Ethical Standards for Transactional Lawyers

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Competence, Confidentiality, Privilege, and Work Product

Rules of Professional Conduct

Any analysis of ethics, confidentiality, and the attorney-client privilege should begin in the applicable rules of professional conduct (the "Rules"). For purposes of this article, I will review the applicable sections of the Utah Rules of Professional Conduct. Lawyers in other jurisdictions should do a similar analysis of their rules.

Rule 1.1 – Competence, states that "[a] lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation." The practice of law is increasingly one of specialization, and while I think most of us understand what this means in our core areas of practice, we are often asked to assist a client with something that is slightly outside our area of expertise. The Rules don't require that a lawyer have special training or prior experience to handle a particular matter, including one with which the lawyer is unfamiliar. The Rules recognize that the required level of competence can be achieved by preparation, study, and/or associating with another lawyer who has the necessary experience. But can a non-tax lawyer competently advise a client on the tax code? Can a lawyer competently prepare a tax return for a client? Can a lawyer with no accounting background advise a client on its revenue recognition policies? The answer, of course, depends on the particular facts and circumstances of the situation.

Rule 1.6 – Confidentiality of Information, states that "(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).” (emphasis added). Paragraph (b) lists exceptions to the rule of non-disclosure, including when the lawyer reasonably believes it is necessary 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 and in furtherance of which the client has used the lawyer’s services.”

I want to first highlight that confidentiality applies to information “relating to the representation of a client.” Is an employment litigation lawyer, hired to defend a wrongful termination lawsuit, obligated to keep confidential information he obtains that is not related to that lawsuit, such as whether or not the client timely filed its corporate tax returns?

Second, what is a lawyers obligation if, for example, he is asked to review loan documents on behalf of a client and notices that the client has grossly overstated his income in order to get the loan? Will the financial interests of the lender be harmed, because of a fraud committed by the client, such that the exception to confidentiality described above applies?

Other Rules that may apply are Rule 1.7 – Conflict of Interest: Current Clients, Rule 1.8 – Conflict of Interest: Current Clients: Specific Rules, and Rule 1.9 – Duties to Former Client. The full text of these rules is attached.

<u>Protecting Privilege When Working with Accountants and Tax Advisors</u>

There is a fundamental incompatibility between a lawyer’s duty of confidentiality, and an accountant’s duty of disclosure.

The attorney-client privilege generally protects confidential communications between a client and an attorney when the attorney is functioning as a legal advisor. However, federal law recognizes only a very limited accountant-client privilege. As a general rule, disclosure of the information to a third party destroys the privilege.

Recognizing that lawyers need the help of others in order to competently represent their clients, the court in *United States v. Kovel, 296 F.2d 918 (2d Cir. 1961)* created a framework for the attorney-client privilege to apply to accountants. The court drew an analogy with interpreters, stating that there is ‘privilege when an attorney asks a client to give his story first to an accountant, who then ‘interprets’ the story. An attorney may engage the accountant when the

accountant is 'necessary, or at least highly useful, for . . . effective consultation between lawyer and client.'" While some courts have interpreted the Kovel doctrine liberally, others have put limitations on its application, saying that the doctrine only applies when the accountant's role is to clarify or facilitate communications between the attorney and client, or that if an accountant's advice is sought, not the lawyers, then the doctrine will not apply.

To comply with the Kovel framework, the common practice is for an attorney to hire or engage the accountant, not the client directly. The arrangement is further documented in either the engagement agreement, or in a separate letter (a so-called "Kovel Letter") that clearly designates the accountant as an agent of the attorney and outlines that communications are to go through the attorney and that work product belongs to the attorney. The accountant should clearly be rendering services to the attorney, not the client, for the Kovel doctrine to apply. The accountant's bill should be sent to the attorney, and paid by the attorney, even if they are passed-through by the attorney to the client.

Work Product Doctrine

The work product doctrine generally protects (from third parties) documents and other materials prepared by an attorney in anticipation of litigation. This often reaches further than the confidentiality protections provided by the attorney-client privilege, and covers materials prepared by agents for the attorney (such as accountants retained under a Kovel framework).

In order for materials to be protected by the work product doctrine, they must have been prepared "in anticipation of litigation or for trial, and not in the ordinary course of business." This can sometimes be difficult to prove when there is not yet a lawsuit, summons, or subpoena, so care should be taken to document the reason for the engagement of a third party accountant. In cases where there is more than one purpose, the courts will generally look for the "primary" purpose behind creation of the materials.

Confidentiality and Disclosure

Confidentiality obligations arise in all situations, not just those related to a request for information by a third party, such as pursuant to a subpoena or summons. It applies to matters communicated in confidence by the client, and also applies to all information relating to the

representation, whatever its source. For example, the legal fees charged to a client, the date that representation began, and the status of legal fees paid on the client's account are all the subject of a lawyer's duty of confidentiality.

Lawyers as Gatekeepers

The Sarbanes-Oxley Act of 2002, in the wake of the Enron and WorldCom scandals, attempted to create a duty on the part of lawyers to guide public companies toward legal compliance, including proper disclosure, and to protect the company's stockholders. Since the statute's passage, the Securities and Exchange Commission has brought suits against several attorneys.

Section 307 of the Sarbanes-Oxley Act authorizes the SEC to prescribe "minimum standards of professional conduct" for attorneys "appearing or practicing" before it. Although the initial debate has focused on issues of confidentiality, this terse statutory provision frames and seemingly federalizes a much larger question: What is the role of the corporate attorney in public securities transactions? Is the attorney's role that of (a) an advocate, (b) a transaction cost engineer, or, more broadly, (c) a gatekeeper--that is, a reputational intermediary with some responsibility to monitor the accuracy of corporate disclosures? Skeptics of any gatekeeper role for attorneys have long argued that (a) such a role conflicts with the traditional obligations of loyalty that attorneys owe their clients, and (b) imposing gatekeeping obligations on attorneys will chill attorney-client communications and thereby reduce law compliance.

<u>Conflicts of Interest</u>

There are a variety of situations in which the conflict of interest rules arise. These include conflicts with current clients, former clients, and to a certain extent, anticipated future clients.

The general rule is that the representation of one client shall not be directly adverse to another client, or pose a significant risk that an existing client will be materially harmed by the lawyer's responsibilities to another client, a former client, or a third person. Nonetheless, in certain situations, the representation may be allowed if the client gives informed, written consent.

With respect to former clients, a lawyer shall not represent a client in the same or substantially related matter as a former client in which that person's interests are materially adverse to the interests of the former client, unless the former client gives informed written consent.

Reporting Professional Misconduct (self-regulation of the profession)

In Utah, as in most states, a lawyer with knowledge that another lawyer has committed a violation of the Rules that raises a substantial question as to that lawyer's honesty, trustworthiness or fitness as a lawyer, must inform the appropriate professional authority.

The inclusion of "substantial" allows a lawyer to use his or her judgment, and prevents reporting of minor offenses.

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