DELAWARE STATE BAR ASSOCIATION
COMMITTEE ON PROFESSIONAL ETHICS

OPINION 1997 - 4

October 3, 1997

This opinion is merely advisory and is not binding on the inquiry attorney, the courts or any other tribunal.

This opinion involves a joint request by the opposing parties in a lawsuit pending in Delaware. The action arose out of a former director's (the "Former Director") dismissal. from employment by his company (the "Company") for "cause." A side from contentions going to the merits, the Former Director contends that counsel for the Company (the "Law Firm") has a conflict of interest in representing the Company.

FACTS

The parties have provided the committee with a mutually agreed upon Stipulation of Facts, which includes a number of exhibits. The Stipulation, including the exhibits, constitutes the facts on which the parties asked the committee to base its decision. As so stipulated, the facts may be summarized as follows:

The Former Director entered into an Officer Employment Agreement with the Company. At the time the agreement was negotiated and executed, the Law Firm did not represent either the Company or the Former Director in any capacity, nor did it draft the agreement. It happens that the Law Firm represented the Former Director along with nine other officers of the Company previously in connection with the then proposed acquisition of the Company by another company (the "Acquiring Company"). The engagement letter was countersigned by each of the officers, and bore the heading "Retention of [the Law Firm] as Counsel in Connection with Employment Discussions With New Employer." Each of the ten officers already had essentially the same officer Employment Agreement with the Company. An issue of primary concern was whether the consummation of the transaction between the

Company and the Acquiring Company pursuant to the proposed Acquisition Agreement would constitute a "change of control" within the meaning of the respective officers, employment agreements. Termination of employment, other than for cause, meant that Paragraph Eight ("Termination by the Company") and possibly Paragraph Ten ("Termination Upon the Change of Control") of the Officer Employment Agreement would be operative. Determination of whether these paragraphs were operative might require a consideration of Paragraph Nine, "Termination by the Company for Cause." As part of their representation of the Former Director and the other nine officers, the Law Firm reviewed and digested the Officer Employment Agreement, reviewed the officer benefit documents (including the SERP) and reviewed the minutes of the meetings by the officers in which the Former Director participated. The Law Firm also reviewed the employment offers to the officers of the Company by the Acquiring Company, and the officer benefit plans of the Acquiring Company. The Law Firm communicated with certain of the ten officers, in the capacity of representing all of them, concerning these matters, but did not communicate with the Former Director, either individually or in such capacity.

The Former Director did not serve as one of the designated representatives of the officers, and did not meet with the Law Firm attorneys or participate in phone conferences with the Law Firm attorneys. He did participate in the meetings among the officers at which the subjects to be addressed at these meetings were discussed and at which the information obtained at these meetings was reviewed. One member of the group (not the Former Director) was counselled individually, at his request, by the Law Firm. There was no discussion between any representative of the Law Firm and the Former Director, or at the officers' meetings, concerning acts or conduct by the Former Director which the Company subsequently alleged were the basis on which the Company terminated the Former Director's employment.

Each of the ten officers paid the Law Firm for the Law Firm's services.

Subsequently, the Company decided that it wished to be represented by the Law Firm in connection with the ongoing merger negotiations. It was recognized that in order to do

this it would be necessary to terminate the representation of -the Former Director and the other officers by the Law Firm and to obtain a waiver of any possible conflicts of interest which might exist. Accordingly, a letter captioned "Waiver of Conflict" (drafted by an attorney of the Law Firm) and containing a signature line for the Former Director's signature was presented to the Former Director, and was signed by him. Neither in the letter, nor otherwise, was the Former Director, nor any of the other officers to whom the letter was submitted, advised to seek separate counsel before waiving the conflict. The waiver letter made no reference to any other conflict or possible conflict of interest between the Former Director and the Company except those which might result from the Law Firm taking over the representation of the Company in connection with the merger. Specifically, the waiver letter did not in terms relate to any possible conflict which might exist respecting the Former Director individually or personally, separate and apart from his position as one of the ten officers and the joint interests of those ten individuals.

The Law Firm proceeded to represent the Company in connection with the proposed acquisition by the Acquiring Company until the negotiations were terminated by agreement of the parties.

Prior to the termination of the negotiations, the Company informed the Former Director that his employment would be terminated. Within a week of that date, the Company also informed the Former Director that it would be represented by an attorney with the Law Firm in the matter of the Former Director's termination, including any litigation which might flow therefrom. The Company does not contend (nor apparently does anyone else) that the termination of the Former Director's employment had anything to do with the proposed acquisition by the Acquiring Company. The Former Director was not asked to consent to the Law Firm's representing the Company against him, nor was he asked to waive any conflict of interest specifically relating to such representation.

The Former Director, through his counsel, objected to the Law Firm representing the Company in the matter of his termination by the Company, on the basis of a conflict of interest which he had not waived.

The dispute between the Company and the Former Director is based on the Officer Employment Agreement. The primary liability issue is whether the Company had the right to terminate the Former Director "for cause" under Paragraph Nine of the Agreement. The damage issues, in the event it should be held that the Former Director was terminated without cause under the Agreement, are based on Paragraph Eight, which sets forth the categories of compensation to a Company officer terminated without cause. In addition to their disagreement respecting the "for cause" aspect of the termination, the parties dispute the manner in which the calculation of lump sum payments and other benefits should be paid under Paragraph Eight, assuming it be held that the termination was not "for cause".

The Officer Employment Agreement which is under dispute in the instant litigation is the same Officer Employment Agreement which was, at least in part, the subject of the representation by the Law Firm of the ten senior officers of the Company, as described above.

CONCLUSION

There is no conflict of interest which would preclude the Law Firm from representing the Company in the litigation wherein the Former Director is plaintiff and the Company is defendant.

DISCUSSION

In Delaware, conflicts of interest created by former representation of adverse parties are evaluated under the Delaware Lawyers' Rules of Professional Conduct. The general considerations relative to disqualification are governed by Rule 1.9, which provides as follows:

> A lawyer who has formerly represented a client in a matter shall not thereafter:
>
> > (a) represent another person in the same or a *substantially related* matter in which that person's interests are *materially adverse* to the interests of the former client unless the former client consents after consultation; or

> (b) use information relating to the representation to the disadvantage of the former client except as Rule 1.6 or Rule 3.3 would permit or require with respect to a client or when the information has become generally known. (Emphasis supplied.)

(Amended, effective June 1, 1988) (emphasis added).

Generally, Delaware courts will disqualify counsel under Rule 1.9 if a four-part "facts and circumstances" test is satisfied:

> First, the lawyer must have had an attorney-client relationship with the former client. Second, the present client's matter must either be the same as the matter the lawyer worked on for the first client, or a "substantially related" matter. Third, the interests of the second client must be materially adverse to the interests of the former client. Fourth, the former client must not have consented to the representation after consultation.

Nemours Foundation v. Gilbane, Aetna, Federal Ins. Co., 632 F. Supp. 418, 422 (D. Del. 1986).

It would appear that the two clauses appearing in italics above are correlatives, in the sense that one does not reach the "materially adverse" aspect until it has been determined that the former representation was "substantially related" to the current one. Hence, the consideration of the Committee centers around the interpretation and application of the concept "substantially related," within the meaning of the Rule.[1]

[1] Rule 1.9 deals not only with conflicts of interest in the strict sense (i.e., the sense of Rules 1.6, 1.7 and 1.8) but with what might appropriately be called *conflict of communication* or *conflict of information* [subparagraph (b)]. While it seems reasonable to construe the prohibition of subsection (b) as an independent provision, and not dependent upon the "substantially related" concept of subparagraph (a), there is, nevertheless, obviously some relationship between subparagraphs (a) and (b), to the extent that in Webb v. E. I. duPont deNemours & Co., Inc., 811 F. Supp. 158 (D. Del. 1992), Judge Latchum said, in effect, that it was not necessary for the objecting former client to show that he disclosed confidential matters to the attorney who was later adverse to him, but that a court may assume that such former representation, with its opportunity for such confidences, actually involved such confidences, without inquiring into their nature or extent.

The standard for evaluating the "substantially related" factor is set forth in Satellite Fin. Planning v. 1st Nat. Bk. Wilmington, 652 F. Supp. 1281, 1283 (D.Del. 1987), which states:

> The Court must answer three questions to determine whether movants have satisfied the substantial relationship test:
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> 1. What is the nature and scope of the prior representation at issue?
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> 2. What is the nature of the present lawsuit against the former client?
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> 3. In the course of the prior representation, might the client have disclosed to his attorney confidences which could be relevant to the present action? In particular, could any such confidences be detrimental to the former client in the current litigation?

Thus, it appears that the principal practical reason for enacting Rule 1.9 was to preclude the opportunity for counsel who has changed sides, so to speak, to utilize in the second proceeding matters obtained in confidence from the former client in the first. See INA Underwriters Insurance Company v. Nalibotsky, et al., 594 F. Supp. 1199, 1205-07 (E.D. Pa. 1984) (protection against disclosure of confidences appeared there to have been the *sole* reason for disqualification). The Nalibotsky court stated, " . . . the question which I must address is whether the nature and scope of the prior representation were such that confidences *might* have been disclosed during that representation which would be *relevant to the present action."* Id. at 1205, n.4 (emphasis added).

The most critical Satelite factor here appears to be the third. According to the stipulated facts, the law firm never talked to the Former Director, and no discussions occurred concerning acts or conduct which allegedly provided a basis for his termination. This inquiry represents a rather unusual circumstance where a lawyer-client relationship was created with only de minimis communications between the two during the existence of the relationship.

Taking into consideration that the burden of establishing "substantial relationship" falls upon the objecting party (Satelite at 1283; Nalibotsky at 1207), the Committee believes that

the Former Director cannot meet this burden. The circumstances and considerations that would point toward the likelihood of pertinent and relevant disclosure in the course of the earlier representation are not present here. While there may be some degree of conceptual overlap between the matters dealt with in the prior representation of the ten officers and those involved in the instant litigation, these elements are essentially academic in nature and lacking in practical significance. The representation of the ten officers, especially insofar as the Former Director was concerned, dealt only with their group or common interests, and then only with their common interest in one particular aspect - the effect of the anticipated merger on the possible termination of their contracts *without cause.* The principal current issue deals with the right of the Company to have terminated the Former Director *for cause*. There is, however, no inference which the Committee can discern that the prior representation, considering its scope and purpose, provided the Former Director with any occasion to disclose confidential information, or otherwise involved confidential information transmitted to the Law Firm, which could now be used against the Former Director. In view of the Committee's conclusion that there is no conflict, it is not necessary to decide whether or not the alleged waiver letter disposed of any conflict.[2]

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[2] Thomas P. Preston dissents from this Opinion.