NEW YORK STATE BAR ASSOCIATION
One Elk Street, Albany, New York 12207 ◎ PH 518.463.3200 ◎ www.nysba.org

New York State Bar Association
Committee on Professional Ethics

Opinion 991 (11/12/13)

Topic: Lawyer's disclosure of confidential information for personal advantage

Digest: A lawyer who handles foreclosure matters in mediation and at trial desires to provide leads on desirable properties to friends in the real estate business. The lawyer must not reveal confidential information to the disadvantage of a client or to the advantage of the lawyer or a third party unless the client gives informed consent. If a reasonable lawyer would perceive a significant risk that the lawyer's own financial, business, or other personal interests will adversely affect the lawyer's professional judgment on the client's behalf, then the lawyer may not continue the representation unless the conflict is consentable and the client gives informed consent, confirmed in writing. In any event, the lawyer may not use litigation tactics that have no substantial purpose other than delay.

Rules: 1.6(a); 1.7(a) & (b); 1.8(b); 1.9(c); 3.1(a) & (b); 3.2.

FACTS

1. An associate (the "Associate") works at a law firm that represents various lenders (collectively "Lender") in foreclosure actions. The Associate's duties include such tasks as drafting motions for default judgment, reviewing applications from borrowers seeking loan modifications, and appearing at mediation conferences.

2. Some of the Associate's college friends want to form a real estate LLC (the "LLC"). The LLC would evaluate properties that are in the foreclosure process or that have already been foreclosed, and would purchase those that the LLC considers to be sound investments as rental properties. The purchases would be made either (a) in short sales (if the LLC buys a property after the summons and complaint but *before or during* the foreclosure proceedings) or (b) at foreclosure auctions (if the LLC buys a property *after* the foreclosure proceedings end).

3. The Associate's college friends have asked him to join their real estate LLC. If he agrees, they anticipate that he would use information acquired during his law practice to provide leads on properties facing foreclosure that may be sound investments as rental properties. (The Associate does not say that he would represent the LLC or perform any legal services for it, so we assume he will not.)

4. However, the Associate is concerned that his role at mediation conferences may conflict with his role in the LLC. A conflict could arise because it might be to the LLC's advantage (and

therefore to his personal advantage) either to speed up or to slow down or delay foreclosure proceedings, which might be contrary to the Lender's interest in a particular foreclosure case. In particular, the LLC might sometimes prefer to buy a property at a short sale, before the foreclosure proceedings begin or while they are pending, but might at other times prefer to buy a property at auction, after the foreclosure proceedings conclude. The Lender, however, might desire the opposite of what the LLC wants.

5. The Associate is in a position to speed up or slow down foreclosure proceedings regarding a given property because of his role in mediation conferences. In New York State, all foreclosure proceedings are effectively stayed, practically if not formally, while an action is in the mediation part. While an action is in the mediation part, Lenders must participate in good faith in one or more conferences to determine whether a borrower meets eligibility guidelines for a loan modification. If a borrower *does* meet the guidelines, then the pending or threatened foreclosure action will be settled via loan modification. If a borrower *does not* meet the guidelines (or if a borrower does not properly fill out and diligently update an application for a loan modification), then the action is released from the mediation part and the action can move forward toward foreclosure.

6. When the Associate attends a mediation conference on behalf of a Lender, his job (as he describes it) is either (a) to facilitate the loan modification process or (b) to argue that the borrower is ineligible for loan modification and that the action should be released from the mediation part so it can move toward foreclosure. The Associate independently decides which of these alternative courses to follow based on the totality of the facts and circumstances at the time of the conference.

7. If the Associate successfully facilitates the loan modification process and the case settles via loan modification, then neither a short sale nor a foreclosure auction will occur, and the LLC will have no opportunity to buy the property. But if the Associate stalls the mediation process, then the LLC may have an opportunity to buy the property at a short sale before a foreclosure auction occurs. Conversely, if the Associate persuades the mediator to release the matter from the mediation part and allow the case to continue toward foreclosure, the LLC may eventually have an opportunity to buy the property at a foreclosure auction.

QUESTIONS

8. May a lawyer who currently represents a lender in foreclosure proceedings join a real estate LLC and provide leads to the LLC regarding properties in foreclosure that the lawyer believes will be sound investments as rental properties? If not, may the lawyer do so if he waits until he leaves his current firm and joins a different firm in a different practice area?

OPINION

9. The inquiry raises three sets of issues: (i) confidentiality issues, (ii) conflict of interest issues, and (iii) issues regarding diligence and frivolous or dilatory litigation techniques. We will address these three sets of issues one at a time.

A. Confidentiality Issues: Rules 1.6(a), 1.8(b), and Rule 1.9(c).

10. The first set of issues concerns confidentiality. May the Associate disclose leads to the LLC based on information he acquires while representing Lenders in foreclosure proceedings? This question implicates Rules 1.6(a) and 1.8(b) while he is working at his current firm, and implicates Rule 1.9(c) if he waits until after he has moved to a different firm.

Rule 1.6(a) prohibits disclosure absent the client's informed consent

11. Rule 1.6(a), which is the most fundamental confidentiality rule, provides as follows (with emphasis added):

> (a) A lawyer shall not knowingly reveal confidential information, as defined in this Rule, or use such information to the ***disadvantage of a client*** or for the ***advantage of the lawyer or a third person***, unless:
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> (1) ***the client gives informed consent***, as defined in Rule 1.0(j);
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> (2) the disclosure is impliedly authorized to advance the best interests of the client and is either reasonable under the circumstances or customary in the professional community; or
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> (3) the disclosure is permitted by paragraph (b).
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> "Confidential information" consists of information gained during or relating to the representation of a client, whatever its source, that is (a) protected by the attorney-client privilege, (b) likely to be embarrassing or detrimental to the client if disclosed, or (c) information that the client has requested be kept confidential. ***"Confidential information" does not ordinarily*** include (i) a lawyer's legal knowledge or legal research or (ii) ***information that is generally known in the local community*** or in the trade, field or profession to which the information relates. [Emphasis added.]

12. The threshold question is whether information identifying properties that may be sound investments constitutes "confidential information" within the meaning of Rule 1.6(a). If so, then the Associate is prohibited from using the information to his own advantage, or for the advantage of third parties (such as his college friends or the LLC), or to the disadvantage of his client (the Lender). Whether information is confidential depends on multiple criteria.

13. The first of these multiple criteria is whether the information has been "gained during ***or*** relating to the representation of the client …." (Emphasis added.) Here, information about whether properties would be sound investments is plainly "gained during" the representation of the Lender, and is information "relating to" the representation. Only one of these is necessary, see N.Y. State 866 (2011), but here we have both. Accordingly, we need to examine one by one the three categories of confidential information listed in Rule 1.6(a).

14. Regarding privilege, the identity of properties in foreclosure by itself is not "protected by the attorney-client privilege," but communications from the Lender to the attorney about particular properties would be privileged. For example, if the Lender has told the Associate that a particular property is in excellent condition or has attracted interest from a renovator, that communication is privileged.

15. Regarding detriment to the client, if the Lender's interests differ in any material way from the LLC's interests, then revealing confidential information about desirable investment properties to the LLC is "likely to be detrimental" to the Lender. In the context of confidentiality, we understand the term "likely" in Rule 1.6(a) to indicate a "significant risk" that revealing or using the information will harm the client. (This understanding borrows a concept from Rule 1.7(a)(2), which is quoted later in this opinion.) In other words, we think the phrase "likely to be detrimental" falls somewhere in between "probable" (meaning "more likely than not") and "possible" (meaning that it can't be completely ruled out). If there is a significant risk that revealing or using the information will disadvantage the client, then it is "likely to be detrimental" within the meaning of Rule 1.6(a). And the more sensitive the information to be disclosed, the more significant the risk, because the detriment to the client will increase as the sensitivity of the information increases.

16. Regarding client expectations, if the Lender has requested that information about the properties in foreclosure be kept confidential, then the information is presumptively confidential even if it is not privileged and even if disclosing the information is not likely to be detrimental to the client. Moreover, if the Associate's law firm has assured the Lender that all such information will be kept confidential, then that is equivalent to the Lender's request that the information be kept confidential even if the Lender has not expressly made such a request.

17. The fact that foreclosure proceedings are a matter of public record does not make the information "generally known" (which would take it outside the purview of "confidential information"). Comment [4A] to Rule 1.6 says, in relevant part:

> Information that is generally known in the local community or in the trade, field or profession to which the information relates is also not protected, unless the client and the lawyer have otherwise agreed. ***Information is not "generally known" simply because it is in the public domain or available in a public file.*** [Emphasis added.]

18. The emphasized sentence in the quoted language is significant because in 2011 it replaced the following two sentences that were originally in Comment [4A]:

> Information that is in the public domain is not protected unless the information is difficult or expensive to discover. For example, a public record is confidential information when it may be obtained only through great effort or by means of a Freedom of Information request or other process.

19. These two original sentences were criticized as inaccurate, and the New York State Bar Association therefore removed them from Comment [4A] in 2011 and substituted the single sentence in today's Comment [4A] (emphasized above). This legislative history strongly suggests

that information in the public domain may be protected as confidential information even if the information is not "difficult or expensive to discover" and even if it could be obtained without "great effort" and without a Freedom of Information request or other formal process.

20. Here, we think the information in question cannot be "generally known." In our view, information is generally known only if it is known to a sizeable percentage of people in "the local community or in the trade, field or profession to which the information relates." Given that hundreds or thousands of homes are in foreclosure in any locale at any given time, we do not believe that the identity of particular properties that would make sound investments is "generally known" within the meaning of Rule 1.6(a).

21. If information about particular properties – such as which ones are in good repair and which ones have new appliances – is "confidential information" within the meaning of Rule 1.6(a), then the Associate cannot use or reveal that information unless one of the exceptions in Rule 1.6(a) applies. The Associate may not have any such information – we understand that lenders do not always inspect properties in foreclosure, and may not share the foreclosure report with their lawyers – but if the Associate does have confidential information about particular properties, then Rule 1.6(a) prohibits him from using for his own benefit, or for the benefit of his friends in the LLC, or to the client's detriment, regardless of who benefits.

22. The first exception to Rule 1.6 is the client's "informed consent, as defined in Rule 1.0(j)," which is in the Terminology section. Rule 1.0(j) provides as follows:

> (j) "Informed consent" denotes the agreement by a person to a proposed course of conduct after the lawyer has communicated information adequate for the person to make an informed decision, and after the lawyer has adequately explained to the person the material risks of the proposed course of conduct and reasonably available alternatives.

23. We lack sufficient facts to spell out all of the disclosures the Associate would need to make to obtain the Lender's informed consent to revealing the identity of a promising investment property, but at a minimum it would need to include both (a) whether the Associate believes the particular property would be a sound investment for rental purposes and, if so, why; and (b) whether the Associate plans to speed up or slow down the mediation process. Armed with that information, the Lender should be able to decide whether it would also be interested in buying the property or working out a loan modification. If so, the Lender will presumably deny consent for the Associate to disclose the information to the LLC.

24. The second exception to the duty of confidentiality arises when the disclosure (a) is "impliedly authorized to advance the best interests of the client" and (b) is either (i) "reasonable under the circumstances" or (ii) "customary in the professional community." We do not perceive any circumstances in which disclosing a promising investment property to the LLC would advance the Lender's interests. If such circumstances exist, the better practice would be for the Associate to disclose the relevant facts to the client and obtain the client's informed consent. The "impliedly authorized" exception is intended mainly for situations in which time is of the essence and it is impractical for the lawyer to wait for the client's informed consent (such as during settlement negotiations or trial), or for situations in which revealing information about a client with

diminished capacity is "necessary to take protective action to safeguard the client's interests." *See* Rule 1.6, Cmt. [5] (giving examples of circumstances in which disclosure of confidential information is impliedly authorized). Nothing suggests that those situations apply here.

25. The third exception to the duty of confidentiality arises when "the disclosure is permitted by paragraph (b)," meaning that the facts fall within one of the six specified exceptions in Rule 1.6(b) (*e.g.,* the need "to prevent reasonably certain death or substantial bodily harm" or "to prevent the client from committing a crime)." We need not elaborate on these exceptions because none apply here.

Rule 1.8(b) prohibits disclosure absent the client's informed consent

26. Rule 1.8(b) provides as follows:

> (b) A lawyer shall not use information relating to representation of a client to the disadvantage of the client unless the client gives informed consent, except as permitted or required by these Rules.

27. At first glance, Rule 1.8(b) appears to duplicate the prohibition in Rule 1.6(a) against using confidential information "to the disadvantage of a client." But Rule 1.8(b) – unlike Rule 1.6(a) -- applies to *all* information "relating to representation of a client," whether or not the information is protected by the attorney-client privilege, whether or not disclosure would not be embarrassing or detrimental to the client, and whether or not the client has not requested that the information be held inviolate, and whether or not the information has become "generally known." Under Rule 1.8(b), a lawyer simply may not use information relating to the representation of a client unless either (i) "the client gives informed consent" (discussed above) or (ii) disclosure is "permitted or required by these Rules" (an exception that does not apply here).

28. Thus, whenever disclosing the identity of a promising investment property would be disadvantageous to the Lender, the Associate may not do it absent the client's informed consent pursuant to Rule 1.0(j). As Comment [5] to Rule 1.8 says:

> [5] A lawyer's use of information relating to the representation to the disadvantage of the client violates the lawyer's duty of loyalty. Paragraph (b) applies when the information is used to benefit either the lawyer or a third person, such as … a business associate of the lawyer, at the expense of a client. For example, if a lawyer learns that a client intends to purchase and develop several parcels of land, the lawyer may not use that information to purchase one of the parcels in competition with the client or to recommend that another client make such a purchase. …

Rule 1.9(c) prohibits disclosure absent the client's informed consent

29. The Associate also asks whether the answer will change if he waits until he has moved to a different firm working in a different practice area. It will not. Rule 1.8(b) does not apply to former clients, but Rule 1.6 does apply, via Rule 1.9(c), which provides as follows:

> (c) A lawyer who has formerly represented a client in a matter or whose present or former firm has formerly represented a client in a matter shall not thereafter:
>
> > (1) use confidential information of the former client protected by Rule 1.6 to the disadvantage of the former client, except as these Rules would permit or require with respect to a current client or when the information has become generally known; or
> >
> > (2) reveal confidential information of the former client protected by Rule 1.6 except as these Rules would permit or require with respect to a current client.

30. In other words, the duty of confidentiality in Rule 1.6 toward current clients carries over with full force to former clients. To the extent that the Associate is barred from using or revealing confidential information of his current clients while working at his current firm, he will be equally barred from using or revealing the same information after he has moved to a different law firm. Whether his new firm practices in the same area of law or a different area of law will make no difference.

31. In sum, we conclude that Rules 1.6(a), Rule 1.8(b), and 1.9(c) all prohibit the Associate from making the disclosures he proposes to make here unless the Lender gives informed consent.

B. <u>Conflict Issues: Rule 1.7</u>.

32. The second set of issues pertains to conflicts of interest between the Lender's interests and the lawyer's personal interests. Indeed, in his inquiry, the Associate expressly worries that his involvement in a business that buys properties upon which clients of his employer's law office are foreclosing "will create an ethical conflict subject to disciplinary action…."

33. The Associate's concern is well founded. The applicable provision of the New York Rules of Professional Conduct is Rule 1.7(a)(2), which provides as follows:

> (a) Except as provided in paragraph (b), a lawyer shall not represent a client if a reasonable lawyer would conclude that …
>
> > (2) there is a significant risk that the lawyer's professional judgment on behalf of a client will be adversely affected by the lawyer's own financial, business, property or other personal interests.

34. In the circumstances before us, a reasonable lawyer would conclude that there is a "significant risk" that the Associate's professional judgment on behalf of the Lender in foreclosure proceedings regarding each property will be adversely affected by (a) the Associate's own financial and business interests in the LLC, and by (b) the Associate's personal interests in maintaining good relationships with his friends who run the LLC. Thus, a concurrent conflict will arise with respect to each foreclosure proceeding in which the Associate represents the

Lender.[1] In particular, the Lender has a legal duty to participate in the loan modification process in good faith, but the LLC is not involved in that process and has no good faith obligation. Some courts have sanctioned lenders for dragging out the loan modification process or for otherwise failing to negotiate a loan modification in good faith. *See, e.g., U.S. Bank v. Shinaba,* No. 381917/09 (Bronx Sup. Ct., July 31, 2013) (imposing sanctions on bank for "dilatory, and dishonest, conduct" that dragged out settlement conferences in a foreclosure action); *Citibank, N.A. v. Barclay,* No. 381649/09 (Bronx Sup. Ct., June 21, 2013) (same). These decisions underscore the conflict of interest that the Associate will face if the Lender desires to reach a loan modification agreement or otherwise move the foreclosure process along quickly, but the LLC wants to drag it out. (We address below the Associate's separate duty to avoid conduct whose purpose is to delay and prolong litigation.)

35. Because a concurrent conflict of interest exists, the Associate may not represent the Lender in any foreclosure proceeding unless he complies with Rule 1.7(b), which provides, in pertinent part, as follows:

> (b) Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:
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> > (1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client; … and
> >
> > (4) each affected client gives informed consent, confirmed in writing.

36. Under Rule 1.7(b), the Associate may not be involved in the LLC unless he "reasonably believes" that he can "provide competent and diligent representation" to the Lender, and the Lender "gives informed consent, confirmed in writing." This standard will be difficult to meet because the Lender has many interests that may diverge from the LLC's interests. For example, the Lender may desire to establish or maintain a reputation for cooperation with the courts, for fairness to borrowers, or for efficiency in resolving foreclosure proceedings. The Lender will also desire to minimize legal fees and minimize the costs of taxes, insurance, and maintenance on properties in foreclosure. And the Lender will want to avoid sanctions for dilatory or frivolous litigation conduct. The LLC does not share these interests – its only interest is in purchasing sound investments for the LLC. Accordingly, it is unlikely that the Associate can provide competent and diligent representation to the Lender if he is personally involved in the LLC or has agreed to provide "leads" to the LLC. Thus, the conflict may well be non-consentable (non-waivable).

37. Even if a conflict regarding a particular property is consentable – and it usually will not be – the Associate must not continue representing the Lender in the matter without the Lender's informed consent. The disclosures needed to obtain the Lender's informed consent to disclose confidential information to the LLC (see above) should normally suffice to obtain the Lender's informed consent for conflict purposes -- but Rule 1.7(b)(4) also requires that the client's consent

[1] As mentioned earlier, nothing in his inquiry indicates that he will be representing the LLC. As long as the Associate does not perform any legal services for the LLC, the Associate's involvement in the LLC will not involve him in representing "differing interests." and thus will not create a concurrent conflict under Rule 1.7(a)(1).

be "confirmed in writing" – see Rule 1.0(e) (defining "Confirmed in writing"). Moreover, the Associate will have to obtain a separate consent with respect to each property on which he represents the Lender, because each property presents a new and different conflict of interest.

C. Dilatory Tactics in Litigation: Rules 3.1 and 3.2

38. The Associate says in his inquiry that he may have an incentive to frustrate the mediation process by "causing delays in forwarding applications that I receive from borrowers to my client." Deliberately causing such delays would implicate Rule 3.1 ("Non–Meritorious Claims and Contentions"). Rule 3.1(a) provides that a lawyer "shall not bring or defend a proceeding, or assert or controvert an issue therein, unless there is a basis in law and fact for doing so that is not frivolous. …" Rule 3.1(b)) provides that a lawyer's conduct is "frivolous" for purposes of Rule 3.1 if the conduct "has ***no reasonable purpose other than to delay or prolong the resolution of litigation***, in violation of Rule 3.2 …." [Emphasis added.]

39. Thus, the Associate may not advance frivolous claims or defenses, or engage in conduct whose main purpose is to "delay or prolong" the litigation.

40. Moreover, Rule 3.2 ("Delay of Litigation"), which is referred to in Rule 3.1(b)(2), provides that a lawyer representing a client, a lawyer "shall not use means that have no substantial purpose other than to ***delay or prolong*** the proceeding or to cause needless expense." (Emphasis added.) Comment [1] to Rule 3.2 explains the rule as follows (with emphasis added):

> [1] Dilatory practices bring the administration of justice into disrepute. Such tactics are prohibited if their only substantial purpose is to frustrate an opposing party's attempt to obtain rightful redress or repose. … The question is whether a competent lawyer acting in good faith would regard the course of action as having some substantial purpose other than delay or needless expense. ***Seeking or realizing financial or other benefit from otherwise improper delay in litigation is not a legitimate interest of the client.*** [Emphasis added.]

41. Seeking financial or other benefit for the lawyer's own *client* is not a legitimate reason for a lawyer to delay litigation, so seeking financial benefit for the *lawyer* (or a business in which the lawyer is involved) is *a fortiori* not a legitimate justification for using delaying tactics. Thus, even if the Associate obtains the client's consent to disclose confidential information to the LLC pursuant to Rule 1.6(a), and even if the Associate obtains the client's valid consent to the concurrent conflict pursuant to Rule 1.7(b), the Associate still must not use dilatory litigation tactics, such as seeking unwarranted continuances or demanding unnecessary loan documentation, that have "no substantial purpose other than to delay or prolong the proceeding."

CONCLUSION

42. A lawyer must not reveal confidential information to the disadvantage of the client or to the advantage of the lawyer or a third party (such as a business in which the lawyer is involved) unless the client gives informed consent. If a reasonable lawyer would perceive a significant risk that the lawyer's financial, business, or other personal interests will adversely affect the lawyer's professional judgment on the client's behalf, then the lawyer may not continue the representation

unless the conflict is consentable and the client gives informed consent, confirmed in writing. In any event, the lawyer may not use litigation tactics that have no substantial purpose other than delay.

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