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Outside Counsel

Expert Analysis

Advice From Law Firm's In-House Counsel Found Shielded by Privilege

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In a case of first impression, the Appellate Division, First Department, recently held in a malpractice action, *Stock v. Schnader Harrison Segal & Lewis*, that communications among "attorneys who have sought the advice of their law firm's in-house general counsel on their ethical obligations in representing a firm client" during the representation of that client are "not subject to disclosure"—even where "the consultation at issue…might have extended to whether [the firm]…was potentially liable…for malpractice."[1] The court unanimously reversed the trial court's decision, thereby joining the highest courts of Massachusetts and Georgia, among others, in declining to apply the fiduciary and "current client" exceptions to the attorney-client privilege.

Malpractice Claim

According to the First Department, Schnader Harrison Segal & Lewis LLP originally represented plaintiff Keith Stock in negotiating his separation agreement with his former employer. "Unbeknownst to" Stock, his employment "termination triggered the acceleration of the ending dates of the exercise periods of certain stock options granted to him," and "the firm did not negotiate an extension of the truncated exercise periods." After learning that "all of his vested stock options," allegedly "worth more than $5 million," had expired, Stock (still represented by Schnader Harrison) sued his former employer in federal court and commenced a FINRA arbitration against the plan administrator.[2]

> The First Department declined to apply the fiduciary and 'current client' exceptions to the attorney-client privilege.

Shortly before the arbitration, the plan administrator announced its intention to call "as a fact witness" a Schnader Harrison attorney who had represented Stock in the employment negotiations, prompting that attorney and two others "to seek legal advice from [the firm's] in-house general counsel" regarding "their and the firm's ethical obligations…under the lawyer-as-witness rule."[3] After the suit and arbitration failed, Stock sued Schnader Harrison and an individual partner, asserting, among other claims, malpractice in "fail[ing]…to advise…that his termination would accelerate the expiration of his vested stock options."[4] Stock then sought disclosure of "about two dozen email communications…exchanged…among [the firm's]…in-house counsel and the three attorneys who were then representing…or had previously represented him," which the Supreme

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Court granted in an Interim Order in December 2014.[5]

In granting Stock's application, the trial court held that the common-law fiduciary exception to the attorney-client privilege, which initially had developed "as a principle of trust law," compelled disclosure of the attorneys' internal communications with the firm's general counsel. In reversing that ruling, the First Department relied heavily on an analysis of the Delaware Chancery Court's decision in *Riggs National Bank of Washington, D.C. v. Zimmer*[6]—"the leading American case on the fiduciary exception"—in which "a trustee was compelled to produce to the trust's beneficiaries an attorney's legal memorandum that had been prepared for the trustee, at the trust's expense, in anticipation of potential tax litigation on behalf of the trust."[7]

'Real Client'

In view of *Riggs*, the First Department concluded that, "whether the fiduciary exception applies depends on whether the 'real client' of the attorney from whom the fiduciary sought advice was the beneficiary of the fiduciary relationship or, alternatively, the fiduciary in his or her individual capacity." Here, because the attorneys "had their own reasons, apart from any duty owed to plaintiff, for seeking…legal guidance" from the firm's general counsel, "whose time spent on the consultation was not billed to plaintiff and who never worked on any matter for plaintiff," the firm and those attorneys were the "real clients," and the fiduciary exception did not apply.[8]

The plaintiff also argued for disclosure under the "current client exception" recognized by some courts, including the Southern District of New York,[9] which "holds that a law firm cannot invoke attorney-client privilege to withhold from a client evidence of any internal communications within the firm relating to the client's representation, including consultations with the firm's in-house counsel, that occurred while the representation was ongoing," because such consultations "involve [a]…firm in an impermissible simultaneous representation of conflicting interests."[10]

In light of case law that has developed over the past few years, however, the First Department declined to adopt this exception, going so far as to label it "draconian" and reasoning, in accordance with NYSBA Opinion 789, that "a law firm's consideration of its own legal and ethical obligations in connection with [representing]…one or more clients cannot be said to implicate a differing interest that will adversely affect the lawyer's exercise of professional judgment nor the loyalty due a client within the meaning of the Code."[11]

The First Department also observed that the ex-ception "has the effect of penalizing the law firm for seeking advice from one of its own lawyers," as opposed to an outside attorney.[12] Requiring a firm to retain outside counsel in order to safeguard its privilege would only "increase the cost of obtaining ethical advice," and, "more importantly, would likely substantially delay the process of obtaining such advice."[13] A more streamlined approach to obtaining legal advice from the "lawyers knowledgeable about the firm, its client relationships and its culture" seems preferable to creating an incentive for a firm to "withdraw at the first hint of a problem."[14]

This decision thus brings the treatment of law firms closer to that of ordinary businesses seeking legal advice, balancing the practicalities inherent in law practice with counsel's ethical and fiduciary duties.

1. *Stock v. Schnader Harrison Segal & Lewis*, No. 651250/13, 2016 WL 3556655, at *1, *14 (1st Dept. June 30, 2016).
2. Id. at *2.
3. Id. at *3.
4. Id.
5. Id. at *4.
6. *Riggs Nat'l. Bank of Washington, D.C. v. Zimmer*, 355 A.2d 709, 711 (Del. Ch. 1976).
7. *Stock*, 2016 WL 3556655, at *5.
8. Id. at *6–7.
9. *Bank Brussels Lambert v. Credit Lyonnais (Suisse)*, 220 F.Supp.2d 283 (S.D.N.Y. 2002).
10. *Stock*, 2016 WL 3556655, at *11.
11. Id. at *13–14.
12. Id. at *16.
13. Id.
14. Id. at *16–17.