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Divided Loyalties: A Cautionary Tale, at Irell's Expense

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We're a little late to this story, but it's too provocative to let pass. Last week Santa Ana, Calif., federal district court judge Cormac Carney issued an extraordinary 19-page ruling in the criminal stock options backdating case against former Broadcom CFO William Ruehle. Prosecutors wanted to use as evidence statements that Ruehle made to lawyers from Irell & Manella when Irell was conducting an internal investigation of Broadcom's options granting practices. Judge Carney ruled they could not, finding that Ruehle's statements were protected by attorney-client privilege even though Irell had been representing Broadcom, not Ruehle, in the internal investigation--and even though Irell had already disclosed Ruehle's statements to Broadcom's board, its auditors, and the government.

The problem, Carney found, was that in addition to its assignment for Broadcom, Irell was representing Ruehle personally in two shareholder lawsuits. "Mr. Ruehle never gave Irell permission to jettison his rights for those of Broadcom and disclose the confidential information that he shared with Irell to the government and other third parties," the judge wrote. "For Irell to have done so without Mr. Ruehle's consent was wrong and a clear breach of its duty of loyalty to him." Carney was so disturbed by the facts that emerged during the two-day evidentiary hearing that he referred Irell to the state bar for disciplinary action.

Irell defended its action in a statement. "Respectfully, we believe that the court's ruling is in error," the firm said. "The disclosures the firm made to the audit committee and the company's auditors at Ernst & Young were entirely proper. CFO Ruehle testified at the hearing before Judge Carney that the Irell lawyers were 'directed to give all factual information to Ernst & Young.' CFO Ruehle further testified that he understood that the company and its counsel 'were not withholding information from the auditors.'" One of the lawyers who interviewed Ruehle in the internal investigation, Daniel Lefler, also testified at the evidentiary hearing that he and Irell partner Kenneth Heitz informed Ruehle that his

statements could be shared with third parties, including the U.S. attorney's office.

Ruehle's statements to Lefler and Heitz were also deemed privileged by a special master in a Broadcom shareholder derivative suit. After the special master's ruling, Ruehle's prosecutors asked Judge Carney to rule on their admissibility in the criminal case. Ruehle's criminal defense team, headed by Richard Marmaro of Skadden, Arps, Slate Meagher & Flom, did not move to suppress the statements.

The line between a lawyer's duty to a corporate client and to its officers is frighteningly blurry. That's the issue not only in Judge Carney's ruling, but also in the recent malpractice and breach-of-duty suit filed by Stanford Financial CIO Laura Prendergast-Holt, who accuses Proskauer Rose of similarly divided loyalties. For anyone who handles cases like these, it's worth reading Judge Carney's account of Irell's long relationship with both Broadcom and Ruehle, which gave rise to the conflicts the judge identified.

The government has appealed the judge's suppression of Ruehle's statements.