

Client Alert

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N.J. Appellate Division Declines to Extend Attorney-Client Privilege to Corporate Agents in Closely Held Corporations

The New Jersey Supreme Court has described the attorney-client privilege as a principle that “imposes a sacred trust on the attorney not to disclose the client’s confidential communication.”¹ While this foundational privilege extends to corporations and other organizations and associations, such entities nonetheless act through their agents.² Though employees and shareholders may communicate with a corporation’s attorneys in full confidence that the attorney-client privilege protects the communications, how far does the benefit of the privilege extend and who can waive this privilege? As explained by the Appellate Division in *Royzenshteyn v. Pathak*, the answer may lie in the client’s retainer agreement.

In *Pathak*, the Appellate Division declined to adopt a rule that shareholders in a closely held corporation are presumed to hold a personal attorney-client privilege, distinct from the corporate entity, that shields disclosure from future shareholders.³ Plaintiffs, the two sole individual shareholders of Onyx Enterprises Int’l Corp. (“Onyx”) since its founding in 2008, ultimately sold 52% of Onyx’s outstanding common stock to Defendants in 2015. Plaintiffs thus became minority shareholders in Onyx and executed

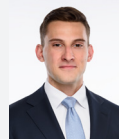


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1 A. v. B., 158 N.J. 51, 56 (1999) (citation omitted).
2 Hedden v. Kean University, 434 N.J. Super 1, 11 (App. Div. 2013) (citation omitted).
3 2024 N.J. Super. Unpub. LEXIS 6 (App. Div. Jan. 2, 2024).



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new employment contracts. Attorneys at McCarter & English, LLP (“McCarter”) advised Onyx in the transaction.

Three years later, Plaintiffs sued Defendants in connection with the transaction, alleging, inter alia, legal and equitable fraud in the inducement. During discovery, Plaintiffs asserted the attorney-client privilege over a significant number of documents. Defendants, however, claimed that some of those documents involved communications with McCarter and, therefore, Onyx, rather than Plaintiffs as individuals, held the right to assert or waive the privilege.

In 2019, after a motion to compel by Defendants, the trial court ordered Plaintiffs to produce all documents on its privilege log. In 2020, Plaintiffs appealed that order, and the Appellate Division reversed and remanded for the trial court to conduct an in-camera review to discern, in part, whether McCarter represented Onyx alone, or jointly, with Plaintiffs⁴. The 2020 Appellate Division decision rejected Plaintiffs’ claim that they, as individuals, were McCarter’s only client in the transaction with Defendants.

On remand, after multiple reports by a special master, the trial court concluded that Onyx was McCarter’s sole client as contemplated by a retainer agreement, which only identified Onyx as a client. Critically, the retainer agreement stated that if any individuals were to be represented, there would be a written agreement memorializing such representation. Though Plaintiffs had personal tax concerns at the time of the transaction, those concerns, as well as indemnity issues, were ancillary to the transaction, were “not stand[-]alone personal concerns of [plaintiffs],” and did not indicate personal representation of Plaintiffs. Accordingly, Onyx, now owned in majority by Defendants, was found to control the attorney-client privilege concerning communications with McCarter⁵.

The trial court adopted the special master’s findings and ordered all documents sought in the 2019 motion to compel be produced. Defendants appealed the order granting Plaintiffs’ motion to compel to the Appellate Division.

An Appellate Division panel affirmed and remanded, emphasizing that under the Rules of Professional Conduct (RPC), when a corporation retains an attorney, the client is “the [corporation] as distinct from its directors, officers, employees, members, shareholders, or other constituents,”⁶ and that “there is no exception for closely held corporations.” The panel also noted the RPC states that, “[i]n dealing with a [corporation]’s directors, officers, employees, members, shareholders or other constituents, a lawyer shall explain the identity of the client when the lawyer believes that such explanation is necessary to avoid misunderstanding on their part.”⁷ The panel explained that the trial court properly found that the record lacked any evidence of an express or implied attorney-client relationship

4 See *Royzenshteyn v. Pathak*, 2020 N.J. Super. Unpub. LEXIS 1562 at *21 (App. Div. Aug. 6, 2020).

5 The trial court did, however, adopt the special master’s conclusion that plaintiffs properly asserted privilege over their communications with a different law firm—this law firm represented plaintiffs in their individual capacities.

6 RPC 1.13(a).

7 RPC 1.13(d).

between Plaintiffs and McCarter. Onyx was deemed to have waived its attorney-client privilege regarding communications with McCarter, and the panel remanded for the trial court to enter an order more specifically identifying the McCarter communications at issue and directing such documents to be produced to Defendants.

For attorneys representing closely held corporations, *Pathak* should serve as a reminder that retainer agreements can significantly impact the availability of the attorney-client privilege. Retainer agreements should be express and unambiguous as to whether the attorney's representation extends solely to the corporate entity, or includes corporate employees, shareholders, or other constituents. While it may be entirely appropriate to name only a corporate entity as the client in a retainer agreement, attorneys should discuss potential ramifications at the outset and clarify that it is the **client** who holds the attorney-client privilege—and in the case of a corporate entity, the client is only the corporate entity—not ancillary parties. Such discussions will help ensure that the attorney-client privilege is not inadvertently waived due to unwitting communications with corporate constituents. As more facts come to light, attorneys are reminded to review their retainer agreements and make amendments, as necessary, to accurately reflect the posture of the representation and expectations of the corporate client and its principals. Taking the time to address these issues at the beginning of representation, and reviewing them periodically, may avoid undesirable outcomes later in litigation.