The Lawyer’s Business Dealings With Clients

In recent cases, Sodikoff v. The State Bar of California and Flanagan v. DeLapp, two state supreme courts have held that even in the absence of a formal attorney-client relationship, a lawyer may by his actions or representations assume a fiduciary duty comparable to that expected of an attorney by his client. In the event that such a fiduciary duty arises, the lawyer who acts adversely toward the interests of one who trusts his judgment stands subject to disciplinary action. This comment will consider several cases in which attorneys have been held to have breached the interests of “clients,” without the presence of a formal attorney-client relationship, and it will examine some of the factors which courts deem pertinent in analyzing such cases.

In Sodikoff v. The State Bar of California, for example, petitioner Sodikoff was the counsel of record for the administrator of the estate of a Mr. Wehrley’s deceased uncle. Wehrley and his uncle had owned certain real property as joint tenants, and following the uncle’s death, Mr. Wehrley was awarded the land in a suit to quiet title. As attorney for the uncle’s estate, Sodikoff wrote Wehrley, an elderly gentleman living abroad, to ask whether Wehrley would like to have petitioner continue to manage the property and to obtain a buyer. Wehrley replied that he wanted petitioner to dispose of the real estate. Subsequently, Sodikoff informed Wehrley that a client corporation had offered a price of 20,000 dollars, a figure less than half the price at which the land had been valued in the estate. Moreover, the alleged corporation was actually Sodikoff’s alter ego, and at the time of the offer it had not even been incorporated. After Sodikoff’s law associate learned of the offer, he advised Wehrley not to accept. Thus, the sale was never consummated.

The Supreme Court of California affirmed the attorney’s six months suspension from the practice of law on the ground that, even though there was no formal attorney-client relationship, the attorney had voluntarily assumed a position of trust and confidence vis-a-vis Mr. Wehrley with respect to the property in issue. The court found that Sodikoff must have known that Wehrley would rely upon

2. 533 S.W.2d 592 (Mo. 1976).
3. 14 Cal. 3d at 429, 535 P.2d at 335, 121 Cal. Rep. at 471.
his judgment and assistance in disposing of the property and, hence, that the attorney had breached a duty of trust. Sodikoff asserted that his statements concerning the supposed purchaser of the property did not actually induce Wehrley to sell his land. Rejecting this argument, however, the court emphasized that the issue was simply "an inquiry into whether petitioner ha[d] lived up to the high ethical standards of his profession." Hence, a mere knowing attempt by the attorney to gain a personal advantage by means of deceit was sufficient proof that he had not acted properly under the circumstances.5

In the second case, Flanagan v. DeLapp, action was brought by the administratrix of the estate of her deceased brother to set aside a deed granted by the deceased to attorney DeLapp on the ground of undue influence. Although the evidence in the case did not disclose that the defendant had served as attorney for deceased in any individual matters, the court found that the only attorney-client relationship which deceased had had with any lawyer was the one with DeLapp in connection with the guardianship of the estate of deceased's brother. As the court stated, "[t]hat relationship had continued over a long period of time and was one in which deceased would look to and rely upon DeLapp for professional and confidential advise and information."6 In affirming the decree of the circuit court setting aside the deed, the Missouri Supreme Court considered that evidence that the deed was executed seven days before the death of the grantor, while grantor was in the hospital after having suffered a stroke, was sufficient to support a finding that the deed had been procured by undue influence.7

The ABA Code of Professional Responsibility has codified the widely recognized rule that a lawyer may not acquire a proprietary interest in the cause of action or subject matter of the litigation he is conducting for a client.8 One Missouri case explains that public policy dictates the necessity to protect the confidential and fiduciary attorney-client relationship. "Consequently," the court says, "when a conveyance from a client to an attorney is attacked it is considered presumptively fraudulent, and the burden is on the at-

4. Id. at 431, 535 P.2d at 336, 121 Cal. Rep. at 472.
5. Id.
6. 533 S.W.2d at 596 (Mo. 1976).
7. Id. at 597.
torney to prove . . . that the transaction . . . was fair and equitable in every respect." For years courts have searched for viable criteria by which to judge the fairness of such purchases, and the guidelines that have developed may be applicable in an attorney's non-employment-related business dealings as well.

In an early landmark case, *McFail v. Braden*, the court required that an attorney include in this proof of fairness (1) that he made a full and frank disclosure of all the relevant information which he possessed; (2) that the consideration was adequate; and (3) that the principal had independent advice before completing the transaction. There is abundant historical support for this triple-requirement analysis, although the presence of independent advice (the third element of *McFail*) is seldom mentioned in more recent cases.

*Deal v. Migoski* suggests why the requirement of showing full consideration (the second element of *McFail*) has also recently been discarded. In that case Deal hired an attorney, Migoski, to settle his grandmother's estate, for which Migoski was to receive as his fee one third of Deal's distributive share. When Deal later became unemployed and desperately in need of money, he sought advice from Migoski as to the price he should ask for his interest in the estate. The attorney suggested a price well below his estimate of what a speculative buyer would be willing to pay for the property. After unsuccessful attempts to procure a buyer, Deal consented to let Migoski sell the land. Claiming he had a buyer, Migoski "advanced" Deal the money and kept that share of the estate for himself. The court reversed a judgment for the attorney in an action by Deal to rescind the contract, because, as the majority reasoned, the attorney had not met the burden of proving full consideration. A concurring opinion, however, suggests that as attorney for the seller, Migoski was obligated to pay his estimate of the property's speculative value, and not his estimate of its present fair market value, which would probably suffice as full consideration for most buyers. In other words, full consideration is a variable concept, depending upon the nature of the sale and the relationship between buyer and seller. Hence, of the three factors given in *McFail v. Braden*, that of full disclosure seems to have become the most signifi-

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10. 19 Ill. 2d 108, 166 N.E.2d 46, 52 (1960).
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icant. For example, in *In re Bond and Mortgage Guarantee Co.*, attorneys for the trustees for holders of mortgage certificates bought certain of these certificates from brokers at depressed market values, which would ordinarily have been deemed to be full consideration from any disinterested buyer. The court states that the question of bad faith or damage is irrelevant, and that the attorneys, like the trustees, owed to these certificate holders the duties of "complete unselfishness" and "inflexible loyalty." Although the attorneys, when asked, advised the certificate holders not to sell at the then depressed prices, the court found that they did not inform such holders that they were buying the certificates. Consequently, the attorneys were unable to show that they had made a full disclosure of their actions with respect to the subject property.

The ABA Code of Professional Responsibility supports the use of the single requirement of full disclosure by providing that a lawyer may not enter into a business transaction with a client if they have differing interests in the transaction and if the client expects the lawyer to exercise his professional judgment for the protection of the client unless the client has consented after full disclosure. This requirement of full disclosure has been invoked successfully in cases wherein the attorney is found to have bought his client's property, albeit for a fair price, through a third person, or "straw party." The court in *Bank of Mill Creek v. Elk Horn Coal Corporation* explains:

> there was a concealment of the real purchaser's identity, and regardless of the tacit understanding, the payment of an adequate consideration, and the fact that the appellants acted in good faith, we do not think they can avoid the effect of well settled principles controlling and governing the relationship between attorney and client.

The concurring opinion in *Deal v. Migoski* quotes from Black's Recission and Cancellation the rule that an attorney's duty of full disclosure is

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13. Id., 103 N.E.2d at 726.
14. ABA Code, DR 5-104; see also Ethical Consideration [hereinafter cited as EC] 4-5.
16. 133 W. Va. 639, 57 S.E.2d 736, 748-49 (1949). This case involves a breach of fiduciary responsibility by the attorney for a receiver of property. See note 32 infra and accompanying text.
disclosure to his client involves not only “refraining from all misrepresentation and concealment,” but the affirmative responsibility of affording the client information about “the nature of the transaction and of his own rights and interests, either by independent advice or else by such advice from the attorney himself as he would have given if he had been a stranger to the transaction.”17 In addition to the burden of proving full disclosure, the attorney must also be able to show that any dealings with his client were fair and free from “undue influence.”18 This burden is particularly difficult when the client is elderly and enfeebled19 or under extreme financial stress.20

The rule most in dispute regarding an attorney's responsibilities when carrying on business dealings with his client is one which limits the fiduciary duties to matters within the scope of the employment. A 1947 case involving an attorney's ability to purchase stock on the open market from his corporate client stipulates that the obligations and duties of a fiduciary are restricted by the employment and do not apply to acts disassociated therefrom, and they do not preclude an attorney or other fiduciary from making personal investments not within the scope of the employment or the result of use of confidential information procured therefrom.21 However, the court in Flanagan v. DeLapp revives the language of a 1923 Missouri case which explicitly provides that the attorney's burden of proving perfect fairness on his part is not restricted to dealings with respect to the property in controversy in the particular proceeding in which the attorney is acting for the client.22 This latter view would seem to be a more accurate statement of the law, especially in light of the cases mentioned at the outset, which hold attorneys liable for deceit in business dealings despite the absence of formal employment.

17. 122 So. 2d at 419-20. See 1 BLACK, RECISION AND CANCELLATION § 51 (2d ed. 1929).
18. See e.g., Flanagan v. DeLapp, 533 S.W.2d 592, 597 (Mo. 1976); McFail v. Braden, 19 Ill. 2d 108, 117, 166 N.E.2d 46, 52 (1960).
Nevertheless, it cannot be said that an attorney may never engage in sales transactions with a client. Authority that an attorney is permitted to purchase real estate from his client under certain circumstances is found in a 1975 case, *Ruth v. Crane.*23 There, the defendant in a suit for specific performance of a contract for sale of land was the client of the plaintiff-attorney, with whom she apparently shared a close personal friendship. The defendant, Mrs. Crane, offered to sell her thirteen acres to the plaintiff because she was having difficulty meeting mortgage payments. Unable to buy the property himself, the plaintiff shortly thereafter entered into a partnership for the purpose of purchasing the land, and after informing the defendant of his role in the transaction and of the legal consequences to her, he prepared the deeds in order to complete the transaction. The attorney also suggested that she might procure another attorney in the matter, but it appears that she never did. The court found that the plaintiff met the burden of demonstrating that the transaction was fair and conscionable and that he did not take advantage of his client.24

*Ruth v. Crane* receives support from *McCray v. Weinberg*25 which upholds the validity of a mortgage on plaintiff’s home given by the plaintiff to his attorney, where there had been a “series of loan transactions between the parties extending over a period of years,” where the plaintiff was an experienced businessman, and where “the interest rate, though high, was concededly legal.”26 The court quotes from a case using the language from Black27 which requires an affirmative duty of disclosure, and it puts to rest the earlier supposition that absent independent advice every transaction between attorney and client must be set aside.28 The result of an empirical study by the court of the history of relations between this attorney and client was simply that there was no overreaching, and no breach of the fiduciary relationship.29

The discussion thus far has centered on the extent of an attorney’s fiduciary responsibility to a client whom he has been hired to represent. The rules regarding an attorney’s duty when no such

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24. Id. at 731.
26. Id. at 521.
27. 1 BLACK, supra note 17; see note 17 supra, and accompanying text.
29. Id.
relationship exists are not as definitive because of the paucity of cases making that distinction.

Before Sodikoff and Flanagan it appears that there was always an employment situation indirectly if not directly involved when an attorney was found liable to a person not his client. For example, in a 1944 case, 536 Broad Street Corp. v. Valco Mortgage Co., the court held that even though the attorney-client relationship had terminated, the attorney had breached his duty by using confidential knowledge or information acquired from the past connection.

In another type of case, courts have found a breach of fiduciary duty by attorneys for trustees and receivers who were found to have purchased property belonging to beneficiaries. Here, although there is an employment situation indirectly related, it is clear that a relationship of trust is found to exist between the attorney and third persons. In In re Bond and Mortgage Guarantee Co., the New York Court speaks of the trustee's fundamental duty of unselfish and inflexible loyalty, and quotes from the appellate division that "by reason of their status as attorneys for the trustee, [they] were no less fiduciaries than was the trustee himself." This rule of law has become so widely accepted that courts have blurred the distinction between these cases and those involving formal attorney-client relationships. Logically, rules of conduct identical to those discussed earlier with respect to actual clients have been imposed on attorneys in cases of this nature.

Presbyterian Church v. Plainfield Trust Co. shows a similar analysis of the duty owed to legatees under a will by the attorney for the executor. Quoting the most important case authority from a number of states, the court emphasizes that if the executors and trustees of a decedent's estate assume a fiduciary duty to represent and defend the interest of all beneficiaries, then their attorneys accept the same obligatory fidelity to those having an interest in the

33. The case of In re Bond and Mortgage Guarantee Co. was before the court for the purpose of determining "whether the attorneys had observed the rule of full disclosure to the beneficiaries with whom they were dealing." 303 N.Y. 423, 103 N.E.2d 721, 723 (N.Y. Ct. App. 1952).
34. 139 N.J. Eq. 501, 52 A.2d 400 (1947); contra, Colorado v. The Ohio Casualty Ins. Co., 232 F.2d 474 (10th Cir. 1956).
administration of the estate.\textsuperscript{35}

Demonstrably, courts have found various policy reasons for holding attorneys to high standards of conduct when dealing with persons not strictly their clients, without expressly noting that in such cases a formal attorney-client relationship simply does not exist. Perhaps the most significant result of \textit{Sodikoff} and \textit{Flanagan} is a recognition that the professional responsibility of an attorney might include some situations in which the attorney "voluntarily assumes a position of trust and confidence" with respect to persons not ordinarily owed a fiduciary duty. Thus far it is unclear to what extent if any these cases will result in a broadening of an attorney’s responsibilities in dealing with the general public, but that question will probably turn on a determination of what actions by the attorney will constitute a voluntarily assumed fiduciary duty and/or reliance by the "client." The court in \textit{Sodikoff} found that, because of his letter implying that he would continue to manage the estate properly, the attorney "must have known that Mr. Wehrley would be likely to rely on him, as attorney for his uncle’s estate, for guidance and assistance in dealing with property that he could not personally dispose of or manage."\textsuperscript{36} There was also a connection between the attorney and the deceased’s family in \textit{Flanagan} that served as strong evidence of reliance in the opinion of the court.

Finally, \textit{Sodikoff}, considered together with \textit{Ruth v. Crane}, indicates a tendency to distinguish the standards for testing an attorney’s professional fitness from those employed by courts of equity in determining the validity of contracts for sale of land to attorneys. The court in \textit{Ruth v. Crane}, while holding that no harm was shown and that therefore the contract was valid, adds that in light of its "duty when presented with conduct of an attorney which violates the stringent requirements set forth in the \textit{Code of Professional Responsibility} to report the possible violation,"\textsuperscript{37} it would forward a copy of the order to the Disciplinary Board of the Supreme Court of Pennsylvania. Similarly, the \textit{Sodikoff} court explains that "an act of violating professional standards of behavior is not excused merely because the client or a third person suffers no loss," adding that an attorney’s "fitness is called into question when as here, the record

\textsuperscript{35} Presbyterian Church of Flemington v. Plainfield Trust Co., 139 N.J. Eq. 501, 52 A.2d 400, 406 (1947).
shows a knowing attempt by the attorney to gain a personal advantage by means of deceit."

In this author’s opinion, a distinction between the requirements for professional competency and those applied in evaluating an attorney’s business dealings is highly artificial. The remedy (or penalty, as the case may be) for breach of a fiduciary duty by an attorney will necessarily vary according to the nature of the proceeding, but the standards should arguably be the same. However, a gradual extension of the professional responsibility of attorneys to include implied as well as formal attorney-client relationships seems quite likely in light of recent case law and the close public scrutiny of the legal practice.

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