

Future Conflict Waiver Allows Firm to Representation Adverse to Former Client

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GEM Holdco, LLC v. Changing World Technologies, L.P., 46 Misc. 3d 1207(A), 7 N.Y.S.3d 242 (Sup. Ct. New York County Jan. 9, 2015), *aff'd*, 2015 WL 4112529 (1st Dep’t 2015)

Brief Summary

A law firm represented two sets of codefendants who later became adversaries; the firm then continued to represent one of the sets of defendants against the former clients. The New York Supreme Court, Appellate Division, First Department, held that because the defendants had specifically waived any conflicts that might arise from the joint defense arrangement, the firm would not be disqualified from its representation of the defendants.

Complete Summary

In March 2013, GEM Holdco, LLC (GEM) brought an action against the “CWT Defendants” seeking to enjoin them from selling defendant Changing World Technologies, L.P. (CWT) to Ridgeline Energy Services, Inc. (Ridgeline) and Dennis Danzik (Danzik) (collectively the “Ridgeline Defendants”). The CWT Defendants retained the law firm of Schalm Stone & Dolan LLP (Schalm Stone) as counsel because the firm had satisfactorily represented them in the past.

In April 2013, GEM amended its complaint, asserting claims against the Ridgeline Defendants. Pursuant to an agreement between the defendants, the CWT Defendants had to pay for the Ridgeline Defendants’ legal costs. It was, therefore, suggested by the CWT Defendants that Schalm Stone represent all of the defendants. At the time, GEM’s claims against both sets of defendants concerned the same issues, and their interests appeared to be aligned.

Accordingly, Danzik signed a “retainer letter” with Schalm Stone. The letter expressly contemplated future conflicts between the CWT Defendants and the Ridgeline Defendants.

At the present time, based upon the facts known to us, including those supplied to us by you, we do not perceive any actual conflict of interest between [the CWT Defendants and the Ridgeline Defendants]. We understand, of course, that in this case of joint representation, there is a possibility that the CWT Defendants’ status as ongoing clients of [Schalm Stone] could be perceived as adversely affecting our ability to represent [the Ridgeline Defendants] with complete loyalty and exercise of independent judgment. Certainly, joint representation can result in shared and divided loyalty. Although we are not currently aware of any actual or reasonably foreseeable adverse effects of such shared or divided loyalty because everyone’s interests appear to be aligned, it is possible that issues may arise as to which of representation of [the Ridgeline Defendants] may be materially limited by our representation of [the CWT Defendants]. We bring this possibility to your [i.e., Danzik] attention so that you can decide for yourself whether you are sufficiently concerned with this possibility that you do not wish joint representation.

The letter further provided:

We anticipate that if a conflict or dispute were to arise or if any other reason joint representation does not continue, [Schalm Stone] would continue to represent [the CWT Defendants]. Accordingly, we are now asking [the Ridgeline Defendants] to consent to our continued representation of [the CWT Defendants], and to agree not to assert any such conflict of interest or seek to disqualify us from representing [the CWT Defendants] in this or any other matter, notwithstanding any adversity or litigation that may exist or develop. By signing and returning to us the agreement and consent set forth at the end of this letter, [the Ridgeline Defendants] are consenting to such an arrangement and waive any conflicts regarding that arrangement.

The Ridgeline Defendants were further advised in the retainer letter that their confidential, attorney-client communications would be shared with the CWT Defendants.

Schalm Stone thereafter represented both sets of defendants in the action. During the course of appearing in court to discuss discovery deadlines and disputes, Jeffrey Eilender of Schalm Stone explained that certain discovery from the Ridgeline Defendants had not been produced because Mr. Eilender’s relationship with the Ridgeline Defendants had broken down, leading him to file a motion to withdraw as counsel on July 25, 2014. Schalm Stone continued to represent the CWT Defendants.

The Ridgeline Defendants retained new counsel, and settled their disputes with GEM. However, at a discovery conference in September 2014, the Ridgeline Defendants advised the court that they would be moving to disqualify Schalm Stone from representing the CWT Defendants, claiming that a continued conflict existed due to cross-claims asserted by the CWT Defendants against the Ridgeline Defendants, and an action pending in Canada wherein the Ridgeline Defendants alleged that they were fraudulently induced to enter into the agreement with the CWT Defendants.

In their disqualification motion, the Ridgeline Defendants argued that Schalm Stone's continued representation of the CWT Defendants would violate Rules 1.7 and 1.9 of the New York Rules of Professional Conduct; they later conceded, however, that Rule 1.7 was not applicable because it governs conflicts of interest between current clients. Rather, Rule 1.9, which governs duties to former clients, applied. The issue was whether the conflict waiver in the retainer letter permitted Schalm Stone to continue representing the CWT Defendants. The court concluded that it did, and denied the motion to disqualify.

New York courts have recognized that where a valid waiver exists, the traditional concerns about confidential information are inapposite. The Ridgeline Defendants argued that the confidential information shared with an attorney in a joint representation inherently gives rise to the unfair advantages that Rule 1.9 seeks to prohibit, and warranted disqualification. But the court concluded that if the transmission of confidential information vitiated the validity of a conflict waiver notwithstanding the retainer letter's disclaimers to the contrary, virtually all conflict waivers would be ineffectual.

The Ridgeline Defendants further argued that the waiver was not made with informed consent as evidenced by the subsequent action against the CWT Defendants for fraud. The court disagreed. The retainer letter anticipated that a future conflict of interest between the parties could arise, and a dispute between the parties pursuant to their agreement was foreseeable, even if the dispute that had arisen in the Canada action was not specifically foreseen at the time the waiver was signed.

The Appellate Division for the First Department agreed, and affirmed the lower court's denial of the disqualification motion. In the retainer letter, the Ridgeline Defendants specifically waived any conflict of interest that might arise from the joint representation. Further, the Ridgeline Defendants' contention that they did not give informed consent to Schalm Stone's assertion of claims against them on behalf of the CWT Defendants in the underlying action was belied by the clear language of the retainer letter. The Ridgeline Defendants could "not now compel the disqualification of counsel simply because the representation to which [they] consented had since devolved into litigation." "Nor does the fact that [Schalm Stone] obtained confidential information from the Ridgeline [D]efendants warrant disqualification since the Ridgeline [D]efendants knowingly and expressly agreed in the retainer agreement to the firm's use of their confidential information and the disclosure of that information to the CWT [D]efendants."

Significance of the Opinion

The court upheld the waiver of future conflicts of interest, and allowed the continued representation of one client against the former client, even if information obtained during the joint representation from the former client could result in an advantage for the continuing client.