From Deal to Dispute: Ethics Lessons in Business Transactions

CLE Written Materials – Issue Spotting

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Part 1: The Deal and the First Red Flag

You are the General Counsel of Midstate University. The Board of Trustees of Midstate University is considering constructing a new Life Sciences building on an undeveloped parcel it owns in a strategic partnership with a local developer. During a Facilities Subcommittee meeting, Sarah mentions she recalls hearing a rumor years ago about possible soil erosion issues on the site, though nothing was documented.

Another Subcommittee member, Tom, suggests an environmental engineer he knows who can "take an unofficial look." The engineer provides an oral "all-clear," and the Subcommittee recommends moving forward. The Board approves the project, and you, as General Counsel, oversee negotiation of a sophisticated development agreement.

At the groundbreaking, within your earshot, Sarah thanks the engineer for easing her concerns about "the old rumor." The engineer responds that he was "happy to do a solid for his partner," and that he and Tom "have been working together on deals for years, and both their wallets appreciate it."

Part 2: Warning Signs and Internal Pressure

You speak to the Board Chair and the President about what you heard at the celebratory ground-breaking. You agree on next steps to address Tom's conflict of interest, but take no further action with respect to the soil erosion issue, reasoning that, aside from the conflict issue, there is no clear basis to question the engineer's conclusions.

Construction continues apace, with only one small incident of contained damage to the foundation of a building adjoining the parcel. The owner investigates and determines that the damage was attributable to a soil erosion issue resulting from Midstate's development, of which the developer denies any knowledge. Midstate's Assistant Director of Risk and Insurance notifies Midstate's insurer of the incident as a matter of course, and when asked in a follow-up communication from the insurer whether there was any prior knowledge of the soil erosion problem says – truthfully, in light of her limited knowledge – that there was not.

You raise concerns with the Board Chair and President about this statement, and they tell you to "stay in your lane," "don't over-think it," and take no further action. You are uncomfortable but unsure whether this rises to the level requiring further escalation.

Part 3: Litigation, Privilege, and Exposure

Times have gotten tough for Midstate. The owner of the neighboring parcel has sued both Midstate and the developer. The developer proposes a litigation cooperation agreement without fully addressing potential conflicts or privilege implications. The President and Board Chair are eager to do so, as they think this will "save money" and "we're all on the same side." You raise concerns about the non-disclosure of the soil erosion "rumor," engineer's oral report, and identified conflict of interest, as well as the Assistant Director's statements to the insurer.

Outside counsel, a transactional lawyer brought on to work on the deal, tells you not to worry and they "can handle it" because "it will likely settle anyway." Feeling troubled, you check your email, and there is correspondence from counsel for the neighbor, who has apparently told their attorney that Midstate must have known about the soil erosion problem because Sarah is on the Board, and "would have heard all about it." You are increasingly concerned about your own ethical obligations.

Please note: ***bolded*** *text is included verbatim in slides.*

Part 1: The Deal and the First Red Flag

Nonprofit Board Member Duties:

- **Duty of Care: To ensure prudent use of assets, including financial resources, human resources, and goodwill**
- **Duty of Loyalty: To act in the best interests of the organization, and to recognize and disclose any conflicts of interest**
- **Duty of Obedience: To ensure institutional compliance with law and regulation and trustee compliance with same, and with institutional bylaws/charter/articles**

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Model Rule 1.13: Organization as Client
Client-Lawyer Relationship

(a) A lawyer employed or retained by an organization represents the organization acting through its duly authorized constituents.

(b) If a lawyer for an organization knows that an officer, employee or other person associated with the organization is engaged in action, intends to act or refuses to act in a matter related to the representation that is a violation of a legal obligation to the organization, or a violation of law that reasonably might be imputed to the organization, and that is likely to result in substantial injury to the organization, then the lawyer shall proceed as is reasonably necessary in the best interest of the organization. Unless the lawyer reasonably believes that it is not necessary in the best interest of the organization to do so, the lawyer shall refer the matter to higher authority in the organization, including, if warranted by the circumstances to the highest authority that can act on behalf of the organization as determined by applicable law.

(c) Except as provided in paragraph (d), if

> (1) despite the lawyer's efforts in accordance with paragraph (b) the highest authority that can act on behalf of the organization insists upon or fails to address in a timely and appropriate manner an action, or a refusal to act, that is clearly a violation of law, and
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> (2) the lawyer reasonably believes that the violation is reasonably certain to result in substantial injury to the organization, then the lawyer may reveal information relating to the representation whether or not Rule 1.6 permits such disclosure, but only if and to the extent the lawyer reasonably believes necessary to prevent substantial injury to the organization.

(d) Paragraph (c) shall not apply with respect to information relating to a lawyer's representation of an organization to investigate an alleged violation of law, or to defend the organization or an officer, employee or other constituent associated with the organization against a claim arising out of an alleged violation of law.

(e) A lawyer who reasonably believes that he or she has been discharged because of the lawyer's actions taken pursuant to paragraphs (b) or (c), or who withdraws under circumstances that require or permit the lawyer to take action under either of those paragraphs, shall proceed as the lawyer reasonably believes necessary to assure that the organization's highest authority is informed of the lawyer's discharge or withdrawal.

(f) In dealing with an organization's directors, officers, employees, members, shareholders or other constituents, a lawyer shall explain the identity of the client when the lawyer knows or reasonably should know that the organization's interests are adverse to those of the constituents with whom the lawyer is dealing.

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

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Part 2: Warning Signs and Internal Pressure

Model Rule 4.1: Truthfulness in Statements to Others
Transactions With Persons Other Than Clients

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

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

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

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Model Rule 1.2: Scope of Representation & Allocation of Authority Between Client & Lawyer
Client-Lawyer Relationship

(a) Subject to paragraphs (c) and (d), a lawyer shall abide by a client's decisions concerning the objectives of representation and, as required by Rule 1.4, shall consult with the client as to the means by which they are to be pursued. A lawyer may take such action on behalf of the client as is impliedly authorized to carry out the representation. A lawyer shall abide by a client's decision whether to settle a matter. In a criminal case, the lawyer shall abide by the client's decision, after consultation with the lawyer, as to a plea to be entered, whether to waive jury trial and whether the client will testify.

(b) A lawyer's representation of a client, including representation by appointment, does not constitute an endorsement of the client's political, economic, social or moral views or activities.

(c) A lawyer may limit the scope of the representation if the limitation is reasonable under the circumstances and the client gives informed consent.

(d) A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent, but a lawyer may discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client to make a good faith effort to determine the validity, scope, meaning or application of the law.

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Model Rule 2.1: Advisor
Counselor

In representing a client, a lawyer shall exercise independent professional judgment and render candid advice. In rendering advice, a lawyer may refer not only to law but to other considerations such as moral, economic, social and political factors, that may be relevant to the client's situation.

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Part 3: Litigation, Privilege, and Exposure

Model Rule 1.1: Competence
Client-Lawyer Relationship

A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation.

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Model Rule 3.3: Candor Toward the Tribunal
Advocate

(a) A lawyer shall not knowingly:

> **(1) make a false statement of fact or law to a tribunal or fail to correct a false statement of material fact or law previously made to the tribunal by the lawyer;**
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> (2) fail to disclose to the tribunal legal authority in the controlling jurisdiction known to the lawyer to be directly adverse to the position of the client and not disclosed by opposing counsel; or
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> (3) offer evidence that the lawyer knows to be false. If a lawyer, the lawyer's client, or a witness called by the lawyer, has offered material evidence and the lawyer comes to know of its falsity, the lawyer shall take reasonable remedial measures, including, if necessary, disclosure to the tribunal. A lawyer may refuse to offer evidence, other than the testimony of a defendant in a criminal matter, that the lawyer reasonably believes is false.

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

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

(d) In an ex parte proceeding, a lawyer shall inform the tribunal of all material facts known to the lawyer that will enable the tribunal to make an informed decision, whether or not the facts are adverse.

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Model Rule 1.6: Confidentiality of Information
Client-Lawyer Relationship

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

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

(1) to prevent reasonably certain death or substantial bodily harm;

(2) to prevent the client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's services;

(3) to prevent, mitigate or rectify substantial injury to the financial interests or property of another that is reasonably certain to result or has resulted from the client's commission of a crime or fraud in furtherance of which the client has used the lawyer's services;

(4) to secure legal advice about the lawyer's compliance with these Rules;

(5) to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client;

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

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

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

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Model Rule 1.7: Conflict of Interest: Current Clients
Client-Lawyer Relationship

(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.