
WHO IS THE CORPORATION'S LAWYER?

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INTRODUCTION

Many attorneys employed by large law firms are frustrated by their need to produce high-quality and high volume work product under short deadlines. Their situations are complicated by the need for them to please multiple masters. These demands engender complex ethical issues, particularly where a formal system to identify and resolve moral dilemmas is absent or underutilized. Even if attorneys examine a jurisdiction's rules governing their professional conduct, they are likely to find that such rules are not only ambiguous, but appear to be written primarily with a solo practitioner or small law firm in mind, working almost exclusively on legal matters that never involve the application of the law of more than one state or country.

In many large firms, the relationships that associates and non-equity holding lawyers have with one another and their law firms have many of the characteristics of corporate employees. Today, fewer attorneys function as professionals who exercise their own judgment on substantive matters. Furthermore, lawyers at large law firms often lack an identity of interests with those of their employers, colleagues, and clients.

Typically, a corporation's general counsel will select one or more law firms to handle its outside legal work. The arrangements between the corporate clients and their law firms are typically embodied in retainer agreements, and not with individual attorneys at the firms. This occurs even though corporate general counsels may want specific attorneys at a law firm to handle or supervise their corporation's matters. Unless otherwise agreed, law firms typically have discretion in staffing assignments for their clients. It is not unusual that lawyers who work on a particular client's matter will have only a minimal knowledge of the corporate client's goals, and may never have direct contact

with corporate client's personnel. Indeed some corporations are trying new approaches in their dealings with outside counsel.¹

To complicate the situation, today's lawyers are increasingly expected to take into account their obligations with respect to their clients (i.e. the legal entity and its owners) as well as other stakeholders (including the public). Regulators, legislators, reporters and the public are increasingly questioning certain fundamental assumptions underlying the lawyers' professional conduct. This dynamic situation has and will continue to generate novel legal and ethical issues for lawyers serving corporate clients.

This article examines whether the American Bar Association's Model Rules of Professional Conduct (the "Model Rules") are providing lawyers at large law firms sufficient guidance concerning how to uphold their ethical obligations, while at the same time advancing their clients' and protecting their employers' interests.² On first impression, it seems that some complex ethical issues arise because ultimately the attorney-client relationship is a product of personal interactions. The interests of attorneys who directly deal with corporate clients' personnel may differ from that of their law firms. Similarly, under U.S. law, a corporation is a legal person, the interests of which are not always the same as those of corporate management. Furthermore, the fact that corporate management pays for legal services with someone else's money (i.e., the legal entity and ultimately the owners) produces a different dynamic than when an individual is the client.

This article is organized into five sections. The first section examines the subordinate attorney's obligations as set forth in the Model Rules. Most states rely on the Model Rules as a starting point for developing their own rules regulating the practice of law. This means that while the rules in all states are not the same, they are similar. The second section identifies certain practical dilemmas for lawyers assisting corporate clients to obtain their business objectives. The third section analyzes management strategies to minimize the potential consequences of a difference between the interests of the client and its law firm (outside counsel). The fourth section discusses certain ethical dilemmas

¹ See Ron Peppe and David G. Briscoe, "Strategize This: Rethinking Outside Counsel Use," ACC Docket, Vol. 22, No. 9, at 24-44, (October 2004) (discussing management techniques for more cost-effective use of outside counsel); see also James R. Buckley, "Welcome to Lawyerland: Why Even Brilliant Outside Counsel Cost Too Much," ACC Docket, Vol. 23, No. 1, at 22-32 (January 2005) (an inside counsel of a major corporation's analysis of how a law firm's organization and culture drives up the cost of legal services).

² MODEL RULES OF PROF'L CONDUCT R. 1.0 (2004). Terminology does not explicitly define "lawyer" – the meaning of which can be gleaned from the Model Rule's Preamble – A Lawyer's Responsibilities and other provisions. In contrast, a "[f]irm" or "law firm" is defined as "a lawyer or lawyers in a law partnership, professional corporation, sole proprietorship or other association authorized to practice law; or lawyers employed in a legal services organization or the legal department of a corporation or other organization."

that can arise under the Model Rules and also identifies areas where state legislatures and the courts might act to reduce the gap between professional ideals and practical realities. The last section examines different approaches for establishing a more user-friendly foundation for the ethical conduct of lawyers servicing corporate clients.

I. LAWYERS AND CORPORATE GOVERNANCE

The American Bar Association (ABA) Task Force (the "Task Force") on Corporate Responsibility Report (the "Report") concluded that lawyers play an important role in the proper governance of public corporations.³ The ABA House of Delegates approved the bulk of the Report's analysis and recommendation, after making certain minor revisions.⁴ The final version of the Report observes:

Lawyers are and should be important participants in corporate governance and important contributors to corporate responsibility. Lawyers employed by the corporation and outside lawyers retained by the corporation often serve as key advisers to senior management and usually participate in the negotiation, structuring and documentation of the corporation's significant business transactions. Additionally, lawyers often serve as counselors to the board to assist it in performing its oversight function. In such roles, lawyers obviously do and should play a critical role in helping the corporation recognize, understand and comply with applicable laws and regulations, as well as to identify and evaluate business risks associated with legal issues. The Task Force believes that a prudent corporate governance program should call upon lawyers – notably the corporation's general counsel – to assist in the design and maintenance of the corporation's procedures for promoting legal compliance.

This conception of the lawyer as a promoter of corporate compliance with law emanates from the basic values of the legal

³ The Task Force issued a preliminary version of this report two weeks before Congress enacted the Sarbanes-Oxley Act. *See generally*, Chi Soo Kim & Elizabeth Laffitte, *The Potential Effects of SEC Regulation of Attorney Conduct Under the Sarbanes-Oxley Act [of 2002]*, 16 GEO. J. LEGAL ETHICS 707 (2003) (discussing whether ethical rules for lawyers should be federalized and noting that in accordance with the Act's § 307, the Securities and Exchange Commission promulgated rules establishing "minimum standards of professional conduct for attorneys" who practice before the SEC).

⁴ *See* ABA Website, *ABA House of Delegates Adopts Policies Recommended By Task Force on Corporate Responsibility*, available at <http://www.abanet.org/buslaw/corporateresponsibility/> (last accessed Sept. 2, 2004). The ABA House of Delegates issued its own document approving the Report, but noted certain positions it did not endorse.

profession. It follows naturally from the ABA's goal "to increase public understanding of and respect for the law, the legal process, and the role of the legal profession." It is also in keeping with the [Model Rules], which emphasize the lawyer's responsibility "[a]s advisors [to] provide[] a client with an informed understanding of the client's legal rights and obligations and explain their practical implications."⁵

The Report states that the Model Rules⁶ support effective corporate governance in a variety of ways, such as by requiring lawyers to:

- (i) be competent;⁷
- (ii) respect a client's right to determine corporate objectives;⁸
- (iii) assist the manner by which the client pursues its objective, (presumably in a lawful manner);⁹
- (iv) preserve client confidences;¹⁰ and
- (v) avoid conflicts of interest.¹¹

Furthermore, the Report properly notes that:

lawyers for the public corporation must bear in mind that their responsibility is to the corporation, and not to the corporate directors, officers or other agents with whom they necessarily communicate in representing the corporation. This is the bed-

⁵ *Report of the American Bar Association Task Force on Corporate Responsibility*, at 20-21 (2003), available at http://www.abanet.org/buslaw/corporateresponsibility/final_report.pdf (last accessed September 21, 2004). The Task Force's Preliminary Report was published at 58 BUS. LAW. 189 (2002).

⁶ In 1908, the American Bar Association issued the Canons of Ethics. In 1969, the ABA developed the Model Code of Professional Responsibility to replace the Canons. Then in 1983, the ABA came out with the Model Rules of Professional Conduct, which more clearly set out standards for attorney conduct. The ABA continues to amend this last document in order to address issues as they arise. In addition, the ABA issues non-binding ethics opinions. Courts, bar counsel, and other rule-establishing bodies are often influenced by these opinions.

⁷ MODEL RULES OF PROF'L CONDUCT R 1.1 & 1.3.

⁸ MODEL RULES OF PROF'L CONDUCT R 1.2.

⁹ MODEL RULES OF PROF'L CONDUCT R 1.4.2(a)(s).

¹⁰ MODEL RULES OF PROF'L CONDUCT R 1.6.

¹¹ MODEL RULES OF PROF'L CONDUCT R 1.6 & 1.7; *see also* Report, *supra* note 6, at 21-22.

rock principle recognized in Rule 1.13(a) of the Model Rules. Outside lawyers retained by the corporation and lawyers employed by the corporation both must exercise professional judgment in the interests of the corporate client, independent of the personal interests of the corporation's officers and employees.¹²

The Task Force took the position that lawyers for a corporation, both in-house and outside counsel, were not "gatekeepers;" i.e. agents of regulatory or law enforcement bodies. This role is similar, but not identical to that of accounting firms performing audits for publicly traded corporations.¹³ Nevertheless, in addition to having the duty to protect their clients' interests, lawyers are obliged to exercise independent judgment (while not facilitating their clients' and their agents' unlawful acts).

In recent days, however, many legislators and regulators have demonstrated that they did not fully share this longstanding view.¹⁴ The inviolable relationship between lawyer and client, which is based in part on principles of fiduciary duty and the confidentiality of attorney-client communications, has apparently lost its sanctity. Some legislators and regulators have adopted the view that under certain circumstances lawyers indeed should act as gatekeepers. A lawyer fulfilling a gatekeeper function in essence fulfills a governmental regulatory or law enforcement role, the implication of which is that lawyers also have obligations to the public's interest.¹⁵

¹² Report, *supra* note 6, at 23.

¹³ Report, *supra* note 6, at 22-24; see Richard W. Painter, *Convergence and Competition in Rules Governing Lawyers and Auditors*, 29 IOWA J. CORP. L. 397, 401-411 (2004) (differing evaluations of risk depend on information asymmetry and cognitive bias); see also David A. Skeel, *The Anatomy of Corporate Law: A Comparative and Functional Approach*. By Reinier Kraakman, et al., New York, Oxford University Press, 2004, 113 YALE L.J. 1519 (2004) (discussing in part that gatekeeper regulation can improve but not solve the gatekeeper-agency problem. The existence of significant financial rewards makes the existence of rules of limited value where corporate management is inclined to run risks and the punishments for "white collar" crime not particularly severe. Furthermore, gatekeepers within law firms are subject to the same temptations as corporate management. Nonetheless, law, rules and regulations, if controls are well crafted and rigorously enforced and where whistle blowing is encouraged, may have a deterrent effect).

¹⁴ Jill E. Fisch & Kenneth M. Rosen, *Is There a Role for Lawyers in Preventing Future Enrons?* 48 VILL. L. REV. 1097, 1097 (2003) (contending requiring lawyers to act as corporate gatekeepers is not a panacea for corporate governance problems); Thomas D. Morgan, *Sarbanes-Oxley: A Complication, Not a Contribution, in the Effort to Improve Corporate Lawyers' Professional Conduct*, 17 GEO. J. LEGAL ETHICS 1 (contending that Sarbanes-Oxley in isolation confuses rather than clarifies what is required of lawyers acting as "gatekeepers"); but see John C. Coffee, Jr., *Gatekeeper Failure and Reform: the Challenge of Fashioning Relevant Reforms*, 84 B.U. L. REV. 301 (2004) (rejecting the conventional wisdom by advancing the view that imposing gatekeeper obligations on attorneys will increase their leverage over their clients).

¹⁵ *Id.*

Some critics of this development contend that making lawyers gatekeepers burdens them with incompatible conflicts of interests, which clash with lawyers' numerous duties to their clients and jeopardizes the clients' ability to communicate honestly with their lawyers, fearing certain disclosures made to their lawyers will not enjoy confidentiality.¹⁶ In addition, there is the practical concern that many lawyers lack the substantive knowledge to perform adequately gatekeeper tasks, are willing to put the government's (or public's) interest ahead of their own, and what punishments are appropriate if a lawyer knowingly puts his clients' interests first.¹⁷

Organized groups representing the interest of segments of the legal community have been largely successful in preventing Congress from imposing gatekeeping responsibilities on lawyers.¹⁸ There have been two notable exceptions: (i) the U.S.A. Patriot Act of 2001 (the "Patriot Act")¹⁹ and (ii) the Sarbanes-Oxley Act of 2002 (popularly known as "SOX"),²⁰ both of which were adopted in response to national crises, the former law responding to the trauma of the terrorist attacks on 9/11 and the latter at a time when public confidence in "Corporate America" and the stock market had precipitously dropped following a waive of major corporate and financial scandals. In both instances, Congress "deputized" lawyers to serve as regulatory gatekeepers.²¹ Not surprisingly,

¹⁶ MODEL RULES OF PROF'L CONDUCT R 1.6 – Confidentiality of Information & R 1.7 – Conflicts of Interest, Current Clients (along with their respective comments); *see generally* RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 16 (2000) (A Summary of the Duties under the Client-Lawyer Relationship).

¹⁷ Fisch & Rosen, *supra* note 14.

¹⁸ *See* WILLIAM N. ESKRIDGE, JR., *ET AL*, LEGISLATION AND STATUTORY INTERPRETATION 67-114 (2000) (Professors William Eskridge, Phillip Frickey and Elizabeth Garrett provide an examination of the ability of organized groups to influence the legislative process and achieve their objectives).

¹⁹ The full name of the Patriot Act is *Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001*, available at <http://www.epic.org/privacy/terrorism/hr3162.html> (last accessed March 16, 2005). Congress adopted the USA Patriot Act with little debate and virtually no detailed examination of the Act's substantive provisions, including those dealing with terror financing and money laundering. Immediately after 9/11, few if any legislators were willing to entertain the political risk of questioning the additional powers granted to the federal government to combat terrorism. For a skeptical analysis of the Patriot Act's anti-terrorist financing provisions, *see* Ethan S. Burger, Why Following the Money Won't Stop Terrorist Financing, Bank Security News, Vol. 2, No. 8, October 27, 2004, at 10-11.

²⁰ The full name of the Sarbanes-Oxley Act is *Act To Protect Investors by Improving the Accuracy and Reliability of Corporate Disclosures Made Pursuant to the Securities Laws, and for Other Purposes*, available at <http://news.findlaw.com/hdocs/docs/gwbush/sarbanesoxley072302.pdf> (last accessed June 14, 2004).

²¹ *See* Edward J. Krauland and Benjamin Coats, *International Regulation of the Legal Profession: An Impending Possibility?* INTERNATIONAL LAW NEWS, Spring 2004, at 6-8, and Kevin L.

various organizations of lawyers have sought to reduce the possibility that the Patriot Act²² and SOX would interfere with their existing obligations to their clients.²³

Many of those lobbying on behalf of the legal community sought to minimize a lawyer's obligation to society. Such efforts continued after the

Shepard, *USA Patriot Act and the Gatekeeper Initiative: Surprising Implications for Transactional Lawyers*, A.B.A. PROBATE & PROPERTY, Oct. 1, 2002, available at <http://www.abanet.org/rppt/publications/magazine/2002/so/shepherd.html> (accessed Feb. 11, 2005).

²² The United States is a member of the Financial Activities Task Force ("FATF"). After the 9/11 terrorist attacks, FATF adopted 40 "Special Recommendations" to combat terrorist financing. This document would appear to call for lawyers to conduct client due diligence and perform record-keeping activities in the same manner as financial institutions. Special Recommendation 12(d) provides:

Lawyers, notaries, other independent legal professionals and accountants when they prepare for or carry out transactions for their client concerning the following activities:

- buying and selling of real estate;
- managing of client money, securities or other assets;
- management of bank, savings or securities accounts;
- organi[z]ation of contributions for the creation, operation or management of companies; [and]
- creation, operation or management of legal persons or arrangements, and buying and selling of business entities.

The 40 Recommendations of the Financial Activity Task Force on Money Laundering, June 20, 2003, at 7, available at <http://www.fsa.gov/fiu/fiue/fme001a.pdf> (accessed Feb. 11, 2005).

There has been considerable concern within the legal community that lawyers were being made subject to rules requiring them to file currency transaction reports (CTRs) (reporting transactions above \$10,000) and suspicious activities reports (SUAs) as required under the Bank Secrecy Act, as amended by the Patriot Act, which now provides an expanded list of entities falling within the definition of "financial institutions." To date there have been no special requirements established for lawyers. Nonetheless, in April 2003, the U.S. Financial Crimes Enforcement Unit (the U.S. financial intelligence entity) gave notice of a proposed rulemaking concerning persons involved with real estate transactions. Financial Crimes Enforcement: Anti-Money Laundering Program Requirements for Persons Involved in Real Estate Closings and Settlements, 68 Fed. Reg. 17,569 (April 10, 2003) (to be codified at 31 C.F.R. pt. 103). To date, there have been no final regulations issued in this area, though the ABA is closely monitoring developments in this area. Under certain circumstances, various provisions of the Patriot Act's anti-money laundering provisions and their implement regulations might cover individuals who are lawyers.

²³ Bernard S. Carrey, *Enron—Where Were the Lawyers?* 27 VT. L. REV. 871 (2003) and (Symposium), *Developments in the Law: Corporations and Society*, 117 HARV. L. REV. 2169, 2227 (2004) (both items largely discussing the implication of SOX's requirements, the need for security law reform, the confidentiality of attorney-client communications and the Model Rules).

adoption of the aforementioned legislation, largely focusing on the agency rule-making process. At present, these two Acts remain notable exceptions to the principle that attorneys are not gatekeepers for the public. The future impact on the practice of law of assigning gatekeeper roles is difficult to predict. Traditionally, lawyers were prohibited from assisting clients in the commission of a crime or other wrongdoing, now they are being asked to report arguably improper conduct to the authorities. This development may have a chilling effect on attorney-client communications.

Similarly, it is not clear that lawyers have adequately fulfilled their gatekeeper roles with respect to the owners of their corporate clients. Notably, the Task Force observed that the existing Model Rules do not deal with the reality of how lawyers provide services to corporate clients:

This Report continues the practice traditionally used in the Model Rules of speaking about responsibilities of individual lawyers. However, in many cases involving the representation of publicly held corporations, the corporate client is advised by a law firm. The interplay of lawyer obligations to the corporation and lawyer obligations to each other in the context of law firm practice are generally addressed in Model Rules 5.1 and 5.2. A direct, detailed analysis of the responsibilities of a law firm and the lawyers within the firm and the procedures that would facilitate discharge of their responsibilities would be a useful addition to the literature on professional responsibilities, and the Task Force recommends that an appropriate committee of the ABA undertake such an analysis.²⁴

While there are some formal (and informal) efforts underway in this area, the ABA has not completed its work in this area.²⁵

²⁴ Report, *supra* note 6, at 35, n. 66.

²⁵ Nicole Kroetsch & Samantha Petrich, *Task Force on Corporate Responsibility: Should the American Bar Association Adopt New Ethics Rules?* 16 GEO. J. LEGAL ETHICS 727 (2003) (noting that the Task Force's Report, had the objective of creating a guide for corporate lawyers who are confronted with misconduct by corporate officers and insiders, but did not complete the task. The authors provide an assessment and offer recommendations for amending the Model Rules since, as the Task Force admits, the "Model Rules currently encourage lawyers to go beyond legally required minimum standards and consider the moral and ethical considerations of situations and decisions."); see Rachel Reiland, *The Duty to Supervise and Vicarious Liability: Why Law Firms, Supervising Attorneys and Associates Might Want to Take [a] Closer Look at Model Rules 5.1, 5.2 and 5.3*, 14 GEO. J. LEGAL ETHICS 1151 (2001) (arguing that the existing rules in the area are inadequate and calling for a re-examination of the area); see also Ethan S. Burger, *The Use of Limited Liability Entities for the Practice of Law: Have Lawyers Been Lulled into a False Sense of Security?* 40 TEX. J. BUS. L. 175 (2004) (contending that often liability described as "vicarious" can also be properly classified as "direct.").

The Task Force proposed 12 Recommendations for improving corporate governance; each of which largely concern changes to the operation of a corporation's board of directors, management, the conduct of lawyers (both in-house and outside counsel) as well as the role other institutions (the Securities and Exchange Commission (SEC), courts, state attorney disciplinary authorities, etc.) to improve the effectiveness of corporate controls and compliance with relevant requirements.²⁶

The Report concludes with specific recommendations to modify the Model Rules, which the ABA House of Delegates largely accepted in their entirety.²⁷ The Task Force subsequently prepared a second report in conjunction with the resolution being considered at the time by the ABA House of Delegates (hereinafter the "Report for ABA House of Delegates").²⁸ On August 12, 2003, after considerable debate, the ABA House of Delegates accepted the latter version of the Task Force's recommendations concerning the responsibility of lawyers representing organizational clients. Generally, the House of Delegates thought the amendments to be necessary to make the Model Rules consistent with the requirement imposed by SOX to "report up the ladder," pursuant to § 307.²⁹

²⁶ Report, *supra* note 6, at 12.

²⁷ Report, at 77-89 available at http://www.abanet.org/buslaw/corporateresponsibility/final_report.pdf (last accessed February 28, 2005).

²⁸ The Report for the ABA House of Delegates is available at http://www.abanet.org/buslaw/corporateresponsibility/final_report.pdf (last accessed February 28, 2005). It consists of 17 pages.

²⁹ There was considerable opposition by some lawyers to the amendments to Model Rule 1.13. The opponents advanced various arguments against the proposed changes such as the claim that the relationship between corporate wrongdoing and the role of the lawyer was not well established, and that the new rules could have unforeseen consequences in their impact on attorney-client relations. Furthermore, since the Model Rules applied to all organizations, not just publicly owned companies, too much power and responsibility was being placed in the hands of lawyers. See *ABA Amends Ethics Rules on Confidentiality, Corporate Clients, to Allow More Disclosures*, LAWS. MAN. PROF. CONDUCT NEWSL (ABA/BNA) Aug. 13, 2003, at 467. The states have not uniformly accepted the changes to the Model Rules. For example, while Louisiana amended its own ethical rules along the lines proposed by the ABA, Pennsylvania did not follow the ABA's lead. See *Louisiana Adopts Rule Changes That Mostly Conform to ABA Models*, LAWS. MAN. PROF. CONDUCT NEWSL (ABA/BNA) Feb. 11, 2004, at 70; and *Pennsylvania Rule Amendments Contain Numerous Departures from ABA Model*, LAWS. MAN. PROF. CONDUCT. NEWSL (ABA/BNA) Sept. 8, 2004, at 8.

To make Model Rule 1.6 consistent with existing law and policy objectives, the ABA House of Delegates approved the addition of two new sub-paragraphs to paragraph (b), so the rule now reads:

Model Rule 1.6, CONFIDENTIALITY OF INFORMATION, [as amended August 11, 2003, American Bar Association House of Delegates, Denver, Colorado, Report No. 119A]:

(a) A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation or the disclosure is permitted by paragraph (b).

(b) A lawyer may reveal information relating to the representation of a client to the extent the lawyer reasonably believes necessary:

(1) to prevent reasonably certain death or substantial bodily harm;

(2) to prevent the client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's services;

(3) to prevent, mitigate or rectify substantial injury to the financial interests or property of another that is reasonably certain to result or has resulted from the client's commission of a crime or fraud in furtherance of which the client has used the lawyer's services;

(4) to secure legal advice about the lawyer's compliance with these Rules;

(5) to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client; or

(6) to comply with other law or a court order.

The Commentary for Rule 1.6, was also changed to be consistent with the revised paragraph (b).

Similarly, the ABA House of Delegates approved major changes to Model Rule 1.13. These changes are largely found in paragraphs (b), (c) and (d):

Model Rule 1.13 – ORGANIZATION AS CLIENT [as amended August 12, 2003, American Bar Association House of Delegates, Denver, Colorado, Report No. 119B].

(a) A lawyer employed or retained by an organization represents the organization acting through its duly authorized constituents.

(b) If a lawyer for an organization knows that an officer, employee or other person associated with the organization is engaged in action, intends to act or refuses to act in a matter related to the representation that is a violation of a legal obligation to the organization, or a violation of law that reasonably might be imputed to the organization, and that is likely to result in substantial injury to the organization, then the lawyer shall proceed as is reasonably necessary in the best interest of the organization. Unless the lawyer reasonably believes that it is not necessary in the best interest of the organization to do so, the lawyer shall refer the matter to higher authority in the organization, including, if warranted by the circumstances, to the highest authority that can act on behalf of the organization as determined by applicable law.

(c) Except as provided in paragraph (d), if

(1) despite the lawyer's efforts in accordance with paragraph (b) the highest authority that can act on behalf of the organization insists upon or fails to ad-

The Report for the ABA House of Delegates contained some important observations concerning the relationship between outside counsel and corporate clients. The Report noted that in addition to boards of directors, public accounting firms, and shareholders, private sector participants, “[l]egal counsel who provide advice to public corporations, through their directors, officers and employees, on compliance with the corporation’s legal obligations” play a vital role in effective corporate governance.³⁰ Unfortunately, some lawyers do not ade-

dress in a timely and appropriate manner an action or a refusal to act, that is clearly a violation of law, and

(2) the lawyer reasonably believes that the violation is reasonably certain to result in substantial injury to the organization, then the lawyer may reveal information relating to the representation whether or not Rule 1.6 permits such disclosure, but only if and to the extent the lawyer reasonably believes necessary to prevent substantial injury to the organization.

(d) Paragraph (c) shall not apply with respect to information relating to a lawyer's representation of an organization to investigate an alleged violation of law, or to defend the organization or an officer, employee or other constituent associated with the organization against a claim arising out of an alleged violation of law.

(e) A lawyer who reasonably believes that he or she has been discharged because of the lawyer's actions taken pursuant to paragraphs (b) or (c), or who withdraws under circumstances that require or permit the lawyer to take action under either of those paragraphs, shall proceed as the lawyer reasonably believes necessary to assure that the organization's highest authority is informed of the lawyer's discharge or withdrawal.

(f) In dealing with an organization's directors, officers, employees, members, shareholders or other constituents, a lawyer shall explain the identity of the client when the lawyer knows or reasonably should know that the organization's interests are adverse to those of the constituents with whom the lawyer is dealing.

(g) A lawyer representing an organization may also represent any of its directors, officers, employees, members, shareholders or other constituents, subject to the provisions of Rule 1.7. If the organization's consent to the dual representation is required by Rule 1.7, the consent shall be given by an appropriate official of the organization other than the individual who is to be represented, or by the shareholders.

Not only was Model Rule 1.13, changed, the comments to the Rule were changed to reflect the enhanced responsibilities lawyers owed clients, which were organizations. Nonetheless, the Task Force indicated that the revised Model Rule 1.13 should not be viewed as “a guide to best legal practices.” See Proposed Amendments to Model Rules and Other Materials on the ABA Presidential Task Force on Corporate Responsibility’s Website, at <http://www.abanet.org/buslaw/corporateresponsibility/home.html> (last accessed Sept. 2, 2003).

³⁰ Task Force Report submitted by the ABA House of Delegates in support of the Governance Policy Resolution, at 7, (August 2003), available at

<http://www.abanet.org/leadership/2003/journal/119c.pdf> (last accessed November 11, 2004).

quately protect their corporate clients' interests, perhaps because their relationships are with individuals (each with their own interests and perceptions, rather than their organizational client – a fictional person). The Report candidly states that “[t]he competition to acquire and keep client business, or the desire to advance within the corporate executive structure, may induce lawyers to please the corporate officials with whom they deal rather than to focus on the long-term interests of their client, the corporation.”³¹

In a resolution, the ABA House of Delegates approved the 12 recommendations (or practices) originally proposed by the Task Force. The recommendations primarily covered two areas: “(1) the role of lawyers in facilitating the flow of information and analysis concerning legal compliance issues within the organizations they represent (including public corporations); and (2) the limitations on the ability of the lawyer to disclose to third parties information concerning criminal or fraudulent conduct by the client.”³²

As noted above, a majority of the ABA House of Delegates' recommendations proposed practices concerned the behavior of corporate personnel and corporate structure. The most important recommendations concerning the role of lawyers were:

- A lawyer representing a public corporation shall serve the interest of the entity, independent of any personal interest of any particular director, officer, employee or shareholder. (Recommendation 5).³³

- Public corporations should adopt practices in which . . . (c) [a]ll reporting relationships of internal and outside counsel for a public corporation establish at the outset a direct line of communication with general counsel through which these lawyers are to inform the general counsel of material potential or ongoing violations of law by, and breaches of fiduciary duty to, the corporation (Recommendation 7(c)).³⁴

- Engagement of counsel by the board of directors, or by a committee of the board, for special investigations or independent advice should be structured to assure independence and direct reporting to the board of directors or the committee (Recommendation 9).³⁵

³¹ *Id.*

³² *See supra* note 6, at 34.

³³ *Id.*

³⁴ *Id.*

³⁵ *Id.*

- The courts, law schools and lawyer professional responsibility organizations such as the ABA should promote awareness of, and adherence to, the professional responsibilities of lawyers in their representation of public corporations (Recommendation 11).³⁶

- Law firms and law departments should adopt procedures to facilitate and promote compliance with rules of professional conduct governing the representation of public corporations (Recommendation 12).³⁷

It is exceedingly difficult, if not impossible, to predict, with any confidence, the impact of these recommendations on the conduct of lawyers if they were adopted and put into practice. To evaluate whether the relevant actors are implementing the recommendations would require a major research effort involving extensive fieldwork. Merely sending out surveys, which were not subsequently verified, would be insufficient and likely to produce misleading results. One would have to confirm not merely whether written policies have been adopted, but whether they were in fact being observed, and if so to what degree.

It may be significant that the ABA House of Delegates' resolution in the last point used the permissive word "should," rather than the mandatory command "shall." Although there may be a number of explanations for this, it is noteworthy that the Delegates felt more comfortable suggesting mandatory practices of corporate governances for corporations in lieu of establishing requirements concerning the management of law firms. It at least reflects the ABA's reluctance to issue standards governing its members and their law firms.

II. ISSUES THAT MAY ARISE WHEN THE CLIENT IS A CORPORATION

The Model Rules do not overlook the situation where the client is an organization; they merely treat the topic in a cursory manner.³⁸ The Model Rules

³⁶ *Id.*

³⁷ *See supra* note 27, at 31-32.

³⁸ Model Rule 1.13 and the accompanying comment are rather lengthy, which is indicative of the complexity of providing legal services to organizations. This Rule provides:

(a) A lawyer employed or retained by an organization represents the organization acting through its duly authorized constituents.

(b) If a lawyer for an organization knows that an officer, employee or other person associated with the organization is engaged in [an] action, intends to act or refuse to act in a manner related to the representation that is a violation of a legal obligation to the organization, or a violation of law that reasonably might be imputed to the organization, then the lawyer shall proceed as is reasonably necessary in the best interest of the organization. Unless the lawyer reasonably believes that it is not necessary in the best interest of the organiza-

are most relevant to the litigation context. Lawyers working for corporate clients, however, are often structuring transactions, looking at complex securities issues, examining difficult tax questions, and resolving regulatory matters.³⁹

tion to do so, the lawyer shall refer the matter to higher authority in the organization, including, if warranted by the circumstances, to the highest authority that can act on behalf of the organization as determined by applicable law.

(c) Except as provided in paragraph (d), if

(1) despite the lawyer's efforts in accordance with paragraph (b) the highest authority that can act on behalf of the organization insists or fails to address in a timely and appropriate manner an action or a refusal to act, this is clearly a violation of law, and

(2) the lawyer reasonably believes that the violation is reasonable certain to result in substantial injury to the organization, then the lawyer may reveal information relating to the representation whether or not Rule 1.6 [Confidentiality of Information] permits such disclosure, but only if and to the extent the lawyer reasonably believes necessary to prevent substantial injury to the organization.

(d) Paragraph (c) shall not apply with respect to information relating to a lawyer's representation of an organization to investigate an alleged violation of law, or to defend the organization or an officer, employee, or other constituent associated with the organization against a claim arising out of an alleged violation of law.

(e) A lawyer who reasonably believes that he or she has been discharged because of the lawyer's actions taken pursuant to paragraphs (b) or (c) or who withdraws under circumstances that require or permit the lawyer to take action under either of those paragraphs, shall proceed as the lawyer reasonably believes necessary to assure that the organizations highest authority is informed of the lawyer's discharge or withdrawal.

(f) In dealing with an organization's directors, officers, employees, members, shareholders or other constituents, a lawyer shall explain the identity of the client when the lawyer knows or reasonably should know that the organization's interests are adverse to those of the constituents with whom the lawyer is dealing.

(g) A lawyer representing an organization may also represent any of its directors, officers, employees, members, shareholders or other constituents, subject to the provisions of Rule 1.7 [Conflict of Interest: Current Clients]. If the organization's consent to the dual representation is required by Rule 1.7, the consent shall be given by an appropriate official of the organization other than the individual who is to be represented or by the shareholders.

MODEL RULES OF PROF'L CONDUCT R. 1.13 (2002).As is often the case, a particular jurisdiction does not adopt a particular Model Rule in its entirety. *See e.g.* D.C. Rules of Prof'l Conduct, R. 1.13, *available at* http://www.dcbbar.org/for_lawyers/ethics/legal_ethics/rules_of_professional_conduct/Rule_one/rule01_13.cfm.

³⁹ According to Deborah Rhode and Geoffrey Hazard, Jr., most legal practice today occurs in transactional settings. Deborah L. Rhode and Geoffrey C. Hazard, Jr., Professional Responsibility

Since the Model Rules can't possibly address all the ethical issues arising from a wide range of legal matters, it often relies on vague language and makes frequent use of the words "reasonable" and "reasonably." These makes the Model Rules understandably nuanced and frequently open to interpretation. Consequently, the Model Rules (and their state equivalents) are of less practical value than might be the case since the authors seemed to have drafted them as if the client is generally an individual or closely-held company, where the management and owners of the entity have similar, if not identical, interests.⁴⁰ In any event, the Model Rules relating to this area are frequently ambiguous and often of little relevance to the realities of law firm corporate practice in the transactional area.

The Restatement examines the duties of lawyers who represent organizational clients, but only has contact with the organization's constituents (e.g., management or the board of directors). The text of the Restatement is compatible with the requirements flowing from the Model Rules. It provides:

(1) When a lawyer is employed or retained to represent an organization:

(a) The lawyer represents the interests of the organization as defined by its responsible agents **acting pursuant to the organization's decision-making procedures; and**

(b) Subject to Subsection (2), the lawyer must follow instructions in the representation, as stated in § 21.2 [dealing with the allocation of authority between a client and a lawyer], given by persons authorized so to act on behalf of the organization.

(2) If a lawyer presenting an organization knows of circumstances indicating that a constituent of the organization has engaged in action or intends to act in a way that violates a legal obligation to the organization that will likely cause substantial injury to it, or that reasonably can be foreseen to be imputable

and Regulation (2002) at 79.

⁴⁰ The ABA takes the view that a lawyer's non-compliance with the Model Rules does not constitute malpractice *per se*. ABA Model Rules of Prof'l Conduct, Preamble and Scope; *see also* Michelle Craven and Michael Pitman, *To the Best of One's Ability: A Guide to Effective Lawyering*, 14 GEO. J. LEGAL ETHICS 983, 996 (2001). Nonetheless, such non-compliance can serve as evidence of legal malpractice. Unlike the ABA Model Rules, The Restatement of the Law (THIRD) of the Law Governing Lawyers deals with the topic of the liability of lawyers for their professional malpractice. (RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS, Forward (2001) (emphasis added).

to . . . it, the lawyer must proceed in what the lawyer reasonably believes to be the best interests of the organization.

(3) In the circumstances described in Subsection (2), the lawyer may, in circumstances warranting such steps, ask the constituent to reconsider the matter, recommend that a second legal opinion be sought, and seek review by appropriate supervisory authority within the organization, including referring the matter to the highest authority that can act on behalf of the organization (emphasis added).⁴¹

While the documents establishing the specific rules that form the basis for corporate governance vary slightly from corporation to corporation, in theory, the shareholders, hold the ultimate, though frequently ineffective, power to determine how the corporation is to operate; in practice, a corporation's board of directors performs the critical function of overseeing management's actions and providing strategic insights/objectives. These provisions of the Restatement, like the Model Rules in general, do not seem to adequately address circumstances where the lawyer practices within a large law firm, the very type of structure likely to have large corporate clients.

This is of great practical importance for lawyers because the Model Rules sometimes refer to the "highest" authority within an organization, but the lawyer may not have ready access to this authority. Rather, the lawyer is far more likely to take his instructions from a lawyer within the office of general counsel, or some other subordinate official. Also, query whether the "highest authority" is the chief executive officer, the chairman of the board of directors, or the annual meeting of shareholders. The answer may vary by jurisdiction.

This situation is not academic. The so-called "agency problem" constitutes the principal shortcoming of U.S. corporate governance. The agency problem arises since most shareholders in publicly traded companies (i.e. the owners) act in a passive fashion and if they are unhappy with the performance of a company will sell their shares – that is, they will not usually be interested in improving the management of the company (though they may end up as plaintiffs in a class action law suit if a corporations or directors do not follow relevant legal norms).

Boards of Directors typically focus on their relationship with corporate management than their role as the shareholders' agent. Furthermore, board members are usually dependent on management for the information on which they base their decisions. This situation has changed somewhat following the

⁴¹ RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS, § 96 (2001); *see also* the corresponding Comments and Reporter Notes.

enactment of the SOX, since Boards of Directors and Audit Committees have become more independent and assertive.⁴²

The Restatement discusses briefly the appropriate manner for lawyers to overcome the agency problem.⁴³ According to traditional corporate governance theory, management is responsible for the day-to-day operation of the corporation, while the board of directors conducts oversight over management and offers the company some strategic direction. In addition, the board may initiate investigations and establish special committees to examine particular areas of concern.

In recent years, boards of directors were often ineffective because they were dependent on management for the information on which they are to make decisions, had personal ties to management, or treated their responsibilities in a lackadaisical fashion. Ultimately boards were not independent of management. This phenomenon has been termed "board capture."⁴⁴

Ultimately, both management and the board are responsible to the corporation's shareholders. The shareholders meet at least annually to adopt resolutions on topics such as proposed mergers, elections of the board, and other issues identified in the corporation's governing documents. In practice, however, most shareholders are not well informed about the activities of the corporations in which they hold shares. The majority of shareholders vote by proxy to approve the board's recommendations, or do not vote at all. Few shareholders attend meetings. Shares held by mutual funds are usually not voted. Some entities such as TIA-CREFF and Calpers, however, played a more active role in most shareholder activity.⁴⁵ As noted above, many shareholders simply "vote with their feet," in that they sell shares in underperforming companies.

⁴² Donald C. Langevoort, *Agency Law Inside the Corporation: Problems of Candor and Knowledge*, 71 U. CIN. L. REV. 117 (2003) (discussing the tensions between agency and corporate law, both of which require properly informed actors); John M. Holcomb, *Corporate Governance: Sarbanes-Oxley Act, Related Legal Issues and Global Comparisons*, 32 DENV. J. INT'L. L. & POL'Y 175 (2004) (discussing SOX's impact on the elements of good governance, in particularly the regulation of lawyers, and proposes additional measures for improvements in this area drawing from experiences in other countries). See also, ROBERT A. G. MONKS AND NELL MINOR, *CORPORATE GOVERNANCE*, (3rd Ed., 2004); Henry Hannsmann and Reinier R. Kraackman, *Agency Problems and Legal Strategies and The Basic Governance Structure*, 21-70, in *The Anatomy of Corporate Law: A Comparative and Functional Approach* (Reinier R. Kraackman ed., 2004); JOHN L. COLLEY, JR., *CORPORATE GOVERNANCE*, (2004).

⁴³ James L. Gunderson, *The Evolving Legal and Ethical Role of the Corporate Attorney After the Sarbanes-Oxley Act of 2002: Panel 1: The Collapse of the Corporate Model*, speaking at a symposium held at Washington College of Law, Washington, D.C. (Nov. 22, 2002) in 52 AM. U.L. REV. 579, 584-85 (Feb. 2003); see generally Hansmann and Kraakman, *supra* note 34 at 22.

⁴⁴ Steven M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, 97 NW. U.L. REV. 547, 563-68 (2003) (describing the relationship between boards of directors and shareholders).

⁴⁵ Corporate Governance, *Ending the Wallstreet Walk: Why Corporate Governance Now?*

The Model Rules, with a few notable exceptions (e.g. Rules 5.1, 5.2 and 5.3), seem to ignore the peculiarities of practicing law within a large organization where the lawyers' interests can diverge and their views of a particular matter differ. This leads to a situation where the Model Rules are not always enlightening for subordinate attorneys who are working on tasks for their firm's corporate clients.

In many instances, subordinate attorneys have minimal or no client contact. Therefore, it should not be surprising that subordinate lawyers would be reluctant to contact the management of clients directly if they feel that their firm is not serving the corporate client's best interests. As a result, the Model Rules and their Comments are of limited practical use to a lawyer seeking to understand his obligations to corporate clients.

The state supreme courts have the ultimate authority to regulate the practice of law within their respective state's borders. Traditionally, lawyers have been relatively successful in persuading state supreme courts, state legislatures,⁴⁶ and bar counsel to adopt rules and issue opinions largely favorable to the legal community's interest as a whole. This is often achieved at the expense of the public, which includes corporate shareholders and other stakeholders (whose interests are often overlooked in courtrooms, legislatures, and administrative agencies).

(available at <http://www.corpgov.net/forums/commentary/ending.html> (last accessed January 15, 2005) (discussing the role of pension funds such as TIA-CREF and CALPERS in increasing corporate accountability to shareholders); see also Ronald J. Gilson, *Corporate Governance: Convergence of Form or Function*, 49 AM. J. COMP. L. 329, 346-47 (2001) (discussing, *inter alia*, CALPERS Six General Principles concerning accountability in corporate governance).

⁴⁶ There is a common misperception that a majority of legislators were trained as lawyers, but this apparently is not true. According to Professor Benjamin Barton, only 15% of state legislators in 1995 were lawyers. See Benjamin H. Barton, *An Institutional Analysis of Lawyer Regulation: Who Should Control Lawyer Regulation—Courts, Legislatures, or the Market?* 37 GA. L. REV. 1167, 1219 (2003) (suggesting that legislatures and not state supreme courts should regulate lawyers since "these justices are too busy, too connected and sympathetic to lawyers, and too inaccessible to the public to do any more than allow bar associations and lawyers almost total control of the system." *Id.* at 1246. He contends that while lawyer-lobbyists may have considerable influence over state legislatures or Congress, the public may be able to serve as a counterweight). *Id.* According to data appearing on the website of the United Electrical, Radio and Machine Workers of America, a majority of the U.S. Senate were trained as lawyers, while slightly less than half of the Democratic members of the House of Representatives worked as lawyers prior to being elected; the figure for Republican members is approximately one-third. See Chris Townsend, *Where do These People Come From?*, available at http://www.ranknfile-ue.org/cap_st07.html (last accessed August 27, 2004). See Kelley R. Ross, *A Modest Proposal: Separation of Lawyers and Politics*, available at <http://www.friesian.com/lawyers.htm> (last accessed August 27, 2004) (perhaps partially in jest, Dr. Ross, the Libertarian Party Candidate for California's 28th Congressional District, proposed that in order to reduce the political power of lawyers in general, lawyers (from private practice) should either not be permitted to hold elective office or be required to win election by a supermajority).

III. THE RESPONSIBILITIES OF THE SUBORDINATE ATTORNEY & THE CORPORATE CLIENT

A. *Theory & Practice*

Most law firms are organized as pyramids with respect to both management and compensation. While law firms have different categories of lawyers: ((i) partner, (ii) non-equity partner, (iii) *of counsel*, (iv) senior associate, and (v) associate), this differentiation is not adequately addressed in the Model Rules.⁴⁷ Within a law firm, not all partners (members) have equal rights, benefits and responsibilities.⁴⁸ A lawyer's managerial and substantive role within a law firm can be complex and change over time as well as vary from matter to matter. The Model Rules do not reflect this reality. They simply divide lawyers into two categories: the subordinate lawyer and the supervisory lawyer ignoring the intricacies (and intrigues) of law firm practice (including client relations).

Model Rule 5.2 – Responsibilities of a Subordinate Lawyer, provides:

(a) A lawyer is bound by the Rules of Professional Conduct notwithstanding that the lawyer acted at the direction of another person.

(b) The duties imposed by this Rule on managing and supervising lawyers do not alter the personal duty of each lawyer in a firm to abide by the Rules of Professional Conduct.⁴⁹

⁴⁷ See Douglas R. Richmond, *Subordinate Lawyers and Insubordinate Duties*, 105 W. VA. L. REV. 449, 451-452 (2003) (discussing the obligations of subordinate and supervisory lawyers under the ABA Model Rules and the Restatement); see also Susan Saab Forney, *Are Law Firm Partners Islands unto Themselves? An Empirical Study of Law Firm Peer Review and Culture*, 60 TEX. B. J. 1056, 1057-60 (1997) (discussing the results of a survey of law firms about their peer review policies and the reliance placed by managing partners and law firm principals on limited liability firms to reduce exposure to vicarious liability for the legal malpractice of others).

⁴⁸ See David S. Hilzenrath, *Law Firm Accused of Discrimination*, WASHINGTON POST, Jan. 14, 2005, at E1 (discussing that “partners” at the law firm Sidley, Austin, Brown & Wood, who were forced into retirement by the law firm’s management committee, were “employees” and not “employers” for the purposes of the Age Discrimination Act in Employment; see also Sid Steinberg, *Business of Law on Trial in EEOC v. Sidley Austin*, THE LEGAL INTELLIGENCER, Vol. 232, No. 27, at 5 (February 9, 2005)(discussing Equal Employment Opportunity Commission’s law suit against law firm managed as if it were a corporation on the grounds that former “partners” were illegally demoted as a result of age discrimination).

⁴⁹ MODEL RULE PROF'L CONDUCT R. 5.2 (2002).

The Comment to Rule 5.2 provides:

[1] Although a lawyer is not relieved of responsibility for a violation by the fact that the lawyer acted at the direction of a supervisor, that fact may be

Read at face value, subordinate lawyers cannot violate the Model Rules by asserting that they were following the instructions of more senior lawyers. The analysis, however, does not end here.⁵⁰

Comment Two to this Rule indicates that when carrying out a task requiring “professional judgment as to an ethical duty,” the supervised lawyer can defer to a supervisory lawyer’s directive if “reasonable.” While reasonable persons can disagree, if the supervisory lawyer’s view is not clearly incorrect, it can be followed and the supervisory lawyer will assume responsibility for the subordinate lawyer’s actions.

Model Rule 5.1 – Responsibilities of Partners, Managers and Supervisory Lawyers provides:

(a) A partner in a law firm, and a lawyer who individually or together with other lawyers possesses comparable managerial authority in a law firm, shall make reasonable efforts to ensure that the firm has in effect measures giving reasonable assurance that all lawyers in the firm conform to the Rules of Professional Conduct.

relevant in determining whether a lawyer had the knowledge required to render conduct a violation of the Rules. For example . . . [a] subordinate would not be guilty of a professional violation unless the subordinate knew of the document’s frivolous character.

[2] When lawyers in a supervisory-subordinate relationship encounter a matter involving professional judgment as to ethical duty, the supervisor may assume responsibility for making the judgment. Otherwise, a consistent course of action or position could not be taken. If the question can reasonably be answered [in] only one way, the duty of both lawyers is clear and they are equally responsible for fulfilling it. However, if the question is reasonably arguable, someone has to decide upon the course of action. **That authority ordinarily reposes in the supervisor, and a subordinate may be guided accordingly.** For example, if a question arises whether the interests of two clients’ conflict under Rule 1.7, the supervisor’s reasonable resolution of the question should protect the subordinate professionally if the resolution is subsequently challenged.

Model Rule Prof’l Conduct R. 5.2 c. 1-2 (2002) [emphasis added].

⁵⁰ See Rachel Reiland (Note), *The Duty to Supervise and Vicarious Liability: Why Law Firms, Supervising Attorneys and Associates Might Want to Take a Closer Look at Model Rules 5.1, 5.2 and 5.3*, 14 GEO. J. LEGAL ETHICS 1151, 1152-53 (2001) (observing that “[d]espite the imposing language of Rule 5.1 and the specter of numerous disciplinary actions raised by its reference to ‘all [of the] rules of professional conduct,’ Rule 5.1 is seldom read, enforced, or mentioned in disciplinary proceedings.” The author urges that these rules be re-examined to make them more effective, presumably by increasing the consequences of their violation. [citation omitted]).

(b) A lawyer having direct supervisory authority over another lawyer shall make reasonable efforts to ensure that the other lawyers conform to the Rules of Professional Conduct.

(c) A lawyer shall be responsible for another lawyer's violation of the Rules of Professional Conduct if:

(1) the lawyer orders or, with the knowledge of the specific conduct ratifies the conduct involved; or

(2) the lawyer is a partner or has comparable managerial authority in the law firm in which the other lawyer practices, or has direct supervisory authority over the other lawyer, and knows of the conduct at a time when its consequences can be avoided or mitigated but fails to take reasonable remedial action.⁵¹

⁵¹ MODEL RULE PROF'L CONDUCT R. 5.1 (2002)

The Comment to Model Rule 5.1 provides:

[1] Paragraph (a) applies to lawyers who have managerial authority over the professional work of a firm. See Rule 1.0(c). This includes members of a partnership, the shareholders in a law firm organized as a professional corporation, and members of other associations authorized to practice law; lawyers having comparable managerial authority in a legal services organization or a law department of an enterprise or government agency; and lawyers who have intermediate managerial responsibilities in a firm. Paragraph (b) applies to lawyers who have supervisory authority over the work of other lawyers in a firm.

[2] Paragraph (a) requires lawyers with managerial authority within a firm to make reasonable efforts to establish internal policies and procedures designed to provide reasonable assurance that all lawyers in the firm will conform to the Rules of Professional Conduct. Such policies and procedures include those designed to detect and resolve conflicts of interest, identify dates by which actions must be taken in pending matters, account for client funds and property and ensure that inexperienced lawyers are properly supervised.

[3] Other measures that may be required to fulfill the responsibility prescribed in paragraph (a) can depend on the firm's structure and the nature of its practice. In a small firm of experienced lawyers, informal supervision and periodic review of compliance with the required systems ordinarily will suffice. In a large firm, or in practice situations in which difficult ethical problems frequently arise, more elaborate measures may be necessary. Some firms, for example, have a procedure whereby junior lawyers can make confidential referral of ethical problems directly to a designated senior partner or special committee. See Rule 5.2. Firms, whether large or small, may also rely on continuing legal education in professional ethics. In any event, the ethical atmosphere of a firm can influence the conduct of all its members, and the partners may

Rule 5.1(a) can be read as making all supervisory attorneys directly responsible for ensuring that proper ethical (and risk management) systems are in place to avoid another attorney's violation of the Model Rules.⁵² Furthermore, law firm partners' views may differ on vital issues such as the appropriate manner to structure the firm's management, the best approach to take on a particular matter, or whether it is desirable for the law firm to represent a specific client.

Perhaps of greater significance with respect to behavior is that attorneys typically have different financial stakes in the outcome of a particular law firm decision (such as taking on a new client, agreeing to handle a matter outside the firm's traditional area of practice, etc.).⁵³ Another factor not to be ignored is that

not assume that all lawyers associated with the firm will inevitably conform to the Rules.

[4] Paragraph (c) expresses a general principle of personal responsibility for acts of another. See also Rule 8.4(a).

[5] Paragraph (c)(2) defines the duty of a partner or other lawyer having comparable managerial authority in a law firm, as well as a lawyer who has direct supervisory authority over performance of specific legal work by another lawyer. Whether a lawyer has supervisory authority in particular circumstances is a question of fact. Partners and lawyers with comparable authority have at least indirect responsibility for all work being done by the firm, while a partner or manager in charge of a particular matter ordinarily also has supervisory responsibility for the work of other firm lawyers engaged in the matter. Appropriate remedial action by a partner or managing lawyer would depend on the immediacy of that lawyer's involvement and the seriousness of the misconduct. A supervisor is required to intervene to prevent avoidable consequences of misconduct if the supervisor knows that the misconduct occurred. Thus, if a supervising lawyer knows that a subordinate misrepresented a matter to an opposing party in negotiation, the supervisor as well as the subordinate has a duty to correct the resulting misapprehension.

[6] Professional misconduct by a lawyer under supervision could reveal a violation of paragraph (b) on the part of the supervisory lawyer even though it does not entail a violation of paragraph (c) because there was no direction, ratification or knowledge of the violation.

[7] Apart from this Rule and Rule 8.4(a), a lawyer does not have disciplinary liability for the conduct of a partner, associate or subordinate. Whether a lawyer may be liable civilly or criminally for another lawyer's conduct is a question of law beyond the scope of these Rules.

[8] The duties imposed by this Rule on managing and supervising lawyers do not alter the personal duty of each lawyer in a firm to abide by the Rules of Professional Conduct. See Rule 5.2(a).

MODEL RULE PROF'L CONDUCT R. 5.1 c. 1-8 (2002).

⁵² Ted Schneyer, *Professional Discipline for Law Firms?*, 77 CORNELL L. REV. 1, 17-20 (1992) (contending that the Rules of Professional Conduct are not appropriate for law firm practice).

⁵³ Professor Schneyer has proposed that law firms be subject to liability in the way that corporations may be held criminally liable. *Id.* at 8-13, 28. One of the rationales for this idea is to pe-

individual attorneys may be affected by their particular financial circumstances when making decisions involving the law firm as a whole. In fact, an attorney's dependence on a particular client may affect the lawyer's ability to provide independent and unbiased advice since such advice, if viewed as too negative or cautious by corporate management, may lead to a change in outside counsel.⁵⁴

Financial considerations, the priority given to ethical concerns, and the role of law firm management are not static factors. Law firms that are having difficulty keeping their attorneys busy, may be more inclined to take on work in areas that under other circumstances they would refuse. Firms undergoing structural changes may be reluctant to take on new matters. These factors can make a law firm's role in a particular corporation's operations unpredictable (or incapable of reliably playing the gatekeeper role).

Perhaps the most significant variable affecting law firm behavior is how it compensates its equity holders. Depending on the compensation system utilized, its principal beneficiaries may deliberately underestimate the risks or consequences to the law firm associated with pursuing the objectives of a client's management to ensure that it remains satisfied and continues to use the law firm's services. For example, some law firms pay their equity partners according to a fixed formula based on their tenure at or contribution to the law firm; others offer major incentives such as a high percentage of the law firm's billings (attribution) to the lawyer who generated the client.

Salaried attorneys, such as associates, non-equity partners and some *of counsel*, are probably less likely than a law firm's equity holders to have their independent legal judgment "influenced" by suspect aims of corporate management. Nonetheless, a law firm's profitability can still exercise an indirect effect on such lawyers' compensation and/or promotion. Thus they may still be reluctant to say "no" to a corporation's management that is willing to "push the envelope."

nalize the law firm for its "firm culture," where it is not possible to identify one or a small group of lawyers who contributed to a violation of the rules of professional conduct. *Id.* Professor Schneyer contends that the reason that the majority of the lawyers who are disciplined are either solo practitioners or lawyers at small firms is the difficulty of identifying the lawyer at fault in a large law firm where "group practice is the norm." *Id.* See also Ted Schneyer, *A Tale of Four Systems: Reflections on How Law Influences the 'Ethical Infrastructure' of Law Firms*, 39 S. TEX. L. REV. 245 (1998). *Contra* Julie Rose O' Sullivan, *Professional Discipline for Law Firms? A Response to Professor Schneyer's Proposal*, 16 GEO. J. LEGAL ETHICS 1, 31-41 (2002). Professor O'Sullivan believes that the most effective system is where individuals know they are at risk of being disciplined and is skeptical that the "entity can be the culprit." [Citations omitted].

⁵⁴ Nancy B. Rapoport, *The Legal Profession: Looking Backward: Enron, Titanic, and the Perfect Storm*, 71 FORDHAM L. REV. 1373, 1385-87 (2003) (discussing the concepts of "Moral Independence" versus "Moral Interdependence," and its role in bringing about Enron's collapse by not acting as a gatekeeper.) University of Houston Law School Professor Dean Rapoport observes that "[l]awyers need to behave as true counselors to their clients, rather than as hired guns who are just following orders." [insert cite] Professor David Luban has termed the reluctance of lawyers to dissuade a client from taking a particular course of action as "advocacy to excess." David Luban, *Integrity its Causes and Cures*, 72 FORDHAM L. REV. 279, 287-89 (2003).

According to Southern Illinois University School of Law Professor Leonard Gross, a law firm associate is:

both a servant and a sub-agent. The associate owes fiduciary obligations to the law firm consistent with those that servants and agents traditionally have owed to principals. Thus, the law firm associate owes the following duties, among others, to the law firm by which he is employed: good care and skill, loyalty, and obedience.⁵⁵

Unfortunately, these duties may conflict with a lawyer's duties to his client. Such conflicts may arise with respect to billing practices. Each attorney exercises considerable discretion when accounting for his or her billable time. Some attorneys write down their time on their own to reflect that they are not experienced in a given area or simply did not approach the matter in the most effective matter.

It is not unusual for law firms to tell associates to account for all their time and rely on the billing partner to make appropriate adjustments. This assumes that the billing partner can accurately evaluate the time needed to perform a specific task. Furthermore, the billing partner must be willing to accept the consequences of writing off unproductive time – which may cost him or the firm money. It is difficult to assess based on limited knowledge whether a particular bill is excessive because a task may be more difficult than originally expected.

Sometimes the billing partner incorporates an associate's time into his own or that of another attorney so that fewer attorneys are identified as working on a particular matter. Ideally, the partner will make such "adjustments" while ensuring that the cost to the client is the same as otherwise would be the case. Nonetheless, the transfer of time expended from one attorney to another can produce a variety of issues apart from potential ethical issues. The partner may not have as thorough an understanding of a particular issue that the associate who worked on it had. This means that the client may assume that the partner is better informed about the matter than he is in fact.

The degree to which in-house counsel scrutinizes a law firm's bill greatly varies. It is by no means clear that a particular in-house counsel is competent to judge the time needed to complete certain tasks and whether the task was essential. Ultimately, this becomes a matter of whether the amount billed to the client seems justified. The law firm, in many instances, has both financial and liability concerns that create incentives to "over lawyer" a particular matter. Not surprisingly, billing disputes can poison a law firm's relationships with clients. To reduce the risk of such disputes, the responsible partners needs to see that projects are properly handled and that clients be kept informed about the

⁵⁵ Leonard Gross, *Ethical Problems of Law Firm Associates*, 26 WM. & MARY L. REV. 259, 262 (1985).

progress of work being performed for their benefit as well as any unforeseen problems.

There is a widespread concern among many consumers of legal services that lawyers (most often associates) "pad" their hours.⁵⁶ This practice may be more common at large law firms servicing corporate clients. A factor contributing to problem (apart from the incentive structure within the law firm) is that so long as the total cost of legal services procured by in-house counsels remain within budget for the relevant time period, there often is no incentive for the corporation to contain expenses. In fact, if a corporation's office of general counsel does not spend all the funds allocated to it, the likelihood that its budget will be reduced in the future is increased. These are some of the factors reducing the likelihood that law firm bills are contested and associates do not encounter repercussions for their actions as their conduct may not be closely monitored.

Nonetheless, as Professor Gross has noted:

[i]n addition to the fiduciary duties that the associate owes to his law firm, the associate has other responsibilities. He owes a fiduciary duty to the client on whose behalf he is working. His duty to the client is much the same as if he were the attorney in charge of the representation. The bases for this responsibility can be found in the law of agency and in the attorney's professional duty to the client as set forth in the various codes of professional responsibility. In many situations, the associate also has a duty to the public, or at least to a segment of the public.⁵⁷

Unfortunately, the associate's connection to the "public" may be nebulous and direct interactions with the client superficial or non-existent. Since the Model Rules often call on the lawyer to decide what is "reasonable" under a particular set of circumstances, the lawyer can be tempted to take the path of least resistance and conform the unethical billing practices at the law firm.

⁵⁶ Many associates react to the pressure to bill excessive hours by aggressive billing practices that may border on larceny. See Lisa G. Lerman, *Blue-Chip Bilking: Regulation of Billing and Expense Fraud by Lawyers*, 12 GEO. J. LEGAL ETHICS 205, 293-300 (1999) (presenting the results of a study suggesting a high level of padding, manipulating, and fabricating time sheets and expense vouchers); Daniel Schweimler & Reena Sengupta, *A Question of Time and Money: Billable House: The Clifford Chance Memo Has Thrown Harsh Light on Lawyers; Charging Practices*, THE FINANCIAL TIMES, *19; see also David Callahan, *The Cheating Culture: Why More Americans Are Doing Wrong to Get Ahead* (2004) at 33-42 (seeing the decline of legal ethics of lawyers as reflecting a larger cultural phenomenon); but see William J. Wernz, *The Ethics of Large Law Firms – Responses & Ethics*, 16 GEO. J. LEGAL ETHICS 175 (2002) (arguing that corporate counsel should scrutinize large law firm's bills, preventing fraudulent billing in most cases; the author believes that overall the quality of legal work today is excellent).

⁵⁷ *Id.* at 267.

Professor Mona L. Hymel proposed addressing issues such as these by moving away from reliance on the interpretation of general ethical rules⁵⁸ and the adoption of specific guidelines or protocols analogous to those used by the medical profession.⁵⁹ Perhaps, such guidelines might address the manner by

⁵⁸ According to Professor Hymel, the state codes of professional ethics “serve two broad goals. First, they serve a disciplinary function. Second, legal ethics codes provide guidance to lawyers in resolving ethical dilemmas. Through their standards and rules, state ethics codes furnish principles that are designed to guide lawyers in maintaining good lawyer-client relationships, conducting transactions with non-clients, and maintaining the integrity of the profession. The guidance provided applies to all lawyers, regardless of specialization.” Mona L. Hymel, *Controlling Lawyer Behavior: The Sources and Uses of Protocols in Governing Law Practice*, 44 ARIZ. L. REV. 873, 879 (2002) (citations omitted).

⁵⁹ In her article, Professor Hymel uses the word ‘protocol’ to mean specific guidelines or rules that govern the practice of law. Professional organizations and agencies could develop such protocols to govern the conduct of their members or lawyers practicing for them. *See id.* at 873-74. Medical protocols (procedures) are followed in processing trauma patients in emergency rooms for purposes of diagnosis and treatment. *See* New York Trauma Protocol Resources, available at <http://www.nyerrn.com/er/tg.htm> (last accessed January 15, 2005).

Professor Hymel advances three rationales for developing protocols to replace the states’ ethical rules that are largely derived from the Model Rules.

First, although more lawyers are now counselors than litigators, state ethics codes are still largely based on the model of the lawyer as advocate. Unlike traditional lawyer/client relationships in the adversary system, where the lawyer’s duties run almost exclusively to clients, the transactional lawyer, in many cases, may have or be perceived to have obligations that run to third parties. Furthermore, issues regarding to whom the corporate lawyer owes his or her loyalty within the corporate structure often arise. As transactional/corporate practices grow and become more elaborate, the model of “lawyer as advocate” becomes increasingly irrelevant. Existing ethics codes do almost nothing to clarify the lawyer’s responsibilities to non-clients when working in the corporate context. But regulatory agencies like the IRS [Internal Revenue Service] and OTS [Office of Thrift Supervision] can tailor specialized rules and enforcement practices to tax and banking lawyers with minimal vagueness or internal contradiction. Furthermore, because these rules apply primarily to corporate practice, agency rules can take into account corporate externality problems - i.e., non-client interests - without unduly chilling advocacy. As Professor Wilkins has observed,

corporate clients, with their superior ability to monitor and control lawyer conduct, have the power both to press their lawyers to act in ways that jeopardize systemic norms and the rights of third parties, and to protect themselves against any loss of zealous advocacy or individual autonomy that might otherwise follow from an increase in external regulation.

Second, state ethics regimes do not regulate firms. As firms grow and become more decentralized, and as lawyers frequently move from one firm to another, accountability for ethical violations is weakened. This situation is made even more complex on matters having a nexus with more than one state or country since it is often unclear which jurisdictions ethical rules apply. Lawyers are always bound by ethical rules of the state in which they are admitted. Furthermore, by becoming more specialized and compartmentalized, lawyers in large law firms know little about firm colleagues and clients outside their own narrow area of expertise. Thus, unscrupulous lawyers and

which the cost for legal services are generated, rather than merely stating that they should be reasonable.

Since legal practice has become so specialized, Professor Hymel persuasively argues that such guidelines or protocols should be carefully tailored for different practice areas.⁶⁰ Given that lawyers are regulated at the state level, and rules vary from jurisdiction to jurisdiction, an effort should be made to make these guidelines uniform (though there probably is a need for adjustments to reflect differences in the cost of living in within the country). Currently, corporate law is largely determined at the state level. Given that public corporations must make federal filings with the SEC and that most conduct business across state lines, would it not be unreasonable for all issuers of securities to be governed by federal corporate law?

Professor Hymel contends that a change of approach is desirable since the ethical rules generally:

- (i) address issues that arise more frequently in the litigation context, but today lawyers as a group spend more time as counselors and transaction attorneys than as litigators;

clients operate unimpeded when one obvious source of oversight is overlooked - the firm. Regulation within a firm through its own internal procedures can be an efficient policing mechanism. The OTS, SEC and the IRS have not overlooked this fact and have not hesitated to impose regulations and sanctions on law firms.

Third, specific rules work well in addressing the problems associated with corporate law practice and large law firms. [University of Illinois College of Law Professor] Richard Painter suggests that protocols (which he calls tailored rules) need to be more common-place because '[t]ailored rules for problems unique to particular practice areas also may be easier to draft, easier to muster political support for, and easier to enforce than pure majoritarian rules.' He concludes that the '[r]epresentation of organizational clients is one area that badly needs tailored rules.' The recent Enron bankruptcy highlights the problems with representing organizations that have plagued regulators in the past. Judge Stanley Sporkin articulated several key problems in the S&L crisis that also appear to be factors in the Enron bankruptcy. For example, in corporate practice, determining to whom the lawyer owes her loyalties is complicated (i.e., shareholder derivative suits). The lawyer's duties may not be clear when conflicts arise between management, corporate shareholders and the board of directors. In addition, when public documents such as registration statements are prepared, the lawyer's disclosure duties are not clear. Furthermore, a whole host of problems arise when dealing with regulatory agencies, such as whether lawyers may use litigation tactics to delay agency investigations or inquiries. Thus, agency regulators, who responded to the S&L crisis with protocols, are likely to respond in a similar fashion to the most recent wave of corporate scandals. Hymel, *supra* note 50 at 884-86 (footnotes omitted).

⁶⁰ Legal practice, however, has gotten so specialized that it makes it impossible to adopt separate guidelines for each particular area of the law. *Id.* Consequently, there will probably be a need for a set of generalized guidelines and when feasible, specific guidelines, e.g. banking, domestic real estate, intellectual property, international transactions, securities, tax, etc. *Id.* Of course, certain activities do not fit cleanly into one category. *Id.* Therefore several sets of guidelines may apply at the same time. To some extent, the different set of guidelines already exists in the form of agency regulations at the federal level. *Id.*, at 891-904.

(ii) inadequately reflect what occurs at larger decentralized law firms; and

(iii) are incompatible with the management structure for many contemporary law firms.⁶¹

Her critique is essentially accurate. To identify what changes are necessary in the ethical rules, it is important to view the situation both from the client's as well as the lawyer's prospective. This methodology may bring to light certain complexities that otherwise might not be adequately addressed.

IV. FIXING SOME OF THE GAPS IN THE ABA'S MODEL RULES WITH RESPECT TO CORPORATE CLIENTS

Much has been written about what are the lawyer's obligations to the client in general and the corporate client in particular. The Model Rules' primary function is to set out the governing of the client-lawyer relationship. As noted by the Task Force, the Model Rules' focus is on an individual lawyer. They cover topics such as (i) competence, (ii) scope of representation and allocation of authority between the client and the lawyer, (iii) communications, (iv) fees, (v) confidentiality of information, and (vi) conflicts of interests.

Of these topics, the last two are the most difficult to regulate. Typically, Model Rule 1.6 – Confidentiality of information concerns a lawyer's obligation not to reveal information provided by a client having an expectation of confidentiality.⁶² Rule 1.6(b)(3), however, contains a provision that the lawyer has

⁶¹ *Id.*,

⁶² ABA Model Rule 1.6 --Confidentiality of Information provides:

(a) A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation or the disclosure is permitted by paragraph (b). A lawyer may reveal information relating to the representation of a client to the extent the lawyer reasonably believes necessary:(1) to prevent reasonably certain death or substantial bodily harm;

(2) to prevent the client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's services;

(3) to prevent, mitigate or rectify substantial injury to the financial interests or property of another that is reasonably certain to result or has resulted from the client's commission of a crime or fraud in furtherance of which the client has used the lawyer's services;

(4) to secure legal advice about the lawyer's compliance with these Rules;

the right to reveal confidential information s/he reasonably believes necessary "to prevent, mitigate or rectify substantial injury to the financial interests or property of another"

The express language of this provision is not restricted to instances where the attorney would be acting in furtherance of a crime or fraud. The Comment to this paragraph emphasizes the limited nature of this exception and refers to Model Rule 1(d) that relates to fraud or fraudulent conduct. Thus, the extent to which one believes that the Comment can trump the text of the Rule appears to be a critical issue. According to the Model Rules, the Comments "do not add obligations to the Rules, but provide guidance for practicing in compliance with the Rules."⁶³ The Comments are not regarded as mandatory particularly since the Model Rules are "rules of reason" that do not anticipate every, or even most, situation(s).

Consequently, a lawyer working for a corporate client would (i) under the Patriot Act and SOX be obligated to reveal confidential information to regulatory authorities, but (ii) under the Model Rules have "discretion" to report up the ladder to an organization's management where there is the danger of "substantial injury," including to the corporation.

SOX's enactment has heightened awareness of who is the lawyer's (law firm's) client.⁶⁴ The legal community has been particularly concerned by the SEC's proposed rules for SOX's "noisy withdrawal," as mandated by § 307. This section concerns what a lawyer should do if reporting improper actions up the ladder does not result in management taking appropriate action. If a corporation's management (or board) reacts in a manner in which a lawyer does not feel addresses the problem(s) at issue, then management will probably choose to deal only with those lawyers within the law firm who are less likely to challenge management decisions. This could result in corporate management retaining

(5) to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client; or

(6) to comply with other law or a court order.

⁶³ ABA, Model Rules of Professional Conduct, Scope ¶14.

⁶⁴ Stephen Fraidin and Laura B. Mutterperl, *Advice for Lawyers: Navigating the New Realm of Federal Regulation of Legal Ethics*, 72 U. CIN. L. REV. 609, 627-30 (2003) (analyzing the obligation of lawyers to "report up the ladder" when they believe that wrongdoing by a corporate client's employees has or will occur and noting that while lawyers understand that when representing a corporation, they represent the legal entity and not its officers, in practice determining the interests of the entity is not always a straightforward matter. Since corporations can only act through "their constituents such as their officers, directors, employees, and shareholders" lawyers may have "confused allegiances." The danger being that "executive officers and other employees of public companies may succumb to the temptation to serve personal interests in maximizing their own wealth or control at the expense of long-term corporate well-being.").

law firms that support aggressive interpretations of ambiguous laws and regulations.

The practical rules in this area are open to considerable discretion. For example, what is "appropriate action," and within what time frame must such action be taken? Who within a law firm decides what is appropriate and what is not? When an organization is expected to take appropriate action is discussed in a U.S. Department of Justice memorandum.⁶⁵

According to the DoJ memorandum, the decision of whether to prosecute an organization (which often occurs in conjunction with the prosecution of individuals), will depend on a corporation's culture, the operation of its regulatory compliance program, and how quickly management informs the appropriate government authorities of a possible violation of law. If management waits until the conclusion of any investigation, it may have waited too long.

Mr. Fraidin and Ms. Mutterperl have offered a defensible view of how the Model Rules and SOX's requirements are likely to work in practice,

[A] company which has already failed to live up to its obligations is unlikely to report itself. The lack of an actual obligation on attorneys in such a situation also would ultimately make the "permissive" option [of noisy withdrawal] almost entirely fictitious. The lawyer who is not required to take action has more than ample reason not to do so . . . [A] lawyer will encounter certain resistances, often from his or her own firm which might be hesitant to lose a well paying client.

In a permissive situation, an associate or partner may easily be talked out of taking action, especially where the lawyer is only allowed to give the faintest hint to allow the SEC to help the client corporation. When that is compared with the risk to hundreds of thousands of dollars in potential fees, the "noisy withdrawal" is not the least bit attractive to a lawyer and his or her firm. Corrupt officers will know this.⁶⁶

What if an attorney feels that corporate management is engaging in an activity that is not best for the corporation? First, it is necessary to define the specific nature of outside counsel's function. Where outside counsel is retained to address a simple issue, assist in the preparation of an SEC filing, or to paper a par-

⁶⁵ Larry D. Thompson Deputy Attorney General, entitled "Principles of Federal Prosecution of Business Organizations," dated January 20, 2003. Timothy J. Coleman, Esq., Senior Counsel to the Deputy Attorney General, made available a copy of the memorandum at the Annual Meeting of the Association of Corporate Counsel held in Chicago on October 25, 2004.

⁶⁶ Fraidin, *supra*, note 56 at 656.

ticular transaction, the lawyer (law firm) has a relatively narrow set of responsibilities.

In contrast, if outside counsel serves a broader role (e.g. provided all the legal work to the corporation and its components), where to draw the line is less clear. Where the lawyer (law firm) is acting as a counselor, that is providing legal advice on a range of issues and participating in decision-making, the line between law and business becomes less clear.

Model Rule 2.1 – Advisor, provides:

In representing a client, a lawyer shall exercise independent professional judgment and render candid advice. In rendering advice, a lawyer may refer not only to law but also to other considerations such as moral, economic, social and political factors, which may be relevant to the client's situation.

Comment 5 to this Rule states that:

[i]n general, a lawyer is not expected to give advice until asked by the client. However, when a lawyer knows that a client proposes a course of action that is likely to result in substantial adverse legal consequences to the client, **the lawyer's duty to the client under Rule 1.4 [Communication] may require that the lawyer offer advice if the client's course of action is related to the representation** [emphasis added].

This avoids the questions to whom (or what) is the lawyer required to offer advice and if a lawyer's advice is ignored at a particular level such as (i) General Counsel, (ii) Chief Executive Officer, or (iii) Board of Directors, is the lawyer obligated to inform the shareholders, and if so how, particularly where there are concerns about confidentiality and maintaining the value of the corporation?

Furthermore, there are competing theories of corporate governance. One theory holds that increasing the corporation's value is the primary goal to be pursued by management and the board of directors. The other posits that the corporation must take into account the interests of all the stakeholders, not just the shareholders. In accordance with this latter view (which is prevalent in most European Union countries), the interests of the work force and community cannot be ignored. Finally, taking account of all stakeholders may have a significant impact on a corporation's value in the long term.

Gradually, there seems to be some convergence of the two corporate governance systems, which is not merely understandable, but desirable. If a corporation is focused entirely on the near-term – it can lead to underinvestment, problems with suppliers and customers, and potentially labor/institutional memory loss problems. In addition, it may give rise to political difficulties with both local, state, and national level officials and politicians. In contrast, corpo-

rations that in the past operated principally on the stakeholder model sometimes experienced difficulty in sustaining their competitiveness in the increasingly globalized economy, in part due to high labor costs.

Irrespective of which philosophy of corporate governance is observed, all players in corporate governance (management, board of directors and shareholders) may each have different concepts of time for purposes of planning. This is principally an issue for the business client to resolve, but at times lawyers are consulted. Again, how much initiative should a lawyer show in this area and what if all the lawyers in the firm do not share the same opinion? In most instances, the law firm should have internal rules addressing this subject, but this is not always the case.

Such internal rules may place principal decision-making power in (i) the billing partner, who typically communicates directly to corporate management on a regular basis, (ii) all the supervisory lawyers rendering services to a particular client, (iii) the firm's management or supervisory committee, or (iv) the firm's ethics partner or ethics committee. Clearly there are different possibilities and one approach might not be appropriate for all law firms.

The Model Rules make clear that each individual lawyer is bound by all relevant ethical rules pursuant to Rule 5.2(a), but under Rule 5.2(b) a "supervised" lawyer may reasonably rely on a "supervisory lawyer's reasonable resolution of an arguable question of professional duty." This includes Model Rule 8.3, which makes mandatory a lawyer's obligation to report the professional misconduct of another member of the bar to the relevant authority (typically bar counsel).

It would be undesirable to create a situation of "legal anarchy" where attorneys felt morally obliged to communicate directly to a client (or component thereof) or bar counsel. To avoid this situation, the law firm needs to establish a viable procedure for resolving whether the supervisory lawyer's resolution of an issue is indeed reasonable. Junior lawyers, or lawyers inexperienced in a particular field, may not have the knowledge to properly judge a situation.

The Model Rules could be improved if they explicitly provided for whistleblower protections to ensure that attorneys are willing to act in compliance with their ethical duties without running the risk of retaliation. Existing whistleblower legislation would probably have to be strengthened for this to occur. Irrespective of what protections might be established, it is difficult to create effective whistleblower protections without dedicating sufficient financial resources to the problem.

The Model Rules also need to be revised so that the obligation to report professional misconduct is in fact followed.⁶⁷ At present, attorneys seldom re-

⁶⁷ Arthur F. Greenbaum, *The Attorney's Duty to Report Professional Misconduct: A Roadmap for Reform*, 16 GEO. J. LEGAL ETHICS 259, 333 (2003) (noting that after "more than thirty years, the ABA and the vast majority of the states have recognized lawyer reporting of professional misconduct as a central tenet of the profession. Yet, whether by happenstance or design, the reporting rules adopted to achieve this goal have proved wanting.").

sort to use Model Rule 8.3, known as the “ratting provision.” A lawyer’s filing a complaint about another member of the bar does not usually bring one any tangible benefits (except possibly where the individual being complained about is a competitor). It could trigger retaliation and may demand a lot of (unpaid) time.⁶⁸ “Professional misconduct” is an imprecise term and can mean different

⁶⁸ Rule 8.3 – Reporting Professional Misconduct

(a) A lawyer who knows that another lawyer has committed a violation of the Rules of Professional Conduct that raises a substantial question as to that lawyer's honesty, trustworthiness or fitness as a lawyer in other respects, shall inform the appropriate professional authority.

(b) A lawyer who knows that a judge has committed a violation of applicable rules of judicial conduct that raises a substantial question as to the judge's fitness for office shall inform the appropriate authority.

(c) This Rule does not require disclosure of information otherwise protected by Rule 1.6 or information gained by a lawyer or judge while participating in an approved lawyers assistance program.

Comment

[1] Self-regulation of the legal profession requires that members of the profession initiate disciplinary investigation when they know of a violation of the Rules of Professional Conduct. Lawyers have a similar obligation with respect to judicial misconduct. An apparently isolated violation may indicate a pattern of misconduct that only a disciplinary investigation can uncover. Reporting a violation is especially important where the victim is unlikely to discover the offense.

[2] A report about misconduct is not required where it would involve violation of Rule 1.6. However, a lawyer should encourage a client to consent to disclosure where prosecution would not substantially prejudice the client's interests.

[3] If a lawyer were obliged to report every violation of the Rules, the failure to report any violation would itself be a professional offense. Such a requirement existed in many jurisdictions but proved to be unenforceable. This Rule limits the reporting obligation to those offenses that a self-regulating profession must vigorously endeavor to prevent. A measure of judgment is, therefore, required in complying with the provisions of this Rule. The term "substantial" refers to the seriousness of the possible offense and not the quantum of evidence of which the lawyer is aware. A report should be made to the bar disciplinary agency unless some other agency, such as a peer review agency, is more appropriate in the circumstances. Similar considerations apply to the reporting of judicial misconduct.

[4] The duty to report professional misconduct does not apply to a lawyer retained to represent a lawyer whose professional conduct is in question. Such a situation is governed by the Rules applicable to the client-lawyer relationship.

[5] Information about a lawyer's or judge's misconduct or fitness may be received by a lawyer in the course of that lawyer's participation in an approved lawyers or judges assistance program. In that circumstance, pro-

things to different people.⁶⁹ A long-term member of the bar, defended by competent counsel, is seldom found liable of professional misconduct for commit-

viding for an exception to the reporting requirements of paragraphs (a) and (b) of this Rule encourages lawyers and judges to seek treatment through such a program. Conversely, without such an exception, lawyers and judges may hesitate to seek assistance from these programs, which may then result in additional harm to their professional careers and additional injury to the welfare of clients and the public. These Rules do not otherwise address the confidentiality of information received by a lawyer or judge participating in an approved lawyers assistance program; such an obligation, however, may be imposed by the rules of the program or other law.

⁶⁹ Rule 8.4 – Misconduct states:

It is professional misconduct for a lawyer to:

- (a) violate or attempt to violate the Rules of Professional Conduct, knowingly assist or induce another to do so, or do so through the acts of another;
- (b) commit a criminal act that reflects adversely on the lawyer's honesty, trustworthiness or fitness as a lawyer in other respects;
- (c) engage in conduct involving dishonesty, fraud, deceit or misrepresentation;
- (d) engage in conduct that is prejudicial to the administration of justice;
- (e) state or imply an ability to influence improperly a government agency or official or to achieve results by means that violate the Rules of Professional Conduct or other law; or
- (f) knowingly assist a judge or judicial officer in conduct that is a violation of applicable rules of judicial conduct or other law.

Comment

[1] Lawyers are subject to discipline when they violate or attempt to violate the Rules of Professional Conduct, knowingly assist or induce another to do so or do so through the acts of another, as when they request or instruct an agent to do so on the lawyer's behalf. Paragraph (a), however, does not prohibit a lawyer from advising a client concerning action the client is legally entitled to take.

[2] Many kinds of illegal conduct reflect adversely on fitness to practice law, such as offenses involving fraud and the offense of willful failure to file an income tax return. However, some kinds of offenses carry no such implication. Traditionally, the distinction was drawn in terms of offenses involving "moral turpitude." That concept can be construed to include offenses concerning some matters of personal morality, such as adultery and comparable offenses, which have no specific connection to fitness for the practice of law. Although a lawyer is personally answerable to the entire criminal law, a lawyer should be professionally answerable only for offenses that indicate lack of those characteristics relevant to law practice. Offenses involving violence, dishonesty, breach of trust, or serious interference with the administration of justice are in that category.

ting acts arguably falling within "gray areas." Typical disciplinary cases involve the improper use of client funds, lying to the court, not warning a client of the impending expiration of the statute of limitations or the failure to make the timely filing of a court or administrative document.⁷⁰

V. CONCLUDING OBSERVATIONS AND THE NEED FOR FUTURE ACTION

If lawyers are to practice in limited liability entities, they need to adopt a form of corporate governance that reflects the best practices used in the corporate world, with appropriate additional risk management mechanisms specific to different categories of legal practice. That being said, the corporate model of governance cannot be transplanted into law firms without modification.⁷¹

One option would be to require law firms above a fixed number of attorneys to have its own "Ethics Counsel." This individual should not have an

A pattern of repeated offenses, even ones of minor significance when considered separately, can indicate indifference to legal obligation.

[3] A lawyer who, in the course of representing a client, knowingly manifests by words or conduct, bias or prejudice based upon race, sex, religion, national origin, disability, age, sexual orientation or socioeconomic status, violates paragraph (d) when such actions are prejudicial to the administration of justice. Legitimate advocacy respecting the foregoing factors does not violate paragraph (d). A trial judge's finding that peremptory challenges were exercised on a discriminatory basis does not alone establish a violation of this rule.

[4] A lawyer may refuse to comply with an obligation imposed by law upon a good faith belief that no valid obligation exists. The provisions of Rule 1.2(d) concerning a good faith challenge to the validity, scope, meaning or application of the law apply to challenges of legal regulation of the practice of law.

[5] Lawyers holding public office assume legal responsibilities going beyond those of other citizens. A lawyer's abuse of public office can suggest an inability to fulfill the professional role of lawyers. The same is true of abuse of positions of private trust such as trustee, executor, administrator, guardian, agent and officer, director or manager of a corporation or other organization.

⁷⁰ See Leslie C. Levin, *The Emperor's Clothes and Other Tales about the Standards for Imposing Lawyer Discipline Sanctions*, 48 AM. U. L. REV. 1 (1998) (describing the range of sanctions imposed for disciplinary violations by lawyers and calling for better standards).

⁷¹ See Jeffrey W. Stempel, *Embracing Descent The Bankruptcy of a Business Paradigm for Conceptualizing and Regulating the Legal Profession*, 27 FLA. ST. U. L. REV. 25, 32-42, 78-80 (1999) (arguing that a "kinder and gentler" system advanced by Professor Russell G. Pearce will not produce the needed results, refinement of the professionalism paradigm is the better approach since lawyers have a high level of autonomy and professional discretion in rendering services to clients. A regulatory regime to be successful requires that the group in which the lawyer works must play an active role in upholding existing (or updated) professional norms reflecting a desirable value-based system).

equity interest in the law firm, but must be senior enough to be familiar with law firm practices sufficient to earn the respect from both experienced and junior lawyers.⁷² Ethic Counsel's compensation should not depend on the number of hours worked or law firm profitability. Furthermore, the Ethics Counsel should be recruited from outside the law firm to minimize the impact that personal relations might have on the individual holding the position.

Ideally, the individual should hold the position for a fixed term (e.g., four years). In practice, finding a qualified person to take such a job might prove exceedingly difficult. Some law firms have already established such positions, but it is still too early to assess the effectiveness of these systems given the diverse nature of law firm structures, practices, locations, personnel, etc.

The Ethics Counsel should oversee the law firm's conflict check system and the production of a detailed and user-friendly ethics manual specific to the firm. The Ethics Counsel should keep all lawyers at the firm apprised of developments involving ethics and professional responsibility. For instance, within each jurisdiction in which the law firm has an office (or even where one of its lawyers is admitted to the bar), the Ethics Counsel should disseminate by e-mail and maintain on an internal website, Bar Counsel Decisions, Bar Professional Responsibility Office's Opinions, changes in the rules of professional conduct for all jurisdictions where the law firm's attorneys are members of the bar, significant judicial decisions as well as specific items applicable to particular attorneys' practice areas (e.g. securities, intellectual property, etc.).

Under such a scheme, all attorneys would be required to acknowledge that they have reviewed the documents that they have been given by Ethics Counsel. It would be difficult to assess the impact of requiring an Ethics Counsel in each firm since each organization is *sui generis* with respect to its personnel, nature of practice, location, etc. Nonetheless, the creation of such an institution and giving the individual sufficient resources and power to have an impact would make an important statement. The legal professional liability insurance industry would appear to have an incentive to promote this system (or another concept) as part of a risk management program.

An alternative approach would be for the bar to require law firms to establish an "Ethics Committee" fulfilling the functions that would be accomplished by an Ethics Counsel. This would reduce the possibility that one person

⁷² Diana Bentley, *Leaving Nothing to Chance – The Rise of General Counsels in Law Firms*, *Int'l Bar News*, Vol. 58, No. 2, at 19-22 (June 2004) and Jonathan D. Glater, *In a Complex World, Even Lawyers Need Lawyers*, N.Y. TIMES, Feb. 3, 2004 at C1 (both articles noting that increasingly law firms are hiring a general counsel to "advise lawyers confronting thorny conflicts, [ensure] compliance with state bar association rules and [provide] advice on firm management. While some of the largest firms have had general counsels for several years, the trend has picked up at late, lawyers say." While this is a desirable development, some firms simply designate an existing law firm partner to take on these duties. Unfortunately, such an individual may not be sufficiently independent as would a dedicated Ethics Counsel within the law firm).

might be tempted to make decisions for reasons other than the merits of the situation. Having an Ethics Committee, rather than an individual, might also be desirable since members would have had different areas of practice and varying opinions on particular matters.⁷³

A third approach would be for the ABA to prepare and the states to adopt versions of ethical rules appropriate to lawyers particular to different organizational structures and practices. As the nature of the practice of law has developed along different lines, it is only reasonable that the applicable ethical rules would reflect this situation.⁷⁴ Perhaps, the ABA's Standing Committee on Lawyers Professional Liability the National Organization of Bar Counsels, Association of Professional Liability Lawyers, and an appropriate unit of the U.S. Department of Justice should undertake to make the ethical rules more compatible with the existing practice of law.⁷⁵ Unfortunately, this task may prove to be too complex to implement effectively.

A fourth option might require a law firm to institute a system of partner rotation for the firm's various management bodies as well as the individual tasks for maintaining contacts with the law firm's major corporate clients. In practice, such a system might be difficult to institute given the importance of personal relationships between management and lawyers working for clients.⁷⁶

Unfortunately, it is not possible to legislate or regulate morality. Even establishing the best possible professional conduct system will not guarantee ethical behavior by lawyers. Consequently, the best strategy for achieving desirable results is to amend Model Rule 8.3 – Reporting Professional Misconduct (or its state equivalent) to give it real “teeth” and actually enforce it.⁷⁷ One way of making Model Rule 8.3 meaningful would be to discipline a lawyer for failing to report misconduct by another member of the bar (such as not reporting

⁷³ See Fraidin and Mutterperl, *supra* note 56 at 664-66 (analyzing how such a committee might operate).

⁷⁴ See J. Robert Brown, Jr., *The Irrelevance of State Corporate Law in the Governance of Public Companies*, 38 U. RICH. L. REV. 317 (2004) (arguing in favor of having a single set of rules governing the operations of corporation to deter the “race to the bottom.”); see also Fred C. Zacharias, *Federalizing Legal Ethics*, 73 TEX. L. REV. 335 (1994) (analyzing the pros and cons of federalizing ethical rules for lawyers, and though he generally believes that it should occur for reasons such as the nationalization of the practice of law, multi-state litigation, client expectations, and that federal law takes precedence over state law, he recognizes that Congress lacks experience to do so, potentially leading to unforeseen consequences.)

⁷⁵ Professor Hymel has noted that the insurance carriers that issue professional liability policies to attorneys often provide their insured with manuals outlining “best practices” to help reduce their insureds’ risk of malpractice. Lawyers who work for the insurance industry could make a valuable contribution to this effort by examining these manuals to ascertain their usefulness in producing more practical ethical guidelines. See Hymel, *supra* note 50, at 911-13.

⁷⁶ For a discussion of instituting a system of partner rotation within a law firm, see Fraidin, *supra*, note 56 at 667-70.

⁷⁷ The text of Mode Rule 8.3 — Reporting Professional Misconduct is set out *supra*, note 60.

conduct that constitutes a crime⁷⁸ or would support a Federal Rule of Civil Procedure 11 sanction.⁷⁹ Under these rules, even judges would be required to report professional misconduct to the appropriate disciplinary authorities.

Others have also called for reform in this area.⁸⁰ For example, Professor Arthur F. Greenbaum contends that Model Rule 8.3 is so vague and ambiguous as to make it of little practical value.⁸¹ This is not simply the view of academics, but courts and the ABA as well.⁸² The ABA has established a Joint Commission to Evaluate the Model Code of Judicial Conduct (the "Commission") to review the ABA's model ethics code for judges and to recommend revisions for possible adoption in August 2005; a similar effort should be made for the Model Rules of Professional Conduct as well.⁸³ Such a Commission should set as its goal the creation of a framework for professional conduct that is relevant to the practice of law in the 21st Century. Indeed, the ABA has organized a number of "special projects," the work of which could make important contributions in this area.⁸⁴

For even amended and improved rules to have a desirable impact, real reform needs to be from the bottom up as well as the top down. Lawyers and law firms need to recognize that problems exist in this area and must be addressed sooner rather than later.

⁷⁸ See THANE ROSENBAUM, *THE MYTH OF MORAL JUSTICE* (2004) (discussing how application of the "law" often does not lead to "moral" outcomes, in part as a result of our "advocacy" system as well as the absence of moral imperatives to act in most states (unlike many European countries, where there is a mandatory duty to rescue)).

⁷⁹ Misconduct is defined in Model Rule 8.4, *supra*, note 61.

⁸⁰ Greenbaum, *supra*, note 59. See also Peter K. Rofes, *Another Misunderstood Relation: Confidentiality and the Duty to Report*, 14 *GEO. J. LEGAL ETHICS* 621 (2001) (arguing that an attorney's obligation to preserve attorney confidences can interfere with the attorney's duty to report misconduct).

⁸¹ *Id.* at 281-83.

⁸² *Id.* at 275-88.

⁸³ See The Joint Commission's website describing its origin, available at <http://www.abanet.org/judicialethics/about.html> (last accessed October 4, 2004).

⁸⁴ The entities include the Joint Committee on Lawyer Regulation, the Task Force on the Model Definition of the Practice of Law, Commission on Multidisciplinary Practice, Commission on Multijurisdictional Practice of Law and the Ethics 2000 Commission. The Ethics 2000 Commission takes the lead role in proposing revisions to the Model Rules. For a description of each of these entities' activities, see the ABA website at http://www.abanet.org/cpr/special_projects.html (last accessed October 4, 2004).