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"The Lawyer, the Law and Regulations – Is there a case for gatekeeping?"

I. Introduction

When corporate scandals erupt or market misdemeanours are uncovered, the question which typically emerges is, "*Where were the lawyers?*"[1] Judge Stanley Sporkin had famously echoed the public sentiment along these lines in the wake of the American Savings and Loans crisis of the late 1980s[2], and the same question resurfaced following the collapse of Enron in 2002[3] and the recent Global Financial Crisis.

This question – "*where were the lawyers?*" – no doubt carries an accusatory undertone to which we lawyers might well take offence. After all, one would have thought that any finger-pointing exercise that follows the discovery of corporate misconduct should, as a matter of fairness, take in a whole host of other actors, such as the auditors, corporate managers, regulators and perhaps even the ordinary consumers themselves. However, I urge that you curb that defensive instinct and treat the question as an invitation to the legal profession to conduct some serious soul-searching into how we advise on financial transactions. In particular, I propose that

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[1] Cassandra Burke Robertson, *Judgment, Identity and Independence* (2009) 42 Connecticut Law Review 1 at 3

[2] *Lincoln Sav. & Loan Ass'n v. Wall*, 743 F. Supp. 901, 920 (D.D.C. 1990) per US District Court Judge Stanley Sporkin:

> *Where were these professionals…when these clearly improper actions were being consummated?... Why didn't any of them speak up or disassociate themselves from the transaction?... What is difficult to understand is that with all the professional talent involved (both accounting and legal), why at least one professional would not have blown the whistle to stop the overreaching that took place in this case.*

[3] Bernard S Carrey, *Enron – Where Were the Lawyers?* (2003) 27 Vermont Law Review 871

we consider seriously whether lawyers should perform the role of corporate gatekeepers with proactive duties to monitor our clients, to blow the whistle on dubious corporate practices, and to put a premature end to highly risky corporate decisions that appear destined for a road to ruin.

There is, of course, no straightforward answer to a question as controversial as this. Owing to the great deal of creativity possessed by private actors in the financial industry and the diverse needs of the market, corporate transactions are often complex, constantly evolving and highly varied. Therefore, lawyers may be regarded as operating at the sharp end of the law where they discover, not infrequently, that the law has "run out"[4]. Once this happens, the lawyer is situated, to borrow from the conference theme, "*beyond the law*" and how he should advise his client within this extra-legal grey area will certainly divide opinion.

First, there will be lawyers of a more libertarian bent who are generally suspicious of formal authority and so will take creative action whenever black-letter laws do not clearly impede the pursuit of their client's private ends. They are motivated by the belief that such an adversarial approach towards the law forces its clearer articulation and as this "cycle of evasion and re-articulation" continues, the laws will naturally "move upwards to greater completeness and clarity"[5]. Next, there is another breed of lawyers who will similarly adopt innovative solution towards unclear laws, but for altogether different reasons. The law to this group of lawyers is merely instrumental, "to be moulded to suit one's purposes rather than … to be respected as defining the limits of acceptable activity"[6]. In their view, much of the "genius"[7] of lawyering

[4] This phraseology is borrowed from the well-known legal positivist, HLA Hart.
[5] William H. Simon, *After Confidentiality: Rethinking the Professional Responsibilities of the Business Lawyer* (2006) 75(3) Fordham Law Review 1453 at 1459
[6] Christine E. Parker, Robert Eli Rosen and Vibeke Lehmann Nielsen, *The Two Faces of Lawyers: Professional Ethics and Business Compliance with Regulations* (2009) 22 Georgetown Journal of Legal Ethics 201 at 211

involves helping their clients find creative ways of complying with regulations. The mantra of these so-called "gamester"[8] lawyers is therefore essentially this – "*if it's grey, we can play*"[9]. Finally, there is a group of lawyers who occupy a completely different end of the spectrum. These lawyers eschew both the earlier-mentioned formalistic and opportunistic approaches as they are willing to submit themselves not just to the letter but also the spirit of the law. Therefore, even when placed in a grey area, they continue to be constrained by other ethical and public interest considerations which temper what would otherwise have been a single-minded pursuit of their client's interests.

Given these disparate philosophical approaches which shape one's practice of the law, it seems clear that the question of whether lawyers should be corporate gatekeepers is not one that will be easily resolved within our different legal fraternities. Despite that being so, I firmly believe that as the global community continues to explore ways to avert future financial crises, it would be remiss of us if we did not at least accord this question the full attention it deserves. To this end, do allow me to briefly sketch out the cases for and against imposing a gatekeeping role on lawyers which should, I hope, contribute to future discussions on this matter.

II. To gatekeep or not

a. The case against gatekeeping

Let me begin with the case against gatekeeping.

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[7] *Ibid*.
[8] *Ibid*.
[9] Richard Moorehead, "Judgment-based Practice and Lawyers as Gatekeepers: A Return to Ethics?", posted on 7 Feb 2012: accessible at http://lawyerwatch.wordpress.com/2012/02/07/judgment-based-practice-and-lawyers-as-gate-keepers-a-return-to-ethics/ (last visited on 13 October 2013)

The case against gatekeeping essentially posits that the introduction of gatekeeping duties necessarily displaces the various traditional roles which the lawyer serves for his client and that such a fundamental alteration in the lawyer-client relationship is undesirable.

First, what has perhaps traditionally been the most defining aspect of a lawyer is his role as a ***zealous advocate*** of his client's interests. This emphasis on an unbending loyalty to the client is embodied in this classic statement by Lord Brougham, which I quote:

> *"[A]n advocate, in the discharge of his duty, knows but one person in all the world, and that person is his client. To save that client by all means and expedients, and at all hazards and costs to other persons, and, amongst them, to himself, is his first and only duty; and in performing this duty he must not regard the alarm, the torments, the destruction which he may bring upon others."*

Almost two centuries have passed since this statement was made, but the traditional aspiration of zealous advocacy has been observed to remain "the dominant standard of lawyerly excellence"[10] among lawyers even today. Gatekeeping, therefore, has been strongly resisted because by positioning the lawyer as watchdog over, rather than attack dog for his client, it is a notion that it wholly incongruent with the gold standard of zealous advocacy.

Secondly, the lawyer's traditional role as ***trusted confidant*** of his client would also be eroded by the imposition of gatekeeping duties. The effectiveness with which the lawyer can perform this function depends heavily on the established lawyer-client privilege which exists to promote communication and candour. However, by taking on the role of a gatekeeper who is expected to check on client conduct, one can only imagine that the lawyer-client privilege will

[10] Monroe H. Freedman, *Henry Lord Brougham and Zeal* (2006) 34 Hofstra Law Review 1319

become attenuated. The result is a "chill" on the lawyer-client discourse which could, perversely, lead to less effective gatekeeping since it would presumably be much harder to detect misconduct when clients are less forthcoming with their information[11].

Thirdly, the lawyer is also traditionally understood to be no more than a ***legal adviser*** to his client. His role extends no further than "identifying legal problems and presenting options to the client so that the client can ultimately select its course of action"[12]. However, by assuming the role of gatekeepers, lawyers potentially become "moral policemen"[13] who are elevated to sit in judgment over the strictly commercial decisions of their corporate clients. This can become stifling for businesses because it is not inconceivable for a conservative lawyer with a risk appetite that cannot match that of his client to blow the whistle on what the latter simply views as an aggressive or high-risk/high-reward strategy. This possibility of the lawyer "crying wolf" could also lead to subsequent reports of misconduct losing their "sting" and eventually becoming "de-stigmatized"[14].

And, finally, besides precipitating an erosion of the lawyer's various traditional roles, the decision to turn lawyers into gatekeepers may also be instinctively objected to on the grounds that it is, well, simply ***unfair***. For one, it is not inconceivable that the new, possibly nebulous, obligations of the lawyers would mean that they become easy targets with deep pockets against whom litigation may be commenced when investments go awry. As a commentator has

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[11] Marianne C Adams, *Breaking Past the Parallax: Finding the True Place of Lawyers in Securities Fraud* (2009) 37(4) Fordham Urban Law Journal 953 at 981

[12] Steven L Schwarcz, *The Role of Lawyers in the Global Financial Crisis* (2010) 24 Australian Journal of Corporate Law 214 at 220

[13] David B Wilkins, *Team of Rivals? Toward a New Model of the Corporate Attorney-Client Relationship* (2010) 78(5) Fordham Law Review 2067 at 2075

[14] Stephen M Bainbridge, *Corporate Lawyers as Gatekeepers* (2012), 8 Journal of Scholarly Perspectives 1 at 12

observed, the courthouse may well be transformed into "a routine stop on the path of disgruntled clients"[15]. A sense of unfairness also arises from the view that it is simply too onerous to expect lawyers to have to decide, at the risk of liability, whether certain client actions are socially harmful when "society itself has not made that explicit determination"[16] through a clear articulation of its laws.

b. The case for gatekeeping

With that, I close the case against gatekeeping and turn my attention now to the case in support of it. In one sense, as the Attorney-General and the Public Prosecutor, I have assumed a gatekeeping role of a much larger and complex scale. So I speak with some experience!

First, to provide a sense of balance and perspective, it must be said that as entrenched as Lord Brougham's statement on zealous advocacy has become in influencing the outlook of the legal profession, the idea of lawyers as "*officers of the court*" owing duties to uphold the public interest is of equal vintage. On this note, Justice Brandeis' proclamation that a lawyer is "counsel to the situation" rather than merely "counsel to the client" certainly comes to mind[17]. By conceptualising the role of a lawyer from this broader perspective, we are given to appreciate that lawyers *always have had* obligations which transcend those owed to any particular client[18]; and, on this view, it is not difficult to see why many feel that the opponents of gatekeeping have

[15] *Ibid*. note 11 at 967
[16] *Ibid*. note 12 at 224
[17] Geoffrey C Hazard Jr, *Lawyer for the Situation* (2004) 39 Valparaiso University Law Review 377
[18] Robert F. Cochran Jr. et. al., *Symposium: Client Counseling and Moral Responsibility* (2003) 30 Pepperdine Law Review 591 at 608

perhaps overstated their case[19]. The narrow representation of the lawyer as zealous advocate of his client's interests is not only incomplete, but also harmful as it threatens to "systematically marginalise, and indeed delegitimise" [20] a lawyer's allegiance to his broader public role. The criticism, simply, is that if one wishes to hold fast to the traditional roles of the lawyer, one should not do so selectively.

My second point in support of gatekeeping stems from the fact that the lawyer naturally has strong incentives to keep a close watch on his client's transactions. In many structured-finance transactions, it is the lawyer's imprimatur which assures investors of legal compliance and, in this way, he performs the role of a "*reputational intermediary*"[21]. Accordingly, he can little afford to be lackadaisical in satisfying himself about the propriety of a transaction because he stands to lose far more in reputational capital than he could possibly gain in fees from a single transaction. A fundamental concern for self-preservation therefore already exists to motivate the lawyer to be thorough in his inspection of corporate transactions and so the concept of gatekeeping is not necessarily as radical as one might think.

Finally, together with other professionals such as accountants, the lawyer is often seen as a suitable candidate for performing the gatekeeping role because he has "*systematic opportunities*"[22] to detect and prevent risky corporate conduct or fraud. In contrast, public regulatory bodies, are generally detached from such corporate activity and so the enforcement measures which they adopt are likely to only be reactive rather than pre-emptive, by which time

[19] See, for example, Fred Zacharias, *Lawyers as Gatekeepers* (2004) San Diego Law Review, where the author states plainly that "Lawyers are gatekeepers and always have been … [I]t is important to avoid the misconception that lawyers should have no role to play in preventing client misconduct."
[20] *Ibid*. note 13 at 2075
[21] See, for example, John C. Coffee, Jr., *Can Lawyers Wear Blinders? Gatekeepers and Third Party Opinions* (2005) 84 Texas Law Review 59
[22] *Ibid*. note 12 at 221

the damage may be irretrievable. Moreover, these regulatory bodies also suffer from resource constraints which limit their oversight capabilities[23], hence having corporate counsel as a first layer of checks would certainly enhance their enforcement efforts.

III. Quick trends overview

These competing considerations for and against gatekeeping should hopefully inform any discussion about the direction in which the legal profession ought to progress. However, as we debate these issues among ourselves, it appears that the ground has already begun to shift beneath our feet. In this final segment of my speech, I intend to provide you with a brief survey of the latest developments in the US, UK, Australia and Singapore which have some bearing on this topic of corporate gatekeeping. My sense is that there is a growing consensus that lawyers *should* play the more proactive role of gatekeepers in corporate dealings and so, regardless of whether you position yourself as an opponent or proponent of gatekeeping, I suggest that you at least position yourself to be ready to meet these enhanced expectations.

a. USA

My brief trends overview starts off in the US. I choose to start here as I believe that the American experience immediately brings into view the spectre of corporate gatekeeping for the benefit of those who would prefer to dismiss this as a mere remote possibility. Ever since the Sarbanes-Oxley ("SOX") Act was passed in 2002, our American counterparts have *already* come under a legislative regime which both imposes and enforces positive gatekeeping duties on them; these duties include, for instance, having to "report evidence of a material violation of law or

[23] *Ibid*. note 12 at 221

breach of fiduciary duty"[24] up the corporate ladder. This state of affairs persists even though the American Bar had "aggressively lobbied"[25] against the passage of the Act and still "continues to denounce the Securities and Exchange Commission for targeting lawyers"[26]. The reality, therefore, is that lawyers *can* and already *have* been made corporate gatekeepers, despite strong resistance to the initiative.

As one might predict, the debate in the US is no longer centred on the question of whether lawyers *should* be gatekeepers but, rather, on the question of *how much* can be expected of the lawyer-gatekeeper. And, in this regard, it would appear that the level of expectation is fairly high.

The tone was set early on. For example, in the SEC's very first "up-the-ladder" enforcement action against a lawyer, the allegation was *not* that the general counsel of Electro Scientific Industries had been complicit in the fraud perpetrated by the company's CFO and Controller, but rather that it was his "failure to fulfill his gatekeeping role"[27] that made him culpable for the false financial results reported to the public. The shortcomings in his conduct included a failure to aggressively question the CFO on a false statement and also a failure to provide important information to the company's Audit Committee and Board. The matter was eventually settled with the general counsel paying a US$50,000 civil penalty.

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[24] Part 205.3(b)(1) of the Code of Federal Regulations promulgated pursuant to section 307 of the Sarbanes-Oxley Act

[25] Sung Hui Kim, *Naked Self-Interest? Why the Legal Profession Resists Gatekeeping* (2011) 63 Florida Law Review 129 at 132

[26] *Ibid*. at 134

[27] *Securities Exchange Commission v. John E. Isselmann Jr.*, Case No. CV 04-1350 MO (District of Oregon) at para. 1

A more recent example which is illustrative of the standards expected of American attorneys arises from the collapse of Lehman Brothers. The Bankruptcy Examiner's Report found that Lehman had engaged in an accounting treatment which clearly amounted to "balance-sheet manipulation"[28]. What is of relevance to us is that a legal opinion had been obtained as a necessary precursor to this accounting treatment. While the Report found that the opinion was legally accurate, debate has since ensued over whether the law firm providing the opinion should have done more as gatekeeper especially since Lehman's request appeared to be "very unusual"[29]. Some commentators have therefore expressed the view that the law firm should have conducted "further robust inquiry"[30], such as finding out how its opinion would be deployed and the auditor's view on the propriety of the accounting treatment.

b. UK

These accounts provide us with some insight into the gatekeeping demands placed on American lawyers. We might, of course, attribute this to the SOX Act. But, as we turn now to the position in the UK, we find that even though no equivalent of the SOX Act exists, there is nevertheless a visible movement in the direction of gatekeeping.

Such a sentiment may be drawn from the recent action taken by the UK Financial Services Authority[31] against hedge-fund boss, David Einhorn, for insider trading[32]. In this case,

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[28] See Lehman Bankruptcy Examiner's Report at http://lehmanreport.jenner.com/VOLUME%203.pdf (last visited on 13 October 2013)

[29] David Kershaw and Richard Moorhead, *Consequential Responsibility for Client Wrongs: Lehman Brothers and the Regulation of the Legal Profession* (2013) 76(1) Modern Law Review 26 at 51

[30] *Ibid*.

[31] As part of the UK's new regulatory "twin peaks" structure, the FSA has, with effect from 1 April 2013, been split into two separate authorities, namely, the Financial Conduct Authority and the Prudential Regulation Authority

[32]See generally, Ross Dixon and Nicholas Querée, *Inside Information and "Wall Crossing": FSA Enforcement and Intent* (2012) Law and Financial Markets Review 145 at 147

Einhorn had become privy to information that the company (Punch Tavern) in which his hedge fund (Greenlight Capital) had a significant shareholding was preparing an equity fundraising that would considerably depress the share price. He obtained this information through a phone conversation with the company's management and brokers and, immediately afterwards, gave instructions for his shareholding to be sold. When the FSA action was brought, Einhorn contended that the company's management had assured him that the equity issuance was only being discussed in general terms and that, moreover, he had repeatedly refused to be "wall-crossed". Despite his protestations, Einhorn was still slapped with a hefty £7.2 million fine by the FSA. The view, essentially, was that Einhorn should have relied on his own judgment and not reassurances he had sought from others.

It is worth noting that the FSA has since publicly articulated that it will not tolerate market participants who "just take the narrow perspective of what they can get away with"[33]. My view is that if this is the regulatory expectation placed on market players, then it may be difficult to argue that any less will be demanded of their legal advisers.

c. Australia

In Australia, it appears that the pendulum may also have been swung in the direction of gatekeeping. This may be gleaned from the case of *Australian Securities and Investment Commission v Macdonald (No.11)*[34] where Justice Ian Gzell propounded the view that "*guarding [the corporate client] against legal risks*" sits at the "core" of a general counsel's duties[35]. This

[33] "Financial sector must change, says Sants", The Financial Times, 6 Feb 2012: accessible at http://www.ft.com/intl/cms/s/0/cf9fc604-50e7-11e1-8cdb-00144feabdc0.html#axzz2hZpg6pAF (last visited on 13 October 2013)
[34] [2009] NSWSC 287
[35] *Ibid*. at [394] and [560]

duty certainly appears "expansive in scope"[36] as the lawyer in that case was required to not only advise the company on its compliance with statutory obligations but also to protect it from adopting a course of action that might result in an adverse market perception of the company. This broad formulation of the duty appears to have been accepted by the High Court on appeal[37]. The tentative view taken by some, therefore, is that these decisions "can be expected to have far-reaching implications" because they may well have "transformed in-house lawyers into gatekeepers responsible for promoting the public interest" since it is arguable that "being a good corporate citizen [is] also *in the corporation's interests*"[38]. If such a duty is imposed on in-house counsel, there appears to be no compelling reason why it should not likewise be extended to external counsel.

d. Singapore

Turning finally to Singapore, I find that the recent regulatory action taken against OCBC in the Jade Technologies takeover is consistent with the general trend that has been observed elsewhere.

In this case, Asia Pacific Links Ltd (APL) appointed OCBC as financial adviser in its offer for all the issued shares in Jade Technologies which it did not already own. The offer announcement stated that APL held 46.54% of Jade's issued capital and also confirmed that APL had sufficient financial resources to satisfy the offer. However, it turned out that APL's director and sole shareholder had intentionally made false representations to OCBC and so the

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[36] Anil Hargovan, *Australian Securities and Investment Commission v Macdonald (No.11): Corporate Governance Lessons from James Hardie* (2009) 33 Melbourne University Law Review 984 at 1013

[37] *Shafron v Australian Securities and Investments Commission* [2012] HCA 18 at [15]

[38] Michael Legg, "The Hardie Judgment II: Lawyers as Gatekeepers": accessible at http://www.clmr.unsw.edu.au/article/deterrence/court-cases/hardie-judgment-ii-lawyers-gatekeepers (last visited on 13 October 2013)

announcement was misleading. The Securities Industry Council nonetheless found that OCBC had fallen short of the standard expected of it under the Takeover Code. First, OCBC was aware that APL had a share lending agreement with a third party and this should have prompted it to *independently* verify APL's shareholding in Jade. Secondly, OCBC should also have conducted an *independent* verification of APL's financial resources.

The SIC action against OCBC therefore clearly conveys that professional advisers cannot conduct themselves as if they were mere passive receptacles of their client's information or rubberstamps for their client's transactions. Rather, they must not only be diligent in processing such information but also proactive in making further independent inquiries. Is there any legitimate reason why the category of such professional advisers should not encompass lawyers, in-house or otherwise?

e. Client behaviour

What this brief overview demonstrates is that both the *courts* and the *regulators* across various jurisdictions are displaying an increased willingness to cast lawyers in the role of corporate gatekeepers. However, before I end, I wish to make one final observation, and this is that, interestingly, it appears that *clients* may also be demanding more from their lawyers as well.

We often assume that the market for corporate services is one where "lawyers supply what clients demand"[39] and that what clients demand is essentially "gatekeeper acquiescence"[40] to their transactions. If we do not accede, then we are left vulnerable to having our services terminated by such clients who are all too ready to 'shop' around for a second opinion. This view

[39] *Ibid*. note 6 at 203
[40] Sean J. Griffith, *Afterword and Comment: Towards an Ethical Duty to Market Investors* (2003) 35 Connecticut Law Review 1223 at 1225

is premised on the common conception of the corporate client as the opportunist to whom the law is no more than an obstacle in the way of, but also a bundle of opportunities for, achieving its private ends[41].

However, while this may be true of *some* clients, it is hardly representative in an age of corporate social responsibility. A recent survey[42] of in house and external counsel in the US, UK and Israel has in fact found that 11 out of 20 corporations had "Outside Counsel Guidelines" which contained some form of ethical guidance for external counsel. These guidelines do not originate from some legislative or regulatory source but are created and imposed unilaterally by the corporations. It has therefore been commented that we may be witnessing a new kind of "privatised regulation"[43], where the pressure on counsel to act "ethically" and with "integrity" is exerted through the amalgam of behaviour-setting norms that have been formulated in an array of contexts *by their very own clients*. This emerging notion of "client control" is certainly interesting and one which I imagine you would wish to keep your eye out for in the future.

IV. Conclusion

I started off this speech with the *retrospective* question, "Where were the lawyers?" It has been my platform for an *introspective* inquiry into whether there is a case for gatekeeping, and I hope it becomes yours as well. But even as you plunge into deeper thought over this most vexing of issues, I urge you to remain always mindful of the changing currents around you. The trends which I have surveyed suggest that the legal profession is quickly finding itself sitting at the

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[41] Robert W. Gordon, *The Citizen Lawyer – A Brief Informal History of a Myth with Some Basis in Reality* (2009) 50 William & Mary Law Review 1169 at 1176

[42] Christopher J Whelan and Neta Ziv, *Privatizing Professionalism: Client Control of Lawyer's Ethics* (2012) 80(6) Fordham Law Review 2577 at 2583

[43] *Ibid*. at 6

pointed end of a convergence of upward expectations by the courts, the regulators and perhaps even the clients as to how we conduct ourselves in corporate affairs. For some of us, this heightened level of scrutiny may prove to be an increasingly uncomfortable experience; yet, for others, the higher standards to which our profession comes to be held is a development to be readily embraced. The way each of us adapts within this evolving landscape will be determined very much by our philosophical underpinnings and so, if I may, I end off this speech in the same way as I had started it, with a question, but a question which this time invites you to think *prospectively*, and that is – "*What will <u>you</u> do when you next find yourself 'beyond the law'*?"

Thank you.