Section 876 (of Torts, Not the Tax Code) & Why It's Important to Business Lawyers

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On March 6, the Oregon Supreme Court heard oral arguments in *Reynolds v. Schrock*, 197 Or App 564, 107 P3d 52, *rev allowed*, 339 Or 475 (2005), a major lawyer liability case for anyone who advises fiduciaries—whether they are in formal roles such as trustees or informal ones such as joint venture partners. In *Reynolds*, the Court of Appeals held that a lawyer could be liable for assisting in a client's breach of fiduciary duty by giving the client legal advice on evading a fiduciary duty and then helping the client implement that advice. In doing so, the Court of Appeals relied on *Granewich v. Harding*, 329 Or 47, 985 P2d 788 (1999), where the Supreme Court upheld the more general proposition that a lawyer could be held liable for assisting a client in breaching a fiduciary duty to a third party. *Granewich*, in turn, drew on Section 876 of the Restatement (Second) of Torts (1979), which deals with tortiously acting in concert with another resulting in injury to a third person.

Because lawyers often advise and assist fiduciaries of one stripe or another, Section 876 and the decisions applying it create significant risk of civil liability to Oregon lawyers.[1] In this column, we'll look at those risks and what lawyers can do to lessen them.

Section 876

Section 876 isn't aimed at lawyers. Rather, it sets out three broad categories where someone acting in concert with another can be liable for resulting harm to a third person:

"For harm resulting to a third person from the tortious conduct of another, one is subject to liability if he

(a) does a tortious act in concert with the other or pursuant to a common design with him, or

(b) knows that the other's conduct constitutes a breach of duty and gives substantial assistance or encouragement to the other so to conduct himself, or

(c) gives substantial assistance to the other in accomplishing a tortious result and his own conduct, separately considered, constitutes a breach of duty to the third person."

The Supreme Court in *Granewich* found that prior Oregon case law recognized each element of Section 876 and noted that "to state that this court recognizes section 876 as reflecting the common law of Oregon breaks no new ground."[2] The Supreme Court went on to "conclude that persons acting in concert may be liable jointly for one another's torts under any one of the three theories identified in *Restatement* section 876."[3]

Depending on the circumstances, subsections (a) and (c) can create risks for lawyers. But, subsection (b) poses the greatest practical risk to lawyers because it creates liability to a *nonclient* for advice and other legal work performed for a *client*. *Granewich* and *Reynolds* illustrate the potential sweep of subsection (b).

Granewich

Granewich involved a "minority squeeze out." Granewich and two business associates, Harding and Alexander-Hergert, formed a closely held financial corporation in 1992. All three were directors, officers and employees of the company and each owned one-third of its shares. About a year later, Harding and Alexander-Hergert had a falling out with Granewich and began planning to remove him from the company. At that point, they hired a law firm to represent the company. The complaint alleged, however, that the law firm soon exceeded this neutral role as corporate counsel and began to advise and assist Harding and Alexander-Hergert individually in their efforts to oust Granewich by amending the company's bylaws and calling special meetings that resulted in Granewich's removal.

After he was forced out, Granewich sued his fellow owners, the corporation and the lawyers. The two other owners and the corporation settled, leaving only the lawyers. The charge against them was that they allegedly assisted in the two majority owner-directors in breaching *their* fiduciary duties to Granewich. The trial court dismissed on the pleadings and the Court of Appeals affirmed, holding that if the lawyers had no direct fiduciary duty to Granewich they could not be vicariously liable for the majority owner-directors' asserted breach. The Supreme Court reversed.

Relying on Section 876, the Supreme Court found that the complaint stated a claim against the lawyers:

> "There is no Oregon law directly addressing whether someone can be held liable for another's breach of fiduciary duty. Legal authorities, however, virtually are unanimous in expressing the proposition that one who knowingly aids another in the breach of a fiduciary duty is liable to the one harmed thereby. **That principle readily extends to lawyers**."
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> 329 Or at 57 (emphasis added; footnotes omitted).

Reynolds

Reynolds was painted against the backdrop of a real estate joint venture. Reynolds and Schrock purchased two parcels—one was commercial timber and the other was recreational. They had a falling-out and later entered into a settlement agreement to wind-up the joint venture. Under the settlement, Reynolds conveyed his interest in the recreational parcel to Schrock and, in return, Reynolds was to receive all proceeds from the sale of the timber. Reynolds had invested $500,000 in the joint venture by that point. To make Reynolds whole, the settlement provided that if the timber sale did not net him at least $500,000, Schrock would pay Reynolds any deficiency and Reynolds would have a lien on the recreational parcel to secure the deficiency.

After Reynolds had deeded his interest in the recreational parcel to Schrock, Schrock asked her lawyer if the settlement agreement required her to keep the recreational property pending the timber sale. Schrock's lawyer concluded that the settlement agreement contained no such obligation and advised Schrock accordingly. Schrock then sold the recreational parcel with the lawyer's assistance. Schrock later prevented the timber sale—leaving Reynolds

without either his interest in the recreational property or his share of the timber sale proceeds.

Reynolds sued Schrock. Reynolds framed the primary claim against Schrock as breach of fiduciary duty. He argued that Schrock had a fiduciary duty to wind-up the joint venture as contemplated by the settlement agreement and that her failure to do so—notwithstanding the apparent loop-hole in the settlement agreement allowing the sale of recreational property—constituted a breach of that duty. Reynolds also sued Schrock's lawyer. Reynolds did not contend that Schrock's lawyer had an independent fiduciary duty to him. Rather, he argued that the lawyer was jointly liable with Schrock for the breach of Schrock's fiduciary duty to Reynolds by providing the advice and assistance in implementing that advice to Schrock. Schrock settled with Reynolds. Her lawyer moved for summary judgment, which the trial court granted. The Court of Appeals reversed.

Relying principally on Section 876 and *Granewich*, the Court of Appeals concluded that a lawyer advising a client to act contrary to a fiduciary duty may be liable to a nonclient to whom that duty is owed *even if* the act would otherwise be permitted by an associated contract: "[I]f the attorney knows that the fiduciary relationship imposes a higher standard of conduct than the agreement, then the attorney who advises the client that he or she may do an act that the contract permits but that is incompatible with the fiduciary relationship may be liable for the breach of fiduciary duty."[4]

Lessening Risks

Granewich and *Reynolds* each suggest ways to lessen the risk of liability flowing from Section 876.

The law firm in *Granewich* initially agreed to represent the corporation only. The plaintiff asserted that the law firm expanded this role to advise the majority owner-directors, too. In situations like *Granewich*, if a law firm confines its role to corporate counsel only it will lessen the risk of being accused later of having "taken sides" and, in doing so, assisting one camp in an internal corporate dispute in breaching fiduciary duties to the other.

Reynolds stressed that simply outlining a range of options for a client and the consequences of those options would *not* reach Section 876. Instead, the lawyer would need to affirmatively and knowingly act to further the client's breach of fiduciary duty.[5] If put in that situation, both *Reynolds* and OSB Formal Ethics Opinion 2005-119, which addresses fiduciary representation, counsel that a lawyer should be permitted to withdraw if the client cannot be dissuaded from breaching a fiduciary duty.

Summing Up

The Court of Appeals in *Reynolds* acknowledged that its decision had "serious implications for attorneys" and cautioned that it should be narrowly construed. The Supreme Court will shape the final parameters of *Reynolds*. But, even the Supreme Court's own *Granewich* decision creates the specter of liability if lawyers who advise fiduciaries don't carefully tailor both the scope of their representation and the content of their advice.

[1] Oregon lawyers are not alone. For a discussion of this facet of lawyer civil liability from a national perspective, see Ronald E. Mallen & Jeffrey M. Smith, 1 Legal Malpractice § 6.6 (2006).
[2] 329 Or at 54.
[3] *Id.* at 55.
[4] 197 Or App at 577. By contrast, OSB Formal Ethics Opinion 2005-92 concludes that a lawyer can ethically advise a client to breach a contract.
[5] *See also Roberts v. Fearey*, 162 Or App 546, 556, 986 P2d 690 (1999) (holding that for a lawyer to assist in the breach of a fiduciary duty under *Granewich* the lawyer's conduct must be affirmative rather than passive). *Roberts* does not address situations in which the lawyer has an independent duty to report the breach involved.