

## California Court Of Appeal Holds LLC's Former Counsel May Represent Insider Defendants In Derivative Suit

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Derivative actions can be somewhat confusing. Although the entity is essentially the plaintiff, it is named as a defendant. Initially, one might question why must the corporation be named as a party? I can think of at least two reasons. First, the litigation involves the rights of the entity directly. Second, including the entity as a party helps to ensure that the defendants will enjoy the protection of *res judicata* should they prevail. Those are reasons for naming the entity as a party, but why name the entity as a defendant rather than as a plaintiff? In California, this seemingly odd result follows from Section 382 of the Code of Civil Procedure: "If the consent of any one who should have been joined as plaintiff cannot be obtained, he may be made a defendant, the reason thereof being stated in the complaint . . .".

In the case of a limited liability company, a lawyer may at times represent the company and the manager of the company. When a derivative suit is brought by a member, does the attorney's prior representation of the company disqualify the attorney from representing the company's manager? That was the question before the California Court of Appeal in *Beachcomber Management Crystal Cove, LLC v. Superior Court*, 2017 Cal. App. LEXIS 664 (Cal. App. 4th Dist. June 28, 2017).

Writing for the Court, Justice [Richard M. Aronson](#) concluded that an attorney may represent the insiders in a derivative lawsuit despite the attorney's previous representation of the company regarding issues raised in the suit. In reaching this conclusion, the Court focused on a line of cases that govern governing successive representation in derivative lawsuits brought by small or closely held companies (*Forrest v. Baeza*, 58 Cal. App. 4th 65 (1997) and following cases). The *raison d'être* for disqualification in successive representation cases is to prevent the attorney from using confidential information gained from the representation of the entity. This rationale breaks down when the insider defendants essentially had access to the same information. Thus, that becomes the "critical inquiry".

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