LAWYERS AS POLICE?

WHAT'S NEW IN CONFIDENTIALITY

BY DAVID D. DODGE

In case you haven't heard, the Arizona Supreme Court has adopted a new version of ER 1.6 (Confidentiality of Information). That version reflects changes recently added to the Model Rules of Professional Conduct at the American Bar Association's annual meeting last summer. In their most basic form, the amendments allow lawyers under certain circumstances to disclose to third parties, including law enforcement officials, information about their clients' activities that would otherwise be confidential.

This article explores the history of the client confidentiality rules, examines the amendments to the rules as adopted by the Arizona Supreme Court, and concludes that the amendments essentially bring to ER 1.6 a notion similar to the "crime-fraud exception" we all know in the attorney–client privilege cases.[1] With rare exception, the amendments should not materially change the way ethical lawyers practice law.

History of the Rule

A history of the confidentiality rule demonstrates that it has over the years been one of the most controversial issues in the field of legal ethics.[2]

In 1983, when the Model Rules were first being debated, ER 1.6 as originally proposed, like the new ER 1.6, would have allowed lawyers to reveal information to third parties to prevent a client from committing a fraud or crime and to rectify the consequences of a fraud or crime in which the lawyer's services had been used. The ABA Commission on the Evaluation of Professional Standards argued that there was no public interest in protecting otherwise confidential communications that would implicate lawyers in their clients' wrongdoing and that lawyers should not be required to be silent when their services were used to inflict harm on others.

But the American College of Trial Lawyers, an accomplished group of litigators most often associated with insurance defense work, the ABA's Section of Litigation, and others, argued that the

"prevent and rectify" provisions would undermine the lawyer–client relationship. They offered an amendment deleting the provisions. After what was described as a "long and emotional debate," that amendment prevailed as our former ER 1.6.

The issue was revisited in 1991 when the ABA's Standing Committee on Ethics and Professional Responsibility urged the House of Delegates to adopt a "rectification" amendment to ER 1.6 so lawyers would have the discretion to reveal otherwise confidential information to cure the problem of a client misusing a lawyer's services. This suggestion was defeated by a wide margin.

Shortly thereafter, the ABA, in Formal Opinion 92-366, affirmed its position that existing Rules 1.6 and 1.2(d), prohibiting a lawyer from assisting a client in breaking the law, were sufficient protection for the lawyer, and that withdrawal with disclaimers by the lawyer (known as a "noisy withdrawal") was sufficient to protect both the public as well as the lawyer–client relationship. However, the Opinion permitted only such indirect disclosure as the lawyer found necessary to avoid giving assistance to the client's *continuing* fraud. Revelations of a client's past fraud to rectify its consequences were deemed to be improper.[3]

Now enter the ABA's Ethics 2000 Commission and the slowly gathering consensus that the ethical constraints on transactional lawyers dealing with corporate clients might be different from those placed on their litigating brothers and sisters. The Commission, formed to review

and update the Model Rules (after which Arizona has patterned its Rules of Professional Conduct), again recommended "prevent and rectify" exceptions to ER 1.6—but was again overruled.

But then came the Enron, WorldCom and Tyco scandals, prompting the ABA to appoint yet another committee, this one called the Task Force on Corporate Responsibility. As you might have guessed, it recommended a "prevent and rectify" exception that, at its annual meeting in San Francisco this summer, the ABA House of Delegates finally passed, again over objection.[4]

Meanwhile, as the ABA was suffering through its latest case of ethical schizophrenia, 19 states, including Arizona,[5] passed new ER 1.6 provisions, including "prevent and rectify" exceptions. Some of these actually *require* a lawyer to notify authorities in order to prevent a client from injuring the financial interests of third parties.[6]

So now you know how we got where we are. Where do we go from here?

First, Read the Rule

Before we start wringing our hands about the awful things we might be hearing concerning new ER 1.6, let's begin by reading it.[7]

ER 1.6(a) provides that a lawyer shall not reveal information relating to the representation of a client unless the client consents, impliedly allows it or unless such disclosure is permitted or required by paragraphs (b), (c) or (d) which follow, or is required by ER 3.3 (Candor Toward the Tribunal).

ER 1.6(b), one of the exceptions, requires a lawyer to reveal information sufficient to prevent a client from killing someone or causing substantial bodily harm. This is the same as the old rule in effect since 1984. ER 1.6(c), another exception, states that a lawyer may reveal the client's intent to commit a crime and the information necessary to prevent it. Again, this is no different from the old rule. Compliance with ER 3.3, another exception, requires that a lawyer disclose to a tribunal, after other remedial measures have failed, the fact that the client has given false evidence before that tribunal. The new ER 3.3 clarifies some troublesome areas of the old rule, but the disclosure requirement to rectify perjury in a civil case is nothing new.

This leaves ER 1.6(d), the last exception, which has five subparts, three of which essentially restate what the Rules, comments to the Rules or the cases have previously provided—that disclosure of client confidences is appropriate:

- when a lawyer seeks legal advice about his ethical duties pertaining to the client
- to defend himself in disputes with the client over fees, in a legal malpractice case or against charges or claims against the lawyer based on conduct in which his client was involved
- to comply with a court order, such as a subpoena, directing the lawyer to disclose such information

Nothing new here. That leaves the first two subparts to ER 1.6(d), which are new and which have caused the only real controversy involving amended ER 1.6.

New ERs 1.6(d)(1) and (2) and the "Prevent and Rectify" Exceptions

ERs 1.6(d)(1) and (2) provide that a lawyer may (but is not required to) reveal such information, otherwise confidential, and only to the extent the lawyer believes reasonably necessary, (a) to *prevent* the client from committing a crime or fraud reasonably certain to result in substantial injury to the financial interests or property of a third person *and in furtherance of which the client has used or is using the lawyer's services* or (b) to *mitigate or rectify* substantial injury to the financial interests or property of a third person 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.*

Note that the crime or fraud involved has to have been facilitated by the client's use of the lawyer's services. Note further that this critical precondition to disclosure obviates the specter of a lawyer dialing 911 as he fills out the client's new engagement form: The "prevent and rectify" exceptions to ER 1.6(a) presume that a client has by either misrepresentation or concealment tricked the lawyer into being an unwitting participant in a crime or fraud. As the following demonstrates, this is most probably the way an ethical lawyer would find himself in such a predicament.

Next, Read ERs 1.2(d) and 1.4(a)(5)

ER 1.2(d) provides that a lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent. ER 1.4(a)(5) provides that a lawyer must consult with the client about any relevant limitation on the lawyer's conduct whenever the lawyer knows that the client expects assistance not permitted by the Rules of Professional Conduct or other law.

Read together, these rules require the lawyer to avoid aiding or abetting a client in doing a "criminal or fraudulent act" and require that the lawyer so advise the client of those constraints, as well as the limitations on the lawyer's duty of confidentiality found in ERs 1.6(d)(1) and (2).

Then Read ER 1.16

ER 1.16(a) requires a lawyer to withdraw or decline to represent a client if the representation will result in a violation of the Rule of Professional Conduct or other law. ER 1.16(b) allows the lawyer to withdraw if the client persists in a course of action involving the lawyer's services that the lawyer believes is criminal or fraudulent (presumably after the client is advised of the lawyer's ER 1.4(a)(5) limitations), or if

the client has used the lawyer's services to perpetuate a crime or fraud.

So what's the difference? Apparently one of degree.

If the client demands that the lawyer engage in what is clearly an illegal or unethical act, withdrawal is mandatory. If the client is engaging in illegal activities even without the lawyer's assistance, or if the client has misused the lawyer's services in the past and the misconduct has ceased, the lawyer may still withdraw. Withdrawal is the lawyer's basic protection against a dishonest client. The only issue that should remain after such a withdrawal is whether the lawyer should report the client's activities to others, and/or should disavow any work product generated as a result of a client's deception, especially if it's to avoid assisting in the client's criminal or fraudulent act.

Finally, Read ER 4.1

ER 4.1(b) forbids a lawyer, while representing a client, from knowingly failing to disclose a material fact to a third party when such disclosure is necessary to avoid in assisting a criminal or fraudulent act by that client, unless such disclosure is *prohibited* under ER 1.6. Disclosure to prevent a client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another while using the lawyer's services, and disclosure to mitigate or rectify such injuries, are no longer prohibited and are now in fact discretionary.

YOUR LIABILITY WITH RESPECT TO CLIENT DISHONESTY IS NOW MORE HEIGHTENED THAN EVER: IT IS NO LONGER RESTRICTED TO LIABILITY UNDER THE ETHICS RULES BUT MAY TRIGGER LIABILITY UNDER THE TORT SYSTEM TO NONCLIENTS.

This means that, in some instances, just withdrawing from representing a dishonest client may not be enough. Some sort of additional disclosure may be required to protect third parties and, last but not least, to protect the lawyer from claims brought by those third parties if they claim to have been injured by acts about which the lawyer could have warned them. In other words, your liability with respect to client dishonesty is now more heightened than ever: It is no longer restricted to liability under the ethics rules but, as discussed below, may now trigger liability under the tort system to nonclients.

Some New Ground Rules

Let's see where all of this leaves us, and settle on some basic rules.

1. The time-honored rules about confidentiality and privilege still apply when a client comes to you for legal advice concerning what you believe are *past* or *present* criminal or fraudulent acts *not* using your services. This is one of a lawyer's essential purposes.
2. When you discover that your client expects *assistance* from you that is not permitted by the ERs or other law, you are required by ER 1.4(a)(5) to consult with the client regarding the limitations on your conduct. This might also be a good time to remind him of the "prevent and rectify" exceptions to ER 1.6.
3. If, after consultation, your client still insists on pursuing illegal or unethical objectives, look to ER 1.16 and prepare to withdraw. By now, the client should be well aware of your mandatory obligations under ER 1.2(d) not to assist a client in conduct that is criminal or fraudulent.

The final hypothetical is, of course, the present or former client whom you learn has deceived you into unwittingly assisting him in a criminal or fraudulent act, using your services, and which is reasonably certain to result in injury to the financial interests or property of third parties. I use the words "unwittingly" and "deceived" because it is assumed that you would never knowingly consult or assist a client in doing something illegal.

Let's set aside the natural question of how a client who has deceived his lawyer into aiding and abetting an illegal act could conceivably insist that the lawyer not take steps to protect himself and others from the consequences of the illegal act. Where would you perceive your most basic loyalties to be: with a dishonest client who may have exposed you to liability, or to the public and/or to third persons you may have assisted in injuring?

Let's take the easiest example first.

Say you've been misled by a client into putting together a document, like an offering circular or private placement memorandum, that contains false information and that is being relied upon by investors

who are being or may be defrauded. You've determined that what the client has done is criminal or fraudulent. It's too late to dissuade the client as required by ER 1.4(a)(5). In this case, ERs 1.6, 1.16 and 4.1 require you to withdraw from representation and to disavow the accuracy of the documents you have assisted in preparing. The disavowal needs to be effective, which means you may have to find out who has read the tainted documents and make sure they receive your disavowal.

LAWYERS RUN THE RISK OF BEING SUED FOR NOT HAVING DISCLOSED OTHERWISE CONFIDENTIAL INFORMATION SO THAT THIRD PARTIES WOULD NOT BE HURT.

How about the situation where you discover that the client has deceived you concerning certain facts that you have either told others or that you realize you should have disclosed to others but didn't? You've determined that what the client has done is criminal or fraudulent. ER 4.1 would cover this situation because, if the deception was done while using your services and is reasonably certain to result, or has already resulted, in substantial injury to the financial interests or property of others, disclosure of the deception is specifically not prohibited by ER 1.6 and is therefore "disclosable."

How much to disclose is left up to the discretion of the lawyer. Unfortunately, it may take case law to develop some hard-and-fast rules of operation in this area. In both of these situations, the fact that the crime-fraud exception to the attorney–client privilege may require you to testify about your conversations with the client if ordered to do so by a court doesn't answer the question of what you now may have to *voluntarily* disclose under the Rules of Professional Conduct.

Why Bother?

If disclosure of a client's wrongdoing is voluntary, why worry?

Remember, you have a mandatory obligation under ER 4.1 to disclose a material fact to a third person if it is necessary to avoid assisting your client in a criminal or fraudulent act. And, now that disclosure in order to prevent or rectify a client's criminal or fraudulent acts is no longer prohibited, lawyers run the risk of being sued for not having disclosed otherwise confidential information so that third parties would not be hurt. The last decade has seen several lawsuits against lawyers for keeping their clients' fraudulent activities secret, and more will no doubt be filed.[8] The cases that have held lawyers liable to third parties have turned more on the lawyers' aiding and abetting the wrongdoing or not having withdrawn in time. Only one case, using New Jersey law, used a violation of the prevent and rectify rules as a basis for holding the lawyers liable.[9]

A final thought: Even under the old ER 1.6, a lawyer who has been sued has been allowed to reveal confidential information to establish a defense to a criminal charge or civil claim against the lawyer based on conduct in which the client was involved. The "prevent and rectify" exceptions to ER 1.6 simply move up the timing so that the same lawyer can reveal the same confidences concerning the same client to avoid becoming a party in a lawsuit.

Conclusion

Remember that the "crime-fraud exception" to the rules concerning attorney–client privilege merely allows a court to force a lawyer to disclose information about a dishonest client that otherwise would be privileged. The new ER 1.6 and its "prevent and rectify" exceptions go further and may require a lawyer, without a court order, to disclose confidential information concerning the representation in order to prevent or rectify harm his client has inflicted upon others.

Will our clients be shocked by all of this? Probably not. It makes good sense that lawyers shouldn't be helping crooks, the same scenario that the public found so appalling in the Enron, Tyco and WorldCom fiascos. Remember when the Zlaket Rules concerning voluntary disclosures of harmful information came out, and many of us rushed to put warnings of the new rules in our engagement letters so the client would be forewarned? Well, maybe we need to revise the engagement letters again, especially now that the rules require them, to remind our clients that if they deceive us and use our services to hurt someone, they should not look to us for protection.

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endnotes

1. *See Clark v. United States*, 289 U.S. 1, 15 (1933); followed in Arizona in *Buell v. Superior Court*, 391 P.2d 919 (Ariz. 1964); *see also Pearce v. Stone*, 720 P.2d 542 (Ariz. 1986).
2. In writing this section of the article, I have borrowed shamelessly from the treatment found in *ABA/BNA Lawyer's Manual on*

Professional Conduct, pp. 55:108, *et seq.*

3. For guidance on noisy withdrawals, *see ABA Formal Opinion 92-366* (Aug. 8, 1992) (Withdrawal When a Lawyer's Services Will Otherwise Be Used to Perpetuate a Fraud).
4. For a well-reasoned argument against the proposed amendments, *see Testimony of Patricia Lee Refo*, Chair of the ABA's Section of Litigation, Nov. 11, 2002, before the ABA Task Force on Corporate Responsibility, at www.abanet.org/buslaw/corporateresponsibility.
5. *See* Dodge, *The Secrets Lawyers Keep*, 39 ARIZ. ATTORNEY 8 (October 2002) at n.8.
6. Florida, New Jersey, Virginia and Wisconsin.
7. ER 1.6. This and all ERs are available online at http://azrules.westgroup.com/home/azrules.
8. *See Philadelphia Reserve Supply Co. v. Norwalk & Associates, Inc.*, 1992 WL 210590 (E.D. Pa. 1992) (under New Jersey law where lawyers are required to reveal information to prevent financial injuries to others, lawyer for one of the members of a building materials cooperative held liable to third party for failing to disclose information about a bust-out scheme. Evidence indicated lawyer actually participated in a scheme, so it may be a stronger case for an ER 1.2(d) violation); *FDIC v. Clark*, 978 F.2d 1541 (10th Cir. 1992) (action against lawyers for damages suffered in a "heist money scheme" involving purchase by bank officers of stolen money using fraudulent loans from client bank. The scheme was described in allegation in a lawsuit defended by lawyers who relied on bank officers' explanation of facts. Lawyers held liable for failing to investigate allegations of officers' fraudulent activities and failing to disclose allegations to bank's board of directors. As such, it's more of an "up the ladder" reporting failure under ER 1.13); *In re American Continental Corporation/Lincoln Savings and Loan Securities Litigation*, 794 F. Supp. 1424 (D. Ariz. 1992) (cause of action stated against bank's lawyers for violations of conduct governed by ER 1.16, court stating that lawyer must withdraw from representation when his services are being used to deceive others. Court held that lawyer had obligation to actively discuss and discourage illegal conduct with client, urge ceasation of the activity and withdraw if client continues the conduct. As such, this was an ER 1.2(d) violation also); *FDIC v. O'Melveny & Myers*, 969 F.2d 744 (9th Cir. 1992) (lawyers found liable for failing to make an independent investigation of status report of failed bank, done by it accountants and its previous corporate counsel, before assisting in dissemination of misleading private placement memoranda. Liability based on securities laws).
9. *See Philadelphia Reserve Supply Co.*, 1992 WL 210590.