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Commentary on the Epistemology of Corporate-Securities Lawyering: Beliefs, Biases and Organizational Behavior

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COMMENTARY: *THE EPISTEMOLOGY OF
CORPORATE-SECURITIES LAWYERING: BELIEFS,
BIASES AND ORGANIZATIONAL BEHAVIOR**

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As a full time academic administrator my claims to subject matter expertise are much diminished. Nevertheless, Professor Norman Poser graciously asked for my comments on Professor Langevoort's wonderful Article on the epistemology of corporate and securities lawyering. Professor Langevoort's Article, which I have renamed "When Bad Things Happen to Relatively Good Companies," is a model of the best in contemporary legal scholarship. It begins with a sophisticated review of research from literature that is not often cited in legal scholarship, in particular focusing on the literature of management science (business psychology). Professor Langevoort utilizes this non-legal perspective to generate important insights about substantive law, legal education, and practical issues for corporate lawyers.

The Article reminds us of the range of tasks that our graduates who will practice business law will face. It implies that our obligation is to provide a broad range of exposure to different kinds of learning experiences when training corporate practitioners. A principal lesson of the Article is that we are training our graduates to exercise judgment in the context of uncertainty, uncertainty as both law and facts. Moreover, we are training our graduates to practice in a profession that is experiencing ongoing dramatic restructuring. These changes raise questions about whether historic professional values such as lawyerly independence can be sustained. Because the Article is an archetype of the best in contemporary academic

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legal discourse, I will comment on its implications for legal scholarship, legal education, and the structure of the legal profession.

Currently, there is a great debate about the nature of academic scholarship in law. Some important voices have suggested that legal scholarship produced by law professors has lost its way.¹ The claim is made that most legal scholarship has become irrelevant to the profession as a whole. The critics claim academic lawyers are producing little traditional practical doctrinal scholarship that can be of immediate use to practicing lawyers and judges.² Instead, too much scholarship is written primarily for an audience of other academic lawyers.

Legal scholarship comes in three basic flavors. Traditional legal (doctrinal) scholarship is largely based on an internal critique. This mode of scholarship relies almost exclusively on analysis of legal texts and text-based structural arguments, and applies rules generated by precedent.³ To the extent that non-legal perspectives are deemed relevant to such an analysis, these perspectives are invoked secondarily in making prudential arguments. A second type of scholarship comes from the "Law and . . . movement." "Law and . . ." scholarship generates descriptive and normative arguments about law based upon the intellectual capital of another discipline. The impact of "Law and . . ." scholarship has been very strong as the consequence of the use of economic insights in developing legal rules on an enormous range of issues.⁴ The third type of scholarship is empirically based social science scholarship, a

¹ Harry T. Edwards, *The Growing Disjunction Between Legal Education and the Legal Profession*, 91 MICH. L. REV. 34 (1992).

² There is some substantial empirical question about whether the amount of doctrinal scholarship produced by academics has declined. Considering the growth in the number of law professors and the number of law reviews, it is in fact likely that the amount of traditional doctrinal scholarship produced by academics has actually increased. Robert W. Gordon, *Lawyers, Scholars, and the "Middle Ground,"* 91 MICH. L. REV. 2075, 2099-2101 (1993). Moreover, as the legal profession has increased in size, the commercial publishing market has responded by providing a wealth of new treatises and looseleaf services. A third level of traditional practical scholarship is provided by the bar itself through publications by continuing legal education providers.

³ For a particularly clear account of the styles of argument from this perspective, see DENNIS PATTERSON, *LAW AND TRUTH* 135-142 (1996).

⁴ These areas include environmental, tort, and corporate law.

type of scholarship that looks at the social context of rule formation and enforcement and the actual social consequences of the implementation of a particular legal rule or regime.⁵

Professor Langevoort's Article is a classic of the "Law and . . ." mode. He thoughtfully examines the management science literature on the predictable sources of bias in business decision making. This enables Professor Langevoort to develop a new framework in which to look at legal issues such as proof of scienter in securities fraud actions, efficacy of supervision in the assessment of corporate liability, and the conundrum of whether reliance on the advice of counsel should be a defense to particular types of claims. By identifying in a systematic manner the phenomenon of cognitive conservatism, over-optimism, and commitment bias, his suggestions for legal evaluation of managerial behavior are greatly enriched. Professor Langevoort recognizes that these sources of bias have real adaptive value for managers, but the challenge is to develop ways of ascertaining when these types of bias create significant difficulties.

The Article also ties the sources of cognitive bias to evaluating the role of the business lawyer in counseling. A challenge is to develop ways for the lawyer to retain sufficient cognitive independence while capturing the benefits of being an in-group participant. The lawyer can add real value by bringing cognitive independence to analysis of a transaction, but cannot have a perspective so different than management that she is thought to be irrelevant by managers. The tension is between the lawyer as a full in-group participant and the lawyer as inefficient deal killer. Thus, Professor Langevoort's explanation of the practice of lawyer's overthreatening is most significant. Mediating the tension becomes all the more complex when we recognize that the lawyer's own economic interest does not fully match that of the firm she is representing.

From the perspective of the intellectual history of American legal scholarship, Professor Langevoort's work falls solidly with the realist tradition. The mixture of using

⁵ A good quantity of this scholarship in recent years has analyzed the structure of the legal profession. *See, e.g.,* MARC GALANTER & THOMAS PALAY, *TOURNAMENT OF LAWYERS: THE TRANSFORMATION OF THE BIG LAW FIRM* (1991).

economics and business psychology to elegantly elaborate upon whether the policy basis of a legal rule is sensible reflects the dominant mode of scholarly discourse since at least the 1940s.⁶ Professor Langevoort is a "bricoleur."⁷ Like other American legal realists he collects ideas from economics, psychology, and sociology, to develop practical prescriptive proposals. In the area of corporate law and policy making the impact of this mode of discourse has been powerful. The discourse has affected the decisions of legislators, administrators and judges in areas such as integrated disclosure, the market for corporate control, and the calculation of damages in securities fraud actions. Such scholarship is practical in that, just like traditional doctrinal scholarship, it enables lawyers to better analyze existing rules and predict future developments. Moreover, as a normative matter, legal policy is best created when it is informed by theory, empirical evidence, and a good sense of the craft of lawyering. Thus, scholarship like Professor Langevoort's remains important to both academic and practicing lawyers. As the Scots would say, claims of a great disjunction between the academy and the practicing bar is not proved.

Professor Langevoort's Article also has important implications for the development of law school based training for future corporate lawyers. In most typical first year doctrinal law school classes the facts are controlled. Students seem to get positive feedback from making creative, even outlandish arguments. They are rarely asked to exercise judgment in a client centered manner. Competition among law schools and pressure from the practicing bar⁸ has led to a reassessment of whether this type of education is sufficient. There is an increased understanding that to create well trained self-learners, legal educators must expose students to a set of educational experiences richer than simply teaching legal doctrine and analysis. For example, it is now accepted

⁶ Gordon, *supra* note 2, at 2081-82.

⁷ The notion of the legal realist as a bricoleur comes from N. E. H. HULL, ROSCOE POUND AND KARL LLEWELLYN: SEARCHING FOR AN AMERICAN JURISPRUDENCE 10-11 (1997).

⁸ The pressure from the bar reflects at least in part the growing competition in the legal profession. Because of the desire to control costs, the bar wishes to off-load costs traditionally borne by practitioners and clients to the law schools.

that law students should be trained in interviewing, counseling and negotiation. Law students should also be prepared to do fact investigations. A client centered perspective informs this broader notion of legal education. Students gain a greater understanding that often *ex ante* neither the facts nor the law are fixed. The essence of lawyering is exercise of judgment under conditions of uncertainty.

There is almost uniform recognition that the skills a new graduate needs can best be taught by traditional classroom teaching enriched with experiential learning through simulations and clinical teaching. A broad-based standard model exists for the teaching of general litigation skills. Most law schools today teach pretrial advocacy, trial advocacy, and interviewing, counseling and negotiation through simulations. In addition, students participate in actual client representations through law school clinics.

I would like to sketch out a model for teaching broad based skills to students who are planning to be transactional lawyers. Professor Langevoort's Article focuses our attention on some issues in training future transaction lawyers. In the basic business organizations class, many professors now include such exercises as interviewing mythical clients about a choice of entity problem or those which engage the students in writing a simple opinion letter on a transaction where the student needs to conduct some modest simulated fact investigation. In upper level courses, more complex simulations can involve students in counseling simulated clients on the typical problems that a young in-house counsel may face. In such exercises, the student must understand the business background and factual basis of the problem as well as the legal issues. To develop the client centered perspective, the attorney work product could be a client memo aimed at the business person.⁹ The capstone to such an education might be a semester long simulation of a complex transaction such as a management buyout.¹⁰ Actual

⁹ At Rutgers we teach a semester long course on corporate counseling, where students complete four counseling projects. This course is taught with the assistance of a number of in-house counsel who provide the problems and often serve as the "clients."

¹⁰ For a description of such a course, see Karl S. Okamoto, *Learning and Learning-to-Learn by Doing: Simulating Corporate Practice in Law School*, 45 J. LEGAL EDUC. 498, 502-12 (1995).

representations of clients in clinical experiences could be offered in conjunction with a Small Business Administration Development Center.

In teaching transaction oriented courses, we must consciously highlight for students the sources of cognitive bias in clients and in ourselves as lawyers. In teaching such courses, my experience is that students often take opposed extreme positions. Some start by taking all of the representations of their clients at absolute face value without critical review; others assume that their clients are underhanded thieves that must be cross-examined obnoxiously as hostile witnesses. As we know, neither position is correct. Professor Langevoort gives us a framework for working with students on the much more subtle role of sympathetic detachment. Thus, our efforts at skills training are informed and enriched through explicit reference to academic research.

Professor Langevoort's Article is also an important part of the growing literature concerning the state of professionalism in the practice of law. In this literature, there is much discussion about the perception that there has been a decline in the ethical norms of legal practitioners. Many commentators deplore a perceived lack of civility among lawyers and a decrease in the ability of lawyers to give truly independent counsel to our clients. There is a fear that there has been a decline in the technical competence and the ethical conduct of the bar.

The academic in me wants to ask some tough questions about these perceptions. As we are faced with increasingly intense economic competition among lawyers, is the current interest in professionalism merely a nostalgic questing for a return to a guild-like practice that may have existed in nineteenth century rural America? It is clear we are no longer the tight guild of earlier times. By 1990, law had become a \$91 billion service industry employing more than 940,000 people.¹¹ The range of practice settings has become increasingly complex. The profession now supports the 1000 lawyer mega-firm, the traditional one or two person local law office and everything in between. Law has also become a much more

¹¹ U.S. Industrial Outlook 1991, Professional Services: Legal Services (SIC 81), at 52-4.

personally diverse profession. In the past two decades there has been an explosion of women and minorities entering the profession. At the same time, economic competition among lawyers has escalated significantly.

The increasing complexity of society is fundamentally impacting the practice of law. We are in the midst of a technological revolution based on computers and the transmission of information at extraordinary rates that will fundamentally transform many legal tasks. A proficient lawyer must now have a range of skills from the traditional legal reasoning and argumentation skills to the skills of understanding intricate scientific questions that may arise in litigation or transactional work to the ability to operate complex computer systems that are now a necessary part of the practice of law.

As a former antitrust lawyer, I confess a great affection for the competitive process and change through innovation. Law should not be immune from the forces of competition. Clients *do* benefit from active competition among lawyers. Sophisticated purchasers of legal services, particularly the larger corporations that are the focus of Professor Langevoort's Article, are seeing a dramatic impact in the methods of providing service. The days of the unquestioned fee-for-service hourly rate billing for corporate clients by outside counsel are long gone. And many corporations are internalizing almost all of their legal work, including the most sophisticated transactional work. Even individuals have seen a decline in the relative expense of such services as probate and residential real estate transactions.

As discussed in my comments on legal scholarship and legal education, a major focus of Professor Langevoort's Article relates to the professional value of lawyerly independence. The conventional story is that increased competition within the legal profession leads to a loss of traditional lawyerly independence. Professor Langevoort shows that the conventional claim is that simple. In the current economic climate for the legal profession, there are pressures both for and against lawyerly independence. Both the status of in-group member and the status of independent expert have adaptive value.

As the legal profession continues to restructure, we need more research linking structure and incentives to performance. In particular, a fruitful area for further empirical research is the effect of the expansion of in-house corporate counsel representation on independence. In-house counsel are pulled in two directions on developing and maintaining independence. Certainly there may be more of a risk for in-house counsel of developing in-group bias. On the other hand, the attenuated pressures for revenue through direct billings might enhance incentives for appropriate independence. The balance of pressures may be affected by the methods of compensation for in-house counsel and the ways in which services are billed out to the operating unit.

Another opportunity to gain insight into the problem of cognitive independence is to compare notions of independence in accounting and law. The accounting profession is also undergoing significant restructuring as mergers are decreasing the number of firms that have the capacity and reputation to audit large publicly traded companies. Moreover, accounting firms are increasingly seeing the consulting side of their business as a major source of revenue. Some have expressed the concern that independence in auditing will be sacrificed in the battle to compete for consulting income. How each profession reacts to economic changes offers an occasion to reexamine the regulation of independence through ethical rules. The examination of the issue across professions can only enrich the inquiry.