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The Ethical Considerations of Representing Multiple Parties

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Rule 1.7 of the American Bar Association (ABA) Model Rules of Professional Conduct, which underlie the rules of professional conduct for every state bar except California, prohibits lawyers — both bankruptcy and nonbankruptcy practitioners alike — from representing multiple clients in matters where the clients are directly adverse to each other, regardless of the clients' consent. "Loyalty and independent judgment are essential elements in the lawyer's relationship to a client," and neither element can be fully satisfied when a lawyer's clients are directly adverse to one another.[1]

The Second Circuit's long-standing statement on this point bears repeating: Conflicts of interest arising out of concurrent representation "must be measured not so much against the similarities in litigation, as against the duty of undivided loyalty which an attorney owes to each of his clients."[2] Even where parties are not directly adverse, lawyers must be cognizant of the possibility that representing one party may materially limit the representation of another client. In these instances, representation is generally prohibited unless (1) the lawyer reasonably believes that he/she will be able to provide competent and diligent representation to each client, and (2) each client provides informed consent, confirmed in writing.

Bankruptcy courts enforce professional responsibility rules over the attorneys before them, meaning that lawyers can be disqualified from representing a party if a court determines in its discretion that the rules have been breached.[3] Unfortunately, the ABA Comments to Rule 1.7 do not specifically address how conflicts of interest can be resolved in the bankruptcy context where the competing interests of the parties involved may constantly evolve over the course of the bankruptcy proceedings. This leaves many bankruptcy practitioners scratching their heads as they try to figure out whether the representation of multiple parties — such as creditors — is permissible, and if it is, how they may represent each of those parties fairly and equally when nuanced conflict issues abound.

There is no bright-line test that bankruptcy lawyers can readily apply to see if their conduct runs afoul of the rules; a court's determination of whether an insurmountable conflict of interest exists can often only be made on a case-by-case basis. As a result, bankruptcy lawyers need to be vigilant lest they face an unexpected disqualification. This article examines the ethical considerations of representing multiple parties in a bankruptcy.

The Bankruptcy Code

Unlike traditional litigation, the concept of "conflict" can be much more subtle in bankruptcy proceedings because parties' interests are not often directly adverse to one another. For instance, creditors and debtors are not *per se* adverse for the simple reason that they are both seeking to increase the debtor's value through the debtor's restructuring. As a result, ethical questions over conflicts in bankruptcy proceedings can become very complex. As one court has noted, "[u]nlike other forums and battlefields, where the lines of conflict are clearly drawn, in bankruptcy court, interested parties face proceedings with multiple litigants where the parties' interests, positions and relationships may change several times from pre-filing to post-filing and even thereafter."[4] However, while the Bankruptcy Code and Rules provide little statutory guidance related to the considerations of representing multiple parties in the same bankruptcy case, they do provide some guidance on the representation of certain parties in specific situations.

Section 327 of the Bankruptcy Code provides that "the trustee ... may employ one or more attorneys ... that do not hold or represent an interest adverse to the estate, and that are disinterested persons." Meanwhile, § 327(c) explains that "[i]n a case under chapter 7, 12, or 11 ... a [lawyer] is not disqualified for employment under this section solely because of such person's employment by or representation of a creditor." However, if a party objects to the employment, the court must evaluate the potential conflict.

Section 1103 of the Bankruptcy Code prohibits lawyers that represent a committee from representing any other entity having an adverse interest in connection with the case. This section explicitly provides that the representation of one or more creditors of the same class as represented by the committee is not a *per se* adverse interest.

Fed. R. Bankr. P. 2019 requires that a lawyer who represents multiple creditors or equity security-

1 ABA Model Rule 1.7, cmt. [1].
2 *Cinema 5 Ltd. v. Cinerama Inc.*, 528 F.2d 1384, 1386 (2d Cir. 1976).
3 *See Baron & Budd PC v. Unsecured Asbestos Claimants Comm.*, 321 B.R. 147 (D.N.J. 2005).
4 *In re Flanigan's Enters. Inc.*, 70 B.R. 248, 250 (Bankr. S.D. Fla. 1987).

holders, ad hoc committees or groups, or official committees must file a statement identifying the parties and any disclosable economic interest if the parties are "(a) acting in concert to advance their common interest, and (b) not comprised entirely of affiliates or insiders of one another."[5] This rule is limited to chapter 9 and 11 filings. Outside of these limited circumstances, attorneys' actions in the bankruptcy context are governed by their ethical obligations as established by the rules of professional conduct in their respective jurisdictions.

Multiple Parties: What Is Advisable?

Generally speaking, it is improper to represent parties with competing positions in the same bankruptcy case. Thus, it is generally not advisable to represent (1) creditors in different classes, (2) creditors and creditors' committees, (3) debtor and creditors, or (4) multiple secured creditors holding interest in the same collateral.[6] Creditors may properly object on conflict grounds in such situations and obtain disqualification as a result.[7]

On the other hand, it is not inherently problematic to represent (1) multiple unsecured creditors,[8] (2) multiple secured creditors holding interest in different collateral, (3) multiple creditors' committees, or (4) creditors and debtors involved in different bankruptcies. Lawyers are also not automatically disqualified if their former law firms are representing adverse creditors.[9] In evaluating whether to represent multiple parties, lawyers should carefully evaluate the permissibility of representing multiple parties, taking into consideration the extent of the actual existing conflict (if any), the likelihood and nature of an actual developing conflict and the lawyer's ability to effectively represent all parties. If the risks are minimal, the parties can move forward with representation, as long as the lawyer discloses the dual representations to the clients, discusses the issues and risks associated with the representation, and obtains informed consent from all clients.

ABA Model Rule 1.0(e) defines "informed consent" as "the agreement by a person to a proposed course of conduct after the lawyer has communicated adequate information and explanation about the material risks of and reasonably available alternatives to the proposed course of conduct."[10] However, even a waiver may not be valid if a court determines that the conflict is such that it creates an unavoidable appearance of impropriety.[11] Further, a waiver might be disregarded if the competing interests change to such an extent that an actual and direct conflict exists between the parties.

Representing Multiple Parties

In representing multiple parties, conflicts often arise after obtaining written consent from clients. Depending on the conflict, a lawyer may have no other option than to withdraw from representing all of the affected clients.

Future Conflicts

In many instances, lawyers request that a client waive any future conflicts that might arise. The effectiveness of such waivers is generally determined by the extent to which the client reasonably understands the material risks that the waiver entails.[12] Thus, the more open-ended and general the consent, or the less sophisticated the client, the less effective the waiver will be because the client will not have reasonably anticipated the future conflict that could arise.

> **With the increasing complexity and constant evolution of issues and interests during the life of a bankruptcy proceeding, lawyers representing multiple parties may quickly and unexpectedly find themselves staring down the path of a conflict.**

The ability to utilize an advance waiver in the bankruptcy context is limited because advance waivers cannot waive direct conflicts. Thus, even though a waiver may allow a lawyer to represent an unforeseen creditor in the same class at a future date, it would not permit him/her to represent an unforeseen creditor if, for example, the current client or future client expressed an intent to have the other's claim challenged as a preference or other avoidable transfer. Indeed, even if neither client expressed an intent to have another's claim challenged, if the lawyer is aware that a challenge is likely, the representation is not advisable and the advance waiver will provide little benefit.

Without express language that the client is willing to waive a specific right that it might otherwise have, an advance waiver is meaningless because it was not executed with informed consent. Thus, at the time that a claim conflict arises among multiple creditor clients, the lawyer must attempt to obtain a waiver from all affected clients, and if he/she is unable to obtain such waiver, representation of all of the affected clients is no longer permitted, but even then, a court may still disregard the waiver. Indeed, some courts hold that "[i]t is universally recognized that attorneys are prohibited from representing *actual* conflicts of interest in bankruptcy."[13] However, if it is only a potential conflict, disqualification may not be in order.[14]

Confidential Information

Conflicts can also arise when dealing with confidential information, but lawyers must uphold their obligation of con-

5 Fed. R. Bankr. P. 2019(b)(1).

6 *See, e.g., Matter of Whitman*, 101 B.R. 37 (Bankr. N.D. Ind. 1989) (lawyers cannot represent creditors' committee and committee member holding both secured and unsecured deficiency claim because of conflict between secured and unsecured creditors); *In re The Harris Agency LLC*, 462 B.R. 514 (E.D. Pa. 2011) (impermissible representation of creditor that also was co-obligor with debtor in possession).

7 *See, e.g., In re Meridian Auto. Sys.-Composite Operations Inc.*, 340 B.R. 740 (Bankr. D. Del. 2006) (order of disqualification proper where one creditor objected to former or current counsel's appearance for another creditor where lawyer did not obtain waiver from both clients).

8 There must be no issues related to the receipt of fraudulent conveyances or preferential treatment.

9 *See In re ProEducation Int'l. Inc.*, 587 F.3d 296 (5th Cir. 2009) (if lawyer not personally involved in creditor one's representation leaves firm, he may represent creditor two adverse to creditor one).

10 *See In re Congoleum Corp.*, 426 F.3d 675, 691 (3d Cir. 2005) ("[T]he effect of a waiver, particularly a prospective waiver, depends upon whether the clients have given truly informed consent.").

11 *See, e.g., In re McGregory*, 340 B.R. 915, 920-22 (B.A.P. 8th Cir. 2006) (representation presented such "inherent and impermissible conflict" that it could not be waived, particularly because of "unavoidable appearance of impropriety").

12 ABA Model Rule 1.7, Consent to Future Conflict, cmt. 22; *see also* ABA Formal Op. 05-436 (2005) (lawyer may obtain advance waiver from client, thus allowing lawyer to represent unidentified future clients with interests potentially adverse to existing client's interests; waiver more apt to be enforceable if client was "experienced user of legal services").

13 *In re Diamond Mortg. Corp.*, 135 B.R. 78, 90 (Bankr. N.D. Ill. 1990).

14 *See In re Marvel Entm't Grp. Inc.*, 140 F.3d 463, 476 (3d Cir. 1998).

continued on page 69

from page 33

fidentiality for each client. In some instances, the obligation of disclosure to one client may conflict with the obligation of confidentiality to the other. Advance waivers may help alleviate the concerns associated with conflicts arising as a result of confidential information. The ABA has indicated that an "advance waiver" can allow a lawyer to continue representation even if a conflict arises related to confidential information.[15] However, the ABA also noted in the same opinion that "whether any agreement made before the lawyer understands the facts giving rise to the conflict may satisfy 'informed consent' (which presumes appreciation of 'adequate information' about those facts) is highly doubtful." Thus, absent a unique set of circumstances where a party knowingly waives its right to have a specific group of information kept confidential, the advance waiver will provide little benefit.

Absent the aforementioned advance wavier, a lawyer who obtains information that may be harmful to one client but helpful to another is not permitted to disclose the information under ABA Model Rule 1.6 unless informed consent is obtained. If the lawyer cannot obtain valid consent, he/she must generally withdraw from representing all parties. In practice, larger law firms establish firewalls to prevent these types of disclosures or to alleviate the necessity of obtaining the consent in the first place. However, smaller law firms may not have such options, and without that added protection, they will need to be especially diligent in drafting their consent waivers.

Billing

Lawyers representing multiple parties in the same proceeding may also face billing issues. ABA Model Rule 1.5 prohibits unreasonable billing. A lawyer may not bill more than the actual time spent on a matter regardless of the number of clients that he/she represents. The ABA has stated that billing is not done "from the perspective of what a client could be forced to pay, but rather from the perspective of what the lawyer actually earned."[16] In the bankruptcy context, a lawyer appearing on behalf of multiple creditors at a hearing must allocate the time spent for each client at the hearing. Further, travel time and any costs associated with the travel should be split equally, unless the attendance at the hearing was predominantly for one creditor client.

Lawyers may also need to split billing for duplicative work product that was done simultaneously. The general test is whether the lawyer knew, at the time of drafting, that multiple parties would use the filing. If so, the general drafting should be allocated among all clients. On the other hand, if an attorney is recycling previous work, he/she can only bill the time spent updating the original work product. If a lawyer is not billing by the hour, he/she could potentially bill multiple clients for a single court appearance (*e.g.*, when the lawyer arranges a fixed fee for each appearance). However, the court fee must still be reasonable.

Conclusion

With the increasing complexity and constant evolution of issues and interests during the life of a bankruptcy proceeding, lawyers representing multiple parties may quickly and unexpectedly find themselves staring down the path of a conflict. Hopefully, that lawyer can rest easy knowing that he/she, at the beginning of the journey, carefully evaluated the multiple representations, considered actual and potential conflicts, disclosed and discussed the risks of the representation with all of the affected clients, and obtained informed consent from all clients through a well-drafted conflict waiver letter. Throughout the winding course of the representation of multiple clients, the lawyer should also use care in handling confidential information, billing clients and continuing to keep the clients informed about the representation, including any future conflicts that arise. abi

15 ABA Formal Op. 08-450.

16 ABA Formal Op. 93-379.

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