# Will the *Real* Intended Third-Party Please Stand Up?


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TRADITIONALLY, absent fraud or collusion, the only parties with standing to sue an attorney for malpractice were those in privity of contract with the attorney, that is, the lawyer's clients.[1] However, over the past several decades, the traditional "privity" doctrine has eroded as courts have begun to allow beneficiaries of an attorney's estate-planning services to bring malpractice claims.[2] The modern trend in the estate-planning context is to recognize the existence of an attorney's duty to those outside the attorney-client relationship. Outside the estate-planning context, the legal landscape is less clear.

This article addresses three legal doctrines that have been found to provide non-clients with standing to sue an attorney: the third-party beneficiary rule (outside the context of wills, estates, and trusts), the implications of opinion letters, and the potential exposures that lawyers face to non-clients for fraud, and aiding and abetting the alleged wrongful conduct of their clients.

## I. Attorney Malpractice Liability to Non-Clients

In certain contexts, courts have found that a non-client has standing to sue an attorney for malpractice. They have done

[1] *See, e.g.*, Berry v. Dodson, Nunley & Taylor, P.C., 717 S.W.2d 716, 718 (Tex. Ct. App. 1986) ("It has long been the majority view in this country that an attorney will not have to answer for his negligence to a party not in privity of contract with him in the absence of fraud or collusion.") (citing Nat'l Sav. Bank v. Ward, 100 U.S. 195 (1879)).

[2] *See, e.g.*, Berry, 717 S.W.2d at 718 (acknowledging that there is a trend to the contrary of the majority view, "[p]articularly when the plaintiffs are the intended beneficiaries of negligently drafted or executed wills.") (collecting cases).

so under a number of different theories. The first approach is a multi-criteria balancing test, which originated in California.[3] A related approach adopts a contractual third-party beneficiary analysis, which requires that the non-client be a "direct and intended beneficiary" of the attorney's services before the courts will impose a duty.[4] Another approach is contained in the Restatement (Third) of the Law Governing Lawyers Section 51(3);[5] however, this approach has been widely criticized as unworkable.[6]

A more recent trend has been the recognition of an attorney's duty of care to non-clients outside the estate-planning context. With few exceptions, courts recognizing this duty of care have applied some version of the third-party beneficiary theory, requiring that non-clients be "direct and intended beneficiaries" of the transaction for which the client has engaged the attorney's services.

The cases below are some of the most recent and important decisions regarding this issue. They highlight the factual contexts in which courts have recognized, and have refused to recognize, the standing of a non-client in a legal malpractice action.

## A. McIntosh County Bank v. Dorsey & Whitney, LLP[7]

*McIntosh* provides a good starting point from which to survey the contours of this evolving doctrine. The case involved a syndicated lending transaction and asked whether the attorneys for the lead bank in the transaction could be held liable in malpractice to the banks participating in the loan as investing third parties. Plaintiffs, thirty-two banks participating in a syndicated loan transaction originated by lead bank, Miller & Schroeder ("M & S"), collectively sued legal counsel for M & S – Dorsey & Whitney, LLP ("Dorsey") – alleging that it had committed legal malpractice and breached fiduciary duties owed to the participating banks in structuring the loan.

M & S closed two loans to a company (the "Company") formed to develop and manage a casino on the reservation of the St. Regis Mohawk Tribe (the "Tribe") in the State of New York. During Dorsey's preparation of the loan documents, a question arose as to whether National Indian Gaming Commission ("NIGC") approval of some of the documentation was required. Dorsey knew that failure to

[3] *See, e.g.*, Lucas v. Hamm, 364 P.2d 685, 688 (Cal. 1961).

[4] *See, e.g.*, Flaherty v. Weinberg, 492 A.2d 618 (Md. 1985) (as to the existence of the seller's attorney's duty to the buyer of real property, the non-client must allege and prove that the intent of the client to benefit the non-client was a direct purpose of the transaction or relationship); Pelham v. Griesheimer, 440 N.E.2d 96 (Ill. 1982) (as to the existence of the divorce attorney's duty to children of divorcing parents, same).

[5] RESTATEMENT, Section 51(3) reads, in pertinent part: [A] lawyer owes a duty of care … to a nonclient when and to the extent that: (a) the lawyer knows that a client intends as one of the primary objectives of the representation that the lawyer's services benefit the nonclient; (b) such a duty would not significantly impair the lawyer's performance of obligations to the client; and (c) the absence of such a duty would make enforcement of those obligations to the client unlikely.

[6] Several commentators have questioned the Restatement approach, noting several substantial deviations from the intended beneficiary approach that render it unwieldy, inconsistent, and ultimately unworkable. *See, e.g.*, Ronald E. Mallen and Jeffrey M. Smith, 1 LEGAL MALPRACTICE § 7:8 (2012 Ed.); Kevin H. Michaels, *Third-Party Negligence Claims Against Counsel: A Proposed Unified Liability Standard*, 22 GEO. J. LEGAL ETHICS 143, 157–159 (2009).

[7] 745 N.W.2d 538 (Minn. 2008).

obtain NIGC approval might place the participating banks' interest in the collateral at risk, but advised M & S that NIGC approval was not required. Dorsey failed to advise M & S of the risks to closing without NIGC approval. M & S would not have closed the loans if it had known the risk of closing without NIGC approval. The loans closed without approval from the NIGC. M & S then sold most of the participation interests in the loans to plaintiffs. Shortly thereafter, the Tribe defaulted on the loans. Because the NIGC had not approved the changes, plaintiffs lost their interest in the collateral.

Affirming the trial court's grant of summary judgment in favor of Dorsey, the Minnesota Supreme Court extended the application of the California balancing test and found that non-clients could gain standing to sue an attorney for malpractice outside the estate-planning context. In doing so, it reaffirmed the threshold requirement that to have standing to sue an attorney for malpractice, a non-client "must be a *direct and intended beneficiary* of the attorney's services."[8] The court defined a "direct beneficiary" to require that the benefit to the non-client be the "end and aim of the transaction" in which the attorney rendered his services.[9] It did so to "prevent nonclients who receive incidental benefits from the representation, or who only receive downstream benefits, from holding the attorney liable."[10]

The court also required that the attorney "must be aware of the client's intent to benefit the third party," before a non-client could gain standing to sue.[11] Even if the client intended the attorney's work to benefit a third-party, unless the attorney acted knowing of that intent, the attorney owes no duty of care to the third-party. "Such a requirement is in keeping with the fiduciary and ethical duties attorneys owe their clients. Imposing on attorneys a duty toward beneficiaries of whom they are unaware would risk dampening their zealous advocacy on behalf of clients, for fear of harming a third party to whom a duty might later be found."[12]

Applying these principles to the facts of the case, the Minnesota Supreme Court found that the participating banks "were not direct and intended beneficiaries of the attorney-client relationship between M & S and Dorsey."[13] The court emphasized that this situation was "far from the will-drafting context in which the third-party beneficiary theory was first developed."[14] Because plaintiffs' position relative to the transaction "was that of parties with whom defendant's clients might negotiate a bargain at arm's length," they could not have been direct and intended beneficiaries of the attorney-client relationship.[15]

[8] *Id.* at 547 (emphasis added).

[9] *Id.* (quoting Glanzer v. Shepard, 135 N.E. 275, 275–276 (N.Y. 1922)).

[10] *Id.*

[11] *Id.*

[12] *Id.* at 548.

[13] *Id.*

[14] *Id.*

[15] *Id.* (quoting Goodman v. Kennedy, 556 P.2d 737, 743 (Cal. 1976)). In *McIntosh*, the court made note of the fact that Dorsey had no knowledge of the plaintiffs' identities prior to the closing of the loans. *Id.* at 543. In a subsequent unpublished opinion, the Minnesota Court of Appeals stated that mere awareness of the identity of a non-client was insufficient to grant standing to sue the attorney for malpractice; it was "a distinction without a difference." Alerus Fin., N.A. v. St. Paul Mercury Ins. Co., 2012 WL 254484 at *3, A11-680 (Minn. Ct. App. Jan. 30, 2012).

### B. State of California Public Employees Retirement System v. Shearman & Sterling[16]

In *Shearman & Sterling*, the New York Court of Appeals decided a closer question. Addressing whether California Public Employees' Retirement System ("CalPERS") was an intended third-party beneficiary of the relationship between one of its business partners and their counsel, the court applied a form of the "direct and intended beneficiary" test later articulated in *McIntosh*.

CalPERS sued Shearman & Sterling for professional negligence following the default of a loan it had acquired from Shearman & Sterling's client, Equitable Real Estate Investment Management, Inc. ("Equitable"). The New York Supreme Court dismissed CalPERS' direct causes of action because CalPERS failed to demonstrate that it was an intended third-party beneficiary of the work Shearman & Sterling performed on behalf of Equitable. CalPERS appealed.

Pursuant to an agreement between CalPERS and Equitable (the "Agreement"), Equitable originated and closed commercial property loans for sale and assignment to CalPERS. Sherman & Stearling represented Equitable in connection with the loans. In the course of their relationship, CalPERS and Equitable developed standard form loan documents, including a promissory note that contained a prepayment and acceleration penalty, which they used in their loan transactions. CalPERS asked Shearman & Sterling to incorporate the standard promissory note into the loan documents. However, during negotiation of a commercial loan between Equitable and the borrower, the terms of the standard form loan documents were modified; the acceleration clause in the promissory note had been changed. Shearman & Sterling provided a draft note to CalPERS, which had been black-lined to reflect changes in the loan documents. CalPERS made no objection to the loan documents. Following the closing, Equitable assigned the loan to CalPERS. The borrower later defaulted and, when CalPERS accelerated the loan, discovered that the acceleration fee had been reduced, which harmed CalPERS.

The Court of Appeals found the allegations in the complaint insufficient to establish that CalPERS was an intended third-party beneficiary of the work Shearman & Sterling performed on behalf of Equitable. In addressing CalPERS' argument it was an intended third-party beneficiary of the legal services Shearman & Sterling provided to Equitable, the court stated:

> A party asserting rights as a third-party beneficiary must establish (1) the existence of a valid and binding contract between other parties, (2) that the contract *was intended for his benefit* and (3) that *the benefit to him is sufficiently immediate*, rather than incidental, to indicate the assumption by the contracting parties of a duty to compensate him if the benefit is lost.[17]

The court found a valid and binding contract between Equitable and Shearman & Sterling for the law firm's services in the loan transaction. However, contrary to CalPERS' assertion, the court held that Equitable did

[16] 95 N.Y.2d 427 (2000).

[17] *Id.* at 434–435 (citations omitted) (emphasis added).

not retain Shearman & Sterling for CalPERS' benefit. Although the sole purpose of the business relationship between CalPERS and Equitable was to allow CalPERS to invest in long-term commercial real estate loans obtained by Equitable, the court determined that CalPERS and Equitable did not *at all times* share the same interests. The court noted the Agreement declared the agents of Equitable acted independently, and were not the agents of CalPERS. The Agreement also required CalPERS' counsel (and not Shearman & Sterling) to approve all closing documents on CalPERS' behalf. Relying on the language of the Agreement and the scope of Shearman & Sterling's representation, the court held that CalPERS was not an intended third-party beneficiary Shearman & Sterling's relationship with Equitable. CalPERS could not maintain its malpractice claim as a result.

## C. Gould v. Mellick & Sexton[18]

The courts' holdings in *McIntosh* and *Shearman & Sterling* also extend to a variation on a similar factual context, whether investors in a limited partnership's private placement offering are third-party beneficiaries with standing to sue counsel for the limited partnership. Like the Minnesota Supreme Court and the New York Court of Appeals, the Connecticut Supreme Court found that investors engaging in an arms'-length transaction were *not* intended third-party beneficiaries of the relationship between a limited partnership and its attorneys.

Plaintiffs, limited partners in Wildomar Square Associates LP ("Wildomar"), sued the attorneys representing Wildomar in the private placement offering for malpractice. The defendant served as legal counsel to Wildomar and, in that capacity, drafted a private placement memorandum. Pursuant to the private placement memorandum, all cash payments and promissory notes were to be held in escrow until the partnership and the defendants authorized the escrow agent to release the funds. The private placement memorandum provided that the partnership would use the promissory notes as collateral to obtain a $4 million loan, an amount equal to the aggregate face value of the notes. Wildomar was unable to obtain a loan in that amount, and the partnership had insufficient funds to carry out its objectives. As a result, plaintiffs lost their entire investment.

The trial court concluded defendant owed no duty of care to plaintiffs, and granted summary judgment in their favor. Affirming the trial court, the Connecticut Supreme Court focused on the existence of defendant's duty of care to plaintiffs. The court stated that "[t]he existence of a duty is a question of law and only if such a duty is found to exist does the trier of fact then determine whether the defendant violated that duty in the particular situation at hand."[19] In *Gould*, whether a legal duty exists to required "(1) a determination of whether an ordinary person in the defendant's position, knowing what the defendant knew or should have known, would anticipate that harm of the general nature of that suffered was likely to result, and (2) a determination, on the basis of a public policy analysis, of whether the defendant's responsibility for its negligent conduct should extend to the particular consequences or particular plaintiff in the case."[20]

Analogizing to the third-party beneficiary theory of liability applied in the estate planning context, the court found

[18] 819 A.2d 216 (Conn. 2003).

[19] *Id.* at 223 (internal quotation omitted).

[20] *Id.*

that "[d]etermining when attorneys should be held liable to parties with whom they are not in privity is a question of public policy," and asked "whether the *primary or direct purpose* of the transaction *was to benefit the third party*."[21] Among the considerations important to the court was whether "the imposition of potential malpractice liability on the defendants would undermine their duty of entire devotion to the interest of the client."[22]

The court found the partnership retained the defendant to further its own interests, and not those of the plaintiffs and other investors, with whom it engaged in an arms'-length transaction. The court found that defendant did not owe a duty of care to the plaintiffs, in part because doing so would interfere with the defendant's duty of undivided loyalty to its client.

## D. DeMartino v. Marion County[23]

In *DeMartino*, the Oregon Court of Appeals was asked to apply the third-party beneficiary doctrine to grant standing to a citizen taxpayer to bring a malpractice claim against bond counsel to Marion County. The plaintiff – a Marion County taxpayer – filed a complaint against the county and the law firm of Ater Wynne LLP, who acted as bond counsel for the County in the issuance of a $5 million revenue bond to help finance the Oregon Garden. The principal and interest were to be paid by the Oregon Garden. In the event of default, the County guaranteed payment of both principal and interest. The County planned to cover any default through the diversion of lottery funds the County received from the state lottery commission. The Oregon Garden defaulted, leaving the County responsible for payment on the bonds.

Plaintiff's complaint alleged that the manner in which the bonds were issued and guaranteed violated the Oregon Constitution and other state law. The plaintiff included Ater Wynne in the suit and alleged the attorneys were liable to plaintiff for malpractice. The trial court dismissed the claims against Ater Wynne for failure to state a claim. In affirming the trial court's dismissal, the Oregon Court of Appeals recognized that one is not liable for negligently causing another's purely economic losses in the absence of some source of duty beyond the common-law duty to exercise reasonable care to prevent foreseeable harm, such as a special relationship or status. The relationship of an attorney and client is one such special relationship, but it runs only to the client or to an intended third-party beneficiary of the attorney's agreement with the client.

Plaintiff pointed to an Oregon statute that allowed a government body to appoint "bond counsel to advise and *assist the public body* in the issuance of bonds," as evidence that a special relationship existed between plaintiff and Ater Wynne.[24] The court did not accept this argument, finding the statute merely authorized a public body to retain bond counsel and did not extend the attorney-client relationship to the public at large. As

[21] *Id.* at 224 (internal quotation omitted) (emphasis added).

[22] *Id.* (internal quotation omitted).

[23] 184 P.3d 1176 (Or. Ct. App. 2008).

[24] *Id.* at 1181 (quoting OR. REV. STAT. § 288.523(1) (2005)) (emphasis added).

a result, plaintiff lacked standing to sue Ater Wynne for malpractice.

### E. Credit Union Central Falls v. Groff[25]

Following the Minnesota Supreme Court's decision in *McIntosh*, the Rhode Island Supreme Court addressed the issue of attorney malpractice liability to a third-party beneficiary in a different factual context. Perhaps because of the egregious behavior of the attorney present in this case, the court in *Groff* arrived at a different conclusion than the court in *McIntosh*.

*Groff* addresses the unique relationship of a real estate closing attorney to both the bank and the borrower. Groff, an attorney, handled real estate closings for Credit Union Central Falls ("CUCF"). CUCF was not Groff's client, but would refer Groff to the bank's borrowers to act as a closing attorney. When acting as a closing attorney, Groff was responsible for, among other things, handling and disbursing the loan proceeds pursuant to the terms of the loan documents.

In at least two instances, Groff failed to use the loan proceeds to discharge the prior mortgages and instead absconded with the funds and began making monthly payments on the prior mortgages to conceal their continuing existence. When CUCF discovered Groff's wrongdoing, CUCF sued Groff, alleging malpractice and claiming standing as a third-party beneficiary.

The trial court granted summary judgment in favor of CUCF. In affirming the ruling of the trial court, the Rhode Island Supreme Court noted that, although "Groff's actions strongly suggest *fraudulent* misrepresentation, CUCF did not allege fraud or deceit in its complaint."[26] As a result, the court noted that it would be required to "adopt a theory of attorney liability to nonclients novel to this jurisdiction" in order to find Groff liable to CUCF.[27] It did.

In extending attorney liability to a non-client, the court recognized the third-party beneficiary theory "as an exception to the rule of strict privity that generally adheres in attorney malpractice cases."[28] The *Groff* court explained, "the courts adopting this theory require that for a non-client to establish a duty owed by the attorney to the non-client, the latter must allege and prove that the *actual intent of the client to benefit the non-client was a direct purpose of the transaction or relationship*."[29] "Thus, the test for third party recovery is *whether the intent to benefit actually existed*, not whether there could have been an intent to benefit the third party."[30]

Consistent with *McIntosh*, the *Groff* court agreed "that the attorney must be aware of the client's intent to benefit the third party in order for the exception [to the traditional privity requirement] to be applicable."[31] It viewed "a lack of direct

[25] 966 A.2d 1262 (R.I. 2009).

[26] *Id.* at 1271 ("Fraud is a well-settled exception to the privity requirement that historically bars nonclient recovery for attorney malpractice.") (citation omitted).

[27] *Id.*

[28] *Id.* (citing *Flaherty*, 492 A.2d at 625).

[29] *Id.*(quoting *Flaherty*, 492 A.2d at 625) (emphasis added).

[30] *Id.* (emphasis added) (internal quotation omitted).

[31] *Id.* at 1273 (quoting *McIntosh*, 745 N.W.2d 538) (brackets in original).

communication between the purported third-party beneficiary and the attorney as tending to disprove the existence of such a relationship."[32] As a result, "the liability of an attorney may extend to third-party beneficiaries of the attorney-client relationship *if it is clear that the contracting parties intended to benefit the third party*."[33]

The court concluded Groff's legal services were intended to benefit CUCF. The transactions were "for the direct purpose of providing CUCF with a first secured mortgage, thereby inducing CUCF to disburse the refinancing loan funds to his clients."[34] The court also found Groff "had direct and extensive communication with CUCF, and he received explicit instructions from CUCF."[35] Given these facts, the court held that CUCF, "if not a client [of Groff's], was at the very least an intended beneficiary of the contractual obligations between Mr. Groff and his borrowers, and as such, the attorney owed CUCF a duty of care."[36] Given these facts, the court held CUCF had standing as a third-party beneficiary to sue Groff for malpractice.

### F. Paradigm Insurance Company v. Langerman Law Offices[37]

One often-litigated variation on the intended third-party beneficiary theory involves "tripartite relationships" between insurers, their insureds, and defense attorneys retained by the insurer on behalf of the insured. One illustrative case addressing this issue is *Paradigm*. The Arizona Supreme Court considered whether an attorney assigned by an insurer to defend the insured, could later liable in malpractice to the insurer on a third-party beneficiary theory. Underlying the facts of this case, Dr. Benjamin Vandewerf and another doctor at Samaritan Health Service were sued by a patient for medical malpractice. The patient also sued Samaritan. Dr. Vandewerf was covered by an insurance policy issued by Paradigm.

Paradigm hired attorney Langerman to defend Dr. Vandewerf. During the course of his representation, Langerman did not investigate Samaritan's insurance policy to determine whether it covered Dr. Vandewerf or whether Paradigm could tender the defense to Samaritan's insurer. Following a disagreement between Langerman and Paradigm, Paradigm replaced Langerman with a new lawyer, who discovered Samaritan had insurance coverage through Samaritan Insurance Funding ("SIF"). The policy not only covered Dr. Vandewerf, but also operated as the primary coverage for the claim. New counsel advised Paradigm to tender Vandewerf's defense to SIF. When it did so, however, SIF rejected the tender as untimely. The claim later settled and Paradigm was unable seek contribution or indemnification from SIF.

Paradigm later sued Langerman for malpractice. The trial court granted summary judgment in favor of Langerman, holding that no attorney-client relationship existed between Paradigm and Langerman. In reversing the trial court, the

[32] *Id.*

[33] *Id.* at 1272 (emphasis added).

[34] *Id.* at 1274.

[35] *Id.*

[36] *Id.*

[37] 24 P.3d 593 (Ariz. 2001).

Arizona Supreme Court looked to the much-criticized Restatement formulation of the third-party beneficiary theory of attorney liability. The court also relied upon a line of professional negligence cases arising outside the attorney malpractice context and found "[w]hen the interests of insurer and insured coincide, as they often do, it makes neither economic nor practical sense for an insurer to hire another attorney to monitor the actions and decisions of the attorney assigned to an insured."[38] It went on:

> For instance, the insurer depends on the lawyer to represent the insured zealously so as to honor its contractual agreement to provide the defense when liability allegations are leveled at the insured. In addition, the insurer depends on the lawyer to thwart claims of liability and, in the event liability is found, to minimize the damages it must pay.[39]

In this context, the court determined that "the lawyer's duties to the insured are often discharged for the full or partial benefit of the nonclient."[40]

The court concluded, "based on a long line of precedent, when an insurer assigns an attorney to represent an insured, the lawyer has a duty to the insurer arising from the understanding the lawyer's services are ordinarily intended to benefit both insurer and insured when their interests coincide. This duty exists even if the insurer is a nonclient."[41]

## II. Negligent Misrepresentation / Opinion Letters

Where courts have—for the most part—placed strict standing requirements on non-clients asserting general professional negligence claims against attorneys, courts have been more relaxed in permitting non-clients to assert negligent misrepresentation claims against attorneys. Although couching their analysis in the same "intended beneficiary" doctrine applied in malpractice cases, a subtle shift in its application renders a different outcome in these cases. In the attorney malpractice context, courts require a non-client to be a "direct and intended beneficiary" of the

[38] *Id.* at 601.

[39] *Id.*

[40] *Id.*

[41] *Id.* at 602. As an aside and in so holding, *Paradigm* joined the majority of jurisdictions holding that the attorney representing an insured could be liable to the insurer under one theory or another. "While the courts of other jurisdictions generally recognize [a cause of action by an insurer against the law firm it retains to defend an insured], they differ markedly on the theory of liability under which such a claim may be brought. In most jurisdictions, the retaining insurer may sue the law firm directly as its client." Gen. Sec. Ins. Co. v. Jordan, Coyne & Savits, LLP, 357 F. Supp.2d 951 (E.D. Va. 2005) (collecting cases); *see also* Hartford Ins. Co. of Midwest v. Koeppel, 629 F. Supp.2d 1293 (M.D. Fla. 2009) (collecting cases). Other courts, however, have explicitly rejected such an approach. *See, e.g.*, Pine Island Farmers v. Erstad & Riemer, 649 N.W.2d 444 (Minn. 2002). Courts engaging in an analysis of the tripartite relationship between the insured, insurer, and insurance defense counsel, have concluded – at least hypothetically – that in the absence of a conflict of interest, there are circumstances in which both insured and insurer can become clients of the attorney. *See, e.g.*, *Pine Island Farmers*, 649 N.W.2d 444 (Minn. 2002); Shaya B. Pacific, LLC v. Wilson, Elser, Moskowitz, Edelman & Dicker, LLP, 827 N.Y.S.2d 231 (N.Y. App. Div. 2006).

attorney-client *relationship*; however, in the negligent misrepresentation context, courts typically require that non-clients are "intended beneficiaries" only of the attorney's *representation*. In general, a non-client may maintain a negligent misrepresentation claim against an attorney where the attorney made a representation – whether in an opinion letter or otherwise – with the intent that the non-client rely on the representation. In the case of opinion letters drafted by counsel at the direction of the client, which are to be delivered to a third-party as part of a transaction, courts have found that the *de facto* purpose of such an opinion letter is to induce reliance by the third party.[42] Courts have generally not extended standing to non-clients alleging negligent omission.[43]

[42] Typically, courts have allowed non-clients to bring claims against attorneys for negligent misrepresentation where the client solicited an opinion letter from the attorney for the express purpose of inducing reliance by a third party, and the attorney was aware that the third party would rely and intended to induce such reliance. *See, e.g.*, Mehaffy, Rider, Windholz & Wilson v. Cent. Bank Denver, N.A., 892 P.2d 230, 236 (Colo. 1995) (law firm which prepared an opinion letter on behalf of client for express purpose of inducing non-client to purchase municipal bonds may be liable for negligent misrepresentation); Kirkland Constr. Co. v. James, 658 N.E.2d 699, 701–702 (Mass Ct. App. 1995) (buyer may state claim for negligent misrepresentation against law firm that wrote letter with intent to induce buyer to enter into contract with client); Roberts v. Ball, Hunt, Hart, Brown & Baerwitz, 128 Cal. Rptr. 901, 905–906 (Cal. Ct. App. 1976) (law firm may be liable to third-party lender for negligent misrepresentation where firm knew that misrepresentations would be used to obtain loan).

[43] *See, e.g.*, Banco Popular N. Am. v. Gandi, 876 A.2d 253, 266 (N.J. 2005) (an attorney has no duty that would support a claim for negligent omission by a non-client where the attorney made no representations, and there was no reliance by a remote third-party with whom the attorney had no relationship).

## A. Prudential Insurance Company of America v. Dewey, Ballentine, Bushby, Palmer & Wood[44]

One of the leading cases addressing attorney liability to non-clients for negligent misrepresentation is the New York Court of Appeals' decision in *Prudential v. Dewey Ballentine*. In this case, a lender sued a borrower's attorney ("Dewey Ballentine") for negligently preparing an opinion letter provided to the lender as a condition for restructuring the debt. The trial court granted summary judgment in favor of Dewey Ballentine, believing Prudential lacked standing as an intended beneficiary.

Prudential and U.S. Lines, Dewey Ballentine's client, a major shipping concern, engaged in negotiations to restructure Prudential's loan to U.S. Lines, after U.S. Lines informed its creditors that it was anticipating difficulty in meeting its debt obligations. Following negotiations, the parties agreed to a restructuring of the debt. One of the conditions of the restructuring was that Dewey Ballentine draft an opinion letter to Prudential on behalf of U.S. Lines, containing an assurance that the mortgage documents that were to be recorded in connection with the debt restructuring, and which, incidentally, had been prepared by other counsel, represented legal, valid, and binding obligations of U.S. Lines. Prudential later learned that one of the recorded documents erroneously stated the outstanding balance of the first preferred fleet mortgage securing the debt as $92,885, rather than the correct sum of $92,885,000. As a result, Prudential suffered significant losses when U.S. Lines subsequently filed for bankruptcy.

[44] 80 N.Y.2d 377 (N.Y. 1992).

Prudential sued the lawyers asserting Dewey Ballentine could be held liable to it on a third-party beneficiary theory. In reversing the trial court, the New York Court of Appeals found that the law imposed a duty where "the representations at issue had been made for the very purpose of inducing action" of the party receiving the representation.[45] In other words, the law imposes a duty where reliance on a representation "was not an indirect or collateral consequence" of the representation, but was instead "the end and aim of the transaction."[46]

The court found that Dewey Ballentine knew Prudential would rely on the opinion letter in deciding whether to permit the debt restructuring. "Thus, the end and aim of the opinion letter was to provide Prudential with the financial information it required."[47] The court also found that Prudential had relied upon the opinion letter and that Dewey Ballentine had expected Prudential to so rely. The court focused on language in the opinion letter, which represented the mortgage documents would be fully enforceable against U.S. Lines in accordance with their terms.

The end and aim of the opinion letter was to secure Prudential's reliance. Prudential relied on the representations. Dewey Ballentine intended for Prudential to rely on the representations. As a result, the court found "the bond between [the parties] was sufficiently close to establish a duty of care running from the former to the latter."[48]

## B. McCamish, Martin, Brown & Loeffler v. F.E. Appling Interests[49]

In *McCamish*, the Texas Supreme Court was asked to determine whether defendant McCamish, Martin, Brown & Loeffler ("McCamish"), a law firm, could be liable to F.E. Appling Interests, a general partnership, and Boca Chica Development Company, a joint venture partnership managed by Appling (collectively "Appling"), for negligent misrepresentation arising during the course of settlement negotiations. Appling obtained a loan and line of credit from Victoria Savings Association ("VSA") to finance a real estate project. Appling accepted the loan based on VSA's oral representation that VSA would later expand the line of credit. When Appling later requested an extension of credit, VSA declined. Appling subsequently filed for bankruptcy and brought a lender liability claim against VSA for $15 million in damages. During the course of litigation, Appling became concerned that the Federal Savings & Loan Corporation ("FSLC") would declare VSA insolvent and take it over before it could obtain a judgment. If that occurred, Appling's claim would be unenforceable. Anxious to settle under the circumstances, Appling struck a deal with VSA, but required VSA's attorneys – McCamish – to affirm the agreement was enforceable against the FSLC. However, prior to the execution of the settlement documents, the FLSC placed VSA under "voluntary supervision," which gave the FLSC – and not the VSA board – authority to settle lawsuits against VSA. The parties and their attorneys subsequently executed the settlement

[45] *Id.* at 383.

[46] *Id.* (quoting Glanzer v. Shepard, 233 N.Y. 236, 238–239 (1922)).

[47] *Id.* at 385.

[48] *Id.*

[49] 991 S.W.2d 787 (Tex. 1999).

documents. McCamish was not aware the VSA board lacked the authority to approve the settlement agreement when he signed the settlement agreement on behalf of VSA. The FLSC never ratified the settlement.

Appling thereafter sued McCamish, alleging the lawyers negligently misrepresented that the VSA board had approved the settlement. The trial court granted summary judgment in favor of McCamish on the grounds that, absent privity, McCamish owed no duty to Appling. The Texas Supreme Court reversed. Central to its analysis was "[w]hether the absence of an attorney-client relationship precludes a third-party from suing an attorney for negligent misrepresentation."[50] It concluded, "there is no reason to exempt lawyers from [non-client claims for negligent misrepresentation] or to impose a privity requirement."[51]

In doing so, the court remained concerned that allowing such non-client suits against attorneys threatened lawyers with "almost unlimited liability." As such, the court limited an attorney's liability for negligent misrepresentation only to those situations where the non-client was *invited* by the attorney to rely, and *did* justifiably rely, on the attorney's representations. The court noted other jurisdictions have refused to find justified reliance when the representation takes place in an adversarial context. However, "[b]ecause not every situation is clearly defined as 'adversarial' or 'nonadversarial,' the characterization of the interparty relationship should be guided, at least in part, by the extent to which the interests of the client and the third party are consistent with each other."[52] The court held that "a nonclient cannot rely on an attorney's statement, such as an opinion letter, unless the attorney invites that reliance."

## C. Petrillo v. Bachenberg[53]

In *Petrillo*, the New Jersey Supreme Court addressed whether defendant Bruce Herrigel, an attorney representing a seller of real property, could be held liable to a prospective purchaser for negligent misrepresentation. Rohrer Construction, Herrigel's client, owned a tract of real property that it wanted to sell. In preparing to sell the property, Roher hired an engineering firm, which conducted thirty separate percolation tests to determine the suitability of the soil for a septic system and prepared a report. The municipality required two successful percolation tests before it would approve installation of a septic system.

Rohrer listed the property with a real estate broker, to whom Herrigel sent a two-page document consisting of two one-page excerpts from the engineer's report. Read together, the two pages appeared to describe a series of only seven tests, of which two were successful. In reality the property passed only two of thirty tests. The document became part of the broker's sales packet.

Lisa Petrillo entered into an agreement to purchase the property from Roher, which permitted her 45 days to conduct her own soil tests, and allowed her to rescind the contract if they were unsatisfactory. Petrillo's engineers found the site inadequate for a septic system, as each of the soil tests failed. She rescinded the contract and sued Herrigel, among others, claiming that had she known the property

[50] *Id.* at 791.

[51] *Id.* at 795.

[52] *Id.* at 794 (internal quotation omitted).

[53] 655 A.2d 1354 (N.J. 1995).

passed only two of *thirty* tests, she would not have signed the contract.

The trial court concluded that Herrigel did not owe Petrillo a duty of care. The New Jersey Supreme Court reversed, holding an attorney has a duty not to provide misleading information to potential buyers who the attorney knows, or should know, will rely on the information. The court found that other jurisdictions had "relaxed traditional privity requirements when an attorney induce[d] specific non-clients to rely on the attorney's representations."[54] "When courts relax the privity requirement, they typically limit a lawyer's duty to situations in which the lawyer intended or should have foreseen that the third-party would rely on the lawyer's work."[55] The court identified several situations in which attorneys owed a duty to non-clients:

(1) where an attorney drafted an opinion letter in connection with a client's securities offering on which the attorney has knowledge the non-client will rely;[56]
(2) where an attorney prepared a private offering statement in connection with a debt offering with the intent that third parties would rely;[57] and
(3) where an attorney performed real estate title work and reasonably foresaw that third parties would, for a proper business purpose, detrimentally rely on the attorney's work.[58]

Under the facts of the case, the court held "Herrigel had a duty not to misrepresent negligently the contents of a material document on which he know others would

[54] *Id.* at 1358 (citing Greycas, Inc. v. Proud, 826 F.2d 1560 (7th Cir. 1987) (holding that a borrower's attorney owed a duty to the lender not to negligently misrepresent the status of the borrower's collateral in an opinion letter, notwithstanding the lack of privity)); Horizon Fin., F.A. v. Hansen, 791 F. Supp. 1561 (N.D. Ga. 1992) (holding under Pennsylvania law that attorney for borrower has duty to lender bank to whom attorney issued opinion letters expressly for bank's benefit); *Mehaffy, Rider, Windholz & Wilson*, 892 P.2d at 237 ("by issuing opinion letters for purpose of inducing [reliance], the attorneys may be liable ... for negligent misrepresentation."); McEvoy v. Helikson, 562 P.2d 540 (Or. 1977) (holding that attorney for ex-wife owed duty to former husband when attorney undertook to enforce order obligating him to hold ex-wife's passport unless she relinquished custody of children); Trask v. Butler, 872 P.2d 1080, 1084 (Wash. 1994) (stating that "[t]he intent to benefit the plaintiff is the first and threshold inquiry" in determining existence of duty to non-clients).

[55] *Id.* at 1359.

[56] *Id.* (citing Norman v. Brown, Todd & Heyburn, 693 F. Supp. 1259, 1265 (D. Mass 1988) ("As a general matter, tax opinion letters are drafted so that someone can rely upon them.")); *In re* Rexplore, Inc. Sec. Litig., 685 F. Supp. 1132, 1146 (N.D. Cal. 1988) (holding that an attorney owes a duty to a non-client where an attorney foresees, or should foresee, that a non-client will rely upon an opinion letter issued by the attorney in connection with a client's securities offering); Alpert v. Shea Gould Climenko & Casey, 559 N.Y.S.2d 312, 315–316 (N.Y. Sup. Ct. 1990) (no duty owed by attorney to non-client investors in the absence of evidence that attorneys knew and understood that non-client investors would rely on tax-opinion letters issued in connection with tax-shelter offering).

[57] *Id.* (citing Molecular Tech. Corp. v. Valentine, 925 F.2d 910, 915–917 (6th Cir. 1991) (under Michigan law, an attorney preparing a private offering statement in connection with his client's corporate debenture offering owed a duty of care to potential investors whom the attorney knew, or should have known, would rely on the statement)).

[58] *Id.* (citing Century 21 Deep South Props., Ltd. v. Corson, 612 So.2d 359 (Miss. 1992)).

rely to their financial detriment."[59] Although refusing to characterize the document Herrigel prepared as an "opinion letter," the court concluded he did provide a document to the broker that he knew or should have known would be relied upon by prospective purchasers in deciding whether to sign a purchase contract and move forward with the purchase of the property. The court noted that Herrigel could have limited his liability by sending complete copies of the reports to the broker, or by sending a letter to the broker simply stating that the property had passed two percolation tests as required by the township, or by qualifying the composite report with a cover letter. He did none of these. The court concluded he should have foreseen Petrillo would rely on the composite report.

## D. Banco Popular North America v. Gandi[60]

Several years later, *Banco* invited the New Jersey Supreme Court to address the contours of its previous decision in *Petrillo*. Banco also addressed the circumstances under which an attorney may be liable to a non-client for conspiracy and aiding and abetting the client's fraud. In this case, Banco Popular North America (the "Bank") brought a cause of action against an attorney who assisted a client in transferring assets to defraud a creditor, for fraud, conspiracy to commit fraud and for negligent misrepresentation.

Gandi, the operator of several fast food restaurants, obtained a loan for $550,000.00 from the Bank. At some point thereafter, Gandi transferred all of his assets into his wife's name to place them beyond the reach of another creditor on the advice of his counsel, Richard Freedman. Following the asset transfer, Gandi obtained additional loans from the Bank. Gandi executed guarantees in connection with those loans, stating he had not engaged in any action that would place the Bank's collateral at risk. In addition, Freedman prepared an opinion letter in connection with the second loan, in which he stated that "[a]fter due investigation, we are unaware of any material matters contrary to the representations and warranties" Gandi made to the Bank.[61] The opinion was "rendered solely to, and for the benefit of [the Bank], its successors and assigns, and its counsel, and may not be relied upon by any other party."[62] Gandi later defaulted on the loans and the bank obtained a judgment against Gandi.

With regard to the Bank's conspiracy claim, the New Jersey Supreme Court held that a creditor may bring a conspiracy claim against one who assists another in executing a fraudulent transfer. "Such an action would require the creditor prove that the conspirator agreed to perform the fraudulent transfer, which absent the conspiracy, would give a right of action" for creditor fraud as defined under the Uniform Fraudulent Transfer Act.[63] "A creditor asserting a claim against a conspirator must satisfy the agreement and knowledge aspects of civil conspiracy and all of the underlying components of a UFTA claim: An unwitting party may not be liable under a conspiracy theory."[64] Under the facts of the case, the court held the Bank stated a conspiracy claim against Freedman for encouraging Gandi to violate

[59] *Id.* at 1362.

[60] 876 A.2d 253 (N.J. 2005).

[61] *Id.* at 258.

[62] *Id.* at 267.

[63] *Id.* at 263 (internal quotation omitted).

[64] *Id.*

the UFTA and transfer assets to avoid a creditor. Simply because Freedman represented Gandi did not insulate him from liability.

The Bank also brought two claims against Freedman for negligent misrepresentation, first with respect to his involvement in the asset transfer and, second, with respect to the opinion letter. In addressing the Bank's claims, the court revisited its previous decision in *Petrillo*, which found the attorney must have "intended or should have foreseen that the [non-client] would rely on the lawyers work," before the attorney would owe a non-client a duty of care.[65] "Put differently, the invitation to rely and reliance are the linchpins of attorney liability to third parties."[66]

Addressing Freedman's participation in the asset transfer, the court emphasized that the attorney must do *something* to induce a third party's reliance. The court found that "[i]n aiding Gandhi in the asset transfer, not only did Freedman make no representations to the Bank seeking to induce reliance, but the entire transaction was intended to be, and in fact was, carried out without the Bank's knowledge."[67] The court refused to extend liability to third-parties for negligent omissions, stating that no duty exists in circumstances "involving no representations, no reliance, and a remote third party with whom the attorney had no relationship."[68]

As to the opinion letter, the court stated "[i]t goes without saying that representations in negotiations are made to induce reliance."[69] Further, "[t]he purpose of a legal opinion letter is to induce reliance by others."[70] "To the extent the loan negotiations or opinion letter contained misstatements of material facts on which Freedman knew or should have known the Bank would rely, they will support a negligence cause of action under *Petrillo*."[71]

The court found that Freedman rendered an opinion letter falsely stating he was "unaware of any material matters contrary to the representations and warranties" made by Gandi. The court found Freedman intended that the Bank rely on his misrepresentation. Even further, "given Freedman's knowledge of the worthlessness of the guaranty, he had a duty, in light of what he had done and what he knew, either to counsel Gandi to tell the Bank the truth and see to it that he had done so or discontinue his representation."[72] Under these circumstances, "Freedman could *not* assist Gandi in fraudulently securing further loans and, on the facts alleged, overstepped his bounds in penning an opinion letter on Gandi's behalf."[73]

## III. Attorney Liability for Aiding and Abetting Client Breach of Fiduciary Duty, Conspiracy and Common-Law Fraud

In addition to attorney liability to third-parties under theories of negligence, as addressed in *Banco*, courts have imposed liability on attorneys for their intentional

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[65] *Id.* at 265.

[66] *Id.*

[67] *Id.* at 266.

[68] *Id.*

[69] *Id.*

[70] *Id.*

[71] *Id.*

[72] *Id.* at 268 (citation omitted) (when a client misrepresents or omits material facts to induce third-party reliance, attorney must counsel client to disclose truth and cease representation if client refuses.)

[73] *Id.* (emphasis in original).

torts and also for their acts in furtherance of the intentional torts of their clients. Although courts routinely state the maxim that "in the *absence* of fraud or another improper motive, an attorney is liable for professional negligence only to a person with whom he has an attorney-client relationship," courts have rarely addressed the inverse situation.[74] While the privity requirement may still be the majority rule and apply in the majority of circumstances, decisions addressing an attorney's liability to a third party for intentional misconduct are far and few between.

## A. Reynolds v. Schrock[75]

In *Reynolds*, the Oregon Supreme Court was presented with the question: "whether, and under what circumstances, a third party may assert a claim against a lawyer, acting in a professional capacity, for assisting a *client* in breaching the client's fiduciary duty."[76] The *Reynolds* decision can be seen as a companion case to *Granewich v. Harding*,[77] a previous decision of the Oregon Supreme Court, wherein it held that an attorney acting *outside* the scope of its representation of a corporation it represented, could be held liable for aiding and abetting a majority shareholder's fiduciary duties to a minority shareholder of the corporation.[78] In *Reynolds*, the court amplified its decision in *Harding*, concluding that although the Plaintiff has the burden to show that a lawyer acted outside the scope of the attorney client relationship, the lawyer is not protected once he is outside the permissible scope of representation:

> [The rule] does not protect lawyer conduct that is unrelated to the representation of a client, even if the conduct involves a person who is a client. Because such unrelated conduct is, by definition, outside the scope of the lawyer-client relationship, no important public interest would be served by extending the qualified privilege to cover it. For the same reason, the rule does not protect lawyers who are representing clients but who act only in their own self-interest and contrary to their clients' interest. Similarly, this court would consider actions by a lawyer that fall within the "crime or fraud" exception to the lawyer-client privilege ... to be outside the lawyer-client

[74] *McIntosh*, 745 N.W.2d at 545 (emphasis added). *See also, e.g.*, Berry v. Dodson, Nunley, & Taylor, P.C., 717 S.W.2d 716 (Tex. Ct. App. 1986) ("It has long been the majority view in this country that an attorney will not have to answer for negligence to a party not in privity of contract with him in the absence of fraud or collusion.") (citing Nat'l Sav. Bank v. Ward, 100 U.S. 195, 205–206 (1879)).

[75] 142 P.3d 1062 (Or. 2006).

[76] *Id.* at 1065 (emphasis in original).

[77] 985 P.2d 788 (Or. 1999).

[78] Because the attorney in *Granewich* acted outside the scope of his representation of the corporation, the Oregon Supreme Court did not address whether aiding and abetting liability could be imposed on attorneys acting within the scope of their representation. *See Granewich*, 985 P.2d at 795. In *Granewich*, the plaintiff's complaint "allege[d] that the corporation hired the lawyers, that the corporation had no interest in the dispute between [the shareholders], and that the work that the lawyers performed was outside the scope of any legitimate employment on behalf of the corporation." *Id.* The court found that outside the attorney-client relationship, "the lawyers stand in no different position in relation to plaintiff than anyone else, *and their status as lawyers is irrelevant*." *Id.* (emphasis added).

relationship when evaluating whether a lawyer's conduct is protected.[79]

## B. Greenberg Traurig of New York v. Moody[80]

In *Greenberg Traurig v. Moody*, a law firm performed legal services for a corporation whose CEO repeatedly violated a permanent injunction against the sale of unregistered securities. The plaintiffs in the suit were several accredited investors who purchased IFT stock without knowledge of the injunction. The plaintiffs alleged that Greenberg Traurig knew of the CEO's wrongful conduct and yet continued to represent IFT in connection with an initial public offering contemplated by the company. The Texas Court of Appeals, reversing a jury verdict against the law firm, held the law firm owed no duty to disclose the fraud to the investors. However, it did hold the law firm could be liable for conspiracy to defraud the investors for its role in assisting the corporation in its efforts to obtain additional financing, when it knew or should have known that the many securities violations committed by the CEO and corporation were undisclosed.

In analyzing the investors' claim that Greenberg Traurig failed to disclose the fact that IFT had issued its securities in violation of the SEC injunction, the court found a plaintiff must establish that a defendant had a duty to disclose in order to state a claim of fraudulent omission. The court found a duty to disclose will arise: "(1) when one party makes a partial or incomplete statement that requires clarification; (2) when the parties are in a fiduciary or confidential relationship; and (3) when one party possesses superior knowledge, not readily available to the other, and knows that the other is acting on the basis of mistaken knowledge."[81]

Applying this law, the court found no attorney-client or other fiduciary relationship giving rise to a duty to disclose. The court also concluded that the rules of professional conduct did not impose such a duty. It found that the applicable rule of professional conduct provided only that a lawyer was *permitted* but not affirmatively *required* to reveal the intention of his client to commit a crime.[82] Thus, Greenberg Traurig was under no duty to make any such disclosures to the investors in the absence of an attorney-client relationship between them.

The court then turned to analyze the plaintiff's claim that Greenberg Traurig conspired to commit fraud.[83] The court held that before the investors could "recover on their claim for conspiracy to defraud, [they] were required to show that Greenberg Traurig specifically intended to

[79] *Reynolds*, 142 P.3d at 1069 (internal citations omitted).

[80] 161 S.W.3d 56 (Tex. Ct. App. 2004).

[81] *Id.* at 77.

[82] *Id.* at 79 (citing New York Disciplinary Rule 4-101(c)(3)). *See also* Model Rule of Professional Conduct 1.6(b)(2) ("A lawyer *may* reveal information relating to the representation of a client … to prevent the client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's services.).

[83] The elements of a civil conspiracy are (1) an agreement between two or more persons; (2) an overt act in furtherance of the agreement, (3) the parties' intentional participation in the furtherance of a plan or purpose, and (4) resulting damage or injury. *Id.* at 80 (citations omitted); *see also id.* at n. 22.

agree to accomplish an unlawful purpose or lawful purpose by unlawful means."[84] However, "because of an attorney's duty to preserve client confidences, there must be some indication that the attorney agreed to the fraud."[85] As such, "an attorney may be held liable for conspiracy to defraud if he knowingly agrees to defraud a third party."[86] Under the facts of the case, the court determined that there was sufficient evidence from which a jury could infer that Greenberg Traurig agreed to conspire to commit common law fraud.

## IV. Closing Thoughts

The traditional 'privity' requirement governing standing to sue a lawyer is eroding, even outside the estate-planning context. In its place, courts are developing a sliding-scale standard, depending upon the perceived severity of the lawyer's misconduct, for determining whether a non-client has standing to sue a lawyer. These evolving standards raise serious questions about the sanctity of the attorney-client relationship, which have yet to be resolved by the courts. Courts have recognized that the imposition of a duty on lawyers toward *non*-clients may threaten the integrity of a lawyer's advice to his or her client under certain circumstances. As these cases demonstrate, the courts continue to tinker with the balance to be struck between lawyers' professional obligations to their clients and affording justice to aggrieved non-clients. Although trends are emerging, the precise duties and the third-parties to whom those duties are owed are not yet well defined. Until they are, lawyers should proceed with an awareness that – in a growing number of contexts – a lawyer's work product, representations, and conduct in representing a client may provide a basis for third-party liability.

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[84] *Id.* at 89.

[85] *Id.*

[86] *Id.*