Sarbanes-Oxley, the Gatekeeper Initiative, and Other Forks in the Road: Current Issues in U.S. Law Governing Lawyers

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United States Law Governing Client-Lawyer Confidentiality

Confidentiality law applying to United States lawyers is found in three related bodies of law: attorney-client privilege law, the work product doctrine, and the lawyer's ethical duty of confidentiality. The United States attorney-client privilege "belongs" to the client, on the theory that the ethical duty of confidentiality is part of the lawyer's obligation to his client. This contrasts with the concept of professional secrecy of many civil law traditions, which is absolute and cannot be revealed by the lawyer even with the client's consent.

Attorney-client privilege is a creature of evidentiary law and provides when a lawyer can, and indeed must, resist disclosure of communications between client and lawyer if such communications are sought under lawful discovery processes. The privilege covers only communications between lawyer and client. Clients can be asked to reveal the information given to a lawyer if requested to do so under lawful process but cannot be required to reveal what they told their lawyer or what their lawyer told them. A number of conditions must be satisfied for the privilege to apply, e.g., the communications [1] are made confidentially [2] without third parties present other than agents of the lawyer or the client [3] for the purpose of securing and providing legal advice. There are several exceptions to privilege. Notably for the subject today, client communications with a lawyer used by the client to further a crime or fraud are not entitled to the protection of the privilege.

The work-product doctrine protects the work of attorneys developed in anticipation of litigation. The legal standard for work product protection originally was articulated by the Supreme Court in *Hickman v. Taylor*[1] and is now codified to some degree in the Federal Rules of Civil Procedure and the Federal Rules of Criminal Procedure. "Ordinary" work product, including witness statements, is subject to discovery if the inquiring party has a substantial need for the material to prepare for trial and is unable to obtain its substantial equivalent without undue hardship. "Opinion work product," involving the mental impressions of the lawyer, is not discoverable.

The ethical duty of confidentiality, as expressed in ABA Model Rule 1.6, requires the lawyer to keep confidential all material "relating to the representation" of a client, unless it comes within one of the disclosure exceptions in Rule 1.6 or another Rule

[1] *Hickman v. Taylor*, 329 U.S. 495 (1947).

requires its disclosure.[2] All disclosure options found in Model Rule 1.6 are permissive but some state versions of the rule provide for mandatory disclosure in particular circumstances. When Model Rule 1.6 is read with Model Rule 3.3 or 4.1, disclosure can become mandatory. Rule 3.3 requires a lawyer to take "reasonable remedial measures" with respect to a fraud on a tribunal, which can include disclosure of client perjury. Rule 4.1 requires disclosure to third parties if disclosure is necessary to avoid the lawyer's own assistance in a client crime or fraud.

Proposed Amendments to the D.C. Rules of Professional Conduct Regarding Confidentiality

This month, the D.C. Bar Board of Governors (BOG) acted on the recommendations of the D.C. Bar's Rules of Professional Conduct Review (DCRPC) Committee. Those recommendations include enacting the substance of ABA Model Rule 1.6(b)(2) and (3) on client crime and fraud, and the "reporting up" provisions in Model Rule 1.13, but not the "reporting out" option of Model Rule 1.13. The DCRPC Committee recommended adoption of the ABA's Rule 1.6 option for a permissive disclosure option when a lawyer's services have been used to further a crime or fraud and the disclosure is necessary to prevent, mitigate, or rectify reasonably certain substantial injury to the financial interest or property of a third party.

If these changes are adopted, a D.C. lawyer could comply fully with the provisions regarding lawyers in the Sarbanes-Oxley Act with one exception. The excepted situation is when a lawyer representing a publicly traded company had reported up to the higher internal authority, but the lawyer deemed that the highest internal authority had not acted to address the situation. In that instance, Model Rule 1.13(c) would allow the lawyer to "report out" even though the lawyer's services had not been used regarding the criminal or fraudulent act involved. The DCRPC Committee concluded that their proposed amendment to D.C. Rule 1.6 for client crime or fraud using the lawyer's services went far enough with regard to disclosure and hence did not recommend adoption of this provision of the Model Rules.

The Gatekeeper Initiative

We are aware of the Japanese Bar's considerable concern concerning the "gatekeeper initiative" of the Financial Action Task Force on Money Laundering (FATF). A U.S. government interagency working group is charged with developing U.S. policy on the Gatekeeper Initiative for the legal profession, but the U.S. government has not yet developed or passed any legislation or regulation.[3] An Advance Notice of Proposed

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[2] The American Bar Association is a voluntary organization. The Model Rules have no binding legal authority. They are merely "models" for the states. It is codes of the jurisdictions in which a lawyer is admitted to practice that have binding legal force.

[3] ABA Section of International Law, Ad Hoc Task Force on Money Laundering and Professional Responsibility, Comments to the ABA Task Force on Attorney-Client Privilege, May 5, 2005, p. 4. *available at* http://www.abanet.org/buslaw/attorneyclient/publichearing20050421/testimony/laundering3.pdf.

Rulemaking issued by the Treasury Department's Financial Crimes Enforcement Network (FinCEN) in 2003 "made clear that any anti-money laundering requirements that may be promulgated in the future would not include a suspicious transaction/activity reporting requirement."[4] No formal rulemaking proceeding in the Treasury Department has occurred since the 2003 advance notice of proposed rulemaking. The ABA Task Force on Money Laundering and Professional Responsibilities is in active contact with the Department of the Treasury.

The D.C. Bar's Consideration of Confidentiality Provisions for New Professional Conduct Rules; Current Concerns in the ABA

Compliance issues with Sarbanes-Oxley were much more in the forefront of the DCRPC Committee's and BOG's consciousness than those related to the Gatekeeper Initiative, although we have a member of the ABA Ad Hoc Task Force on our DCRPC Committee and the Chair of the Gatekeeper initiative is the law partner of the DCRPC's Vice-Chair.

In September 2004, the ABA created a Task Force on Attorney-Client Privilege, which was charged with making policy recommendations regarding the attorney-client privilege and work-product doctrine. Their initial report, filed with the ABA on May 18, 2005, focused primarily on pressure by prosecutors on corporate clients to waive the attorney-client privilege in order to receive more lenient treatment in sentencing. Some of this concern relates to two memoranda of the Department of Justice on principles of prosecution.[5] The Task Force reports that the SEC has implemented similar policies. A second concern of the May 2005 report is issues relating to auditors and their regulating body, the Public Company Accounting Oversight Board, regarding disclosures by lawyers to auditors. The concern is that some court decisions have held that disclosing privileged documents to outside auditors waives the privilege.[6]

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[4] *Id.* at p. 5 ; *see* 68 Fed. Reg. 17569, 17570-71 (Apr. 10, 2003).

[5] Memorandum from Deputy Attorney General Larry Thompson to Heads of Department Components and U.S. Attorneys, Principles of Federal Prosecution of Business Organizations (Jan. 20, 2003) (available at http://www.usdoj.gov/dag/cftf/corporate_guidlines.htm). The Thompson Memorandum expanded and revised previous policies of the DOJ that were established in a memorandum drafted by former Deputy Attorney General Eric Holder. Memorandum from Deputy Attorney General Eric Holder to Head of Department Components and U.S. Attorneys, Bringing Criminal Charges Against Corporations (June 16, 1999) reprinted in Justice Department Guidance on Prosecution of Corporations, in CRIM. L. REP. (BNA) (1999) (available at http://www.usdoj.gov/criminal/fraud/policy/Charging corps.html) *cited in* ABA Task Force on Attorney-Client Privilege Report to ABA House of Delegates, May 18, 2005, n.68 *available at* http://www.abanet.org/buslaw/attorneyclient/materials/hod/report.pdf.

[6] *In re Pfizer, Inc. v. Securities Litig.*, 1993 U.S. Dist. LEXIS 18215, *22 (S.D.N.Y. December 23, 1993) (90 Civ. 1260).

Relevant Principles in United States Law Governing Lawyers

The following points should be kept in mind regarding American law governing lawyers as it relates to government efforts that are alleged to erode confidentiality.

1. **Confidentiality rights belong to the client.** The confidentiality protections in ethical rules and the privilege "belong" to the client. The policy supporting confidentiality regarding organizational clients is usually expressed as the need for full and free communication so the lawyer can assist the client in obeying the law. Thus, it follows logically that privilege law and the ethical duties do not protect a client's use of the lawyer's services to further a crime or fraud.

2. **American law distinguishes between past conduct and on-going or future conduct of a client, as well as prohibiting assistance in criminal or fraudulent conduct.** A bedrock principle of the ethical rules, found in Model Rule 1.2(d), is that a lawyer cannot knowingly counsel or assist in a crime or fraud. The law governing lawyers distinguishes between a lawyer's role with regard to clients' *past* conduct versus *on-going or future* conduct. A lawyer is ethically obliged to protect a client's secrets with regard to past conduct, and the attorney-client privilege protects communications about such conduct. If the lawyer's services were not used to further that crime or fraud, the crime-fraud exception to privilege and the related exception of Rule 1.6 do not apply. Thus, a criminal defense lawyer may, and indeed is obligated, to keep his guilty client's secrets, and the lawyer is acting ethically in requiring the state to prove his client's guilt beyond a reasonable doubt. When a lawyer is asked to conduct an internal investigation of conduct in which the lawyer was not involved, the lawyer must keep confidential the results of that investigation unless the client wishes to waive confidentiality.[7] Indeed, it is the prosecutorial pressure to force clients to waive the privilege with regard to such investigations that is the ABA Privilege Task Force's main concern.

A lawyer defending a client against criminal or civil charges, or a lawyer conducting an internal investigation, is different from a lawyer counseling a client about the client's current and future plans and assisting in the implementation of those plans. If the lawyer cannot dissuade a client from engaging in a future crime or fraud, the lawyer must withdraw from representation if continued representation would constitute the lawyer's assistance in those plans or otherwise cause the lawyer to violate the law or an ethical rule. Where necessary, the lawyer has the option of a "noisy withdrawal," withdrawing anything previously filed by the lawyer on behalf of the client. With new Model Rule 1.6(b)(2) and (3), the lawyer can go further and disclose confidential information to the extent reasonably necessary to prevent substantial injury to the financial or property interests of a third party when the lawyer's services were used to further the crime or fraud from which they resulted. Comments to Rules 1.6 and 4.1

[7] A lawyer ordinarily should not accept a retention to conduct an investigation of a matter in which his law firm's conduct might be implicated because that likely would present a conflict of interest. An internal investigation at Enron, which included work done by Vinson & Elkins, is one of the bases on which the conduct of both Enron and the law firm have been criticized.

indicate that "to the extent reasonably necessary" means that the lawyer should employ the least drastic means that will achieve the end sought.

3. **Differing policy premises for Model Rule 1.6 and Model Rule 1.13.** While Model Rule 1.6's crime-fraud disclosure provisions are triggered by abuse of the lawyer's services, Model Rule 1.13's policy starting point is that a lawyer representing an organization represents the interests of the organization as a whole, not the interests of an individual constituent such as the president or general counsel. Rule 1.13's obligation on the lawyer to "report *up*" assumes that the highest levels of the organization will act to protect the organization when a self-interested constituent is doing something that would harm the organization. Model Rule 1.13's option to "report *out*" is justified by the notion that the lawyer should act to protect the organization, e.g., the interests of the shareholders, even when the highest authority that can act has failed the organization.

4. **State regulation of lawyers**. The legal authority to regulate lawyers in the United States generally is vested in the highest judicial tribunal in the system in which the lawyer is admitted to practice.[8] To become a licensed lawyer in the U.S., one must have been admitted to the bar of at least one state. Authority to practice in federal courts and before federal agencies and commissions is granted based on a state admission.[9]

Regulation of lawyers is exercised through admission, promulgation of conduct rules, and discipline. While much of the actual work of these processes is done by paid staff and volunteer bar members, these processes operate under the legal authority of the highest court in the state systems.

For example, bar dues paid by the approximately 80,000 members of the D.C. Bar fund D.C.'s bar disciplinary system. In D.C., cases are heard by three-member hearing panels made up of volunteers—two lawyers and one non-lawyer. The panel issues a written report with findings of fact, an application of the facts to law, and a proposed sanction. This is reviewed by a five-member Board of Professional Responsibility (BPR), who are also unpaid volunteers. Serious sanctions are issued directly by the DCCA, and all sanctions can be appealed to the DCCA. Paid staff manage this process, provide assistance to volunteers, and represent the BPR in matters going to the DCCA.

Bar dues also support activities of the D.C. Bar including support for committees such as the Rules of Professional Conduct Review Committee and the Legal Ethics Committee. The DCRPC Committee's recommendations for rule changes go to the Board of Governors of the D.C. Bar, which in turns sends them on to the District of Columbia Court of Appeals (DCCA). The Legal Ethics Committee issues informal

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[8] Many lawyers have multiple admissions—in more than one state and to practice in federal trial and courts Federal agencies generally do not have, for lawyers, a specific separate admission application to practice before them. They do have the authority to, and often do, write their own rules of conduct They also have the authority to administer their own discipline of lawyers practicing before them.

[9] In general, admission to a single state bar will be sufficient for admission to the bar of all the federal appellate courts. By contrast, most federal district (i.e., trial) courts require admission to the bar of the state where the court is located.

opinions interpreting the D.C. Rules, but their opinions do not have the binding effect of law (unless, of course, the DCCA has approved the point in a court opinion). The Board of Governors is elected annually by a mail and electronic ballot of the entire D.C. Bar membership.

Fees paid by bar applicants fund the admissions system. The National Conference of Bar Examiners (NCBE) prepares a number of bar exam test options for the bar exam given in all states in February and November. Individual jurisdictions decide for what part of the bar exam they will contract with the NCBE and whether they will write any of their own portions on their own state's law. Forty-seven states and D.C. also require passage of the NCBE's two-hour Multistate Professional Responsibility Exam (MPRE) given in March, August, and November.

Federal tribunals have separate admission procedures, the authority to make ethical rules, and can exercise their own discipline. In most respects, they look to the rules of their home states in exercising those functions. But it is the Securities and Exchange Commission's authority to make rules for lawyers appearing before them and discipline such lawyers that Congress called upon the SEC to invoke with the passage of § 307 of SOX.

In a major controversy in the early 1980s, then-Attorney General Richard Thornburgh asserted the Department of Justice's authority to "preempt" state ethical rules and promulgate contradictory standards for federal prosecutors with regard to contacting represented criminal defendants (i.e., despite the prohibition of Model Rule 4.2). This raises serious questions of federalism and separation of powers of a type the U.S. democratic system seeks to avoid. By enacting the McDade Amendment, Congress generally required the federal government's lawyers to comply with the professional conduct rules, including those governing contact with represented parties, of the states in which they practice. This issue arises again with SOX and would arise if the U.S. government issued gatekeeper regulations that contradicted state ethics rules.

The original rules proposed by the SEC under SOX would have mandated a lawyer to notify the SEC if he withdrew from representation of a public company for "professional considerations" or made a "noisy withdrawal" of previously filed material. The ABA and other elements of the organized bar forcefully argued that permissive disclosure would better serve the government's objectives. That portion of the proposed rule-making was not implemented (though it remains under consideration by the SEC) and the current SEC regulations only address permissive disclosure options. The ABA Corporate Responsibility Task Force recommendations, which resulted in amendments to ABA Model Rules 1.6 and 1.13, allow lawyers to make all the permissive disclosures to which SOX refers.

A number of states already had ethics codes that allowed this compliance or even went beyond it. Some states have not yet amended their rules to allow compliance with SOX. If a state's rules would not allow the permissive disclosure that the SOX regulations specify, the SEC theoretically could revoke a lawyer's right to appear before

the SEC. Conversely, at least theoretically, a lawyer who disclosed under the SEC regulations could be disciplined by her state bar if the disclosure was not permitted by the state rules.

Ethical issues Arising in Large United States law Firms

Confidentiality issues rarely come up in the day-to-day consultation on ethical issues within a large firm. Moreover, the concerns that do arise tend to be motivated more by fear of civil liability (e.g., for malpractice or breach of duty) than of professional discipline.

The preoccupying concerns in terms of time and attention in large law firms are conflicts of interest and risks occasioned by taking on "unworthy" clients. Conflicts issues arise not only in the context of litigation but also those of negotiation and legislation. For example, may a lawyer negotiate on behalf of one client when the party on the other side of the negotiation also is a client of the lawyer (though not represented by the lawyer in that particular matter)? Conflict issues sometimes arise in the context of corporate families: For example, may a law firm that represents one subsidiary of a corporation simultaneously oppose a different subsidiary of that corporation in another matter? The conflicts rules are stricter where the adverse party is a current (as opposed to a former) client, so there often are disputes as to which category applies.

Because a careless or ignorant lawyer may be drawn into culpable involvement in a client's fraud or other misconduct, the issue of "unworthy" clients also is important to large law firms. This is especially so because often a dishonest client will be without assets to compensate its victims—a circumstance that leads plaintiffs and their lawyers to look to "aiding and abetting" law firms and accountants as "deep pockets" for their clients' recompense.