fucile & reising | LLP

February 2020 WSBA *NWLawyer Ethics & the Law* Column

Dual Roles:
Lawyers as Corporate Directors

By Mark J. Fucile
Fucile & Reising LLP

Lawyers have long served as directors for both corporations and non-profit organizations. According to one comparatively recent survey, for example, approximately 40 percent of public company boards included lawyers.[1] From a law firm's perspective, board service has traditionally been seen as a way to cement relationships with key corporate clients and to network in local communities through non-profit organizations. From the perspective of corporations and non-profit organizations, having a lawyer on the board is often viewed as a unique asset in an increasingly legal-centric environment.

Although board service can provide benefits to lawyer-directors and their law firms, board service can also present distinct risks—especially when the corporation or non-profit involved is also a law firm client. In this column, we'll look at five areas that lawyers and their law firms should evaluate when considering whether a firm member should also serve as a director of a law firm client: (1) conflicts; (2) attorney-client privilege; (3) insurance coverage; (4) competence; and (5) corporate knowledge. These are not intended to be either an exhaustive list or a catalog of issues that arise for every lawyer-director. Rather, they are simply intended to represent some of the more commonly recurring issues.[2]

Conflicts

Conflicts for a lawyer-director can arise from both the roles as "lawyer" and "director."

On the "lawyer" side, RPC 1.7(a)(2) governs conflicts between a lawyer's business or personal interests and the interests of the client involved.[3] Comment 35 to Washington RPC 1.7 addresses lawyer-director conflicts and uses the illustration of a lawyer-director who—as a lawyer—is approached about advising a corporation on matters involving the actions of the board on which the lawyer serves. Whether the conflict may be waived under RPC 1.7(b) will turn on the specific circumstances and ordinarily entails a careful review of the lawyer's participation in the issues involved as a board member.

On the "director" side, statutory and decisional law typically impose fiduciary duties of ordinary care and good faith on directors.[4] ABA Formal Opinion 98-410 (1998), which provides a comprehensive national[5] survey of lawyer-director issues, uses the example of a lawyer-director who—as a director—is asked to participate in the selection of counsel for matters that would be particularly lucrative to the lawyer-director's law firm.[6] The ABA opinion notes that whether lawyer-directors should recuse themselves turns on the applicable substantive law of corporate governance rather than the RPCs.[7]

Privilege

Courts have long drawn a line between legal and business advice provided by lawyers—with the former generally accorded protection under the attorney-client privilege and the latter usually not.[8]

This can have important practical consequences for lawyer-directors given the potential overlap.

With business advice, if privilege is not available, the lawyer may become a fact witness in later litigation over the matters concerned. In that event, the lawyer-witness rule—RPC 3.7—may come into play. RPC 3.7(a) generally prohibits a lawyer from acting as trial counsel if the lawyer is a "necessary" witness. Under RPC 3.7(b), personal disqualification can ripen into firm disqualification if the testimony from the lawyer-witness will be adverse to the lawyer's client.

With legal advice, ABA Formal Opinion 98-410 counsels that lawyers should keep it separate from business advice in an effort to preserve privilege:

> "[I]t is vital that that the lawyer who also serves as a director be particularly careful when her client's management or board of directors consults her for legal advice. The lawyer-director should make clear that the meeting is solely for the purpose of providing legal advice. . . . When appropriate, the lawyer-director should have another member of her firm present at the meeting to provide the legal advice."[9]

Given the sensitivity of privilege, the ABA opinion suggests that lawyer-directors discuss this area with their fellow board members and executives at client organization when they join the board involved.

Coverage

Most legal malpractice insurance policies cover just that—errors and omissions arising out of law practice. By contrast, serving as a director may be excluded—depending on the policy—because it is primarily a business activity.[10] From the risk management perspective, therefore, it is critical to determine whether a prospective board position is covered by the law firm's malpractice policy or separate directors and officers insurance provided by the company or non-profit concerned.[11]

Competence

Particularly with smaller non-profits, lawyer-directors may be viewed by their fellow directors as authoritative voices on all things legal. Today's practice reality, however, forces most of us into relatively narrow niches and a lawyer-director may not necessarily have substantive expertise on the particular legal point confronting the board. In that situation, lawyer-directors need to be diplomatic enough to demur on providing legal advice in an area beyond their competence. Simply because legal advice is provided pro bono to a non-profit

does not exempt it from the regulatory duty of competence or the civil standard of care.[12] Even if they are not able to advise on a particular matter, lawyer-directors are often in an excellent position to identify other lawyers within their firms or the community at large who can provide the specialized advice required.

For lawyers who are invited to join the board of a non-profit organization in particular and may not be familiar the duties of a director, the Attorney General and the Secretary of State have a joint booklet available on-line oriented around board service for charities and other non-profits.[13]

Corporate Knowledge

Engagement agreements are a key tool of law firm risk management. Among other benefits, an engagement agreement that defines the scope of the representation concerned will assist the law firm in avoiding "blame" for events beyond what it was hired to do. Having a firm lawyer as a director of a client, however, can lessen that benefit. With a firm lawyer on a client's board, it becomes more difficult on a practical level to argue that the firm was not aware of or involved in matters within the client that may later become the subject of litigation that attempts to "blame" the law firm.

This risk is not a reason to either stop using engagement agreements or to avoid having a firm lawyer on a client's board. At the same time, the risk should

at least be examined when a firm considers whether to approve having one of its lawyers serve on a client's board. Although circumstances vary, this risk is often sharpest when the business is closely held and takes in customer money for private investments. When seemingly successful businesses later turn out to be Ponzi schemes, their law firms are usually on the short list of litigation targets for defrauded investors—with the claim being that the law firm "should have known."[14]

ABOUT THE AUTHOR

Mark J. Fucile of Fucile & Reising LLP handles professional responsibility, regulatory and attorney-client privilege issues for lawyers, law firms and corporate and governmental legal departments throughout the Northwest. Mark has chaired both the WSBA Committee on Professional Ethics and its predecessor, the WSBA Rules of Professional Conduct Committee. Mark is a member of the Oregon State Bar Legal Ethics Committee and the Idaho State Bar Section on Professionalism & Ethics. Mark writes the Ethics Focus column for the Multnomah (Portland) Bar's *Multnomah Lawyer*, the Ethics & the Law column for the WSBA *NWLawyer* and is a regular contributor on legal ethics to the WSBA *NWSidebar* blog. Mark is a contributing author/editor for the current editions of the OSB Ethical Oregon Lawyer, the WSBA *Legal Ethics Deskbook* and the WSBA *Law of Lawyering in Washington*. Before co-founding Fucile & Reising LLP in 2005, Mark was a partner and in-house ethics counsel for a large Northwest regional firm. He also teaches legal ethics as an adjunct for the University of Oregon School of Law at its Portland campus. Mark is admitted in Oregon, Washington, Idaho, Alaska and the District of Columbia. He is a graduate of the UCLA School of Law. Mark's telephone and email are 503.224.4895 and Mark@frllp.com.

[1] *See* Lubomir P. Litov, Simone M. Sepe and Charles K. Whitehead, *Lawyers and Fools: Lawyer-Directors in Public Corporations*, 102 Geo. L.J. 413, 427 (2014).

[2] Some of these issues—such as insurance coverage and competence—can arise even if the organization involved is not a firm client.

[3] Other conflict rules may also come into play. For example, a lawyer-director might be offered the opportunity to invest in the client business involved—triggering RPC 1.8(a) on investments in law firm clients. Comments 13 and 14 to RPC 1.13 and *Hicks v. Edwards*, 75 Wn. App. 156, 876 P.2d 953 (1994), discuss the special considerations involved in shareholder derivative litigation.

[4] *See, e.g.,* RCW 23B.08.300 (standards for directors); *Riss v. Angel*, 131 Wn.2d 612, 632, 934 P.2d 669 (1997) ("[D]irectors have a fiduciary duty to exercise ordinary care in performing their duties and to act reasonably and in good faith.").

[5] WSBA Advisory Opinions1068 (1987) and 1686 (1996) also discuss lawyer-director issues.

[6] *Id*. at 10.

[7] *Id*.

[8] *See, e.g., Chandola v. Seattle Housing Authority*, 2014 WL 4685351at *3 (W.D. Wash. Sept. 19, 2014) (unpublished) (discussing the distinction).

[9] *Id*. at 6 (footnote omitted).

[10] *See, e.g., Continental Cas. Co. v. Smith*, 243 F. Supp.2d 576, 581-82 (E.D. La. 2003) (declaratory judgment action by malpractice carrier arguing no duty to defend or indemnify because lawyer's actions arose from work as a corporate officer rather than as a lawyer).

[11] Although RCW 4.24.264(1) provides immunity from personal liability for discretionary decisions made as the director of a non-profit organization, there is an exception for gross negligence.

[12] Competence in a regulatory sense is defined by RPC 1.1. Washington Pattern Jury Instruction 107.04 addresses the standard of care in the legal malpractice context.

[13] *Charitable & Nonprofit Board Service in Washington State—A Quick Guide*.

[14] *See, e.g., Norton v. Graham and Dunn, P.C.*, 2016 WL 1562541 (Wn. App. Apr. 18, 2016) (unpublished) (investors in Ponzi scheme sued law firm).