1 MR. JOHN ALLEN: Is there a way you would
2 like me to proceed?
3 CHAIRMAN CHEEK: No, sir, our format is
4 very fluid but I think what we would like to do, we
5 received your written testimony and all of us,
6 I think, have reviewed that and read that so I think
7 that if you would have some preliminary remarks that
8 are related to that testimony or would like to just
9 summarize that testimony for others in the room that
10 may not have had the opportunity to hear your views
11 that would be a good starting point and then we will
12 ask you a few questions.
13 MR. JOHN ALLEN: First of all, I'm John
14 Allen, and I'm admitted to the Michigan Bar and four
15 other jurisdictions but my home is in Michigan.
16 I have served there as chair of the State
17 Bar Ethics Committee and presently the grievance
18 committee; I chair the Tort, Trial and Insurance
19 Practice Section Professionalism Committee; however;
20 I wish to emphasize I'm not here to represent the
21 committees since they have not had the opportunity to
22 consider and act upon these proposals.
23 My views expressed here are personal and
24 only my own.

1 I also want to thank all of you for the time
2 that you take for these very important activities and
3 those that were on the Corporate Responsibility Task
4 Force. I do that with real sincerity particularly
5 because I'm here to tell you that I disagree
6 vehemently with many of the recommendations in your
7 preliminary report but that does not mean we do not
8 appreciate the time spent examining the issues on
9 behalf of our profession and on behalf of our
10 country.
11 I do not engage in the work of the Worldcoms
12 and Enrons of the world, I am not involved in any of
13 those controversies nor, to my knowledge, is my law
14 firm, although we do have well over 100 lawyers and
15 represent a lot of businesses, by the comparison to
16 many of your practices, we are country lawyers.
17 I'm here in part to remind you that when you
18 recommend changes to the rules of professional
19 conduct, those changes apply to every lawyer in
20 America, not just those that are on the front pages
21 of "The Wall Street Journal" or "The New York Times."
22 I have spent a good portion of my career trying
23 myself and also to assist others in obeying those
24 rules.

1 I think too often our profession, because we
2 have jurisdiction over those rules and because they
3 are our legislation, we, like our civilian government
4 counterparts, tend to adopt the hubris that any
5 problem may be solved if we only change our rules.
6 And, in fact, I do not believe that is true.
7 Generally nor specifically in this case.
8 Since the work of the Kutak Commission and
9 the adoption of model rules of professional conduct,
10 those rules have been disciplinary rules, they are
11 not aspirational, ethical guidelines, they are rules
12 by which a person's career may be ruined in fairly
13 short order. They are quasi criminal, they are
14 strict liability. They are not the place for
15 political positions, they are not the place for
16 public relations ploys, they are not the place for
17 negligence standards or terms which are ill-defined
18 or not defined at all.
19 The problems I see, and I restrict my
20 comments not so much to the corporate governance
21 standards as to the amendments to 1.13 and 1.6, and
22 that is these: You are making three crucial changes
23 in each of those rules if you adopt your preliminary

24 report as the final and admittedly, it doesn't have

1 any final language in it, it doesn't tell us what the
2 rules ought to say. But as I read the report, there
3 are three fatal flaws to each of those changes.
4 One is that you are taking away from the
5 lawyer the discretionary authority to reveal
6 information under particular sets of circumstances or
7 once certain thresholds have been met and you are
8 changing that discretionary authority into a
9 mandatory affirmative duty of disclosure to third
10 persons. That, I think, is a frightful error.
11 Because now jurisdictions have been able to
12 experiment, as some 40 of them have, with various
13 thresholds for that third-party disclosure but
14 reliant always upon finally the discretion of the
15 lawyer. So the lawyer could never be disciplined for
16 not making a disclosure. And in certain
17 circumstances, when the threshold could be reached, a
18 disclosure could be made without discipline being
19 applied.
20 The second fatal flaw which both of the
21 proposals demonstrate is that they wish to change a

22 level, a threshold level of knowledge of the lawyer

23 from one of actual knowledge to a should have known

24 standard which by the very English used is an

1 after-the-fact determination. One that I think

2 necessarily involves a good deal of crystal ball use

3 and when combined with a mandatory, affirmative

4 disclosure, which would be violated under the should

5 have known standard puts the lawyer in just an

6 impermissible degree of jeopardy. It also would

7 present the conscientious lawyer with the prospect of

8 setting up a due diligence system to police that

9 should have known standard and I envision us having

10 to go out and hire auditors to devise inquiry systems

11 and sending questionnaires to our own clients about

12 what they are doing, safe in the knowledge that after

13 this is all over and using that hindsight

14 determination, our own personal and professional

15 liability will be on the block if we do not do so.

16 The third flaw that each of the proposals

17 demonstrate is the altering of the threshold. For

18 instance, under 1.6, you wish to alter the threshold

19 and invoke this mandatory duty of disclosure not just
20 in case of serious bodily injury or death but also in
21 terms of what amount to money damages for a fraud.
22 And an economic fraud at that.
23 I would submit that there is probably no
24 one, even people of your esteemed knowledge and

1 experience that would claim to have a controlling
2 knowledge of what economic fraud is in the United
3 States. It is a very, very broad topic. Likewise,
4 the use of crime as a criteria, since practically
5 every fraud now is a crime.
6 If you use the U.S. mail or a telephone or a
7 cell phone more than once, you have become a
8 racketeer and are guilty of fraud. There is almost
9 no circumstance, at least that I can think of, where
10 a business client would not be facing civil
11 liability, that they would not be automatically
12 joined by the poor lawyer or law firm who tried to
13 give them advice along the way where your standards
14 under 1.13 and 1.6 in your report adopted as changes
15 to the model rules and then thereafter implemented by
16 the various state jurisdictions.

17 Likewise, under the 1.13 standard, my
18 problem there is and it is reflective, I think, of
19 what I see winding its way through both of the
20 proposals for 1.13 and 1.6 and that is that you wish
21 for us to have another client, not just the client we
22 have chosen and not just the client that has chosen
23 us, you wish for us to represent the public.
24 In the case of 1.13, it is what you call the

1 shareholders with a publicly sold corporation,
2 I don't know how one would define those interests in
3 a way that a lawyer could represent them. That's
4 simply why when there is a derivative action,
5 usually, usually the same lawyer, the same law firm
6 cannot represent the shareholder bringing the action
7 and the corporation which is a nominal defendant.
8 The conflict would be too profound, it would
9 be impossible to resolve the variety of interests
10 which would be presented by any significant group of
11 publicly sold at least and publicly purchased
12 shareholders, it is difficult enough in a closely
13 held corporation to do it when you're only dealing

14 with two or three shareholders where you can identify

15 them and you can pick up the phone and call them or

16 make an appointment and sit down and have the

17 consultation that is required by 1.7.

18 In the case of a publicly sold corporation,

19 one could never do that and I think we delude

20 ourselves, I think we commit a grave injustice to

21 lawyers to try to tell them that they should try to

22 do that. On the contrary, everything we have done

23 under both the former code and the present model

24 rules, has been to admonish lawyers to distinguish

1 plainly to the client and sometimes to those third

2 parties who they represent and who they do not

3 represent. 1.13 has been very clear in saying we

4 represent the organization unless we do a specific

5 disclosure and obtain the consensus that are required

6 by 1.7 (b). Your proposal runs directly contrary to

7 that. Likewise, I think your desire for disclosures

8 under 1.6 to protect the public are really grounded

9 more in the sort of duty that a public accountant has

10 and rightfully has, to regard, first and foremost,

11 those financial statements and reports being produced

12 by that public accountant are suitable for truthful
13 reading by the public or by third parties such as
14 creditors, or whoever else may be relying upon it.
15 That has never been the duty of a lawyer in America.
16 Our duties to third parties are very limited
17 and particularly where it comes to confidential
18 communications from our clients, the threshold, which
19 is even authorized, just authorized discretionary
20 disclosure have been very, very high and very sharply
21 defined.
22 Your proposal would cloud all of that
23 I think and also make it such that every client would
24 come to believe quickly that whatever they said to

1 their lawyer might well be revealed to third parties
2 based upon a very low criteria threshold and based
3 upon circumstances which they would certainly not
4 contemplate.
5 The true service of the public interest is
6 to preserve the attorney-client privilege, to make
7 clients believe that when they come and talk to a
8 lawyer, that's going to be kept secret except under

9 the most extraordinary of circumstances and,

10 therefore, the lawyer will have an opportunity to

11 admonish that client to obey the law which is what

12 most of us do. And after we do it, most of our

13 clients obey the law and take that advice only

14 because we had the opportunity to give it to them.

15 If they believe we are going to be ratting them out

16 to third parties based upon grounds as flimsily

17 described as a financial fraud, I cannot imagine that

18 any client is going to talk to any lawyer about

19 anything whether they are from Worldcom or Enron or

20 whether they are in to talk to somebody about a

21 traffic ticket.

22 I really think we should be, instead of

23 folding into the movement to do this, folding into

24 the Edward Oxley idea of what we ought to be doing is

1 using the substantial resources of this organization

2 to point out the error of those proposals. And to

3 preserve the attorney-client privilege and the

4 loyalty to one client at a time.

5 I've probably spoken longer than you

6 intended me too.

7 CHAIRMAN CHEEK: We appreciate very much

8 your thoughtful comments and I would like to just

9 begin by trying to explore a couple of things.

10 Obviously, you are correct, the task force

11 did not undertake to provide any specific language

12 with respect to the concepts that we articulated and

13 we purposely left that for further deliberation after

14 we heard reactions to our concepts.

15 So the language that might be applicable to

16 each of those concepts has not yet been formulated

17 and a lot of the points you make could be, I think,

18 considered in connection with the specific language

19 but conceptually we had to make some judgments and

20 conceptually in your articulation, you made some

21 judgments on 1.6 and 1.13.

22 I would like to explore the limits of those

23 judgments.

24 In 1.6 the task force made a judgment that

1 where there was a crime of fraud that would result in

2 substantial loss, financial loss, that there would be

3 mandated disclosure to third parties to prevent that

4 crime or fraud.

5 As you know, the current model rules differ

6 in regard to 41 jurisdictions, I think, is the latest

7 count, where those jurisdictions permit disclosure

8 where there is a crime that involves a substantial

9 financial loss.

10 Is your position, your view that the current

11 model rules that do not have -- that only go to

12 substantial bodily harm, is the right judgment or

13 would you follow the permissive standard that 41

14 jurisdictions do follow and if you follow permissive

15 standard, do you limit it to crime or do you also

16 include fraud?

17 MR. JOHN ALLEN: I think that there is

18 probably reasonable debate about what the threshold

19 ought to be, whether it should include crime beyond

20 serious bodily injury and death even whether it ought

21 to, in some cases, include a financial fraud.

22 I think the real key, though, however, is

23 whether the lawyer is then authorized to use

24 discretion to make a disclosure or whether there is a

1 mandatory affirmative duty to make a disclosure.

2 Because when it is left to the lawyer's discretion as
3 so many things rightfully are under the rules of
4 professional conduct, the lawyer is then able to
5 weigh the various circumstances that are at hand and
6 make a judgment about that. Keep in mind what we are
7 looking at originally here is a set of disciplinary
8 rules. When is the lawyer going to be disciplined
9 for not obeying the rules of conduct of our
10 profession? I think authorizing discretion in that
11 area is -- it is indeed very appropriate and so long
12 as it is discretionary authority, I think you allow
13 the States, as they have in their federalist approach
14 to this, have looked at a variety of different
15 thresholds and experimented with them to see how they
16 work. With the discretionary standard I think most
17 of them work pretty well.
18 Once you use a mandatory affirmative duty,
19 and I think that's really the key and if I have to
20 post one thing I object the most to that's it, it is
21 changing that discretionary authority to a mandatory
22 duty of disclosure because that does two things:
23 Not only does it force everyone to be very narrow in
24 those thresholds and very well defined, much more

1 well defined than I think crime is, all right.
2 I don't think all crimes ought to be included in
3 that, there are too many crimes out there. But with
4 discretion we can use that and decide which ones are
5 the important ones that require third-party
6 disclosure and which ones don't. If you're going to
7 require it, we have to tell people which crimes we're
8 talking about. Not all should be in there. More
9 importantly and we have to face a practical fact on
10 this, the rules of professional conduct are the
11 principal platform for professional lawyers liability
12 in this country.
13 All right. The principal platform. And
14 that they are used repeatedly for that purpose. They
15 form a platform from which expert witnesses can
16 testify to juries, and in which a duty of reasonable
17 care can be fleshed out, at least as a minimum.
18 CHAIRMAN CHEEK: In the context of legal
19 malpractice?
20 MR. JOHN ALLEN: Exactly. If you change
21 that disclosure authority in 1.6 to an affirmative
22 duty, what you have done, in effect, is virtually
23 guaranteed that every time there is a business
24 accused of a fraud in a civil context, the lawyers

1 will be joined in as codefendants. There is going to
2 be almost universal aiding and abetting liability.
3 In hindsight, particularly using a should have known
4 standard, there is no one, no plaintiff that isn't
5 going to be able to survive a Rule 56 motion on that.
6 And that's all you have to do these days in
7 order to give the case worth. That's not what those
8 rules are there for. I fear that's what we would be
9 turning into. The discretionary standard is most
10 important.
11 CHAIRMAN CHEEK: I think there are six
12 jurisdictions that have a mandated version of this.
13 Are you aware of instances in those states in which
14 there have been difficulties that lawyers held to
15 that standard have incurred?
16 MR. JOHN ALLEN: I'm not aware of any lawyer
17 in those jurisdictions being disciplined for
18 violating that rule so I suppose the logical
19 conclusion is that there are no instances of fraud in
20 that jurisdiction. There are no instances where
21 third-party disclosures ever should have been made,
22 all right. I just don't think sometimes the
23 enforcement data on the rules indicates what the
24 effect would be if you enacted it across the nation.

1 CHAIRMAN CHEEK: One other question and I'll
2 open it up for others to ask you questions.
3 As you know, Section 3.07 of the
4 Sarbanes-Oxley bill requires the SEC to set forth
5 minimum standards of questionable conduct including a
6 mandated expanded version of 1.13. How do you think
7 that impacts the way this task force or the Bar
8 should deal with that issue?
9 MR. JOHN ALLEN: Let me start by saying the
10 way I think it will impact client behavior, I think
11 if that is enacted --
12 CHAIRMAN CHEEK: It is.
13 MR. JOHN ALLEN: -- if it is carried through
14 fully all right, and the rules are enacted and put
15 into force and enforced, I think the net effect of
16 that will be there will be fewer clients consulting
17 lawyers about the matters and the simple reason is
18 they will not do it if what all they are doing is
19 gathering together an investigation file for the SEC.
20 They would rather plow through on their own and not
21 tell people.

22 CHAIRMAN CHEEK: The distinction that I
23 would ask you to comment on is that in 1.13 the
24 mandated obligation is all in the corporate client,

1 the organization, it's not the external third
2 parties.
3 MR. KELLER: Up to the board not the
4 shareholders.
5 CHAIRMAN CHEEK: That's correct. Up to the
6 board not the shareholders. If you took that view,
7 would that change your mind?
8 MR. JOHN ALLEN: I think there are a good
9 deal of people, including my colleagues that I
10 discussed the proposal with, to take comfort in the
11 fact that the amendment to 1.13 as described in the
12 report is one that occurs only within the internal
13 organization of the client. I see two problems to
14 it: Number one, 1.13 combined with what you are
15 talking about in 1.6 still brings you to the same
16 result with third-party disclosures being involved.
17 Secondly, I think if it is a mandatory duty
18 again and that appears to be the spirit of the
19 preliminary report, to make it a mandatory duty to

20 take it out of the discretion of the lawyer and to
21 use a should have known standard rather than actual
22 knowledge standard, I think that means that every
23 time the board and management gets sued for anything,
24 no matter what the grounds are, the lawyers will be

1 joined in as codefendants every single time. Why
2 not? We have another insurance policy and a group of
3 assets to execute against, we have standards that are
4 so mushy that use hindsight that have a mandatory
5 duty imposed, that we're almost guaranteed surviving
6 a Rule 56 motion, why not join in the lawyers and the
7 law firms every time.
8 I think we're inviting a problem there that
9 in the end reads out not just that lawyers may be at
10 risk for civil liability, that's not the principal
11 concern, the principal concern is that clients are
12 not stupid and lawyers are not stupid and if you put
13 them in a position where they will create greater
14 grounds for civil liability, they will not consult as
15 often with the lawyer. If the lawyer doesn't know
16 about it then the lawyer doesn't have the duty to go

17 forward. Anybody who has ever represented a criminal
18 defendant who just might have committed the acts of
19 which he or she is accused, knows how the
20 conversations occur and do not occur.
21 That is unrealistic. 1.13 is not the place
22 to make that change. If there are places to make it,
23 it is not a strict liability, quasi criminal
24 disciplinary code to impose that.

1 MR. JACOBS: To follow up on your concerns
2 and I'm the first to acknowledge your concerns,
3 undoubtedly reflect similar concerns for a
4 substantial constituency within the bar.
5 MR. JOHN ALLEN: I cannot say that with
6 certainty but I believe it to be true.
7 MR. JACOBS: I believe that to be the case.
8 But in wrestling with them, particularly your issues
9 on 1.6, let me just tell you some of the problems
10 that I have and see whether you have anything else to
11 say about it. And that's really to determine if you
12 are going to rely on the discretionary disclosure
13 opportunity, what are the criteria that we expect
14 lawyers to use in determining whether to exercise

15 that discretion. It's largely now unaddressed.

16 And in some respects isn't it less

17 oppressive on lawyers to mandate disclosure so that

18 they don't have this wrestling function to perform

19 and also less likely to create disputes with clients

20 because the client will or should understand that the

21 lawyer has an obligation and that this is not an

22 issue for negotiation between the client and the

23 lawyer where there is an even more inherent conflict

24 of interest between the client's desire to have the

1 lawyer behave in a certain fashion with respect to an

2 eligible disclosure and the lawyer's own personal

3 completely undefined discretion as to whether he

4 believes, for whatever reason it may be, whether it

5 is personal ethics, concern about third parties,

6 worries about perception of that lawyer in the

7 community or by others that a disclosure and a

8 prevention of harm are more appropriate.

9 Right now it seems to me we have left

10 lawyers with a more profound dilemma than the

11 problems that you identify, recognizing that neither

12 case is an ideal solution to the problem.

13 The second issue that I'm wrestling with is

14 what should a lawyer do beyond withdraw if a lawyer

15 believes that a client is misusing or abusing the

16 lawyer's services and if, in fact, is the premise for

17 part of the rule, the lawyer has concluded that the

18 fraud or the crime actually relied upon some screen

19 of legal services in order to be accomplished in the

20 first place.

21 And then my third and final question to you

22 is when we come back to the underlying dilemma that

23 we face in this report that is the organization as

24 the client, I think we all have recognized that at no

1 level of decision making for an organizational

2 client, whether it is management level, and whether

3 at the board level, at the independent director

4 level, or at the shareholder level, each of which

5 could apply to a particular decision under normal

6 corporate law principles.

7 At none of those points is the decision

8 always going to be free from conflict of interest or

9 from multiple interests by a client representative.

10 Who is it that you would say, if you don't

11 like it to be the shareholders, who is it that the

12 lawyer for the organization should be looking to as

13 the organization's authority for instructing the

14 lawyer? Now, that's several questions and I

15 apologize.

16 MR. JOHN ALLEN: There are a few there and

17 none of them are particularly easy. I think when you

18 have a client, be it an organization or not, just as

19 the client chooses the lawyer, the lawyer doesn't

20 choose the client. The client should have

21 substantial discretion in telling the lawyer how to

22 operate with the client. And so when the

23 organization tells the client, deal with Mr. or

24 Mrs. Whoseit over here for your direction, I think

1 the lawyer is entitled to rely upon Mr. and Mrs.

2 Whoseit for that discretion within very, very broad

3 parameters.

4 The other questions touch upon what is the

5 essential core that I see weaving its way through not

6 only Sarbanes-Oxley but also these proposals and

7 that's a very stalwart attack on the attorney-client
8 privilege.
9 Generally speaking, I don't think anybody
10 likes secrets in our society, likewise, people don't
11 like the idea, I say "people," generally when you ask
12 them, they don't like the idea that other people can
13 go to a lawyer and talk to the lawyer and have that
14 talk be in secret and the lawyer not be required to
15 reveal it, particularly for it being helpful in
16 prosecuting a criminal or in curing a fraud or in
17 compensating damage that has occurred. And gracious
18 only knows, we can probably make all trials a lot
19 shorter if we called all the lawyers involved as
20 witnesses and required them to testify under oath as
21 to everything they knew about their clients. That
22 would be a very efficient way of enforcing the law in
23 those instances.
24 But our law and the law of our

1 English-speaking forefathers for generations before
2 us, has placed a very, very high value, has given a
3 privilege to those conversations. And it has
4 privileged them above the law, put them above the

5 rest of the law, it deemed, not for the protection of
6 lawyers and not for the protection of clients. The
7 reasons are plainly stated in the comments to 1.6 and
8 the reasons are, if people know they can speak with a
9 lawyer confidentially, then they will ask the tough
10 questions, they will reveal the facts that are
11 necessary and give the lawyer an opportunity to give
12 advice to obey the law which the lawyer must do and
13 which I believe lawyers do do.
14 And I believe in most instances once the
15 clients understand what the law is, they obey the
16 law. And that's the principle behind the privilege.
17 That it serves the public interest and serves the
18 interest of society to make that privilege as
19 ironclad as possible.
20 Now, when do we deem the interest of third
21 parties superior to that? Under the model rules,
22 really in only two instances and that is when the
23 bodily injury or death may result. Now that's
24 probably not something that most corporate lawyers

1 run up against every day but ask somebody that does

2 divorce cases, all right. They've had that instance,

3 that's real, that happens, but just because someone

4 in the middle of their divorce says, "Boy, if I had

5 the opportunity, what I would do to him or her,"

6 doesn't mean you pick up the phone and dial 911

7 immediately. Why? Because you have discretion. You

8 have the discretionary authority to do it.

9 What do you do? You weigh the

10 circumstances, how you know that person, what you

11 know with about their history. What you know is the

12 likelihood of what they would do. Does that lead you

13 to an absolutely positive sure answer? No, certainly

14 not. As you said, Mr. Jacobs, you struggle. And

15 lawyers struggle with those rules of professional

16 conduct every single day. In the preliminary

17 comments it says every difficult ethical question a

18 lawyer has involves three competing considerations,

19 first and foremost the client, sometimes the public,

20 sometimes the interest of the lawyer in wishing to

21 earn a decent living and to remain an upstanding

22 person and virtually every one of those rules has

23 those considerations winding through it that the

24 lawyer has to balance. I'll tell the same thing I

1 tell students here at Northwestern when I have a
2 chance to talk to them and they say "what do I do
3 when I go to my summer courtship and I think that
4 someone at the law firm is disobeying the rules of
5 professional conduct?" Do we explain to them how we
6 go about that. They said if we bring it up isn't
7 there a chance that you may be fired? To that the
8 answer is yes. Do I want to take that risk? The
9 response if you don't want to take the risk don't be
10 a lawyer, be something else. There are many
11 honorable jobs where you are not burdened by the
12 rules of professional conduct and the struggles
13 within them. To the extent we can give people
14 perfect answers, and easier answers great. Most of
15 the rules don't work that way. Look at 1.7 and 1.9
16 on conflict. Very complex analysis. We tried to
17 give people fact-based tests to work their way
18 through and the comments tell you in the first
19 instance we must rely on the judgment of the lawyer
20 to administer the rules. I do not think putting a
21 rule in that says that you have an absolute duty on a
22 should have known basis of knowledge to reveal even
23 what might likely result in an economic fraud. If
24 you think will reduce the conflict between lawyers

1 and clients I'm sorry, Mr. Jacobs, I disagree. I
2 think it will increase the controversies or claims
3 whatever you want to call it between lawyers and
4 clients. Again, I think the first and most important
5 is that clients will stop talking to us and bringing
6 us the hard issues and stop bringing us the things
7 that come when the demons arrive in their dreams at
8 night and they come up with some bizarre idea about
9 what they want to do and they are smart enough to
10 bring it to the lawyer. In the final analysis it's
11 like raising my kids. As a lawyer the only thing I
12 get paid for is to say no. My clients can figure
13 out, yes, like my kids all by themselves. They don't
14 need help with yes, they come to me knowing that
15 sometimes I'm going to tell them no, but they know in
16 the course of doing that whatever they tell me about
17 the underlying facts will be absolutely private,
18 confidential and privileged above the law. Unless it
19 involves something as serious as bodily injury, death
20 or the commission of a crime.
21 And I think that's a good rule, we have been
22 through this with Ethics 2000. We looked at it for a
23 period of years and the most controversy being in
24 this area and I think arrived at a reasonable

1 conclusion.

2 CHAIRMAN CHEEK: We have ten minutes.

3 MR. MUNDHEIM: You have given an eloquent

4 presentation on a set of recommendations which I

5 think are not in the report. I want to read to you

6 the recommendation in the report and see whether or

7 not -- because I think it is a lot narrower than what

8 you said. See whether you still feel as passionately

9 about it.

10 If you look at Page 32 of the report, it

11 says that the task force recommends amending 1.6 and

12 making disclosure mandatory. This is the only place

13 it goes beyond -- in order to prevent client conduct

14 known -- not should have known -- known to the lawyer

15 to involve a crime. "In furtherance of which the

16 client has used or is using the lawyer's services,

17 and which is reasonably certain to result in

18 substantial injury." That's a lot narrower, that

19 doesn't come anywhere close to the situation that you

20 posited of a wife saying "I'm going to kill my

21 husband." Look back in the way that the report

22 phrases its recommendation. Are you still so

23 passionately against it?

24 MR. JOHN ALLEN: If indeed you are going to

1 retain the actual knowledge standard, I commend you

2 and I think that's a wonderful idea. If that's the

3 intent of the report, marvelous.

4 MR. MUNDHEIM: It says no.

5 MR. JOHN ALLEN: If indeed it is to be a

6 mandatory duty of disclosure, it still concerns me

7 greatly.

8 MR. MUNDHEIM: Even where it is limited to

9 situations in which the client has used or is using

10 the lawyer's services because under those

11 circumstances any way you have to do something.

12 MR. JOHN ALLEN: Well, indeed I do not think

13 the lawyer can participate in that knowingly, no

14 doubt about that. No doubt about that. But whether

15 that involves a mandatory duty of disclosure to third

16 parties is another matter all together because what

17 you are -- I think in part the result of that would

18 be that there also might be a tendency on the part of

19 some lawyers to say that threshold has not been

20 reached. Maybe I'll stay in the deal.

21 I don't think that's a good result either. By

22 allowing it to be something which is discretionary

23 authority about revelation. Frankly as a practical

24 matter is much easier for the lawyer to say "so long,

1 I'm not part of this anymore. Good-bye." And all

2 they have to do is leave.

3 Under your proposal, they would not only

4 have to leave but if it were circumstances sufficient

5 to require the withdrawal, then I'm afraid that -- I

6 don't see how the lawyer in good conscience could do

7 it without reporting it to a third party. Because

8 both of the thresholds seem to be the same.

9 MR. MUNDHEIM: Let me push you one step

10 further. One of the things that you also articulated

11 is extending the grounds to substantial injury of a

12 financial sort. You said that weights incorrectly

13 the value confidentiality and financial harm.

14 MR. JOHN ALLEN: Especially when combined

15 with an affirmative duty of disclosure, yes.

16 MR. MUNDHEIM: Well, now, tell me how that

17 fits in with what is in the rule now that allows one

18 to forego the privilege of confidentiality in a fee
19 controversy with a client. Why is that so much more
20 important than the ability to protect third-party
21 financial investors?
22 MR. JOHN ALLEN: Only because it is put
23 there in the rule, I'm not here necessarily to defend
24 the text of every word that's in the present rule.

1 And there may be good reason why lawyers should not
2 be able to reveal, but, again, it is not something
3 where it is mandatory, it's not mandatory that the
4 lawyer reveal all privileged facts in the fee
5 controversy. It is only a discretionary authority to
6 do it and only to the extent necessary in the
7 lawyer's judgment to enforce the debt. That's a lot
8 different than saying you have to call up the SEC
9 which is essentially what your proposal says.
10 MR. McCALLUM: Let me make a comment.
11 We, in getting this report out, were under
12 some time pressure, we were not quite as clear as we
13 should have been what I thought it said, what it
14 intended to say was, as to the fraud exception,

15 we recommended what Ethics 2000 recommended which

16 would have been permissive but not mandatory

17 disclosure to prevent or rectify the financial

18 results of a crime or fraud in which the lawyer

19 services have been used. What Bob read, the somewhat

20 -- the mandatory only gets to the much more narrowly

21 crafted and defined exception and you have commented

22 on that. But if that were dropped and we retained

23 the feeling that that the House ought to reconsider

24 and act affirmatively now on the two proposals that

1 were rejected, the Ethics 2000 proposals, how would

2 you feel about that?

3 MR. JOHN ALLEN: But to leave it in with

4 discretionary authority?

5 MR. McCALLUM: Ethics 2000 it was permissive

6 not mandatory.

7 MR. JOHN ALLEN: As I mentioned before,

8 I think if the authority to disclose and keep in mind

9 this is disciplinary code. What you are saying is

10 you have permission to disclose, you will not be

11 disciplined with these various criteria. That makes

12 excellent sense. Not only does it prohibit it from

13 being corrupted into a civil liability platform,

14 which I think an affirmative mandatory duty would be.

15 But it gives the various state jurisdictions an

16 opportunity to experiment as they have already done

17 with underlying criteria to see what works well and

18 what doesn't. What is appropriate to test against

19 the value of the privilege and what is not.

20 MR. McCALLUM: One follow up here, we may

21 not have time to debate it at length here, you may

22 want to think about it. On the definition of

23 knowledge, where we address that is in 1.13, 1.2 and

24 4.1, and the standard in the rules and those three

1 sections now is that the knowledge standard which

2 is 1.0 (f) definition, knowingly known or knows. And

3 we debated whether we should go to 1.0 (j) which is

4 in our proposal which is the reasonably should know

5 standard. Or whether we should craft something in

6 between knows and reasonably should know and

7 the -- the issue we were wrestling with is this: How

8 do you deal with the lawyer who turns a blind eye,

9 willful ignorance, and it's there in front of him but

10 chooses not to see it? Now, some say that's already
11 comprehended within the definition of knowingly or
12 known but as it says knowledge may be inferred from
13 circumstances and you may feel that and I would be
14 interested in your views or you may feel there may be
15 some merit in looking at something in between the
16 reasonable should know which we recognize did hint
17 the need to maybe do some investigation, and a
18 standard that says you don't have to do it but you
19 cannot ignore what is in front of you.
20 MR. JOHN ALLEN: Part of the problem is what
21 you noted in your introduction to your remarks, you
22 were in a hurry with this. I think if there is one
23 rule or principle that ought to abide by considering
24 amendments to the model rules of professional conduct

1 it's not the place to be hurried.
2 MR. McCALLUM: We intended that there would
3 be comment, that is we intended that this is not our
4 final report, maybe you missed that point.
5 MR. JOHN ALLEN: I understand that, however,
6 it is being billed by the general news media and if
7 you don't know by your colleagues here in the

8 profession, as something that had to be ginned up in
9 a hurry to try to balance off the political pressure
10 at hand with Sarbanes-Oxley and secondary to the
11 Enron, Andersen fiasco.
12 I do think there is a concern on the part of
13 your colleagues in the profession that very vital,
14 profound, fundamental changes to the attorney-client
15 relationship and the privilege, the loyalty to an
16 organizational client are being considered. And they
17 are being considered largely in reaction to items in
18 the popular press. Items in the popular news, as
19 opposed to this sort of very deliberate and I think
20 appropriate study done by the Ethics 2000 Commission
21 in approaching that. That brings me to the problem
22 of knowledge. And that is this is a strict liability
23 quasi criminal code that is intended for the
24 discipline of the lawyers who do not obey the

1 standards of the profession. To introduce a should
2 have known standard which by the English words
3 involved is a let's look back after it is all over
4 and see what somebody should have done back then.

5 I think that it implies something that is
6 different than a quasi criminal strict liability code
7 and as a lawyer -- I run our firm's quality control
8 committee. If you were to enact that rule, I can
9 tell you right now we would be forced to sit down and
10 say "What do we have to do to fulfill a should have
11 known standard?" I suspect what we have to do is
12 some form of due diligence. That means that every
13 time we talk to a client in the circumstances that
14 give rise to the threshold of the rule, including
15 financial fraud, we have to ask some questions and do
16 some investigation ourselves of our own client. And
17 I think in that circumstance, it's not appropriate
18 and it is not what we ought to be doing through this
19 code. Maybe you want to enact a congressional
20 statute for lawyer's civil liability. Maybe you want
21 to raise again aiding and abetting liability under
22 the securities laws. There are all sorts of ways to
23 approach that problem but if I have one message to
24 bring you today, the rules of professional conduct

1 should not be the vehicle.
2 MR. McCALLUM: You don't have a response to

3 my particular question?

4 MR. JOHN ALLEN: If you want to catch the

5 lawyer who doesn't have absolute knowledge but maybe

6 should have checked more?

7 MR. McCALLUM: Not really.

8 MR. JOHN ALLEN: Or whose approach to

9 something is close his eyes and ears to it?

10 MR. McCALLUM: Yes.

11 MR. JOHN ALLEN: Again, I think if you are

12 going to move, that may be a very, very desirable

13 idea. A strict liability quasi criminal disciplinary

14 code is not the place to do it.

15 CHAIRMAN CHEEK: In fairness to others we

16 need to move on. Ms. Hennessy has one short

17 question.

18 MR. JOHN ALLEN: You have been indulgent.

19 MS. HENNESSY: I would like to focus on 1.13

20 and ask whether you believe in the situation where

21 the lawyer is advising management and is unable to

22 persuade them away from a course of conduct that the

23 lawyer knows is fraudulent, should the lawyer go to

24 the board?

1 MR. JOHN ALLEN: Well, again, you say
2 fraudulent and these things are very circumstantial,
3 they are --
4 MS. HENNESSY: No, just let's assume they
5 know it is a crime. Let's make it a crime. He knows
6 it is a crime. Should the lawyer go to the board?
7 MR. JOHN ALLEN: First of all the lawyer
8 cannot participate in that at all and it could be
9 that even going to the board might end up being
10 participating so the first decision the lawyer has to
11 make is can I be around here any longer. His duty is
12 to the organization not to management. It is not in
13 that sense even to the board although ultimately it
14 gets to that point, and, yes, I think the first thing
15 you do is the same thing you do with any client who
16 says anything that is wrong. You have a talking to
17 what we call it, you call it remonstration is the
18 fancy word in the comments. Back where I come from
19 you sit down and you have a talking to with that
20 person and say, "That is wrong," and if you keep on
21 doing it, I'm going to have to do some things myself
22 and I have to start out going to your boss, I don't
23 run to the board the first time but I figure out who
24 the supervisor is and look at the corporate wire

1 diagram and do the same thing the Army taught you to
2 do when it was time to face an order that was illegal
3 and that is you go up the chain of command. You do
4 not run to the board, you don't run to the newspaper.
5 You don't go to the SEC or cops. There are a lot of
6 steps along the way before you get there. Your
7 client is the organization.
8 CHAIRMAN CHEEK: Thank you, Mr. Allen.
9 Thank you.
10 MR. JOHN ALLEN: We appreciate all of your
11 help.