whether representation adverse to an affiliate should be considered adverse to the client. Illustration 6 of that Comment explains:

---

130. Case No. 1:07-CV-485, 2007 U.S. Dist. LEXIS 74342 (N.D. Ohio Oct. 4, 2007) (denying motion to disqualify based on Model Rule 1.7(a)(1) where the adversity was derivative, but finding violation of Rule 1.7).

131. *Id.* at *5 (effect of the engagement letter is discussed in greater detail *infra*).

132. *Id.* at *11.

133. *Id.* at *11-13.

134. *Id.* at *16.

> Lawyer represents Corporation A in local real-estate transactions. Lawyer has been asked to represent Plaintiff in a products liability action against Corporation B claiming substantial damages. Corporation B is a wholly owned subsidiary of Corporation A; any judgment obtained against Corporation B will have a material adverse impact on the value of Corporation B's assets and on the value of the assets of Corporation A. Just as Lawyer could not file suit against Corporation A on behalf of another client, even in a matter unrelated to the subject of Lawyer's representation of Corporation A, Lawyer may not represent Plaintiff in the suit against Corporation B without the consent of both Plaintiff and Corporation A under the limitations provided in §122.[135]

Illustration 7 of that Comment demonstrates that the ALI's position does not ignore corporate formalities entirely:

> The same facts as in Illustration 6, except that Corporation B is not a subsidiary of Corporation A. Instead 51% of the stock of Corporation A and 60% of the stock of Corporation B are owned by X Corporation. The remainder of the stock in both Corporation A and Corporation B is held by the public. Lawyer does not represent X corporation. The circumstances are such that an adverse judgment against Corporation B will have no material adverse impact on the financial position of Corporation A. No conflict of interest is presented; Lawyer may represent Plaintiff in the suit against Corporation B.[136]

In light of the pre-existing authorities addressing adversity when the Comment was written, the omission of the subject in Comment 34 to the Model Rules is best seen as a rejection of the principle that litigation against an affiliate presents a unique obstacle for adversity purposes. Because Comment 34 included the explicit requirement that "the lawyer's obligations to either the organizational client or the new client are [not] likely to limit materially the lawyer's representation of the other client," which is the subject of Rule 1.7(a)(2), the omission of an adversity limitation should be read as a rejection of any special adversity standard in the context of affiliates, rather than a reliance on the more general provisions of Rule 1.7(a)(1) to incorporate those standards into the Rule.

This approach, which has been adopted by at least one court,[137] leaves open the possibility that an attorney will be disqualified when the representation directly affects a client, but permits the attorney to sue subsidiaries of a client when that is not the case.[138] In *iSmart International Ltd. v. I-Docsecure, LLC*,[139] the United States District Court for the Northern District of California noted an overlap in ownership between a client and the affiliate that the attorneys had undertaken to sue.[140] Nonetheless, the court denied the motion to disqualify on the grounds that the proper inquiry was

---

135. RESTATEMENT, *supra* note *122* § 121, at 251-52.

136. *Id.*, cmt. d, illus. 7, at 252.

137. *iSmart*, 2006 U.S. Dist. LEXIS 77323, at *13-14.

138. *See, e.g.*, Avacus Partners, L.P. v. Brian, C.A. No. 11001, 1990 Del. Ch. LEXIS 31, at *7-8 (Del. Ch. Mar. 9, 1990) (disqualifying the firm that took the litigation position that a fairness opinion prepared by an investment bank was unreliable when the firm represented that investment bank in unrelated matters because that position rendered the representation directly adverse to the investment bank client).

139. No. C 04-03114 RMW, 2006 U.S. Dist. LEXIS 77323 (N.D. Cal. Oct. 12, 2006).

140. *Id.* at *13-14.

whether the representation of the client gave the attorney any "significant practical advantage" in litigating against the affiliate; the financial impact on the client did not play a role in that analysis.[141] The approach of both *iSmart* and Formal Opinion 95-390 is therefore consistent with Comment 34's permissive opening sentences because the alternate position would effectively create a *per se* prohibition of suing the subsidiary of a client.[142]

G. Although Comment 34 Prevents Disqualification Based Solely On The Corporate Relationships Of A Different Client, It Does Not Eliminate The Possibility Entirely

Comment 34 to the Model Rules creates a system under which a firm is not disqualified from undertaking representation adverse to an affiliate solely on the basis of the affiliate's relationship to a client, with the caveat that the facts of the situation may be such that disqualification may be proper.[143] As the foregoing analysis has demonstrated, courts examine many different factors when assessing whether disqualification is proper in a particular case. The outcome of that analysis can vary dramatically from case to case. Therefore, as a result of the potentially spiraling scope of representation in the corporate context, it becomes important for attorneys to be aware of other tools for managing the scope of a particular representation of a client.

II. ADVANCE WAIVERS PROVIDE THE BEST SOLUTION TO THE PROBLEM OF AFFILIATES UNEXPECTEDLY BEING DECLARED CLIENTS

As the above analysis demonstrates, even when courts apply Comment 34's limitations to attorney-client relationships in corporate families, unexpected and unintended relationships arise.[144] Those relationships can persist for years after the legal work has been completed.[145] It may be tempting in that situation to effect the intended scope of representation by sending a letter to the conflicting affiliate, terminating the unexpected and unintended relationship.[146] If successful,

141. *Id.*

142. "A lawyer who represents a corporation or other organization does not, by virtue of that representation, necessarily represent any constituent or affiliated organization, such as a parent or subsidiary. *See* Del. Prof. Cond. R. 1.13(a). Thus, the lawyer for an organization is not barred from accepting representation adverse to an affiliate in an unrelated matter, unless…." Del. Prof. Cond. R. 1.7 cmt. 34.

143. Del. Prof. Cond. R. 1.7 cmt. 34.

144. *See, e.g.*, *Cliffs Sales*, 2007 U.S. Dist. LEXIS 74342 (N.D. Ohio Oct. 4, 2007).

145. Richard W. Painter, *Advance Waiver of Conflicts*, 13 Geo. J. Legal Ethics 289, 329 n.162 (2000). Note that "[s]ome decisions tolerate relatively long periods of inactivity and find nonetheless that a client remains a current client, subjecting the lawyer to the stricter concurrent-representation rules of conflict." Restatement, *supra* note *122* § 132 cmt.c (citing Shearing v. Allergan, Inc., CV-S-93-866-DWH (LRL), 1994 U.S. Dist. LEXIS 21680 (D. Nev. Apr. 4, 1994) (law firm that had served client for 13 years and had not formally ended relationship was concurrently representing client, despite fact that client had not engaged firm for more than one year)).

146. *See* Truck Ins. Exch. v. Fireman's Fund Ins. Co., 6 Cal. App. 4th 1050, 1057 (Cal. Ct. App. 1992) ("[M]ay the automatic disqualification rule applicable to concurrent representation be avoided by unilaterally converting a present client into a former client prior to hearing on the motion for disqualification? We answer [the] question in the negative and hold, consistent with all applicable authority, that a law firm that knowingly undertakes adverse concurrent representation may not avoid disqualification by withdrawing

continued on page 152

that termination would convert the unexpected current client into a former client so that Rule 1.9[147] would apply to the conflict analysis instead of Rule 1.7.[148] Under Rule 1.7, an attorney may not undertake representation adverse to any current client; under Rule 1.9, however, the representation is only prohibited if the matters are substantially related.[149] When all of the legal work involved in a representation is performed for a related entity, the substantial relationship test provides substantial protection from an otherwise disqualifying conflict of interest.

However, under the "hot potato" rule, a law firm is not ordinarily permitted to discharge a client for the purpose of eliminating a conflict where it desires to accept the representation of another (perhaps more lucrative) client.[150] The rationale behind the "hot potato" rule is that a law firm owes its client a duty of undivided loyalty.[151] Furthermore, even if the law permitted an attorney to drop an unwanted client, business considerations may prevent the post hoc adjustment of an attorney's relationships with affiliates should the firm intend to continue the representation of the client.

continued from page 151

from the representation of the less favored client before hearing." (citing Unified Sewerage Agency v. Jelco, Inc., 646 F.2d 1339, 1345 n.4 (9th Cir. 1981); *Picker Int'l*, 670 F. Supp. at 1366; Margulies v. Upchurch, 696 P.2d 1195 (Utah 1985); and Ransburg Corp. v. Champion Spark Plug Co., 648 F. Supp. 1040, 1043 (N.D. Ill. 1986)). *See also* Flatt v. Superior Court, 885 P.2d 950, 957 (Cal. 1995) ("So inviolate is the duty of loyalty to an existing client that not even by withdrawing from the relationship can an attorney evade it."); Am. Airlines, Inc. v. Sheppard, Mullin, Richter & Hampton, 96 Cal. App. 4th 1017, 1037 (Cal. Ct. App. 2002) ("[A] lawyer may not avoid breaching the duty of loyalty which the concurrent representation rule is designed to avoid by unilaterally converting a present client into a former client. In fact, such conversion may itself be a breach of loyalty."). *But see* Hybrid Kinetic Auto. Holdings, Inc. v. Hybrid Kinetic Auto. Corp., Cause No. 3:09CV00035-MPM-DAS, 2009 U.S. Dist. LEXIS 52322, at *12-13 (N.D. Miss. June 18, 2009) (where a law firm undertook representation adverse to a current client and dropped the current client part way through the litigation, court considered the firm's representation in the new matter under Rule 1.9, not Rule 1.7, for conflict of interest purposes).

147. Model Rule 1.9(a) provides:

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

Model Rule 1.9(a).

148. *See* El Camino Res., LTD. v. Huntington Nat'l Bank, 623 F. Supp. 2d 863, 878 (W.D. Mich. 2007); Patrick J. Johnston, *Amended Rule of Professional Conduct 1.11: Long-Standing Controversy, Imperfect Remedy and New Questions*, 11 Widener J. Pub. L. 83, 124 n.63 (2002).

149. "In determining whether a 'substantial relationship' exists between the two representations, three questions are to be considered: (a) What is the nature and scope of the prior representation at issue; (b) what is the nature of the present lawsuit against the former client; and (c) in the course of the prior representation, might the client have disclosed to his attorney confidences which could be relevant to the present action." Barcher v. Shipman, No. 398, 1993, 1994 Del. LEXIS 274, at *4 (Del. Sept. 15, 1994).

150. *See, e.g.*, Unanue v. Unanue, C.A. No. 204-N, 2004 Del. Ch. LEXIS 37, at *16 (Del. Ch. Mar. 25, 2004) ("The 'hot potato' rule is generally invoked when an attorney drops a small client in order to represent a larger client."); Pennwalt Corp. v. Plough, Inc., 85 F.R.D. 264, 268-69 (D. Del. 1980) (stating that counsel may not eliminate a conflict "merely by choosing to represent the more favored client and withdrawing its representation of the other"); ABA/BNA Lawyers' Manual on Professional Conduct, 51:117-18 (2009) (hereinafter "Lawyers' Manual") ("The weight of authority holds, however, that once the lawyer finds themselves representing clients with adverse interests, they generally may not drop one client in order to represent the other, preferred client. In other words, a lawyer or firm may not drop a current client like a 'hot potato' in order to turn the client into a former client as a means of curing the simultaneous representation of adverse interests." (citing Universal City Studios, Inc. v. Reimerdes, 98 F. Supp. 2d 449, 453 (S.D.N.Y. 2000) and Int'l Longshoremen's Ass'n, Local Union 1332 v. Int'l Longshoremen's Ass'n, 909 F. Supp. 287, 293 (E.D. Pa. 1995))); Restatement, *supra* note *122* § 132 cmt. c ("If a lawyer is approached by a prospective client seeking representation in a matter adverse to an existing client, the present-client conflict may not be transformed into a former-client conflict by the lawyer's withdrawal from the representation of the existing client. A premature withdrawal violates the lawyer's obligation of loyalty of the existing client and can constitute a breach of the client-lawyer contract of employment.").

151. Picker Int'l, Inc. v. Varian Assocs., Inc., 670 F. Supp. 1363, 1366 (N.D. Ohio 1987), *aff'd*, 869 F.2d 578 (Fed. Cir. 1989).

The best response to a morass of corporate affiliations is an engagement letter clearly delineating the scope of representation in accordance with Rule 1.2. Such a letter should not only establish the intended tasks, but, as described below, also should delineate the intended client, specify the situations in which the firm would be disqualified, and establish the intended expiration of the attorney-client relationship, perhaps to the point of modifying the "hot potato" rule itself. As with any advance waiver, the client must provide informed consent to the limitations to the scope of representation; however, when dealing with conflicts implicating Comment 34, that process should be eased by the relative sophistication of large corporate clients and the presence of in-house counsel providing independent legal advice.

Finally, should efforts to obtain an advance waiver fail, if the waivers were not obtained from the proper parties, or if the formation of the attorney-client relationship did not give the attorney the opportunity to obtain proper waivers, there are a limited number of circumstances under which the "hot potato" rule has been waived. These exceptions, discussed in more detail at the end of this article, have not been applied broadly or consistently by courts. Moreover, when used, these exceptions are more likely to damage a relationship with the client than would have been the case had the scope of the relationship been established at the start; thus, they should be viewed as a life raft rather than a row boat.

A. The Power Of Advance Waivers

Advance waivers have been frequently discussed in terms of their ability to waive conflicts of interest generally. Under Rule 1.2(c), advance waivers may be used to restrict any aspect of the scope of the representation so long as the limitation "is reasonable under the circumstances and the client gives informed consent." While the comments to Rule 1.2 do not directly discuss limiting the scope of the relationship by specifying the client, or by redefining, as opposed to waiving, conflicts of interest, by implication Rule 1.2 permits those types of limitations.[152]

1. The Delaware Lawyers' Rules Of Professional Conduct Lay The Groundwork For Flexibly Defining The Attorney-Client Relationship

a. Rule 1.2: The Scope Of Representation

Rule 1.2 governs the "Scope of Representation," providing, in pertinent part: "(c) A lawyer may limit the scope of the representation if the limitation is reasonable under the circumstances and the client gives informed consent."[153] The comments to Rule 1.2 state that "this Rule affords the lawyer and client substantial latitude to limit the representation, [so long as] the limitation [is] reasonable under the circumstances."[154] The comments to Rule 1.2 neither narrow that broad grant of leeway nor clarify what might constitute a reasonable limitation. Comment 6 to Rule 1.2 simply states:

> The scope of services to be provided by a lawyer may be limited by agreement with the client or by the terms under which the lawyer's services are made available to the client. When a lawyer has been retained by an insurer to represent an insured, for example, the representation may be limited to matters related to the insurance coverage. A limited representation may be appropriate because the client has limited objectives for the representation.[155]

152. Del. Prof. Cond. R. 1.2.

153. *Id*. at 1.2(c).

154. *Id.* at 1.2(c) cmt. 7.

155. *Id.* at cmt. 6.

Nonetheless, Formal Opinion 95-390, discussed *supra*, although technically addressing Rule 1.7, not Rule 1.2, expressly advocates limiting the attorney-client relationship prior to representation through the use of an engagement letter: "Clearly the best solution to the problems that may arise by reason of clients' corporate affiliations is to have a clear understanding between lawyer and client, at the very start of the representation, as to which entity or entities in the corporate family are to be the lawyer's clients, or are to be so treated for conflicts purposes."[156] Therefore, the limitation of representation to the intended client is not only permitted, but encouraged.

b. Rule 1.7: Conflicts With Current Clients

Rule 1.2 must be interpreted in light of Rule 1.7 when constraining or defining the attorney-client relationship in order to limit conflicts. Rule 1.7 provides, in part, that a lawyer may undertake the representation of a client, notwithstanding a concurrent conflict of interest, if the client gives informed consent, confirmed in writing.[157] Comment 22 to Rule 1.7 specifically addresses prospective waivers:

> [22] Consent to Future Conflict. – Whether a lawyer may properly request a client to waive conflicts that might arise in the future is subject to the test of paragraph (b). The effectiveness of such waivers is generally determined by the extent to which the client reasonably understands the material risks that the waiver entails. The more comprehensive the explanation of the types of future representations that might arise and the actual and reasonably foreseeable adverse consequences of those representations, the greater the likelihood that the client will have the requisite understanding. Thus, if the client agrees to consent to a particular type of conflict with which the client is already familiar, then the consent ordinarily will be effective with regard to that type of conflict. If the consent is general and open-ended, then the consent ordinarily will be ineffective, because it is not reasonably likely that the client will have understood the material risks involved. On the other hand, if the client is an experienced user of the legal services involved and is reasonably informed regarding the risk that a conflict may arise, such consent is more likely to be effective, particularly if, e.g., the client is independently represented by other counsel in giving consent and the consent is limited to future conflicts unrelated to the subject of the representation. In any case, advance consent cannot be effective if the circumstances that materialize in the future are such as would make the conflict nonconsentable under paragraph (b).

---

156. ABA Formal Op. 390-90, *supra* note *5,* at 1001:259.

157. Delaware Professional Conduct Rule 1.7, provides:

> (a) Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:
>
> (1) the representation of one client will be directly adverse to another client; or
>
> (2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.
>
> (b) Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:
>
> (1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;
>
> (2) the representation is not prohibited by law;
>
> (3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and
>
> (4) each affected client gives informed consent, confirmed in writing.

DEL. PROF.COND. R. 1.7.

While Comment 22 provides general direction regarding the requirements of a valid prospective waiver, significant questions remain. For example, Comment 22 does not discuss the scope of consultation with the client required for the consent to be informed consent. In fact, the wording of Comment 22 suggests that consultation may not be required when a client has independent knowledge of the material risks that the waiver entails,[158] although the informed consent requirement of Rule 1.7 appears to incorporate a duty to consult because Rule 1.0(e) defines informed consent as a process that includes consultation.[159] Viewed at a more nuanced level, no Rule directly addresses whether a written waiver alone can constitute sufficient consultation.

Also noteworthy is Comment 22's suggestion that a more comprehensive explanation of the types of conflicts that might arise and the adverse consequences of those representations increases the likelihood that a client's consent will be informed.[160] While encouraging a comprehensive explanation of conflicts, Comment 22 omits any explanation of what is meant by "types of conflicts" or "adverse consequences." It also fails to provide guidance regarding the critical question of whether a waiver must identify those parties that the lawyer may at some later time wish to represent. On a more general note, Comment 22 provides no guidance regarding the proper balance between the express desire for comprehensive specificity and the inevitable risk that highly specific waiver descriptions will become less effective at conveying the scope of the representation and may lead to arbitrary results when a broad waiver is sought.

Finally, Comment 22 suggests that when a prospective waiver is sought from an experienced user of legal services, a lesser degree of disclosure is required, but the interplay between the amount of disclosure and the sophistication of the client is not clear. For example, when consent is sought from an experienced user of legal services, is counsel required to disclose the types of conflicts that may arise or is it sufficient to disclose only the adverse consequences of a future representation? And, is the advice of in-house counsel weighed differently than that of outside counsel when factored into the equation?

Thus, although Comment 22 outlines general principles bearing on the validity of an advance waiver, it does not provide the sort of detailed guidance that would aid counsel in drafting an effective engagement letter. Therefore, this article turns to case law to address the question of how to stipulate which entities will become clients and what other limitations to possible conflicts of interest might be effective if included in an engagement letter.

2. Some Courts Have Held That A Properly Drafted Engagement Letter Permits A Limitation As To The Client

The first and most important, in this context, use of advance waivers is as a tool to limit the "client" in the attorney-client relationship to the intended client. Law firms may limit the scope of their representation by defining which affiliates in a corporate structure are represented and which are not.[161] Defining the scope of representation by specifying

158. Del. Prof. Cond. R. 1.2 cmt. 22 ("The effectiveness of such waivers is generally determined by the extent to which the client reasonably understands the material risks that the waiver entails.").

159. Delaware Professional Conduct Rule 1.7 requires informed consent, which Rule 1.0(e) defines 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." Del. Prof. Cond. R. 1.0(e).

160. Del. Prof. Cond. R. 1.2 cmt. 22.

161. *See* Ass'n of the Bar of the City of New York Comm. on Prof'l & Judicial Ethics, Formal Op. 2005-05 (hereinafter "New York City Ethics Op. 2005-05"); KBA Bench & Bar, *What Do Hot Potato Clients Have in Common With Thrust Upon Clients? One Heck of a Conflict of Interest Dilemma* (May 2006), Vol. 70, No. 3, at 5, *at* http://www.lmick.com/_resources/documents/bench_and_bar/2006_bench_and_bar_may.pdf (hereinafter "KBA Bench & Bar"); *Advance Waiver of Conflicts*, *supra* note 145, at 314; Lara E. Romansic, *Stand by Your Client?: Opinion 95-390 and Conflicts of Interest in Corporate Families*, 11 Geo. J. Legal Ethics 307, 311 n.119 (1998).

the client in this manner has a number of advantages over a straightforward request for a traditional conflict waiver in the context of a corporate family. First, when the client is undefined, the firm runs the risk that an affiliate will be found to be a client but the conflict waiver will not function because the affiliate was not a party to the waiver.[162] Second, while there is neither statutory authority nor case law on the topic of when it might be impermissible to obtain a limitation as to the client, under Rule 1.7, once an affiliate is a client, some conflicts are unwaivable.[163] Third, if the representation is properly defined, then the substantial relationship test will not apply later when an affiliate has been spun off and still claims a fiduciary duty under Rule 1.9.[164] Finally, employing a definition of the client being represented, rather than solely a waiver of possible future conflicts, has the added benefit of more accurately defining the relationship with the client. In order to prevent the representation from escaping the limitations of the engagement, a law firm can also specify that any new business requires a new agreement of engagement; however, because relationships can form unintentionally, the utility of such letters is limited.[165] Some courts have held that a properly drafted engagement letter precludes a finding that an affiliate was also a client for the purposes of conflict of interest analysis.[166] In practice, a court's willingness to respect such waivers varies dramatically based on the facts of the situation, as shown in the following examples.

a. Some Courts Permit Limitation By Engagement Letter

In *Synergy Tech & Design, Inc. v. Terry*,[167] a law firm's engagement letter provided: "Our representation is limited to Synergy Tech & Design Inc. d/b/a Road Armor, and does not extend to any directors, officers, employees, consultants, or other affiliates. The scope of representation is limited to intellectual property matters."[168] When Synergy's CEO was later terminated and the CEO moved to disqualify the law firm on the grounds that the law firm had also represented him, the United States District Court for the Northern District of California found that the law firm's engagement letter "clearly set[] out the limitation of the engagement to intellectual property matters and explicitly describe[d] the scope of the representation to Synergy as a corporate entity and not to its directors and officers."[169]

Cliffs Sales, discussed *supra*, demonstrates the dangers of representation creep and the possible problems resulting when a law firm employs limited term engagement letters to set contractual limitations as to client, but fails to consistently obtain a new letter each time the intentional engagement is extended.[170] There, an affiliate moved to disqualify opposing

162. *See, e.g.*, *Honeywell*, 2009 U.S. Dist. LEXIS 12496, at *9.

163. *See* Del. Prof. Cond. R. 1.7(a).

164. *See Whiting*, 567 F.2d at 715-16 (affirming denial of motion to disqualify where client owned 20% of defendant's stock and its officers served on defendant's board).

165. *See* New York City Ethics Op. 2005-05; KBA Bench & Bar, *supra* note 161, at 5.

166. *See, e.g.*, *Cliffs Sales.*, 2007 U.S. Dist. LEXIS 74342, at *5. *Cf.* Pamlab, L.L.C. v. Hi-Tech. Pharmacal Co., C.A. No. 08-cv-00967-REB-BNB, 2009 U.S. Dist. LEXIS 3528, at *12-13 (D. Colo. Jan. 9, 2009) (holding that engagement letter specifying that firm, not individual attorneys reprsented client dictated terms of representation for conflict of interest purposes when attorney working on the case left firm and sought to undertake adverse representation).

167. No. C 06-02073 JSW, 2007 U.S. Dist. LEXIS 34463 (N.D. Cal. May 2, 2007).

168. *Id*. at *5.

169. *Id.* at *24.

170. *See Cliffs Sales*, 2007 U.S. Dist. LEXIS 74342.

counsel on the grounds that the representation of the client encompassed representation of the affiliate.[171] The United States District Court for the Northern District of Ohio noted that had the firm obtained its typical engagement letter, the court would not have analyzed the possibility that representation adverse to the affiliate created a conflict of interest.[172] The firm's typical engagement letter provided:

> You should understand, however, that in those matters where we are representing a corporation or other legal entity, our attorney-client relationship is with that specific corporation or legal entity and not with its individual officers, directors, executives, employees, shareholders, partners, or other persons in similar positions, or with its parent, subsidiary, or affiliated corporations or persons. In such cases, our professional duties are owed only to the corporation or legal entity that we have agreed to represent, and you will not assert a conflict because we represent other persons, corporations, or entities that are adverse to any of such related persons, corporations, or other legal entities.[173]

Although the firm was not disqualified, the court found that the representation was a conflict of interest and a clear violation of Rule 1.7.[174] Thus, it is clear that courts do look to and apply the terms of engagement letters when evaluating motions to disqualify; however, a pattern of applying client limitations is insufficient prevention if there is ever a lapse in those limitations, because in that context the affiliate will not have waived the conflict.

b. Some Courts Appear To Ignore Limitations On The Scope Of Representation In An Engagement Letter

In contrast, some courts interpret engagement letters seeking to limit the scope of representation under Rule 1.2 only in the context of conflict waivers under Rule 1.7. If considered in that manner, engagement letters attempting to define the entity represented have not prevented disqualification either because they fail to meet the requirements of Rule 1.7 as to the affiliate or because the affiliate's consent was never obtained.[175] In *McKesson Information Solutions, LLC v. Duane Morris, LLP*, [176] the Superior Court of Georgia considered a motion to disqualify Duane Morris, LLP ("Duane Morris") from representing parties adverse to McKesson Information Solutions, LLC ("MIS") in an arbitration proceeding.[177] "The … engagement letter [in the bankruptcy matter] attempt[ed] to distinguish between McKesson Corporation's entities and contain[ed] a waiver of future conflicts."[178] The portion limiting Duane Morris' representation read:

---

171. *Id.* at *5.

172. *Id.*

173. *Id.*

174 *Id*. at *13.

175. *Id.* at *5

176. No. 2006-CV-121110 (Ga. Super. Ct. Nov. 8, 2006) (on file with authors).

177. Judge Thelma Wyatt Cummings Moore decided *McKesson* and was the Chairwoman of the ABA Judge's Advisory Committee on Ethics. Michael J. DiLernia, *Advance Waivers of Conflicts of Interest in Large Law Firm Practice*, 22 Geo. J. Legal Ethics 97, 100 (Winter 2009) (discussing the contemporaneous controversy surrounding *McKesson*).

178. *Id.*

> This will also confirm that unless we reach an explicit understanding to the contrary, we are being engaged by and will represent McKesson Medication Management LLC and McKesson Automation, and not any parent, subsidiary or affiliated entities of McKesson Medication Management LLC and McKesson Automation, and that we are not being engaged to represent any officers, directors, members, partners, shareholders or employees of McKesson Medication Management LLC and McKesson Automation.[179]

Although the court referenced the engagement letter when discussing the facts of the case, the court did not perform a scope of representation analysis despite the fact that the engagement letter explicitly stated that Duane Morris was "engaged by and will represent McKesson Medication Management LLC and McKesson Automation, and not any parent, subsidiary or affiliated entities."[180] Rather, on the basis of the overlap in personnel and operations, the court concluded that "[the affiliates] are separate and distinct legal entities for contract and liability purposes. However, they are a single entity for purposes of conflict of interest analysis."[181]

The court later discussed whether the conflict of interest, rather than the entire representation of any of the affiliates, had been waived by the engagement letter, holding that the McKesson Engagement Letter did not satisfy Rule 1.7(b) "because it is not a knowing waiver that identifies the specific adverse clients and details of adverse representation…. Defendant's engagement letter does not refer to any particular parties or circumstances under which adverse representation would be undertaken."[182] Therefore, "[the affiliates] could not have reasonably anticipated that Defendant would actually consider representation … where the adverse party is attacking McKesson … accusing it of fraudulent conduct."[183]

This approach has been followed in more recent cases. In *GSI Commerce Solutions, Inc. v. BabyCenter, L.L.C.*,[184] the United States District Court for the Southern District of New York denied a motion to compel arbitration, finding that Blank Rome, the movant's attorneys, had a conflict of interest due to prior representation of Johnson & Johnson ("J&J"), the parent corporation of BabyCenter, L.L.C. ("BabyCenter"), the non-movant.[185] Blank Rome had attempted to prevent this disqualification by including the following provision in its initial engagement letter with J&J:

> Unless agreed to in writing or we specifically undertake such additional representation at your request, we represent only the client named in the engagement letter [*i.e.*, J&J], and not its affiliates, subsidiaries, partners, joint venturers, employees, directors, officers, shareholders, members, owners, agencies, departments, or divisions. If our engagement is limited to a specific matter or transaction, and we are not engaged to represent you in other matters, our attorney-client relationship will terminate upon the

---

179. McKesson Engagement Letter, dated May 30, 2006 (on file with authors) (hereinafter "McKessson Engagement Letter").

180. *Id.*

181. *Id.* at 5.

182. *McKesson*, No. 2006-CV-121110, at 11 (citing Worldspan, L.P., v. The Sabre Group Holdings, Inc., 5 F. Supp. 2d 1356 (N.D. Ga. 1998)).

183. *Id.*

184. 644 F. Supp. 2d 333 (S.D.N.Y. 2009).

185. *Id.* at 334 (applying New York law, which has not adopted Model Rule 1.7 cmt. 34 verbatim).

> completion of our services with respect to such matter or transaction whether or not we send you a letter to confirm the termination of our representation.

Despite contractually limiting its representation to J&J via the engagement letter, Blank Rome periodically

> provide[d] legal advice relating to J&J's subsidiaries and affiliates on specific matters or transactions…. "[m]ost of the work Blank Rome performed pursuant to the Engagement Agreement was for J&J's operating companies rather than for J&J itself." … "One such representation was of BabyCenter." … [However,] at no time did Blank Rome provide any advice to BabyCenter in connection with its agreement with GSI, nor did [Blank Rome] have access to any privileged information relating to that agreement or the parties' course of dealings.[186]

The court held that the engagement letter was ineffective in the face of Blank Rome's work for BabyCenter[187] and then found that the letter failed to waive the resulting conflict of interest. After reaching those conclusions, the court appears to have held that the engagement letter was irrelevant to the analysis of whether BabyCenter should be considered a client of Blank Rome:

> GSI reads the Engagement Agreement rather more broadly than its language justifies. In particular, it may not fairly be read to limit Blank Rome's duty of loyalty to J&J's subsidiaries that it undertakes to represent nor to authorize Blank Rome to sue those companies at the same time it is representing them…. Moreover, the Engagement Agreement itself contains prospective waivers of certain conflicts, thus indicating (at least implicitly) that Blank Rome was aware of the potential conflict of interest that would be posed by its representation of interests adverse to J&J and its subsidiaries. [188]

> In short, notwithstanding the scope of representation set forth in the Engagement Agreement, the court is satisfied that the relationship between BabyCenter and J&J is sufficiently "close as to deem them a single entity for conflict of interest purposes."[189]

The court's willingness in *BabyCenter* to set aside the engagement letter between Blank Rome and J&J can be attributed to a number of factors that mitigate the broader impact of the case. First, *BabyCenter* was decided under New

---

186. *Id.* at 335 (quoting declarations) (third modification in original).

187. *Id.* ("The Engagement Agreement also noted that Blank Rome had reviewed its then-current engagements, and found a conflict requiring J&J's waiver: its representation of Kimberly-Clark Corporation in patent litigation against J&J affiliate McNeil PPC…. Aside from this 'specifically defined category of matters … for Kimberly-Clark,' Blank Rome did not seek, nor did it receive, any prospective waiver from J&J for any other future conflict.").

188. *Id.* at 336. The court goes on to write:

> Although technically BabyCenter is a wholly owned subsidiary of J&J, … as a practical matter it is part and parcel of J&J. Among other things, BabyCenter shares accounting, audit, cash management, employee benefits, finance, human resources, information technology, insurance, payroll, and travels service and systems with J&J…. Of particular relevance here, BabyCenter … relies on J&J's Law Department for legal services … Further, the agreement … that is the subject of the underlying arbitration was negotiated by an attorney in J&J's Law Department …. Indeed, it is undisputed that members of J&J's Law Department have been involved in this action on behalf of BabyCenter since the parties' dispute arose in October 2008, … and Blank Rome … has dealt with J&J attorneys during the pendency of this action…. Further, since BabyCenter is a wholly owned subsidiary, its liabilities directly impact [J&J.].

Id. at 336-37.

189. *Id.* (internal citations omitted) (quoting Stratagem Dev. Corp. v. Heron Int'l N.V., 756 F. Supp. 789, 792 (S.D.N.Y. 1991)).

York Law, which has historically been more willing to adopt a bright-line rule that affiliates should be treated as clients than are jurisdictions that have adopted the Model Rules verbatim.[190] Second, although the court did not discuss Blank Rome's work for BabyCenter while finding BabyCenter to be a client of Blank Rome, the fact that Blank Rome had done work for BabyCenter while the engagement letter was in place likely played a role in the outcome.[191] Therefore, *BabyCenter* demonstrates some possible pitfalls when using an engagement letter to limit representation, but it is not necessarily a representative approach.

c. The Entity Whose Consent Is Required For An Effective Limitation Of The Scope Of Representation Turns On Whether A Limitation As To Scope Is Sought Under Rule 1.2 Or Whether An Advance Conflict Waiver Is Sought Under Rule 1.7

Limiting the scope of representation under Rule 1.2 requires the consent of the intended client.[192] Whereas, once the court determines that the affiliate deserves to be treated as a client, the affiliate's informed consent is required for an advance waiver under Rule 1.7.[193] The distinction can be explained by the fact that "'as a general rule, courts do not disqualify an attorney on the grounds of conflict of interest unless the former client moves for disqualification.'"[194] Thus, before the court determines that the affiliate is also a client, the affiliate's consensual waiver is unnecessary; after the court determines an affiliate is also a client, its consent becomes relevant.

When a court analyzes whether an affiliate is or should be treated as a client, the client's, not the affiliate's, consent is required because, under current case law, the affiliate has no legal right to be included in the relationship.[195] In *Whiting Corp. v. White Machinery Corp.*,[196] White Machinery Corp. ("White") moved to disqualify counsel for the plaintiff because the firm also represented a client that was a corporation owning 20 percent of White's stock and controlling two seats on White's board.[197] White argued that "its interests will be prejudiced by the continued dual representation."[198] Despite reciting that argument, the court's analysis did not weigh possible prejudice to White. Instead, the United States Court of Appeals for the Seventh Circuit pointed out that the stockholder client and the plaintiff client had been informed of the

---

190. *See, e.g.*, *Stratagem*, 756 F. Supp. at 793 (impact by litigation on the client's bottom line required disqualification); *compare* Formal Op. 390-95, 1001:267 (derivative adversity, such as an indirect impact on the client's bottom line, should not result in disqualification); *Pennwalt*, 85 F.R.D. at 270 (relationship between client and affiliate is not the proper inquiry).

191. *BabyCenter*, 644 F. Supp. 2d at 335.

192. *See Whiting*, 567 F.2d at 715-16 (affirming denial of motion to disqualify where client owned 20% of defendant's stock and its officers served on defendant's board).

193. *See Honeywell*, 2009 U.S. Dist. LEXIS 12496, at *7-8.

194. Concat LP v. Unilever, PLC, 350 F. Supp. 2d 796, 818 (N.D. Cal. 2004) (quoting Kasza v. Browner, 133 F.3d 1159, 1171 (9th Cir. 1998) (quoting United States v. Rogers, 9 F.3d 1025, 1031 (2d Cir. 1993) (quoting, in turn, *In re* Yarn Processing Patent Validity Litig., 530 F.2d 83, 88 (5th Cir. 1976)))).

195. *See Whiting*, 567 F.2d at 715.

196. 567 F.2d 713 (7th Cir. Ill. 1977).

197. *Id.* at 715-16.

198. *Id.*

situation and neither objected to the firm's dual representation.[199] Because both clients consented to the representation, the court denied the motion to disqualify without additional discussion of the interests of White.[200] Nevertheless, "because of the sensitivity of this matter and in order to take all appropriate prophylactic measures to avoid a development of the possibility of a conflict and in order to preclude the impression of any impropriety whatsoever, the … firm is directed to disassociate and refrain from representing and/or advising [the Client] in connection with any proceedings related to [the products involved in the litigation] during the pending litigation."[201] *Whiting* is useful for two propositions. First, it demonstrates that in a conflict of interest analysis the pertinent focus will be on the interests of the client, not the interests of the affiliate. Second, the case demonstrates that a client's decision to waive a conflict will be binding on the affiliate. That second proposition forms the basis for any limitation of representation through engagement letters.

In contrast, once courts determine that an affiliate should be treated as a client, only the affiliate may waive the conflict.[202] For example, in *Honeywell*, discussed *supra*, the United States District Court for the Eastern District of Texas found that an affiliate was also a client because of the overlap in operations between the client and the affiliate.[203] The court then went on to consider the possibility that the conflict had been waived.[204] The court stated: "Here, there is no indication that [the affiliate] gave its consent to [the firm]; in fact, [the affiliate] denies such consent. In situations such as this one, where the 'problem has been created by modern corporations, the onus is squarely on the lawyer to anticipate and resolve conflicts of interest involving corporate affiliates.'"[205] Thus, the court found the attorney to be disqualified.[206]

Avocent, discussed *supra*, demonstrates an even more problematic possibility. There the United States District Court for the Western District of Washington first determined that the engagement letter did not preclude representation of the affiliate. The court then considered whether the conflict was waived under the engagement letter and found that "even if this prospective waiver applied to the issues in this case, only [the client] agreed to waive prospective conflicts. Given that defendants construe this letter as a representation of [the client] only, the agreement cannot also be construed by defendants as a waiver by [the affiliates]."[207] Thus, the firm was whipsawed by a finding that, on the one hand, it had not limited the scope of representation, and, on the other hand, its argument on that topic precluded reading the engagement letter to apply to the affiliate. Given authority such as *Honeywell* and *Avocent*, which look to the affiliate's waiver of conflict, it may be worth sending affiliates a non-engagement letter, while also obtaining their consent to future conflicts where practicable as a "belt and suspenders" measure.

---

199. *Id.*

200. *Id*.

201. *Id.*

202. *Avocent*, 491 F. Supp. 2d at 1006.

203. *Honeywell*, 2009 U.S. Dist. LEXIS 12496, at *7-8.

204. *Id.* at *9.

205. *Id.* (quoting *In re* Dresser Indus., Inc., 972 F.2d 540, 545 (5th Cir. 1992)).

206. *Id.*

207. *Avocent*, 491 F. Supp. 2d at 1006.

3. Some Commentators Have Suggested That Advance Waivers Can Permit Early Termination Of The Attorney-Client Relationship, In Addition To Preventing Its Development

While the "hot potato" rule prohibits mercenarily terminating attorney-client relationships, several secondary sources have suggested alternatives, in the form of advance waivers, which would address the same concerns.[208] Advocates of advance waivers argue that absent the ability to obtain such waivers, law firms may refuse to undertake representation of a prospective client because of fear that by doing so it could expose the firm's more established (and presumably more lucrative) clients to the loss of their counsel.[209]

Professor Richard W. Painter, a legal ethics scholar,[210] has identified several prophylactic measures that law firms could use as an alternative to attempting to terminate a client-relationship in violation of the "hot potato" rule through the use of advance waivers in engagement letters.[211] These measures, relying on Rule 1.2(c)'s permission to limit the scope of a client's representation, are discussed below.[212]

a. Engagement Letters May Define What Is And Is Not A Substantially Related Matter

The simplest solution to the problem of a client relationship being analyzed under Rule 1.7 rather than Rule 1.9 is to terminate the relationship. But the "hot potato" rule prohibits that solution. The next most sweeping solution is to

---

208. *See* KBA Bench & Bar, *supra* note 161, at 3 (noting that "[s]ome lawyers try to anticipate the ['hot potato'] problem by getting an advance waiver for possible future conflicts in a letter of engagement"); Henry M. Kelln, *Dropping the Hot Potato: Resuscitating the Permissive Withdrawal Rules in the Model Rules of Professional Conduct*, 42 (Mar. 20, 2006), bepress Legal Series, *at* http://law.bepress.com/expresso/eps/1164 (hereinafter "*Dropping the Hot Potato*") ("[T]he efficacy of the ['hot potato'] rule is limited under the fact that the prohibition is 'contracted around' via advance waiver agreements offered by large law firms."); Edward C. Brewer, *The Ethics of Internal Investigations in Kentucky and Ohio*, 27 N. Ky. L. Rev. 721, 791 (2000) ("[a]n 'advance waiver' is in part an effort to avoid the 'hot potato' rule"); John A. Edginton, *Managing Lawyers' Risks at the Millennium*, 73 Tul. L. Rev. 1987, 2039 n.104 (1999) (finding that the "hot potato" rule "is another risk that can possibly be addressed by advance waivers if a conflict can at all be anticipated, such as mergers or purchases of businesses"); Brian J. Redding, *The Conflicts Jungle in Modern Litigation*, *in* The Litigation Manual: Special Problems and Appeals 560-71 (John G. Koeltl & John S. Kiernan eds., 1999) (suggesting that a possible solution to avoid the "hot potato" problem is for law firms to include waiver language in engagement letters in advance of adverse representation on matters unrelated to the firm's current representation); Mass. Bar Ass'n Comm. on Prof'l Ethics Op. 92-3 (Sept. 22, 1992) (finding that some lawyers were using advance consents in order to avoid the "hot potato" situation).

209. *See* Nathan M. Crystal, *Enforceability of General Advance Waivers of Conflicts of Interest*, 38 St. Mary's L.J. 859, 881 (2007) (citing Jonathan J. Lerner, *Honoring Choice by Consenting Adults: Prospective Conflict Waivers as a Mature Solution to Ethical Gamesmanship - A Response to Mr. Fox*, 29 Hofstra L. Rev. 971, 1004 (2001)). *See also* Kennecott Copper Corp. v. Curtiss-Wright Corp., No. 78 Civ. 1295, slip op. at 6-7 (S.D.N.Y. Apr. 11, 1978) ("Quite clearly, Skadden, Arps, a burgeoning law firm, was unwilling to close its doors to future clients by risking disqualification in its field of specialty merely because Curtiss-Wright [a "one shot client"] might set its sights on some company which happened to be a client of Skadden, Arps.") (upholding advance waiver).

210. Professor Richard W. Painter was the former chief ethics lawyer for former President George W. Bush, has been active in law reform efforts aimed at improving ethics of corporate managers and lawyers, is active in the Professional Responsibility Section of the ABA, is a co-author of Professional and Personal Responsibilities of the Lawyer (2d ed. 2001), and has written many other books, articles and essays concerning ethics. *See* Richard W. Painter's Faculty Profile, http://www.law.umn.edu/facultyprofiles/painterr.html.

211. *Advance Waiver of Conflicts*, *supra* note 145, at 313.

212. *Id.*; Lawyers' Manual, *supra* note 150, at 51:119-20. *See also* Rule 1.2(c) (quote).

contract in the engagement letter to effectively apply Rule 1.7 rather than Rule 1.9. A law firm and its client could agree *ex-ante* that the substantial relationship test applies to current client conflicts.[213] As previously discussed, the substantial relationship standard is a prerequisite to demonstrating former client conflicts, but is not a prerequisite when analyzing conflicts between current clients.

"Retainer agreements could [also] address … what is or is not a 'substantially related matter' and when a subsequent representation should be allowed to proceed, even though two matters are substantially related."[214] For instance, a law firm and its client could specify in the retainer agreement:

> (a) that a subsequent matter will not be substantially related to a matter worked on by the lawyer unless confidential information is imparted to the lawyer in the first matter that could be used adversely to the client in the second matter;
>
> (b) that transactions entered into by the client within a certain time frame are/are not substantially related to a matter worked on by the lawyer;
>
> (c) that certain categories of transactions are/are not substantially related to a matter worked on by the lawyer;
>
> (d) that certain categories of transactions engaged in by a subsidiary or affiliated entity of the client are/are not "substantially related" to a transaction of the client;
>
> (e) circumstances in which the lawyer is/is not free to attack her own work; and
>
> (f) circumstances in which "playbook" arguments [i.e., where a former client claims that a lawyer learned of information of very general nature – such as strategies for negotiating transactions, launching hostile takeovers, or settling litigation] would/would not be waived.[215]

b. Engagement Letters May Define What Is An Adverse Interest

In addition to or in lieu of contracting to apply a substantial relationship test, a law firm and its client could also agree *ex ante* what is and is not an "adverse interest."[216] Examples of such definitions include the following:

> (a) an economic competitor of the first client does/does not have interests that are adverse to the first client;
>
> (b) a potentially adverse interest is/is not an adverse interest;

---

213. *Advance Waiver of Conflicts*, *supra* note 145, at 317-19. *See also id*. at 321 (citing Interstate Props. v. Pyramid, 547 F. Supp. 178 (S.D.N.Y. 1982) and Fisons Corp. v. Atochem N. Am., Inc., No. 90 Civ. 1080 (JMC), 1990 U.S. Dist. LEXIS 15284 (S.D. Cal. Nov. 14, 1990) as examples of where courts essentially based their enforcement of advance waivers to a concurrent conflict on their findings that the matters were not substantially related).

214. *Advance Waiver of Conflicts*, *supra* note 145, at 319.

215. *Id.* at 319-20.

216. *Id.* at 316.

> (c) a certain category of legal work, such as negotiating on the opposite side of a transaction from a client, is/is not representation of an adverse interest; and
>
> (d) a positional conflict [i.e., where a lawyer advocates on behalf of one client a legal argument that is inconsistent with an argument advanced on behalf of another client] is/is not an adverse interest.[217]

c. Engagement Letters May Define The Duration Of The Representation

Finally, a law firm could define whether the representation is ongoing.[218] Professor Painter stated, with respect to limiting the duration of representation:

> A lawyer and client presumably could *contract around the hot potato rule* by agreeing ex-ante that the representation shall have a defined duration or that the lawyer may resign at will from representing the client. Alternatively, the lawyer and client could agree that the lawyer may resign if the client later refuses to give consent to the lawyer's representation of another client with an adverse interest in an *unrelated* matter.[219]

Delaware courts will likely disfavor any contractual agreement between a law firm and a current client where the current client agreed in advance of a conflict that the law firm could simply drop the current client in order to represent another preferred client with an adverse interest in a *related* matter.[220] Professor Painter has explained that "information learned in an unrelated representation is generally of limited value and the client is furthermore still protected by separate prohibitions on disclosure or adverse use of client information."[221]

B. How Much Information Is Required For A Client To Give The Informed Consent Necessary To Agree To Any Of These Limitations?

"At the heart of any conflict waiver analysis is the question of whether the client provided informed consent."[222] Advance waivers will be ineffective in the absence of truly informed consent,[223] and attorneys have the burden of proving

---

217. *Id.* at 316-17.

218. *See* New York City Ethics Op. 2005-05; KBA Bench & Bar, *supra* note 161, at 5.

219. *Advance Waiver of Conflicts*, *supra* note 145, at 322 (emphasis added; no citations provided).

220. *See* D.C. Bar Ass'n Legal Ethics Comm., Op. 309, at 1 (2001) (finding that advance waivers are not valid, even if reviewed by independent counsel, "where the two matters at issue are substantially related to one another"); *Advance Waiver of Conflicts*, *supra* note 145, at 303 (noting that the court in *Interstate Props.*, 547 F. Supp. 178, implicitly acknowledged a limit to *ex ante* contracting in not approving a waiver where the law firm had represented the client in a matter substantially related to the present litigation).

221. *Advance Waiver of Conflicts*, *supra* note 145, at 321 (citing Model Rules 1.6 & 1.8(b)).

222. Irvin M. Freilich & Meghan O. Murray Robertson, *Advance Waivers Of Conflicts - Real Or Theoretical?*, Metropolitan Corporate Counsel (Oct. 2008), at 47, *available at* http://www.metrocorpcounsel.com/pdf/2008/October/47.pdf. *See also* Del. Prof. Cond. R. 1.7 cmt. 22 ("The effectiveness of [advance] waivers is generally determined by the extent to which the client reasonably understands the material risks that the waiver entails.").

223. Century Indem. Co. v. Congoleum Corp., 426 F.3d 675, 691 (3d Cir. 2005). *See, e.g.*, Worldspan L.P. v. Sabre Group Holdings Inc., 5 F. Supp. 2d 1356, 1360 (N.D. Ga. 1998) (disqualifying law firm from representing new client in tort matter directly

continued on page 165

full disclosure and of establishing the fact and scope of consent.[224] "Informed consent" is defined in Rule 1.0(e) 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."[225] "[T]he requirement of informed consent is more likely to be met if the prospective waiver is specific about the types of matters and parties covered, and if the client is relatively sophisticated,[226] and the client has an opportunity to seek advice of other counsel before agreeing to the waiver."[227]

Law firms should be as specific as possible with respect to the types of possible future adverse representations, the types of matters that might present conflicts, and at least the class of potentially conflicted clients.[228] "Such clarity in the ex-ante waiver is critical to accomplishing what the waiver was intended to accomplish: avoidance of ex-post litigation over disqualification."[229] Comment 22 to Rule 1.7 states: "If the consent is general and open-ended, then the consent ordinarily

continued from page 164

adverse to existing client in tax matters, despite firm's claim that existing client prospectively waived future conflicts through standing consent in engagement letter six years earlier, because conducting litigation against an existing client was a matter so serious that any agreement purporting to grant standing consent must clearly and specifically identify that possibility); *In re* Suard Barge Servs., Inc., C.A. 96-3185, 1997 U.S. Dist. LEXIS 12364, at *15-16 (E.D. La. Aug. 14, 1997) (holding that a valid waiver must "disclose the nature of the actual or potential conflict" and that no waiver existed because the client "believed at that time that no conflict existed, so [the lawyer] did not explain the conflict in the requisite detail"); Schwartz v. Indus. Valley Title Ins. Co., C.A. No. 96-5677, 1997 U.S. Dist. LEXIS 8176, at *15-16 (E.D. Pa. June 4, 1997) (finding that a 1993 prospective conflict waiver in a related but separate suit was ineffective to waive a conflict in connection with an action beginning three years later because the lawyer failed to inform the client that there could be future adverse litigation) (internal quotation omitted).

224. *El Camino*, 2007 U.S. Dist. LEXIS 67813, at *43. *See also* Glidden Co. v. Jandernoa, 173 F.R.D. 459, 480 (W.D. Mich. 1997) ("The law imposes certain obligations upon … attorneys who seek to advance conflicting interests. They have the duty to make full disclosure and obtain clear and informed consent. If the transaction thereafter goes sour, theirs is the burden of proving full disclosure and the fact and scope of consent. This burden is not met by arguing that the party to whom the duty was owed had constructive knowledge of the conflict. Such a position would shift the burden from the fiduciary to the party to whom the duty is owed. To satisfy the burden of full disclosure, it is not sufficient that both parties be informed of the fact that a lawyer is undertaking to represent both of them. Rather, there must be a disclosure of risks in such detail that the person can understand the reasons why it may be desirable to withhold consent.").

225. Del. Prof. Cond. R. 1.0(e). *See also* Restatement § 122 (stating that informed consent requires "that the client or former client have reasonably adequate information about the material risks of such representation to that client or former client"); Nathan M. Crystal, *Enforceability of General Advance Waivers of Conflicts of Interest*, 38 St. Mary's L.J. 859, 885 (2007) ("Informed consent normally requires explanation of the advantages, disadvantages, and alternatives available to the client from whom the waiver is sought." (citing Model Rule 1.0 cmt. 6 & Restatement, *supra* note *122* § 122 cmt. c(i))).

226. "According to the Restatement, courts should not be looking at a client's education and business in a vacuum, but instead should be considering whether the client has experience dealing with questions of conflict and has had the opportunity to 'receive independent legal advice about the consent.'" Irivn M. Freilich & Meghan O. Murray, *Advance Waivers of Conflicts – Real or Theoretical?*, Metropolitan Corporate Counsel (Oct. 1, 2008), at 47, *available at* http://www.rfbclaw.com/upload/103108084655MCC%20Article%20-%2010-08%20-%20IMF%20and%20MOM.pdf (quoting Restatement, *supra* note *122* § 122 cmt. d).

227. Lawyers' Manual, *supra* note 150, at 51:119. *See also* Visa U.S.A., Inc. v. First Data Corp., 241 F. Supp. 2d 1100, 1106 (N.D. Cal. 2003) ("An evaluation of whether full disclosure was made and the client made an informed waiver 'is obviously a fact-specific inquiry.' … Factors that may be examined include the breadth of the waiver, the temporal scope of the waiver (whether it waived a current conflict or whether it was intended to waive all conflicts in the future), the quality of the conflicts discussion between the attorney and the client, the specificity of the waiver, the nature of the actual conflict (whether the attorney sought to represent both clients in the same dispute or in unrelated disputes), the sophistication of the client, and the interests of justice.").

228. N.Y. City Eth. Op. 2004-02.

229. *Advance Waiver of Conflicts*, *supra* note 145, at 326.

will be ineffective, because it is not reasonably likely that the client will have understood the material risks involved."[230] If clients are experienced consumers of legal services who are reasonably informed and independently counseled, general and open-ended consent is more likely to be effective.[231]

In addition to the black and white issue of enforceability, the grey area issue of business relationships also plays a role whenever the attorneys' objective is to perform work for the entities in the future. Thus, not only enforceability, but the long-term feasibility of future relationships turns on a solid understanding and genuine agreement to the terms of the waiver.

In *Celgene Corp. v. KV Pharmaceutical Co.*,[232] a patent dispute involving methylphenidate, defendant's counsel, Buchanan Ingersoll & Rooney PC ("Buchanan"), concurrently represented plaintiff Celgene in two separate matters involving securities and thalidomide.[233] Buchanan had obtained prospective waivers in both the securities[234] and thalidomide[235]

230. DEL. PROF. COND. R. 1.7 cmt. 22. Courts take a fairly critical view of such "blanket" future waivers. *See* LAWYERS' MANUAL, *supra* note 150, at 51:219 (citing Fl. Ins. Guaranty Ass'n, Inc. v. Carey Canada, 749 F. Supp. 255, 260 (S.D. Fla. 1990) and Univ. of Rochester v. G.D. Searle & Co., 00-CV-6161L(B), 2000 U.S. Dist. LEXIS 19030, at *32-33 (W.D.N.Y. Dec. 11, 2000)).

231. ABA Comm. on Ethics & Prof'l Responsibility, Formal Op. 05-436 (2005). *See also* RESTATEMENT, *supra* note *122* § 122 cmt. d ("A client's open-ended agreement to consent to all conflicts normally should be ineffective unless the client possesses a sophistication in the matter in question and had had the opportunity to receive independent legal advice about the consent."); DEL. PROF. COND. R. 1.7 cmt. 22 ("[I]f the client is an experienced user of the legal services involved and is reasonably informed regarding the risk that a conflict may arise, such [general and open-ended] consent is more likely to be effective, particularly if, e.g., the client is independently represented by other counsel in giving consent and the consent is limited to future conflicts unrelated to the subject of the representation."); Angela R. Elbert, *Switch Hitting? Ethical Implications of Advance Conflict Waivers*, ABA 2007 Annual Meeting, at 7, (Aug. 11, 2007) (acknowledging a trend toward allowing more "open-ended" advance consents from sophisticated and independently represented clients); NYCLA Ethics Op. No. 724 (Jan. 28, 1998) (blanket waiver may be permissible, "depending on the client's sophistication, its familiarity with the law firm's [multidisciplinary] practice, and the reasonable expectations of the parties at the time consent is obtained"). *See, e.g.*, St. Barnabas Hosp. v. N.Y. City Health & Hosp. Corp., 7 A.D.3d 83, 93, 97 (N.Y. App. Div. 2004) (where a hospital was a sophisticated, institutional client and had full knowledge of the law firm's representation of another hospital regarding similar issues, court held that plaintiff's informed consent was adequate to defeat any appearance of impropriety created by the waiver's failure to include litigation as a possible conflict); Elonex I.P. Holdings, Ltd. v. Apple Computer, Inc., 142 F. Supp. 2d 579, 582-83 (D. Del. 2001) (finding attorney "sufficiently explained the conflict in order to obtain a prospective waiver" and client was sophisticated); Laborers Local 1298 Annuity Fund v. Grass (*In re* Rite Aid Corp. Sec. Litig.), 139 F. Supp. 2d 649, 653, 659-60 (E.D. Pa. 2001) (relying on § 132 of the RESTATEMENT, court found that a CEO gave informed consent to an advance waiver even though he alleged that he never had the opportunity to speak with outside counsel and never received a copy of the engagement letter); Zador Corp. v. Kwan, 31 Cal. App. 4th 1285 (Cal. Ct. App. 1995) (allowing law firm to continue to represent long-time client over protest of another client who was sophisticated and aware of the longtime relationship and had been advised to look for independent counsel before approving the joint representation); *Fisons*, 1990 U.S. Dist. LEXIS 15284, at *15-16 (finding that a prospective waiver should be enforced when adequate disclosure was made to a sophisticated client even though the disclosure did not include the exact nature of the future dispute). *But see* Celgene Corp. v. KV Pharm. Co., C.A. No. 07-4819 (SDW), 2008 U.S. Dist. LEXIS 58735, at *23, *31-32 (D.N.J. July 28, 2008) (finding that a law firm failed to demonstrate that it obtained a sophisticated client's "truly informed consent" where the retention agreement proposed a future course of conduct that was very open-ended and vague).

232. C.A. No. 07-4819 (SDW), 2008 U.S. Dist. LEXIS 58735 (D.N.J. July 28, 2008).

233. *Id.* at *2.

234. The securities litigation waiver provided:

> Recognizing and addressing conflicts of interest is a continuing issue for attorneys and clients. We have implemented policies and procedures to identify actual and potential conflicts at the outset of each engagement. From time to time we may be asked to represent someone whose interests may differ from the interests of the Company. We are accepting this engagement with the Company's understanding and express consent that our representation of the Company will not preclude us from accepting an engagement from a new or existing client, including litigation or

continued on page 167

representations.[236] The United States District Court for the District of New Jersey, ruling on plaintiff Celgene's motion to disqualify Buchanan as counsel for defendant KV, first observed that Buchanan's representation of KV constituted a concurrent conflict of interest under Rule 1.7(a) of the New Jersey Rules of Professional Conduct.[237] Noting that the parties had framed the issue as one of contractual interpretation of the "substantially related" language in the securities and thalidomide waivers, the court held that the relevant legal issue was, rather, whether Celgene had given informed consent, confirmed in writing, after full disclosure and consultation.[238] The court further noted that it must look beyond the waiver to determine whether informed consent was given.[239]

Looking to the text of the waivers, the court found that neither waiver manifested informed consent within the meaning of Rule 1.0(e) because: (1) the course of conduct proposed was vague and open-ended, (2) adequate information regarding the risks of the proposed course of conduct was lacking, and (3) an explanation of reasonably available alternatives to the course of conduct was lacking.[240] The court found unpersuasive the fact that one of the waivers was executed by in-house counsel for Celgene, explaining that because consent in this case was not informed, the provisions in Comment 22 and ABA Formal Opinion 05-436 (according weight to the fact that a waiver transaction was negotiated by outside counsel) did not apply to validate the waiver.[241]

continued from page 166

> other matters that may involve the Company. However, we will not accept an engagement that is directly adverse to the Company or any of its subsidiaries if either: (1) it would be substantially related to the subject matter of our representation of the Company or representation of Anthrogenesis Corp.; or (2) would impair the confidentiality of proprietary, sensitive or otherwise confidential communications made to us by the Company or Anthrogenesis Corp.

Id. at *4.

235. The thalidomide litigation waiver provided:

> From time to time we may be asked to represent someone whose interests may differ from the interests of the Company. The firm is accepting this engagement with the Company's understanding and express consent that our representation of the Company will not preclude us from accepting an engagement that is adverse to the Company or its interests, including litigation. However, we will not accept an engagement that is directly adverse to the Company or any of its subsidiaries if either: (1) it would be substantially related to the subject matter of our representation of the Company; or (2) would impair the confidentiality of proprietary, sensitive or otherwise confidential communications made to us by the Company.

Id. at *5.

236. *Celgene*, 2008 U.S. Dist. LEXIS 58735, at *2-5.

237. *Id.* at *8. Rule 1.7 of the New Jersey Rules of Professional Conduct requires, in addition to the requirements of Model Rule 1.7, that "full disclosure and consultation" precede a client's proffer of informed consent.

238. *Celgene,* 2008 U.S. Dist. LEXIS 58735, at *11.

239. It is unclear, however, whether this statement reflects the law regarding prospective waivers generally or the requirement of full disclosure and consultation set forth in the New Jersey Rules of Professional Conduct.

240. *Celgene*, 2008 U.S. Dist. LEXIS 58735, at *22-23.

241. *Id.* at *26-27. Specifically, the court noted:

> [Formal Op. 05-436] merely acknowledges that a consent that is informed but general is likely to be valid if the client was represented by independent counsel in the waiver transaction. In the instant case, this court finds no evidence that the consent was informed, and so the fact that Celgene spoke through in-house patent counsel … does not have the weight contemplated in Opinion 05-436.

Id. at *27.

continued on page 168

Turning its attention to evidence outside of the waivers, the court observed that Buchanan did not consult with Celgene regarding the waiver and did not disclose anything regarding conflicts of interest prior to obtaining Celgene's consent. It then held that Celgene's sophistication did not excuse Buchanan from obtaining informed consent, implying that Buchanan was obligated to provide disclosure and consultation.[242]

The court next examined Buchanan's argument that the KV representation was not substantially related, as that phrase is used in the securities and thalidomide waivers, to the Celgene representation, and that Buchanan's KV representation therefore falls within the scope of conduct that Celgene consented to. Restating its earlier holding that the motion to disqualify does not depend upon contract construction, but rather upon interpretation of the Rules of Professional Responsibility, the court noted that even if the contract issue was dispositive, the representations at issue were substantially related. The court based this conclusion on the premise that the phrase "substantially related" was ambiguous, and under New Jersey contract law principles, ambiguities are construed against the drafter.[243]

There are several principles to keep in mind in this context. First, a general waiver may be invalidated notwithstanding the fact that a sophisticated party is represented by counsel in the waiver transaction. Second, courts may examine evidence outside of the waiver in determining whether consent was informed.[244] Third, if there is a concurrent conflict of interest, the requirements of Rule 1.7(b) must be met, and those requirements cannot be circumvented by contract. Redefinition efforts such as those in previously described *Celegene* cannot sidestep such analysis.

C. Are Limitations On The Scope Of Representation Or Advance Waivers Reconcilable?

Even if a law firm employs the above-mentioned techniques in specifying the scope of representation, a client always has the right to revoke an advance waiver.[245] Whether the revocation will be effective as to a matter that the firm has undertaken depends on a number of factors.[246] Comment 21 to Rule 1.7 states that these factors include "the nature of the conflict, whether the client revoked consent because of a material change in circumstances, the reasonable expectations

---

continued from page 167

This conclusion is questionable, however, because the natural reading of Comment 22 and Formal Op. 05-436 is that when a client is represented by counsel in a waiver transaction, the fact of the representation weighs in favor of a finding that the client gave informed consent, notwithstanding the fact that the waiver is general. The court here concludes that because the waiver was general, the client did not give informed consent, implying that the fact that the client was represented by counsel does not affect the determination of whether the consent was informed. Thus, rather than weighing the generality of the waiver against the fact of representation, the court makes its conclusion solely on grounds of generality. This approach is difficult to square with the clear language of Comment 22.

242. It is again worth noting that Rule 1.7 of the New Jersey Rules of Professional conduct explicitly requires full disclosure and consultation, unlike the Delaware version of the rule. Query whether, in light of Rule 1.0(e), the consultation and disclosure requirements of New Jersey Rule 1.7 are redundant.

243. *Celgene*, 2008 U.S. Dist. LEXIS 58735, at *35-40.

244. *Id*.

245. *See* Del. Prof. Cond. R. 1.7 cmt. 21 (explaining a client's right to revoke a waiver).

246. *Id*.

of the other client and whether material detriment[247] to the other clients or the lawyer would result."[248] Illustration 7 of § 122 of the Restatement provides the following relevant example:

> Client A, who consulted Lawyer about a tax question, gave informed advance consent to Lawyer's representing any of Lawyer's other clients against Client A in matters unrelated to Client A's tax question. Client B, who had not theretofore been a client of Lawyer, wishes to retain Lawyer to file suit against Client A for personal injuries suffered in an automobile accident. After Lawyer informs Client B of the nature of Lawyer's work for Client A, and the nature and risks presented by any conflict that might be produced, Client B consents to the conflict of interest. After Lawyer has undertaken substantial work in preparation of Client B's case, Client A seeks to withdraw the advance consent for reasons not justified by the conduct of Lawyer or Client B. Even though Client A was Lawyer's client before Client B was a client, the material detriment to both Lawyer and Client B would render Client A's attempt to withdraw consent ineffective.[249]

This illustration is instructive for the principle that if there has been substantial reliance by the law firm on the advance waiver and revocation of the waiver would result in material detriment to other clients or the law firm,, the likelihood that revocation will be effective as to a matter that the law firm has already undertaken is substantially diminished.

D. Exceptions To The "Hot Potato" Rule

Although the "hot potato" rule normally prevents a law firm from prematurely ending a suddenly undesirable attorney-client relationship, as explained below the rule is not inflexible. Some courts have applied a "tempered approach" to effect a just result, while other courts have carved out exceptions to the "hot potato" rule that may allow a law firm to drop one client in favor of another when a conflict arises as the result of a client's unilateral acts or through factors not within the law firm's control. These exceptions have been labeled as the "thrust upon" rule and the "accommodation client" rule.

1. The "Tempered" Approach

A recent case discussing the "hot potato" rule has stated that "courts should not be overly eager to substitute a clever phrase for thorough legal analysis."[250] In *Metropolitan Life Insurance Co. v. Guardian Life Insurance Co. of America*,[251]

247. Material detriment may occur, for example, when (i) the other client and the lawyer already have invested time, money, and effort in the representation, (ii) the other client already has disclosed confidential information and developed a relationship of trust and confidence with the lawyer, or (iii) a client relying on the consent might reasonably have elected to forgo opportunities to take other action. Restatement, *supra* note *122* § 122 cmt. f.

248. Del. Prof. Cond. R. 1.7 cmt. 21.

249. Restatement , *supra* note *122* § 122 illus. 7. *See also Unified Sewerage Agency*, 646 F.2d at 1346 (refusing to disqualify a law firm when the former client tried to revoke a prior consent that the present client and the law firm had relied upon in creating the lawyer-client relationship); *Fisons*, 1990 U.S. Dist. LEXIS 15284 (relying on *Unified Sewerage* as authority for the proposition that reliance on the consent estopped the client from revoking the consent at a later time).

250. *Metro. Life Ins. Co. v. Guardian Life Ins. Co. of Am.*, No. 06 C 5812, 2009 U.S. Dist. LEXIS 42475, at *13-14 (N.D. Ill. May 18, 2009). *See also* 1 Geoffrey C. Hazzard, Jr. & William Hodes, The Law of Lawyering, § 20.10 (3d ed. Supp. 2005-1) (criticizing a strict approach to the "hot potato" rule that applies the rule whenever a lawyer drops a client for the purpose of suing that client on behalf of someone else, finding that it "is inconsistent with the permissive withdrawal scheme of Model Rule 1.16(b) and Restatement, *supra* note *122* § 32(3), for … those provisions permit a lawyer to cease representation – assuming no harm to the client – for no reason or because the lawyer is bored or overworked or because more lucrative work presents itself").

251. No. 06 C 5812, 2009 U.S. Dist. LEXIS 42475 (N.D. Ill. May 18, 2009).

the United States District Court for the Northern District of Illinois questioned whether the "hot potato" rule applies in situations where "a lawyer's representation is sporadic, non-litigious, and unrelated to the issues involved in the newer case."[252] That case involved a dispute between two insurance companies where the plaintiff insurer moved to disqualify the law firm representing the defendant insurer because the defendant's law firm had previously represented the plaintiff and the law firm had never formally terminated its representation of the plaintiff until the defendant entered the picture.[253] Although the court found a technical violation of the "hot potato" rule, it held that the violation did not require disqualification because the plaintiff failed to show that it would suffer any harm if the law firm represented the defendant.[254] The law firm's previous non-litigation work for the plaintiff was wholly unrelated to the plaintiff's current action against the defendant.[255] The law firm's conduct was neither "nefarious [n]or underhanded,"[256] and disqualifying the law firm "would only delay the movement of [the] case, increase the parties' costs and deprive [the defendant] of its choice of counsel."[257] "The [c]ourt [would] not furnish such a result, despite any ethical violations that may have occurred."[258]

Another example of a court applying a "tempered approach" to effect a just result is *Air Products & Chemicals, Inc. v. Airgas, Inc.*[259] In that case, industrial gas producer Airgas, Inc. ("Airgas") filed suit against Cravath, Swaine & Moore LLP ("Cravath") over the law firm's role as legal adviser to rival Air Products & Chemical, Inc. ("Air Products") on that company's $5.1 billion bid for Airgas.[260] Airgas argued that Cravath terminated its attorney-client relationship with the company after nearly a decade in order to represent Air Products, a 40-year client, in the transaction.[261] Airgas also claimed that Cravath was working on financing deals with Airgas during the same time it was advising Air Products in the deal that was the subject of the litigation.[262]

The Delaware Court of Chancery found that no basis existed to disqualify Cravath from representing Air Products in the pending litigation and thus denied Airgas's motion to disqualify Cravath.[263] The court noted that motions to disqualify opposing counsel require a high burden of proof that the disqualification is really necessary to prevent real

---

252. *Id.* at *13.

253. *Id.* at *1-2, *9. The case did not involve an engagement letter permitting withdrawal.

254. *Id.* at *14-15.

255. *Id.* at *15.

256. *Id.* at *8.

257. *Id.* at *15-16.

258. *Id.* at *16.

259. C.A. No. 5249-CC, 2010 Del. Ch. LEXIS 35 (Del. Ch. Mar. 5, 2010) ("*Airgas II*").

260. *Id.* at *4; Press Release, Air Products & Chemicals, Inc., *Air Products Offers to Acquire Airgas for $60.00 Per Share in Cash* (Feb. 5, 2010), at http://www.airproducts.com/PressRoom/CompanyNews/Archived/2010/05Feb2010.htm.

261. Airgas, Inc. v. Cravath, Swaine & Moore LLP, C.A. No. 10-612, 2010 U.S. Dist. LEXIS 15120, at *2 (E.D. Pa. Feb. 22, 2010) ("Airgas I").

262. *Id.* at *3.

263. *Airgas II*, 2010 Del. Ch. LEXIS 35, at *6.

harm to the movant client.[264] "Airgas … [had] not demonstrated even simply persuasively, let alone clearly and convincingly, that it would be disadvantaged by the presence of its former counsel as advocate for its opponent, Air Products."[265] Cravath's work for Airgas was limited in scope and nature.[266] Moreover, even if Cravath had access to information that might be relevant in the current proceeding, it declared that it did not intend to use such information and had erected an "ethical wall" between those members of the firm who worked with Airgas and those working with Air Products.[267] The court reasoned that, "[g]iven the absence of any credible threat of prejudice to Airgas from Cravath's continued participation in this lawsuit, I think the threat of harm to Air Products from disqualification far outweighs the threat of harm to Airgas from a failure to disqualify."[268]

Therefore, although the "hot potato" rule generally prohibits mercenarily terminating an attorney-client relationship, there is support for a more case-specific application of the rule that would permit attorneys to end representation in order to avoid conflicts where it would not be unjust to the terminated client for the attorney to do so.

2. The "Thrust Upon" Exception

The "thrust upon" exception typically applies when a conflict results from client merger activity or additional parties join a lawsuit.[269] Comment 5 to Model Rule 1.7 provides authority for the "thrust upon" exception. It states, in relevant part:

> Unforeseeable developments, such as changes in corporate and other organizational affiliations … might create conflicts in the midst of a representation[.] Depending on the circumstances, the lawyer

---

264. *Id.* at *7-8. Specifically, the court stated:

> Before this Court may enter the Draconian order of disqualification, a moving party seeking that drastic relief must come forward with clear and convincing evidence establishing a violation of the Delaware Rules of Professional Conduct so extreme that it calls into question the fairness or the efficiency of the administration of justice…. [E]ven when a violation of the ethical rules has, in fact, occurred, it need not automatically result in disqualification. And, more recently, in the Dow Chemical case, I refused to disqualify counsel when there was no showing that counsel's participation as an advocate unfairly benefited its present client, in that instance Rohm & Haas, or unfairly prejudiced its former client, the Dow Chemical Company, even though the representation of the two clients may have overlapped.

Id.

265. *Id.* at *8.

266. *Id.* at *9.

267. *Id.*

268. *Id.* at *10.

269. LAWYERS' MANUAL, *supra* note 150, at 51:118. *See, e.g.*, Pennwalt Corp. v. Plough, Inc., 85 F.R.D. 264, 268-69 (D. Del. 1980) (denying motion to disqualify, in part because the purported conflict had been "thrust upon" the law firm by the merger activities of the company that sought to disqualify the law firm); Bd. of Regents of the Univ. of Nebraska v. BASF Corp., 4:04CV3356, 2006 U.S. Dist. LEXIS 58255, at *31-32 (D. Neb. Aug. 17, 2006) (discussing the "thrust upon" exception and denying motion to disqualify because of an "unforeseeable development"). *But see, e.g.*, United States v. Nabisco, Inc., CV-86-3277, 1987 U.S. Dist. LEXIS 16795, at *19-21 (E.D.N.Y. July 10, 1987) (E.D.N.Y.1987) (granting motion to disqualify despite the fortuity that the conflict was produced by the client's merger into the opposing party).

> may have the option to withdraw from one of the representations in order to avoid the conflict. The lawyer must seek court approval where necessary and take steps to minimize harm to the clients[.][270]

In order for a conflict to be considered "thrust upon" the lawyer, the Bar of the City of New York has stated that four elements must exist:

> 1) [the conflict must] not exist at the time either representation commenced, but arose only during the ongoing representation of both clients, where 2) the conflict was not reasonably foreseeable at the outset of the representation, 3) the conflict arose through no fault of the lawyer, and 4) the conflict is of a type that is capable of being waived …, but one of the clients will not consent to the dual representation.[271]

"Many courts have found that the duty of loyalty concerns underpinning the 'hot potato' rule are not present in the 'thrust upon' situation where the lawyer has not instigated the conflict or deliberately sought to abandon a client."[272] Consequently, several courts have applied a flexible approach to the "thrust upon" situations that focuses on balancing the interests of all affected parties, rather than mechanically applying the "hot potato" rule to prevent a lawyer from withdrawing from one client in order to continue representing the other.[273]

One well-known example where a court has applied such an approach is *Ex parte AmSouth Bank N.A.*,[274] "where the conflict was created by a mid-suit change in the configuration of the parties."[275] In that case, a law firm represented AmSouth Bank N.A. ("Am South") in various transactional matters.[276] The law firm was later retained by Drummond Co. ("Drummond") to defend a stockholder suit challenging a merger with Alabama By-Products Corporation ("ABC").[277] AmSouth, as trustee for trusts owning stock in ABC, also sued Drummond over the merger.[278] When the law firm realized that a direct adversity conflict had been thrust upon it, the law firm sought the consent of both AmSouth and Drummond

---

270. Del. R. Prof. Cond. 1.7 cmt. 5. *See also* Restatement, *supra* note *122* § 132 cmt. j ("A lawyer may withdraw in order to continue an adverse representation against a theretofore existing client when the matter giving rise to the conflict and requiring withdrawal comes about through initiative of the clients. An example is a client's acquisition of an interest in an enterprise against which the lawyer is proceeding on behalf of another client.").

271. NYC Ethics Op. 2005-05, *supra* note 161.

272. *Id*.

273. *See, e.g.*, Eastman Kodak Co. v. Sony Corp., 04-CV-6095, 04-CV-6098, 2004 U.S. Dist. LEXIS 29883, at *27-28 (W.D.N.Y. 2004) (holding that "the 'flexible approach' provides a far more practical framework to disqualification issues generated by mergers and acquisitions than the rigid 'hot potato' rule," but balancing the interests in favor of disqualification).

274. 589 So.2d 715 (Ala. 1991).

275. The Law of Lawyering, *supra* note 250, § 11.21.

276. *Ex parte AmSouth Bank*, 589 So.2d at 716.

277. *Id.*

278. *Id.* at 716-17.

to waive the conflict.[279] When AmSouth refused, the law firm withdrew from its representation of AmSouth.[280] The Supreme Court of Alabama refused to disqualify the law firm from continuing to represent Drummond, finding that the law firm did not play a role originally in creating the conflict.[281] Moreover, Drummond would be prejudiced by the law firm's disqualification in the stockholder suit more than AmSouth would be prejudiced by the loss of the law firm's services in its routine transactional matters.[282] The court followed a "common sense" approach and found that the law firm may avoid disqualification by "moving swiftly to withdraw from its representation" to minimize prejudice to each client concerned.[283]

A court also applied a flexible approach to the resolution of a "thrust upon" conflict in *Gould Inc. v. Misui Mining & Smelting Co.*[284] In that case, a law firm represented Gould, Inc. ("Gould") in a patent infringement suit against Pechiney.[285] At the same time, the law firm represented IG Technologies ("IGT") in various matters.[286] Soon thereafter, a conflict arose when Pechiney acquired IGT.[287] The law firm never attempted to obtain Pechiney's consent to the law firm's continuing representation of both IGT and Gould, and the law firm refused a request that it withdraw as counsel for Gould.[288] The United States District Court for the Northern District of Ohio held that concurrent representation of the two parties would be considered inappropriate and determined that the law firm had committed ethical violations.[289]

The court then considered the following factors in determining whether disqualification was required: prejudice to the moving party, receipt of confidential information as a result of prior representation, the cost of retaining new counsel (in terms of both time and money), the delay to the litigation caused by requiring plaintiff to obtain new counsel, the complexity of the issues in the case, the time it would take new counsel to acquaint themselves with the facts and issues, and the fact that the conflict was created by merger after the case was commenced, not by any affirmative act of counsel.[290] The court ultimately found that disqualification was not warranted, but emphasized that "the conflict must not be allowed to endure."[291] The court thus allowed the law firm to discontinue representation of either Gould or IGT.[292]

---

279. *Id.* at 717.

280. *Id.*

281. *Id.* at 719, 722.

282. *Id.* at 719.

283. *Id.* at 719, 722.

284. 738 F. Supp. 1121 (N.D. Ohio 1990).

285. *Id.* at 1122.

286. *Id.* at 1123.

287. *Id.*

288. *Id.*

289. *Id.* at 1125-26.

290. *Id.* at 1126-27.

291. *Id.* at 1127.

292. *Id.* The court did, however, report the law firm's ethical violation to the state disciplinary counsel. *Id.*

The court rationalized its decision by indicating that it did not see how "the rules of ethics will be furthered by forcing [the law firm] to withdraw as counsel … due to a conflict that it did not create[.]"[293]

3. The "Accommodation Client" Exception

Courts permit withdrawal from some relationships on the grounds that the relationship was not entitled to the primary duty of loyalty. Thus, some courts have held that a lawyer may withdraw from representation to cure a conflict involving an "accommodation client" under certain circumstances.[294] An accommodation client relationship is formed when, with the informed consent of each client as provided in Section 122 of the Restatement, a lawyer undertakes representation of another client as an accommodation to the lawyer's regular client, typically for a limited purpose and in order to avoid duplication of services and the consequent higher fees.[295] Comment i to Section 132 of the Restatement provides that circumstances warranting the lawyer's continued representation of the regular client when adverse interests later develop between the clients include "that the lawyer has represented the regular client for a long period of time before undertaking representation of the other client, that the representation was to be of limited scope and duration, and that the lawyer was not expected to keep confidential from the regular client any information provided to the lawyer by the other client."[296]

Illustration 9 of Section 132 of the Restatement provides the following relevant example of the "accommodation client" exception:

> Law Firm has represented Financial Corporation for many years as outside general counsel. Financial Corporation, represented by Law Firm, and Client Two, represented by separate counsel, entered into an agreement to operate a business. A shareholder derivative suit was later filed against both Financial Corporation and Client Two on a claim related to the agreement. Client Two by this point had become hard-pressed financially. Financial Corporation and Client Two had potential claims against each other arising out of the transaction but did not assert them so as to present a united front to the plaintiffs in the shareholder suit. Although separately represented in the shareholder derivative action, Financial Corporation and Client Two exchanged information in that action for the common purpose of defending against it … During pretrial, Law Firm, with the informed consent of Financial Corporation and Client Two, filed motions in the action in behalf of both Financial Corporation and Client Two. Later, Client Two filed for bankruptcy, and the Trustee in bankruptcy brought suit against Financial Corporation, seeking to recover damages based on the same underlying agreement. Notwithstanding Trustee's objection …, Law Firm may withdraw from representing Client Two in the derivative action

---

293. *Id. See also* Installation Software Techs., v. Wise Solutions, No. 03 C 4502, 2004 U.S. Dist. LEXIS 3388, at *10-11 (N.D. Ill. Mar. 2, 2004) (applying a flexible approach to the resolution of a conflict arising out a corporate acquisition, balancing several factors including (i) prejudice, (ii) cost, (iii) the complexity of the case, and (iv) the origin of the conflict, *but* finding that the law firm should be disqualified).

294. *See* LAWYERS' MANUAL, *supra* note 150, at 51:118 ("If adversity develops between a lawyer's regular client and another client that the lawyer undertook to represent as an 'accommodation' to the lawyer's regular client, 'circumstances might warrant the inference that the 'accommodation' client understood and impliedly consented to the lawyer's continuing to represent the regular client in the matter.") (quoting RESTATEMENT, *supra* note *122* § 132 cmt. i).

295. THOMAS D. MORGAN, *Lawyer Law: Comparing the ABA Model Rules of Professional Conduct with the ALI Restatement (Third) of the Law Governing Lawyers* (ABA Ctr. for Prof'l Responsibility, 2005), at 525.

296. RESTATEMENT, *supra* note *122* § 132 cmt. i.

> and represent Financial Corporation in defending against Trustee's suit. Circumstances warrant the inference that Client Two understood that Law Firm would continue to represent Financial Corporation in any such action.[297]

The most often cited case supporting an "accommodation client" theory is *Allegaert v. Perot*.[298] In *Allegaert*, a bankruptcy trustee of duPont Walston, Inc. ("Walston"), a brokerage firm, moved to disqualify the two law firms who represented some of the defendants in a preference action brought by the trustee.[299] The preference action arose out of Walston's joint venture realignment with another failing brokerage, duPont Glore Forgan ("DGF").[300] The law firms had represented DGF and other interested parties in the joint venture realignment and had thereafter represented Walston in a derivative action, which all parties conceded was substantially similar to the current lawsuit.[301] The bankruptcy trustee based his disqualification motion on the law firms' representation of Walston in the derivative action.[302]

The trial court declined to disqualify the law firms in an analysis under Canon 4 of the New York Code of Professional Responsibility (which provides that "a lawyer should preserve the confidences and secrets of a client"), and the Second Circuit Court of Appeals affirmed.[303] The appellate court noted that an attorney may be disqualified pursuant to Canon 4 if he has accepted employment adverse to the interests of a former client on a matter substantially related to the prior litigation.[304] The appellate court stated:

> Once the substantial relationship is established, the court need not inquire whether the attorney in fact received confidential information, because the receipt of such information will be presumed. However, … before a substantial relationship can be implicated it must be shown that the attorney was in a position where he could have received information which his former client might reasonably have assumed the attorney would withhold from his present client.[305]

"Because Walston necessarily knew that information given to [the law firms] would certainly be conveyed to their primary clients [*i.e.*, DGF and its Affiliates], in view of the realignment agreement," the court reasoned that "the substantial relationship test [was] inapposite."[306] Walston reasonably could not have believed that any information that it gave to the law firms in the course of the derivative action would be withheld from the regular clients.[307] Moreover, Walston always had another law firm as its own counsel.[308]

---

297. *Id*., illus. 9.

298. 565 F.2d 246 (2d Cir. 1977).

299. *Id.* at *248-49.

300. *Id*.

301. *Id.* at *248-49.

302. *Id.* at *248.

303. *Id.* at *251.

304. *Id.* at *250.

305. *Id*. (emphasis in original) (internal citation omitted).

306. *Id*.

307. *Id*.

308. *Id*. Other cases following the *Allegaert* approach include: Skidmore v. Warburg Dillon Read, 99 Civ. 10525 (NRB),

continued on page 176

A relatively recent case from the Third Circuit that adopts the *Allegaert* approach is *In re Rite Aid Corp. Securities Litigation v. Grass*.[309] In *Rite Aid*, a law firm represented a company and its former CEO in securities class litigation.[310] The law firm memorialized its representation in an engagement letter to the company's general counsel, which explained that while there did not appear to be a conflict of interest that would prevent the law firm from representing both the company and its CEO, it was possible that such a conflict might arise in the future.[311] Should that occur, it was "understood" that the CEO would retain separate counsel and that the law firm would continue to represent Rite Aid.[312]

When it later became evident that the CEO had breached his fiduciary duty to the corporation, the law firm withdrew from its representation of the CEO.[313] The United States District Court for the Eastern District of Pennsylvania found that Rule 1.9, rather than the more stringent Rule 1.7, applied and that the representation did not warrant disqualification because the CEO was simply an "accommodation client" and the corporation was clearly the "primary client."[314] "In other words, the law firm's representation of the CEO was by virtue of the concurrent representation of the corporation and existed for the sake of lowering attorney costs."[315] The court relied on Comment i to Section 132 of the Restatement, which explains that in situations that arise between the "primary client" and the "accommodation client," the accommodation client "impliedly consent[s] to the lawyer's continuing to represent the regular client in the matter."[316]

Factors other than the "accommodation client" concept also warranted the court's conclusion. Because the CEO did not object to the law firm's representation of the company for approximately one year and was represented by sophisticated counsel the entire time, the CEO's delay constituted a waiver.[317] Moreover, the engagement letter made it clear that in the event of the conflict, the law firm would cease representation of the CEO and continue to represent the company.[318]

---

continued from page 175

2001 U.S. Dist. LEXIS 6101 (S.D.N.Y. May 11, 2001); Host Marriott Corp. v. Fast Food Operators, Inc., 891 F. Supp. 1002, 1006-08 (D. N.J. 1995); Kempner v. Oppenheimer & Co., 662 F. Supp. 1271, 1276-78 (S.D.N.Y. 1987); Am. Special Risk Ins. Co. v. Delta Am. Re Ins. Co., 634 F. Supp. 112, 120-21 (S.D.N.Y. 1986); C.A.M. v. E.B. Marks Music, Inc., 558 F. Supp. 57, 59 (S.D.N.Y. 1983); Anderson v. Pryor, 537 F. Supp. 890, 895-96 (W.D. Mo. 1982).

309. 139 F. Supp. 2d 649 (E.D. Pa. 2001).

310. *Id.* at 652.

311. *Id.* at 652-53.

312. *Id.* at 653.

313. *Id.* at 654.

314. *Id.* at 658, 660.

315. *Dropping the Hot Potato*, *supra* note 208, at 31 (citing *Rite Aid*, 139 F. Supp. 2d at 658).

316. *Rite Aid*, 139 F. Supp. 2d at 658. In some cases, courts have rejected the "accommodation client" concept. *See, e.g.*, *Universal City Studios*, 98 F. Supp. 2d at 453-56 (rejecting law firm's argument that it represented a particular corporation only as an accommodation to the parent corporation, who was the firm's long-standing client, and denying the law firm permission to withdraw and sue the former client in an unrelated matter); Ins. Co. of N. Am. v. Westergren, 794 S.W.2d 812, 814-15 (Tex. Ct. App. 1990) (where lawyer argued that he could represent a contractor in litigation against a surety even though the lawyer had earlier represented the surety in substantially related matters in which the contractor was also a party pursuant to the accommodation client concept and the surety did not pay his fees, and "at no time did [the attorney] receive confidential information from or give advice to [the surety]," court concluded the attorney shared an attorney client relationship with the surety and rejected the accommodation client argument).

317. 139 F. Supp. 2d at 654, 661-62.

318. *Id.* at 660.

III. CONCLUSION

The ever-changing developments in corporate structures due to mergers, spin-offs, purchases and sales of corporations have resulted in the very real potential for conflicts of interest in corporate families. While a law firm may be tempted to simply drop a corporate affiliate when a conflict of interest arises in order to represent a more desirable corporate family member, such a reaction is prohibited under the "hot-potato" doctrine. Advance waivers thus present a practical approach by which law firms can control the risk of disqualification resulting from corporate family conflicts. Because advance waivers will be ineffective in the absence of truly informed consent, law firms should ensure that a client waiver is reviewed by independent counsel and that the client is sufficiently informed of the advantages, disadvantages and alternatives available to the client from whom the waiver is sought. Even where an advance waiver is lacking, however, some courts have carved out exceptions to the "hot potato" doctrine that allow a law firm to withdraw from representing one client in favor of another client where a conflict was "thrust upon" a law firm or where a law firm undertakes representation of another client as an "accommodation" to the law firm's regular client.