

**THE PROFESSIONAL ETHICS COMMITTEE
FOR THE STATE BAR OF TEXAS
Opinion No. 626**

April 2013

QUESTION PRESENTED

Under the Texas Disciplinary Rules of Professional Conduct, may a lawyer, who had formerly represented a corporation in circumstances where the lawyer came to possess confidential proprietary information relating to the former client's competitive position in its market, make a significant investment in a new business that will compete with the former client's business?

STATEMENT OF FACTS

A lawyer represented Corporation A in several matters including the sale of Corporation A to an unrelated corporation. During the course of the representation, the lawyer had access to a range of non-public information concerning Corporation A's business, including proprietary information belonging to Corporation A that gives Corporation A a competitive advantage in its field. The lawyer's representation of Corporation A ended with the sale of the corporation. After the sale, Corporation A has continued to conduct the same business it conducted before the sale. Several months after the sale of Corporation A, the lawyer makes a significant investment in a new corporation, Corporation B, which he knows is intended to compete with Corporation A. The lawyer is not involved in the organization or formulation of the initial business plan of Corporation B and he does not provide legal services or otherwise participate in the management or operation of Corporation B's business. Corporation A has not consented to the lawyer's use of its confidential information to the disadvantage of Corporation A.

DISCUSSION

Although Corporation A has been sold by its prior owners and has not been represented by the lawyer since the sale, the lawyer remains obligated to protect from disclosure proprietary information he acquired during the representation of Corporation A. The lawyer is also prohibited from using the proprietary information to the disadvantage of Corporation A. These obligations of the lawyer to Corporation A, as the lawyer's former client, are not eliminated or diminished by the fact that Corporation A has new owners following its sale. With respect to information that is obtained by a lawyer in the course of the lawyer's representation of a client and that has not become generally known, after the termination of the representation the lawyer has continuing obligations to the former client not to reveal the information and not to use the information to the disadvantage of the former client.

Rule 1.05 of the Texas Disciplinary Rules of Professional Conduct provides in relevant part:

“(a) ‘Confidential information’ includes both ‘privileged information’ and ‘unprivileged client information.’ ‘Privileged information’ refers to the information of a client protected by the lawyer-client privilege of Rule 503 of the Texas Rules of Evidence or of Rule 503 of the Texas Rules of Criminal Evidence or by the principles of attorney-client privilege governed by Rule 501 of the Federal Rules of Evidence for United States Courts and Magistrates. ‘Unprivileged client information’ means all information relating to a client or furnished by the client, other than privileged information, acquired by the lawyer during the course of or by reason of the representation of the client.

(b) Except as permitted by paragraphs (c) and (d), or as required by paragraphs (e) and (f), a lawyer shall not knowingly:

(1) Reveal confidential information of a client or a former client to:

(i) a person that the client has instructed is not to receive the information;

or

(ii) anyone else, other than the client, the client’s representatives, or the members, associates, or employees of the lawyer’s law firm.

....

(3) Use confidential information of a former client to the disadvantage of the former client after the representation is concluded unless the former client consents after consultation or the confidential information has become generally known.”

In the circumstances here considered, none of the exceptions to the lawyer’s obligations specified in paragraphs (c), (d), (e) and (f) of Rule 1.05 are applicable. Rule 1.05(b)(3) would permit the use of confidential information to the detriment of a former client if the former client gave consent after consultation or if the confidential information has become generally known. In addition, it is permissible for a lawyer to act to the disadvantage of a former client so long as he can do so without breaching his continuing obligations to the former client, including those involving confidential information. See e.g. Professional Ethics Committee Opinion 544 (April 2002).

Knowing that Corporation B will be competing with Corporation A, the lawyer makes a significant investment in Corporation B. The lawyer has confidential information of Corporation A including proprietary information that gives Corporation A a competitive advantage in its market. The lawyer’s decision to invest in Corporation B is made at a time when the lawyer’s information concerning Corporation A continues to be relevant to Corporation A’s current business operations and such confidential information is part of the lawyer’s knowledge that he uses in making the decision to invest in Corporation B. The funds invested by the lawyer will be used by Corporation B to its own advantage and, since Corporation B competes with Corporation A, this use of the lawyer’s funds will be to the disadvantage of Corporation A. In addition, a significant investment by the lawyer in Corporation B could reveal to interested persons information concerning the lawyer’s assessment of Corporation A that is based on confidential information obtained by the lawyer in his representation of Corporation A. Thus the

lawyer, in using confidential proprietary information belonging to Corporation A in the decision to make a significant investment in a competitor of Corporation A, will be using such confidential information to the disadvantage of Corporation A in violation of Rule 1.05(b)(3) and may also be revealing to interested persons confidential information concerning Corporation A in violation of Rule 1.05(b)(1).

It should be noted that the lawyer's decision to invest in Corporation B might not violate Rule 1.05 if the lawyer's investment were not significant for Corporation B. The lawyer's investment would not be significant if it was a sufficiently small portion of the total amount invested in Corporation B and there were other investors ready to make an investment in the same amount if the lawyer did not. In that case, the lawyer's investment would make no difference in the business operations of Corporation B and no disadvantage to Corporation A would result from the lawyer's investment. Moreover, if the lawyer's former representation of Corporation A had been limited in scope so that he had not gained any confidential information that would be relevant to Corporation B's business, then the lawyer would not be using confidential information concerning Corporation A when the lawyer invested in Corporation B. Whether an investment is significant to a corporation's business or whether a lawyer in a prior representation acquired confidential information that continues to be relevant to a competing business at the time of a lawyer's investment in the competing business are questions that can only be answered based on consideration of the facts of a specific situation.

CONCLUSION

Under the Texas Disciplinary Rules of Professional Conduct, a lawyer who had formerly represented a corporation in circumstances where the lawyer came to possess confidential proprietary information of the client corporation relating to the former client's competitive position in its market is not permitted to make a significant investment in a new business that the lawyer knows will compete with the former client's business at a time when the confidential information concerning the former client remains relevant to the former client's current business. The prohibition will no longer apply when confidential information possessed by the lawyer with respect to the former client ceases to be relevant to the current business operations of businesses competing with the former client.