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by
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It is axiomatic that a corporation is a distinct, discrete legal entity that exists separate and apart from its officers, agents, directors, and shareholders. It is almost equally axiomatic that a lawyer who is retained to represent a corporation owes his allegiance solely to that legal entity, and not to the corporation's officers, directors, and shareholders.[1]

These simple predicates, however, mask a morass when applied to the problems confronting the lawyer who represents a publicly held corporation that is the target of an unwanted tender offer or takeover. In this context, the lawyer's ethical problems have as their root cause the very nature of corporate existence. A corporation is a legal fiction. Its independent existence has been created out of statutory "whole cloth." Only by reason of legislative fiat has this "entity" been separated from its owners and its managers.

Therefore, we have the perverse situation in which the lawyer who represents a publicly held corporation is selected and retained by, and reports to and may be fired by, the principal officers and directors of the corporation—*who are not his clients.* Moreover, the shareholders of a corporation, who, collectively, are the owners of the mythical beast, typically do not participate in the process by which the lawyer is selected, retained, or fired. Furthermore, the attorney who represents the corporation does not consult nor owe any duty or allegiance of any kind whatsoever to the shareholders.[2]

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1. MODEL CODE OF PROFESSIONAL RESPONSIBILITY EC 5-18 (1980); MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.13 (1983).

2. Meehan v. Hopps, 144 Cal. App. 2d 284, 290, 301 P.2d 10, 14 (1956) (the attorney for a corporation represents the corporation stockholders and officers in their respective capacity and not its officers personally); *see* Egan v. McNamara, 467 A.2d 733, 739 (D.C. App. 1983) (only obligation of corporate attorney in drawing up a buy-sell agreement was to ensure the agreement was in the best interest of the corporation regardless of the impact on individual shareholders); Wayland v. Shore Lobster & Shrimp Co., 537 F. Supp. 1220, 1223-24 (S.D.N.Y.

The arguments underlying this seemingly preposterous result appear very straightforward:

A. A corporation is separate and distinct from its shareholders, directors, and officers and has an independent existence.

B. The legal and economic interests of a large, diverse group of shareholders may be internally adversarial.

C. The legal and economic interests of one or more groups of shareholders may conflict with the best interests of the corporation, when that entity is looked upon as a discrete, independent entity having a perpetual life of its own.

D. The officers of a publicly held corporation may have legal and economic interests directly adverse to the corporate entity which employs them.

E. The directors, although selected by the corporation's shareholders, may have legal and economic interests adverse to and conflicting with both the shareholders (or one or more groups of shareholders) and the corporation.

This analysis apparently convinced the Bar that an attorney retained by a publicly held corporation owes his undivided and unwavering allegiance to the corporation as a discrete entity. In the world of corporate takeovers, mergers, acquisitions, and break-ups, however, the assumptions upon which the conclusions rest seem less than solid. When a lawyer liquidates his corporate client and dissolves that entity or when his client disappears by operation of law, such as a merger in which the client is not the survivor, the lawyer presides over his client's voluntary destruction. Is it functional to argue that the lawyer's absolute allegiance to his corporate client, to the exclusion of that corporation's shareholders, permits the attorney to preside over his client's death?

Obviously, the question suggests the answer. The liquidation, dissolution, or disappearance of a corporation is clearly adverse to its interests. Such an action occurs *only* when the directors (and theoretically a majority of the shareholders) perceive that such action is in the *shareholders'* best interests.

The same issue arises in the payment of large liquidating dividends to fend off an unwanted takeover. Is the attorney who represents the

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1982) (no conflict of interest for general counsel of corporation when sued by former shareholder, officer, director of close corporation); Bobbitt v. Victorian House, Inc., 545 F. Supp. 1124, 1126, 1128 (N.D. Ill. 1982) (no conflict of interest for general counsel of corporation when sued by a shareholder, director); Goldstein v. Lees, 46 Cal. App. 3d 614, 618, 120 Cal. Rptr. 252, 255 (1975) (holding former counsel to a corporation cannot represent minority shareholder in a proxy fight to gain control of the corporation).

corporation "loyal" solely to the corporation if he designs such a dividend in order to foil an unfriendly tender offer? Whose interests are served by structuring a large debt burden solely for the purpose of distributing cash to existing shareholders? Clearly, the lawyer representing the corporation is representing the interests of the shareholders in these situations and not the interests of the corporation.

Other methods for inhibiting or fending off unwanted tender offers are less obviously adverse to the corporate client's interests. "Poison pills," staggered boards, and even "golden parachutes" might arguably be deemed to be in the best interests of the corporation, as an entity. Therefore, implementation of such plans by a lawyer representing a publicly held corporation seems to present less serious ethical problems for a lawyer, since he has the right to rely upon the decisions of his client's board of directors even if the utility or prudence of the defensive plans is doubtful.[3]

The lawyer must be cautious, however, even in these situations. If the lawyer acts on behalf of his client's officers, directors, or shareholders, ethical considerations involving conflicts of interest may easily exist. Since a corporation obviously can only act through its human representatives, it is sometimes painfully difficult for a lawyer to understand who he is really representing. When a board of directors asks the lawyer who represents the corporation to revise the corporate bylaws in order to create a staggered board, can the lawyer "assume" that he is representing the interests of the corporation, and not the interests of the officers?

The questions that I have raised make one realize that, in the corporate arena, the lawyer lives in an "Alice in Wonderland" world. The client to which he owes undivided loyalty, fealty, and allegiance cannot speak to him except through voices that may have interests adverse to his client. He is hired and may be fired by people who may or may not have interests diametrically opposed to those of his client. And finally, his client is itself an illusion—a fictional "person" that exists or expires at the whim of its shareholders, whom the lawyer does not represent.

It is not surprising, therefore, that to a great extent lawyers simply do not concern themselves with these ethical considerations, or if they do, become so frustrated in their application that they throw up their hands in despair. In the main, the Bar seems to position itself so as to avoid criticism or claims of unethical conduct by "papering" its position with the requisite legal formalities. The substance of the problem, however, remains untouched and untreated. Similarly, the Bench gives the

3. MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.13 comment (1982).

lawyer little guidance in this area. The limited number of cases that refer to the issues raised in this Essay pretend that corporate clients have a reality separate and apart from a corporation's officers, directors, and shareholders and should be treated as "natural persons" for purpose of the lawyer's ethical standards.[4]

Thus, illusion appears to have overcome reality.

Let us analyze the ethical problems presented in the preceding section to the following, somewhat simplistic scenario that commonly confronts the corporate lawyer. The firm of *AB&C* acts as outside counsel to Big Corporation, a publicly held company, incorporated under the laws of the State of California. One day the chief executive officer of Big Corporation calls Mr. *A*, a partner in the firm of *AB&C* for advice. The *AB&C* firm is retained by Big Corporation because of their skill and competence as corporate lawyers, *and* because Mr. *A* has been a close personal friend of the chief executive officer of Big Corporation for twenty years. The board of directors of Big Corporation consists of nine members, four of whom are officers of Big Corporation and five of whom are "independent" directors. Three of the independent directors comprise a substantial minority of shareholders of Big Corporation, and the other two are professional directors owning no shares of the corporation. The chief executive officer advises Mr. *A* that he has just received a letter from the chief executive officer of Biggest Corporation, indicating serious interest in tendering for all of the issued and outstanding stock of Big Corporation. The chief executive officer of Big Corporation tells Mr. *A* that he is concerned that if Biggest Corporation successfully acquires control of Big Corporation, he and his entire senior management will be fired; he implores Mr. *A* to do everything in his power to prevent an unwanted takeover. Shortly after this call, several "independent" members of the board of directors call Mr. *A* seeking advice concerning (1) their fiduciary obligations as directors; (2) the construction of appropriate defenses to the proposed takeover; and (3) the construction of "golden parachutes" or similar devices to protect the economic interests of both management and independent directors who receive substantial fees and emoluments by reason of their positions as board members.

At the outset, Mr. *A* must decide whether he can ethically advise the board of directors and also continue to represent Big Corporation. It is clear that advice relating to the board's fiduciary obligations does not conflict with Mr. *A*'s representation of the corporation. It is equally clear, however, that the economic interests of management and the board

4. *See supra* note 2.

may conflict with the interests of the corporation. Therefore, Mr. *A* may well advise the board to create a committee of the board of directors, consisting of the independent directors to evaluate the desirability of remaining independent.

Mr. *A*, however, being a cautious lawyer, will probably urge the independent committee to retain separate counsel and to employ the services of an investment banker to rationalize the committee's decision to accept or reject Biggest Corporation's tender. Mr. *A* will then turn to his friend of twenty years and advise him that, although he can represent Big Corporation in connection with certain matters including the construction of "golden parachutes," he cannot represent his old and loyal friend in that endeavor. He will make this clear in writing and will recommend that his friend retain separate counsel to represent the beneficiaries of the "parachutes." Mr. *A* may advise the shareholder directors that he cannot advise them with respect to their rights as shareholders and may advise them to seek independent counsel to obtain that advice. Finally, Mr. *A* will probably instruct both the officers and directors of Big Corporation that they must put aside their individual economic concerns, disregard the possibility that they may lose a substantial portion of their livelihood, and act solely in accordance with the heavy fiduciary responsibility imposed upon them by the law.

If this scenario does not remind one of Lewis Carroll, it should remind one of Kafka. Mr. *A*, however, will not be subject to criticism by either the Bench or Bar because of any failure to fulfill his ethical responsibilities, as established by the Model Code or the Model Rules. He will have carefully documented all of the possible conflicts between the various players, allocated each conflicting group to a separate law firm, and fulfilled his ethical responsibilities to the letter.

It is equally clear, however, that illusion has transcended the realities of the situation. The management directors of Big Corporation cannot possibly set aside their concerns over their livelihood. The independent directors cannot set aside their concerns over the loss of their directors' fees and emoluments; the shareholder directors cannot set aside their concerns as shareholders; and Mr. *A* cannot possibly forget who hired him and who can fire him. Yet Mr. *A* is entitled to rely upon the judgment of the board of directors with respect to their judgment as to what is in the best interests of Big Corporation, even if that decision flies in the face of reason—so long as the decision does not involve an unlawful act.[5] Mr. *A* may safely and ethically construct the "golden parachutes," create the "poison pills," and erect the barricades designed to prevent the unwanted suitor from gobbling up his client. He is now free to represent the interests of Big Corporation to the exclusion of the interests of its officers, directors and shareholders, all of whom are safely represented by other lawyers.

It seems to me that the Bar should re-think some of the fundamental assumptions underlying the principle that a corporate lawyer owes his allegiance solely to the legal entity he represents. Perhaps lawyers representing corporations should not have abstractions as clients. Rather, in reality, they should owe their duty of loyalty to the boards of directors who hire them and can fire them. The law has imposed a heavy fiduciary burden on the board to conduct its activities solely in accordance with the shareholders' best interests. Therefore, proper advice to the board of directors should insure adequate representation of the corporation, which is, after all, merely the vessel which holds assets belonging to the shareholders. If the directors perform their responsibilities properly, the corporation's interests when viewed as a separate entity become a *non sequitur*. It is the shareholders' interests which should be paramount, and the existence, destruction, or liquidation of the corporation should only have meaning when viewed from the perspective of the shareholders. This suggestion would bring the professional responsibilities of the corporate attorney closer to reality.

5. Ethics Committees of the Los Angeles County Bar Association, Formal Op. No. 353 (1976).