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Representation Of Intraclient Conflicts Can Raise Thorny Ethics Issues

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A notable portion of California lawyers dedicate their practice to representing organizations. While the law commonly treats these organizations as unified entities or legal persons, they are comprised of multiple constituents with potentially conflicting interests, giving rise to intraclient conflicts that are less often encountered in individual representation. Resolving client identity and corresponding duties is a critical issue due to its substantial impact on conflicts of interest, confidentiality, and legal obligations.

The fundamental question for lawyers is defining their client: Is it solely the business organization as an entity, multiple constituents (e.g., shareholders or partners), one constituent to the exclusion of others, or a combination of these possibilities? Failure to discern this distinction can result in potential civil liability. A lawyer who incorrectly assumes someone is not a client and acts accordingly may face adverse consequences, including potential malpractice claims, disqualification, fee forfeiture, or disciplinary actions.

The courts have developed a body of law that provides substantial guidance, applying organizational and corporate law principles and ethical norms to lawyers dealing with intraclient conflicts. This body of law primarily addresses three categories of claims:

Breach of Duty: Lawyers may face allegations of professional misconduct or tort liability for facilitating or endorsing actions by certain constituents within an organization that allegedly harm others.

Privileged Communications: Constituents within an organization alleging managerial

misconduct may seek access to privileged communications between management and legal counsel.

Disqualification: Either the organization or one of its constituents may contend that a lawyer should be disqualified due to conflicts of interest.

Historically, California acknowledges a lawyer's duty to a presumed non-client when it is evident that the non-client was the intended beneficiary of the client's services, such as when the lawyer is retained by the client to draft a will or testamentary trust (*Biakanja v. Irving* (1958) 49 Cal. 2d 647, 650.) *Biakanja* and its progeny have outlined three sets of criteria for extending this duty in the context of organizations, either by implying an attorney-client relationship or utilizing a traditional third-party benefit analysis.

The first set of factors examines the extent to which the transaction between the lawyer and the client was intended to benefit the non-client plaintiff, foreseeability of harm, certainty of injury, the closeness of the connection between the lawyer's conduct and the non-client plaintiff's injury, and the alignment of this recognition of duty with the policy of preventing future harm.

The second set of factors assesses the potential interference with the lawyer's ethical duties to the client when imposing liability on the lawyer toward the non-client plaintiff.

The third set of factors evaluates whether recognizing a duty to the non-client plaintiff and the resulting liability for the lawyer would impose an undue burden on the legal profession. This could arise from conflicting duties to different sets of non-client beneficiaries or create open-ended liability that might discourage lawyers from practicing in that specific legal area (*Gordon v. Ervin Cohen & Jessup LLP* (2023) 88 Cal. App. 5th 543, 555-556 (internal citations omitted).)

In general, the courts have found it easier to support duties to constituents in the partnership than in the corporate context (*Responsible Citizens v. Superior Court* (1993) 16 Cal. App. 4th 1717, 1732; *Johnson v. Superior Court* (1995) 38 Cal. App. 4th 463, 479 (holding that under certain circumstances, a lawyer for a partnership owes fiduciary duties to the partners, whether or not that lawyer can be said to have an actual attorney-client relationship with them).) The *Johnson* holding suggests that an attorney-client relationship will be implied between the lawyer and the individual partners when the circumstances demonstrate that the partners are actually co-clients with the partnership entity. (*Id.*) This may reflect the doctrine that partners owe fiduciary duties to each other or the greater legal informality of partnerships.

While there exists a framework of analysis, courts have appeared willing but reluctant to extend the duty to a corporate shareholder notwithstanding compelling facts (*Skarbrevik v. Cohen, England & Whitfield* (1991) 231 Cal. App. 3d 692, 705-706 (lawyer for a corporation had no fiduciary duty to minority shareholders).) The *Skarbrevik* court heavily considered the presence of corporate formalities, as well as the arm's length relationship between the shareholders and the lawyer in declining to extend their duty to the minority shareholders. Yet, in cases where a lawyer formally represents a closely-held corporation and has close contact with the shareholders, a duty may extend to minority shareholders.

Consider a hypothetical scenario involving a closely-held corporation where the lawyer

maintains close communication with both the majority and minority shareholders, the corporation has disregarded corporate formalities, and the majority shareholders (the CEO and the board of directors) have taken actions to harm the interests of the minority shareholders. Does the lawyer have a fiduciary duty to disclose concealed or suppressed information about these actions to the minority shareholders?

In this hypothetical scenario, recognizing a duty for the lawyer to disclose concealed information to minority shareholders may be justified under the factors. The lawyer's close communication with both the majority and minority shareholders shows an intention to benefit all shareholders, while the concealed actions directly harm the minority shareholders' financial interests. Given the disregard for corporate formalities and the concealed actions, the harm to minority shareholders who depend on the lawyer's transparency and ethical guidance to protect their interests is foreseeable.

Recognizing a fiduciary duty for the lawyer to disclose concealed information aligns with the policy of preventing future harm. Lawyers uphold ethical standards, promote transparency, and protect the interests of all shareholders, which is in line with the broader policy of corporate integrity and protection of shareholder rights.

While the lawyer primarily owes a duty to the corporation, recognizing a duty to disclose information to minority shareholders aligns with the lawyer's role as an ethical lawyer responsible for protecting the interests of all shareholders.

Recognizing a fiduciary duty for the lawyer to disclose concealed information to minority shareholders, despite the ethical complexity, should not impose an undue burden on the legal profession. It underscores the lawyer's responsibility as an officer of the court and guardian of ethical standards, promoting transparency and protecting the rights of all shareholders.

Representing organizations, particularly closely held businesses, is as common as representing individuals for many lawyers. These lawyers must appreciate the ethical concerns presented by organizational representation. While there are well-established norms for representing traditional public corporations, the interests and identities of closely held businesses are often indistinguishable from those of their individual owners. Consequently, identifying the client or clients is more difficult and raises concerns that lawyers must consider.

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