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In House Counsel's Duty to Give "Miranda" Warnings to Corporate Officers and Employees



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This article discusses in-house counsel's ethical obligations in dealing with corporate officers and employees whose interests may be at odds with the corporation's. The discussion will focus on the attorney's obligations under the ABA's Model Rules of Professional Conduct, which have been adopted in a majority of states.¹ The following scenarios, based loosely on real cases, illustrate the types of problems that counsel can encounter.

Case No. 1: Payoffs in Penang: internal corporate investigation.

You are the Assistant General Counsel for Regulatory Matters of Breakrock Industries, Inc., a publicly traded manufacturer of construction equipment. Your boss has asked you to look into a rumor that someone in the International Sales Division has been paying bribes to officials in Malaysia to encourage sales of Breakrock's earth movers. You begin your investigation by meeting the assistant controller for the International Division. He says, "This is all confidential, right?" What should you say?

Case No. 2: Cantankerous CEO: claim against corporation and its officer.

You are Vice-President for Employment Law at Good Samaritan Industries, Inc., which owns and operates health care facilities in several states. Recently, the CEO of Good Samaritan, against your

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advice, fired a Senior Vice President and terminated his salary and benefits. The firing led to a loud and acrimonious argument between the CEO and the Senior V.P. as the Senior V.P. was being led out of the building. A few weeks later, the CEO calls you into her office and shows you a letter from the Senior V.P.'s attorney asserting claims against both Good Samaritan and the CEO individually and demanding a response in ten days. The CEO says, "You'll handle this, right?" What should you do?

Case No. 3: Nettlesome Nepotism: advice to corporate officer with a personal stake.

You are the Assistant General Counsel for Business Affairs of Ye Olde Shoppes, Ltd., a regional chain of convenience stores owned by the second generation of the extended MacGuffin family. Ye Olde Shoppes is about to merge with Future Mart, a fast-growing national chain. You have been assigned to complete the necessary due diligence for the representations and warranties that Ye Olde Shoppes has agreed to make. You meet with your friend Seth MacGuffin, Vice President for Operations of Ye Olde Shoppes, nephew of the founder, and an 8% shareholder, to review the representations and warranties. Seth says, "This is a good deal for me, right?" In fact, you know from discussions with your counterpart at Future Mart that Future Mart management regards Ye Olde Shoppes' operations as backward and sleepy and plans to shake them up, but the President of Ye Olde Shoppes has instructed you to keep these discussions quiet. How should you respond?

Discussion:

In the three scenarios described above, as in many other cases, analysis of the lawyer's ethical obligations starts with the question, Who is the lawyer's client? It is now axiomatic that the lawyer for a corporation represents the corporation, not its officers, employees, or shareholders. This principle, sometimes referred to as the "entity theory" of representation, is enshrined in Rule 1.13(a) of the ABA's Model Rules of Professional Conduct, which has been adopted in 42 states:²

"A lawyer retained by an organization represents the organization acting through its duly authorized constituents."³

"Constituents" in this context means the corporation's officers, directors, employees and shareholders.⁴ Even in states which have not adopted the Model Rules, the entity theory has been adopted by rule or court decision.⁵

Although the in-house lawyer's client is the corporation, the corporate officers and employees the lawyer deals with every day are something more than the "third parties" of legal lore. As duly authorized agents

of the corporation, they speak for the corporation and direct its affairs. They may also determine the in-house lawyer's salary and prospects for promotion. On a more personal level, in-house counsel will often develop informal working relations with the corporation's "constituents", share jokes around the coffee machine, exchange personal information, and develop close friendships. As Professor Geoffrey Hazard put it, the corporate lawyer never deals with "the client as such" but only with "client people."⁶ Thus the role and the loyalties of in-house counsel are clear in concept but potentially ambiguous in human terms.

Notwithstanding these potential ambiguities, it is usually clear whom the corporate lawyer represents and where the lawyer's loyalties should lie. For example, if a department manager consults corporate counsel about personnel issues within her department, the context usually makes it clear that the manager is seeking advice on behalf of the corporation.⁷ Likewise, when a colleague approaches in-house counsel with a legal question that is wholly outside the colleague's role as employee - say, his liability as a Little League coach - counsel's loyalty to the corporation is not at issue.

The situation becomes more complicated, however, when a corporate employee with whom the attorney is dealing has interests that may be in conflict with those of the corporation. Rule 1.13(d) of the ABA's Model Rules provides guidance in such situations. In the form in force in most states, that rule provides:

In dealing with an organization's directors, officers, employees, members, shareholders or other constituents, a lawyer shall explain the identity of the client when it is apparent that the organization's interests are adverse to those of the constituents with whom the lawyer is dealing.⁸

This formulation provokes a question: *To whom should the conflict be apparent?* In 2002, the ABA answered the question by deleting "it is apparent" and substituting "the lawyer knows or reasonably should know."⁹ The new terminology indicates that the adversity of interests must be apparent to a lawyer of reasonable prudence and competence.¹⁰ While the states have not yet adopted the new formulation, courts and disciplinary authorities are as a practical matter likely to apply a reasonably prudent lawyer test.¹¹

On its face, Rule 1.13(d) uses the phrase "shall explain" and thus appears to require the attorney to remind the corporate employee that the attorney represents the corporation in every case where there is an adversity of interests. The Comment to Rule 1.13 goes further, suggesting that the lawyer should advise the constituent "that such person may wish to obtain independent representation" and that "discussions between the lawyer for the organization and the

individual may not be privileged."¹² The Comment muddies these clear waters, however, by adding a Delphic qualification: "Whether such a warning should be given by the lawyer for the organization to any constituent individual may turn on the facts of each case."¹³

Corporate counsel may find additional guidance in Model Rule 4.3, "Dealing with Unrepresented Persons." In the form originally promulgated by the ABA, Rule 4.3 provides:

In dealing on behalf of a client with a person who is not represented by counsel, a lawyer shall not state or imply that the lawyer is disinterested. When the lawyer knows or reasonably should know that the unrepresented person misunderstands the lawyer's role in the matter, the lawyer shall make reasonable efforts to correct the misunderstanding.¹⁴

This formulation did not include a prohibition on giving legal advice to an unrepresented person, a ban that formerly appeared in DR 7-104(A)(2) of the ABA's Model Code of Professional Responsibility.¹⁵ When the Model Rules replaced the Model Code in 1983, the ban on giving legal advice to unrepresented persons was moved from the text of the Rule to the Comment, suggesting that it was merely a "guide for interpretation," not part of a lawyer's ethical obligations.¹⁶ However, eleven of the states that adopted the Model Rules added a prohibition similar to DR 7-104(A)(2) to their versions of Rule 4.3,¹⁷ and a least one state court determined that the relegation of the ban to the Comment was a change in form only, not a change in substance.¹⁸ The 2002 amendments to the Model Rules restored the ban to the text of the Rule by adding the following sentence:

The lawyer shall not give legal advice to an unrepresented person, other than the advice to secure counsel, if the lawyer knows or reasonably should know that the interests of such a person are or have a reasonable possibility of being in conflict with the interests of the [lawyer's] client.

Read together, Rules 4.3 and 1.13(d) stand for the proposition that when a lawyer, acting on behalf of a client, deals with an unrepresented person, the burden is on the lawyer to clear up any misunderstandings about whom the lawyer represents and where the lawyer's loyalties lie. In the corporate context, Rule 1.13(d) obliges in-house counsel to clarify his loyalties whenever he is dealing with an officer, employee, or other constituent whose interests are adverse to the corporation's. Whenever counsel knows or reasonably should know of such adversity, he must at a minimum remind the officer or employee that he represents the corporation. In addition, to avoid misunderstanding about counsel's role, it will in many cases be prudent for counsel to suggest that the individual obtain independent representation and to make it clear that the individual may not claim

the protections of the attorney-client privilege for communications with counsel.

The warnings required by Rules 1.13(d) and 4.3 should not prevent in-house counsel from doing his or her job. The Comment to Rule 4.3 indicates that a lawyer may, for example, negotiate the terms of a transaction or settle a dispute with an unrepresented person, but again, only if the lawyer has first made it clear that he represents an adverse party and cannot be relied on for disinterested legal advice.¹⁹

The consequences of failure to provide the required warnings can be severe. The lawyer may be subject to professional discipline.²⁰ Moreover, under the law in many states, an attorney-client relationship can result if the corporate officer or employee reasonably relies on the lawyer to protect his interests, and the lawyer knew or should have known of the reliance but did nothing to discourage it.²¹ Thus, the in-house counsel who fails to give the required warnings may find himself with an unanticipated and unwanted attorney-client relationship with a corporate officer or employee.²² That inadvertent client relationship may in turn lead to the lawyer's disqualification in any subsequent legal proceedings involving the officer or employee,²³ and perhaps even the disqualification of the entire corporate law department.²⁴ In the worst case, failure to give the required warnings may also lead to a malpractice action by the officer or employee against the in-house counsel.²⁵

With these general principles in mind, let's return to the three scenarios described at the beginning of the article.

Case No. 1: Payoffs in Penang.²⁶

Even before the interview begins, it is apparent that the interests of the Assistant Controller may be adverse to the interests of Breakrock Technologies. If the employee participated in paying bribes, he may lose his job. He may also be subject to criminal penalties under the Foreign Corrupt Practices Act.²⁷ Thus, under Rule 1.13(d), you must "explain the identity of the client," that is, make it clear that you are the lawyer for Breakrock Technologies, not the Assistant Controller.

The Assistant Controller has also raised a question about confidentiality, so you should address the issue of privilege, as suggested by Rule 1.13(d), Comment [7]. The interview may, however, be privileged under *Upjohn v. United States*,²⁸ so you need to make it clear that the privilege belongs to the corporation, not to the Assistant Controller. You should tell the employee that the information will be held in confidence and will be disclosed only to senior management for purposes of insuring that Breakrock complies with the law. You should also, however, make it clear that Breakrock may ultimately decide that the information should be disclosed to

government enforcement agencies or others outside the corporation.

You may be tempted to postpone these disclosures until you learn whether the Assistant Controller was actively involved in the bribery, but you should resist that temptation. A uniform set of disclosures, prepared in advance and made to each employee at the beginning of the interview, will avoid misunderstandings and the creation of inadvertent attorney-client relationships. Uniform disclosures will also make it easier to establish that the interview is protected by the corporation's attorney-client and work product privileges.²⁹

Should you also suggest that the Assistant Controller retain his own attorney? Comment [7] to Rule 1.13(d) recommends this additional step, but there are practical considerations suggesting that you may want to postpone this warning. If you begin the interview by telling the Assistant Controller that he should consider retaining his own counsel, he may want to postpone the interview while he looks for an attorney. In some circumstances, the corporation may be required to indemnify the employee for any legal expenses he incurs. That delay and additional expense may be unnecessary if the Assistant Controller had no personal involvement in the payment of bribes. Thus you may want to postpone discussion of separate counsel until you are in a better position to judge whether the employee was culpably involved in illegal conduct.³⁰

Case No. 2: Cantankerous CEO.³¹

The lawyer for the Senior Vice President has asserted claims against Good Samaritan and against the CEO individually. The CEO obviously expects you to take care of all the claims, not just the claims against the corporation. However, since you advised the CEO not to fire the Senior Vice President, and since the CEO compounded the problem by getting in an argument with the Senior Vice President in the hall, the interests of the corporation may well be in conflict with the interests of the CEO.

The demand letter requires a prompt response, so there is a temptation to get to work and worry about the formalities later. If, however, you proceed without immediately clarifying whom you represent, there is an excellent chance that a court will later conclude that you had an attorney-client relationship with the CEO. If the interests of the CEO do turn out to be adverse to the corporation's, you may be disqualified from representing Good Samaritan.³²

Model Rule 1.13(e) permits you to represent both the corporation and a corporate officer, subject to the provisions of Rule 1.7 concerning conflicts of interests. Since the interests of Good Samaritan and the CEO may well be adverse, Rule 1.7 requires, at a minimum, that the corporation consent to the dual representation. Under Rule 1.13(e),

that consent must come from "an appropriate official" other than the CEO-in this case that may mean getting the consent of the Board of Directors or Executive Committee. Moreover, if the conflict is sufficiently severe, dual representation may be impermissible even with consent.³³

Given this thicket of ethical problems and a looming deadline, your best course is to remind the CEO, as tactfully as possible, that you represent the corporation and urge her to retain her own attorney. Since you have to regularly deal with the CEO on other matters, it would also be prudent to retain a different outside attorney to respond to the Senior Vice President's claims on behalf of the corporation.

Case No. 3: Nettlesome Nepotism.³⁴

Your friend Seth MacGuffin has asked what is, from his perspective, the \$64 question, but you can't answer it. It appears likely that the merger will lead to major changes in Seth's department, perhaps even the loss of his job, so his interests are potentially adverse to the corporation's. You may not give legal advice to a person whose interests are adverse to the interests of your client, the corporation. Moreover, the information you have learned about the impending reorganization is "information relating to the representation of the client" within the meaning of Model Rule 1.6.³⁵ You may not disclose this information without client consent-and the President has told you to keep it under your hat.

Moreover, if you try to answer Seth's question, you are at great risk of acquiring an inadvertent client. Since you are a friend of Seth's and Ye Olde Shoppes is family owned, you have probably discussed his stock ownership and employment on other occasions. You may have even helped him with his taxes or estate plan. If Seth is fired after the merger, he could dredge up these past dealings to show that it was reasonable for him to rely on you for legal advice.

Accordingly, you should not try to answer Seth's question. Instead, you should remind Seth that you are interviewing him in your capacity as counsel for Ye Olde Shoppes as part of the corporation's due diligence. A checklist of questions, prepared in advance, may help to keep the meeting focused. If Seth persists in his question, you may want to refer him to others who are authorized to speak for the corporation-perhaps to the President who told you to keep quiet in the first place.

Conclusion:

The scenarios discussed above illustrate a fact of life for in-house counsel: In performing his or her duties for the corporation, counsel must sometimes deal with officers and employees whose personal interests may be in conflict with the interests of the corporation.

Whenever that occurs, the Model Rules require the lawyer to make it clear that the lawyer represents the corporation, not the officer or employee. The Model Rules also recommend the lawyer give more specific warnings, including advice to retain independent counsel and clarification of the lawyer's duty of confidentiality. These "Miranda" warnings ensure that the officer or employee is not unfairly lulled into relying on the corporation's lawyer for legal advice. Equally important, they also protect the corporation's interests by ensuring that the lawyer does not inadvertently acquire another client, thereby undermining the lawyer's duties of loyalty and confidentiality to the corporation.

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Footnotes

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1. The ABA extensively amended the Model Rules in 2002. Those amendments have not yet been adopted by most states. Model Rules 1.13(a) and 1.13(e) cited in the article were not affected by the 2002 amendments. Amendments to Rules 1.13(d) and 4.3 are described in more detail in the "Discussion" section of article. In the author's judgment, the amendments to these two sections clarify but do not change the substance of the corporate lawyer's obligations.

2. ABA/BNA Lawyers' Manual on Professional Conduct, State Ethics Rules (ALI/BNA) (March 26, 2003).

3. See also RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS, Â§96(1) (2000) [hereinafter RESTATEMENT].

4. ABA MODEL RULES OF PROFESSIONAL CONDUCT, R. 1.13 cmt. 1 (1983) (amended 2002) [hereinafter MODEL RULES].

5. See, e.g., CALIF. RULES OF PROFESSIONAL CONDUCT, R. 3-600; Meehan v. Hopps, 301 P.2d 10 (Cal. Dist. Ct. App. 1956); Thompson U.S., Inc. v. Gosnell, 582 N.Y.S.2d 3, 6 (N.Y. App. Div. 1992); N.Y. CODE OF PROFESSIONAL RESPONSIBILITY, DR 5-108.

6. G. Hazard, Ethical Dilemmas of Corporate Counsel, 46 Emory L.J. 1011, 1013 (1997).

7. See, e.g., *Cole v. Ruidoso Mun. Sch.*, 43 F.3d 1373 (10th Cir. 1994).
8. ABA MODEL RULES OF PROFESSIONAL CONDUCT 1.13(d)(1983) [hereinafter OLD MODEL RULES].
9. MODEL RULES supra n.4 at 1.13(d).
10. See the definition of "reasonably should know" in MODEL RULES supra n.4 at 1.0(j).
11. For example, in *Professional Services Industries, Inc. v. Kimbrell*, 758 F. Supp. 676, 683-4 (D.Kan. 1991), the court characterized the "it is apparent" standard as a subjective test, but then observed in a footnote, "[t]he court in evaluating the credibility of testimony and evidence on this matter obviously considers its reasonableness." *Id.* at n.5.
12. MODEL RULES supra n.4 at 1.13, cmt. 7.
13. *Id.* at cmt. 8.
14. OLD MODEL RULES supra n.8 at 4.3.
15. ABA MODEL CODE OF PROFESSIONAL RESPONSIBILITY, DR 7-104(A)(2) (1980).
16. The Preamble and Scope to the Model Rules provides, "[t]he Comments are intended as guides to interpretation, but the text of each Rule is authoritative." The Scope also provides, "[c]omments do not add obligations to the Rules but provide guidance for practicing in compliance with the Rules."
17. ABA Center for Professional Responsibility, Ethics 2000 Commission Report, Model Rule 4.3 Reporter's Explanation of Changes (October 28, 2003).
18. *Attorney Q v. Mississippi State Bar*, 587 So.2d 228, 232-33 (Miss. 1991).
19. MODEL RULES supra n.4 at 4.3, cmt. 2.
20. See, e.g., *Attorney Q*, 587 So.2d 228 (plaintiff's attorney disciplined for telling an unrepresented defendant to do nothing and not to worry).
21. RESTATEMENT Â§ 14(1)(b) & cmt. f.
22. *Id.* Â§ 103, cmt. e.
23. *Home Care Industries, Inc. v. Murray*, 154 F.Supp.2d 861 (N.J. 2001)(disqualification required); *Schiffli Embroidery Workers Pension Fund*, 1994 U.S. Dist. LEXIS 2154 (D.N.J. 1994)(disqualification required); compare, *Doe v. Poe*, 595 N.Y.S.2d 503 (N.Y. App.Div. 1993)(no attorney-client relationship when the attorneys told the corporate officer that they represented the corporation).
24. To date, there are no reported cases disqualifying an entire law department. A law department, however, is a "firm" within the meaning of the Model Rules. MODEL RULES 1.0(c). Under Model Rule 1.10(a), none of the lawyers in a firm may represent a client when any one of them would be prohibited from doing so by Rule 1.7 (conflict involving current client) or Rule 1.9 (conflict involving former client).
25. See *Perez v. Kirk & Carrigan*, 822 S.W.2d 261 (Tex.Civ.App. 1991)(malpractice suit by employee-driver against corporate lawyer who took driver's statement about

an accident, then turned it over to the district attorney); see also Robertson v. Gaston Snow & Ely Bartlett, 404 Mass. 515 (1989)(in malpractice suit by officer/shareholder against attorney for corporation, judgment for attorney affirmed, but only after two trials and an appeal).

26. This case is based on Upjohn Co. v. United States, 449 U.S. 383 (1981).

27. 15 U.S.C. Â§78dd-3(e)(2).

28. 449 U.S. 383 (1981).

29. For a form of pre-interview notification that can be adapted by in-house counsel, see J. Villa, 2 Corp. Counsel Guidelines, App. 5-5 (2002 ed.).

30. For a discussion of the factors to consider, see G. Wallace, Internal Investigation of Suspected Wrongdoing by Corporate Employees, 1057 PLI/Corp. 515, 519-520 (1998).

31. This case is based on Home Care Industries, Inc. v. Murray, 154 F.Supp.2d 861.

32. In Home Care Industries, Inc, 154 F.Supp.2d 861, the court disqualified the corporation's lawyer.

33. In the form adopted by most states, Rule 1.7 prohibits dual representation unless the lawyer reasonably believes that the representations will not be adversely affected. OLD MODEL RULES supra n.8 at 1.7(a)(1) & (b)(1). The 2002 amendments to the Model Rules reorganized Rule 1.7 and changed some of the terminology, but the result is the same. See MODEL RULES supra n.4 at 1.7(b)(1). If, for example, the CEO had fired the Senior Vice President in violation of an express contractual commitment or a board resolution, dual representation would probably be impermissible even with consent.

34. This case is based on Robertson v. Gaston Snow & Ely Bartlett, 404 Mass. 515.

35. In the form now in force in most states Model Rule 1.6(a) provides, "[a] lawyer shall not reveal information relating to the representation of a client unless the client consents after consultation, except for disclosures impliedly authorized in order to carry out the representation..." OLD MODEL RULES supra n.8 at 1.6(a). The confidentiality rule applies "to all information relating to the representation, whatever its source." Id. at 1.6, cmt. 5.



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