On Submission By
Matthew S. Lerner

No.: 60

Court of Appeals
State of New York

MARC S. KIRSCHNER, AS TRUSTEE OF THE REFCO LITIGATION TRUST,

Plaintiff-Appellant,

---against---

KPMG LLP, GRANT THORNTON LLP, MAYER BROWN LLP, INGRAM MICRO INC., CIM VENTURES INC., WILLIAM T. PIGOTT, MAYER BROWN INTERNATIONAL LLP, PRICEWATERHOUSECOOPERS LLP, LIBERTY CORNER CAPITAL STRATEGIES, BANC OF AMERICA SECURITIES, LLC, CREDIT SUISSE SECURITIES (USA) LLC, DEUTSCHE BANK SECURITIES, INC.,

Defendants-Respondents,

BECKENHAM TRADING COMPANY, INC., ANDREW KRIEGER, ERNST & YOUNG LLP, TONE N. GRANT, ROBERT C. TROSTEN, REFCO GROUP HOLDINGS, INC., PHILLIP R. BENNETT, SANTO C. MAGGIO, EMF FINANCIAL PRODUCTS, DELTA FLYER FUND, LLC, AND ERIC M. FLANAGAN,

Defendants.

PROPOSED AMICUS CURIAE BRIEF

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PRELIMINARY STATEMENT

New York has a well-established body of law relating to the *in pari delicto* doctrine and the adverse interest exception. The *in pari delicto* doctrine itself—along with the related rule of standing known as the "*Wagoner*" rule—has its roots in ancient common law principles. The narrowly defined adverse interest exception in its current form stems back almost a half-century and is based on the age-old idea that the knowledge of an agent is presumptively imputed to his principal. Plaintiff Marc Kirschner, as Trustee of the Refco Litigation Trust ("the Trustee") now urges this Court to abandon this well-established body of law, in service of what he calls "the vital gatekeeping functions performed by professionals who serve corporate clients" (Br for Plaintiff-Appellant at 2). Attorneys already face regulatory, legal, and ethical limitations with respect to corporate fraud. This Court should reject the Trustee's invitation, in light of the doctrine of stare decisis and the impact his proposed rule would have on lawyers, law firms, and the attorney-client relationship.

The Trustee advances a broad interpretation of the adverse interest exception based on his claim that a departure from this well-established body of law is necessary to deter corporate fraud. Casting aside the rule requiring a "total abandonment" of a corporation's interests, the Trustee

argues that a corporation should be empowered to avoid imputation merely by showing that the insiders "actually received personal benefits" from the fraud, "and/or" that the fraud's ultimate disclosure led the corporation to suffer harm, which he claims is "self-evident[]" anytime a corporation files for bankruptcy. This proposed rule would dramatically alter established agency principles in an effort to maximize the ability of bankruptcy trustees to transform attorneys, law firms, and other professional service providers into insurers against bad corporate decisions by their clients' most senior executives. The Trustee has not demonstrated beyond conclusory statements why this Court should depart from well-established law on this subject.

Attorneys are not "gatekeepers" serving the public; instead, they owe a duty of loyalty to their clients. This duty includes rendering well-informed, forthright legal advice, within the constraints imposed by the rules of ethics. If this Court were to adopt the Trustee's rule, the consequences flowing from it will represent a sea change in the relationships attorneys have with their corporate clients. The broad definition of the adverse interest exception that the Trustee proposes will fundamentally alter the risk attorneys incur in their representation of corporate clients. This change will place a significant strain on the attorney-client relationship and undermine the loyalty attorneys owe to their clients, as they are increasingly exposed to

the risk of potentially crippling liability based on the decisions of their clients' own management. Effectively, the Trustee's proposed reformulation of the adverse interest exception would transform attorneys into enforcement agents against their own clients, requiring attorneys to police the strategic decisions made by corporate management in an effort to minimize their own liability. This is inconsistent with a bedrock principle of legal representation—namely, that an attorney's principal duty is to his or her client alone.

Indeed, imposing a gatekeeper role on attorneys and law firms may well be counterproductive to the goal of deterring corporate misconduct. Client communications will change if corporations know that their outside counsel has such a gatekeeping role. Such a role would inevitably chill client-lawyer communications and result in the exclusion of lawyers from strategic meetings, thus generally degrading the ability of lawyers to render well-informed advice to their corporate clients, including advice about avoiding or preventing illegal conduct by or for the corporation.

A gatekeeper role will also lead to defensive advising, where attorneys will err on the side of caution because of concerns about the possibility of their own liability. The preservation of client confidences will

also be disrupted if attorneys need to reveal those confidences to defend themselves in bankruptcy trustee litigation.

Further, the Trustee's rule would also impact the cost and availability of legal services. Under the Trustee's rule, as Defendants aptly point out in their Respondents' Brief, bankruptcy trustees will almost always avoid a dismissal on the pleadings based on the *in pari delicto* doctrine. Once past the motion to dismiss stage, the probability that an attorney or law firm will settle, irrespective of the lawsuit's merit, will dramatically increase. This phenomenon will encourage an increase in lawsuits against attorneys, law firms, and other professional advisors, which, in turn, will lead to higher malpractice premiums. Attorneys and law firms will have no choice but to pass on the higher costs to their corporate clients. The cost of doing business will thus increase, thereby harming corporations and their various constituencies, which include their employees. Certain smaller companies will then be priced out of obtaining these specialized legal services. Other fast-growing companies whose business models or finances are extremely complex will have difficulty obtaining legal services because attorneys or law firms will be hesitant to involve themselves in work where the risk of litigation outweighs the value of providing the legal services.

After independent investigations, both the New York City Bar and the American Bar Association ("ABA") have separately recommended against imposing a gatekeeper role on attorneys and law firms. DRI -- The Voice of the Defense Bar ("DRI"), as *Amicus*, agrees with their recommendations. Accordingly, and for the reasons that follow, this Court should not accept the Trustee's invitation to make a dramatic change in the narrow adverse interest exception. It should frame its answers to the certified questions based on the principle that the wrongdoing company itself cannot sue based on a fraud masterminded by its own management for its own benefit.

STATEMENT OF INTEREST OF AMICUS CURIAE

Pursuant to 500.23 of the Rules of this Court, DRI moves for leave to file this brief as *amicus curiae* in support of Defendants' position regarding five of the eight certified questions the United States Circuit Court of Appeals for the Second Circuit certified to this Court. DRI is an international organization that includes over 24,000 lawyers involved in the defense of civil litigation against corporations, government entities, and law firms, among others. Committed to enhancing the skills, effectiveness and professionalism of defense lawyers, DRI seeks to address issues germane to defense lawyers and the civil justice system, promote appreciation of the role of the defense lawyer, and improve the civil justice system. DRI has

long been a voice in the ongoing effort to make the civil justice system more fair and efficient.

DRI participates as *amicus curiae* in cases that raise issues of vital concern to its membership. This is such a case. The *in pari delicto* doctrine is important to professional advisors such as attorneys and law firms in defense of bankruptcy trustee litigation, and thus the answers to these certified questions are of particular interest to DRI's members.

DRI respectfully submits that the motion for leave to file this brief as *amicus curiae* should be granted.

ARGUMENT

I. COURTS SHOULD CONTINUE TO INTERPRET THE ADVERSE INTEREST EXCEPTION NARROWLY PURSUANT TO THIS COURT'S WELL-SETTLED AGENCY JURISPRUDENCE.

This Court's jurisprudence regarding the "adverse interest exception" is deeply rooted in New York's common law of agency. This Court's analysis of the presumption of imputation and the adverse interest exception in *Center v Hampton Affiliates, Inc.*, for example, hinged on ancient common law principles that form the underpinning of modern corporations law in this State (66 NY2d 782, 784 [citing, among other authorities, *Farr v Newman*, 14 NY2d 183 [1964]; *Henry v Allen*, 151 NY 1 [1896]]). This Court's analysis in *Center* indicates the stringency of the standard for invoking the adverse interest exception, even at the pleading stage of a lawsuit.

In *Center*, the plaintiff argued that the defendant corporation wrongly took delivery of shares of stock from a third party (66 NY2d at 784). The plaintiff claimed that the shares of stock were supposed to have been transferred to him (*id.*). The main issues on appeal to this Court were (1) whether the defendant corporation had imputed knowledge of the plaintiff's

adverse claim to the shares when it took delivery because its agent -- an attorney and director of the corporation -- had knowledge of the third party's obligation to the plaintiff, and (2) if so, whether the defendant corporation could successfully invoke the adverse interest exception.

In analyzing the applicability of the adverse interest exception, this Court recognized the long-standing general rule that the knowledge of an agent is presumptively imputed to the principal (*id.*). As the Court explained:

> The general rule is that knowledge acquired by an agent acting within the scope of his agency is imputed to his principal and the latter is bound by such knowledge although the information is never actually communicated to it (*Farr v Newman*, 14 NY2d 183, 187; *Henry v Allen*, 151 NY 1, 9, *see, Restatement [Second] of Agency § 272*, at 591). Underlying the rule is the presumption than an agent has discharged his duty to disclose to his principal "all the material facts coming to his knowledge with reference to the subject of his agency" (*Henry v. Allen*, *supra*, at p 9; *Marine Midland Bank v Russo Produce Co.*, 50 NY2d 31, 43) (*id.*).

Because the defendants did not dispute the general rule, this Court analyzed whether summary judgment was warranted based on the application of the adverse interest exception. This Court explained the exception, stating

> This exception provides that when an agent is engaged in a scheme to defraud his principal, either for his own benefit or that of a third person, the presumption that knowledge held by the agent was disclosed to the principal fails because he cannot be presumed to have disclosed that which would expose and defeat his fraudulent purpose . . . . To come within the exception, the agent must have totally abandoned his principal's interests and be acting entirely for his own or another's purposes. It cannot be invoked merely because he has a conflict of interest or because he is not acting primarily for his principal . . . .

(*id.* [quoted case law and authority omitted] [emphasis added]).

This Court found no triable issue of fact related to the adverse interest exception, stressing that a litigant cannot avoid the fundamental agency-law principle of imputation through speculation and conclusory assertions that the agent's true purpose was to enrich himself at the principal's expense (*id.* at 785). This Court held that conclusory assertions claiming that the agent "was seriously conflicted" throughout the transactions and tried to defraud the corporation "[did] not establish sufficient adversity as a matter of law to negate imputed knowledge to the corporation at the time it took delivery of the shares" (*id.*).

The holding in *Center* emphasized that the adverse interest exception is extremely narrow and requires a showing that the agent has "totally abandoned his principal's interests" and is "acting entirely for his own or

another's purposes" (*id.*). This strict standard has direct roots dating back almost a half-century (*see Farr*, 14 NY2d at 190-191), and has its origins in case law over a century old (*see Henry*, 151 NY at 11). New York courts continue to define the exception narrowly (*see e.g. 546-552 W. 146th St. LLC v Arfa*, 54 AD3d 543, 544 [1st Dept. 2008] [holding that the exception "cannot be invoked merely because the agents have a conflict of interest or are not acting primarily for their principal" and dismissing the complaint on its pleadings], *leave dismissed in part & denied in part* 12 NY3d 840 [2009]; *Bullmore v Ernst & Young Cayman Island*, 20 Misc 3d 667 (Sup Ct, NY County 2008) (holding that the adverse interest exception was inapplicable as a matter of law when the fraudulently inflated value of a hedge fund's portfolio resulted in higher management fees because the fraud permitted the fund to attract and retain capital from investors]).

The Trustee in this appeal has not demonstrated that the standard to invoke the adverse interest exception at the pleadings stage is unworkable (*People v Damiano*, 87 NY2d 477, 489 [1996] [Simons, J. concurring]). In fact, the public policy implications of expanding the exception's reach, as discussed in Sections II and III, *infra*, heavily weighs against adopting the Trustee's position. Consistent with the doctrine of stare decisis, well-settled authorities compel this Court to frame its answers to the certified questions

based on the principle that a wrongdoing company cannot so easily disclaim the corporate acts of its own officers and directors.

II. THE TRUSTEE'S PROPOSED RULE WOULD HAVE A DRAMATIC AND NEGATIVE IMPACT ON LAWYERS AND THE RELATIONSHIP BETWEEN LAWYER AND CLIENT.

Attorneys, law firms, and their corporate clients (small, medium, and large) will be dramatically impacted if this Court adopts the Trustee's proposed standard for the adverse interest exception. As Defendants aptly point out in their Respondents' Brief, "the Trustee's rule would make it nearly impossible for courts to resolve imputation issues on pleadings [because] [i]n virtually every case, the plaintiff can allege that the insiders intended to benefit themselves" (Defendants' Br at 31). Under the Trustee's rule, attorneys and law firms named as defendants will be faced with a real economic dilemma -- i.e., settle a lawsuit with the bankruptcy trustee, even if the lawsuit is baseless, or incur large litigation defense costs, disrupt business, and move forward to defend against the lawsuit (*see* Lin, *Lawyers' New Nightmare: Bankruptcy Trustee Suits*, NYLJ, Nov. 26, 2007, at 1, col 3 ["Getting past a motion to dismiss is often enough for the bankruptcy trustee to extract a settlement."]; Lewinbuk, *Let's Sue All the Lawyers: The Rise of Claims Against Lawyers for Aiding and Abetting a Client's Breach of*

Fiduciary Duty, 40 Ariz. St. L.J. 135, 169 [2008] [noting that aiding and abetting cases are "'less likely to result in summary judgment for the attorney'" and will probably go to trial, costing the defendant attorney a substantial amount of time and money]). This dilemma adds to the existing incentive for attorneys and law firms to settle bankruptcy trustee lawsuits against them (*id.*). Bankruptcy trustee lawsuits are "highly disruptive to ongoing practices, and most law firms think they will be unsympathetic defendants should a case ever get to trial" (*id.)*.

Attorneys and law firms are already facing an increase in these types of lawsuits. Several interrelated factors already exist that motivate bankruptcy trustees to sue attorneys, law firms, and other professional advisors. The collapse of a number of major businesses has sparked an increasing number of bankruptcy trustee lawsuits in the past two decades (Sloan, *Legal Malpractice Suits May Surge*, www.law.com [Feb. 23, 2009] <http://www.law.com/jsp/article.jsp?id=1202428510900> [accessed July 14, 2010] [noting that one New York legal malpractice attorney predicted an increase in legal malpractice suits initiated by bankruptcy trustees that target attorneys who worked for the bankrupt entity]; Johnson, *The Unlawful Conduct Defense in Legal Malpractice*, 77 UMKC L. Rev. 43, 48 [2008] [same]). Law firms, like other third-party professional service providers,

"are appealing targets because they tend to have more resources than the now-bankrupt corporation and are therefore more likely to be able to pay damage awards" (Wasserman, *Can the Trustee Recover? Imputation of Fraud to Bankruptcy Trustees in Suits Against Third-Party Service Providers*, 77 Fordham L. Rev. 365, 366 [2008]).

Bankruptcy trustees already have a strategic advantage against law firms in this type of lawsuit. "Bankruptcy trustees in large corporate failures can generally tap multi-million-dollar litigation trusts, allowing them to more vigorously pursue their claims against firms" (Lin, *supra*). In some cases, distressed-debt hedge funds, which buy bankruptcy claims on the cheap as an investment, drive the trustees' inclination to sue lawyers and other third-party providers (*id.*; *see Maxwell v KPMG LLP*, 520 F3d 713, 718 [7th Cir. 2008] [noting that a trustee of a defunct business has little to do besides filing claims that if resisted he may decide to enforce]).

In the face of these incentives, the *in pari delicto* doctrine takes on heightened importance. A bankruptcy trustee has every incentive (and ample funding) to shift as much cost as possible to third parties in an effort to maximize the value of the estate (Frey et al., *An Introduction to Bankruptcy Law* 423 [3d ed. 1997]). He or she enters the forum knowing that attorneys and law firms are averse to litigating lawsuits asserted against

them (Lin, *supra*). Trustees are looking for deep pockets, which tend to be with the insurance companies and the professionals (Abbott et al., *Old Code, New Code: Views on Bankruptcy From the Bench and Bar: Panel 1: A Deeper Look at Deepening Insolvency*, 4 DePaul Bus. Comm. L.J. 529, 534 [2006]). As one bankruptcy litigator recently noted, trustees will "fight for every two or three cents" (Lin, *supra* [quoting bankruptcy litigator Denis F. Cronin]). Another bankruptcy litigator at a law-school symposium explained the tenacity of trustees, stating

> [w]e are scrappy trustees' and creditors' committee professionals, and we are good at it. And what we do well is -- and I spend a lot of my time doing that -- is scratching and clawing and trying to get leverage, to find a way to get recovery from those who have money for the creditors (Abbott, *supra*, at 546).

The Trustee's expansive interpretation of the adverse interest exception would only add fuel to the fire. Under the Trustee's rule, a bankruptcy trustee—knowing that the *in pari delicto* doctrine will likely have no teeth at the pleading stage—will be more apt to sue the debtor's outside counsel and force a settlement, irrespective of the merits of the lawsuit, once the suit survives a motion to dismiss.

Even beyond bankruptcy trustee lawsuits, attorneys and law firms have already encountered an increase in actions asserted against them in the

past few years. Poor economic conditions, like this state and country have been experiencing for the past few years, often precipitate an increased number of suits against professional advisors (*see e.g.* Forsloff, *Legal Malpractice Claims Increase in Recession*, Digital Journal [May 10, 2009] <http://www.digitaljournal.com/article/272436> [accessed July 14, 2010] [noting that there has been a recent increase in suits against attorneys and that increases frequently coincide with economic downturns]); Zahorsky, *Clients, Law Firms Get 'Savage' As Legal Malpractice Claims Increase*, ABA Journal [Feb. 17, 2009] [noting that "[a]ttorney malpractice claims are escalating in numbers and intensity . . . ."])[1]; Shimshak and Welber, *In New Economy, 'Wagoner' Doctrine Takes On Added Significance*, NYLJ, Feb. 19, 2002, col 1 [observing that claims against third-party advisors increase in difficult economic conditions]); ABA Press Release, Sept. 30, 2008 http://www.abanet.org/abanet/media/release/news_release.cfm?releaseid=469 [accessed July 13, 2010]) ("The frequency of claims goes up as the economy goes down."). This increase in lawsuits has resulted in a substantial increase in malpractice coverage sales (*see e.g.* Fisher, *Sue the Lawyers!*, Forbes Magazine, Dec. 28, 2009 [noting that the amount of

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[1] The article may be found at <http://www.abajournal.com/news/article/clients_law_firms_get_savage_as_legal_malpractice_claims_increase/> [accessed July 14, 2010].

malpractice coverage sold to in-house counsel has increased 150% since 2006])[2]; Lewinbuk, *supra*, at 169 ["The number of third party aiding and abetting as well as conspiracy claims against attorneys arising in the context of their representation of clients has risen tremendously in the last 15 years, resulting in a serious concern for attorneys and their malpractice insurance carriers."]).

Any more of an increase in the number of claims filed against attorneys and law firms could in turn result in increased malpractice insurance premiums. Potentially higher premiums and the disruption of malpractice litigation to an attorney's or law firm's ongoing practices increase the likelihood of a change in numerous aspects of legal services for companies in the future. For one, attorneys and law firms will pass increased expenses of doing business onto their clients. Legal services will be more expensive and, as such, the cost of doing business will be more expensive for corporations. This harms corporations and their various constituencies, which include their employees, and the public (*see generally Stoneridge Inv. Partners, LLC v Scientific-Atlanta, Inc.*, 552 US 148, 163-64 [2008] [describing dangers of raising costs on business to public]; Winter, *Paying Lawyers, Empowering Prosecutors, and Protecting Managers,*

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[2] This article may be found at <http://www.forbes.com/forbes/2009/1228/outfront-sarbanes-oxley-bribery-sue-lawyers.html> [accessed July 14, 2010].

Raising the Cost of Capital in America, 42 Duke L.J. 945, 962 [1993] ("overbroad doctrine tends to deter beneficial activity and to undermine capital markets"). These concerns are especially pronounced for "newer or smaller companies" that may be unable to obtain the specialized legal services necessary to run a company successfully (*Cent. Bank of Denver, N.A. v First Interstate Bank of Denver, N.A.*, 511 US 164, 189 [1994]). Also, fast-growing companies whose business models or finances are extremely complex will find it more difficult to obtain legal services (Lin, *supra*). The complexity of the work will make attorneys or law firms hesitant to involve themselves where the risk of litigation outweighs the value of providing legal services to the company.

A broader adverse interest exception would also impact the quality of legal services. One commentator predicts that "[i]t is certain that such 'overbroad liability might diminish the quality of legal services, since it would impose "self protective reservations" in the attorney-client relationship'" (Lewinbuk, *supra*, at 169). She notes,

> [a]ttorneys will constantly try to balance their duty to zealously represent their clients with the fears of potential exposure to liability in instances when their legal advice may disregard the interests of the third parties. In fact, the "mere threat of an aiding-and-abetting claim is enough to create pause in an attorney's zealous representation of her client and force her to consider her own self-interests -

> resulting in a damned-if-you-do/damned-if-you-don't situation" (*id.*).

This concern creates tension with the bedrock duty of a lawyer to render forthright advice to his or her client (*see* Rules of Professional Conduct [22 NYCRR 1200.0] rule 1.4 [a] [2]). The possibility of defensive advising by attorneys concerned about their own liability directly conflicts with an attorney's role as an advocate for his or her client.

The possibility of an increase in lawsuits against attorneys and law firms in this context also raises concerns about the attorney-client privilege. A chilling of client-lawyer communications is almost inevitable where attorneys are concerned about the possibility of their own liability. One commentator explains this concern, stating

> [S]uch claims also often lead to unwanted disclosure of the privileged communications between the attorney and her client, thus "rupturing . . . any client relationship that may have pre-existed." Such disclosure will likely be unavoidable in a majority of aiding and abetting cases as the attorney will need to establish how much she knew or did not know about her client's alleged breach of fiduciary duty. In such instances, the attorney-client privilege covering confidential communications will likely be waived without the client's consent (Lewinbuk, *supra*, at 170).

This concern begs the question as to how attorneys will be expected to defend themselves without waiving their clients' confidential

communications. Moreover, as discussed further below, the chilling effect on attorney-client communications will impair the ability of attorneys to provide well-informed advice to their clients—even with respect to how the company can avoid illegal or fraudulent conduct.

As demonstrated, the risk of an increase in lawsuits asserted against attorneys and law firms will ultimately harm the public. The consequences flowing from broadening the definition of the adverse interest exception warrant this Court's adherence to its long-standing rules of agency law (*see Center*, 66 NY2d at 784).

III. THIS COURT SHOULD NOT TRANSFORM LAWYERS AND LAW FIRMS INTO PUBLIC GATEKEEPERS.

If this Court were to broaden the requirements necessary to satisfy the adverse interest exception, bankruptcy trustees will shift as much cost as possible to third parties such as attorneys and law firms. As such, the Trustee's proposed rule will essentially cast attorneys and law firms into the role of "gatekeepers" or insurers against corporate fraud. Such a role would create an inevitable conflict with an attorney's ethical duties to his or her client.

Attorneys owe a duty of loyalty to their clients. This duty includes rendering well-informed, forthright legal advice. In light of recent corporate bankruptcies, the New York City Bar investigated whether attorneys should be duty-bound to play a gatekeeper role for the protection of the investing public (New York City Bar Association Task Force on the Lawyer's Role in Corporate Governance Report, Nov. 2006).[3] The Task Force did not favor the recognition of a duty to the investing public by lawyers representing public companies (*id.* at 64). It observed that "[r]ecognition of a duty to the investing public would represent a sea change in the ethical duties of

[3] The Report can be found at : <http://www.abcny.org/pdf/report/CORPORATE_GOVERNANCE06.pdf> [accessed July 12, 2010]).

lawyers and potentially in their relationships with clients" (*id.* at 61). The Task Force warned that "[a]ll of the consequences of such a fundamental change cannot be predicted" (*id.*).

One consequence that the Task Force was able to predict, however, is a chilling of communications between attorneys and clients (*id.*). It noted that "clients would be more guarded in sharing information with their lawyers, and less inclined to include attorneys in meeting to discuss sensitive issues, if attorneys were viewed as having whistle-blowing duties to the investing public" (*id.* at 61-62).

In addition to the potential conflict created by imbuing lawyers with a duty to the *public*, the "gatekeeper" role would also magnify the tension between the client's interests and the interests of the lawyer or law firm itself. The New York Bar Association's Task Force expressed concern about the problem of "defensive lawyers," where attorneys will err on the side of overly conservative advice to clients to minimize or ward off the risk of liability (*id.* at 63).

The ABA has cited the same consequences concerning casting attorneys and law firms in a "gatekeeping" role to the investing public. In an April 2, 2003 letter to the then-Secretary of the SEC, the ABA President recommended against the gatekeeping role that certain proposed sections of

the Sarbanes-Oxley Act of 2002 contemplated (Alfred P. Carlton, Jr. Letter to Jonathan G. Katz, Apr. 2, 2003).[4] For example, the ABA recommended against a proposed rule known as the "noisy withdrawal" provision, which would have required outside attorneys to withdraw and notify the SEC of the withdrawal because of "professional considerations" and to disaffirm any violative document or filing (Volz & Tazian, *The Role of Attorneys Under Sarbanes-Oxley: The Qualified Legal Compliance Committee as Facilitator of Corporate Integrity*, 43 Am. Bus. L.J. 439, 465 n 10 [2006]). The SEC ultimately did not adopt the "noisy withdrawal" provision (*id.*).

In both instances, the New York City Bar and the ABA concluded that to impose general whistle-blowing or gatekeeping duties on lawyers—so contrary to their traditional role as confidential advisors to their clients—would be counterproductive. In fact, the bar organizations' reasons for rejecting imposing a "gatekeeper" role for attorneys representing public companies are, if anything, more persuasive as applied to lawyers for private companies—as Refco was for most of the relevant period. DRI agrees with the bar associations' conclusions because imposing those duties would

[4] The Letter can be accessed at: <http://www.abanet.org/buslaw/committees/CL410000pub/comments/20030402000000.pdf> [accessed July 17, 2010]).

fundamentally change the role of attorneys and degrade their ability to render well-informed advice to their corporate clients.

Attorneys already face regulatory, legal, and ethical limitations with respect to corporate fraud (*see e.g.* 22 NYCRR 1200.0 rules 1.2[d] [lawyer shall not counsel client to engage, or assist client, in conduct lawyer knows is illegal or fraudulent], 1.4 [a] [2] [reasonably consult with the client about the means by which the client's objectives are to be accomplished]; 3.3[a][3][b] [lawyer shall not knowingly offer or use evidence that the lawyer knows to be false]; 4.1 [Truthfulness in statements to others]; 8.4[b] [lawyer or law firm shall not engage in illegal conduct that adversely reflects on the lawyer's honesty, trustworthiness or fitness as a lawyer]; 8.4[c] [lawyer or law firm shall not engage in illegal conduct that adversely reflects on the lawyer's honesty, trustworthiness or fitness as a lawyer]). Placing enforcement responsibility on corporate outside counsel would be an unprecedented step with potentially sweeping consequences. DRI urges this Court to decline the Trustee's invitation to make such a change.

CONCLUSION

For the foregoing reasons, this Court should respond to the certified questions as follows:

Question 1: This Court should decline to answer "the over-arching question whether the allegations of the complaint in this case satisfy the 'adverse interest' exception," which requires consideration of federal pleading standards. If this Court does answer this question, it should hold that the complaints' allegations do *not* satisfy the adverse interest exception to the *Wagoner* rule.

Question 2: *No*, the adverse interest exception is not "satisfied by showing that the insiders intended to benefit themselves by their misconduct."

Question 3: *Yes*, "the exception is available only where the insiders' misconduct has harmed the corporation."

Question 4: *No*, such harm may not include "any detriment to a corporation resulting from the eventual unmasking of the misconduct."

Question 7: *Yes*, the adverse interest exception "is precluded where the misconduct conferred some benefit upon the corporation."

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