Ouch! First your company sees its stock price go down, and then it gets a class action alleging securities fraud. A double whammy! You review the allegations and wonder where the plaintiffs got their information. It sounds like plaintiffs' counsel is getting, and using, confidential information from one of your employees—a corporate mole. Are plaintiffs' counsel permitted to do that? Can they be forced to identify the mole? And can you do anything about the mole, once he or she is found?

The Most Dangerous Game: Hunting the Corporate Mole

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The clearest answer, is, unfortunately: Whatever you do, be careful. The corporate mole is big game, and its hunt is marked by barriers and pitfalls.

Can You Find Your Mole?

Let's start with the complaint. A class-action securities fraud plaintiff generally is not required to identify confidential sources for the complaint in order to satisfy the heightened pleading requirements of the Private Securities Litigation Reform Act (PSLRA),[1] provided that other facts alleged in the complaint adequately show fraud.[2] This rule is premised on the view that disclosure would not serve the purpose of the pleading, and could deter informants from providing critical information to legitimate investigators or expose them to retaliation.[3] But the plaintiffs may have to disclose the information during discovery.[4]

Can Plaintiffs' Counsel Exploit a Mole?

As discussed above, you may not be able to force disclosure of the mole's identity. Here the information is confidential, and the unidentified source, a corporate insider, was clearly not authorized to disclose the information. Do you have any recourse against plaintiffs' counsel?

The best one can say is that the few reported decisions are mixed. Where the receiving attorney actively solicited the receipt of an adversary's confidential information, courts have imposed sanctions that included disqualification for violation of the ethical rules.[5] Some courts have even punished attorneys, either by disqualification or with an evidentiary bar, for using confidential information that they did not solicit where the courts deemed the sanction necessary to preserve "the integrity of [the] judicial proceeding."[6]

Counsel who seek out moles . . .

A recent case illustrates these principles. In *EEOC v. Hora, Inc.*,[7] the intervenor-plaintiff alleged that the defendants engaged in unlawful employment practices with respect to the intervenor and other female employees. Some of the information the intervenor relied on in her claim against her employer came from a corporate mole: the administrative assistant to the defendant's general manager. Before any lawsuit or EEOC investigation, intervenor's counsel had communicated via email with this assistant, seeking information about counsel's client as well as other employees. Following her client's termination, counsel continued to seek information from the assistant whom, the court found, she knew or should have known was a disgruntled employee "who occupied a position of intimate business trust at the high level of [defendant's] management."[8] The emails showed that counsel explicitly encouraged the administrative assistant to gather and relay information, including confidential business and personnel information to which she had "continuous exposure and direct access."[9]

The court disqualified counsel, rejecting her contention that she was merely "the fortuitous recipient of unsolicited information."[10] Instead, the court found that counsel knew that defendant's administrative assistant "was a well-placed, potentially useful 'mole'," and that counsel "was unabashed and unreserved in her exploitation of [the administrative assistant's] position and of [her] obvious personal agenda."[11] Consequently, the court ruled that counsel had subverted the discovery process and violated a number of ethical rules:

> *[b]y using [the defendant's employee] as an informational mole and subsequently representing the information from [the employee's] reports as factually true as part of her campaign with the EEOC, [counsel] has not only violated her adversaries' legal rights that permit an appropriately calculated and sometimes negotiated flow of information through the traditional*

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discovery process, but she also contemporaneously risked undermining the EEOC's official role and thwarted policies underlying a number of ethical rules.[12]

The court grouped counsel's violations of the Rules into three categories.[13]

Communicating with person represented by counsel. Rule 4.2 bans communications relating to the subject of the representation with a person whom the lawyer knows to be represented by counsel. Here the assistant arguably fell within this category, as her broad responsibilities and position central to management operations, which gave her access to confidential information, may have placed her in a position to impute liability to the defendants. At a minimum, the court held, counsel should have considered waiting for proper discovery procedures and then notifying the defendants that she wanted to speak with the assistant.

Violating the legal rights of defendants. Rule 4.4(a) bars a lawyer from obtaining evidence by methods that violate the legal rights of third persons. In this case, the court found emails clearly showed that counsel encouraged the assistant to disclose all information, and counsel did not present credible evidence that she had informed the assistant that relaying confidential and privileged information was improper.

Inducing ethical violations. Rule 8.4(a) bars as misconduct a lawyer's violation of the ethical rules or the lawyer's knowing assistance or inducement of another to violate the ethical rules; Rule 8.4(c) bars as misconduct a lawyer's participation in conduct involving dishonesty, fraud, deceit, or misrepresentation. The court found that counsel violated these provisions by surreptitiously inducing the assistant to help her violate the ethical rules by giving her privileged and confidential information.

Because of these violations and the resulting prejudice to the defendants in their defense of the EEOC claim, the court ordered the disqualification of intervenor's counsel.

The approach in *Hora* is analogous to cases involving counsel's solicitation of privileged and confidential information from *former* managerial employees of a defendant corporation. These cases vary on whether some of the ethical rules, such as Rule 4.2, preclude counsel's contact with the former employee.[14] There is, however, more consensus on the application of other rules; many of these cases hold, and the American Bar Association (ABA) has cautioned,[15] that counsel might be disqualified for violating other ethical rules, such as Rule 4.4,[16] or because their receipt of confidential information taints the judicial process.[17]

What if the attorney does not actively solicit confidential information from a current or former employee of an adversary, but is presented with such information after initial contact by the employee?

. . . and counsel who have moles thrust upon them

What if the attorney does *not* actively solicit confidential information from a current or former employee of an adversary, but is presented with such information after initial contact by the employee? Sanctions imposed for the subsequent use of that information may fall short of disqualification. For example, in *In re Shell Oil Refinery*,[18] involving a class action lawsuit against Shell arising out of a refinery explosion, a Shell employee, through an attorney, contacted the plaintiffs' counsel because the employee believed that the company was intentionally concealing facts or misleading plaintiffs' counsel. During discovery, it became clear to Shell that plaintiffs' counsel had obtained Shell documents by means other than discovery, probably from a mole—an unidentified Shell employee. Shell sought discovery of all documents in the possession of plaintiffs' counsel as well as the identity of the employee who provided those documents. The court ordered plaintiffs to produce the documents and prohibited their further use by the plaintiffs, but denied Shell's request for the identity of the mole on the grounds that disclosure was not relevant to remedying the unfairness caused by plaintiffs' use of the documents.

Both parties unsuccessfully sought reconsideration. The court rejected Shell's argument based on the "no-contact" prohibition of Rule 4.2. The court found that whether the rule had been violated or not, the real issue was counsel's surreptitious receipt of the Shell documents from the employee, because such receipt was both "inappropriate and contrary to fair play."[19] Based on its inherent authority to remedy practices that threatened judicial integrity and the adversary process, the court held that an order requiring production of the documents and prohibiting their further use would not only preserve the integrity of the proceeding but would also balance the scales between the parties.

A Spectrum of Sanctions

The difference in sanctions imposed in *Shell* and *Hora* resulted from the courts' differing views of the mole's motives and of the culpability and complicity of the attorney in receiving and using the mole's unauthorized disclosures. At one end of the courts' spectrum would be the righteous mole, motivated by a desire to blow the whistle on fraud, and the attorney who receives the mole's information unsolicited. The *Shell* court, for example, acknowledges the mole's apparently valid motive to remedy the company's perceived failure to comply with a discovery request.[20] The ABA has also cited the legitimacy of the whistleblowing motive in its

refusal to prohibit an attorney from using an opponent's confidential materials received without solicitation from an unauthorized source. The ABA has instead set out a general duty:

- to refrain from reviewing the materials,
- to notify the adversary's lawyer as to the receipt of the material, and
- to await instructions from that lawyer or from a court as to the proper disposition of the material. [21]

At the other end of the spectrum would be an attorney who actively solicited confidential information from a corporate insider in violation of the ethical rules. Of course, the ABA's logic would *not* justify that kind of behavior,[22] and *Hora*'s reasoning might well justify sanctions against the attorney.

Somewhere between these two poles lies the current practice of some plaintiffs' class action counsel, who arguably solicit potential clients on their websites by encouraging employees to reveal corporate frauds that could be the basis of a class-action lawsuit.[23] Questions as to the ethical propriety of these types of solicitations have not been resolved.

Moles and Morals

Although the law is far from settled, there are still some lessons to be learned.

Receive information with care. Receiving information from the employee or officer of an adverse party can be risky. Carefully examine the circumstances and applicable ethical rules before accepting the information.

Plug the leaks. You should promptly raise in court any indication that your company's information is being leaked to an adversary. Often your corporation can obtain some relief even if the court will not order disclosure of the leaker's identity.

Treat moles with caution. Approach any investigation of the mole's identity with caution and with the advice of experienced counsel. Whistleblower protection provisions, such as those contained in the Sarbanes-Oxley Act of 2002[24] and in various state statutes, can have draconian penalties.

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Notes

1. 15 U.S.C. § 78u-4(b)(1).
2. *See e.g., In re Daou Systems, Inc.*, 411 F.3d 1006 (9th Cir. 2005); *California Public Employees' Retirement System v. Chubb Corp.*, 394 F.3d 126 (3d Cir. 2004); *In re Cabletron Systems, Inc.*, 311 F.3d 11 (1st Cir. 2002); *ABC Arbitrage Plaintiffs Group v. Tchuruk*, 291 F.3d 336 (5th Cir. 2002); *Florida State Bd. of Admin. v. Green Tree Financial Corp.*, 270 F.3d 645 (8th Cir. 2001); *Novak v. Kasaks*, 216 F.3d 300 (2d Cir. 2000).
3. *Novak*, 216 F.3d at 314.
4. *See Florida State Bd. of Admin.*, 270 F.3d at 668.
5. *See, e.g., EEOC v. Hora, Inc.*, No. Civ.A. 03-CV-1429, 2005 WL 1387982 (E.D. Pa. June 8, 2005); *Camden v. Maryland*, 910 F. Supp. 1115 (D. Md. 1996); *see also ABA Comm. on Ethics and Professional. Responsibility*, Formal Op. 91-359 (1991) (Contact with Former Employee of Adverse Corporate Party) (hereinafter "ABA Opinion on Former Employee Contact").
6. *In re Shell Oil Refinery*, 143 F.R.D. 105, 108 (E.D. La. 1992); *see ABA Comm. on Ethics and Professional Responsibility*, Formal Op. 94-382 (1994) (Unsolicited Receipt of Privileged or Confidential Materials) (hereinafter "ABA Opinion on Receipt of Confidential Information").
7. No. Civ.A. 03-CV-1429, 2005 WL 1387982 (E.D. Pa. June 8, 2005).
8. *Id.* at *2 –*3.
9. *Id.* at *3. Information provided to intervenor's counsel included the defendant's employment handbook, the content of private interviews between management and employees that were conducted by defendant's counsel following the filing of the EEOC claim, the content of private attorney-client conversations between the defendant's owners and defendant's counsel overheard by an employee who was eavesdropping on the conversations, the content of the personnel file of an employee alleged to be involved in harassing the intervenor, and the content of a confidential document from the defendant to the EEOC in response to the EEOC charge. *See id.* at *4–*7.
10. *Id.* at *3.
11. *Id.*
12. *Id.* at *9.
13. The court applied the Pennsylvania Rules of Professional Conduct, which are substantially similar to the ABA Model Rules of Professional Conduct.
14. *See Arnold v. Cargill Inc.*, No. 01-2086 (DWF/AJB), 2004 WL 2203410, at *9 (D. Minn. Sept. 24, 2004).
15. *See* ABA Opinion on Former Employee Contact.
16. *See Cargill Inc.*, 2004 WL 2203410 at *7–*8 (finding that law firm cultivated its relationship with former managerial employee of defendant corporation "precisely because he possessed a wealth of relevant information," and, instead of advising employee not to disclose privileged information as it was obligated to do, encouraged employee to send over any documents pertaining to the defendant in employee's possession, including privileged documents).
17. *See MMR/Wallace Power & Indust., Inc. v. Thames Assoc.*, 764 F. Supp. 712, 727 (D. Conn. 1991).
18. 143 F.R.D. 105 (E.D. La. 1992).
19. *Id.* at 108.
20. *Id.*
21. *See* ABA Opinion on Receipt of Confidential Information; *see also* Gloria A. Kristopek, "To Peek or Not to Peek: Inadvertent or Unsolicited Disclosure of Documents to Opposing Counsel," 33 *Val. U. L. Rev.* 643, 658 (Spring 1999) (public policy considerations may outweigh confidentiality concerns when reviewing the unsolicited receipt of confidential documents).
22. *Cf. Va. State Bar Standing Comm. on Legal Ethics*, Op., 1786 (Dec. 12, 2004) (Disclosure and Use of Confidential Documents Obtained by a Client Without Authorization) (a lawyer's use of confidential documents received from a whistleblower client depends on whether the use will violate Rules 3.4(a) or 4.4; in applying Rule 4.4, how the client acquired the documents is crucial).
23. *See* the "Report a Fraud" webpages at *www.milbergweiss.com/contact/reportafraud.aspx*, and at *www.lerachlaw.com/lcsr-cgi-bin/mil?templ=report-fraud.html*.
24. Pub. L. No. 107-204, § 806, 116 Stat. 745, 802 (2002), to be codified at 18 U.S.C. § 1514A.