Without Prejudice
CLIENTS AND CONDUCT
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ETHICAL CONFLICTS AND IN-HOUSE COUNSEL

The global financial crisis has prompted much discussion over the past few months, and as the community engages in debate about how to cope with the growing debt corresponding discussions have been taking place about who is to blame. Fingers are being pointed everywhere and everyone is talking but the discussions took a controversial turn on 26 January this year when a UK newspaper, *The Guardian*, published an article entitled "25 people at the heart of the meltdown." The article identified, as the title suggests, 25 individuals that caused the crisis, for the first time publicly named and blamed. Since being published the article has sparked an array of comment and blogging about who really is to blame – and as the discussions have developed the list of people facing condemnation has expanded considerably and now includes the lawyers. As Richard Ackland recently stated, "every other professional and quasi-professional group is in the frame….why not toss lawyers in as well?"

Ackland's comment may not be as facetious as it suggests. The legal profession is more than indirectly involved in the financial crisis. The lawyers were the ones who advised on the deals, approved the paperwork and facilitated sometimes questionable transactions. Commentators have estimated that by the end of this year over 630 lawsuits related to the sub-prime meltdown will have been filed in federal courts in the United States alone since the crisis arose. Similar lawsuits will invariably be filed in Australian courts. Allegations against lawyers may include failure to disclose, unfair and deceptive trade practices, discrimination, fraud, insider trading, failure to monitor, misrepresentation, negligence and breaches of fiduciary duties. A large number of these may include claims against in-house counsel, who will attract much greater scrutiny of their role. This is not surprising especially when one considers the proliferation of the use of in-house counsel and the difficult position they hold.

Over the past decade there has been a considerable increase in the size and sophistication of the modern in-house legal department. This increase is, according to commentators, the result of the proliferation of transnational legal practice, the rising costs of legal services, an increasing number of claims against lawyers and complex professional regulation. Today some in-house counsel sit on the board of directors and are considered among the top officers of the company. Chairman have much greater expectations of in-house counsel in helping them to discharge their duties than ever before. As a result in-house counsel are expected to have business acumen and maintain current awareness regarding corporate governance and risk issues. They are also expected to maintain open communications with other business units and be "in the know." In-house counsel today have become, in effect, gatekeepers of the corporate community.

ETHICAL CONFLICTS AND IN-HOUSE COUNSEL *continued*

The term "gatekeeper" was first used by Professor Reiner Kraakman to describe the role of professionals in corporate reporting and the capital markets. Kraakman used the term to describe the function of outside directors, accountants, lawyers and underwriters in using their good reputation to prevent corporate misconduct. As third parties they are uniquely placed to act as private party monitors on behalf of the market, by withholding a specialized good, service or certification needed for the misconduct to be permitted. The concept was revitalised in the Enron debacle, with some concluding that the failure of Enron was more a failure of "gatekeepers" than the Enron Board. Since Enron, the use of in-house counsel as gatekeepers has increased considerably, particularly in the United States since the passing of the *Sarbanes-Oxley Act 2002*.

Section 307 of the *Sarbanes-Oxley Act* requires counsel who discover credible evidence of a material violation on the part of an issuer or its agent to report the evidence "up the ladder" within the issuer to determine whether an "appropriate response" has been undertaken. These rules can act as a "safe harbour", permitting counsel who follow them to equate them with the due diligence standard to which they will be held. In-house counsel can face a wide array of penalties if they fail to carry out their compliance duties. The American Bar Association has further defined the duties of the in-house counsel, instructing them to act in the best interest of their employer when dealing with illegal conduct by executive officers.

As gatekeepers, in-house counsel today represent the moral conscience of their organisation. This is not a role that in-house counsel have readily embraced. It is a demanding and challenging role especially if one's continued employment may be in jeopardy. In assuming the gatekeeper role in-house counsel are however in a position to ask questions that are rarely asked like – just because it's legal, should it be allowed here? How is the public served by our behaviour? How would this look on the front page of the newspaper? If allowed, will other employees see it as an excuse to go farther? Is there any reason preventing us from erring on the side of caution and taking the high road? Asking such questions can however become difficult if there is tension between the desired ethical behaviour of employees and the commercial and business goals and objectives set by senior management.[1]

In-house counsel can experience situations where they are asked by both junior and senior employees to do something that raises an ethical dilemma. A common source of conflict is when employees ask in-house counsel for advice about an issue personal to them (e.g. reviewing an employment contract). Other common dilemmas include a CEO who is reluctant to disclose information relevant to an upcoming vote by the board and asks in-house counsel not to disclose the information; or a CEO's request that the in-house counsel generate business or garner political favour by using his/her legal contacts. Another common dilemma is a CEO's request that in-house counsel serve on a committee tasked with the responsibility of overseeing or governing an activity, which the in-house counsel, had helped design or implement. Similarly what about the situation where in-house counsel is asked to draft a document in a way that achieves a successful outcome for the corporation. Knowing that the obligation of an in-house counsel is to the organisation as "the client" but that there is a higher duty to the administration of justice – what should the in-house counsel do in each of these instances?

Notwithstanding the fiduciary obligation of loyalty that stems from the lawyer/client relationship, in-house counsel must reject the corporation's requests if they undermine their primary duty to the administration of justice and the rule of law. With this in mind there are questions in-house counsel should ask to ensure that they are not putting their position in jeopardy:

1. Who is your client?
2. Am I being asked to give advice to someone other than my actual employer?
3. Do I have a personal interest in the matter I am being asked to give advice on?
4. Am I being asked to give advice that is against the law?
5. Is the communication subject to legal professional privilege?
6. Where do my duties lie?
7. Is it appropriate for me to give advice on this matter or should I obtain independent advice?

In-house counsel should also recall the best practice guidelines "Ethics for In-House Counsel" published by the Australian Corporate Lawyers Association in conjunction with the St James Ethics Centre.

[1] K.S. Yates, an in-house lawyer's perspective on ethics, (2005) Texas Bar Journal at p. 922

OLSC WEB/ON-LINE SURVEYS

The OLSC has developed three short web based or on-line surveys that will enable us to obtain feedback from those who have had access or contact with the services of the OLSC. The three surveys we have developed allow complainants who have accessed the OLSC's services, practitioners who have been the subject of a complaint and users of the OLSC website to provide information about their experiences.

The complainants' satisfaction survey for example, asks complainants about their experience with OLSC staff and if contacting the OLSC was worthwhile. The practitioners' satisfaction survey, for example, asks practitioners whether they were happy with the way their complaint was dealt with and whether they were given enough time to deal with the complaint. The survey on the OLSC website asks respondents about the effectiveness and ease of using the OLSC website.

The surveys are quick, user-friendly and completely confidential. We will not know and have no way of knowing if you have completed a survey unless you choose to tell us. The surveys will assist us in reviewing everyday practice to ensure efficiency and effectiveness and will help us achieve our goal of promoting high standards of conduct in the delivery of legal services.

We will publish and regularly update the results and as a matter of transparency to enable people who have given us feedback to compare their feedback with the feedback others have given us.

The surveys can be accessed at **http://www.lawlink.nsw.gov.au/olsc**

RECENT PAPERS

LEGAL EDUCATION AND THE 21ST CENTURY LAW GRADUATE

On Thursday 16 October 2008 the Legal Services Commissioner presented a paper at the Continuing Legal Education Association of Australasia Conference.

The paper entitled "Legal Education and the 21st Century Law Graduate" discussed the impact of globalisation and change on the nature of legal practice for law graduates in the 21st century. The Commissioner noted that twenty-first century Australian legal graduates are entering a more complex and structurally different professional environment from that of their predecessors and that as a result today's law graduates are seeking employment in a multitude of roles.

A law degree has now become a passport to work in a wide range of fields, only one of which is private legal practice. However these different types of practices raise ethical issues for today's legal practitioner that were never experienced before. The Commissioner argued that this will become a growing problem unless it is addressed sooner rather than later – that is at the undergraduate level rather than at a later time when bad habits have already been formed. The problem is however, that the current structure of the undergraduate law degree is rigid and does not cater for the introduction of new core subjects such as emotional intelligence training. The Commissioner suggested that we ought to reconsider the current structure of the undergraduate law degree and make it relevant for the practice of law in the 21st century.

A copy of this paper is available on the OLSC's website at **http://www.lawlink.nsw.gov.au/olsc**

IMPLEMENTING ANTI-MONEY LAUNDERING LEGISLATION AND THE PROFESSIONS

On Friday 7 November 2008 the Commissioner presented a paper at a Symposium on Money Laundering Tax Evasion and Tax Havens, which was hosted by the Faculty of Economics and Business at the University of Sydney. The Commissioner discussed the anti-money laundering and counter-terrorist financing legislation that was enacted in December 2006 and the impact this legislation will have on the professions when the second tranche reforms are enacted possibly later this year.

The Commissioner then discussed the reporting requirements under the legislation and the substantial impact these requirements will have once they are introduced. The Commissioner also discussed the measures that have been taken by the Australian Government to assist reporting entities in setting up and maintaining a reporting programme.

The Commissioner noted that in the United Kingdom, where similar anti-money laundering legislation has been enacted, the professional associations have been very active in assisting their colleagues to set up reporting programmes. The Law Society of England and Wales has for example, produced a 130 page anti-money laundering practice note to assist solicitors in England and Wales to meet their AML/CTF obligations. The purpose of the Practice Note is to outline the legal and regulatory framework of AML/CTF obligations for solicitors within the UK; outline good practice on implementing the legal requirements; outline good practice in developing systems and controls to prevent solicitors being used to facilitate money laundering and terrorist financing; and provide direction on applying the risk-based approach to compliance effectively. The Commissioner advised the Symposium that similar work is being undertaken by the legal profession in Australia. The Commissioner argued that if the legislation is to be a success it must have a strong educative impact.

A copy of this paper is available on the OLSC's website at **http://www.lawlink.nsw.gov.au/olsc**

WITHOUT PREJUDICE VIA EMAIL

As indicated in our last issue the OLSC can send out future issues of *Without Prejudice* via email. If you would like to receive *Without Prejudice* via email please contact us at **OLSC@agd.nsw.gov.au**

Comments? Suggestions? Something you'd like to know more about? Write to the editor, Tahlia Gordon at **Tahlia_Gordon@agd.nsw.gov.au**

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