

QUESTION 2

Linda is a lawyer with experience in representing small businesses, both for-profit and nonprofit. Nonprofit, Inc. (Nonprofit) is a newly formed California nonprofit corporation with few assets and limited income. Nonprofit is governed by a volunteer board of three directors, one of whom holds the position of board chair. Nonprofit's only employee is Ellen, who has no official title.

Ellen contacted Linda and said that Nonprofit would like to retain Linda to help it develop a formal employment agreement with Ellen, to make Ellen officially the Executive Director of Nonprofit. Ellen's position as Executive Director would be as an officer of the company, but not as a board member. Linda agreed to accept the matter. Linda did not memorialize her retainer agreement in writing.

Ellen drafted an employment agreement that included a proposed salary and sent the agreement to Linda. Ellen told Linda that her proposed salary was data-driven from a survey of similar positions, but based in the for-profit field. Ellen asked Linda not to tell the Board about the source of the survey data. Linda saw many other provisions in the draft agreement that were more favorable to Ellen than those in a typical employment agreement. Linda arranged a meeting with the Nonprofit board to discuss the terms of Ellen's employment agreement. The board chair asked Linda to invite Ellen to attend the board meeting and join their discussions.

1. With whom did Linda establish an attorney-client relationship and what ethical violations, if any, did Linda commit at the time the attorney-client relationship was created? Discuss.
2. What are Linda's ethical obligations with regard to:
 - a. Ellen's employment agreement? Discuss.
 - b. Ellen's request for confidentiality regarding the source of the survey data? Discuss.

Answer according to California and ABA authorities.

QUESTION 2: SELECTED ANSWER A

- 1. In order to have an effective attorney-client relationship, particularly when dealing with business associations, identification of the client is critical. The fact pattern is unclear as to the identity of the client. The potential clients are (1) Ellen individually, (2) Nonprofit, Inc., and (3) both.**

Based on the facts presented, it is likely that Linda was representing Nonprofit only. Ellen said "*Nonprofit* would like to *retain* Linda to help it develop a formal employment agreement with Ellen." At the same time, Linda has experience representing "small businesses," and it does not indicate that she has experience representing employees individually in negotiations with such businesses.

Importantly, a lawyer representing a corporation does not represent that corporation's employees, including senior officers and even if there is only one employee. The corporation is a distinct legal entity entitled to independent and zealous counsel. Therefore, on the facts presented, Nonprofit is probably the only client at the inception of the attorney-client relationship.

It does not matter that Ellen was the company's only employee, because there is no merger in such a situation—not even when the sole employee is also the sole shareholder. Here, it was a nonprofit, and therefore it is all the more clear that the attorney-client relationship was with Nonprofit only.

A very important (but missing) fact is Linda's fee. The client can often (but not always) be identified based on who is paying the fee. There is no reference to any fee arrangement. It thus appears that Linda is doing this work pro bono. The ABA does not require written fee agreements. If Linda was receiving a fee and more than \$1000, she might have violated the California rule requiring such agreements to be in writing if not for the fact that Nonprofit is a corporation, because that is an exception to the rule on written fee agreements (other, inapplicable exceptions include when the client in writing says it does not want a written fee agreement or there is a prior relationship and an exigent circumstance arises requiring prompt action by the lawyer to protect the client's interests). If Ellen paid the fee personally, however, that would materially alter the analysis and suggest either (1) an unethical dual representation of parties with an actual conflict without a waiver (which would have had to be obtained from members of the Nonprofit board since Ellen couldn't authorize that herself due to her own conflict), and also it would have required the fee agreement in writing as to Linda if over \$1,000, or (2) improper payment of legal expenses by a third party, without taking adequate precautions to ensure independent representation and preservation of confidentiality.

Despite the fact that the representation is for the company and, the absence of a written retainer agreement clearly identifying the client and the scope of representation is problematic. Indeed, it is clear that Ellen is receiving personal legal advice from Linda. Ellen also asked Linda to advance her personal interests and withhold information from the board. Although this

happened after the initial attorney-client relationship was formed, it could arguably have created a reasonable expectation by Ellen that Linda was her personal lawyer, too. To the extent that this rose to the level of creating an attorney-client relationship with Ellen individually, as noted above, that would be unethical. It is an improper dual representation of clients with actually conflicting interests in the absence of an effective disclosure and consent. The ABA rules apply a reasonable lawyer standard that prohibits representing actually conflicting clients unless the lawyer reasonably believes that it will not materially impair their ability to perform the required legal services competently and diligently. That conflict waiver must be confirmed in writing by both clients affected by the joint representation, after receiving complete disclosure of the risks from the lawyer. In California, there is no reasonable lawyer standard; the rule applies to both potential and actual conflicts; in case of conflicts between clients (as here), the disclosure must be in writing as well as the clients' consent to it; and in case of personal and professional conflicts, the disclosure must be in writing. Here, no such waiver occurred. Again, Ellen could not have authorized it herself on behalf of the corporation, even though she was the only employee, because she was conflicted. Consent to the dual representation could only have come from the board (since it's a nonprofit, there are no shareholders to potentially consent instead).

Moreover, Linda should have advised Ellen to retain independent counsel (though Ellen was free not to do so if she chose). From the fact that Ellen drafted an employment agreement, it is unclear whether Ellen herself was a lawyer but it certainly suggests that she did not believe she needed a lawyer of her own. Still, especially in this situation, Linda should have told Ellen this suggestion.

In conclusion, on the facts presented (though some important ones are missing), the client was Nonprofit only and Linda did not *clearly* violate any ethical rules at the point when the relationship was created. Based on Linda's subsequent discussions with Ellen, however, it seems clear that Ellen did not understand the scope of Linda's duties and may have believed Linda to be her personal attorney, and therefore under the circumstances, Linda should have disclosed the scope of representation more clearly and ideally had a written retainer agreement making that clear to Ellen.

2.a. **With respect to the employment agreement, Linda was obligated to zealously and competently represent Nonprofit's interests.**

The fact that Ellen drafted the employment agreement is not necessarily unethical in and of itself. A lawyer is entitled to rely on their employees and independent contractors to perform services subject to their supervision. A lawyer can also allow a client (or in this case, the employee of a client) to prepare documents so long as the lawyer exercises diligent and competent review and independent legal judgment in rendering advice. Here, because Ellen was on the other side of the transaction, it was essentially her opening offer to Nonprofit.

Upon receiving the draft from Ellen, Linda was required to review the document carefully and to attempt to revise and negotiate the terms to benefit Nonprofit. Because it was drafted by a nonlawyer (presumably), Linda was also required to review the draft to ensure compliance with all applicable laws. (The most significant issue presented in these facts is the salary, based on

the source of the info, and that is discussed in part b.)

When Linda recognized that the terms were unusually favorable to Ellen, she should have pushed back on those provisions and attempted to at least get them to conform to what is standard in the typical employment agreement.

At the minimum, if Linda did not seek to negotiate or revise the draft herself, Linda was right to call for a board meeting because she is obligated to tell the board about the provisions that she has recognized as too favorable to Ellen. A lawyer has the duty to communicate with the client, and where, as here, the only employee is in an adverse position, the board represents the interests of the corporation.

As a lawyer, Linda is not obligated to make business decisions for her client. The decision about the terms and how much ultimately to pay to Ellen is one for the board, not Linda.

Linda is also required to inform that board that it cannot have a privileged conversation with her about the employment agreement if Ellen is present. Accordingly, Linda should probably recommend that the board chair retract his invitation to Ellen, or at the very least ensure at the outset of the meeting that they all understand that there will be no privilege between them.

2.b. The duty to communicate includes the duty of candor and honesty to the client. Here, Linda could not honor Ellen's request for confidentiality because Nonprofit is her client, not Ellen. Linda is obligated to ensure that Nonprofit has all material facts relevant to the contract when deciding whether to agree to Ellen's requested salary.

Even if this were a dual representation situation, where Linda represented both Ellen and Nonprofit, she would have a duty to disclose this fact to Nonprofit's board because the fact is material to the representation. It is one of the reasons why disclosures in such situations are so critical, because it puts the duty to protect confidentiality in tension with the duty to communicate, and in a joint representation, that means disclosing all facts material to the representation.

Linda should have told Ellen that she could not honor her request.

Linda would not have to tell the board that Ellen violated her duty of loyalty to Nonprofit, however, because the duty of loyalty is not implicated when negotiating employment agreements. That said, Linda should tell the Board that Ellen asked her to keep the information secret, as that is important for the board to know when making the decision about whether to expand Ellen's current untitled role.

QUESTION 2: SELECTED ANSWER B

1. **With whom did Linda establish an attorney-client relationship, and what ethical violations did Linda commit at the time the Attorney-client relationship was created**

Attorney Client Relationship

Organizational Client

When a lawyer is hired to represent a corporation or organization, the lawyer's fiduciary duties are to the organization and not to the individual members, directors, or officers. A lawyer has a duty to act on the best interests of the organization and can, therefore, not engage in conduct which would benefit any individual or group of individuals at the expense of the organization.

Here, Linda was contacted by Ellen, who said that Nonprofit would like to hire her. Linda was further told that this was for the purpose of creating a formal employment agreement with Ellen, to make her the Executive Director of the Nonprofit. Therefore, Linda was hired by Nonprofit and as such, owed fiduciary duties to Nonprofit and not to Ellen.

Linda's Ethical Violations

Fee Agreement

Under ABA, a lawyer who agrees to represent a client must not put the agreement in writing, unless it is for contingency fees. However, California Rules of Professional Conduct, mandate that lawyers must put the agreement in writing if it is over \$1000. However, when the client is an organization, or a repeat client (or if there is an emergency) a lawyer does not have to write up the agreement.

Here, since Linda is representing Nonprofit, which is an organization, Linda did not violate the ABA or CA rules by failing to put the retainer agreement in writing for the purpose of the fees.

Duty of Loyalty

A lawyer owes her client a duty of loyalty, which includes the duty to avoid a conflict of interest. A conflict can arise where the lawyer knows that her client's interest will be materially adverse to that of the lawyer's own interest, or another client. When such a conflict arises, a Lawyer might still be allowed to represent the clients so long as there is no claim by one client against the other, such representation is not prohibited by law, and the lawyer's lawyer gets the informed written consent of both clients. California also allows a lawyer who has a potential conflict of interest to continue to represent the clients so long as there is informed written consent.

Here, Linda is not officially representing Ellen. However, the fact that Ellen is the one who

reached out to Linda, and the fact that the representation was for the purposes of drafting up an employment agreement between Nonprofit and Ellen, suggests that Linda was at least informally also representing Ellen. This would create a concurrent conflict of interest. As such, Linda should have sought the informed written consent of the board of Nonprofit, before she agreed to represent t Nonprofit in the manner Ellen asked. There are no facts to suggest that Linda did this and therefore, she was likely in violation of her duty of loyalty to Nonprofit.

Duty of Diligence

Under both ABA and CA, a lawyer has to promptly, adequately and zealously represent her client.

Here, Linda failed to adequately represent her client, Nonprofit, when she failed to inform Nonprofit of the potential conflict of interest that could arise. Given the fact that Linda had experience in representing businesses, both nonprofit as well as for profit, further gives rise to the fact that she should have sought t the written consent of Nonprofit before agreeing to representing them in the matter regarding Ellen's employment agreement.

At this point, Linda should have informed both Ellen, as well as the Board of Nonprofit, that this might give rise to some conflict of interest issues as she was retained by Ellen, but to work on Nonprofit's behalf in forming a formal agreement with Ellen.

2.a. Linda's ethical obligations with regard to the Employment agreement

Duty to Report (loyalty)

When a lawyer represents an organization, and learns of conduct made by an individual in the corporation which materially harms the organization in terms of financial harm or even reputation harm, the lawyer has a duty to report up. Under ABA, the lawyer has to first report the individual's conduct up to a higher authority in the company, such as the board of directors. If the board does not do anything to remedy the harm, the lawyer has to report to a relevant authority outside of the corporation. CA rules differ slightly. Under CRPC a lawyer has the duty to first report up the chain to the board of directors ,for example. If the board fails to act, the lawyer may not report out but rather should seek withdrawal.

Here, the employment agreement which Ellen prepared would clearly cause financial harm to the nonprofit because it would pay Ellen based on the appropriate payment for a for-profit company. Linda's client, will therefore be forced to pay more than they should for Ellen's job. Linda should immediately report this to the board of directors. Although Linda did set a meeting with the board to discuss Ellen's financial compensation. she should refuse to allow Ellen to attend so that she could discuss the fact that the employment agreement contained a number of provisions that were more favorable to Ellen than those in typical employment agreements.

Duty to Communicate

Under both ABA and CA rules, a lawyer has a duty to communicate important material matters regarding the representation to her client.

Here, Linda has a duty to tell the board about the fact that Ellen drafted up the employment agreement herself. Furthermore Linda must tell the board that there are provisions in the agreements that are more favorable to Ellen than usual. These are all things that are material to Linda's representation because she is representing Nonprofit for the purpose of drafting up the employment agreement.

Linda's failure to promptly notify the board as to these matters will surely result in her committing an ethical violation.

Duty of Competence/ Diligence

(See rules above)

Under ABA, a lawyer must be competent, in terms of skill, knowledge and experience to represent her client. Under California rules, a lawyer may not intentionally, recklessly represent a client. California punishes repeated acts of incompetence in representing clients.

Here, although Linda seems to have plenty of experience representing businesses, she seems to have failed to.

(See rule above)

In addition to the rule above, a lawyer owes her client the absolute duty to act in the clients' best interest. A lawyer may not benefit herself or anyone else at the expense of her client

Here, Linda is allowing Ellen to draft up the agreement. She should not allow Ellen to do this as this would constitute a violation of her duty of competence and diligence because 3

2.b. Ellen's request for confidentiality regarding the source of the survey data

Duty to Report (loyalty)

When a lawyer represents an organization, and learns of conduct made by an individual in the corporation which materially harms the organization in terms of financial harm or even reputation harm, the lawyer has a duty to report up. Under ABA, the lawyer has to first report the individuals' conduct up to a higher authority in the company, such as the board of directors. If the board does not do anything to remedy the harm, the lawyer has to report to a relevant authority outside of the corporation. CA rules differ slightly. Under CRPC, a lawyer has the duty to first report up the chain, to the board of directors for example. If the board fails to act, the lawyer may not report out but rather should seek withdrawal.

Here, Linda should certainly not keep the source of the data confidential from her own client. As discussed above, she is representing the Nonprofit and, as such, owes it her duties of loyalty. Linda should immediately report the source of the data to the board. If, for some reason, the board decided not to do anything with the information, then under ABA, Linda would have to report this to a relevant agency, such as the Secretary of the State in this case. Although the nonprofit might not have shareholders, it is a 501c3 corporation which is in essence not paying taxes precisely because of its nonprofit nature. Ellen, is seeking to have the nonprofit pay her the salary that she would have earned had it been a for profit. This would potentially be a violation of the nonprofit's tax obligations and could devastate the nonprofit if caught doing it (not to mention the harm it causes on the taxpayers as a whole). Therefore, Under ABA authorities, Linda should have reported this first to the board, and if it failed to act, to the Secretary of State. Under CA authorities, however, Linda would not be allowed to go the extra step of reporting outside of the organization if the board fails to act. She should then seek to withdraw from representing the nonprofit.

Duty to Communicate/Duty of Diligence

Under both ABA and CA rules, a lawyer has a duty to communicate important material matters regarding the representation to her client.

Here, again, Linda should communicate the source of Ellen's survey data to the board. Failing to do so will result in her being in violation of her duty to communicate as well as loyalty and diligence.