ETHICS ADVISORY OPINION

10-03

UPON THE REQUEST OF A MEMBER OF THE SOUTH CAROLINA BAR, THE ETHICS ADVISORY COMMITTEE HAS RENDERED THIS OPINION ON THE ETHICAL PROPRIETY OF THE INQUIRER'S CONTEMPLATED CONDUCT. THIS COMMITTEE HAS NO DISCIPLINARY AUTHORITY. LAWYER DISCIPLINE IS ADMINISTERED SOLELY BY THE SOUTH CAROLINA SUPREME COURT THROUGH ITS COMMISSION ON LAWYER CONDUCT.

Factual Background:

Several years ago, an attorney conducted a transaction which pertained to a bond for title/contract for sale for two parties. This transaction does not transfer legal ownership in the subject real property, only an equitable interest in the property at the time of the transaction, and legal ownership does not transfer to prospective purchasers until the legal title owner of that property is paid in full by said prospective purchasers.

Another attorney with the same law firm, who practices at another location than the previous attorney, may be retained by the Homeowners Association to address a violation of the recorded covenants and restrictions on the subject real property. This would include sending letters to the prospective purchasers on behalf of the Homeowners Association regarding such violations, and potentially filing a lawsuit on behalf of Homeowners Association against both prospective purchaser and title owner.

Question Presented:

Is it a conflict of interest under the rules of ethics, particularly under Rule 1.9, for Attorney/law firm to represent the Homeowners Association in this matter?

Summary:

No. Without more, the mere conduct of a residential closing is not substantially related, for purposes of Rule 1.9, to an HOA's later efforts to enforce covenants or restrictions against the buyer.

Opinion:

Assuming the buyer is a former client and not a current client, the analysis is the same regardless of whether the HOA is represented by the lawyer involved in the closing or another lawyer in the same firm. See Rule 1.10(a) ("While lawyers are associated in a firm, none of them shall knowingly represent a client when any one of them practicing alone would be prohibited from doing so by Rule[] … 1.9.").

Rule 1.9(a) states, "A lawyer who has formerly represented a client in a matter shall not thereafter represent another person in the same or a substantially related matter in which that person's interests are materially adverse to the interests of the former client unless the former client gives informed consent, confirmed in writing." The HOA's interests in enforcing the restrictions would necessarily be adverse to the former client; therefore, the representation would be prohibited (absent informed consent) if the two matters were substantially related. The Committee believes that the matters are not "substantially related" as contemplated by Rule 1.9.

The South Carolina Supreme Court has held that representing a borrower in a residential transaction and later representing the lender in foreclosure does not create an appearance of impropriety. In re Anonymous, 298 S.C. 163, 378 S.E.2d 821 (1989). The "appearance of impropriety" standard, applicable at the time, was a higher standard of conduct (i.e., a lower conflict threshold) than the "substantially related" test, which today applies to former-client conflicts. Therefore, what was proper under the former test must be proper under the new test, absent a specific prohibition. Nothing in Rule 1.9 or the comments thereto would prohibit foreclosure after a residential closing.

When the closing involves an installment land sale contract, rather than a sale by deed, whether a substantial relationship exists between the closing and a later action against the buyer would depend on 1) whether the lawyer advised the buyer about the specific contract involved or merely advised the buyer about land contracts generally and 2) whether the subsequent adverse representation involved the same legal issues about which the lawyer gave the buyer advice. Ordinarily, neither would occur. Therefore, without more, enforcement of HOA covenants or restrictions based solely on post-closing acts or omissions of the buyer would not ordinarily be substantially related to the prior closing.

Comment 3 to Rule 1.9 gives examples of permissible and impermissible subsequent representation. It states that a lawyer who assists a developer in obtaining environmental permits for a shopping center cannot later represent "neighbors seeking to oppose rezoning of the property on the basis of environmental considerations, but would not be precluded … from defending a tenant of the completed shopping center in resisting eviction for nonpayment of rent." Rule 1.9 cmt. 3 (emphasis added). These examples are consistent with the court's language in In re Anonymous. While the residential closing-foreclosure paradigm falls somewhere between the bookends provided in these comment examples, the rule and comments appear directed at subsequent representation that involves either legal advice on the same specific substantive issues

or legal claims based on the same facts. In short, not all related matters are substantially related for Rule 1.9 purposes. Compare Townsend v. Townsend, 323 S.C. 309, 474 S.E.2d 424 (1996) (where lawyer guardian ad litem for minor child in parents' divorce later represented father in claim for child support reduction, in which child was joined as a party, substantial relationship was found because, as guardian, lawyer had obtained confidential factual information about child that was relevant to child support reduction claim) with Madison v. Graffix Fabrix, Inc., 304 S.C. 321, 404 S.E.2d 37 (Ct. App. 1991) (no substantial relationship where lawyer had represented employer in dispute with former employee accused of trying to steal employees, then represented different employee against employer in dispute over termination).

The Committee notes that this opinion is a odds with prior opinions on similar issues. The reasons are explained below.

In 1984, this Committee advised that it would be impermissible for a lawyer to represent a buyer at a residential closing and later represent a lender in a foreclosure proceeding that is adverse to the buyer and involves the same property. See EAO 84-24. In 1989, the South Carolina Supreme Court came to the opposite conclusion, effectively overruling 84-24 but without mentioning it. In re Anonymous. Both 84-24 and In re Anonymous were decided under the former Code of Professional Responsibility, and the Supreme Court applied the "appearance of impropriety" standard then applicable to questions of conflicts with former clients. In re Anonymous was a disciplinary opinion in which a lawyer in a sale transaction represented the buyer and also prepared the seller's deed, then later represented the buyer in an action against the seller related to the condition of the property at closing. Finding no appearance of impropriety, the court stated,

[I]n the event there is a subsequent dispute between purchaser and seller regarding the transaction, the attorney should not represent purchaser or seller so as to avoid the appearance of impropriety.

We emphasize that this rule is limited to litigation directly related to the sale itself. In the absence of some other reason for disqualification, the closing attorney would not be prevented from representing either the seller, purchaser or lender in a subsequent mortgage foreclosure regarding the property.

In re Anonymous, 298 S.C. at 164, 378 S.E.2d at 821, & n. 1. Nevertheless, in 1990, the Ethics Advisory Committee again advised that a lawyer may not represent a lender in foreclosing a loan if the lawyer previously represented the borrower in closing that loan. See EAO 90-22.

Opinion 90-22 was decided under then-new Rule 1.9, which governs conflicts with former clients. With the adoption of Rule 1.9, the "substantially related" test replaced "appearance of impropriety" as the standard against which questions of former-client conflicts are measured. Opinion 90-22 expressly relied on 84-24 for the conclusion that the closing and foreclosure are substantially related, but the "substantially related" test was not the governing rule at the time of 84-24, and 84-24 was implicitly overruled by In re Anonymous. 90-22 also relied on specific language from the comments to Rule 1.9, but that language (now delineated as part of Comment 2), expressly relates to the scope of a single "matter" as contemplated by the rule and upon examination is inapplicable to the "substantially related" test. Comment 3 to Rule 1.9 addresses the "substantially related" test

and is consistent with the language in In re Anonymous. The Committee notes that the comments were not delineated in 1990 and that the comment language regarding the "substantially related" test did not exist; what the Committee relied on in 1990 was later delineated as Comment 2 (which entirely relates to the scope of a matter under Rule 9) and Comment 3 was added.

Comment 3 states that matters are substantially related if 1) "they involve the same transaction or legal dispute" or 2) "there otherwise is a substantial risk that confidential factual information as would normally have been obtained in the prior representation would materially advance the client's position in the subsequent matter." The residential closing-foreclosure circumstance does not involve the same transaction or dispute; it involves a transaction and a later tangentially related—but not substantially related— dispute over facts (i.e., default on the loan) that typically occur after the closing is completed and would not be contemplated at the time of closing. In certain unusual circumstances, a substantial relationship could exist if some event from the closing (e.g., document execution) were a disputed issue in the foreclosure. Likewise, the residential closing-foreclosure circumstance, without more, does not involve a substantial risk that confidential information gained at closing would materially advance the lender's position in foreclosure. Foreclosures are based on default, which typically would not occur until after closing. A substantial relationship could exist if the lender's position in the foreclosure would be materially advanced by information obtained at closing, but this circumstance would be unusual. Residential closing lawyers rarely learn anything confidential about the borrower, as most if not all information is shared among all parties, and a residential closing lawyer ordinarily does not learn anything about the borrower that both would relate to a later foreclosure and is not shared with the lender at closing. "Information that has been disclosed … to other parties adverse to the former client ordinarily will not be disqualifying." Rule 1.9 cmt. 3.

In a subsequent opinion closer to the specific issue in this inquiry, the Committee in 2005 advised that a lawyer who represents a buyer in the closing of a residential sale transaction cannot later represent a Homeowners Association against the buyer in collecting a debt for unpaid HOA dues related to the property purchased at the prior closing. See EAO 05-05. However, 05-05 relied entirely on 90-22 and 84-24 for its conclusion; it quoted the same Comment 2 language as 90-22; and, like 90-22, concluded without analysis that the matters are substantially related because the 1984 advisory opinion had said as much. Opinion 05-05 also did not acknowledge that 84-24 was overruled by In re Anonymous.

The Committee advises today that 84-24 has been overruled and that 90-22 and 05-05 do not accurately reflect the applicability of the "substantially related" test of Rule 1.9 to the closing-foreclosure paradigm. A lawyer who closes a residential real estate transaction and advises the borrower about mortgages generally, without more, is not prohibited from later representing the lender in a foreclosure action based on post-closing acts or omissions of the borrower. An HOA enforcement action involving a lien or other encumbrance or restriction against the same property, which arises after closing based on post-closing acts or omissions, is even less related to the closing than is a foreclosure and therefore would also not be substantially related, nor would foreclosure of a subsequent mortgage not closed by the same lawyer but affecting the same property.