

Chicago Daily Law Bulletin®

Volume 157, No. 216

Thursday, November 3, 2011

New rule expands confidentiality limits

By Donald M. Devlin
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This is part one of a two-part series. The second part will be in Friday's paper.

The Illinois Rules of Professional Conduct, effective January 2010, have broadened the scope of client confidentiality. The prior Rule 1.6 stated that a lawyer could not "use or reveal a confidence or secret of the client" The new Rule 1.6 is much more expansive in nature. It states that a lawyer shall not reveal "information relating to the representation of a client" The new Rule 1.6, as did the old rule, establishes a flat prohibition regarding revealing or using client information and then it carves out certain exceptions. This is a two-part series dealing with just how some of these exceptions might come into play.

The problem

You have just finished a meeting in your office conference room with a longtime client, Bill, who built a successful brokerage/investment firm from the ground up. You have prepared many corporate documents for him. You have also dealt with regulators and the occasional difficult customer. You have prepared his Security Exchange Commission and state regulatory filings.

During the meeting, he seemed depressed and preoccupied. Then, as the meeting was ending, he blurted out that his business was a fraud, a big Ponzi scheme.

"It's not Madoff, but there is very little of it that is completely legitimate. I was nearly wiped out when the market tanked in October of '87," he said. "I had to start robbing Peter to pay Paul — then I just started robbing

Peter and Paul and everyone else. I've paid out just enough to keep people from getting suspicious. But if we have another steep market downturn and enough people decide to pull their money to the sidelines, I'm cooked. I can't cover."

The two of you sat in silence for a while, and then you said, "Bill, I have to think this over and talk with some other attorneys in my firm, but you should start thinking about filing for bankruptcy protection. One of the fellows in my office might be able to work out a deal with the U. S. attorney."

That startled Bill out of his funk. "I can't do that. I've got two kids in college and a wedding to pay for next spring. I'll find some way out of this. I've made it this long and I can keep it up longer. Don't say anything to anyone." He got up and walked out of the conference room, leaving you stunned.

Confidentiality and its limitations

It is generally against the nature of most lawyers to even consider revealing client information. The confidentiality of client information is one of the cornerstones of the practice of law and, indeed, our legal system as a whole. It facilitates the flow of information between client and attorney necessary for efficient legal representation. The client can provide necessary information secure in the knowledge that it will remain confidential. From their first moments in practice, lawyers are taught to guard information received from their clients. If a lawyer is conscientious, it becomes second nature.

But there is something greater than the sanctity of client confidentiality: In instituting the new rules, the Illinois Supreme Court explicitly found that a lawyer should never stand by and allow a client to commit a crime nor should the lawyer allow himself or herself to be used by a client to perpetrate a fraud. It would be illogical and perverse to allow the privilege when one of the purposes of retaining the lawyer is to commit a crime or fraud.

In part, Rule 1.6(b) (1), (2) and (3) allow a lawyer to reveal information relating to the representation of a client to the extent the lawyer reasonably believes disclosure is necessary:

"(1) To prevent the client from committing a crime in circumstances other than those specified in Paragraph (c) (preventing death or

substantial bodily harm);

"(2) To prevent the client from committing fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's services; and

"(3) To prevent, mitigate or rectify substantial injury to the financial interests or property of another that is reasonably certain to result or has resulted from the client's commission of a crime or fraud in furtherance of which the client has used the lawyer's services."

As in many aspects of the Rules of Professional Responsibility, the "rule of reason" applies. First, the lawyer's belief in his or her client's commission of a crime must be "reasonable." With respect to Subsections (2) and (3), the injury must be "reasonably certain to result" from the client's crime. As a final requirement, the lawyer's services must have been used in the furtherance of the crime or fraud alluded to in (2) and (3). If these elements are present, the Illinois Supreme Court's intent is clear as stated in Comment 7 to the Rule 1.6: "Such a serious abuse of the client-lawyer relationship by the client forfeits the protection of this rule." (Emphasis added.)

Beside preventing or ameliorating a client's fraud, the provisions of Rule 1.6(b) (2) and (3) provide the lawyer with a salutary advantage: They allow the lawyer to get out in front of an almost inevitable discovery of the client's nefarious activities and avoid allegations of complicity in that fraud. If the client has used the lawyer's services in perpetuating or attempting to perpetuate the fraud, Rule 1.6 gives the lawyer the opportunity to explain how he or she was unwittingly used in the client's scheme. This opportunity is much more valuable when used in disclosure of the client's fraud than it is when the fraud is discovered by others and the lawyer is called upon to explain his or her conduct. If, after counseling and remonstrating, the client agrees to reveal the fraud, the lawyer can assist the client in such a way as to make it known that he or she was not complicit in the crime.

Friday: A course of action, and a caveat.

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Volume 157, No. 217

Friday, November 4, 2011

Rule guides lawyers to report clients for fraud

By Donald M. Devlin and Jann M. Johnson

This is the second article of a two-part series dealing with the question of client confidentiality under Rule 1.6 of the Rules of Professional Responsibility. The first part was published in Thursday's paper.

You have discovered that the business of your client, Bill, is a fraud that endangers the investments and savings of his customers. Bill is unwilling to voluntarily reveal his fraud to his customers. You know that he has used your services to keep his fraud going. Although Rule 1.6 prohibits you from revealing "information relating to the representation of a client," you know that the rule contains exceptions for a fraud perpetrated by the client when a lawyer's services are used in furtherance of the fraud.

In adopting Rule 1.6, the Illinois Supreme Court, in the comments to the rule, made it clear that it is unacceptable for a lawyer to knowingly allow his or her services to be used in the furtherance of a fraud. When a client uses the lawyer's services in furtherance of a fraud, the client forfeits the protections of Rule 1.6.

A course of action

Before proceeding, you should ask yourself whether Bill's statements during the meeting gives rise to a reasonable belief that Bill has or is committing a fraud. It might be necessary for you to check your records or notes for clues regarding Bill's activities. Maybe circumstances that would be inconsistent or suspicious only in light of Bill's statements may crop up to corroborate Bill's statements. In any event, make sure that you are reasonably sure that Bill's business is a fraud.

You also must consider whether you are now in a position of a conflict of interest with Bill. Can you continue to represent Bill and counsel him regarding his affairs when you may decide to disclose Bill's fraud? In whose best interest will your advice be?

You should probably meet with Bill and explain the provisions of Rule 1.6 to him. You should tell Bill that you cannot allow your legal services to be used to perpetuate a fraud on his investors and that if he wishes to continue the

fraud, he will have to retain another attorney. You should also make it clear to Bill that Rule 1.6 (b) (3) is already implicated by his past fraudulent activities.

During this meeting, you can present procedures for ending the fraud while, as best as possible, minimizing the adverse consequences to Bill and his family. However, you should make it clear that if Bill refuses to end the fraud and take remedial measures, you will reveal the fraud to the authorities. In the event that you end up following the latter course, you should advise Bill that your attorney-client relationship is at an end and that he should retain other counsel since the situation has now put the two of you in a conflict of interest. You should give no further advice.

Finally, should you report Bill? Although the language of Rule 1.6 (b) (2) and (3) is discretionary in nature, it is clear that the Illinois Supreme Court has answered that question in the affirmative. Bill has "forfeited" the protections of Rule 1.6. In

adopting Rule 1.6 (b) (2) and (3), the Supreme Court threw you a lifeline. All you have to do is have the wisdom and courage to take it.

A caveat

The Illinois Rules of Professional Responsibility are based on the ABA Model Rules of Professional Responsibility with certain modifications for Illinois law, practice and tradition. It took four attempts before the ABA finally adopted Subsections (2) and (3) to Section (b) regarding financial crimes and fraud. There were two reasons for the reluctance of the ABA to expand the scope of disclosure beyond bodily harm. First, it did not want to dilute the attorney-client relationship of confidentiality with disclosures beyond a crime involving bodily harm. Second, it was concerned about potential tort liability. As one set of commentators has stated:

"They were also concerned that 'may disclose' would become 'must disclose' when lawyers factored in tort liability exposure under a new rule. In other words, if a lawyer may disclose, but chooses not to disclose, and a disgruntled investor sued the lawyer for failure to disclose, the lawyer may not be able to rely on her (his) ethical obligation not to disclose because it would have permitted disclosure. Hence, for tort purposes, 'may' might become 'must.' "

The subsections were finally adopted in 2003 in the wake of the Enron scandal and other financial problems.

The issue of tort liability may be addressed in some future case. As of this writing, the authors are unaware of any suits or decided appellate cases against an attorney or attorneys for failure to disclose a client's fraud pursuant to Rule 1.6 (b) (2) or (3).

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