

Undercover Investigators & The Disciplinary Rules

BY ROY SIMON

Suppose you represent a furniture manufacturer of high quality designer furniture in a suit alleging trademark infringement, Lanham Act violations, and unfair competition. You want to prove that the defendant, a furniture store, is engaging in “bait and switch” tactics by advertising your client’s brand and then palming off” furniture made by other manufacturers as equal in quality to your client’s products. Practically speaking, the only way to prove that the store is “palming off” is to catch sales clerks in the act. But how do you do that? May you ethically send undercover investigators to the defendant’s store posing as customers? May the investigators secretly record their conversations with the sales clerks? Will the secret recordings be admissible in evidence at trial?

In *Gidatex, S.R.L. v. Campaniello Imports, Ltd.*, 1999 WL 731609 (S.D.N.Y. Sept. 20, 1999), *WHERE THE FACTS PARALLEL OUR HYPOTHETICAL*, Judge Shira Scheindlin answered “yes” to all of these questions. But lawyers should tread carefully over this ground. The *Gidatex* decision seems narrowly direct to situations where (a) the only way to obtain the necessary evidence is by using undercover investigators, and (b) the public policy in deterring the defendant’s conduct is strong. Judge Scheindlin found these criteria satisfied in the particular factual and legal context of the *Gidatex* case, which involved trademark litigation. In other types of cases—for example, in typical personal injury cases, divorce matters, or routine breach of contract suits—the rationale for Judge Scheindlin’s holding might not apply.

Amusing Facts

The facts of the *Gidatex* case were amusing. *Gidatex* owned a federally registered trademark, “Saporiti Italia,” for a brand of furniture. The defendant, *Campaniello*, a well-known store on 57th Street in Manhattan that sells designer Italian furniture, had been a licensed sales agent of *Saporiti Italia* furniture for twenty years, until *Gidatex* terminated *Campaniello*’s agency in 1995. When *Campaniello* continued to use the *Saporiti Italia* trademark in its advertising after its termination, *Gidatex* sued *Campaniello* for Lanham Act violations, trademark infringement, and unfair competition.

At trial, *Gidatex* sought to prove that *Campaniello* engaged in “bait and switch” tactics by luring customers into its showrooms with signs and advertisements bearing the *Saporiti Italia* trademark, and then selling them furniture produced by other manufacturers. To prove the store was “palming-off” or “passing-off,” *Gidatex*’s counsel hired private investigators to pose as interior designers visiting *Campaniello*’s showrooms and warehouse. Before the complaint was filed, a private investigator visited the *Campaniello* store and secretly tape-recorded conversations with a sales clerk. When the investigator asked for *Saporiti Italia* furniture, the sales clerk informed him that the company “doesn’t exist anymore...it dissolved.” The conversation continued as follows:

Investigator: So that company doesn't exist anymore then?

Sales Clerk: No.

Investigator: Okay, So would I be getting [] the same quality?

Sales Clerk: Oh absolutely. Absolutely.

Investigator: Would I be getting the same, I mean, if I guess the same workmanship?

Sales Clerk: Oh absolutely.

Investigator: What happened, they changed or something?

Sales Clerk: Well, they had a fight. The two brothers I guess.

Investigator: Okay. So where would I be able to get the Saporiti then?

Sales Clerk: Well there is one brother. Saporiti Italia as it existed doesn't exist anymore.

Investigator: So, there is no place to get their furniture?

Sales Clerk: As far as I know.

After the complaint was filed, two investigators visited Campaniello's warehouse, where they observed two Campaniello delivery trucks and a fork-lift displaying the Saporiti Italia name. They also observed Saporiti Italia furniture on sale at the warehouse. They also visited the retail store again, where the sales clerk told them that the Saporiti Italia name "is no longer there...We have very few Saporiti items in the store...These two brother[s] that were working together, but they spit. And now the second brother is doing this other line. But it is still Saporiti ...The quality and everything is still the same.

Before trial, Campaniello moved for an order *in limine* precluding Gidatex from offering the testimony and reports of gidatex's investigators and the secretly-obtained tape recordings of their conversations with Campaniello's sales clerks. Campaniello claimed that Gidatex's investigators had used their "superior legal knowledge" to trick Campaniello's sales clerks into making statements to support Gidatex's claims under the Laham Act, and that Gidatex's use of undercover investigators violated DR 7-104(A) and DR 1-102(A)(4).

DR 7-104—The "No-Contact" Rule

The courts denied the motion *in limine*. Turning first to DR 7-104, the court said:

[T]he purpose of DR 7-104(A)(1) "is to preserve the proper functioning of the attorney-client relationship." Under the circumstances presented here, Gidatex's investigators did not intrude upon Campaniello's attorney-client privilege or attempt to use superior legal knowledge to take advantage of Campaniello's salespeople. Neither investigator was an attorney and neither attempted to interview party witnesses.

The investigators posed as interior designers—typical Campaniello customers...While it might have been annoying and time-consuming for Campaniello sales clerks to talk with phony customers who had no interest in buying furniture, the investigators did nothing more than observe and record the manner in which Campaniello employees conducted routine business...There was no risk that Campaniello's low-level employees would disclose, or were even aware of, any information protected by the attorney/client privilege.

DR 1-102(A)(4)—Preventing Dishonesty & Fraud

DR 1-102(A)(4) prohibits an attorney from engaging in conduct involving “dishonesty, fraud, deceit, or misrepresentation.” It is not a crime in New York for a person to secretly record his or her own conversations with another person, but is hiring investigators to pose as consumers a “misrepresentation” that violates DR 1-102(a)(4)? Some ethics committees have said that using undercover investigators is unethical, since such conduct involves deceit or misrepresentation. Nevertheless, the court refused to find a violation of DR 1-102(A)(4), calling the use of undercover investigators “an accepted investigative technique.”

The policy interests underlying the prohibition on misrepresentations by attorneys are (a) to protect parties from being tricked into making statements in the absence of their counsel and (b) to protect clients from misrepresentations by their own attorneys. The presence of investigators posing as interior decorators did not cause the sales clerks to make any statements they otherwise would not have made. There is no evidence to indicate that the sales clerks were tricked or duped by the investigators’ simple questions such as “is the quality the same?” or “so there is no place to get their furniture?”

Court Applies Three-Pronged Test

The court then focused on the policy interests expressed by trademark and unfair competition law. Referring to DR 1-102(A)(4) and DR 7-104(A)(1), the court stated:

These ethical rules should not govern situations where a party is legitimately investigating potential unfair business practices by use of an undercover investigator posing as a member of the general public engaging in ordinary business transactions with the target. To prevent this use of investigators might permit targets to freely engage in unfair business practices which are harmful to both trademark owners and consumers in general. Furthermore, excluding evidence obtained by such investigators would not promote the purpose of the rule, namely preservation of the attorney/client privilege.

[E]nforcement of the trademark laws to prevent consumer confusion is an important policy objective, and undercover investigators provide an effective enforcement mechanism for detecting and proving anti-competitive activity which might otherwise escape discovery or proof. It would be difficult, if not impossible, to prove a theory of “palming off” without the ability to record oral sales representations made to consumers.

The court next noted that even if DR 7-104(A)(1) and DR 1-102(A)(4) applied here, Campaniello had not established any violations. The court considered but rejected the three-part test used in the Second Circuit to determine whether lawyers have violated DR 7-104(A):

- (1) Did counsel communicate with a “party”?
- (2) If so, did counsel know that the party was represented by a lawyer in this matter?
- (3) Finally, did counsel “cause” the communication to occur?

Under this test, whether Gidatex’s lawyer violated DR 7-104 “turns on whether the sales clerks were parties, whether they were represented by counsel at the time of the communication, and whether [the lawyer] knew they were represented by counsel at that time.”

Applying this test, the court said that a corporate employee is “a party” if “(1) he/she had high-level managerial responsibility and was capable of binding the corporation; or (2) his/her acts or omission maybe be imputed to the corporation for the purposes of civil or criminal liability; or (3) his/her statements may constitute an admission by [the corporation].” In *Niesig v. Team I*, 76 N.Y.2d 363, 373 (1990), the New York Court of Appeals has defined “party” to include:

Corporate employees whose acts or omissions in the matter under inquiry are binding on the corporation (in effect, the corporation’s “alter-egos”) or imputed to the corporation for purposes of its liability, or employees implementing the advice of counsel. All other employees may be interviewed informally.

Were The Sales Clerks “Parties”? (1)

Campaniello’s sales clerks are “low-level employees with no management responsibilities whatsoever” and therefore would not generally be considered parties under DR 7-104(A)(1)—but Campaniello argues that Gidatex intends to offer the clerks’ statements regarding Saporiti Italia furniture as admissions that Campaniello itself is involved in a “palming-off” scheme. As a result, the sales clerks are “parties” for purposes of DR 7-104(A)(1).

Were Defendants “Represented” By Counsel? (2)

An organization “should be considered a party anytime it has specifically retained counsel to represent its interests regarding the subject of representation or has specifically referred the matter to house counsel.” To come within the protection of DR 7-104, the attorney’s retention “must have a nexus to a potential dispute.” Retaining an attorney for “general business purposes” is irrelevant unless there is “a specific connection to a potential lawsuit.” Often, a potential defendant does not retain counsel until a complaint is filed. Here, two of the four investigators’ visits occurred before the Complaint was filed and a third occurred before Gidatex served the Complaint on Campaniello. However:

[D]efendants argue that based on the adversarial history of these parties, Gidatex knew Campaniello was represented both before and after Gidatex filed its Complaint. Indeed, for over three years prior to the initiation of this trademark infringement suit, the parties were embroiled in two additional lawsuits on two different continents involving Campaniello’s claims against Gidatex for breach of contract, misrepresentation, unjust enrichment and fraud. During those litigations, Campaniello was represented by three different trial counsel, none from the law firm that represents Campaniello in the instant trademark action.

Gidatex stuck by its “technical argument” that Campaniello had not yet specifically retained counsel to represent it in this trademark infringement dispute. It is true that when the investigators visited Campaniello the first two times, Gidatex had not filed its trademark infringement case and Campaniello had not yet retained its current counsel. Nevertheless, “after years of related litigation between Gidatex and Campaniello, it is unrealistic to conclude that [plaintiff’s lawyer] did not know that Campaniello was represented by counsel.” Accordingly, the conduct of Gidatex’s counsel “technically satisfies the three-part test generally used to determine whether counsel has violated the disciplinary rules.”

Did Counsel “Cause” The Communication To Occur? (3)

This element was so obvious from the facts that the court did not separately address it. The plaintiff’s attorneys had already freely acknowledged that they hired the investigators.

In sum, the facts satisfied all three prongs of the Second Circuit test for a violation. Nevertheless, the court concluded as follows:

[Plaintiff’s attorney] did not violate the rules because his actions simply do not represent the type of conduct prohibited by the rules. The use of private investigators, posing as consumers and speaking to nominal parties who are not involved in any aspect of the litigation, does not constitute an end-run around the attorney/client privilege. Gidatex’s investigators did not interview the sales clerks or trick them into making statements they otherwise would not have made. Rather, the investigators merely recorded the normal business routine in the Campaniello showroom and warehouse.

Even if the rules had applied, and even if the plaintiff’s attorney had violated them, the court would not have suppressed the evidence. “[A] court is not obligated to exclude evidence even if it finds that counsel obtained the evidence by violating ethical rules...New York State courts will admit evidence procured by unethical or unlawful means in violation of the NYSBA Code of Professional Responsibility.” Here, “the remedy of preclusion would not serve the public interest or promote the goals of the disciplinary rules.” Accordingly, the court denied defendant’s motion to exclude the evidence obtained by the undercover investigators.

Our Advice – Exercise Caution

The Gidatex decision is a thoughtful, nuanced, careful analysis of the issues raised by an attorney’s use of undercover investigators wielding concealed recording equipment. Given its legal and factual context, the Gidatex decision is probably right. But attorneys should not take it as a general statement of the law regarding undercover investigators and secret tape recordings. Other authorities in New York and elsewhere have also addressed the subject of secret taping, and some of these authorities have labeled it unethical.

For example, in *N.Y. State 328 (1974)*, the ethics committee concluded that except in special situations, it is improper for a lawyer in private practice to record a conversation with another attorney or any other person without first advising the other party. Even if secret electronic recording of a conversation with one party’s consent is not illegal, the Committee said, it offends the traditional standards of fairness and candor that should characterize the practice of law. In *ABA 337 (1974)*, relying on DR 1-102(A)(4), the ABA’s ethics committee also concluded that no lawyer should record any conversation without the poor consent or knowledge of all parties to the conversation.

More to the point, in *ABA Informal Op. 1320 (1975)*, the ABA ethics committee opined that a lawyer would be acting unethically if the lawyer asked an investigator to tape his conversation with a sales clerk when the investigator knew that the recording was being made but the clerk did not. (In some jurisdictions, recording a conversation without the consent of both parties is a crime, not just an ethical violation.) In *N.Y. State Op. 515 (1979)*, the Committee said that a lawyer in private practice may under certain circumstances counsel a client concerning conversations to be recorded without notice or consent,

but the Committee stressed that the permissible circumstances were narrow. And in N.Y. City Op. 1995-10 (1995), the City Bar's ethics committee flatly stated that a lawyer "may not ethically record telephone or in-person conversations with opposing counsel without first advising him or her that the inquirer intends to record the conversations."

Of course, some ethics committees have concluded that secret taping, in itself, does not violate any ethical rules as long as the taping is lawful where it is undertaken and the lawyer makes no affirmative misrepresentations as to whether the conversation in question is being recorded. See N.Y. County 696 (1993); Arizona 90-2; Kentucky E-279 (1984); Oklahoma 307 (1994); Oregon 991-74; Utah 90 (1989). But a lawyer who follows those authorities—or the *Gidatex* holding--- is taking a risk. Unless all other avenues of gathering the information are closed off, a lawyer should avoid undercover investigators and secret taping.

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