

**THE PROFESSIONAL ETHICS COMMITTEE
FOR THE STATE BAR OF TEXAS
Opinion No. 603**

November 2010

QUESTION PRESENTED

Do the Texas Disciplinary Rules of Professional Conduct require or permit a lawyer to reveal to a corporation's creditors the lawyer's advice to the corporation that the person who owns and manages the corporation has engaged in conduct that constitutes a breach of the person's fiduciary duty to the corporation?

STATEMENT OF FACTS

A lawyer represents an insolvent corporation that is controlled and managed by an individual who is the corporation's sole shareholder, sole director, and sole officer (the "Corporate Representative"). The lawyer concludes that the Corporate Representative is engaged in conduct that, although not criminal, constitutes a breach of the Corporate Representative's fiduciary duty to the corporation and that the conduct will likely result in substantial harm to the corporation's creditors. Because of the corporation's insolvency, the Corporate Representative's breach of fiduciary duty is unlikely to cause any material harm to the corporation but is likely to cause significant harm to the corporation's creditors. The lawyer advises the Corporate Representative that his conduct constitutes a breach of his fiduciary duty to the corporation and should be stopped. The Corporate Representative nevertheless continues his conduct and specifically instructs the lawyer not to share the lawyer's conclusions or advice with the corporation's creditors.

DISCUSSION

Preservation of a client's confidential information is one of the fundamental obligations of a lawyer. "Both the fiduciary relationship existing between lawyer and client and the proper functioning of the legal system require the preservation by the lawyer of confidential information of one who has employed or sought to employ the lawyer." Comment 1 to Rule 1.05 of the Texas Disciplinary Rules of Professional Conduct. Conclusions reached by a lawyer regarding the conduct of a corporate client's representative and the resulting advice that the lawyer gives to the corporation are "confidential information" as defined in Rule 1.05(a).

Rule 1.05(b) provides that, with certain exceptions, a lawyer shall not knowingly "(1) Reveal confidential information of a client or a former client to: (i) a person that the client has instructed is not to receive the information" An exception to this general prohibition that requires particular consideration with respect to the factual situation

presented here is specified in Rule 1.05(c)(7), which provides that a lawyer may reveal a client's confidential information "[w]hen the lawyer has reason to believe it is necessary to do so in order to prevent the client from committing a criminal or fraudulent act." The Terminology section of the Rules provides that "'Fraud' or 'Fraudulent' denotes conduct having a purpose to deceive and not merely negligent misrepresentation or failure to apprise another of relevant information."

An initial question in the circumstances considered here is whether the Corporate Representative's breach of fiduciary duty to the corporation results in conduct by the corporation that constitutes a crime or fraud. In this case, the lawyer has concluded that the corporation's conduct resulting from the breach of fiduciary duty does not constitute a crime. As to fraud, not all breaches of fiduciary duty are fraudulent. See *Duncan v. Lichtenberger*, 671 S.W.2d 948, 954 (Tex. App.-Fort Worth 1984, writ ref'd, n.r.e.) (fraud is not a required element of breach of fiduciary duty). If the Corporate Representative's breach of fiduciary duty does not result in corporate conduct constituting fraud, then nothing in the Texas Disciplinary Rules would authorize the lawyer to reveal the lawyer's conclusions and advice to the corporation's creditors.

On the other hand, if the Corporate Representative's breach of fiduciary duty results in fraud likely to result in substantial financial harm, Rule 1.02(d) requires that the lawyer attempt to dissuade the corporate client from engaging in such conduct:

"When a lawyer has confidential information clearly establishing that a client is likely to commit a criminal or fraudulent act that is likely to result in substantial injury to the financial interests or property of another, the lawyer shall promptly make reasonable efforts under the circumstances to dissuade the client from committing the crime or fraud."

Because the client is a corporation and the Corporate Representative is violating legal duties to the corporation, the requirements of Rule 1.12, applicable when an organization is a lawyer's client, must be considered. Rule 1.12(b), which requires a lawyer to act when an officer's or employee's breach of an obligation to an organization will likely result in substantial injury to the organization, will not apply because, under the facts presented here, there is no likelihood of significant harm to the corporation. Nevertheless Rule 1.12(c) will apply, requiring that "[e]xcept where prior disclosure to persons outside the organization is required by law or other Rules, a lawyer shall first attempt to resolve a violation by taking measures within the organization." Here, the lawyer has acted within the corporation by raising the issue with the Corporate Representative but the lawyer has not been successful in causing the client to stop the conduct.

Where, as here, the client insists on continuing in a course of conduct that the lawyer has advised against, the lawyer remains bound by requirements of the Texas Disciplinary Rules to protect the client's confidential information unless an exception applies: "When a client's course of action has already begun and is continuing, the

lawyer's responsibility is especially delicate. The lawyer may not reveal the client's wrongdoing, except as permitted or required by Rule 1.05." Comment 8 to Rule 1.02.

The facts here do not fall within the provisions of paragraphs (e) and (f) of Rule 1.05 that *require* the lawyer to reveal confidential information in certain circumstances. As noted above, however, Rule 1.05(c)(7) provides that a lawyer *may* reveal confidential information when the lawyer reasonably believes that disclosing the information is necessary in order to prevent the client from committing a criminal or fraudulent act. In the situation considered, if the Corporate Representative's breach of fiduciary duty results in fraudulent conduct by the corporation, then under Rule 1.05(c)(7), the lawyer is permitted to reveal his conclusions and advice to the extent necessary to prevent the fraudulent conduct, including, if such is necessary, by revealing confidential information to the corporation's creditors. But if the lawyer believes that revealing confidential information to the corporation's creditors would not prevent the fraud, then Rule 1.05(c)(7) would not permit the lawyer to reveal confidential information to the creditors even if the corporation's conduct constituted fraud.

Rule 1.05(c)(7) does not specify to whom confidential information may be revealed when the Rule permits disclosure. Comment 14 to Rule 1.05 explains that "a disclosure adverse to the client's interest should be no greater than the lawyer believes necessary to the purpose." Thus, in the circumstances considered, if fraud is involved and the lawyer chooses to disclose confidential information, the lawyer must do so in a manner that minimizes the extent of the disclosure and the adverse effect of the disclosure upon the corporate client while also accomplishing the goal of preventing the client from committing fraud. For example, if an opportunity exists for confidential disclosure to a court, in camera, and such disclosure would likely be sufficient to prevent the corporation's fraud, then disclosure to the court may be the appropriate course of action.

Finally, regardless of the lawyer's determination with respect to disclosure of confidential information to the client corporation's creditors, the lawyer may terminate his representation of the corporation. Under Rule 1.15(b)(4), one of the circumstances in which a lawyer is permitted to withdraw from representing a client exists when "a client insists upon pursuing an objective that the lawyer considers repugnant or imprudent or with which the lawyer has fundamental disagreement[.]" Such a permitted withdrawal "is optional with the lawyer even though the withdrawal may have a material adverse effect upon the interests of the client." Comment 8 to Rule 1.15. Of course, if the matter is in litigation, a lawyer may not withdraw from representation if the court orders otherwise. See Rule 1.15(c) ("When ordered to do so by a tribunal, a lawyer shall continue representation notwithstanding good cause for terminating the representation."). Rule 1.15(d) requires that, if a lawyer chooses to withdraw from representation, the lawyer must take reasonable steps to protect the client's interests.

CONCLUSION

A lawyer may reveal, but is not required to reveal, to a corporation's creditors the lawyer's advice to the corporation that conduct of the person who owns and manages the corporation constitutes a breach of fiduciary duty owed to the corporation only if: (1) the breach of fiduciary duty results in fraud by the corporation, (2) the lawyer has attempted to, but has been unable to, dissuade the corporation from committing the fraud, and (3) the lawyer has reason to believe that revealing the confidential information is necessary to prevent the fraud. Any such disclosure must be limited in manner and content to the minimum that the lawyer believes is necessary to prevent the fraud.