REPRESENTING BUSINESS COMPETITORS: A CONFLICT OR NOT?

You have just read in the newspaper that one of your principal outside law firms represents your company's primary competitor! Outrageous! You think that such representation would always be a conflict of interest, and you are going to make that point clear to the managing partner. Now that you have made up your mind, let's look at the ethics rules and see whether you are correct. The answer, as you might imagine, is not always but sometimes.

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A law firm's simultaneous, though unrelated, representation of two corporations that directly compete in a particular market might, at first glance, appear to pose a conflict of interest for the firm. After all, how can the firm fulfill its obligation to "act with commitment and dedication to the interests of"[1] Client A without violating its corresponding obligation to Client B, one of Client A's primary rivals in the business world? Doesn't zealous representation of one competitor necessarily preclude zealous representation of the other competitor? And what about the confidentiality requirements of Rule 1.6 of the *Model Rules of Professional Conduct*: even though the representations involve unrelated matters, isn't the risk of disclosure of confidential information too great to permit, from an ethical standpoint, the concurrent representation of these competitors? Although the simultaneous representation of business competitors in unrelated matters does raise intriguing conflict of interest issues, it does not ordinarily result in an ethical conflict requiring withdrawal or disqualification. Whether an ethical conflict exists depends on other factors, such as the nature of the representation, the degree of competition between the clients, and the confidentiality of the information imparted to the lawyer.

The jumping off point for our analysis is Rule 1.7 of the *Model Rules of Professional Conduct*, which sets forth the general rule governing conflicts of interest. The rules squarely address litigation in which both clients are parties. Under 1.7(a), a lawyer is prohibited from representing a client "if the representation of that client will be directly adverse to another client" unless the lawyer can conclude that the representation of the clients will not be affected and the clients consent after the lawyer has explained the conflict.[2] Within the meaning of this rule, direct adversity exists when a firm represents two clients who are engaged in litigation *against* each other.[3] A Rule 1.7(a) conflict also arises in cases in which the lawyer sues a current client that the law firm is representing on an unrelated matter.[4] Such conduct raises concerns regarding the duty of loyalty.[5]

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An entirely different situation arises when a law firm represents, in unrelated matters, two clients with competing economic interests. For example, the law firm could represent a manufacturer of goods in tax litigation or counseling and simultaneously represent one of its largest buyers in an unrelated lease dispute. Or the law firm could represent one bank in a collection suit on a note and also represent a competing bank as lending counsel. Under 1.7(a), direct adversity does not exist in these two scenarios.[6] Any conflict in these two scenarios would be regarded as indirect[7] or

so general that consent of the respective clients is not required.[8] As explained by one court, the fact that the clients "are economic competitors in an allegedly consolidating marketplace is too speculative a basis for finding that [the lawyer's] loyalty to each of its clients will be divided as a result of the representation."[9]

Between these two extremes are situations in which the concurrent representation of clients with competing economic interests may be "directly adverse" and thus preclude the continued representation of one of the clients, such as a case in which the lawyer has been retained by competitors to assist in obtaining a single broadcast license.[10] In this situation, the clients' respective positions in the relevant market dictate a finding of direct adversity because the lawyer's duty of loyalty to Client A would necessarily compromise the lawyer's ability to promote Client B's license application and vice versa.[11]

As a general proposition, however, representation of clients having adverse economic interests is permissible[12] and does not present an ethical conflict in violation of Rule 1.7(a).[13] This general proposition does not mean that, as a practical matter, an existing client cannot threaten to move its business elsewhere if the firm chooses to represent a competitor, only that no impermissible conflict of interest precludes representation of the competitor.

The fact that a law firm can theoretically represent competitors with adverse economic interests, however, does not mean that one outside counsel can strategize with the in-house counsel of one competitor on Monday and then strategize with the in-house counsel of another competitor on Tuesday. Confidential information will presumably be provided to the outside counsel in each conversation. A lawyer is required by Rule 1.6 not to use information secured from the representation of one client for the benefit of another client. How would a law firm enforce that rule in our Monday-Tuesday hypothetical? Implementation of screening devices could alleviate the appearance of impropriety and help protect against disclosure.[14]

Moreover, even though the dual representation of business competitors in unrelated matters may not raise an ethical issue under Rule 1.7(a), a conflict with both representations could subsequently develop if it becomes necessary for the lawyer to advocate a position with respect to one client that is contrary to the position that the lawyer has taken on behalf of the other client. Pursuant Rule 1.7(b), a lawyer is generally precluded from representing a client in cases in which such representation may be "materially limited by the lawyer's responsibilities to another client."[15] Although it ordinarily may be permissible for a lawyer to represent clients having antagonistic positions on similar legal issues arising in their respective cases, an ethical conflict exists under subsection (b) if the lawyer's representation of either client in the separate cases[16] would be adversely affected[17]—that is, if the lawyer cannot zealously represent the interests of both clients because of the detrimental effect that advocating one position on behalf of Client A would have on the interests of Client B.[18] According to the ABA, an impermissible positional conflict can occur at the appellate, as well as the trial court, level.[19]

As recognized by the *Restatement,* "[a] lawyer ordinarily may take inconsistent legal positions in different courts at different times."[20] Any other rule would severely limit the scope of a firm's practice.[21] In the case of concurrent representations of business competitors, there is no per se prohibition against taking a position on behalf of one that is antago-

nistic to the position to be advocated on behalf of the other in an unrelated case, provided that taking such a position would not interfere with the lawyer's duty to provide effective advocacy of the clients' positions. Of course, clients can consent to their lawyer's advocacy of a particular position, notwithstanding its potential risks.[22] Clients can also limit the representation or take their business to another firm.

What have we learned about the general rule of "business conflicts"?

- As a general rule, it is not a conflict of interest under the Model Rules of Professional Conduct for a lawyer to represent two clients who are economic competitors so long as the two clients are not "directly adverse" to each other.
- Direct adversity, as that term has been interpreted in the context of economic competitors, is a very demanding standard. In substance, it refers to situations in which the two clients are either in a one-to-one or very limited competition for a single goal, such as a contract, an asset, a patent, or a license. Clients who merely compete for larger shares of a market are not generally deemed directly adverse for purposes of Model Rule 1.7.
- Even if there is no conflict of interest under Model Rule 1.7, a lawyer must approach with care the representation of multiple clients who are business competitors to preserve their confidential information as required by Model Rule 1.6. In cases with a substantial risk that a client will impart to the lawyer or law firm confidential information that could be used for the benefit of another client of the firm or to the detriment of the client providing the information, the lawyer or law firm may choose to erect screens and possibly secure consent from the clients. Although such measures may not be ethically required, they can make clients feel more comfortable that their confidences are being protected.
- One must remain alert to the possibility that positions that a lawyer takes in one litigation may be adverse to the positions that the lawyer is taking in another litigation for another client. The rules governing "issue conflicts" vary considerably among jurisdictions, but the most common rule prohibits a lawyer or firm from taking a position directly adverse to the position that the lawyer is taking in another litigation in the same jurisdiction. Policing this rule can be extremely difficult for a large firm.
- Finally, the corporate client's ultimate tool to secure the loyalty of the law firm is not necessarily threat of ethical sanctions but the possibility of terminating the law firm's employment for disloyalty that is not within the ambit of the ethical rules.

NOTES

1. *ABA Model Rules of Professional Conduct*, Rule 1.3, Mt. 1 (2001).
2. *Id*., Rule 1.7(a).
3. *See ABA/BNA Lawyers' Manual on Professional Conduct Reference Manual* 51:101; *see, e.g.*, Cinema 5, Ltd.. v. Cinema, Inc., 528 F.2d 1384 (2d Cir. 1976) (involving analogous provision of *Model Code* under which court disqualifies partner's New York City firm from representing theater operators in action against motion picture distributors alleging conspiracy to acquire control of plaintiff through stock acquisitions for the purpose of creating a monopoly and restraining trade, where partner's Buffalo firm represented one of the motion picture distributors who was also a defendant in a separate action alleging monopolistic licensing and distribution of motion pictures, even though assumption of dual representation was inadvertent and unknowing).
4. *See* Research Corp. Technologies Inc. v. Hewlett-Packard Co., 936 F. Supp. 697, 701 (D. Ariz. 1996) (firm's representation of plaintiff in patent litigation against defendant and its concurrent representation of defendant in unrelated tax matter violated Rule 1.7(a) because representations involved directly adverse interests); *see also ABA Model Rules of Professional Conduct*, Rule 1.7, Mt. 3 (stating that "a lawyer ordinarily may not act as advocate against a person the lawyer represents in some other matter, even if it is wholly unrelated").
5. *See ABA Model Rules of Professional Conduct*, Rule 1.7, Mt. 3.
6. *Id*.
7. Chapman Engineers, Inc. v. Natural Gas Sales Co., Inc., 766 F. Supp. 949, 956 (D. Kan. 1991) (further noting that, because the rule speaks in terms of interests that "will be" directly adverse, the mere possibility of directly adverse interests is insufficient to trigger the rule).
8. *ABA Model Rules of Professional Conduct*, Rule 1.7, Mt. 3. *See also Restatement (Third) of the Law Governing Lawyers* § 121, Mt. c(iii) (2000) ("General antagonism between clients does not necessarily mean that a lawyer would be engaged in conflicted representations by representing the clients in separate, unrelated matters").
9. *In re Caldor, Inc.*, 193 BR 165, 181 (Banker. S.D.N.Y. 1996) (wherein the lawyer represented both the creditors' committees in the debtor's case and the creditors' committees in the Chapter 11 case of the debtor's competitor). Although Caldor was decided under Canon 5 of New York's version of the *Model Code of Professional Responsibility*, the court found comment 3 to Rule 1.7 of the *Model Rules* instructive in analyzing the issue of economic competitors under New York's *Model Code* provision. *Id*.
10. *Restatement (Third) of the Law Governing Lawyers*, *supra* note 8, cmt c(i), illus. 1.
11. *Id*.
12. *See* Texarkana College Bowl, Inc. v. Phillips, 408 S.W.2d 537, 540 (Tex. Civ. App. 1966) (in rejecting petition for receivership brought by minority stockholder, alleging, *inter alia*, that corporate directors' retention of firm that concurrently represented corporation's business competitor constituted a per se fraud upon the corporation or its stockholders, court noted, in dicta, that counsel may, "within

very narrow limits, represent clients having adverse economic interests").

13. *See District of Columbia Rules of Professional Conduct*, Rule 1.7, cmt. 10 ("The fact that two clients are business competitors, standing alone, is usually not a bar to simultaneous representation").
14. As to what features a screening program should have in order to be considered effective, *see* Maritrans GP, Inc. v. Pepper, Hamilton & Scheetz, 602 A.2d 1277 (Pa. 1992) (Nix, J., dissenting).
15. *ABA Model Rules of Professional Conduct*, Rule 1.7(b) (providing further that the prohibition does not apply if the client has consented and the lawyer reasonably believes that the representation will not be adversely affected).
16. Under the District of Columbia's formulation of the *Model Rules*, a lawyer is prohibited from advancing adverse positions in the same matter and, unless consent is obtained, is prohibited from representing a client in a matter if it requires taking a position that is adverse to a position taken by another client *in the same matter*. Although this rule seemingly authorizes taking adverse positions with respect to clients in unrelated matters, the rule also prohibits a lawyer from representing a client in cases in which such representation would adversely affect, or be adversely affected by, the representation of another client. *District of Columbia Rules of Professional Conduct*, Rule 1.7.
17. *Id.*, cmt. 9. Under the *Restatement*, a conflict is presented in this situation "when there is a substantial risk that a lawyer's action in Case A will materially and adversely affect another of the lawyer's clients in Case B." *Restatement (Third) of the Law Governing Lawyers, supra* note 8, cmt. f.
18. A representation would be adversely affected "[i]f the lawyer concludes that issue is of such importance and that its determination in one case is likely to have a significant impact on its determination in the second case, thus impairing the lawyer's effectiveness—or if the lawyer concludes that, because of the dual representation, there will be an inclination by the firm either to 'soft-pedal' the issue or to alter the firm's arguments on behalf of one or both clients, thus again impairing the lawyer's effectiveness[.]" *ABA Comm. on Ethics and Professional Responsibility*, Formal Op. 377 (1993).
19. *Id.* (noting that, even though comment 9 to Rule 1.7 makes a distinction between the level of the court in considering the propriety of advocating antagonistic positions on behalf of two clients, the committee did not believe that such a distinction was warranted in view of the similarity of the effect on the second client's case).
20. *Restatement (Third) of the Law Governing Lawyers, supra* note 8.
21. *Id.*
22. *See, e.g., Philadelphia Bar Ass'n Professional Guidance Comm.*, Op. 89-27 (1990) (permitting law firm to represent clients in different cases requiring adverse positions on same issue, even though resolution of issue will have material significance to both clients, if each client consents after consultation and disclosure).