ETHICS IN THE AGE OF UN-INCORPORATION: A RETURN TO AMBIGUITY OF PRE-INCORPORATION OR AN OPPORTUNITY TO CONTRACT FOR CLARITY?

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In this article, Professor Painter examines the scope of an attorney's professional responsibility in the age of un-incorporation. Judicial opinions and Model Rules defining the responsibilities of attorneys representing incorporated entities are inadequate, he argues, when employed in the context of un-incorporation. Without guidance from case law or rules, attorneys and clients confront many of the same dilemmas which they confronted in the pre-incorporation era when business was done principally through partnerships, trusts, and other unincorporated entities. The fluidity of the un-incorporation framework, however, renders rule making and judge-made law difficult.

Instead of relying on rules and scarce case law, Professor Painter urges the use of private ordering—where lawyers and clients contract with each other ex ante—determining before entering into representation of an unincorporated entity what the attorney's ethical responsibilities will be, and to whom she owes them. By contracting for clarity in an un-incorporation relationship, attorneys can protect themselves from ethical quandaries and avoid the ambiguities that plagued the era of pre-incorporation.

The age of un-incorporation presents both a problem and an opportunity in the field of professional responsibility. The problem is that the ethical obligations of lawyers representing unincorporated entities are uncertain. This ambiguity harkens back to an earlier pre-incorporation era when lawyers were retained principally by individuals and groups of

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individuals, not entities, and when lawyers were often confused as to which individuals behind an enterprise were in fact their clients. One of the most famous lawyers to confront this ambiguity was Louis Brandeis, who tried to solve this and other conflicts in his law practice with his intuitively appealing, if only marginally useful, concept of "lawyering for the situation."[1] Today, lawyers representing partners, joint venturers, and participants in other unincorporated entities are often still viewed as representing the individuals behind these entities, rather than exclusively representing the entities themselves. However, exactly which individuals the lawyers represent is often ambiguous.[2]

The later age of incorporation brought some clarity to lawyers' obligations by elevating a client entity, itself a legal person, above the interests of its individual shareholders, officers, and directors. Incorporation created a client entity that lawyers could purport to represent, while professing not to represent the individuals behind it. The ABA's Model Rules of Professional Conduct now embrace this concept of entity representation,[3] although the specific professional responsibilities of lawyers representing corporations sometimes remain unclear.[4] Two nagging questions in the age of un-incorporation are whether the supremacy of the entity as client could disappear, and, if so, whether the pre-incorporation ambiguity of representing individuals and groups of individuals behind business enterprises could return.

The opportunity created by the new age of un-incorporation grows out of a possible response to this problem. Lawyers, individual owners, and managers behind unincorporated entities could define the lawyer-client relationship through private ordering ex ante rather than rely on public ordering to define that relationship in judicial and bar association

1. *See generally* Richard W. Painter, *Contracting Around Conflicts in a Family Business: Louis Brandeis and the Warren Trust*, 8 U. CHI. L. SCH. ROUNDTABLE 353, 353–54 (2001); *see infra* text accompanying notes 9–14.

2. In some cases, a lawyer representing a partnership is assumed to represent at least some individuals behind the partnership. *See* Prisco v. Westgate Entm't, Inc., 799 F. Supp. 266, 272 (Conn. 1992) (granting motion by former general partner in a limited partnership to disqualify a law firm from representing limited partners in a dispute with the former general partner on the grounds that the law firm had previously been general counsel to the limited partnership and had drafted the partnership agreement). In other circumstances, representation of individuals behind a partnership while representing the partnership itself is an impermissible conflict. *See* Braumstein v. Statewide Grievance Comm., No. CV9904973N8S, 2001 Conn. Super. LEXIS 462 at *26 (Conn. Super. Ct. Feb. 9, 2001) (affirming Grievance Committee finding that lawyer violated Rule 1.7(a) where lawyer simultaneously represented a limited partnership and its general partner in his individual capacity, when the personal interests of the general partner were at odds with the interests of the limited partner investors).

3. *See* MODEL RULES OF PROF'L CONDUCT R. 1.13 (organization as client) (specifically stating that the lawyer for an organizational client represents the organization, not its individual constituents such as managers or shareholders).

4. As recently as 2003, for example, controversy continued within the ABA over when a lawyer must report known illegal conduct to the board of directors or other highest authority within an organizational client, and Model Rule 1.13 remained unclear on this point. Indeed, the ABA only revised Model Rule 1.13 in 2003 to clarify this issue after Congress imposed an "up-the-ladder" reporting requirement on securities lawyers under the Sarbanes-Oxley Act of 2002. *See infra* text accompanying notes 51–53.

opinions. Without definitive case law, ethics opinions, or other precedent specifying what a lawyer's obligations are in the context of un-incorporation, public ordering is at a disadvantage, and lawyers presumably should encourage clients to contract for their own solutions ex ante rather than submitting to an uncertain ex post determination of the lawyer's professional responsibilities. Private contracts that define professional responsibilities of lawyers for unincorporated entities could bring clarity to the age of un-incorporation; indeed more clarity than public ordering has, through decades of judicial decisions and ethics opinions, supplied to corporations. If lawyers and clients in the age of un-incorporation contractually define their relationships more often, legal representations will more closely correspond with expectations of both lawyers and clients, and there should be less litigation over conflicts and other matters. Only time will tell whether this contractarian vision of lawyers' ethics in the age of un-incorporation will prevail, or whether public ordering will, as it did in the age of incorporation, slowly and unpredictably, but eventually, prevail in establishing norms of professional ethics that most lawyers and clients presume to be immutable.

I. ETHICS IN THE AGE OF PRE-INCORPORATION

The corporate form has been recognized in England and the United States for centuries. The corporate form, however, has not always been easy to use. The Bubble Act of 1720, for example, required an Act of Parliament to establish a corporation.[5] Before the early twentieth century, some states denied limited liability to, or refused to recognize, shareholders of foreign corporations doing business within their borders.[6] The corporate form, largely because of its limited liability feature, was also viewed as suspect by private parties, and many businesses resorted to other forms of organization. Sometimes a partnership was used, but variations on the trust, and for family enterprises the dynastic trust, were also popular.[7] Sometimes a lawyer's ethical obligations in representing

5. An Act to Restrain the Extravagant and Unwarrantable Practice of Raising Money by Voluntary Subscriptions for Carrying on Projects Dangerous to the Trade and Subjects of This Kingdom (Bubble Act), 6 Geo. 1, c. 18 (1719) (Eng.).

6. *See generally* Arthur M. Alger, *Consequences of Illegal or Ultra Vires Acquisition of Real Estate by a Corporation*, 8 HARV. L. REV. 15, 16 (1894–95) (describing and criticizing "[t]he view expressed, either directly of inferentially, in the authorities in question, that corporate realty unlawfully acquired may be seized by the State"); Arthur M. Alger, *The Doctrine of Public Policy as Applied to Ownership of Real Estate by Foreign Corporations*, 9 HARV. L. REV. 91 (1895–96) (describing state statutes that prohibit a foreign corporation from taking or holding land within its borders and the prospect of judge-made law imposing a similar prohibition); Jesse W. Lilienthal, *Non-Public Corporations and Ultra Vires*, 11 HARV. L. REV. 387 (1897–98) (describing legal consequences of a corporation exceeding the powers granted in its charter, including in some jurisdictions forfeiture of the charter); George Wharton Pepper, *The Unauthorized or Prohibited Exercise of Corporate Power*, 9 HARV. L. REV. 255 (1895–96) (describing the ultra vires doctrine and its impact on the enforcement of contracts against a corporation and hence on the ability of a corporation to contract).

7. *See generally* Lawrence M. Friedman, *The Dynastic Trust*, 73 YALE L.J. 547, 554–55 (1965).

such entities and their owners and managers were clear, but often they were not.

A poignant example of muddled ethical obligations in the age of pre-incorporation was Louis Brandeis's representation of the Warren Trust (Trust) from 1889 to 1910. Brandeis designed this dynastic Trust to run a large paper mill in Maine and to be inherited by Samuel Warren,[8] Warren's mother, and his four siblings.[9] Brandeis set up the Trust with three trustees: Sam, Sam's mother, Mrs. Warren, and a cousin, Mr. Mason. Brandeis represented the Trust and apparently also represented Sam in his capacity as trustee. In order for Sam to run the paper mills (trust law apparently prohibited him from paying himself for doing so in his capacity as trustee of the Trust), Brandeis set up a separate operating firm owned by Sam, Sam's brother Fiske Warren, and Mr. Mason. The firm would lease the paper mills from the Trust, pay rent to the Trust contingent on the profits of the business, and distribute the remainder of its profits to its principals as compensation for their work. The Trust in turn would make distributions to its beneficiaries who, as passive investors, did not want to participate in operating the paper mills. Two entities, the Trust and the firm, were thus required to operate the business, compensate the persons who operated it, and distribute profits to its owners. Sam Warren, because he was both a trustee of the Trust and a principal of the firm, faced a potential conflict which, apparently, was consented to by the various members of the Warren family. Brandeis also faced a potential conflict because he represented both the Trust and the firm even though they were on opposite sides of the lease. Members of the Warren family apparently consented to Brandeis's conflict as well (although not in writing). What was not clear was whether Brandeis also represented the members of the Warren family in their individual capacities. He probably did not represent them all individually as Trust beneficiaries, although he drafted a will for one of Sam's brothers, Ned Warren, and there was no written clarification of whether Brandeis represented the Trust beneficiaries individually.[10]

These entities that Brandeis cobbled together for the Warren family functioned relatively smoothly for over fifteen years. Trouble started, however, when Ned demanded increased distributions from the Trust to satisfy his insatiable appetite for collecting antiques in Europe. Sam's dispute with Ned had much to do with sibling rivalry. The brothers also disagreed over matters of business judgment such as whether more profits should be reinvested in the business for the benefit of future generations, as Sam wanted, or instead be distributed to the Trust beneficiaries. When Ned was still unsatisfied, he became convinced that Sam was self-

8. Samuel Warren was Brandeis's law partner and his coauthor of the famous "Right to Privacy" article in the Harvard Law Review.

9. *See* Painter, *supra* note 1, at 355.

10. *Id.* at 371–77.

dealing in his dual roles as trustee of the Trust and principal in the firm. In 1910, Ned sued Sam. In the middle of a grueling trial in 1910, Sam shot himself after days of giving testimony, and the matter was settled by the remaining members of the Warren family who hoped it would come to rest.[11]

Sam's situation would have been easier had he been chief executive officer, and perhaps a director, of a corporation—a form of organization in which managers are fiduciaries for shareholders but which is also flexible enough to allow a certain degree of self-interested behavior by managers. In the corporate context, Sam would have been compensated directly by the corporation acting through its board of directors, instead of through a mechanism much more prone to self-dealing accusations: a separate firm under his control that transacted with a trust of which he was a trustee. Most of the issues that Sam and Ned disagreed about also would have been subject to the presumption of the business judgment rule rather than the very strict prohibition on conflicts of interest in the law of trusts.[12] Warren family members who did not like the way the corporation was being run, by majority vote, would have been able to replace Sam as a director at the next shareholders' meeting, a governance feature not available in a trust (the Warren Trust had self-perpetuating trustees). In the pre-incorporation context, the principal remedy for passive investors thus lay in court rather than in the Trust's governance structure; they could sue for breach of fiduciary duty, and trustees charged with self-dealing were judged by a very strict standard.[13]

Brandeis was not named in the suit and was never subjected to a formal allegation of conflict of interest or a motion to disqualify, even though his law firm represented Sam against Ned (another potential conflict if he had in fact represented Ned in connection with the Trust). In 1916, however, the entire episode was brought up, along with other ethics allegations, by Brandeis's opponents at his confirmation hearings for the Supreme Court. His dual representation of the Trust and the firm was alleged to breach professional standards, even though the Warren family members had probably consented. The issue of whether Brandeis's firm could defend Sam in his role as Trustee against Ned's lawsuit also came up. Anti-Semitism perhaps colored the way Ned's Boston lawyers described Brandeis's role in the transaction to the Senate Judiciary Committee. The full Senate, possibly seeing through the motives of Brandeis's accusers, confirmed his nomination to the Court by one vote.[14]

Brandeis's role, like Sam's, would have been clearer had the business been set up as a corporation. Instead of representing a Trust and a firm, and perhaps also the individuals behind these entities, Brandeis

11. *Id.* at 369–71.
12. *Id.* at 364–66.
13. *Id.* at 363.
14. *Id.* at 354, 373–78.

would have had a single entity as his client. He would have represented the corporation with Sam as an officer directing the representation under the supervision of a board of directors annually elected by the Warren family shareholders. Unless Sam was clearly breaching his fiduciary duty, a matter that Brandeis would have had to have taken up with the directors, Brandeis would have been relatively safe following Sam's directions. Only if the directors themselves insisted on a clear breach of Sam's fiduciary duty, or in ignoring Sam's breach, might Brandeis have to resign. Otherwise, so long as Brandeis did not also represent Sam individually, as well as the corporation, most of the conflicts problems that plagued this representation would have been avoided.

II. ETHICS IN THE AGE OF INCORPORATION

Later in the twentieth century, the Warrens' paper mills probably would have been run as a corporation, a single entity that could have done the work of both the Trust and the firm. Although Brandeis's life would have been easier, the age of incorporation has not been a panacea for lawyers' ethics. One area of continued confusion arises when investors who are previously clients of a lawyer form a new corporation or convert a partnership into a corporation. It is not always clear whether the lawyer represents the individuals, the corporation, or both.[15] Confusion also arises over whether the lawyer for a corporation also represents parent, sibling and subsidiary corporations.[16] Confidentiality also is a concern when shareholders demand access to communications between a corporation and its lawyers, access which is often, but not always, granted in the close corporation context and more often than not denied in the context of a large public corporation.[17] Yet another area of difficulty has been lawyer response to corporate fraud.[18] Although corporate statutes are clear that directors, not officers, are the legal authority in charge of a corporation, it took until 2003 for the ABA to recognize in Model Rule 1.13 that a lawyer for a corporation must report unrectified criminal acts

15. *See* Lawrence E. Mitchell, *Professional Responsibility and the Close Corporation: Toward a Realistic Ethic*, 74 CORNELL L. REV. 466, 466–509 (1989).

16. *See generally* Charles W. Wolfram, *Corporate-Family Conflicts*, 2 J. INST. FOR STUDY LEGAL ETHICS 295 (1999) (discussing the lateral and lineal dimensions of the client-identify problem in corporate families).

17. *See* Garner v. Wolfinbarger, 430 F.2d 1093, 1104 (5th Cir. 1970) (articulating a "good cause" exception to a corporation's attorney-client privilege under which shareholders in suits accusing a corporation of acting against their interests have an opportunity to show good cause why the privilege should not be invoked).

18. Richard W. Painter & Jennifer E. Duggan, *Lawyer Disclosure of Corporate Fraud: Establishing a Firm Foundation*, 50 SMU L. REV. 225, 261–63 (1996) (discussing lack of clarity in this area and proposing legislative provisions resembling the subsequently enacted section 307 of the Sarbanes-Oxley Act).

and fraud to its directors[19]—and this was only after Congress mandated the same in section 307 of the Sarbanes-Oxley Act of 2002.[20]

The age of incorporation thus has by no means eliminated confusion surrounding the ethical obligations of lawyers representing corporations. Part of the problem is that public ordering has sought to define the lawyer's ethical obligations with one-size-fits-all rules such as the ABA's Model Rule 1.13. Because particulars differ depending on the representation, these rules have been worded so generally that many questions of professional responsibility are left to ex post determination, usually by judges but occasionally by bar disciplinary boards. Conflicts rules worded as if they applied to individual clients are applied to corporate representations, and these rules also are very general.[21] Here also, much is left to ex post adjudication, perhaps to the benefit of law professors opining as expert witnesses on conflicts and other matters of legal ethics, but hardly to the benefit of the lawyers and clients subjected to these uncertainties.

This author has suggested elsewhere that corporate representation could improve significantly if ethics rules were the subject of more ex ante contracting between lawyers and their clients.[22] This is true for rules on whistle-blowing in response to corporate fraud,[23] conflicts rules,[24] and rules governing the scope of a representation and lawyer use of client information, and other rules.[25] Although corporate clients contract with their lawyers more frequently now than they used to,[26] the contractarian paradigm is relatively weak in the field of legal ethics. Lingering doubts about the enforceability of such contracts, even with sophisticated clients, and doubts about whether seeking to contract around ethical obligations is itself unethical, continue to give a strong advantage to public ordering, however vague the rules it chooses to impose.

Despite these and other problems with corporate representation, however, ethics questions are simplified by the fact that there is a generally agreed upon analytical starting point: a corporation is an independ-

19. *See* Thomas D. Morgan, *Sarbanes-Oxley: A Complication, not a Contribution, in the Effort to Improve Corporate Lawyers' Professional Conduct,* 17 GEO J. LEGAL ETHICS 1, 22 (2003) (criticizing Congress for enacting this up-the-ladder reporting rule).

20. *Id.* at 15, 16.

21. *See, e.g.*, MODEL RULES OF PROF'L CONDUCT R. 1.7 (concurrent conflicts) and R.1.9 (successive conflicts) (2003).

22. Richard W. Painter, *Rules Lawyers Play By*, 76 N.Y.U. L. REV. 665, 666 (2001).

23. *See* Richard W. Painter, *Toward a Market for Lawyer Disclosure Services: In Search of Optimal Whistleblowing Rules*, 63 GEO. WASH. L. REV. 221, 256–57 (1995); *see also* Painter & Duggan, *supra* note 18, at 266.

24. *See* Richard W. Painter, *Advance Waiver of Conflicts*, 13 GEO. J. LEGAL ETHICS 289, 289–92 (2000).

25. *See* Richard W. Painter, *Professional Responsibility Rules as Implied Contract Terms*, 34 GA. L. REV. 953 (1999); Painter, *supra* note 22, at 708–12.

26. *See* Painter, *supra* note 22, at 680.

ent legal person entitled to the undivided loyalty of its counsel.[27] The corporation is not to be confused with the interests of the persons who manage the corporation or the individual interests of its shareholders. The corporation, like an individual client, has an expectation of confidentiality,[28] loyalty,[29] communication,[30] and representation free of conflicts from its lawyer's representation of persons having interests adverse to its own.[31] Unlike Brandeis in the Warren Trust matter, the corporation's lawyer can represent the entire business enterprise by representing only the corporation and by refusing to embroil himself in parallel roles that compromise this representation.

III. ETHICS IN THE AGE OF UN-INCORPORATION

What will happen in the age of un-incorporation? We could go back to the confusion that plagued Brandeis and his contemporaries when persons, not entities, usually retained lawyers, and entities often were not treated as legal persons entitled to legal representation apart from the individuals who owned and managed them. The member managed LLC and some other forms of un-incorporation, particularly partnership based organizations, raise this possibility. In these situations, even if the entity is recognized as a separate legal person, its managers and owners are sometimes one and the same. A court may determine, and perhaps rightly so, that the intent of the owners and managers of the entity was that the lawyer would represent them all. Once, however, conflicts and other ethics questions turn on individuals' intentions and other factual considerations rather than on strong presumptions arising out of the organizational form itself, confusion is likely. On the other hand, rules tied to a specific organizational framework may not work because there are so many different forms of un-incorporation and because most of these forms allow significant deviation from statutory norms in the articles of organization, operating agreement, or other governing instrument.[32] The confusion that public ordering has been unable to eradi-

27. *See generally* Sanford A. Schane, *The Corporation is a Person: The Language of a Legal Fiction*, 61 TUL. L. REV. 563 (1987).

28. MODEL RULES OF PROF'L CONDUCT R.1.6.

29. MODEL RULES OF PROF'L CONDUCT R.1.3.

30. MODEL RULES OF PROF'L CONDUCT R.1.4.

31. MODEL RULES OF PROF'L CONDUCT R.1.7, 1.9, 1.10.

32. These include the Limited Liability Company (LLC), the Limited Liability Partnership (LLP), the Limited Liability Limited Partnership (LLLP), and various forms of statutory trusts, new and old. The statutes governing these various entities contain a large number of default rules that organizers can contract around in organizational agreements if they wish. Statutes for these unincorporated entities are also designed to give organizers maximum contractual freedom. In its LLC statute, for example, Delaware provides a forum selection clause, absent from the Delaware General Corporation Law, which specifically allows members or managers to agree in the LLC agreement, or in another writing, for arbitration of claims under the agreement. *See* DEL. CODE. ANN. tit. 60, § 18-109(d) (2004) ("In a written limited liability company agreement or other writing, a manager or member may consent to be subject to the nonexclusive jurisdiction of the courts of, or arbitration in, a specified jurisdiction, or the exclusive jurisdiction of the courts of the State of Delaware, or the exclusivity of arbi-

cate from the age of incorporation could pale by comparison with the potential uncertainties each time an unincorporated entity retains a lawyer without clarifying who the client is and how the lawyer's specific responsibilities to that client are to be performed.

A. Existing Commentary and Case Law

So far, the ethical obligations of lawyers in the un-incorporation context are not very clear. Relatively sparse academic commentary[33] and practitioner materials[34] tend to focus on the role of lawyers in representing the individuals who set up an LLC or other unincorporated entity at the formation stage. In situations where the lawyer is retained before the entity itself even exists, entity representation is at this stage precluded, and these commentators are right to point out that the lawyer must make clear whether he is representing all of the organizers of the entity or just some of them.[35] More difficult questions, however, arise once the entity is formed. First, it must be decided whether the lawyer who originally represented some or all of the organizers now represents the entity alone or also represents some or all of its organizers. This question might, or might not, be answered differently if the entity is represented by a new lawyer having no prior relationship with the organizers. Even if the lawyer represents the entity alone, is the lawyer necessarily precluded from representing some of its organizers at some later point in time? Second, it must be decided what specific obligations arise from the lawyer's representation of the entity. From whom shall the lawyer take instructions, with whom shall the lawyer share confidences, and to whom shall the lawyer report concerns about illegal activity or breaches of fiduciary duty?

The little case law that exists on these questions is confusing. Perhaps most problematic is the fact that courts seem reluctant to treat unincorporated entities as separate persons that can alone be represented

tration in a specified jurisdiction or the State of Delaware . . . ."). The Delaware Supreme Court interpreted this provision broadly in *Elf Atochem North America, Inc. v. Cyrus A. Jaffari and Malek LLC*, 727 A.2d 286 (1999), emphasizing that freedom of contract is an essential element of the Delaware LLC statute. '"The Act's basic approach is to permit partners to have the broadest possible discretion in drafting their partnership agreements . . . . "' *Id.* at 291 (quoting MARTIN I. LUBAROFF & PAUL M. ALTMAN, DELAWARE LIMITED PARTNERSHIPS, § 1.2 (1999), and stating that this same "observation relating to limited partnerships applies as well to limited liability companies.").

33. *See e.g.*, Robert R. Keatinge, *The Implications of Fiduciary Representations in Representing Limited Liability Companies and Other Unincorporated Associations and Their Partners or Members*, 25 STETSON L. REV. 389 (1995). For more general discussion, see John S. Dzienkowski, *Lawyers as Intermediaries: The Representation of Multiple Clients in the Modern Legal Profession*, 1992 U. ILL. L. REV. 741 and Alysa C. Rollock, *Professional Responsibility and Organization of the Family Business: The Lawyer as Intermediary*, 73 IND. L.J. 567 (1998).

34. *See e.g.*, John M. Cunningham, *The Professional Responsibilities of Lawyers Who Represent Multiple Clients in LLC Formations*, *at* www.Cunningham-Seminars.com; John A. Reed, *Ethical Issues In Business Law Practice* (2003), *at* www.wlaw.com/Reed.

35. The importance of clarifying this in advance is made clear in all of the articles cited in *supra* notes 32–34.

by counsel. *Chaiklin v. Bacon*[36] is an example of how easy it is for courts to hold that a lawyer's fiduciary obligations to an unincorporated client flow through to an individual member, even absent evidence that the lawyer represented that individual member in connection with the entity. Here, the plaintiff was independently represented by private counsel during his negotiations with Boise LLC for a buyout of his interest in a dissolution of Boise that he had requested.[37] The Superior Court in Connecticut still disqualified a different attorney who had previously represented Boise LLC from representing its remaining members in litigation over the sale of Boise's assets and the buying-out of the plaintiff's interest.[38] Even though there was insufficient evidence from which the court could conclude that the Boise attorney had been involved in the formation of the company—the time period during which its members would have had the greatest expectation that the attorney was representing each in their personal capacity[39]—the court held that the attorney could be disqualified from representing the remaining members of Boise in this dispute over their alleged breach of fiduciary duty to the plaintiff.

> [W]hile [the attorney] represented Boise he also must be seen to have represented the interests of the plaintiff concerning his membership in that partnership, pending perfection of his contract for discharge . . . . Until the completion of the plaintiff's discharge from Boise then, while he remained a member in fact, if not a member in name, of that company, the plaintiff was entitled to the fiduciary obligations of [the lawyer], who served as Boise's attorney.[40]

The court cited Rule 1.13 of Connecticut's rules of professional conduct in support of this holding,[41] even though the Connecticut Rule, like the ABA's Model Rule 1.13, concerns the lawyer's obligations to the organizational client itself, not to its individual constituencies. Nowhere does Rule 1.13 state that fiduciary obligations owed to an entity flow through to its individual members. Indeed, Rule 1.13 emphasizes that the lawyer is not the personal attorney for the organization's various constituents and should favor the interests of the organization over the interests of those constituents. Rule 1.13 arguably might be a basis for disqualifying an attorney from representing some members of an LLC in a dispute over buying out another member, but disqualification under Rule 1.13 should require that the proposed representation of the remaining members be adverse to the LLC as an entity, not simply adverse to the interests of one of its former members. The court's equation of Boise's interests with the interests of its individual members is made even more

36. No. CV990594039, 2000 Conn. Super. LEXIS 1729 (Conn. Super. Ct. July 3, 2000).
37. *Id.* at *6.
38. *Id.*
39. *Id.*
40. *Id.* at 22–24.
41. *See id.*

transparent by the court's reference to Boise as a "partnership" even though it was in fact an LLC.[42]

Even absent a finding of a client relationship with individual members of an LLC, a court might still assume that the attorney for the LLC has a heightened duty to disclose information to members, and may hold the attorney liable if he does not. In *Exposition Partners, LP and ICMC Investors, LLC v. King, Leblanc & Bland LLP*,[43] a Louisiana court held that the lawyer for an LLC could be sued for fraud by Exposition Partners when the partners of Exposition mistakenly believed that Exposition had become a member of the LLC.[44] Because Exposition's partners were themselves members of the LLC, they had the right to expect disclosure by the attorney to them of whether Exposition had in fact been made a member of the LLC, as the other defendant members of the LLC apparently misrepresented to Exposition that it had:

> Because the law classifies CRG [LLC] as a distinct business entity, [the defendants, CRG's lawyers] allege that at no time were they retained to represent [CRG's members] Mr. Ryan, Exposition or ICMC. Nevertheless, CRG can only act via Messrs. Dawley, McPhail, Ryan, etc. The premise of the defendants' argument is that representing CRG posed no conflict of interest *vis a vis* the distinct members of CRG.[45]

In rejecting the defendants' argument, the court held that the lawyers could be liable for fraud allegedly committed by some of CRG's members against others, if the lawyers negligently furthered the fraud by acts such as incorrectly naming Exposition as a member of the LLC on official correspondence: "Without proving fraud, the fact that ICMC was excluded and Exposition was included in CRG's official correspondence gives it [Exposition] a right to allege fraud or that it was being misled, even if in fact this amounted to nothing more than documentary confusion."[46]

The most troubling aspect of the *Exposition* holding is that, while the court does not directly say so, it assumes a greater duty to communicate with individual members of an LLC, even absent a lawyer-client relationship with those members, than the lawyers themselves probably believed they had at the time. While no lawyer can sit idly by and allow some members of an LLC client to commit fraud on other members of the LLC, it is troubling to see a fraud claim against a lawyer representing an LLC predicated in part on a supposed duty to communicate to a member of the LLC specific information, particularly apart from something rising to the seriousness of the lawyer's knowledge of an impending

42. *Id.*
43. 869 So. 2d 934 (La. Ct. App. 2004).
44. *Id.* at 944.
45. *Id.* at 942.
46. *Id.* at 943–44.

fraud. If there is an affirmative duty on the part of a lawyer for an LLC to communicate all material facts to all of its members, a statute or ethics rule at least should say so ex ante rather than a court saying so ex post.

These two cases on the ethical obligations of lawyers representing unincorporated entities underscore the inadequacy of public ordering as a mechanism for defining these obligations. Basic questions remain unresolved, including when a lawyer for an unincorporated entity also represents its members, what duties the lawyer owes to those members even when there is no lawyer-client relationship, and to whom the lawyer should communicate important information about the entity. Lawyers who do not know the answers to these questions will find it difficult to effectively and ethically practice law, and their unincorporated clients, as well as the individuals behind those clients, will not know what to expect of the lawyers.

B. Private Ordering and the Opportunity to Contract for Clarity

Resolution of all of these questions is made difficult by the fact that un-incorporation is an organizational framework that is remarkably fluid compared with the more rigid and hierarchical organizational framework of corporations. Corporations for the most part all have directors, officers, and shareholders with specific statutory rights and duties, although individuals may perform more than one of these functions.[47] Some unincorporated entities are run by their members (member-managed entities). Others are run by designated managers (manager-managed entities),[48] although the method for choosing and removing these managers may differ depending on the entity. Statutes and case law seek to define precisely the function and fiduciary duties of members and managers in each context, as well as prohibitions on their conduct (such as related party transactions), but public ordering does not provide anywhere near the volume of precedent that it does in the field of incorporation. Furthermore, because unincorporated entities can differ so much from each other, precedent may not even be particularly valuable.

In the context of representing incorporated entities, as pointed out in Part II above, ethics questions have often been overlooked ex ante, and often dangerously so, because lawyers and clients far too often assume that default rules are clear, even when they are not. In the unincorporation context it should be obvious that, with legal precedent at this point being so thin, it is even more dangerous to assume that certain default rules apply. Private ordering, in which the responsibilities of the entity's lawyers are clearly defined in advance along with the rights and

47. Modern statutory provisions in some jurisdictions allow for the elimination of the board of directors in close corporations, although, perhaps because of the traditional rigidity of the corporate form, these provisions are rarely used.

48. Keatinge, *supra* note 33, at 407.

responsibilities of the entity's members and managers, has a clear advantage over blind reliance on what little clarity public ordering provides. Lawyers and clients who do not define ethics rules ex ante proceed at their own peril.

The age of un-incorporation is thus an opportunity to advance in the direction of clearer professional obligations for lawyers rather than to regress into the muddled ethics of the pre-incorporation era. At least in situations where managers and owners of an unincorporated entity are sophisticated, contracting parties should agree ex ante on questions such as whether the individual members of an entity are also the clients of the entity's lawyer, to whom the lawyer should communicate important information and other specific responsibilities of the lawyer. In this "contractarian" regime, the intent of clients and lawyers would be defined by themselves rather than by courts, and confusion, as well as subsequent litigation, over conflicts and other ethics matters would be minimized.

C. Setting the Default Rules

What, if any, default rules should public ordering supply for a regime in which it is expected that most unincorporated clients and their lawyers would contractually define the lawyers' professional responsibilities themselves? The most frequently tried approach to setting defaults would be for the rule drafter to determine what rule would satisfy the majority of lawyers and clients (a majoritarian default rule).[49] Because, however, of the wide variety in governance structures used for unincorporated entities, majoritarian default rules for one type of entity (such as a rule that the lawyer must disclose all relevant information to all members of a member-managed LLC) would not be suitable for another type of entity (for example, a large manager-managed LLC).

There could be different default rules for different types of unincorporated entities, and some of the possibilities are explored further below. Nonetheless, because of the difficulty of setting majoritarian defaults in the un-incorporation context, rule drafters should not overlook the possibility of using penalty default rules instead. These might include a rule that a lawyer for an unincorporated entity automatically also represents all of its members unless otherwise agreed, and a rule that the lawyer's duty to communicate under Model Rule 1.4 extends to all of the entity's members unless otherwise agreed. Presumably the majority of entities and their lawyers would not want these rules and would contract to avoid them. If the objective of the contractarian regime is to encourage private ordering instead of misplaced reliance on the vagaries of public ordering, penalty default rules might help accomplish this objective.

49. For discussion of majoritarian default rules in the professional responsibility context, see Painter, *supra* note 22.

Going back to possible majoritarian default rules, the most basic rule from which others flow is that which identifies the lawyer's client. The majoritarian rule would probably be the same for unincorporated entities as for incorporated entities under Model Rule 1.13: that the lawyer representing an entity represents the entity alone unless otherwise agreed (for example, the lawyer may have a prior client relationship with one of the entity's members). The case is somewhat stronger for a default rule that the lawyer also represents the individual members of smaller entities that are also member-managed, although this rule would, even in this context, probably not be favored by the majority of users because of the prospect of the lawyer having to resign in the event of a conflict between the entity and one of its members.

A majoritarian rule concerning the duties to communicate and keep confidences, like those in Model Rules 1.4 and 1.6, is particularly difficult to set. Communication of confidential information to individual members of an unincorporated entity might be expected in one case, accepted in another, and considered a breach of confidence in a third. The majoritarian rule would probably require communication with managing members (although not necessarily all of them) of a manager-managed entity and with members (although once again not necessarily all of them) of a member-managed entity. In each case, the entity could contract around the rule by designating in advance a group of managers or members with whom the lawyer is required to communicate. The majoritarian default rule might allow, but not require, communication of confidential information also to nonmanager members of a manager-managed entity;[50] if the entity wished to prohibit such communication, the entity could contract around the rule.

Concerning the identify of the person(s) from whom the lawyer should receive instructions, default rules once again are difficult to set. Model Rule 1.13 appears to impose a duty to take instructions from the individual constituent of the organization with whom the lawyer deals in the ordinary course unless the lawyer knows that the constituent is acting improperly. This is often the person who retained the lawyer on behalf of the entity (this person may or may not also personally be a client of the lawyer, a situation which often gives rise to a thorny set of conflicts). Given the nonhierarchical structure of many unincorporated entities, Model Rule 1.13's flexible approach may be the only workable default rule. In the absence of a board of directors or other supreme authority within the organization, even the revised Model Rule 1.13 provisions concerning consultation with the organization's highest authority may not always work well in the un-incorporation context. Whatever the de-

50. This would be the rough equivalent of allowing a lawyer for a corporation to communicate confidential information to shareholders who are not also officers or directors, which in a publicly held corporation is probably prohibited outside the exception for crime or fraud. *See* MODEL RULES OF PROF'L CONDUCT R.1.6.

fault rule, clients should thus specify in advance the identity of the person from whom a lawyer representing an unincorporated entity should take instructions.

This brings up a final question, which is to whom the lawyer should report fraud and breaches of fiduciary duty. Section 307 of the Sarbanes-Oxley Act and the ABA's 2003 revisions to Model Rule 1.13 provide an answer that is relatively clear in the context of incorporation: "up-the-ladder" reporting should be made first to a corporation's officers and general counsel, and if that does not work, to its board of directors.[51] The SEC rules under section 307 pay some heed to contractarian proposals by allowing the corporation ex ante to designate a committee of its directors (a Qualified Legal Compliance Committee) to whom the report can be made instead.[52] These rules also apply to lawyers for unincorporated entities, such as LLCs, that issue securities to the public.

This arrangement, however, may not work well for unincorporated entities that have no board of directors. In this context, the default rule for a manager-managed entity would probably require only a report to the managers (probably to all of them). Requiring a report also to the members would thus be a penalty default rule, although it is understandable why some clients might want such a rule. The default rule for a member managed entity would probably be a mandatory report to all of the members, if the lawyer's prior report to other constituents of the entity is of no avail. Once again, as recognized by the SEC's rules under section 307, the entity should be allowed some degree of contractual flexibility to have the report made to a special committee of managers or members that has been designated in advance and charged with the responsibility to deal with fraud, breach of fiduciary duty and similar violations.

IV. CONCLUSION

Lawyers representing unincorporated entities face uncertain default rules defining their professional obligations to individuals behind client entities. Lawyers and clients should not wait for unpredictable rules to be imposed on them by public ordering; rather they should define their lawyer-client relationships as much as possible through private ordering. Wherever possible, courts and bar associations should enforce those contracts when ruling on the professional responsibilities of lawyers for unincorporated entities.

For different unincorporated entities there are likely to be different answers to questions such as who is the lawyer's client for conflicts pur-

51. Painter, *supra* note 22, at 718.

52. A similar "contractarian" proposal—that up-the-ladder reporting to directors be required as a default rule, but that the report may be to a committee of directors designated by the corporation in advance—had in 1996 been made in Painter & Duggan, *supra* note 18.

poses, whose confidences must be kept by the lawyer and from whom, to whom the lawyer may communicate information in some circumstances, to whom the lawyer must communicate information in other circumstances, and whose instructions the lawyer should follow. If lawyers and unincorporated clients contractually define their relationships more often, the conduct of lawyers will more closely correspond with expectations of clients. There should also be less litigation over conflicts, misrepresentation, failure to follow instructions, and other matters of professional responsibility. As a result, lawyers and clients will be better off.