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## **ABA Task Force on Corporate Responsibility and the 2003 Changes to the Model Rules of Professional Conduct, The**

Hamermesh, Lawrence A.

### **I. INTRODUCTION**

Established in March 2002 to address "systemic issues relating to corporate responsibility arising out of the unexpected and traumatic bankruptcy of Enron and other Enron-like situations,"<sup>1</sup> the American Bar Association Presidential Task Force on Corporate Responsibility ("Task Force") presented a series of policy recommendations to the ABA House of Delegates at its 2003 Annual Meeting in San Francisco.<sup>2</sup> Two of those recommendations involved proposals to amend the ABA's Model Rules of Professional Conduct ("Model Rules"), specifically Model Rules 1.6 and 1.13.<sup>3</sup>

With one exception accepted by the Task Force in floor debate, the proposals set forth in the Report of the American Bar Association Task Force on Corporate Responsibility ("Final Report")<sup>4</sup> were adopted by the House of Delegates without change. That adoption followed highly charged controversy, including accusations that the Task Force's recommended changes to Model Rules 1.6 and 1.13 would sacrifice "core values" of the legal profession.<sup>5</sup> This Article attempts to illuminate, and perhaps calm, that controversy in three ways: (1) by reviewing the background and content of the 2003 changes to Model Rules 1.6 and 1.13, (2) by responding briefly to some of the concerns expressed by opponents of the changes, and (3) by emphasizing other important and related policies recommended by the Task Force.

This Article's description of the history and context of the recent changes to Model Rules 1.6 and 1.13 may provide, at most, a limited service. A focus exclusively on the changes to the Model Rules would obscure the more important point of this Article: namely, that the revised provisions of Model Rules 1.6 and 1.13 are merely a backstop addressing extraordinary and deviant circumstances, and that the Task Force's recommendations with the greatest importance to the responsibility and value of the legal profession in public company governance are those that prescribe regular modes of communication and advice among in-house lawyers (particularly the general counsel), outside counsel, and independent members of the organizational client's governing body such as the board of directors.

### **II. THE TASK FORCE'S DEVELOPMENT OF THE MODEL RULES AMENDMENTS**

The Task Force began its work in the spring of 2002 - before WorldCom, Tyco, and HealthSouth joined Enron in the ranks of major corporate scandals, and before Senator Sarbanes and

Representative Oxley became irrevocably conjoined through the enactment of the Sarbanes-Oxley Act of 2002.<sup>6</sup> A wide range of institutions and laws - boards of directors, outside auditing firms, ERISA, the system of accounting regulation, and securities analysts, to name a few appeared to be fair game for consideration in the search for appropriate responses to the corporate scandals. Early in its work, however, the Task Force - being, after all, an arm of an association of lawyers - concentrated its attention on the role of lawyers in the promotion of corporate responsibility. The Task Force's recommendations could not conceivably have won acceptance by the legal profession, let alone the public, unless it at least attempted to assess the adequacy of the legal profession's own rules and practices in relation to public company governance.

The Task Force promptly identified two such rules for review. One rule, Model Rule 1.6, was still relatively fresh in the minds of the Task Force members, since the ABA House of Delegates had less than a year earlier rejected key amendments to Rule 1.6 proposed by the Ethics 2000 Commission.<sup>7</sup> Those amendments, dealing with the lawyer's ability to disclose client information in order to prevent or rectify the consequences of client crime or fraud in limited circumstances, appeared to the Task Force to be responsive to swirling charges that lawyers associated with recent corporate scandals had, at least by silence, failed to prevent the criminal or fraudulent conduct of senior corporate officials.<sup>8</sup> Another rule, Model Rule 1.13, was also the subject of active criticism, most notably in the form of a well-publicized letter to the Securities and Exchange Commission from forty law professors, asserting that Rule 1.13 was too weak and urging that the SEC adopt its own rules of attorney conduct to require that lawyers for public companies bring corporate crime or fraud to the attention of the corporation's board of directors.<sup>9</sup> The suggestion that existing Model Rule 1.13 had failed to adequately encourage or require lawyers to raise concerns about corporate fraud with higher organizational authorities invited reconsideration of that rule as well as Rule 1.6.

#### A. EVALUATION AND DEVELOPMENT OF AMENDMENTS TO RULE 1.6

With respect to Rule 1.6, the Task Force was unwavering, from its earliest meetings, in the belief that the ABA House of Delegates should reconsider and adopt the Ethics 2000 amendments it had recently rejected. Although the public record may not reflect it, that Task Force position ripened into a firm view well before any expression of federal interest in regulating the ability or duty of lawyers to report corporate fraud to the SEC. Senator John Edwards first publicly suggested the amendment that became section 307 of the Sarbanes-Oxley Act of 2002 on June 18, 2002,<sup>10</sup> by which time the drafting of the Task Force's Preliminary Report of July 16, 2002 was in an advanced stage." And, as is surely well known to any reader of this Article, section 307 says nothing explicit about "reporting out" - i.e., disclosure of client information to persons outside of the corporate issuer. It was only on November 21, 2002, after publication of the Task Force's Preliminary Report, that the SEC - somewhat surprisingly, given statements in the legislative debate on section 307<sup>12</sup> - advanced the idea of a requirement of such disclosure.<sup>13</sup> In short, the Task Force's embrace of the Ethics 2000 amendments preceded any post-Enron federal regulatory initiative addressing lawyer disclosure of client information to third parties.

In one significant respect, the proposals in the Task Force's Preliminary Report went further than the Ethics 2000 recommendations to amend Model Rule 1.6. Specifically, the Task Force preliminarily urged that Model Rule 1.6 be amended

to make disclosure [of client information] mandatory, rather than permissive, in order to prevent client conduct known to the lawyer to involve a crime, including violations of federal securities laws and regulations, in furtherance of which the client has used or is using the lawyer's services, and which is reasonably certain to result in substantial injury to the financial interests or property of another.<sup>14</sup>

It was perhaps unfortunate that the Task Force's Preliminary Report did not elaborate on the rationale for this proposal. It could have been pointed out, for example, how extremely limited such mandatory disclosure would have been. For that mandate to apply, the lawyer would have to know the client's conduct is criminal. The requirement would not apply to non-criminal fraud, and the requirement would only apply in order to prevent client crime, and not to mitigate or rectify its consequences.<sup>15</sup> Within the Task Force, moreover, there was sentiment that in such extreme and limited circumstances, mandatory disclosure of client crime would strengthen the lawyer's hand in persuading a client to abandon conduct known by the lawyer to be criminal, and would do so more effectively than mere permission to disclose.

Whatever might have been said in its favor, however, the preliminary mandatory disclosure proposal encountered severe criticism, and was withdrawn in the Task Force's Final Report.<sup>16</sup> What ultimately led to that withdrawal was a concern that mandatory reporting out (disclosure of client crime to a third party) would undermine, rather than elicit, compliance with law. The Task Force acknowledged that an enforceable duty to disclose client information would likely have two counterproductive consequences: first, that clients would choose not even to consult lawyers with regard to questionable conduct; and second, that out of (self-protective) concern about promptly fulfilling a professional obligation to disclose to third parties, the lawyer would forgo efforts to remonstrate with the client or to engage in factual inquiry that might establish the legality of the client's conduct.<sup>17</sup> These perceived consequences of a mandatory disclosure rule, in the view of the Task Force, would have undermined the ability of lawyers to play a useful role in promoting compliance with law by their clients.<sup>18</sup>

What remained, then, in the Task Force's Final Report was a verbatim adoption of the extensions of permissive disclosure recommended by the Ethics 2000 Commission but rejected by the House of Delegates in 2001.<sup>19</sup> Several aspects of these extensions merit brief emphasis:

- \* With the 2003 amendments, Model Rule 1.6(b) permits disclosure to prevent crime or fraud, or to mitigate or rectify consequences of such misconduct, only if the required harm - "substantial injury to the financial interests or property of another" - is "reasonably certain" to result.<sup>20</sup>

- \* The authorization to disclose client information in order to rectify the consequences of past client crime or fraud does not extend so far as to permit a lawyer, having disclosed just enough to enable others (including victims) to rectify such consequences, to provide further assistance in pursuing claims against the client, or to assist in apprehending or prosecuting the client.<sup>21</sup>

- \* Most important, the new additions to Model Rule 1.6(b) permit disclosure of client information if and only if the client has used or is using the lawyer's own services in

furtherance of the crime or fraud.<sup>22</sup> This limitation is the moral and ethical linchpin of the 2003 amendments to Model Rule 1.6. As the Task Force (following the Ethics 2000 Commission and the American Law Institute before it) emphasized, the client's use of the lawyer's services to perpetrate crime or fraud "constitutes an abuse by the client of the client-lawyer relationship, forfeiting the client's absolute entitlement to the protection of Model Rule 1.6."<sup>23</sup>

\* As was the case before the 2003 amendments, Model Rule 1.6(b) does not permit disclosure of client information unless the lawyer "reasonably believes" that such disclosure is "necessary" to achieve one of the permitted purposes for disclosure.<sup>24</sup>

\* As was the case before the 2003 amendments, Rule 1.6(b) allows disclosure of client information only "to the extent" reasonably believed necessary to achieve a permitted purpose.<sup>25</sup>

The Task Force was certainly aware that the lawyer's withdrawal from representation (either permissive or mandatory) may largely or sometimes even fully satisfy any duty (under Model Rule 1.2(d) or otherwise) to refrain from assisting a client in committing any criminal or fraudulent acts.<sup>26</sup> Thus, the Task Force in no way intended to limit or alter existing duties or rights on the part of the lawyer to withdraw as counsel in the face of client crime or fraud.<sup>27</sup>

## B. EVALUATION AND DEVELOPMENT OF AMENDMENTS TO MODEL RULE 1.13

In contrast with its early and persistent advocacy of the Ethics 2000 recommendations with respect to Model Rule 1.6, the Task Force's treatment of Model Rule 1.13 varied substantially through the course of its deliberations, in turn influencing and then being influenced by pronouncements by the SEC in promulgating regulations under section 307. While some elements of the Task Force's recommendations were established early in the process,<sup>28</sup> several of the most substantial elements did not come to rest until the Task Force issued its Final Report, and the most elusive element - defining the trigger for lawyer action under Model Rule 1.13 - was not resolved until the debate on the floor of the House of Delegates.

In its Preliminary Report, the Task Force advanced two principal views with respect to Model Rule 1.13. First, Model Rule 1.13 did not articulate with sufficient clarity the steps a lawyer should take upon encountering misconduct by a constituent of an organizational client.<sup>29</sup> Second, Model Rule 1.13's trigger - the lawyer's knowledge of such misconduct - was unduly restrictive and permitted lawyers to "turn[ ] a blind eye to the natural consequences of what they observe and claim[ ] that they did not 'know' that the corporate officers they were advising were engaged in misconduct."<sup>30</sup>

### 1. SPECIFICATION OF ACTIONS REQUIRED UNDER MODEL RULE 1.13

With regard to the first concern - the lack of clarity concerning the choice of remedial measures - the Task Force's Preliminary Report itself did not supply much in the way of specific clarification. In part this was due to the fact that the Task Force initially preferred not to draft specific Rule amendment proposals. The Task Force phrased its recommendations in considerable generality in deference to the long-standing and ongoing drafting role of the ABA's Standing Committee on

Ethics and Professional Responsibility and in the belief that the Standing Committee would be the appropriate body to undertake specific implementation of the Task Force's more general recommendations.<sup>31</sup> At its most specific, the Task Force's Preliminary Report urged that Model Rule 1.13 be amended so as

to emphasize in the text of the Rule itself that the list of potential remedial measures need not be pursued in sequential order, and that in circumstances involving potentially serious misconduct with significant risk to the corporation, an effort to seek reconsideration by a particular officer or employee that is unlikely to succeed should be bypassed in favor of referral to a higher authority in the corporation.<sup>32</sup>

After the Task Force issued its Preliminary Report, however, the enactment of section 307 of the Sarbanes-Oxley Act of 2002 and the implementing regulations promulgated by the SEC supplied a great deal in the way of prescriptive clarity with respect to the "up the ladder" reporting obligations of lawyers for public companies.<sup>33</sup> Once triggered, the lawyer's duty under the SEC's rules require the lawyer to report directly and "forthwith" to either the corporation's chief legal officer or its chief executive officer.<sup>34</sup> These rules thus do not explicitly afford the lawyer any substantial discretion or flexibility with respect to when or to whom specified misconduct is to be reported.

The Task Force rejected such inflexibility in Model Rule 1.13. Recognizing that the lawyer, upon discovering a violation of law by an organizational client's constituent that is likely to result in substantial injury to the client, must take some action to protect the client, the Task Force concluded that the lawyer should nonetheless continue in such circumstances to exercise professional judgment as to the appropriate way to "proceed as is reasonably necessary in the best interest of the organization."<sup>35</sup> In the interest of overcoming natural reluctance on the part of the lawyer to "go over the head" of the constituent with whom the lawyer may be dealing, however, the Task Force felt that Model Rule 1.13 should more actively encourage such reporting.<sup>36</sup> To that end, the Task Force recommended the creation of a presumption in Model Rule 1.13 itself, namely that reporting to higher authority within the organization is required unless "the lawyer reasonably believes that it is not necessary in the best interest of the organization to do so."<sup>37</sup> Thus, when the lawyer encounters illegal behavior by a constituent of an organizational client that is likely to cause substantial injury to the client, the lawyer must either report that behavior or achieve a reasonable belief that reporting such behavior to a higher authority within the organization is not necessary in the best interest of the organization. While this approach does not necessarily mandate reporting to the highest authority of the organization, it explicitly does require such reporting "if warranted by the circumstances."<sup>38</sup> In all respects, the Task Force's recommendations seek to reinforce the norm and perception that the lawyer is to represent the best interests of the organization, and not any particular officer, director, employee, or other constituent.<sup>39</sup>

## 2. DEFINING THE TRIGGER FOR REQUIRING ACTION UNDER MODEL RULE 1.13

The Task Force's handling of its second principal concern about Model Rule 1.13- the fact that the Rule only requires action when the lawyer "knows" of a violation of law threatening substantial harm to the organization - evolved even more substantially. Initially, the Task Force

recommended in its Preliminary Report that this actual knowledge standard in existing Model Rule 1.13 should be replaced with a requirement that the lawyer take action when the lawyer "reasonably should know" of the specified misconduct.<sup>40</sup> The proffered justification for this change was that "while lawyers should not be subject to discipline for simple negligence, they should not be permitted to ignore the obvious."<sup>41</sup>

This preliminary proposal, however, was the subject of some dissension even within the Task Force. As the Preliminary Report explained, "[s]ome members of the Task Force preferred limiting [the] expansion of Rule [ ] 1.13 . . . to matters that should have been obvious to a lawyer of reasonable prudence and competence given the facts actually known to the lawyer."<sup>42</sup> That expressed preference foreshadowed a deluge of criticism of the Task Force's preliminary "reasonably should know" proposal.<sup>43</sup> Although this criticism took on a variety of forms, its general thrust was that the proposed standard would impose upon the lawyer an amorphous duty to investigate a client's actions in circumstances in which the lawyer may not even be able to insist that the client pay for or even permit such investigation, and that any reporting obligation should arise only from facts actually known to the lawyer.<sup>44</sup>

In its proposed rules under section 307, the SEC entered the debate with a proposal resembling the Task Force's suggestion. As originally proposed, SEC Rule 205.2(e) would have defined "evidence of a material violation" (requiring reporting by the attorney) as "information that would lead an attorney reasonably to believe that a material violation has occurred, is occurring, or is about to occur."<sup>45</sup> In the face of criticism similar to that directed to the Task Force's preliminary proposal to amend Model Rule 1.13, however, the SEC's final rule more closely resembled the alternative approach suggested in the Task Force's Preliminary Report: specifically, the final Part 205 Rules require up the ladder reporting only on the basis of "credible evidence, based upon which it would be unreasonable, under the circumstances, for a prudent and competent attorney not to conclude that it is reasonably likely that a material violation has occurred, is ongoing, or is about to occur."<sup>46</sup> In presenting this formulation, the SEC essentially rejected the "reasonably should know" standard for requiring reporting, explaining that an attorney would not be found derelict for having failed in retrospect to draw an inference of reportable misconduct.<sup>47</sup>

Echoing the evolution of the SEC's position on the trigger for reporting up the ladder, the Task Force's Final Report proposed an amendment to Model Rule 1.13(b) that would have triggered reporting only on the basis of facts known to the lawyer, and only where "a reasonable lawyer, under the circumstances, would conclude" that the specified constituent misconduct is present.<sup>48</sup> The proposed Comment associated with this amendment explained that conduct within a "range" would satisfy the lawyer's duties under the rule - suggesting, in essence, that action would not be required simply because some reasonable lawyer would have found a duty to act, and that no such duty would arise if a reasonable lawyer could have concluded that no action was required.<sup>49</sup> Even this formulation, however, elicited expressions of concern from many lawyers that the "reasonable lawyer" standard would create undue risks of civil liability for lawyers on the basis of hindsight judgments that they had a duty to take action under Model Rule 1.13(b).<sup>50</sup>

In a compromise concluded in the debate on the floor of the ABA House of Delegates on August 12, 2003, the Task Force withdrew its trigger proposal, and consented to an amendment to its resolution on Model Rule 1.13 that left the Rule's existing trigger - the actual knowledge standard

- in place.<sup>51</sup> From the standpoint of advocates of reforms to Model Rules 1.6 and 1.13, this withdrawal was a small (or perhaps null) price to pay for eliciting support on what turned out to be close votes on the proposed rule changes. In the face of known facts demonstrating to any reasonable lawyer in the same circumstances that a client constituent is violating the law in a way that is likely to result in substantial injury to the client, it is likely to be a rare lawyer who will be able to say that he nonetheless did not "know" of such misconduct - especially since knowledge can be inferred from circumstances,<sup>52</sup> and the lawyer may not "ignore the obvious."<sup>53</sup> In any event, the lawyer is required by Model Rule 1.3 to "act with reasonable diligence and promptness in representing [the] client,"<sup>54</sup> and it is surely at least arguable that this duty requires the lawyer for the organizational client to take reasonable steps to prevent harm to the client when any reasonable lawyer would be aware that a constituent's misconduct threatens the client with substantial harm.<sup>55</sup>

### 3. DISCLOSING CLIENT INFORMATION UNDER MODEL RULE 1.13(c) AND (D)

In the public hearings that followed the release of its Preliminary Report, Professor Stephen Gillers called to the attention of the Task Force that its proposed amendments to Model Rules 1.6 and 1.13 failed to address a significant gap in the coverage of the Model Rules: namely, the situation in which an organizational client's highest authority, due to conflict of interest or some other factor disabling it from acting in the best interests of the organization, has resolved to persist in a violation of law that is reasonably certain to result in substantial injury to the client.<sup>56</sup> Under the prior version of Model Rule 1.13, the most that the lawyer in such circumstances could do was withdraw under Model Rule 1.16 - with no apparent effective way to protect the client from misconduct by its own constituents. The authorization of permissive disclosure in the Task Force's proposals to amend Model Rule 1.6 would not necessarily even apply, unless the situation happened to be one in which the lawyer's services were used or being used in furtherance of the violation of law.

The solution embraced by the Task Force and reflected in new Model Rule 1.13(c) is a provision, independent of Model Rule 1.6(b), allowing for disclosure of client information if the organization's highest authority insists on or fails to address a violation of law by the organization, and the lawyer reasonably believes that disclosure to a third party is necessary to prevent substantial injury to the organization.<sup>57</sup> The violation of law must be "clear," and the threatened injury to the organization must be "reasonably certain."<sup>58</sup> The Task Force's Final Report, moreover, reflected the limited context in which the authorization to disclose the organizational client's information should apply. The Final Report emphasized the importance of such authorization in the situation in which the organizational client's highest authority is disabled, due, for instance, to conflict of interest on the part of its members.<sup>59</sup> Indeed, it seems highly unlikely as a practical matter, if not inappropriate, that in the absence of such disqualification or disability, a lawyer for an organization would find it necessary to reveal client information to a third party where the organization's highest authority has, in good faith and in a disinterested fashion, rejected the lawyer's view that an organizational constituent is violating the law in a manner that is reasonably likely to result in substantial injury to the organization.

Nevertheless, the Task Force felt it appropriate to limit even further this authority to disclose the organizational client's information to third parties. New Model Rule 1.13(d) would deny such

authority to lawyers for whom the organizational client's confidentiality is most important; namely, lawyers whom the organization engages to investigate a potential violation of law (who particularly depend on frank communication from client constituents in order to protect the interests of the organization and help promote legal compliance), and lawyers retained to defend the organization or a constituent against claims of violating the law (where an effective defense likewise depends on assurances of confidentiality for the constituents who communicate with the lawyers).<sup>60</sup>

#### 4. ALERTING THE ORGANIZATION'S HIGHEST AUTHORITY TO WITHDRAWALS OR DISCHARGES PREMISED ON UP-THE-LADDER REPORTING

The Task Force's recommended amendments to Model Rule 1.13 in its Final Report included one further element, one that tracked a comparable aspect of the SEC's Part 205 Rules:<sup>61</sup> specifically, a requirement (in Model Rule 1.13(e)) that a lawyer take steps to assure that an organizational client's highest authority is informed of the lawyer's withdrawal or discharge in circumstances in which Model Rule 1.13(b) or (c) requires or permits the lawyer to report to higher authority or to third parties.<sup>62</sup> The Task Force believed that withdrawal or discharge in such circumstances would most likely reflect a serious issue of organizational policy, one that should be made known to the organization's highest authority so that it could address any possibility that a constituent (such as a senior corporate officer) might be obstructing efforts to stop conduct threatening substantial harm to the organization.<sup>63</sup>

### III. THE PRINCIPAL OBJECTIONS TO THE TASK FORCE PROPOSALS

The history of debate within the ABA on the subject of disclosure of client information to third parties has been long and frequently acrimonious.<sup>64</sup> It was therefore quite predictable that the Task Force's proposals to amend the Model Rules elicited highly charged criticism. In the public hearings convened by the Task Force in late 2002, most of that criticism was directed at the preliminary proposals to require (rather than merely permit) disclosure of client information to third parties in certain circumstances, and to require lawyers for an organizational client to report constituent misconduct to higher authority when the lawyer "reasonably should know" of such misconduct.<sup>65</sup> Even after those more aggressive proposals were withdrawn in the Task Force's Final Report, however, there remained vociferous objections to the remaining proposals to amend Model Rules 1.6 and 1.13. Lawrence Fox, widely recognized as the leading critic of the Task Force's Model Rule proposals, went so far as to characterize them as "deeply flawed responses that are totally unwarranted either as a factual or a public policy matter, proposals that will destroy the very core values [of the legal profession]."<sup>66</sup>

The principal concerns invoked by the opponents of the Task Force's recommendations are summarized below, along with brief responses explaining why the Task Force believed that its recommendations, now adopted as ABA policy, will strengthen, not destroy, the "core values" of the legal profession.

#### A. "NEW RULES 1.6 AND 1.13 GUT THE TRADITIONAL SCOPE OF THE ATTORNEY-CLIENT PRIVILEGE"

In a statement that will never be faulted as mild, Larry Fox asserted that the Task Force's

proposals "would systematically change lawyers from trusted counselors to flat-footed detectives turning their keys in various watchdog stations spotted strategically throughout their corporate clients."<sup>67</sup> Somewhat less colorfully, the American College of Trial Lawyers has asserted that the 2003 amendments to Model Rule 1.6 would "destroy[ ] the trust, loyalty, and confidentiality that our legal system requires and assumes," and strip away "the most basic protections of the attorney-client privilege."<sup>68</sup>

These assertions, however, did not impress the Task Force as correct, either historically or empirically. As an historical matter, they overlook decades of actual positions and practices within the profession. As noted elsewhere,<sup>69</sup> the Model Rules have never rigidly required lawyers to maintain the confidentiality of their clients' information. No client reasonably informed of the lawyer's obligations could rationally believe that the confidence of the attorney-client relationship was inviolate. Even with regard to disclosure of client information to prevent or rectify the effects of client crime or fraud, there has hardly been a monolithic insistence by the ABA, let alone the states' own professional disciplinary rulemakers, that such disclosure is unethical.

In 1928, when the ABA first adopted a formal declaration of the lawyer's duty to preserve client confidences in its Canons of Professional Ethics ("Canons"),<sup>70</sup> its declaration included the position that "[t]he announced intention of a client to commit a crime is not included within the confidences which he is bound to respect. he may properly make such disclosures as may be necessary to prevent the act or protect those against whom it is threatened." Another Canon, also adopted in 1928, declared further that

[w]hen a lawyer discovers that some fraud or deception has been practiced, which has unjustly imposed upon the court or a party, he should endeavor to rectify it; at first by advising his client, and if his client refuses to forego the advantage thus unjustly gained, he should promptly inform the injured person or his counsel, so that they may take appropriate steps.<sup>7</sup>

These rules obviously substantially limited the lawyer's duty of confidentiality and permitted a broad range of disclosure of client information to prevent or rectify client fraud. These Canons remained ABA policy until 1969, when they were replaced by the Model Code of Professional Responsibility ("Model Code"). The Model Code continued the thrust of the Canons' limits on the duty of confidentiality. Model Code DR 4-101(C)(3) permitted the lawyer to reveal "[t]he intention of his client to commit a crime and the information necessary to prevent the crime"; and Model Code DR 7-102(B)(1), as originally adopted, required the lawyer, if unsuccessful in an appeal to the client, to "reveal the [client's] fraud to the affected person or tribunal."<sup>72</sup> It was only in 1983 fifty-five years after the adoption of the pertinent Canons - that the ABA House of Delegates came to embrace the restrictive version of Model Rule 1.6 that prevailed as ABA policy until 2003. In short, the argument that the Ethics 2000 and Task Force proposals to amend Model Rule 1.6 would eviscerate the core values of the legal profession was impossible to square with long-standing positions of the ABA itself.

Perhaps more importantly, the argument that the proposals would destroy the attorney-client privilege and the relation of trust between attorney and client was difficult to accept in light of the resounding refusal of the states to adopt the ABA's 1983 version of Model Rule 1.6. That response

was a strong vote of no confidence. Many states that had adopted the language of Model Code DR 4-101(C)(2) simply left that language in place, at least tacitly rejecting Model Rule 1.6.73 The Task Force's Final Report recites that the lawyer disciplinary rules of forty-one states permit a lawyer to disclose client information in order to prevent a client from perpetrating a fraud that constitutes a crime, and eighteen states permit such disclosure to rectify substantial loss resulting from client crime or fraud in which the client used the lawyer's services.<sup>74</sup>

Despite this rather substantial refusal by the states to follow the ABA's 1983 decision, the Task Force was unable to discern any evidence that in the majority of states where the older and more permissive confidentiality rules prevailed, the quality of lawyering and the lawyer-client relationship had been suffering from "lack of candor or client reticence, relative to the experience in the small minority of states that adopted a more restrictive approach like the one reflected in the 1983 version of Model Rule 1.6.75 Indeed, in the debate on the Task Force recommendations, the American Corporate Counsel Association ("ACCA") asserted that the experience of its members in the states with relatively permissive disclosure rules indicated that adopting the Task Force's proposed amendments to Model Rule 1.6 would "do no damage to the preservation of an appropriate and trusting relationship between a lawyer and her client. . . ."76

#### B. "NEW RULES 1.6 AND 1.13 WILL DRAMATICALLY EXPAND LAWYER LIABILITY"

The next concern raised by opponents of the Task Force's recommendations was the fear that, once permitted to disclose client information to prevent crime or fraud, lawyers would be exposed to civil liability if they failed to make such disclosure and the crime or fraud ultimately injured third parties.<sup>77</sup> The experience under ethics rules at least as permissive as those proposed by the Task Force, however, also undercuts the validity of this concern. Despite the breadth of such permission existing for many years under the rules of a large majority of states, no case was cited in the debates on the proposed amendments to Model Rule 1.6 in which a lawyer was found liable for having failed to make a permitted disclosure. Even those who have advocated such liability acknowledge that they seek a change in the law.<sup>78</sup> Contrary to the liability concern expressed in opposition to the 2003 amendments to Model Rule 1.6, the most pertinent precedent suggests the absence of any legal duty on the part of the lawyer to warn third parties of client crime or fraud.<sup>79</sup> In any event, if the law were otherwise, and a lawyer had some legal duty to disclose client information to prevent accomplishment of a crime or fraud, it would seem at least arguable that the Model Rules (specifically Rule 1.6(b)(6), formerly (b)(4)) would already have permitted disclosure by the lawyer, in order to "comply with other law."<sup>80</sup>

Finally, one consideration of lawyer self-interest actually (and appropriately) favored the proposed amendments to Model Rule 1.6. A lawyer whose services are being or have been used to further a crime or fraud is inevitably a potential target for liability, along with the client, for having assisted in the misconduct. Where the client refuses to cease or cure the wrongful conduct, a lawyer committed by rule to confidentiality may be helpless ("noisy withdrawal" aside) to prevent or mitigate damages for which the lawyer herself may be held accountable. The ability to disclose client information to third parties in order to prevent or rectify injury due to client crime or fraud dependent on the use of the lawyer's services may be particularly valuable to the lawyer, rather than harmful, because it may be the only effective way for the lawyer to achieve such prevention or mitigation of damages.<sup>81</sup>

### C. "LAWYERS WILL HAVE TO GIVE THEIR CLIENTS 'MIRANDA WARNINGS' "

In a July 8, 2003 letter to members of the ABA House of Delegates, the President of the American College of Trial Lawyers, urging rejection of the Task Force proposals to amend the Model Rules, cautioned that if such proposals were adopted, "lawyers would have to consider giving Miranda-like warnings to clients at the beginning of consultations."<sup>82</sup> The implication, according to the letter, was that the proposals "would change the lawyer overnight from trusted advisor to potential adversary . . . ." <sup>83</sup>

At one level, this criticism implicates some serious questions: when must lawyers inform their clients of the possibility that the clients' information may be disclosed to third parties, and to what extent do lawyers actually fulfill such obligations?<sup>84</sup> These are questions that deserve further consideration. As criticism of the Task Force's proposals, however, these questions are essentially irrelevant. Rules of legal ethics - including the ABA Model Rules prior to their 2003 amendments, and even California's relatively strict confidentiality statute have always prescribed a variety of circumstances in which the lawyer could, or even would be required to, disclose the client's information to third parties.<sup>85</sup> The Task Force proposals to amend Model Rules 1.6 and 1.13 merely add some additional possibilities, and therefore add at most marginally to the content of any "Miranda warning" that a lawyer should give in relation to the possibility of disclosing client information, either at the outset or during the course of the representation.

### D. "THE TEXAS ETHICS RULES WERE PERMISSIVE, SO NEW RULES 1.6 AND 1.13 WON'T STOP FUTURE ENRONS"

The premise of this argument was that much of the alleged lawyer misconduct associated with Enron<sup>86</sup> was by Texas lawyers, subject to Texas ethics rules that already permitted disclosure of client information to prevent client crime or fraud.<sup>87</sup> Indeed, the Texas rules were in several material respects considerably more permissive than new Model Rule 1.6.<sup>88</sup> Therefore, the argument concluded, the Task Force had failed to make out a case establishing that its recommended revisions to the Model Rules would do anything to prevent the corporate misconduct that the Task Force was assigned to address.<sup>89</sup>

In a limited way, this argument was quite cogent: the Task Force did not and could not credibly maintain that revising Model Rule 1.6 would single-handedly nip all future corporate fraud in the bud. Any such assertion would have been particularly absurd given that the Model Rules have no formal legal effect, and that most state ethics rules already provide lawyers leeway in disclosing client information greater in some respects than new Model Rule 1.6.<sup>90</sup> Clearly, empirical evidence that client crime or fraud correlated positively with severe restrictions on lawyer disclosure of client information would have made a much better case for revision of Model Rule 1.6.

To have insisted upon such proof as a condition to such a revision, however, would have been unreasonably unrealistic. Corporate governance, let alone client behavior in general, is a complex web of overlapping motivations and constraints. A state ethics rule like that of Texas which permits lawyers to disclose client information to third parties to prevent criminal fraud, may exist in a system which otherwise discourages lawyers from making such disclosure due, for example,

to a lack of lawyer independence from corporate management. At a minimum, however, if such disclosure would ever be beneficial - and certainly Enron and WorldCom seem like situations in which it might have been helpful it is surely unhelpful to have a prevailing model ethics rule that flatly prohibits it. While there can be no certainty that changing the prevailing ethics rule to permit such disclosure will head off any client crime or fraud, it is almost certain that a rule prohibiting such disclosure will foreclose any such potentially beneficial result.

#### IV. THE RELATION BETWEEN THE NEW ETHICS RULES AND CORPORATE GOVERNANCE REFORM

The adoption of the 2003 amendments to Model Rules 1.6 and 1.13 has been widely, although not universally, praised as a positive step in professional self-regulation.<sup>91</sup> In a number of ways, however, these amendments, standing alone, are ineffectual and incomplete:

- \* Most obviously, the 2003 amendments affect model rules, not rules enforceable by disciplinary authorities or otherwise. The amendments will only have formal consequences if and to the extent that they are adopted by the states. Moreover, and particularly with regard to rules governing confidentiality of client information, many states already have rules that permit disclosure in circumstances that the 2003 amendments to Rule 1.6 address, so the amendments to Model Rule 1.6 will not likely have a major formal impact.

- \* Disclosure of client crime or fraud to third parties, even where now permitted under Model Rules 1.6 and 1.13, is still permissive only, not required.<sup>92</sup> Whether the new authority to disclose client information will help deter client crime or fraud will depend entirely on how lawyers use that new authority.<sup>93</sup>

- \* Nothing in the recent amendments to Model Rules 1.6 and 1.13 will guarantee that a lawyer confronted by incomplete evidence of client misconduct will recognize that a crime or fraud is under way and take steps to prevent it. Lawyers whose representation exposes them only to limited aspects of the client's affairs will inherently be limited in their ability to use the recent rule amendments, or even to recognize that they might apply.

- \* Even as amended, Model Rule 1.13 is not, as the Task Force explained, "a guide to 'best legal practices.'"<sup>94</sup> Except for its insistent focus on the principle that the organization - rather than its constituents - is the client, Model Rule 1.13 only addresses relatively extraordinary exigent circumstances; as the Task Force explained, Model Rule 1.13 "does not limit the responsibility of the lawyer to act always in the best interest of the organization, and it certainly permits the lawyer to bring to the attention of the client, including its highest authority, matters not covered by the Rule, but which the lawyer reasonably believes to be of sufficient importance that the client needs to be informed of them."<sup>95</sup> Thus, new Model Rule 1.13 will only directly encourage effective representation of the organizational client at extreme margins of constituent misconduct.

Fortunately, the Task Force's recommended changes to Model Rules 1.6 and 1.13 were not submitted in a vacuum; they were recommended only as a supplement, or backstop, to corporate compliance initiatives designed to permit both internal and outside counsel to "more readily and effectively convey to appropriate organizational authorities information and analysis concerning

issues of legal compliance."<sup>96</sup>

The treatment of reporting violations of law to higher corporate authority illustrates this point well. As previously discussed, even amended Model Rule 1.13(b) will apply only in relatively extreme cases. Of far greater practical importance, then, is the establishment of mechanisms that will more generally and effectively promote communication of legal compliance concerns to the senior officers or the members of the board of directors who are in a position to deal effectively with such concerns in the interest of the client/corporation.

Thus, the Task Force recommended the creation of channels of communication from general counsel to independent directors, and from outside counsel to general counsel, that are designed to make "up the ladder" communication of legal compliance concerns comfortable and routine, rather than a confrontational challenge to executives' managerial authority.<sup>97</sup> For example, the Task Force recommended that the corporation's general counsel should, "as a matter of routine," meet periodically with a committee of directors independent of senior corporate management, and that the directors should instruct general counsel to use those meetings as the occasion to report on substantial legal compliance concerns.<sup>98</sup> Regularizing this practice, the Task Force explained, "would to some extent insulate such communications from being perceived by senior executive officers as disruptive," and might even "persuade the CEO to take corrective action or personally report such issues directly to the committee."<sup>99</sup>

Similarly, outside counsel may be discouraged from reporting legal compliance concerns to the superiors of the operational personnel with whom they deal directly. Therefore, it may facilitate such communication if the general counsel were routinely to instruct outside counsel that they are expected to inform the general counsel of situations in which an officer or employee is violating the law or breaching a fiduciary duty to the organization.<sup>100</sup> Such communication would direct information about legal compliance concerns to the person (general counsel) most likely to be best able to investigate and evaluate the matter.<sup>101</sup>

All of this is not to say that the 2003 amendments to Model Rules 1.6 and 1.13 lack practical consequence. They do have a practical significance that may help explain what would otherwise appear to be a paradoxical aspect of the intense debate surrounding their adoption. That apparent paradox is this: on one hand, since these amendments only address model rules, and since most states already permitted disclosure of client information in circumstances addressed by the 2003 amendments to Model Rule 1.6, one could argue that these amendments will do little more than conform the Model Rules to pre-existing practice, and will therefore do nothing to change behavior. On the other hand, if this were the only result of the amendments, why did advocates on both sides of the debate labor so hard over a matter with such little apparent practical significance?

The answer to this apparent paradox is that the Model Rules surely have a symbolic importance and salience to practicing lawyers that may even exceed that of formally applicable ethics rules of individual states. The post-Enron controversy over Model Rule 1.6 may not have directly addressed the formally applicable body of professional ethics rules, but the participants undoubtedly considered the controversy as one fought over the spirit of the profession. At a time when business lawyers, at least, appear to be paying more attention than ever before to the ethical

responsibilities that govern their practice,<sup>102</sup> the highly visible battle culminating in the adoption of the 2003 amendments to Model Rules 1.6 and 1.13 is likely to affect profoundly the way in which such lawyers conduct themselves in relation to their corporate clients and their clients' managers. If the intense dialogue associated with the adoption of those amendments does nothing else, it will have contributed significantly - although surely not permanently - to the "consciousness raising"<sup>103</sup> that the Task Force felt necessary to improve our system of corporate governance and, perhaps as well, the value of the legal profession as a whole.

LAWRENCE A. HAMERMESH\*

\* The author is an Associate Professor of Law at Widener University School of Law in Wilmington, Delaware. he served as Reporter to the ABA Task Force on Corporate Responsibility. The views expressed in this Article, however, are the author's own, and do not necessarily represent the views of the Task Force or the American Bar Association. The author gratefully acknowledges the numerous insights provided by the members of the Task Force on the subject of this Article, and particularly acknowledges the relevant assistance of Professor Curtis R. Reitz, who served as Special Reporter to the Task Force on issues relating to lawyer professional responsibility.

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