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In-House Counsel's "Constituencies" Professional Obligations In The Post Sarbanes-Oxley World Here Come The Regulators

By Robert Max Crane

It used to be easy. As General Counsel or Assistant General Counsel to XYZ Corporation you represented the "Company" and traditionally reported to the CEO (if the General Counsel) or to the General Counsel (if an assistant in the General Counsel's office). Things have gotten a lot more complicated. Forget Enron, Tyco and MCI. They now seem like old news. Although they continue to be embroiled in ongoing unresolved investigations, new and more nuanced challenges to in-house legal departments are cropping up daily in the post Sarbanes-Oxley world. Just ask the General Counsel at Marsh & McLennan who recently resigned from his position. Although as of the writing of this article, no one directly involved has commented on the circumstances surrounding his departure, a recent *Wall Street Journal* piece was quoted as highlighting a primary reason as the recent inquiry by the New York Attorney General's office relating to certain Marsh practices and the New York Attorney General's dissatisfaction with Marsh's General Counsel "showing that an "old school" approach in defending financial firms won't fly with aggressive regulators these days."

It used to be hard enough for in-house counsel to balance professional responsibilities between the CEO and the Board of Directors. This became even harder in the post-Enron and Sarbanes-Oxley environment where Boards were reinvigorated with their charge of managing the Corporation for the benefit of the shareholders rather than the Corporation's executive officers. As not only the Board, but the various committees of the Board were also reinvigorated with revised charters and increased responsibility, this balancing act was made even more difficult. And we still have not gotten to the shareholders. When Sarbanes-Oxley was first instituted, one of the primary motivators was to nudge Boards of Directors and their committees away from the excessive influence of executive officers of the Corporation and to realign them with their ultimate constituency, the Corporation's shareholders. Since, in essence, the Corporation's shareholders were the ultimate employer of all in-house executives including those in the General Counsel's office, the Board of Directors was to be the conduit for and manager of shareholder perspectives and views, even if different from the CEO's. The Board's clear mandate was to communicate these views to management and ultimately accept responsibility for their implementation, if not execution.

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As if the interplay between CEOs, Boards of Directors, Board Committees and the shareholders and the relationship of the General Counsel to each was not complicated enough, things are becoming more complicated. Everyone has understood the argument that the shareholders, the ultimate owners of a Corporation,

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benefit from a financially successful and robust company. As long as the Corporation and its executives are performing their job at the highest level, complying with law and the shareholders are making money, all should be well – right? Not so fast. Enter the regulators…sort of.

In-house counsel are more and more frequently being called upon to assist, and, in some cases, perhaps even initiate internal investigations relating to a variety of corporate activity. As the point person in the recent New York State Attorney General investigation of Marsh, the General Counsel was the "point man" in interfacing with Eliot Spitzer's office. While cooperating with the investigation, it appears as if Marsh's General Counsel also took it upon himself to be an advocate for the manner in which Marsh conducted its business and the facts surrounding the manner in which it conducted its business. It appears from recent articles and commentaries as if the Attorney General's office took exception to Marsh's General Counsel's advocacy approach in large part because the facts as revealed by certain e-mails suggested a conclusion different from the one being advanced by its General Counsel, presumably on behalf of Marsh.

The implications of the Marsh investigation and the resignation by its General Counsel are enormous. Since the earliest days of law school, attorneys are trained to be zealous advocates for their clients. This is no less true for in-house counsel than it is for external outside counsel. Since in-house counsel's "client" is the Corporation, part of his or her traditional duty is to be an advocate for that Corporation. However, it would appear that the playing field is shifting. Before being too ardent an advocate for a Corporation, in-house counsel now has to consider the ramifications to his client, the Corporation, as well as to him or herself. The tight-rope act between being an advocate for your Corporation and "cooperating" with various governmental authorities has become an even more difficult act than ever before. Even as an honest and vigorous advocate for your Corporation, one can run afoul of the authorities.

In the Marsh example, the nature of the circumstances surrounding the conduct that may have led to the General Counsel's resignation were unusual and potentially troublesome. Reports seem to suggest that while the Marsh General Counsel cooperated with the New York Attorney General's office, the cooperation was not of the quality expected by that office. In deciding he would not deal with Marsh senior management, including its General Counsel, Attorney General Spitzer believed that the conduct at issue should have been discovered by the Corporation itself and brought to the Attorney General's attention. There are at least two troubling aspects to this perspective. The first appears to be the creation or suggestion of a new type of duty to be imposed on in-house counsel, i.e., to essentially act as an investigative arm of the Attorney General, as necessary, even if it means acting against in-house counsel's own client's interest (presumably as articulated or condoned by the CEO or the Board). An additional potential problem is that the Attorney General's office, which is essentially charged with enforcement of rules, policies and decisions of various executive agencies has extended its reach past enforcement and into regulation. In bypassing the regulators in the Marsh case, the New York Attorney General's office has substituted its "expertise" for that of the regulators charged in this area. Is this permissible? Is this good policy? A Corporation's dilemma is that by the time it tests out these developments, its reputation, etc. has been tattered and it is forced to make the hard choice – give up the right to "defend" itself by utilizing traditional channels or potentially sacrifice its ability to do business (at least reputationally) in the short and perhaps the long term.

What is in-house counsel to do? While there is no clear answer in every situation, the first step is that in all events the position taken by a Corporation either directly, or through its General Counsel, has to be one that is grounded in fact. While different parties might reach different conclusions relating to the same set of facts, what has always been untenable and what potentially triggered the New York Attorney General's animus in Marsh was the perception that Marsh's General Counsel sought to alter, reshape or ignore the facts. The question becomes whether, in order to develop the facts and, thereafter, the Corporation's position relating to those facts, the Corporation should be permitted to be in a reactive mode by responding to inquiry from "regulators" or whether it should be in a proactive mode and consider conducting its own internal investigation when confronted with the possibility of potential internal wrongdoing. Like it or not, while the consequences and methodology of conducting an internal investigation are too detailed for this article (they have their own set of evolving rules and strategies, i.e., having such investigation initially handled by outside counsel, preserving attorney-client privilege, etc.), invariably, taking the proactive position will ultimately stand the Corporation in better stead with the regulators than reacting after the fact. In this environment anything less is fraught with risk – personal risk and ultimately, risk to the shareholders. While it is true that any such investigation may lead to an unpleasant set of circumstances and an awareness thereof may force the Corporation into a position where it has to take certain tough actions, this is at its core among the rationales behind the Sarbanes-Oxley legislation and its rule-making progeny as well as the recent actions of various state and federal regulators. Ultimately, while there may be some short term dislocation to the Corporation's financial prospects, in the long-run, so the argument goes, the shareholders will benefit because it will avoid situations where the Corporation's reputation, long term economic success or even survival comes into question. Moreover, the referenced course of conduct has the ancillary benefit of allowing a General Counsel or someone in the General Counsel's office to discharge his or her professional responsibility in a manner which is not only ultimately good for the shareholders, but consistent with any ethical issues that may arise.

While many may complain about recent governmental actions which force corporations into positions of doing the regulators' job for them, this is the current environment and as the *Wall Street Journal* article commented in connection with the resignation of the Marsh General Counsel, "those that would act in the old fashioned way illustrates how little tolerance there is for company lawyers who use the old play book of taking their company's view on good faith without taking the lead on internal investigations into potential problems." So for those in the General Counsel's office, who thought the entire list of "constituencies" to which they were responsible was covered by the universe of executive officers, Boards of Directors and shareholders they can now add to that group the category of regulators and attorneys general.