

**JULY 1998 CALIFORNIA BAR EXAMINATION
ESSAY QUESTIONS AND SELECTED ANSWERS**

Professional Responsibility

QUESTION

Attorney Ann is a member of the Board of Directors of Californians Against Poverty (CAP), a non-profit corporation. Two years ago, CAP received a grant from the Department of Labor to provide computer training to unemployed individuals. The Department of Labor now wants to audit CAP's books to verify the grant expenditures. CAP's executive director, Dave, has taken the position that CAP's books are confidential and has refused to allow the audit.

Since Ann is the only attorney on the Board of Directors, Dave asked her to assist him in presenting the issue to the CAP Board of Directors. Ann concluded that an argument could be made that the audit request is too broad and is not specifically authorized by the grant documents. However, in the course of discussing the proposed audit, Dave informed Ann that the real reason he opposed the audit was that he used grant funds to purchase two personal computers for his children to use at home. This is a violation of the terms of the federal grant and, arguably, a violation of federal criminal statutes.

At the next meeting of the CAP Board of Directors, Dave presented the matter without making any mention of any misuse of funds. Ann said nothing, and the Board adopted a resolution opposing the audit. Dave then asked Ann to represent CAP on a *pro bono* basis to file an action against the Department of Labor to enjoin the audit.

1. What, if any, ethical issues are raised by Ann's role both as an attorney and a member of CAP's Board? Discuss.
2. Is Ann ethically required to disclose to the Board Dave's misuse of funds? Discuss.
3. Can Ann ethically represent CAP on a *pro bono* basis in a suit to enjoin the audit? Discuss.

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ANSWER A

Ann is an attorney and sitting as a board member on a nonprofit corporate board. Even though it does not appear that Ann is functioning as counsel to CAP, she is obligated as an attorney to conform her behavior so as to not violate her ethical obligations.

1. CONFLICTS BETWEEN BEING BOTH ATTORNEY AND BOARD MEMBER.

As is further discussed below, and as is fully evidenced by the facts of this question, an attorney sitting on a board risks violating a number of ethical obligations.

a. Loyalty.

An attorney owes a duty of loyalty to his or her client. If an attorney is a board member, it is possible that other board members or the corporation might think the attorney represents them. As in this situation, Ann owes a loyalty to the corporation as a result of her fiduciary duties as a board member. These fiduciary duties might conflict with duties owed a client.

b. Confidence.

An attorney owes a duty of confidence to his or her client. If information comes to the attention of a board member who is also an attorney that must be acted upon, a party who thinks that attorney represents him or her might think the attorney has violated this duty of confidence.

This is the exact problem here. Dave talked with Ann and in that conversation told Ann that he had misused grant moneys. In effect, Dave admitted to a crime. Dave might think Ann will keep this information confidential. To do so, however, would violate her duty to the board and to the corporation, as is more fully discussed below.

c. Confusion over Actual Client.

As might be the case here, as is fully discussed below, where a board member such as Ann is also an attorney, an officer of the corporation, like Dave, might think Ann is his personal attorney. To the extent Dave or someone like Dave communicates with Ann and thinks the communications are confidential but in fact conflict with the corporation's best interests, a conflict arises. This is further addressed below.

d. Duty of Candor and Decorum.

In Ann's official duties as board member, she might obtain information that might be detrimental to the corporation or its activities. Yet, in dealing with parties outside the corporation, Ann, as an attorney, has a duty of candor, truthfulness and decorum. As is discussed below, this presents a conflict for Ann in this fact pattern.

2. ANN'S ETHICAL OBLIGATIONS REGARDING DAVE'S DISCLOSURE

a. Ann's Duties as a Board Member to CAP.

Ann is a member of the board of directors of CAP. She is not acting as their counsel, although she is an attorney and is bound to her ethical obligations as an attorney even in this function.

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As a member of the board, Ann owes a duty of care and loyalty to the board. As such, she is required to exercise reasonable care in the execution of her duties as a board member.

Ann has obtained information which is detrimental to CAP. As a board member, she is required to pursue this matter; she cannot simply ignore it. Assuming the information she obtained is not privileged, as is discussed below, Ann has an obligation and duty as a board member, not as an attorney, to bring this matter to the attention of the board members and to take actions as are appropriate.

As a member of the board who has been made aware of a criminal act by the corporation's executive director, she must take whatever steps are necessary to insure that the board members themselves are not held liable (which could happen if proper steps are not taken and their inaction is viewed as ratification).

The Board further might be affirmatively obligated to disclose this information to either the Labor Department or criminal authorities. This might conflict with Ann's duties as an attorney (noted below).

b. Ann's ethical obligations to Dave as an attorney.

An attorney owes a duty of confidence to his or her client. Any confidential information obtained from the client or in the course of representation is to be maintained as confidential. The privilege is held by the client.

c. Is Dave a Client?

It is not clear from the facts whether or not Dave thought he was discussing the matter with Ann as a board member or whether he was talking with her as an attorney. If Dave thought he was talking with Ann as an attorney, there is a further complication because we don't know if Dave thought of Ann as his attorney or as the attorney for CAP.

d. To Whom is the Duty of Confidence Owed?

If Dave thought he was talking with Ann as his attorney, he might think his communications are privileged. Even if he thought he was talking with her as counsel for CAP, he might consider that his position of executive director afforded him the privilege of confidence. However, Ann, if attorney for anyone, is attorney for CAP (and even that is questionable).

e. Inherent conflict Between Corporation and Dave.

If Ann owes Dave a duty of confidence because he thought she was his attorney, Ann will violate her duty as a board member. If, however, Ann is attorney for CAP, she has no choice but to bring Dave's confessions to the board's attention, thereby violating what Dave might have perceived as his privileged communications. This, as is discussed above in #1, is the problem with being an attorney on a board of directors.

f. What should Ann have done?

Ann should have immediately told Dave that she was functioning as a board member, not an attorney, and that her duty was to the corporation. Alternatively, she should have told Dave

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that she represents the corporation, not Dave as the executive director, and that he should seek his own counsel.

g. What can Ann do?

Under California law, Ann, as attorney, cannot report Dave's crimes because the exception exists only for crimes that will cause seriously bodily injury or death.

Ann should report her information to the Board and affirm to the Board that she is a board member, not the corporation's attorney. She should suggest that CAP obtain outside counsel. And she should not represent CAP in its attempt to enjoin the audit, as is discussed below.

Ann might also be required to resign her post as board member to avoid potential additional conflicts.

3. Ann owes a duty of confidence and loyalty to a client, whether or not that client pays her for her fees or the work is done *pro bono*. In addition, Ann owes a duty of candor and decorum to other parties, including opposing parties and the courts.

a. Duties to PAC.

Were Ann to undertake representation of CAP on a *pro bono* basis and attempt to enjoin the audit, she would be required to maintain as confidential attorney-client communications. This means that she would not be able to disclose the information she has obtained from Dave concerning his misuse of grant funds which not, only violates the terms of the federal grant but also constitutes a crime.

However, Ann also has a duty of truthfulness and fairness, and is prohibited by the ethical rules in California from advising, assisting or facilitating criminal activity. Were Ann to undertake the representation of CAP and attempt to enjoin the audit, she would be, at the least, covering up a crime. She might even be aiding and abetting a crime. Accordingly, her representation would violate her ethical duties to PAC and would create a conflict of interest. She should not undertake the representation.

b. Duties to Third Parties.

In addition to violating ethical obligations to her client, representation of CAP to enjoin the audit would violate her duties of candor and decorum to opposing counsel and the tribunals. In order to seek an enjoinder, Ann would have to fabricate reasons other than Dan's misuse of grant funds to support the petition. It would be nearly impossible for Ann to seek to enjoin the audit without violating her duties of candor and fairness to opposing counsel. Even though we are told that Ann could make an argument that the request was too broad and not specifically authorized, which might not be frivolous, the fact that Ann knows the real reason for opposing the audit negates her candor and truthfulness.

In addition, counsel is required to not make frivolous arguments to the courts. Knowing, as Ann does, that the real reason for not wanting the audit is to avoid discovery of misused funds, any argument to support the enjoinder would be frivolous, if not untrue.

For the reasons noted above, Ann cannot ethically represent CAP.

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ANSWER B

1. Ethical Issues Raised by A's Role as attorney and member of board

Attorneys may participate in nonprofit organizations so long as participation doesn't conflict with the interests of any clients.

While acting as a member of the board an attorney, as any director, must exercise reasonable care of an ordinary person under similar circumstance, in good faith and in the best interests of the corporation.

A director also has a duty of loyalty to deal fairly with the corporation and fully disclose any conflicts.

An attorney may not serve as a board member while at the same time representing the organization as one of its constituents because the potential for conflict of interest unless attorney reasonably believes no conflict, and all parties consent in writing. An attorney may not seek consent where a disinterested attorney would conclude consents should not be given.

So long as A was merely operating as a board member there were no ethical problems; when D asked for A's assistance because of her status as an attorney a conflict was created.

2. Duty of disclosure to Boards:

As a board member A owes the corporation a duty of care and a duty of loyalty.

The duty of care requires that A act in good faith, in the best interests of the corporation, and exercise the standard of care a reasonably prudent person would under similar circumstances. If A in good faith believed that an audit was not in the best interests of the corporation, then it was appropriate for her to argue to assist D in presenting the issue to the board of directors.

A duty of loyalty requires that the director act in a fiduciary capacity of fair dealing and full disclosure. When A became aware that D had misappropriated funds from the corporation, A had a fiduciary duty in her role as director to disclose this information to the rest of the board or insist that D do so. By allowing D to present the matter to the board without disclosing the true facts and allowing the board to take actions on the basis of inaccurate information A breached her fiduciary duty of care and loyalty to the corporation and may be personally liable for damages.

A's duties as an attorney potentially conflict with her duties as a director. When D asked A's help to ascertain the corporations duty to allow an audit, he, as a director, was asking for A's legal opinion. Accordingly, it could be argued that A was performing as the organization's attorney.

The attorney represents the organization through its duly appointed constituents. Here, through director Dave. Communications regarding representation through such constituents are subject to the duty of confidentiality. Here, D's disclosure and regarding misappropriation.

When the attorney discovers employee of organization is pursuing illegal conduct that may be attributed to the organization, attorney must ask person to reuonsi6er, refer matter to higher authority and if that fails, withdraw. Here, D's acts constituted a violation of the federal grant and possibly a violation of federal law. Because the grant was issued to the corporation,

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D's acts would be attributed to the corporation. A should have asked D to return property and/or referred matter to a higher authority by possibly disclosing matter to board. However if D, as executive director, is considered the highest authority, A should have withdrawn.

D may argue that the attorney-client relationship existed between A and D. Argument will likely fail because her first responsibility to corporation. But if attorney-client relationship created A had a duty to withdraw as a director because an inherent conflict of interests – D's illegal actions attributable to corporation, and took property belonging to corporation.

As D's attorney, A may not counsel or assist fraudulent conduct but may make good faith effort to ascertain scope and validity of law.

A would also have a duty to protect D's confidences and could not disclose to board. But also may not fail to disclose fact necessary to avoid assisting a fraud. Here, A assisted in D's fraud by attending board meeting and remaining silent. Should have withdrawn as director if acting as D's attorney or require D to obtain separate attorney.

3. Representation of CAP (See earlier analysis)

Again A's duties as a director of the corporation conflict with A's duties as an attorney.

As a director, A has a duty of care and a duty of loyalty to disclose any conflicts.

As an attorney, A must observe a duty of confidentiality. And here, as an attorney, A cannot in good faith participate in this suit because she would be assisting in D's fraudulent conduct, would be allowing an employee to take illegal action that could be attributed to corporation and breaching duty of fairness to others. She may also use means consistent with truth and justice.