



ISBA Professional Conduct Advisory Opinion

Opinion No. 13-04
May 2013

Subject: Conflicts of Interest; Business Transactions with Client; Government Lawyers

Digest: A lawyer serving as an officer of a financial institution who also owns a significant stock interest in it must comply with the requirements of RPC 1.8 when representing a municipality that engages in business transactions with the financial institution. In addition, the lawyer's representation of the municipality is governed by RPC 1.7(a)(2) and may involve nonconsentable conflicts of interest when the municipality deals with the financial institution. Furthermore, abstaining from discussion on matters involving the financial institution while representing the municipality is insufficient to avoid the conflict of interest.

Reference: Illinois Rules of Professional Conduct 1.7, and 1.8

Illinois Municipal Code, 65 ILCS 5 et seq.

Public Officer Prohibited Activities Act, 50 ILCS 105 et seq.

In re Imming, 131 Ill.2d 239, 545 N.E. 2d 715, 137 Ill. Dec. 62 (1989)

In re Rukavina, 07-CH-96 (Review Board, November 18, 2009)
Respondent's petition for leave to file exceptions denied, M.R. 23585 (May 17, 2010)

In the Matter of Childs, 07-CH-95 (Review Board, July 26, 2010)
Respondent's and the Administrator's petitions for leave to file exceptions granted, M.R. 24094, (November 12, 2010)

In re Twohey, 191 Ill. 2d 75, 727 N.E.2d 1028, 245 Ill. Dec. 294 (2000)

Monco v. Janus, 222 Ill. App. 3d 280, 583 N.E.2d 575 (1st Dist. 1991)

Miller v. Norfolk & Western Railway Co., 183 Ill. App. 3d 361, 538 N.E. 2d 1293 (4th Dist. 1989)

ISBA Opinion 02-01 (October 2002)

Restatement Third, The Law Governing Lawyers §135

ISBA Opinion 94-21 (March 1995)

ISBA Opinion 12-12 (May 2012)

FACTS

Lawyer owns an eight percent equity interest in a small community bank (“Bank”). Lawyer also serves as the Bank’s Chairman of the Board. Municipality deposits funds, borrows money, and otherwise has routine financial dealings with Bank. Lawyer has been appointed as city attorney for Municipality.

QUESTIONS

1. Can the conflicts of interest in the facts presented above be waived by the informed consent of the parties?
2. Can Lawyer avoid the conflicts of interest by abstaining from rendering advice or taking any action in matters between the Municipality and the bank?

OPINION

This inquiry poses significant questions of substantive law involving the Illinois Municipal Code, 65 ILCS 5 et seq. and the Public Officer Prohibited Activities Act, 50 ILCS 105 et seq. These statutes can be complex, have been interpreted often by the courts and the Attorney General, and carry significant sanctions for noncompliance. To the extent the above inquiry raises questions under these or other statutes, the Committee is providing no opinion. The opinion expressed below only addresses a lawyer’s obligations under the Illinois Rules of Professional Conduct.

The Committee also notes that the nature of the inquiry is very broad without reference to any specific matters or facts. This necessarily hampers the Committee in providing an opinion, but certain general principles can be addressed.

1. Conflicts and Waiver

A. **RPC 1.8 (Conflicts of Interest - Business Transactions with Clients)**

In relevant part, RPC 1.8(a) provides:

(a) A lawyer shall not enter into a business transaction with a client or knowingly acquire an ownership, possessory, security or other pecuniary interest adverse to a client unless:

(1) the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing in a manner that can be reasonably understood by the client;

(2) the client is informed in writing that the client may seek the advice of independent legal counsel on the transaction, and is given a reasonable opportunity to do so; and

(3) the client gives informed consent, in a writing signed by the client, to the essential terms of the transaction and the lawyer's role in the transaction, including whether the lawyer is representing the client in the transaction.

A threshold question is whether Lawyer's eight percent ownership interest and status as Bank Chairman of the Board is sufficient interest to make RPC 1.8 applicable. Although no precise level of ownership interest or officer status is identified in the RPC, a number of cases have held that partial ownership and senior positions within a business entity is sufficient to require compliance with RPC 1.8. *In re Imming*, 131 Ill. 2d 239, 545 N.E.2d 715, 137 Ill.Dec. 62 (1989)(as president and sole shareholder of company, lawyer suspended for soliciting investments in the company from clients); *In re Rukavina*, 07-CH-96 (Review Board, November 18, 2009) *Respondent's petition for leave to file exceptions denied*, M.R. 23585 (May 17, 2010)(steering business to companies owned, and partially owned, by Respondent improper without satisfying requirements of RPC 1.8); *In the Matter of Childs*, 07-CH-95 (Review Board, July 26, 2010) *Respondent's and the Administrator's petitions for leave to file exceptions granted*, M.R. 24094 (November 12, 2010)(lawyer disciplined for inducing clients to invest in a company on whose board the lawyer was a member). *In re Twohey*, 191 Ill. 2d 75, 727 N.E.2d 1028, 245 Ill. Dec. 294 (2000)(Lawyer suspended for soliciting client investment to a company for which he served as the general counsel). Despite the absence of precise guidelines in the Rules, the Committee believes Lawyer's eight percent ownership and status as Bank Chairman of the Board makes Rule 1.8 applicable. Here, Lawyer has a financial (and possibly reputational) interest to steer business to the Bank and a disincentive to recommend other financial institutions to Municipality. Although not at issue in the facts of this inquiry, the Committee recognizes that not all ownership interests will trigger the obligations of RPC 1.8. For instance, the Committee does not believe that de minimis stock ownership in a multi-national financial institution likely would require the RPC 1.8 disclosures when a lawyer is recommending that financial institution to a client.

Having determined that Rule 1.8 is applicable under these facts, the Lawyer must be cautious. Business transactions between a lawyer and a client create the potential for overreaching. RPC 1.8, Comment [1]. In addition, the courts in Illinois have made it clear that lawyer-client business transactions are presumptively fraudulent. *Monco v. Janus*, 222 Ill. App. 3d 280, 583 N.E. 2d 575 (1st Dist. 1991). To address these broad concerns about overreaching and the potential for fraud, business transactions between lawyers and clients are allowed only when certain requirements are satisfied. *But see* RPC 1.8, Comment [1] (“the Rule does not apply to standard commercial transactions between the lawyer and client for products or services that the client generally markets to others...”). First, under RPC 1.8(a)(1) the transaction must be objectively fair, and its terms fully disclosed, to the client. Second, the client must be advised in writing and given the opportunity to consult with independent legal counsel. Finally, under RPC 1.8(a)(3), the client must give written informed consent to the terms of the transaction and the lawyer’s role in it. In the facts presented to the Committee, we do not know if these requirements have been satisfied. If they are, the Lawyer could potentially proceed with representing the Municipality.

Notwithstanding RPC 1.8(a)(3) and the possibility of informed client consent, Lawyer must be cautioned that not all conflicts, including business transaction conflicts, are consentable. RPC 1.8, Comment [3]. Here, the facts of the inquiry are not sufficiently developed to reach specific conclusions, but it is likely that some transactions between the Bank and Municipality could not be consented to by the Municipality, such as loan transactions where terms and conditions are subject to negotiation and discretion. See RPC 1.7, Comment [28] (“a lawyer may not represent multiple parties to a negotiation whose interests are fundamentally antagonistic to each other...”)

B. RPC 1.7 (Conflict of Interest – Material Limitation)

The above “business transactions” analysis does not fully address Lawyer’s professional obligations. Rule 1.7(a)(2) addresses situations where a lawyer’s personal interests or responsibility to a third person may pose a significant risk that the lawyer’s representation of a client will be materially limited. In the facts presented, Lawyer clearly has fiduciary responsibilities to the Bank as well as his own personal financial interests in the success of the Bank. Given these interests, a very reasonable concern is that Lawyer might structure a Bank – Municipality transaction in such a way that favors Lawyer’s interests at the expense of the Municipality. See RPC 1.8, Comment [3]. It is clearly a concurrent conflict of interest. See ISBA Opinion 02-01 (lawyer prohibited from representing a client with interests adverse to a company on whose board of directors the lawyer sits); Restatement Third, The Law Governing Lawyers § 135 (“a lawyer may not represent a client in any matter with respect to which the lawyer has a fiduciary or other legal obligation to another ...”).

Much like the Rule governing business transactions with a client, Rule 1.7 allows representation in certain circumstances despite a conflict. The exceptions provided in Rule 1.7(b) however, do not appear to be available to Lawyer in the inquiry presented. First, it appears to the Committee that the conflict presented is nonconsentable under Rule 1.7(b)(1)

and (4). Given the relationships at issue, the Committee does not feel that the interests of the Municipality can be adequately protected when its lawyer has a significant financial and business interest in an adverse party with whom the Municipality must negotiate and would ordinarily deal with at arms length. Second, although the Committee is not opining on the applicability of any statutes, it may be that the representation is nonconsentable under Rule 1.7(b)(2) as a violation of the Illinois Municipal Code and the Public Officer Prohibited Activities Act.

2. Abstention

“Abstention” is not a concept recognized in the RPC (the obligation of a municipal officer to “abstain” from involvement in certain matters appears to be a feature of the Illinois Municipal Code and the Public Officer Prohibited Activities Act). Lawyer simply choosing not to participate in matters involving the Bank and the Municipality in an effort to eliminate conflicts of interest is insufficient. A self imposed “abstention” can not act as a substitute for satisfying the requirements of RPC 1.7(b), including a client’s conflict waiver after informed consent (and especially under the facts presented here, where the Committee believes that any Bank-Municipality conflict is nonconsentable). A similar issue was recently addressed in ISBA Opinions 12-12 and 12-13. The question presented in those opinions was whether a lawyer could “recuse” himself in matters involving his representation of a government entity and matters brought before that entity by his partner and thereby continue to represent the government entity in other matters. The answer was that “recusal” was not appropriate. The same analysis is applicable here.

CONCLUSION

A lawyer serving as an officer of a financial institution and who owns a significant stock interest in it must comply with the requirements of RPC 1.8 to represent a municipality that engages in business transactions with the financial institution. However, the conflicts of interest raised by such a representation are so significant that they are nonconsentable by the municipality and would therefore bar the representation. Finally, merely abstaining from discussions of matters involving the financial institution and the municipality is insufficient to avoid the conflicts of interest.

Professional Conduct Advisory Opinions are provided by the ISBA as an educational service to the public and the legal profession and are not intended as legal advice. The opinions are not binding on the courts or disciplinary agencies, but they are often considered by them in assessing lawyer conduct.

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