COMMENTARY

COMMENTARY ON LEGAL AND MANAGERIAL "CULTURES" IN CORPORATE REPRESENTATION

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TABLE OF CONTENTS

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I. INTRODUCTION

Professor Hazard's analysis goes some distance towards enabling clients to effectively incorporate legal counsel into their business decisions. For example, by reminding managers that an attorney's culture tutors him to provide independent, unemotional advice, clients may evaluate difficult problems more objectively.[1] Similarly, by reminding attorneys that managers are geared to make decisions, lawyers may be guided to provide more actionable advice.[2]

In rendering explicit what attorneys and clients usually experience as unconscious influences, Professor Hazard performs an important service. The ability to work across various cultural gaps has become a core business skill in today's increasingly global economy.[3] Improving the ability of attorneys and clients to work across their particular cultural divide can only enhance managers' ability to obtain and employ good legal counsel for the many complex settings in which it is needed.

That said, Professor Hazard's essay focuses, by definition, on only a portion of the problem plaguing attorney–client relations. Let me illustrate by quoting from the beginning of his essay:

> [M]uch legal advice is addressed to legal risks and other negative aspects of a transaction, while clients typically think in terms of opportunity.
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> . . . [F]or the purposes of this Essay it will be assumed that lawyers and their corporate management counterparts are competent and professionally responsible.
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> . . . The different appraisals of a project by management and legal counsel will both be well grounded, but based on somewhat different interpretations of the project.
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> One aspect of such differences in interpretation can properly be described as "cultural": the difference between

1. Geoffrey C. Hazard, Jr., *Legal and Managerial "Cultures" in Corporate Representation*, 46 HOUS. L. REV. 1, 13 (2009) (contrasting the client's subjective view of financial and management problems, labor relations, and key personnel's family issues with the attorney's responsibility to treat every problem in an objective manner).

2. *See id.* at 12–13 (describing the business managers' need for their attorneys to be more direct and specific in delivering legal advice, thus enabling the clients to be certain concerning their obligations).

3. *See id.* at 9 (noting that management attention to cultural differences began in the context of international business).

> the typical culture of responsible business management and the typical culture of responsible lawyers. That difference is the subject of this Essay.[4]

A close examination of these passages reveals the tight boundaries placed on the issue under scrutiny. Only competent and "professionally responsible" clients and attorneys are being discussed. Only one dimension, the difference between management and lawyers' "typical cultures," is examined. In effect, Professor Hazard focuses his attention on the world of reasonable and ethical professionals who struggle with honest misunderstandings rooted in their different cultures. The implied remedy is greater cultural empathy, leading to better communication and to legal advice that receives a better reception.

This Commentary contends that the world addressed by Professor Hazard is not where the most acute lawyer–client problems reside. Why does this issue of attorney–client relations merit the full attention of the *Houston Law Review*? Is it because the business world has been shocked by a series of honest misunderstandings among attorneys and their clients? Or, rather, is it because the business world has been shocked by revelations of prestigious law firms and noted in-house counsels being parties to transactions that later proved blatantly illegal and ultimately catastrophic for clients?

The attorney–client "culture" that needs deeper examination involves factors other than different professional functions. It first involves a fundamental governance issue—the agency problem—which has increasingly infected corporations. Secondly, this agency problem has reinforced an evolution in the nature of "corporate demand" for legal services. Ever more, corporations seek the "technically proficient hired gun" as opposed to the independent legal adviser.[5] The competitive structure of today's legal services market aids corporations in this search. Numerous law firms, offering similar quality basic legal services, populate this market. Corporate clients thus retain multiple law firms eager to provide services and willing to compete on the basis of being more accommodating to the clients' wishes. Finally, reputation risk, defined as the risk that a law firm may be seen as an enabler of unethical or illegal transactions, has eroded as a business concern.

4. *Id.* at 2–4.
5. *See* PAUL G. HASKELL, WHY LAWYERS BEHAVE AS THEY DO 85–86 (1998).

This Commentary will focus on these "structural" and "marketplace" issues. The aim is to get at some of the deeper roots that have prevented attorneys from properly advising their clients. To this end, this Commentary will touch on specific attorney–client cases taken from both the Enron files and the Wall Street insider trading scandal of the late 1980s. These cases will illustrate both the influence of the structural–market issues and also certain successes experienced by attorneys who found means to overcome these forces. Ultimately, the goal is to make individual attorneys, law firms, and clients more aware that the corrupting influences on their relations are powerful, that they have deep roots, and that both additional safeguards and better personal formation are required if they are to be mitigated.

II. STRUCTURAL ROOTS OF THE ATTORNEY–CLIENT PROBLEM: ENRON CASE HISTORIES

The "agency problem" is a well known issue in financial theory. In essence, it concerns firm managers, who are hired to work for shareholders, using their corporate positions to pursue personal financial agendas.[6] Recent history provides numerous examples of senior managers discovering that their ample powers and distance from shareholder scrutiny offer tempting opportunities to profit at the firm's expense. One need only think of Dennis Kozlowski spending Tyco's funds on a Roman toga birthday party and a $6,000 shower curtain,[7] or John J. Rigas's conviction for siphoning $100 million from Adelphia Communications.[8] When this type of abuse occurs, the behavior of the shareholders' agents has become a "problem."

For years, Ken Lay was admired as Enron Corporation's spirited, pillar of the community CEO.[9] Yet, a close examination of his relationship with Enron reveals numerous examples of "agent abuse." Lay's offenses ranged from low profile abuses involving relatively small dollar amounts to others that would

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6. *See* Claudio Storelli, *Corporate Governance Failures—Is Parmalat Europe's Enron?*, 2005 COLUM. BUS. L. REV. 765, 795 (describing how Enron's ownership structure led "to an agency problem between shareholders and management").

7. *See Ex-Tyco CEO Kozlowski Found Guilty*, MSNBC.COM, June 17, 2005, http://www.msnbc.msn.com/id/8261018 (documenting Kozlowski's conviction).

8. *Adelphia Founder Sentenced to 15 Years*, CNNMONEY.COM, June 20, 2005, http://money.cnn.com/2005/06/20/news/newsmakers/rigas_sentencing (describing Rigas's conviction).

9. BETHANY MCLEAN & PETER ELKIND, THE SMARTEST GUYS IN THE ROOM 3 (2003) ("Lay was a hard man not to like. His deliberately modest midwestern manner—Lay made a point of personally serving drinks to subordinates along for the ride on Enron's flagship jet—built a deep reservoir of goodwill among those who worked for him.").

ultimately play a role in Enron's collapse. For starters, Lay used the Enron fleet of planes for personal purposes.[10] In fact, Enron employees dubbed the fleet "the Lay family taxi."[11] Once, for instance, an Enron jet was dispatched to deliver a bed to Lay's daughter in Monaco.[12] Enron also encouraged employees to book travel plans through the Lay/Wittenberg Travel Agency, which Sharon Lay, Ken Lay's sister, half owned.[13] The travel agency received commissions from Enron totaling $4.5 million between 1997 and 1998.[14] Moreover, out of Lay's five children, four worked at Enron or its affiliates.[15] One son, Mark, got into financial and legal troubles at a bankrupt company.[16] Shortly thereafter, Enron agreed to a contract that paid Mark $1 million in salary and bonus plus 20,000 Enron stock options.[17]

The mindset that allowed Ken Lay to engage in these practices would return to haunt Enron in its hour of need. Amazingly, even though he had earned over $200 million in salary, bonuses, and exercised options, in early 2001 Ken Lay began experiencing financial problems.[18] In an ill-starred effort to diversify his holdings, Lay borrowed $95 million from banks, secured with Enron stock, and invested the proceeds in small, illiquid venture companies.[19] Shortly thereafter, Enron's stock price began to fall. Lay began receiving margin calls for which he did not have the necessary cash.[20] Lay's solution was to borrow from Enron and sell stock back to the company to repay the loans. In June 2001 alone, Lay borrowed $24 million from Enron. By July, he had sold more than $52 million of Enron stock back to the company.[21]

Normally, senior executive sales of stock must be disclosed almost immediately. By exploiting this feature of Enron's executive loan program, however, Lay was able to avoid

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10. *Id.* at 4.
11. *Id.* at 90.
12. *Id.*
13. *Id.*
14. *Id.*
15. *Id.* (citing nepotism as one of Enron's bigger issues).
16. *Id.*
17. *Id.*
18. *Id.* at 343.
19. *Id.* at 343–44.
20. *Id.* at 344 (stating that when Enron's stock fell below $80 and $60 per share, respectively, Lay faced margin calls).
21. *See id.* (noting how one board member coined the solution as Lay's "ATM approach").

disclosure until year-end.[22] The entire set of facts and circumstances created a powerful conflict of interest and gave Lay a secret personal reason to avoid disclosures that would further depress Enron's stock price.

A moment of truth arrived in August 2001 when Jeff Skilling resigned as CEO and Lay returned to his previous position.[23] Lay had known about Skilling's pending departure for over a month. The Enron Board meeting at which Skilling resigned involved a thorough examination of the company's increasingly desperate financial situation. If ever there was a moment of opportunity for Lay to tell analysts and employees that all was not well, this was it. Skilling's failed tenure gave Lay the maneuvering room to announce that Enron faced financial challenges and that cleanup measures would be immediately needed. Instead, Lay told Wall Street's analysts and Enron's employees the following:

> I want to assure you I have never felt better about the prospects for the company. . . . One of my top priorities will be to restore a significant amount of the stock value we have lost as soon as possible. . . . Our performance has never been stronger. Our business model has never been more robust; our growth has never been more certain.[24]

During his long tenure as CEO, Lay must have been counseled multiple times about his legal responsibilities when making public statements. He certainly would have known that under section 10 of the Securities Exchange Act of 1934 he was prohibited from making materially misleading statements.[25] Yet, four months before Enron went bankrupt, he chose to tell key audiences that everything was great.

We will probably never know how much influence Lay's personal financial situation had on his decision to "maintain appearances" rather than acknowledge and address Enron's real difficulties. We do know, however, that a more candid treatment of Enron's problems might have exacerbated Lay's personal plight. By August 2001, Enron had many secrets to hide. Disclosure would have further depressed Enron's stock price, intensifying Lay's personal financial situation. When only limited

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22. *Id.*

23. MIMI SWARTZ WITH SHERRON WATKINS, POWER FAILURE 272, 277 (2003) (noting that on Tuesday, August 14, 2001, the board formally accepted Skilling's resignation and that Lay was then "back in charge").

24. MCLEAN & ELKIND, *supra* note 9, at 352.

25. *See* 17 C.F.R. § 240.10b-5 (2008) ("It shall be unlawful for any person . . . [t]o make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading . . . in connection with the purchase or sale of any security.").

disclosures were made two months later, Enron's stock price sank precipitously.[26] It would have taken courage and skill on the part of a disinterested manager to disclose Enron's problems and still mount an effective rescue. For the conflicted Ken Lay, that task proved impossible.

What connection does all of this have with the attorney–client relationship issue? The concern is simply this: acute agency misconduct creates mega problems, rooted in hidden agendas, for attorneys. It is one thing to provide objective legal advice to a manager who is working for shareholders. Even if such a manager has much invested in his plans and a strong wish to take a direct route to some desired result, he likely will also be sensitive to risks that could sabotage a successful outcome. Skilled lawyers can usually read such a manager; they also are well practiced in articulating warnings that are not ignored and in providing alternatives that entail less risk.

Hidden personal agendas, on the other hand, are like a "below the water line" reef for attorneys. Out of sight, they are not "on the table" for discussion. Consequently, the attorney's advice will be somewhat "beside the point" for the manager receiving it. A sense of opaqueness tends to cloud the discussion—one associated with a vague realization that attorneys and their clients are not communicating effectively. Should the attorney press his argument, the manager with the hidden agenda will frequently fall back on his authority or leverage. Diktat and intimidation are used to finalize the discussion.

The problems associated with Ken Lay's questionable "agency-type" behavior were not confined to Enron's endgame. Rather, the problems affected Enron's culture and controls over the entire trajectory of Lay's career. His manifest disregard for conflicts of interest and sound controls spawned several problems. Lay's actions signaled to other Enron employees that self-enrichment might be tolerated. Employees read and decoded such signals, which ended up multiplying the number of Enron agents with hidden agendas. A second result followed. Multiple employees with hidden agendas created a very difficult environment for the attorneys. As in-house and outside counsel both discovered, it is difficult to advise clients who have hidden

26. SWARTZ WITH WATKINS, *supra* note 23, at 305–06 (noting that the stock price fell to $25 per share after receiving negative press in the *Wall Street Journal* regarding Enron's related-party transactions).

agendas that run directly counter to the interests of the firm and shareholders.

III. CONSEQUENCES FOR ATTORNEYS OF SPREADING AGENCY ISSUES WITHIN ENRON

Enron's history is replete with cases of executives other than Lay and Skilling who, to pursue their own agendas, ignored, manipulated, or intimidated their attorneys. The foremost practitioners were CFO Andy Fastow and his sidekick, Michael Kopper. In 1997, Fastow decided that he could achieve a longstanding dream of running a private equity fund while keeping his Enron CFO position. In 1997, Fastow assembled Alpine Investors, a partnership composed of family and friends, with Fastow himself as general partner.[27] He proposed that Alpine receive funding from Enron to purchase certain Enron assets. Enron was willing to sell the assets, which were wind turbines, in order to maintain a favorable regulatory status.[28]

Unfortunately for Fastow, Enron counsel opined that if Fastow and family participated, Alpine would not be sufficiently "independent" from Enron to secure the desired accounting treatment. In fewer words, Alpine Investors did not work.[29] Fastow's next move spoke volumes regarding his views on legal advice and on the behavior he thought would be tolerated by Enron senior managers.

Fastow waited until Enron had another need to sell assets. In this case, Enron had purchased fifty percent of an energy partnership from CalPERS.[30] Enron wanted the partnership off its books by year-end to avoid consolidating the assets and liabilities in its financial statements.[31] Fastow had his assistant,

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27. STEPHEN V. ARBOGAST, RESISTING CORPORATE CORRUPTION: LESSONS IN PRACTICAL ETHICS FROM THE ENRON WRECKAGE 114 (2008) (noting Fastow's partners in Alpine Investors included Kopper, Patty Melcher, a personal friend, and Fastow's wife's family).

28. Enron obtained the wind turbines through their acquisition of a company called Zond. When the acquisition took place, the Zond wind farms enjoyed favorable legal status as qualifying facilities. However, this status would disappear if the facilities were ever more than 50% owned by a utility. Because Enron was about to become a utility upon its acquisition of Portland General, Enron needed to sell 50% of Zond in order to maintain its favorable legal status. Fastow created two special-purpose entities to buy half of Zond and secretly supplied most of the "independent equity" required to complete the deal. MCLEAN & ELKIND, *supra* note 9, at 166–67.

29. KURT EICHENWALD, CONSPIRACY OF FOOLS 143–44 (2005).

30. MCLEAN & ELKIND, *supra* note 9, at 168–69.

31. *See* ARBOGAST, *supra* note 27, at 130 (noting that although Enron purchased CalPERS's stake in JEDI to ensure participation in another Enron deal, "Enron balked at having JEDI's assets and debts returned to its balance sheet").

Michael Kopper, form a new partnership called Chewco Investments, LP. Because Kopper was not an Enron corporate officer, his participation in the partnership did not need to be disclosed. Fastow and Kopper then reached a private understanding to track and divide the profits resulting from this and similar deals.[32]

The rest of Chewco's "independent" equity came from Barclays Bank. Amazingly, it was structured in the form of fixed rate certificates partially collateralized by Chewco, which placed $6 million cash in escrow accounts.[33]

For this transparent legal dodge to work, the identity of the Chewco partners and the details of their involvement had to be kept secret. Kopper undertook this task with a bristly enthusiasm. During the second half of December, deal lawyers tried to determine the identity of the Chewco partners. Jordan Mintz, an Enron attorney who is discussed in more detail below, was called in to draft a tax indemnity for Chewco.[34] Mintz asked Kopper to identify the transaction's full structure and name all the Chewco investors. Kopper replied: "I can't do that . . . . Enron doesn't have a right to know more. We're negotiating for Chewco, but it's behind a black curtain. You're not supposed to know what's there. That's what all the parties have agreed to."[35]

Here we can see the hidden agenda at work. For attorneys to be able to give advice, they need full disclosure of relevant facts and circumstances. Employees with hidden agendas can frustrate legal review simply by withholding the facts necessary to form a sound judgment.

Could the attorneys have pressed their case at a higher level? Where were they to go with an appeal—Fastow, Skilling, Lay? By this point, all attorneys working at Enron knew that these players would not risk closing a short-fused transaction over what they would dismiss as a "legal technicality." The

32. *Id.*

33. WILLIAMS C. POWERS, JR., RAYMOND S. TROUBH & HERBERT S. WINOKUR, JR., SPECIAL INVESTIGATIVE COMM. OF THE BD. OF DIRS. OF ENRON CORP., REPORT OF INVESTIGATION 49–50 (2002) [hereinafter REPORT OF INVESTIGATION] (noting that in order to obtain the $11.5 million in equity required from Chewco's partners, Barclays loaned the money in what looked like regular loan agreements but were labeled "certificates," and required Chewco to pay Barclays "yield" so that Barclays could "characterize the advances as loans . . . while allowing Enron and Chewco simultaneously to characterize them as equity contributions").

34. EICHENWALD, *supra* note 29, at 156.

35. *Id.*

attorneys abandoned their line of questioning, and Chewco closed on December 30th.[36]

Of course, that was not the end of the story. In October 2001, Arthur Andersen accountants suddenly "discovered" that Barclays's cash collateralized certificates did not qualify as equity. Consequently, the Chewco partnership was disqualified from third party accounting treatment.[37] This discovery required accounting restatements back to 1997 or, more specifically, the unbooking of hundreds of millions of dollars of Enron reported profits.[38] The Powers Committee, formed by the Enron Board to investigate the Fastow partnership deals, wrote of the Chewco transaction:

> On October 16, 2001, Enron announced that it was taking a $544 million after-tax charge against earnings related to transactions with LJM2 . . . .
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> Less than one month later, Enron announced that it was restating its financial statements for the period from 1997 through 2001 because of accounting errors relating to transactions with a different Fastow partnership, LJM Cayman, L.P. ("LJM1"), and an additional related-party entity, Chewco Investments, L.P. ("Chewco"). Chewco was managed by an Enron Global Finance employee, Kopper, who reported to Fastow.
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> . . . These announcements destroyed market confidence and investor trust in Enron. Less than one month later, Enron filed for bankruptcy.[39]

That Chewco was essentially the final nail in Enron's coffin is now a well known part of the company's history. Less obvious, but very germane to our concerns, is the effect of this deal and others like it on the Enron attorneys. Counsel became accustomed to expect several recurring elements in Enron deals:

1. Counsel would not get complete disclosure or candid answers from dealmakers.
2. Counsel would be pressured to "make the deal work" technically and timing-wise.

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36. *See id*. at 163 (noting that on December 30, 1997, when the documents finalizing the deal were signed, "most people in the room still didn't know the identities of the independent investors who had put up more than $11 million for Chewco").

37. REPORT OF INVESTIGATION, *supra* note 33, at 41–42.

38. *See id.* at 42 (detailing the consequences to Enron's net income between 1997 and 2001 as a result of the retroactive consolidation of Chewco).

39. *Id.* at 2–3.

3. Dealmakers could always cite prior review with senior managers like Skilling who had "signed off" and expected the deal to close.

These circumstances made the deals something like "black boxes" impervious to legal scrutiny and criticism. And, of course, the hidden agendas at the root of this approach remained out of sight. The law firm of Vinson and Elkins (V&E) did extensive legal work on the Chewco transaction.[40] One of their attorneys, Ron Astin, fought very hard to assure that Fastow and family did not openly participate as investors.[41] Yet, this proved a pyrrhic victory, as Fastow relentlessly acted on his agenda. By the end of the transaction, V&E had exhausted its willingness to scrutinize the deal. Indeed, it was a V&E associate, Joel Ephross, who drafted the side letter establishing the fatal Barclays collateral accounts.[42] Nobody higher up at the firm raised a red flag.[43]

IV. Influence of the Marketplace for Legal Services

Why didn't the attorneys simply resign in protest and refuse to endorse Enron's deals? For this answer, we come to the structure of the legal industry serving large corporate clients. Truth be told, it is a highly competitive marketplace in corporate legal services. There are many large law firms in a city like Houston, most with a full cast of corporate law attorneys. Moreover, large out-of-town firms are also in the game. This abundance of legal providers has caused a commoditization of many types of advice. Individual attorneys with special skills or a niche practice can command top tier clients and earn premium rates. Beyond this, it is hard to say that the general corporate law advice of Baker Botts or Fulbright & Jaworski is clearly superior to that offered by Fried Frank or Sullivan & Cromwell.

This market structure gives corporate clients considerable clout when bargaining for legal services. Some use this leverage to demand careful accounting of billings and to drive down rates. Others use it to push attorneys to accommodate aggressive transactions and tight deadlines. Clients with hidden agendas find it easy to mask their intentions within aggressive deal structures and deadlines.

Enron's "agent managers" used the legal marketplace to get the advice they needed and avoid the scrutiny they feared. Enron

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40. Eichenwald, *supra* note 29, at 161.
41. *See id.* at 152–54 (recounting Astin's warnings to Fastow).
42. *Id.* at 161.
43. *Id.* at 162.

paid well. It had an incredible deal flow, which meant huge amounts of standard legal work each year. Enron wasn't a stickler for tight expense management or cost accounting. They did, however, ask for aggressiveness and deal completion within near impossible deadlines. Enron also spread the work around. Most major firms in Houston got a taste of Enron's legal fees. This left each law firm with an unspoken understanding: if you won't do this transaction on our terms, the guy up the street will, and we can easily drop you from our list for next year.

The cumulative effect of high remuneration, intense competition among firms, and Enron pressure to execute deals on their terms was to disarm the deal attorneys over time. Their antennae for the "out of bounds" fact or the unsavory practice dulled with repeat experiences of "going with the flow." Increasingly, the attorneys assumed the role of "hired technical guns" who fixed problems and gave deals their legal imprimatur. This suited the Enron hidden agenda types perfectly. Unfortunately, this also meant that these agents would eventually booby trap Enron with deals containing not just technical, but catastrophically fatal flaws.

It was just such a set of deals, the LJM2/Raptors, that caused Sherron Watkins to write an anonymous letter to Ken Lay.[44] This letter provided one of Houston's most prestigious law firms with a special test. The Raptors involved another set of Fastow partnerships and were festooned with problems similar to those of Chewco. Watkins argued that they did not appear to pass basic accounting muster, that they could be construed as fundamentally misleading investors, and that she was worried Enron "will implode in a wave of accounting scandals."[45] She later called for a quiet but thorough investigation, and specifically recommended against using either Arthur Andersen or the deal law firm, V&E.[46]

If ever there was a moment that Ken Lay needed objective and independent legal advice, this was it. Faced with a similar task only two months later, the Powers Committee would hire Wilmer, Cutler & Pickering, a firm with no ties to Enron.[47] Instead, Lay and his chief counsel, Jim Derrick, called V&E and

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44. Memorandum from Anonymous [Sherron Watkins] to Ken Lay, CEO, Enron, *reprinted in* SWARTZ WITH WATKINS, *supra* note 23, at 361–62 [hereinafter Sherron Watkins Memo].

45. *Id.*

46. *See* SWARTZ WITH WATKINS, *supra* note 23, at 368 (illustrating Watkins's concern about conflicts of interest).

47. MCLEAN & ELKIND, *supra* note 9, at 390.

asked the firm to do a highly circumscribed investigation. V&E was not to "second-guess[ ]" Arthur Andersen's accounting or engage in any "discovery-style" investigation.[48] Within these boundaries, which foreordained that nothing new would be uncovered, they were to determine if there were any "new" facts to warrant a fuller investigation.[49]

Two V&E attorneys answered Enron's request. One was Joseph Dilg, manager of the Enron account since 1991. Dilg was about to become V&E's managing partner. Thus, he was especially aware of the fact that at $35 million in annual billings, Enron was the firm's largest single client.[50] Because of his long association with Enron, Dilg was familiar with related party transactions such as Chewco and the Raptors. For this assignment, he was joined by Max Hendrick III, V&E's head of litigation.[51] Hendrick did not have prior work associations with Enron.[52]

The two attorneys faced some difficult decisions. V&E had worked on the Raptor deals providing, among other things, true sale opinions.[53] The firm also helped Enron prepare its disclosures of related party transactions in its proxy statements and periodic SEC filings.[54] To this extent, Enron was asking V&E to review its own work. V&E faced a basic conflict of interest.

However, the structure of Enron's relations with other Houston law firms also had to be considered. As noted earlier, Enron spread its work around. If V&E raised objections, declined the request, or both, there was little reason to think Enron would reconsider its investigative approach. Instead, there was every reason to expect Enron to ask another firm to do the inquiry and for that firm to say yes to the conditions Enron demanded. V&E would potentially alienate its biggest client without materially altering the company's course of action. V&E also had to consider that a competing law firm might raise awkward questions about V&E's prior legal work.

From this weak negotiating position, V&E adopted the tactic of accepting the client's conditions while trying to minimize the damage at the margin. To downplay their own conflict of interest, V&E cast the investigation as a "preliminary" inquiry, the

48. SWARTZ WITH WATKINS, *supra* note 23, at 302.
49. MCLEAN & ELKIND, *supra* note 9, at 357–58.
50. *Id.* at 357.
51. *Id.*
52. REPORT OF INVESTIGATION, *supra* note 33, at 173.
53. SWARTZ WITH WATKINS, *supra* note 23, at 368.
54. REPORT OF INVESTIGATION, *supra* note 33, at 25–26.

purpose of which was to determine if another firm should carry out a broader review.[55] V&E then conducted the inquiry exactly as Enron demanded. The firm neither retained an outside accounting firm nor second-guessed any of Arthur Andersen's work. Nobody outside of nine Enron senior executives and two Andersen partners was interviewed. Jeff Skilling, Cliff Baxter, and Michael Kopper were not interviewed because of their status as former employees.[56] After this minimal fact finding, V&E gave Ken Lay the conclusion he wanted to hear: they had found nothing to warrant a broader, independent inquiry.[57]

Having met the client's demands, V&E then delivered a message. The Powers Committee summarized this message as follows: "[T]he 'bad cosmetics' of the Raptor related-party transactions, coupled with the poor performance of the assets placed in the Raptor vehicles, created 'a serious risk of adverse publicity and litigation.'"[58] Published accounts of the Enron story have treated this as a throwaway line, or a "cover V&E's posterior" inclusion. This Author prefers a different interpretation. In my view, V&E's attorneys were sending a calibrated warning across Lay's radar screen. In substance, V&E's message was not much different from Sherron Watkins's comments when she wrote to Lay: "I realize that we have had a lot of smart people looking at this and a lot of accountants including [Arthur Andersen] have blessed the accounting treatment. None of that will protect Enron if these transactions are ever disclosed in the bright light of day."[59]

However, the degree of concern conveyed by V&E and the extent to which it resonated as a warning were quite different. In an attempt to walk a technical line between giving the client what it wanted and saying what needed to be said, V&E left its words open to this interpretation—that the "risk of adverse publicity and litigation" was a low probability event. Ken Lay took it that way. He ignored the warning and delightedly informed the Enron Board that the investigation required no further action.

Of course, within two months the Raptor transactions would be disclosed and the "bright light of day" would shine upon the massive accounting write down they required.[60] Enron's Board

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55. *Id.* at 173.

56. MCLEAN & ELKIND, *supra* note 9, at 360–61.

57. REPORT OF INVESTIGATION, *supra* note 33, at 176.

58. *Id.*

59. SWARTZ WITH WATKINS, *supra* note 23, at 363–64.

60. Memorandum from Sherron Watkins to Ken Lay and Others, *reprinted in*

convened the Powers Committee. Its report in early 2002 would conclude the following: "The result of the V&E review was largely predetermined by the scope and nature of the investigation and the process employed."[61]

Did Dilg and Hendrick miss this point because it was too obscure or because of cultural misunderstandings with the business leader Ken Lay? I think not. Rather, they knew exactly what Lay was asking for. They chose to give it after a careful weighing of the firm's competitive ability to decline Enron's request and the potential costs of doing so. They also gave Lay a warning if he chose to receive it. Clearly, they did not expect the inquiry to become public or anticipate V&E being accused of having produced a whitewash report.

V. Law Firms and Moral Hazard

This brings us to the final factor that explains why law firms accommodate questionable practices by their clients: major firms don't seem to suffer material consequences for doing so. Certainly, in the Enron story, V&E didn't experience anything similar to the huge legal damages that befell financial institutions after the bankruptcy. Both Citibank and J.P. Morgan eventually paid litigation awards of some $2 billion.[62] Canadian Imperial Bank of Commerce paid $2.4 billion.[63] V&E was identified in the Powers Committee report as having done substantial work on the transactions that led to Enron's bankruptcy. Its questionable and conflicted work investigating some of those same transactions was also highlighted. Yet, to date, V&E has paid a total of $30 million to settle outstanding Enron litigation.[64] This figure should be compared with the $162 million that V&E billed Enron for services between 1997 and 2001.[65] V&E also didn't suffer anything like the fate of fellow

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SWARTZ WITH WATKINS, *supra* note 23, at 364; *see also* Floyd Norris, *Enron's Many Strands: The Bookkeeping; Too Clever by Half: Enron's Doomed 'Triumph of* Accounting', N.Y. TIMES, Feb. 4, 2002, at A18 (reporting that Enron's "big loss related to Raptor" occurred in October 2001).

61. REPORT OF INVESTIGATION, *supra* note 33, at 176.

62. Catherine Tomasko, *Canadian Bank Settles with Enron Investors for $2.4 Billion*, ANDREWS PUBLICATIONS, Aug. 22, 2005, http://news.findlaw.com/andrews/bf/bll/20050819/20050819enroncibc.html.

63. *Id.*

64. Debra Cassens Weiss, *Vinson & Elkins Transfers Partners, Prepares to Expand*, ABAJOURNAL.COM, Apr. 29, 2008, http://www.abajournal.com/news/vinson_elkins_transfers_partners_prepares_to_expand.

65. Michael Orey, *Enron's Last Mystery*, BUS. WEEK, June 12, 2006, at 28.

gatekeeper Arthur Andersen, which imploded and was liquidated in the wake of an Enron-related criminal conviction.[66]

This raises the awkward matter of whether there exists meaningful reputation risk for a law firm that accommodates a client's questionable legal practices. Despite the client's scandal-ridden demise, V&E's damages have been small relative to its Enron billings. Top corporate customers continue to seek V&E's advice. Embarrassing revelations notwithstanding, this outcome suggests that V&E's handling of Enron proved to be good business in terms of "dollars and cents."

To sum up this part of the discussion, we have been arguing that the most significant problems in attorney–client relations are not just related to cultural misunderstandings affecting the normal course of business. Rather, they are made of sterner stuff. In particular, the hard problems flow from questionable agency behavior by senior executives. This can introduce hidden agendas into dealings among attorneys and clients; these agendas raise formidable obstacles to giving objective advice. This questionable behavior can also breed a widespread belief within a corporation that self-dealing and conflicts of interest will be tolerated. This creates an increasingly hostile environment for the giving of objective advice. Over time, it can condition attorneys to become "technical enablers" of their client's questionable activities. The attorneys' slide in this direction is also fostered by a marketplace for basic legal services that gives bargaining power to the client. Finally, it is reinforced by a kind of "moral hazard"—the quiet realization that law firms do not tend to suffer major adverse consequences from being involved in their client's questionable schemes.

VI. NEW DIRECTIONS IN THE ATTORNEY–CLIENT RELATIONSHIP

How then can the legal profession combat these more formidable obstacles to sound attorney–client relations? How can new attorneys best prepare for the possibility of finding themselves in hazardous waters?

To begin, law schools must reinforce the message that attorneys have formidable means at their disposal to combat client agency issues. Doing so, however, requires a willingness to see the legal issues and the accompanying challenges concerning corporate politics. It then requires attorneys to employ their legal

66. EICHENWALD, *supra* note 29, at 666–67.

means within a tactical plan. Said differently, attorneys must become practiced in employing their professional skills within the client's own decisionmaking process.

The list of attorneys' special means is longer than generally imagined. In-house counsel can warn clients that their actions will violate specific laws, exposing the company, and possibly the individuals, to civil or criminal penalties. Typically, clients are not familiar with all laws relevant to their proposed actions; seldom are they knowledgeable regarding the full extent of possible penalties. Unambiguous warnings about these risks strike at the heart of the agency issue—which is the agent's sense that he won't get caught. In-house counsel has a powerful means to reinforce these warnings: obtaining outside opinions that buttress their advice and elaborate fully on the law. In-house counsel controls the selection of outside advisers. They also review draft opinions and have considerable scope of authority to influence their composition. Finally, in-house counsel can either keep client communications within the attorney–client privilege or, if they so choose, deliberately communicate in a way that leaves the dialogue with clients unprotected. This latter course allows counsel to advise clients that specific communications leave them open to discovery and personal liability. In such ways, counsel's resolve to deliver a warning can fire heavy salvos across a rogue agent's bow.

This formidable list of means suggests that the attorney's key challenge is maintaining his resolve. However, as noted above, client secrecy and the structure of the legal marketplace also pose obstacles. Nevertheless, the knowledge that potent means can be married to politically effective tactics can be very helpful to attorneys seeking the resolve to do what they know to be right.

The Enron story also provides an excellent case study of able resistance mounted by an attorney. Jordan Mintz, a tax attorney, became Andy Fastow's chief counsel late in 2000. He quickly discovered that Fastow's related-party transactions were questionable and that their supporting documentation was suspiciously sparse.[67] Mintz resolved to challenge Fastow's deals.[68]

The tactics Mintz adopted bear noting. First, he selected a legal issue on which Fastow was vulnerable. This issue concerned disclosure of Fastow's compensation in Enron's SEC filings.

67. MCLEAN & ELKIND, *supra* note 9, at 327–28.
68. *Id.* at 328–29.

Under federal securities regulations, a public company should disclose material amounts of compensation paid to a corporate officer who does business with the company.[69] Mintz did not know the extent of Fastow's compensation from his LJM partnership deals with Enron, but he sensed it was material.[70] The Powers Committee would later disclose that Fastow earned over $30 million from the LJM 1 and 2 partnerships alone.[71]

One year earlier, V&E had advised Fastow that disclosure could be avoided because too many transactions had not settled and his compensation could not be calculated.[72] For year 2000, however, over 20 LJM transactions worth in excess of $500 million had settled. When Fastow told Mintz he wanted to make the same argument used the prior year, Mintz resisted the point.[73]

First, he took the matter up with V&E. The outside firm again supported Fastow's position. Next, he raised the matter with Chief Accounting Officer Rick Causey, arguing that the Enron Board had asked to be informed about Fastow's compensation. Causey dodged the issue. So, on his own, Mintz went to another outside counsel on the matter. He took the matter to Fried, Frank, Harris, Shriver & Jacobson LLP, a firm without a material Enron business relationship. Armed with an opinion supporting his views, Mintz opened a second front. Noting that numerous signature sheets authorizing LJM deals lacked Jeff Skilling's signoff, Mintz documented the facts. He then put himself on Skilling's schedule to pursue the missing signoffs.[74]

The multiple pressure tactics paid off. Just before he was scheduled to meet with Mintz, Skilling called Fastow into his office. Fastow was given a choice to give up his LJM general partner roles or to resign from Enron and work fulltime for LJM. Fastow chose to resign from LJM.[75] Even though he reconstituted the partnerships with Kopper in charge,[76] Fastow's position within Enron had been altered. Mintz's determined campaign of resistance helped establish that Fastow's related-party deals were becoming more trouble than they were worth. Increasingly,

69. 17 C.F.R. § 229.404(a) (2008).

70. *See* MCLEAN & ELKIND, *supra* note 9, at 327–28.

71. REPORT OF INVESTIGATION, *supra* note 33, at 3.

72. MCLEAN & ELKIND, *supra* note 9, at 328.

73. ARBOGAST, *supra* note 27, at 147.

74. MCLEAN & ELKIND, *supra* note 9, at 328–29.

75. *Id.* at 329.

76. EICHENWALD, *supra* note 29, at 458.

Fastow came to be seen as a liability. He was fired less than six months later.[77]

In retrospect, Jordan Mintz's story shows how lawyers can substantially affect their client's ethical behavior by combining clear legal advice with persistent pursuit of a tactical plan. This still leaves the question, however, of how attorneys can overcome their impulse to "look the other way" when clients cross the line. With so much in billings at stake and with competitors eager to take your place, how can attorneys muster the necessary resolve?

In this regard, it seems appropriate to revisit what it means to serve the client. As both the American Bar Association (ABA) Model Rules and the Texas Disciplinary Rules of Professional Conduct make clear, the client is not the corporate executive asking for advice.[78] Rather, the client is the organization that retains the attorney's services. The lawyer's duty is to serve the best interests of that organization. This makes crystal clear that the attorney's role is not to become a "technical fixer" for an agent's dubious schemes. Rather, it is to help the organization pursue the most effective legal course of business and to warn the organization of the potential consequences of illegal activity.[79]

Strikingly, many attorneys in the Enron saga forgot this basic point. For example, consider a 2006 Business Week article quoting internal V&E documents that indicated basic concerns about the efficacy of the Enron–LJM transactions.[80] Of particular interest were notes prepared by a V&E senior partner in regards to the true sale opinions provided by the firm. True sale opinions were crucial to Enron's ability to close these transactions. The V&E lawyer's notes stated, "We [are] unsure of how [the] opinion rendered satisfies [the] requirements of [the Financial Accounting Standards Board]."[81] The V&E partner also noted that the deals were "[l]arge transactions with significant earnings impact," and that he didn't "want [the] deal to blow up at [the] last moment and cause [an] earnings surprise."[82]

V&E eventually addressed its concerns by adding language to its opinion. The additional language provided legal cover for V&E but seemed to contradict the whole point of the opinion,

77. MCLEAN & ELKIND, *supra* note 9, at 377.

78. MODEL RULES OF PROF'L CONDUCT R. 1.13(a) (2008); TEX. DISCIPLINARY R. PROF'L CONDUCT 1.12(a), *reprinted in* TEX. GOV'T CODE ANN., tit. 2, subtit. G app. A (Vernon 2005).

79. ARBOGAST, *supra* note 27, at 159–60.

80. Orey, *supra* note 65, at 28.

81. *Id.* at 30.

82. *Id.*

which was to assure that a true transfer of the assets had occurred. This kind of technical fix enabled V&E to resolve immediate tensions with the client. Enron proceeded with its deals and reported the results as it wished. V&E retained the business.[83] Whether they served their client's real interests is highly debatable. As the Powers Committee would eventually conclude regarding V&E:

> Management and the Board relied heavily on the perceived approval by Vinson & Elkins of the structure and disclosure of the transactions. Enron's Audit and Compliance Committee, as well as in-house counsel, looked to it for assurance that Enron's public disclosures were legally sufficient. It would be inappropriate to fault Vinson & Elkins for accounting matters . . . . However, Vinson & Elkins should have brought a stronger, more objective and more critical voice to the disclosure process.[84]

By focusing on the real client's fundamental interests, attorneys will often find a more effective method for serving the client. An interesting, relevant example comes from an earlier case, the insider trading scandal of the 1980s. The case in point concerns famed arbitrager Ivan Boesky and the lawyer he hired for his defense, Harvey Pitt.[85]

Federal prosecutors were working up the Wall Street food chain. First, they cracked open the Bahamas branch of Bank Leu, determining that a Drexel Burnham Lambert banker, Dennis Levine, had traded in stocks of twenty-eight companies immediately prior to those companies being taken over.[86] Next, they indicted Levine. He agreed to provide evidence against other inside traders in return for leniency.[87] Levine identified Boesky as someone to whom he provided tips in return for a share of the gains.[88] The SEC then subpoenaed a vast quantity of Boesky's trading documents. Boesky called Harvey Pitt the same day.[89]

Pitt was already somewhat familiar with the situation. The SEC began its investigation by delving into Bank Leu. The bank hired Pitt when the Commission subpoenaed one of the employees who had serviced Levine's account. Pitt's approach to

83. *See id.*

84. REPORT OF INVESTIGATION, *supra* note 33, at 26.

85. *See* JAMES B. STEWART, DEN OF THIEVES 275 (1991) (narrating the details surrounding the Boesky insider trading scandal).

86. *See id.* at 237 (describing Levine's reaction to the SEC's request for information about the twenty-eight stocks).

87. *Id.* at 264–65.

88. *Id.* at 266.

89. *Id.* at 275–76.

the bank was noteworthy. After listening to the employee's dubious story, he discussed the perils of lying to one's own attorney: "You may be afraid of telling the truth. . . . But we're very good lawyers. If you tell us the truth, the likelihood is that we can help you."[90]

Slowly, the bank came around. Upon receiving the case details, Pitt determined that bank employees shredded evidence at Levine's request and could be charged with obstruction of justice. If so charged, Bahamian secrecy laws would not protect Bank Leu. Privy to this possible outcome, the bank began to cooperate fully. Levine's name was identified. Pitt used the information to obtain immunity for the bank while giving prosecutors and the SEC what they needed to charge Levine.[91]

The path then led to Boesky. Pitt employed a similar, but even more forceful, approach than he used with Bank Leu. At their pivotal meeting, Pitt told Boesky: "I can tell you what I think the government has got . . . but only you know the truth. If what you tell us isn't truthful and complete, the advice we give you will be defective."[92] Pitt also told Boesky that once he told his lawyers the truth, he could not change his story on the witness stand; the attorneys would withdraw from representing him rather than let him commit perjury.[93]

Boesky agreed to tell Pitt what had happened. As Pitt listened, he became amazed. Boesky was confessing to something far greater than he seemed to realize. The case was much more than trading tips with Levine. Boesky had conspired with Mike Milken to set up huge corporations for takeovers.[94]

Given the magnitude of Boesky's crimes, cooperation was not going to get him off the hook. But, buttressed by a truthful account, Pitt was able to counsel Boesky on how to cooperate most effectively and what to expect from the grueling process.[95] He also cut the best possible deal with federal attorneys. Boesky eventually pled guilty to only one felony and received a fine of \$100 million.[96] Milken, defended by the hardball tactics of Arthur Liman, would end up pleading guilty to six felonies and being fined \$600 million. Despite the fact that Milken was the top target, there is little doubt that his sentence was made more

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90. *Id.* at 241.
91. *Id.* at 244–47.
92. *Id.* at 277.
93. *Id.*
94. *See id.* at 186 (providing examples of Boesky and Milken's takeover tactics).
95. *See id.* at 278.
96. *Id.* at 291.

severe in response to the scorched earth tactics his team employed.[97]

Three things stand out in the Harvey Pitt account. First, Pitt had a strong commitment to obtain an honest and complete rendering of the facts from his client. Pitt asked for this upfront; in a sense, he conditioned his willingness to provide service on his client's full factual disclosure. Second, Pitt directly related having all the facts to his ability to provide the best advice. No shrinking violet, Pitt was not modest about his ability to help clients. But, he told them his best advice was only possible with complete honesty. Third, with all the facts on the table, Pitt could comprehend the issues more clearly than the clients. He could spot exposures that both Bank Leu and Boesky missed. This enabled Pitt to see the worst that could happen, the strategies that would not work, and the course that offered the best outcome. His knowledge and negotiating skills then delivered the best results his clients could expect.

One other fact bears emphasis. Pitt was prepared to withdraw from representation rather than be a party to his client's perjury on the witness stand. Generating billings did not trump Pitt's commitment to the law, his sense of the client's most fundamental interests, or the conditions he needed to serve them best.

The behavior of attorneys like Jordan Mintz and Harvey Pitt demonstrates only that under difficult conditions attorneys have found ways to fight for ethical outcomes that also serve the client. This tells us that effective representation in the face of questionable behavior is possible. It offers new attorneys role models and hope that they can be imitated. It does not mean that in today's circumstances it is easy to emulate their actions. This Commentary has argued that circumstances often put individual attorneys in weak positions when dealing with ethically challenged clients. Thus, to conclude, we must return to the circumstances cited earlier and reflect on changes that might allow attorney–client relations to return to a sounder footing.

VII. RESTORED UNDERPINNINGS FOR THE ATTORNEY–CLIENT RELATIONSHIP

We began by citing the agency problem and the resulting hidden agendas that can frustrate the best efforts of attorneys. The first point is that this is a corporate governance issue. More

97. *See id.* at 313, 435–36.

importantly, it is a governance issue in which attorneys should hold a major stake. Laws, regulations, and improved governance practices that cut down on rogue agent behavior also improve the environment for the practice of law.

In this regard, it would appear that the corporate legal community has a vested interest in seeing the essence of the Sarbanes–Oxley (SOX) law preserved.[98] SOX establishes clear accountability on the part of CEOs and CFOs for the accuracy of the firm's financial statements.[99] No longer is it easy for these executives to plead ignorance of the details or to hide behind the opinion issued by their public auditor. Personal liability and penalties are much clearer than before.

SOX thus creates explicit and personal risks for the top executives of client firms. Attorneys can cite these risks as compelling reasons for foregoing legally questionable transactions. Clarified accountability at the top also dovetails nicely with the ABA model rule advising attorneys to take issues of illegality to the highest authority in the organization.[100] Attorneys can now justify such escalations because the highest authorities now carry personal liability. Finally, SOX provides protection for whistleblowers.[101] This protection creates extra risk of exposure for those disposed toward questionable practices and should render them more receptive to cautionary advice. As Sherron Watkins, a famed whistleblower in her own right, wrote to Ken Lay: "We are under too much scrutiny and there are probably one or two disgruntled 'redeployed' employees who know enough about the 'funny' accounting to get us in trouble."[102]

It is not clear that the legal community has embraced SOX as a positive aid to its own integrity. Supportive comments were conspicuously absent when powerful leaders from Henry Paulson to Michael Bloomberg called for its revision. Partially, this reflects sympathy for the complaints of their corporate clients. It may also reflect a view that SOX is primarily a concern for accounting firms. Both views are shortsighted. The law strikes directly at the lack of accountability at the top that allows bad agent behavior to flourish. It is time for the legal community to find its voice and speak up strongly in support of SOX.

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98. *See* Sarbanes–Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (2002) (codified as amended in scattered sections of 11, 15, 18, 28 & 29 U.S.C.).

99. Sarbanes–Oxley Act of 2002, 15 U.S.C. § 7241(a) (2006).

100. MODEL RULES OF PROF'L CONDUCT R. 1.13(b) (2008).

101. Sarbanes–Oxley Act of 2002, 18 U.S.C. § 1513(e) (2006).

102. Sherron Watkins Memo, *supra* note 44, at 362.

A second area of attention concerns the way in which business ethics is taught in both law and business schools. Curriculums cover the waterfront. Many mix up ethical study with corporate social responsibility. Much of it flows out of philosophy departments that hardly have a practical bent. A diffusion of offerings, many tinged with impracticality, has fostered broad student disinterest in ethics coursework. This needs to be changed.

Refocusing ethics curriculums would be a good start. There is a need to treat these courses as professional training rather than an academic survey. This means grounding instruction in doing as many actual case studies as can be crammed into a semester. Repeat practice in spotting the ethical issues will help prepare students for the day when they must confront their first overzealous executive sponsor and his questionable deal. It also means teaching attorneys how to navigate tactically inside the decisionmaking processes of their clients. Attorneys should learn the ins and outs of ferreting out inconvenient facts and finding corporate allies to support the good cause. Students will want to know that there are many options to exhaust before having to take matters to the highest authority.

It might seem that law firms can do little to change the structure of the legal marketplace. That marketplace is highly competitive and likely to consolidate only under conditions no attorney wishes to see. That said, it may be time to reexamine whether law firms should pursue profit maximization in the same manner as an industrial company or financial firm. A profit maximizing mindset for a law firm can easily become focused on short term fee maximization. The acceptance of questionable business to prevent it from flowing to competitors risks infecting the firm with a "fixer's" mentality that can degrade the quality of advice over time.

As we enter a period of economic retrenchment and increased governmental regulation, firms would be well advised to revisit the timeframe over which they seek to realize profits. They may also want to retool their competitive strategies, putting more emphasis on knowing what business to decline and how to compete on reputation. With increased regulation and a more business-hostile political environment, clients may soon put a premium on advice that keeps them out of expensive litigation as opposed to the next technically brilliant deal structure.

As a final point, it can be argued that law firms enjoy too much insulation from the consequences of their advice. Clearly, this is a sensitive issue. Few firm managing partners are going to be leading the charge to increase their exposure to shareholder or other law suits. Bar associations have also been mounting effective resistance to efforts by the Justice Department to erode the attorney–client privilege and to efforts by the SEC to hold lawyers accountable in a manner similar to public accountants.[103]

Recognizing that this is a difficult and complex area, it still may be in the legal profession's long-term interest to face more accountability. Law firms today enjoy risk mitigants that accounting firms can only envy. Consider the example of V&E. As a limited liability partnership, the individual partners are insulated from personal liability. Typically, only the partnership itself can be sued.[104] Because the partnership holds minimal assets, plaintiffs are basically looking for insurance settlements.[105] Additionally, Texas state law provides insulation from negligence claims.[106] Given these facts, it was unsurprising that the Enron shareholders dropped V&E from their $60 billion suit in the interest of streamlining disposition of their case.

What sort of new laws or regulations might provide law firms the incentives to do the right thing? One possibility would be to increase the level of liability insurance that partnerships are required to carry. There could be a floor amount pegged as a percentage of firm revenue, with the required percentage escalating in the event the insurance is used to pay claims. Premiums, of course, would also go up to the extent that claims are paid. The principle here is to assure that insuring against litigation risk is a meaningful cost of doing business. This cost should also rise in the wake of failures, giving firms more incentive to minimize litigation risk and competitors more basis to compete on reputation.

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103. *See* Sheri Qualters, *State Bars Push Back on Waivers*, NAT'L L.J., Nov. 13, 2006, at 9 (describing the various state bar associations and their efforts to preserve the attorney–client privilege).

104. *See* TEX. REV. CIV. STAT. ANN. art. 6132b, § 3.08(a)(1) (Vernon Supp. 2008) (declaring partners in a registered limited liability partnership not individually liable for debts or obligations of the partnership).

105. *See* TEX. REV. CIV. STAT. ANN. art. 6132b, § 3.08(d)(1)(A)–(B) (Vernon Supp. 2008) (requiring limited liability partnerships to either carry a minimum $100,000 liability insurance policy or set aside $100,000 in funds for the satisfaction of judgments against the partnership); Walter W. Steele, Jr., *How Lawyers Protect the Family Jewels . . . The Invention of Limited Liability Partnerships*, 39 S. TEX. L. REV. 621, 629 (1998) (discussing mandatory insurance requirements for limited liability partnerships).

106. *See* TEX. REV. CIV. STAT. ANN. art. 6132b, § 3.08(a)(2) (Vernon Supp. 2008) ("A partner in a registered limited liability partnership is not individually liable, directly or indirectly, by contribution, indemnity, or otherwise, for debts and obligations of the partnership arising from errors, omissions, negligence, incompetence, or malfeasance committed while the partnership is a registered limited liability partnership . . . .").

The second concept would be to embed into law an affirmative responsibility for attorneys to bring illegal transactions to the attention of the highest authority in the firm. Such a provision would simply express as law a major canon of the legal profession's own code of conduct. The principle, however, would be to convert a voluntary professional code into positive law where there are established penalties for nonperformance. This again would increase risk of litigation and thus increase law firms' interest in promoting attorney behavior that minimizes such risk. Language for any such provision will be much debated. Attorneys will want adequate scope to apply their judgment before escalating matters to the top. Such scope cannot, however, be so expansive as to vitiate the lawyer's affirmative responsibility. Clear cut cases of failing to flag legality issues on transactions that close should bring consequences for the legal advisors and their firm.

VIII. A FINAL WORD

Our country and economy are entering a period where considerable structural reform is likely. Obvious problems and widespread popular disgust over their causes are creating an environment of political support for reform. Change, broad and deep, is in the air. Much of it will impact law firms' clients in ways that may make advising them easier.

It is not obvious that such reforms will directly touch the legal profession. That would be a missed opportunity. It is understandable that major law firms take comfort in the fact that they have suffered nothing like the damage that befell Enron, the banks that financed the company, or Arthur Anderson. However, escaping the consequences should not be confused with not having contributed greatly to the debacle. As the Powers Committee noted, Enron's management and board relied heavily on its outside counsel's "perceived approval . . . of the structure and disclosure of the transactions."[107] When those same transactions are subsequently exposed as artifices designed to mislead the markets, and when their corporate sponsors go to jail for securities fraud, how can the lawyers who approved the transactions not bear a great responsibility?

It is also worth noting that major scandals seem to be occurring with more frequency at the interface between corporations, banks, and the financial markets. Over the last twenty years, at least four major scandals have erupted:

107. REPORT OF INVESTIGATION, *supra* note 33, at 26.

(1) insider trading; (2) dot com stock research; (3) Enron/WorldCom accounting fraud; and (4) mortgage derivatives/debt ratings.[108] Nothing comparable in terms of frequency or severity occurred in the prior decades. There now appears to be an ever shorter cycle encompassing events of scandal, correction, and normal activity. This interface between corporations, banks, and the financial markets is a lawyer intensive zone. Multiple attorneys look at practically every document that governs transactions in this zone. The legal profession in general cannot be content providing comfort letters and opinions that facilitate a cycle of ever intensifying scandals.

It therefore is timely for senior leaders of major law firms to consider whether it is good for their profession to remain exempted from the changes that will soon unfold. Rather than adopting a business-as-usual posture or minimizing issues as primarily rooted in cultural misunderstandings, the profession needs to embrace the fact that it confronts structural and personal formation issues. That will be the first step in accepting the changes in training and structural reforms that will restore the profession's reputation.

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108. *See* Lawrence A. Cunningham, *The Sarbanes–Oxley Yawn: Heavy Rhetoric, Light Reform (And It Just Might Work)*, 35 CONN. L. REV. 915, 923–26 (2003) (chronicling the accounting frauds of the early 2000s and insider trading).