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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FIRST APPELLATE DISTRICT

DIVISION THREE

IAR SYSTEMS SOFTWARE, INC.,

Plaintiff, Cross-defendant and
Respondent,

v.

NADIM SHEHAYED,

Defendant, Cross-complainant and
Appellant.

A141298

(San Mateo County
Super. Ct. No. CIV516550)

Defendant and cross-complainant Nadim Shehayed appeals from an order denying his motion to disqualify the law firm of Valla & Associates, Inc., P.C. (Valla firm). IAR Systems Software, Inc. (IAR), represented by the Valla firm, has filed this action against Shehayed seeking damages and related relief based on the allegation that, while employed by IAR as its chief executive officer, Shehayed converted substantial amounts of IAR's funds to his own use. Shehayed has cross-complained alleging wrongful termination. The motion to disqualify is based on the allegation that an attorney-client relationship between him and the Valla firm developed when he testified at a deposition in another former employee's wrongful termination action against IAR, at which an attorney from the Valla firm appeared as counsel for IAR and, he asserts, also as his attorney. We agree with the trial court's conclusions that the Valla law firm never represented Shehayed, that there was no reasonable basis for Shehayed to believe

otherwise, and that Shehayed disclosed no personal confidential information to the Valla firm attorneys. We shall therefore affirm the order denying the disqualification motion.

Background

With only minor editing changes, the following facts are taken directly from Shehayed's opening brief.

Shehayed was the president and general manager of IAR from 1994 until his employment was terminated on September 10, 2012. IAR is the subsidiary of IAR Systems Group AB (IAR Sweden), which is a publicly traded Swedish corporation. Shehayed was also a director of IAR, along with Stefan Skarin and Stefan Ström. Skarin is the chief executive officer of IAR Sweden. Ström is the chief financial officer of IAR Sweden. Shehayed started IAR as its first employee and built that company over the course of 18 years. During the course of employment he was the person in charge of building the business and was responsible for managing the operation of the business. He was in charge of all aspects of the business, such as sales, marketing, hiring, firing, and legal affairs. He reported to IAR Sweden at various points in time about various issues. He hired the Valla firm to act as counsel to IAR.

For a period of at least 10 to 14 years, Antonio Valla (or law firms that he has been with) provided legal advice to IAR.¹ The Valla firm prepared annual statements, board minutes, resolutions, and shareholder minutes. In 2011, Shehayed worked with the Valla firm on negotiations in which IAR Sweden acquired a company called Segma. A lawsuit brought by Kyle Brown against IAR was the first time that Shehayed had any involvement with litigation.

¹ Shehayed's opening brief states as a fact, "For a period of at least [10] to [14] years, Valla (or law firms he has been with) provided legal advice to Shehayed." In support of this statement, Shehayed directs us to his declaration, which reads: "I hired the law firm of Valla & Associates, Inc. to act as counsel to IAR Systems Software, Inc. I do not recall the date but it was many years ago. [¶] For a period of at least [10] to [14] years, Mr. Valla (or law firms that he has been with) provided me legal advice." As indicated more fully below, there is no indication in the record that Valla or his firm provided any advice to Shehayed other than in his corporate capacity and for purposes of the business.

On August 8, 2011, Brown filed an action against IAR alleging causes of action for wrongful termination in violation of public policy, breach of contract, and breach of the implied covenant of good faith and fair dealing. Brown alleged that his employment as an account manager was terminated because he complained to Shehayed about “unlawful and unethical accounting practices,” which violated the Securities Exchange Act of 1934 (15 U.S.C. § 78a et seq.) and “ ‘other California, federal, and international laws’ ” (*Brown* action). Brown complained IAR’s database “was changed to incorrectly reflect that several large shipments, in the approximate amount of \$500,000, were shipped in the first week of January 2011. In fact, these shipments were shipped in December 2010.” The complaint continued: “Not only was the misallocation illegal, improper and unethical, but it resulted in monetary loss to Brown and other employees of IAR, domestic and international. Brown lost approximately \$5,000 to \$10,000 of his profit sharing and commissions based on this unlawful conduct.” After his last complaint, Brown allegedly was unlawfully terminated.

Shehayed selected and hired the Valla law firm to respond to the *Brown* action. Shehayed had numerous telephone calls and at least three face-to-face meetings with the Valla law firm in connection with the *Brown* action. For example, the Valla firm asked him to collect all documents that pertained to the lawsuit and to provide answers to interrogatories. He met with Valla at his office to discuss the case, the background of Brown’s employment, and how IAR did the invoicing and “the booking of revenues.” Shehayed provided details of timing: the date of shipping products, sending invoices, and reporting revenues. Shehayed explained to Valla that he worked with and coordinated with Skarin on revenue reporting. He explained that Skarin used to give him guidance, on a regular basis, on what was a “good number of revenue to report on a monthly basis and especially at year end.” He worked under Skarin’s direction to give him the number that he wanted. Shehayed understood that these communications with Valla were confidential. According to Shehayed’s declaration, he was acting under the belief and assumption that Valla was acting as both his lawyer and as a lawyer for IAR. Valla assertedly did not explain to Shehayed any difference between representing Shehayed and representing

IAR. He did not tell Shehayed that his law firm was representing IAR alone, and was not serving as his attorney as well. Shehayed states that he placed great personal trust in Valla and his firm.

Shehayed met with Michael Purcell, an attorney in the Valla firm, to prepare for his deposition in the *Brown* action. According to Shehayed, “as a person very first time I go through that deposition, I was very nervous, . . . and Mr. Purcell helped me out. I mean, coached me how to listen, listen to the question. [¶] . . . [He] helped me figure out how to answer and what to answer as well.” “And we did like a role-play practice session.” Shehayed states he understood that Purcell would be guiding him and protecting him at the deposition, and he thought and assumed that Purcell was acting as his attorney and as an attorney for IAR. Purcell assertedly did not tell Shehayed that he was representing IAR only and that he would not be representing Shehayed at the deposition.

On March 1, 2012, Shehayed appeared for his deposition accompanied by Purcell and Valla. The three discussed the deposition before it started and also met on a lunch break at the deposition. Shehayed was questioned about the performance of Brown, the termination of Brown, delays in “booking revenues,” shifting of revenues, shipping dates and orders, and health benefits for Brown. The Valla firm attorneys did not state on the record who they did or did not represent.²

On July 20, 2012, while the *Brown* action was still pending, Ström wrote a memo to Skarin: “We have engaged our lawyer at Valla & Associates to guide us in terminating the employment relationship with Nadim Shehayed on good cause.” Shortly after the July 2012 memo, there was a meeting in the IAR office to discuss strategy in the *Brown* action. The persons present were Valla, Ström, Danielle Burgard and Shehayed. During the course of that meeting, there was discussion of formulating a defense to the lawsuit:

² Shehayed asserts that he and opposing counsel were led to believe that the attorneys represented both the corporation and him personally, and his contention is supported by the declaration of Brown’s attorney. Shehayed cites one instance at the deposition where he referred to “my attorneys” to whom he provided answers to interrogatory questions, and another instance when Brown’s attorney referred to “your counsel” who might object to questions for the record.

according to Shehayed, it was decided that the company would admit that an “accounting ‘mistake’ ” had been made and the company would blame Shehayed for the mistake. Another IAR employee designated as the “person most qualified” subsequently testified that Shehayed was responsible for the improper accounting and Skarin denied discussing the practice with Shehayed as Shehayed had testified at his deposition. In August 2012, Purcell prepared Shehayed to testify at trial without informing him that IAR had engaged the law firm to terminate him. A settlement agreement with Brown was entered on August 27, 2012, and the action was dismissed on September 14.

The present action was filed by the Valla firm on behalf of IAR against Shehayed and his wife on September 7, 2012.³ The complaint alleges causes of action for conversion, fraud, breach of contract, breach of fiduciary duty, and constructive trust. The complaint does not refer to the *Brown* action or to any issues involved in that action, except as follows: “In 2012, while investigating alleged financial improprieties of [Shehayed] that were alleged in a lawsuit filed by a former employee, IAR determined that [Shehayed] had been abusing his position of trust and converting IAR’s funds for his own use.” The sole predicate for each of the causes of action is Sheyahed’s alleged misappropriation of funds by “paying to himself salaries in excess of that which his contract with IAR permitted, paying a salary to his wife . . . despite the fact that [his wife] is not and never was an employee of IAR, pa[y]ing excessive bonuses to himself, paying himself for business expenses that he had never incurred, contributing to a 401k retirement account for [his wife] despite the fact that she is not and never was an employee of IAR and was not entitled to a 401k account, and paying excessive bonuses with IAR’s funds to himself, [his wife], and the other employees of IAR.”

In answering an interrogatory in the present case, IAR stated that “[i]n addition to the facts complained of in [its] complaint, [it] terminated [Shehayed] for incompetent management of the company, including mishandling the termination of an employee that resulted in a lawsuit against [IAR].” Shehayed’s cross-complaint alleges, among many

³ Shehayed was terminated on September 10, 2012.

other things, that he was terminated without good cause, that the incorrect “revenue booking” claimed by Brown was attributable to Skarin and that he (Shehayed) was “scapegoat[ed]” to protect Skarin, and that the alleged misappropriation of funds, which he denies, is “a pretextual attempt to terminate [his] employment.”

Some 10 months after commencement of the action, Shehayed filed his motion to disqualify the Valla firm.⁴ The motion and supporting papers, based on the facts described above, contend the Valla firm represented Shehayed as well as IAR in connection with the *Brown* action and it therefore had simultaneously represented clients with conflicting interests requiring automatic disqualification; and the Valla firm was now representing IAR against a former client who had previously transmitted confidential information to the Valla firm attorneys in a case with closely related issues. The Valla firm filed an opposition asserting that there was never an attorney-client relationship between Shehayed and it or any of its attorneys; that, at the time of Shehayed’s deposition in the *Brown* action, there was no conflict in the interests of Shehayed and IAR; and that Shehayed had never disclosed any confidential information to the Valla firm attorneys. Faced with conflicting declarations, the trial court conducted a one-day evidentiary hearing and the following day provided a full explanation from the bench of its reasons for denying the motion.

The court explained: “I am going to deny the motion to disqualify. And the reasons are these, and I am going to find these things based on the facts that are before me by a preponderance of the evidence here that I have heard. And I think that the first thing that is clear is that the Valla firm was always the lawyers for the [IAR]. They were hired as such by Mr. Shehayed years ago and even though there was some change in the

⁴ After explaining its reasons for denying the motion, the trial court added that the timing of the motion was “very problematic” but that “if there were [a] clear case of conflict of interest of an attorney/client relationship with . . . Shehayed personally, and a conflict of interest [at] the time of [the] Brown deposition triggering disclosure,” the court “wouldn’t let the timing of the motion carry the day and override that.” Since we agree with the basis on which the trial court denied the motion, we need not consider IAR’s alternative contention that the ruling is supported by an unreasonable delay in filing the motion.

actual law firm, it is clear that Mr. Valla himself was the counsel for the corporation for many years, having been hired by Mr. Shehayed originally. [¶] And Mr. Shehayed himself testified that at no time during that long relationship did Mr. Valla or his firms perform any personal legal services for Shehayed for which Shehayed engaged in or paid for legal services. [¶] . . . The question then becomes what happens when the deposition in the [*Brown*] case occurs and the argument [is made here in support of a motion that at that deposition, the law firm's appearance, Mr. Valla's appearance, was a holding out and implied representation of appearing as a lawyer for Mr. Shehayed himself. And while it might be in my opinion that another type of employee could come here and say that the Valla firm that employee thought were his or her own lawyers, my view is that Mr. Shehayed is not able to say that. [¶] . . . [¶] Now, I am going to find here based on the evidence that I have heard, a preponderance of that evidence, that Mr. Shehayed in this situation did neither of those two things[: (1) manifest to a lawyer his intent that the lawyer provide legal services for him, and either the lawyer manifests to the person consent to do so, or the lawyer fails to manifest lack of consent to do so, and the lawyer reasonably knows that he is going to rely on the lawyer to provide those services, or (2) submit confidential information to a lawyer with the reasonable belief that the lawyer was acting as his attorney]. The only confidential information that he imparted, and the evidence is clear on this I think, was the company's confidential information that he had had access to as the chief executive officer. . . . And I think under all of the circumstances here that Mr. Shehayed could not reasonably believe that at the time of the Brown deposition that Mr. Valla and his firm were representing Shehayed personally. [¶] He was there as the chief executive officer. He was being questioned in that capacity. . . . And therefore, I believe that there isn't any way that he reasonably would have generally thought that the lawyers were there representing him in some personal capacity. [¶] I am also going to find that there was no existing conflict of interest at the time of the Brown deposition requiring that the attorneys give warnings to Mr. Shehayed under [*Upjon v. United States* (1981) 449 U.S. 383] or alternatively give advice under the 300 series of the Rules of Professional Responsibility that apply to attorneys in this state as to a need

for Mr. Shehayed to be either separately represented, or of his right to have separate representation. And that is because the preponderance of evidence here is that there was no apparent potential material liability exposure that was personal to Mr. Shehayed in the *Brown* case. . . . [¶] And it is my opinion, and I am going to so find, that an experienced litigation lawyer as Mr. Valla and the kind of business litigation and wrongful termination litigation that was involved in *Brown*, making an evaluation of the liability exposures here would reasonably conclude, as Mr. Valla testified he did, that there was no personal exposure to Mr. Shehayed that presented and triggered a conflict of interest in the company's lawyers representing him at the deposition. [¶] . . . [¶] Finally, I think coupled with the conclusion that the plaintiff's lawyers in this case did not represent Mr. Shehayed as a personal client, and did not have any conflict of interest in doing so, . . . there is no basis for disqualification on the notion that they obtained confidential information of Mr. Shehayed's that was personal to him that could be used against him in this case given that all of the confidential information that was imparted belonged to the company who owned and had control of the attorney/client privilege over that information."

Following the trial court's denial of his motion for reconsideration and this court's denial of his petition for a writ of mandate, Shehayed timely filed a notice of appeal from the order denying the motion to disqualify.

Discussion

Shehayed asserts that disqualification of the Valla firm is required because the attorneys represented clients with conflicting interests in violation of rule 3-310(C) of the Rules of Professional Conduct⁵ (rule 3-310(C)) and failed to provide disclosures required

⁵ Rule 3-310(C) provides: "A member shall not, without the informed written consent of each client: [¶] (1) Accept representation of more than one client in a matter in which the interests of the clients potentially conflict; or [¶] (2) Accept or continue representation of more than one client in a matter in which the interests of the clients actually conflict; or [¶] (3) Represent a client in a matter and at the same time in a separate matter accept as a client a person or entity whose interest in the first matter is adverse to the client in the first matter."

by rule 3-600(D) of the Rules of Professional Conduct (rule 3-600(D)).⁶ The factual basis for the trial court's rulings being very much in dispute, we review its orders under the deferential abuse of discretion standard. "If the trial court resolved disputed factual issues, the reviewing court should not substitute its judgment for the trial court's express or implied findings supported by substantial evidence. [Citations.] When substantial evidence supports the trial court's factual findings, the appellate court reviews the conclusions based on those findings for abuse of discretion. [Citation.]" (*People ex. Rel. Dept. of Corporations v. Speedee Oil Change Systems, Inc.* (1999) 20 Cal.4th 1135, 1143-1144.)

Substantial evidence clearly supports all of the trial court's findings and provides a reasonable basis for its decision. Based on the facts that Shehayed himself describes, the court was fully justified in finding that an attorney-client relationship never arose between Shehayed and the Valla firm, and that neither Valla nor Purcell said or did anything that could reasonably have led Shehayed to believe otherwise. It is undisputed that the Valla firm was the corporation's long-time counsel hired to represent IAR in the *Brown* action. Although Brown's claim against IAR was based in part on an accounting decision in which Shehayed was involved, the claim was asserted only against the corporation, the only defendant in the lawsuit, and there was never any suggestion that Shehayed might be personally liable to Brown. There is no suggestion that the attorneys ever stated or otherwise indicated to Shehayed or to anyone else that they were also Shehayed's lawyers. The fact that corporate counsel prepared Shehayed, the chief executive of the client being sued, for his deposition is hardly unusual and far from sufficient to create an attorney-client relationship with the officer individually. (*Koo v.*

⁶ Rule 3-600(D) provides: "In dealing with an organization's directors, officers, employees, members, shareholders, or other constituents, a member shall explain the identity of the client for whom the member acts, whenever it is or becomes apparent that the organization's interests are or may become adverse to those of the constituent(s) with whom the member is dealing. The member shall not mislead such a constituent into believing that the constituent may communicate confidential information to the member in a way that will not be used in the organization's interest if that is or becomes adverse to the constituent."

Rubio's Restaurants, Inc. (2003) 109 Cal.App.4th 719, 730-731.) The limited references that were made at the deposition to “my attorneys” to whom Shehayed provided information to respond to interrogatories, or “your counsel” who might object at the deposition, were focusing on the person to whom the information was given, or who might object, and not on whose behalf the attorneys were acting. There being substantial evidence to support the finding that an attorney-client relationship *never* arose between Shehayed and the Valla firm, there was neither a violation of the absolute rule against concurrent representation of clients with adverse interests (absent informed written consent) (*Flatt v. Superior Court* (1994) 9 Cal.4th 275, 282-283) nor of the prohibition against successively undertaking a representation adverse to a former client if there is a substantial relationship between the current and former matters (see *Flatt, supra*, at pp. 283-284; *Morrison Knudsen Corp. v. Hancock, Rothert & Bunshoft* (1999) 69 Cal.App.4th 223, 230, 234).

Even if the Valla firm were considered to have become Shehayed's attorney in connection with the Brown deposition, there was no conflict in his interests and the interests of the corporation that existed or was apparent at that time. As the trial court stated, “there was no apparent potential material liability exposure that was personal to Mr. Shehayed in the *Brown* [action]. [¶] The *Brown* [action] was focused entirely on, even in its allegations, of Mr. Shehayed acting as a general manager, and improperly manipulating the plaintiff Brown's compensation by the allegedly unlawful deferment of recognition from income from sales and products. [¶] Even the allegations that assert that that happened by a, quote, ‘general manager,’ and there was testimony I think that conceded that that reference was to Mr. Shehayed. Even that, in my view, did not represent at the time a potential liability exposure that was Mr. Shehayed's personally. And that is because it is all focused on acts that were done within the scope of his management activity as the chief executive officer of the company, and there were no allegations that Brown made in that regard that suggested that at any time Mr. Shehayed stepped outside of the confines of his employment by some other bad faith conduct that might have taken him outside of that scope of his job.” Shehayed's conjecture in his

appellate brief that the accounting irregularities alleged by Brown might have subjected him to scrutiny for Securities Exchange Act or Internal Revenue Code violations is entirely speculative, not shown to have occurred to anyone when defending the *Brown* action, and provides no basis for rejecting the trial court's finding that there was no apparent potential liability exposure for Shehayed at the time.

These well-supported findings negate Shehayed's contentions under rules 3-310(C) and 3-600(D). The Valla firm was never Shehayed's attorney and, at the time of the Brown deposition, his interests were not adverse to those of IAR. Thus, there was no concurrent representation of clients with conflicting interests proscribed by rule 3-310(C) and no duty under rule 3-600(D) for the Valla firm to explicitly advise Shehayed that it was representing only the corporation because it was not then "apparent that the organization's interests are or may become adverse to those of" Shehayed.

Shehayed's reliance on the decision in *E. F. Hutton & Company v. Brown* (S.D.Tex. 1969) 305 F.Supp. 371 is misplaced. In *Hutton*, the district court found that "[n]othing establishes that [the defendant, a former regional vice-president of Hutton] believed or should have believed that [the Hutton attorneys] were appearing only for Hutton—in fact the record has persuaded this [c]ourt to the contrary." (305 F.Supp. at p. 391.) The Hutton attorneys had worked with the defendant in connection with investigations by the Securities and Exchange Commission (SEC) and the Bankruptcy Court into a transaction in which the [defendant] was a central figure, and they appeared with him when he gave sworn testimony to the SEC and when he testified at a public hearing conducted before a bankruptcy trustee, in which the SEC participated. The district court found that it was "not accurate to say, as Hutton does, that the SEC and the Westec trustee were investigating only Hutton, and [the defendant], who appeared solely as Hutton's spokesman. The SEC and the trustee were investigating a multitude of transactions in Westec stock and were examining in depth, the conduct of every person connected with or having knowledge of such transactions. [The defendant] testified for himself as well as for Hutton." (*Id.* at p. 388.) On both occasions in which he testified, the defendant stated on the record that he was represented by the attorneys and both official

transcripts stated that he was represented by the attorneys. (*Id.* at pp. 385-387.) The SEC investigation led to a federal grand jury indictment of eight persons and the bankruptcy trustee’s report became the complaint in civil actions brought against Hutton and the defendant. (*Id.* at pp. 384-385.) Thus, unlike the situation in the present case, the attorneys that were disqualified from representing Hutton in a subsequent action against the defendant based upon the Westec stock transaction were found to have represented and to have been reasonably understood to be representing the former officer as well as the entity in connection with the prior related proceedings. (*Id.* at p. 401.) Other cases cited by Shehayed are similarly distinguishable. (E.g., *Yanez v. Plummer* (2013) 221 Cal.App.4th 180, 187 [former employee asked corporate counsel who would protect him at deposition and attorney responded that he was the employee’s attorney for the deposition]; *Pucket v. Hot Springs School Dist.* (D.S.D. 2006) 239 F.R.D. 572, 580 [attorney-client relationship established between school principal and school district’s attorney because principal “sought and obtained legal advice from” attorney]; *Advanced Mfg. Technologies, Inc. v. Motorola, Inc.*, (D.Ariz. 2002) 2002 WL 1446953, pp. 1, 5 [employee testified at deposition that he was represented by corporate counsel and counsel failed to disagree]; *Home Care Industries, Inc. v. Murray* (D.N.J. 2001) 154 F.Supp.2d 861, 868-869 [based on particular facts, the court found “an implied attorney-client relationship” between a former chief executive officer and the corporate client’s law firm; law firm represented the former officer “[a]t least ostensibly” and the law firm “should have been alerted that [officer] believed or could reasonably believe that [the law] firm represented him personally”].)

At the time of Shehayed’s deposition in the *Brown* action, there was no basis to believe that his interests differed from those of IAR. Moreover, there is no indication that Shehayed’s alleged misappropriations had been discovered by IAR or that a decision had been made to terminate him. The issues raised by IAR’s subsequent complaint against Shehayed—the alleged misuse of corporate funds—are entirely distinct from the issues that were involved in the *Brown* action and that were the subject of discussion in connection with that case. While there may be a relationship between issues raised by

Shehayed's cross-complaint and those involved in the *Brown* action, that is of no significance if, as the trial court found, the Valla firm did not represent Shehayed in the *Brown* action and, as the trial court also found, Shehayed disclosed no personal confidential information to the attorneys.⁷

Thus, substantial evidence supports the trial court's findings and no basis appears to question its conclusion that there are no grounds to disqualify the Valla firm or any of its attorneys.

Disposition

The order denying the motion to disqualify counsel is affirmed. Costs on appeal are awarded to respondent.

⁷ Since there was no disclosure of Shehayed's confidential information, there is no need to consider whether, despite the absence of an attorney-client relationship, the relationship between Shehayed and the Valla firm was sufficient to compel disqualification. (See *Morrison Knudsen Corp. v. Hancock, Rothert & Bunshoft*, *supra*, 69 Cal.App.4th at p. 234.)

Pollak, Acting P.J.

We concur:

Siggins, J.

Jenkins, J.