Negotiation Ethics

Jayme Partridge
Principal
Houston

Bailey Benedict
Associate
Houston

FISH & RICHARDSON

Ethics in Negotiations

- What rules govern attorney conduct in negotiations?
- What do those rules permit?
- What do those rules prohibit?
- What laws apply to attorney conduct in negotiations?
- What are consequences of unethical behavior?
- What is the benefit of behaving ethically in negotiations?

“ As negotiator, a lawyer seeks a result advantageous to the client but consistent with requirements of honest dealings with others.”

Texas Rules of Disciplinary Conduct, Preamble

Truthfulness in Statements to Others

RULE 4.1: TRUTHFULNESS IN STATEMENTS TO OTHERS:

In the course of representing a client a lawyer shall not knowingly:

(a) make a false statement of material fact or law to a third person;

or

(b) fail to disclose a material fact to a third person when disclosure is necessary to avoid assisting a criminal or fraudulent act by a client, unless disclosure is prohibited by Rule 1.6.

4.1 As Adopted Varies By State

- California has not adopted 4.1, but rather relies on tort law principles.
- Connecticut adopted 4.1 as written.
- Delaware has adopted 4.1 as written.
- District of Columbia has adopted 4.1 as written.
- Georgia adds: “The maximum penalty for a violation of this Rule is disbarment.”
- Massachusetts had adopted Rule 4.1 as written.
- Minnesota replaces the MR with: “In the course of representing a client, a lawyer shall not knowingly make a false statement of fact or law.”

4.1 As Adopted Varies By State

- New York made a broader change by deleting “material,” but cut (b) regarding duty to disclose.
- New Jersey added: “The duties in this Rule apply even if compliance requires disclosure of information otherwise protected by RPC 1.6.”
  - *Disclosure of confidential information?*
- Texas substantially narrowed the duty of disclosure in (b) by deleting “or law;” and replacing language after “person” with “when disclosure is necessary to avoid making the lawyer a party to a criminal act or knowingly assisting a fraudulent act perpetrated by a client.”

Not “Material Fact”

- “Under generally accepted conventions in negotiation, a party’s supposed intentions as to an acceptable settlement of a claim may be viewed merely as negotiating positions rather than as accurate representation of material fact.”

- Comment, Rule 4.01

- “a party’s negotiating goals or its willingness to compromise, as well as ... negotiation ‘puffing,’ ordinarily are not considered ‘false statements of material fact’ ....”

- ABA Formal Opinion 06-439 (2006)

Considered “Material Fact”

Examples of unacceptable false statements of material fact include:

- A lawyer representing to the other side that a benefit will cost the company money when it does not.
- Declaring *as a fact* that your authority to settle is limited to a certain amount when it is not.

Duty to Disclose (Omission)

Varies by state:

- California follows applicable tort law.
- Tort law can differ on duty to disclose (misrepresentation by omission).
- State disciplinary rules vary:
  - D.C. adopted model rule 4.01(b)
  - N.Y. did not
  - Texas limited its scope
  - N.J. requires disclosure of confidential information

Duty to Disclose (Omission)

Rule 4.1, cmt. 1:

- Although a lawyer is required to be truthful when dealing with others, a lawyer generally has no affirmative duty to inform an opposing party of relevant facts.

For example:

- No duty to inform an opposing party about things such as settlement authority limits.

The Courts Lean Toward Disclosure

- Death of a client *(Virzi v. Grand Truck Warehouse & Cold Storage* Co., 571 F.Supp. 507 (E.D. Mich. 1983))
- Insurance policies *(Ex rel Nebraska State Bar Ass'n v. Addison*, 412 N.W.2d 855 (Neb. 1987); *contra, NY County Ethics Opinion 731* (2003))
- Misrepresenting settlement terms *(In re Eadie,* 36 P.3d 468 (Ore. 2001))
- Changes to the terms of a contract or settlement agreement *(In re Rothwell,* 296 S.E.2d 870 (S.C. 1982))
- Statements that were true when made but are now false *(In re Williams,* 840 P.2d 1280 (Ore. 1992))
- Side deal with party's lawyer *(In re Zaruba*, 177 N.J. 564 (2003))
- Procuring sham transaction *(In re Hiller,* 694 P.2d 540 (Ore. 1985))
- Concealing financing terms, *(Vega v. Jones Day, 121 Cal. App. 4th 282* (Cal. App. 2004))

Hypothetical One

Your counterpart in a negotiation tells you from its own research it has determined that a continuation patent was never disclosed to a standards organization.

- You know this to be false because under the SSO's disclosure rules, disclosure of one patent is deemed disclosure of the family.
- Tactically, you may want to correct this mistake.
- But are you required to do so?

Answer: Hypothetical One

- A lawyer's knowing failure to disclose a "non-confidential, material, and objective fact" upon inquiry from a third person during settlement negotiations is improper.
  - Pendleton v. Cent. N.M. Correctional Facility, 184 F.R.D. 637 (D. NM 1999).
- If this is seen as a legal issue on what amounts to disclosure, then no, because 4.01(b) never applies to correcting legal assumptions.
- If this is seen as an objective fact, most state rules of conduct would require disclosure, but not all (e.g., NY, CA, TX).
- Even if state rules of conduct do not require disclosure, however, there may be a duty to disclose under state tort law, or enforceability of deal may be disputed if no disclosure (e.g., equitable estoppel).

“Knowingly” Rule 1.0(f)

- Rule 1.0(f) – “knowingly” denotes actual knowledge and the lawyer’s “actual knowledge” may be inferred from the circumstances.
  - “Evil intent or bad purpose” not required.
  - If lawyer makes innocent misrepresentation he/she believes true and later learns it is false, he/she must correct the statement by notifying the person the misrepresentation was made to, even if opposing counsel.
- Comment [2] to Rule 4. 0 1: A misrepresentation can occur if the lawyer incorporates or affirms a statement of another person that the lawyer knows is false.

Softening up opposing counsel.

c.09CharlesFincher02.02 Scribble-in-Law at LawComix.com

Rule 1.05 – Confidentiality of Information

(c) A lawyer may reveal confidential information:

1. When the lawyer has been expressly authorized to do so in order to carry out the representation;
2. When the client consents after consultation;
3. To the client, the client's representatives, or the members, associates, and employees of the lawyer's firm, except when otherwise instructed by the client;
4. When the lawyer has reason to believe it is necessary to do so in order to comply with a court order, a Disciplinary Rule of Professional Conduct, *or other law*.

Disclosure of Confidential Information

Rule 1.05, Comment 21:

- "If the lawyer's services will be used by the client in materially furthering a course of criminal or fraudulent conduct, the lawyer must withdraw…"

Rule 1.05(e):

- "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 death or substantial bodily harm…the lawyer shall reveal the confidential information…"

And recall NJ rule where 4.01 trumps 1.06!

Hypothetical Two

- You are about to close the sale of one of your client's properties to the local church for its construction of a new elementary school.
- The business person on the transaction calls you to congratulate you on working out a great deal.
- She then adds that it is a good thing that the company is selling the property because the internal compliance unit informed her that unknown to corporate HQ or the public, for the last five years large quantities of highly toxic chemicals have been dumped on a regular basis on the property.

Answer: Hypothetical Two

Is it a material fact?

- The fact of large scale contamination would be material if not known by the buyer because it would prevent the use of the property until remediation were complete, and the property may never be safe for its intended use. The buyer would not only be deprived of the benefit of its bargain but left with a huge liability.

Would your client be committing misrepresentation by omission?

- This is a fact that only your client would have access to the information.

If your client refuses to let you disclose this fact what would you do?

- Look at Rule 1.06(b)

Rule 1.06(b)

(b) A lawyer may reveal information relating to the representation of a client to the extent the lawyer reasonably believes necessary:

1) to prevent reasonably certain death or substantial bodily harm;

2) to prevent the client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's service.

Hypothetical Three

- You are negotiating settlement of a breach of contract action your company brought against a supplier.
- You say, truthfully “five major customers cancelled their purchase contracts after the defendant’s breach.”
- But you know they cancelled for reasons unrelated to the breach.

Answer: Hypothetical Three

- The reasons other people settled and what is driving this settlement could be based solely on the individual circumstances of each deal and not material.
- In context the statement could be seen as puffery: for example, if the other settlements were known to be nuisance value while here the exposure is different.
- The answer here will depend on the circumstances of the situation and the governing rule: NJ disclosure might be required, NY or TX or CA probably not, MA, DE, MN, DC maybe.

The Dishonesty Rule 8.04

- Rule 8.04(b), makes it a violation of the rules for an attorney to break, or assist another in breaking, a rule, committing a criminal act, or engaging in fraud, dishonesty, or deceit.
- Rule 8.04(c) prohibits a lawyer from engaging in conduct involving dishonesty, fraud, deceit or misrepresentation.

Hypothetical Four

- While reviewing documents to produce in response to plaintiff's discovery requests in a fraud case, you find emails between the sales representatives joking about the lies they told the plaintiff.
- Before you produce the emails, plaintiff's counsel calls you to say that his or her elderly client has no real recollection of the sale and would be willing to go away for nuisance value.

Answer: Hypothetical Four

Depending in part on representations and circumstances, likely no duty to disclose:

- This event occurs not in a negotiation but in the context of an adversarial event.
- The rules governing document production and discovery govern the obligation to disclose.
- There is no obligation to provide opposing counsel a preview of documents prior to production.
- You have no knowledge of the condition of the plaintiff's memory or motives, and the lawyer's statement could be "puffery" to get a quick settlement.
  - ✓ After all, opposing counsel and his client presumably had enough information to sue your client for fraud.

Hypothetical Five

- The adversary serves you with notices of deposition for every board member.
- You know that one member's testimony will almost definitely establish liability.
- You negotiate a deal with your adversary where he or she agrees to one specific board member's testimony (not the one you were concerned about) in lieu of other discovery concessions.

Answer: Hypothetical Five

- If you are in an adversarial relationship, and made no representations that all board members are fungible?
  - ✓ Then seems like there is no material statement and adversarial relationship would preclude reliance on an omission.
- What if other discovery showed that one member had special knowledge (e.g., document produced or other testimony)?
  - ✓ No material statement and here the adversary had access to facts so there is no reason for adversary to rely on you in any way.
- But what if you have said no one on the Board knows anything different from any one else?
  - ✓ Then there is a material statement and made with the expectation your adversary will rely on falsity.

“Flags”

Balance of power

- Sophistication
- Degree of disadvantage
- Pattern

Common Element

The deal reflects a serious misunderstanding

AND

- Lawyer's "fingerprints"
- Either by action or inaction
- The lawyer's services were used

Tactics

- Non-reliance clause
- Merger clause
- Add conspicuous clauses on topic
- Written offer to inspect

Conclusion

- Lawyers are presumed to know the rules:
  - ✓ Will be held to a higher standard.
  - ✓ Courts are not forgiving of dishonesty and deceit.
- Err on the side of disclosure and honesty.


KARMA

Jayme Partridge
713-654-5357
partridge@fr.com

Bailey Benedict
713-654-5331
benedict@fr.com

Please send your NY CLE forms or questions about the webinar to marketing at lundberg@fr.com.

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