Protecting Consumers: Attorney Ethics and the Law Governing Lawyers

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By Christopher M. Fairman

I. Introduction

A dialogue on the issues confronting lawyers involves with consumer financial services law and litigation is incomplete without exploring attorney ethics, the law governing lawyers, and professionalism. Lawyers specializing in consumer financial services law, both in-house and as outside counsel, face one of the same concerns that exist for the practice of law in general: What are the sources of ethical rules governing lawyers? What are the emerging issues in professional responsibility? What impact does alternative dispute resolution have in the area? In addition, lawyers specializing in consumer financial services law and litigation also confront increasing ethics regulation targeted at their practice. These issues and other recent developments in professional responsibility of importance to lawyers practicing in the financial services area are considered below.

II. Sources of Ethical Rules

A. Sources of Guidance

Lawyers are subject to multiple sources of ethical rules. The Model Rules of Professional Conduct continue to be the standard source for most jurisdictions’ ethical rules. However, the older Model Code of Professional Responsibility remains applicable in key jurisdictions. These traditional sources of ethical guidance must also make room for increasing federal regulation of attorney conduct. Added to this mix are the increasing use of alternative dispute resolution and the new ethical rules that accompany them. One conclusion is clear: A lawyer must now be familiar with more than a single ethics code.

B. Model Rules of Professional Conduct

First adopted in 1983, the American Bar Association’s (ABA’s) Model Rules of Professional Conduct (Model Rules) remain the chief source of ethical rules for lawyers. Most states have adopted codes based on the Model Rules.

Two states, Nebraska and Iowa, recently converted to the Model Rules. Nebraska is the most recent convert, adopting new rules based on the Model Rules effective September 1, 2005. This brings the number of jurisdictions that pattern their lawyer rules after the Model Rules to forty-seven.

Even in the minority of jurisdictions that follow the older Model Code, the Model Rules provide an increasingly important source of ethical rules for a number of reasons. For example, a lawyer not admitted in a jurisdiction is subject to the disciplinary authority of that jurisdiction if the lawyer provides or offers to provide legal services in the jurisdiction. Additionally, under the choice-of-law provisions, in a matter
before a tribunal, the rules of the jurisdiction in which the tribunal sits typically apply. For all other conduct, the rules of the jurisdiction in which the lawyer's conduct occurred apply, unless a particular conduct clearly has a predominant effect in another jurisdiction. Additionally, there is variety in the ethical codes adopted by the federal district courts.

Despite their general applicability, the Model Rules are just that—a model that state jurisdictions can accept, reject, or modify. After a series of significant revisions adopted in 2002 (in response to the Ethics 2000 project) and in 2003 (in response to the corporate scandals that fueled the Sarbanes-Oxley Act), the current Model Rules may not reflect a specific jurisdiction's ethical rules, even if those purport to be "based upon the Model Rules." Consequently, care must be taken when comparing state lawyer codes and the Model Rules.

For example, the Florida Supreme Court recently adopted a set of rules amendments incorporating some, but not all, of the 2002 and 2003 changes to the ABA Model Rules. Both Nevada and Mississippi recently took a similar approach with changes to their respective Rules of Professional Conduct.

C. Model Code of Professional Responsibility

1. Introduction

The ABA's old Model Code of Professional Responsibility is of dwindling relevancy. Only a handful of states retain professional rules based on the old Model Code. The holdouts are New York, and Ohio. California and Maine do not follow either the Model Code or the ABA's newer Model Rules. However, both Ohio and New York are in the process of abandoning the Model Code and shifting to the Model Rules format.

2. Ohio

Ohio adopted the Ohio Code of Professional Responsibility on October 6, 1970, basically enacting the ABA's old Model Code. On March 10, 2003, the Chief Justice of the Supreme Court of Ohio announced the creation of a special Task Force on the Rules of Professional Conduct. The eighteen-member Task Force was charged with engaging in a comprehensive review of the Ohio Code of Professional Conduct, the Model Rules, and the ABA Ethics 2000 revisions. The Final Report of the Task Force was completed in October 2005. According to the Task Force, "[b]y adopting the Model Rules, Ohio will become more relevant in national discussions on the subject of legal ethics." The public comment period on the proposed adoption of the Ohio Rules of Professional Conduct ended on Feb. 15, 2006. In the spring of 2006, the Supreme Court considered the public comments and additional recommendations of the Task Force.

3. New York

On September 30, 2005, after nearly three years of study, the Committee on Standards of Attorney Conduct (COSAC) of the New York State Bar Association issued a report proposing adoption of the ABA Model Rules. Just as the multi-year process has unfolded in Ohio, the earliest the New York Rules could be ready for court consideration and adoption is November 2007. The proposed Model Rules have "a reasonable chance of being accepted," according to COSAC chair Steven C. Crane.

D. Federal Regulation

Federal regulation of attorney conduct is not new. The Patent and Trademark Office regulates patent lawyers. The Internal Revenue Service regulates tax lawyers to some extent. However, the Sarbanes-Oxley Act of 2002 ushered in an era of renewed interest in regulating lawyers by the federal government.
1. Securities and Exchange Commission

The Sarbanes-Oxley Act mandated the Securities and Exchange Commission (SEC) to promulgate “minimum standards of professional conduct for attorneys appearing in practice before the commission.” Complete treatment of the requirements and implications of the new SEC regulations promulgated in January 2003 are beyond the scope of this article. However, the intersection of SEC regulation with state ethics regulations on the disclosure of confidential information provides an interesting lens with which to view the complex landscape of the laws governing lawyers.

Section 307 of the Sarbanes-Oxley Act requires the SEC to issue rules setting forth minimum standards of professional conduct for attorneys appearing and practicing before the SEC including a rule: (1) requiring an attorney to report evidence of a material violation of securities law or breach of fiduciary duty or similar violation by the company or any agent thereof, to the chief legal counsel or the chief executive officer of the company (or the equivalent thereof); and (2) if the counsel or officer does not appropriately respond to the evidence (adopting, as necessary, appropriate remedial measures or sanctions with respect to the violation), requiring the attorney to report the evidence to the audit committee of the board of directors of the issuer or to another committee of the board of directors comprised solely of directors not employed directly or indirectly by the issuer, or to the board of directors.

SEC Rule 205, “Standards for Professional Conduct for Attorneys Appearing and Practicing Before the Commission in the Representation of an Issuer,” was adopted to meet this statutory mandate and became effective on August 5, 2003. Section 205.3 of Rule 205 sets forth the duty of an attorney appearing and practicing before the SEC to report evidence of a material violation of securities law or a breach of fiduciary duty to the chief legal officer and chief executive officer of the client company and, if an appropriate response is not forthcoming, to the audit committee of the board of directors or to the board itself. This is now commonly referred to as “reporting up.” Section 205.3(d)(2) contains a provision permitting, but not requiring, what is commonly referred to as “reporting out,” as described below:

An attorney appearing and practicing before the SEC in the representation of an issuer may reveal to the SEC, without the issuer’s consent, confidential information related to the representation to the extent the attorney reasonably believes necessary:

- to prevent the issuer from committing a material violation that is likely to cause substantial injury to the financial interest or property of the issuer or investors;
- to prevent the issuer, in a SEC investigation or administrative proceeding from committing perjury, proscribed in 18 U.S.C. section 1621; suborning perjury, proscribed in 18 U.S.C. section 1622; or committing any act proscribed in 18 U.S.C. section 1001 that is likely to perpetrate a fraud upon the SEC; or
- to rectify the consequences of a material violation by the issuer that caused, or may cause, substantial injury to the financial interest or property of the issuer or investors in the furtherance of which the attorney’s services were used.

Section 205.6 of SEC Rule 205 addresses sanctions and discipline. Section 205.6(c) provides:

An attorney who complies in good faith with the provisions of this part shall not be subject to discipline or otherwise liable under inconsistent standards imposed by any state or other United States jurisdiction where the attorney is admitted or practices.

The “reporting out” rule is not a problem for lawyers practicing in most jurisdictions. Forty-two states have ethics rules allowing or requiring lawyers to report out under the circumstances described by SEC Rule 205. Eight states and the District of Columbia, however, prohibit disclosure of such confidential client information. Lawyers practicing in these jurisdictions face a dilemma. If an attorney reports out, the attorney could be subjected to disciplinary charges by the state bar. If the attorney does not report out when allowed under the SEC rule, the attorney could face a civil claim by injured investors arguing that the lawyer helped the corporate client commit a civil wrong. The claimant could rely on the SEC Rule 205 to argue that the lawyer was permitted to disclose and declined to do so.

According to the SEC, there is no dilemma because Rule 205 preempts contrary state rules. The SEC position relies on Fidelity Federal v. de la Cuesta, which held that a federal regulation preempts conflicting state law if the agency intended to preempt state law and the agency action was within the scope of its delegated authority.

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20. See id.

21. Id.

Whether SEC Rule 205 effectively preempts state ethics rules limiting the ability of lawyers to disclose information about their clients is a matter of dispute. In 2003, the Washington State Bar Association, in an interim formal ethics opinion, concluded that the state rule prohibiting disclosure of a client’s confidential information was to be followed because the SEC rule permits, but does not require, reporting out. By not disclosing information, an attorney could comply with both state and federal rules. 23

In contrast, the North Carolina State Bar Association recently reached the opposite result. 24 North Carolina agreed with the SEC that under Fidelity, a federal regulation preempts state ethics rules if it was the federal agency’s intention and was within its scope of authority. According to North Carolina State Bar Association, “the [SEC’s] intention to preempt state ethics rules conflicting with Rule 205 is unambiguous.” 25 Finding it beyond the capacity of an ethics opinion to determine whether the provision was validly promulgated, the North Carolina Formal Ethics Opinion concludes that “unless and until the Fourth Circuit Court of Appeals or the U.S. Supreme Court determines that Rule 205 was not validly promulgated, (a) there will be a presumption that Rule 205 was promulgated by the [SEC] pursuant to a valid exercise of authority and (b) a North Carolina attorney may, without violating the North Carolina Rules of Professional Conduct, disclose confidential information as permitted by Rule 205 although such disclosure would not otherwise be permitted by the [North Carolina] Rule.” 26

2. The Lawsuit Abuse Reduction Act of 2005

The so-called Lawsuit Abuse Reduction Act of 2004 that died in Senate Committee last year was reincarnated in this Congress as the Lawsuit Abuse Reduction Act of 2005 (LARA or H.R. 420). 27 The stated purpose of H.R. 420 is to prevent the filing of frivolous lawsuits. According to the bill’s sponsor: “The filing of frivolous suits by attorneys across the nation has made a mockery of our legal system. Instead of concentrating on real cases that need timely rulings, our courts today are forced to wade knee-deep in a pool of false claims and unscrupulous plaintiffs. These suits have increased insurance premiums and raised healthcare costs.” 28

However, others argue that the perception of court dockets being filled with frivolous lawsuits lacks foundation. As Professor Arthur Miller recently said: “the supposed litigation crisis is the product of assumption.” 29 Those touting the view that frivolous lawsuits are being filed often rely mainly on anecdotes of seemingly silly lawsuits. 30

Critics of LARA argue that when empirical research is examined a different picture emerges. For example, rising insurance and healthcare costs may be real, but the link to litigation is questionable. The two most recent empirical studies on the issue reach the same conclusion: The likely cause of insurance premium spikes is insurance market dynamics, not litigation. 31

Perhaps the most compelling evidence concerning frivolous litigation comes from the federal judiciary itself. At the request of the Judicial Conference’s Advisory Committee on the Federal Rules, the Federal Judicial Center recently surveyed a representative sample of federal judges. On the issue of the frequency of groundless litigation, eighty-five percent responded that it was a small problem (thirty-two percent), very small problem (thirty-eight percent), or no problem at all (fifteen percent). 32 Consequently, it can be said that those who deal with these claims on a daily basis barely get their shoes wet, much less “wade knee-deep in a pool of false claims.”

Despite the evidence that there is not a real problem with meritless lawsuits, LARA directly targets Rule 11 of the Federal Rules of Civil Procedure and would reinstate a prior version of Rule 11 that was in place for a decade and subsequently was rejected because of its well-documented negative effects. 33 It would eliminate judicial discretion and transform Rule 11’s permissive sanctions into mandatory ones. It would remove the “safe harbor” provision that currently allows parties to avoid sanctions if they withdraw the challenged filing within twenty-one days of notice. Further, LARA would transform the very nature


33. Rule 11 currently requires that every pleading, written motion, and other paper be signed by at least one attorney of record. This signature certifies to the court that to the best of the person’s knowledge, information, and belief, formed after an inquiry reasonable under the circumstances that:

(1) it is not being presented for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation;

(2) the claims, defenses, and other legal contentions therein are warranted by existing law or by a nonfrivolous argument for the extension, modification, or reversal of existing law or the establishment of new law;

(3) the allegations and other factual contentions have evidentiary support or, if specifically so identified, are likely to have evidentiary support after discovery is complete; and

(4) the denials of factual contentions are warranted by existing law or by a nonfrivolous argument for their absence.

of Rule 11 by requiring sanctions to be sufficient not only to deter future violations, but to compensate parties as well. Finally, it would expand the reach of Rule 11 to cover discovery disputes.

These "back-to-the-future" amendments to Rule 11 are probably unwise. For nearly a century, Rule 11 laid dormant. Then in 1983, it was amended to encourage courts to use their power to sanction. In its 1983 incarnation, sanctions became mandatory following a finding of violation. Rule 11 was broadened to apply to discovery motions. Instead of going to the court, monetary sanctions were commonly paid to the other party, creating a litigation incentive. Rule 11 was dormant no more.

By 1985, just two years after amendment, Rule 11 had become a tool of abuse, rather than a tool for curbing abuse. The problems under the 1983 version are well documented. Litigation costs increased as Rule 11 motion practice took on a life of its own. Fear of mandatory sanctions created a chilling effect, causing parties to avoid raising even meritorious claims and defenses; the burden of the rule fell disproportionately on plaintiffs.

To correct these problems, Rule 11 was amended in 1993 to include many of the beneficial provisions that H.R. 420 would strip away. The 1993 amendments gave flexibility to the district courts to determine whether sanctions were appropriate and what form they should take. With deterrence as the stated purpose of the rule instead of compensation, monetary sanctions were generally to be paid to the court. Discovery motions, already subject to sanctions by Rules 26 and 37, were removed from Rule 11 altogether.

Explicit provision was made for litigants to have notice and an opportunity to respond before sanctions were imposed. The beneficial effects of these changes have been to reduce Rule 11 litigation and equalize the burden of the rule. H.R. 420 would undo these valuable provisions, with predictable results. Rule 11 litigation would increase. The mandatory nature of sanctions, an explicit provision for compensation to parties, and the lure of attorneys' fees can create a financial incentive for those who can afford to litigate the applicability of sanctions. Additionally, by striking subsection (d), the inapplicability to discovery, new rounds of motion practice would ensue over whether Rule 11, discovery sanctions, or both should apply. Meanwhile, the chilling effect would return due to the combination of mandatory sanctions coupled with the abolition of the safe harbor provision. These deleterious effects would, of course, fall disproportionately on plaintiffs—especially civil rights plaintiffs—as post-1983 research indicates. It is therefore unsurprising that eighty-seven percent of the federal judiciary favor the current version of Rule 11; the reforms proposed by H.R. 420 are preferred by only four percent.

All of the negative effects of LARA described above would be magnified by application of the new Federal Rule 11 to selected state cases. However, this provision, requiring state-court judges to determine if a state-court civil action "affects interstate commerce" and if so to apply Federal Rule 11 is, on its face, probably unconstitutional. While Congress has the power to regulate interstate commerce under Article I, section 8, and the power to set procedural rules for the federal courts, it has no constitutional authority to preempt state rules of civil procedure. LARA states that it applies to "any civil action in State court" and requires on motion a determination within thirty days "whether the action affects interstate commerce." Presumably the Commerce Clause could support Rule 11 application if there is a finding of an effect on interstate commerce, but where is the constitutional authority to order the state court to hold the hearing in the first place? Most state court actions do not affect interstate commerce. Consequently, there is no constitutional basis to require the state court to hold the initial hearing required by LARA. In this regard, H.R. 420 would create a gross encroachment on our system of federalism and state control over state judicial systems.

Even if it were constitutional to impose Rule 11, the proposed application is still undesirable. It would yield even more litigation and confusion. Because of its application to "any civil action," a party with resources could unilaterally impose a new round of motion practice with all the inherent costs and delays. Consider a typical civil action for divorce. Either party could file a motion. Given that the determination is to be "based on an assessment of the costs to the interstate economy, including a loss of jobs," a departing spouse might come within the provision. Surely this is not desirable. However, given the lack of clarity, state court judges could be inundated with mandatory requests for such a determination.

The mechanics of the provision are equally troubling. What is the threshold effect on interstate commerce that would trigger application of Rule 11? LARA provides slim guidance. The court would be directed to assess the costs to the interstate economy—including job losses. What quantum of job loss is necessary? Presumably, the court can consider other factors besides job loss, but how are they to be weighed in the new interstate commerce equation? Is the determination to be based on the pleadings alone? Is discovery stayed or encouraged on the motion? It is easy to envision the judicial confusion—and litigant uncertainty—generated by this test alone. Given these serious concerns about LARA, it is not surprising that the fate of H.R. 420 appears to be the same as its sibling from the last congressional session. After passing the House with

36. See Giorgio M. Voino, Rule 11: Where We Are Going, 50 Fordham L. Rev. 475 (1991); Charles E. Weir, THE LAW OF FEDERAL COURTS 486 (5th ed. 1994) (describing American Judicature Society study finding that 20.5% of plaintiffs attorneys and 17.5% of defense attorneys reported not asserting sanctions claim or defense due to Rule 11); Fed. R. Civ. P. 11 advisory committee notes (1993 Amendment) ("The changes...will serve to equalize the burden of the rule upon plaintiffs and defendants.");
37. See Charles Yahn, Midnight, Regret, and Safe Harbors in Rule 11 Litigation, 37 Loy. U. A. L. Rev. 599, 600 (Winter 2004) (concluding that the 1993 amendments have reduced motion practice and that safe harbor provision works to protect access to the courts).
38. See RAMS & WALLACE, supra note 32, at 14.
a vote of 228-184 on October 27, 2005, it was referred to the Senate Judiciary Committee on October 31, 2005. At this writing no further action has been taken.\footnote{For additional analysis of H.R. 420, see Christopher M. Fairman, House Politics, A Frivolous New Bill Ignores Lessons Learned from Rule 11, Legislative, June 13, 2005, at 76.}

3. The Class Action Fairness Act of 2005

On February 18, 2005, President Bush signed into law the “Class Action Fairness Act of 2005” (the Act).\footnote{See Class Action Fairness Act of 2005, Pub. L. No. 109-2, 119 Stat. 4 (2005); Anthony Rollo and Gohbír A. Cliveon, Mapping the New Class Action Frontier—A Primer on the Class Action Fairness Act and Amended Federal Rule 23, 59 Consumer Fin. L. Q. Rep. 11 (2005).} Despite its title, the Act is targeted at limiting the effectiveness of class actions by expanding federal diversity jurisdiction over multi-state class actions. The Act reflects a growing willingness of Congress to involve itself in federal civil procedure, especially in an attempt to curb what it sees as frivolous lawsuits. The legislation also targeted certain settlement practices deemed abusive. As such, the Class Action Fairness Act is an attempt to improve the ethical behavior of attorneys.

The key provision of the Act is to provide federal jurisdiction, with some exceptions, for class actions with one hundred or more members and over $5 million in controversy, provided there is diversity between at least one plaintiff and one defendant. The Act permits liberal removal of class actions filed in state court even by in-state defendants. The combination of the use of minimal diversity requirements and liberal removal provisions reflects a clear congressional intent to move large class actions into the federal forum.

The Act also targets a number of settlement practices. Coupon settlements, often a way to provide something for the plaintiff class in lieu of cash, can no longer form the basis for inflated attorney fees awards. Instead of basing attorney fees on the face value of the coupons (which are frequently unused), the Act requires counsel fees to be calculated on the value of the coupons actually redeemed. Moreover, federal courts can reject the face value altogether and examine the actual value of the coupons to the class. Additionally, the Act restricts certain practices that could cause disproportionate settlements, such as increased awards to those who are closer geographically to the court or provisions requiring class members to pay more to class counsel than they receive in the settlement.

The Act also attempts to increase scrutiny over proposed settlements by requiring notice to the Attorney General or the appropriate state official within ten days of filing the proposed settlement. The Act applies only to those class actions filed on or after February 18, 2005.

4. FTC Regulation Under the Gramm-Leach-Bliley Act

Not all attempts at federal regulation of attorney ethics succeed. The United States District Court for the District of Columbia recently struck down the Federal Trade Commission’s (FTC’s) attempted application of the privacy provisions of the Gramm-Leach-Bliley Act (GLB Act) to attorneys.\footnote{See New York State Bar Ass’n v. Federal Trade Comm’n, 377 Fed. Supp. 2d 110 (D.D.C. 2005).} In an earlier opinion, the district court noted the “approximately two hundred years of exclusive state regulation” and reiterated the dominant role of states in the regulation of attorneys.\footnote{See New York State Bar Ass’n v. Federal Trade Comm’n, 377 Fed. Supp. 2d 110 (D.D.C. 2005).}

The D.C. Circuit recently affirmed in a consolidated appeal the district court’s decision in NYSBA.\footnote{See Amos v. FTC, 540 F.3d 457 (D.C. Cir. 2008) (holding that attorneys engaged in practice of law are not “financial institutions” within the meaning of the statute requiring protection of consumers financial information).} After five years, the organized bar can declare victory, at least for now, over the FTC’s effort to regulate the confidentiality of law office files; the FTC allowed the deadline for filing for review in the Supreme Court pass in March 2006.\footnote{See Rhode Island Bar Ass’n v. Federal Trade Comm’n, 10 F. Supp. 2d 283 (D.D.C. 1994), affirmed, 846 F.2d 1561 (D.C. Cir. 1988).}

D. Supreme Court and Federal Rules

While direct congressional and federal agency meddling with ethics rules may be problematic, another source of attorney ethical guidance is not: the United States Supreme Court. On April 12, 2006, the Supreme Court approved, \textit{inter alia}, a new appellate rule requiring federal appeals courts to allow attorneys to cite unpublished opinions in court pleadings. Rule 32.1 of the Federal Rules of Appellate Procedure now states that a court of appeals cannot prohibit a party from citing an unpublished opinion of a federal court.

Previously, four appellate circuits (the Second, Seventh, Ninth, and Federal Circuits) forbade citation to their unpublished opinions in unrelated cases. In six other circuits (the First, Fourth, Sixth, Eighth, Tenth, and Eleventh Circuits), citation to unpublished cases was discouraged. In the remaining three circuits (the Third, Fifth, and D.C. Circuits), citation to unpublished opinions was already permitted.

New Appellate Rule 32.1 will apply prospectively, affecting only unpublished opinions issued after January 1, 2007.\footnote{See Amos v. FTC, 540 F.3d 457 (D.C. Cir. 2008) (holding that attorneys engaged in practice of law are not “financial institutions” within the meaning of the statute requiring protection of consumers financial information).} The new appellate rule was forwarded to the Supreme Court by the U.S. Judicial Conference in September 2005 and will take effect on December 1, 2006 unless Congress blocks implementation. No such Congressional blockage is expected.\footnote{See Ralph Linder, Supreme Court Approves Rule Change Allowing Unpublished Opinions Citations, 25 ABA/SBA Joint’s Manag. on Prof. & Ethics: Current Reports 104 (Apr. 19, 2006).}

E. Alternative Dispute Resolution

The recent explosion in the use of alternative or appropriate dispute resolution procedures (ADR) is well known.\footnote{See infra pt. III.B. (noting additional civil rule changes).}
While arbitration has been used in America since the eighteenth century, the use of commercial arbitration has recently increased exponentially. Undoubtedly, the United States Supreme Court’s recent and repeated support for a “liberal federal policy favoring arbitration” has fueled the expansion. Use of arbitration is likely to continue to increase, as research reflects that the majority of participants in binding arbitration proceedings see the process as faster, less expensive, and simpler than litigation in court. As ADR’s reach expands, new ethical questions emerge as traditional lawyer-as-advocate models fail to address the newer, dynamic roles of attorneys in this context. The ethical codes governing lawyers were at first slow to respond. However, today there is no dearth of ethical guidelines in the ADR context. This multiplicity—and lack of uniformity—is part of an emerging ethical problem in this field. Key new rules adopted or proposed in this area are considered infra this article at Parts IV.A.-C.

III. Emerging Issues

A. Attorneys and Consumer Protection Statutes

1. Fair Debt Collection Practices Act

A divided panel of the Fourth Circuit U.S. Court of Appeals recently held that attorneys hired as trustees to foreclose on mortgages qualify as “debt collectors” and must comply with the Fair Debt Collection Practices Act (FDCPA). In Wilson, Chase Manhattan Mortgage Corporation retained Draper & Goldberg to foreclose on Karen Wilson’s property due to her failure to make the mortgage payments. Draper & Goldberg wrote to Wilson on several occasions concerning the debt and ultimately initiated foreclosure. Wilson then sued alleging that the law firm violated the FDCPA by failing to verify the debt, by continuing collection efforts after she had contested the debt, and by communicating directly with her when they knew she was represented by counsel. The district court granted summary judgment in favor of the law firm, ruling that trustees foreclosing on property pursuant to a deed of trust are not “debt collectors” under the FDCPA and that actions taken by a trustee in foreclosing on a property pursuant to a deed of trust may not be challenged as FDCPA violations.

A Fourth Circuit panel held that the district court incorrectly concluded that the law firm could not be held liable under the FDCPA: “We hold that Defendants’ foreclosure action was an attempt to collect a ‘debt,’ Defendants are not excluded from the definition of ‘debt collector’ under 15 U.S.C.A. section 1692a(6)(F)(i) merely because they were acting as trustees foreclosing on a property pursuant to a deed of trust, and Defendants can still be ‘debt collectors’ even if they were also enforcing a security interest.” As a result, the court reversed the summary judgment and remanded.

The court made clear that its decision was not intended to bring every law firm engaging in foreclosure proceedings under the ambit of the FDCPA. Nevertheless, the FDCPA applies to lawyers who regularly engage in consumer-debt-collection activity, even when that activity consists of litigation. Because Congress enacted the FDCPA to eliminate abusive debt collection practices by debt collectors, lawyers who regularly engage in consumer-debt-collection activity should not be allowed to thwart this purpose merely because they proceed in the context of a foreclosure. Given that the law firm allegedly initiated over 2,300 foreclosure actions in Maryland in 2003, there was little room to argue the firm was less equipped to comply with the FDCPA than a more “traditional” debt collection agency. Moreover, the law firm was aware that the FDCPA could apply to their conduct, as their letters to Wilson contained clear references to the FDCPA, including the notice: “this is an attempt to collect a debt.” Judge Widener dissented, arguing that the majority misinterpreted the language of the FDCPA.

2. Fair and Accurate Credit Transactions Act

The FTC issued a new rule effective June 1, 2005 that requires businesses and individuals, including lawyers, to take appropriate measures to dispose of sensitive information obtained from consumer reports. The so-called “Disposal Rule” implements requirements of the 2003 Fair and Accurate Credit Transactions Act (the FACT Act).

Any business or individual using a consumer report for a business purpose is subject to the requirements of the Disposal Rule. The Disposal Rule applies to consumer reports and information derived from them. Specifically, consumer reports may include: credit reports; credit scores; and reports that businesses receive concerning employment background, check writing history, insurance claims,
residential or tenant history, or medical history. When it comes to the proper method of disposal, the rule is flexible, allowing the covered businesses to take into account the sensitivity of the information, the costs and benefits of the disposal methods, and changes in technology.


The Colorado Supreme Court declared on January 9, 2006 that lawyers could be liable for deceptive trade practices under Colorado’s Consumer Protection Act, provided the usual elements for establishing a claim are satisfied. The Colorado Supreme Court rejected the argument that lawyers are exempt from state consumer protection laws and refused to create a special test for lawyers. While the court predicted that lawyers would rarely be liable under the statute, it held that the plaintiff could pursue his claim against a personal injury law firm that allegedly engaged in false advertising to generate a high volume of cases.

B. E-Discovery

1. Introduction

In what has been described as “the biggest change to the Rules of Civil Procedure in a generation or two,” on April 12, 2006, the United States Supreme Court approved the entire package of proposed amendments to the Federal Rules of Civil Procedure concerning the discovery of “electronically stored information” (e-discovery). The package includes revisions and additions to Rules 16, 26, 33, 34, 37, and 45, as well as Form 35. These proposed amendments were transmitted to the Supreme Court in September 2005, after the Judicial Conference unanimously approved them. These proposed amendments will go into effect on December 1, 2006 unless Congress decides to take action. Collectively, these amendments address key areas of e-discovery: planning, privilege, scope and form of production, and preservation.

2. Planning

The Advisory Committee notes to the proposed amendments generally indicate that the goal of the amendments is to recognize the importance of electronically stored information and to respond to the increasingly prohibitive costs of document review and protection of privileged documents. It is important for litigants to think about e-discovery early and often. According to the Advisory Committee: “In many instances, the court’s involvement early in the litigation will help avoid difficulties that might otherwise arise.”

Two rule amendments specifically address the need for advanced planning with regards to electronically stored information: Rule 16(b) and Rule 26(f). New Rule 16(b) identifies categories of topics to be discussed at the pretrial conference and now includes “provisions for disclosure or discovery of electronically stored information.” This amendment is designed to alert the court to the possible need to address the handling of discovery of electronically stored information early in the litigation if such discovery is expected to occur. Rule 16(b) also includes discussion of “any agreements that the parties reach for asserting claims of privilege or of protection as trial preparation material after production.”

Rule 26(f) is also amended to direct the parties to discuss discovery of electronically stored information during their required discovery-planning conference. When the parties anticipate disclosure of electronically stored information, discussion at the outset may avoid later difficulties or help ease their resolution. When a case involves discovery of electronically stored information, the issues to be addressed during the Rule 26(f) conference depend on the nature and extent of the contemplated discovery and of the parties’ information systems. It may be important for the parties to discuss those systems; accordingly, counsel should become familiar with those systems before the conference. Similar to new Rules 16(b)(5) and 16(b)(6), new subsections 26(f)(3) and 26(f)(4) are added to make sure the Rule 26(f) conference includes a discussion of e-discovery issues. Rule 26(f)(3) specifically identifies “any issues relating to disclosure or discovery of electronically stored information, including the form or forms in which it should be produced” as a discussion item during the discovery conference. Similarly, “any issues relating to claims of privilege or of protection as trial preparation material, including—if the parties agree on a procedure to assert such claims after production—whether to ask the court to include their agreement in an order” are also to be discussed.

3. Privilege

The risk of privilege waiver, and the work necessary to avoid it, add to both the costs and delay of e-discovery. When electronically stored information is at issue, the waiver risk and time and effort needed to avoid it can increase substantially because of the sheer volume of information to be produced. Rule 26(b)(5)(A) provides a procedure for a party that has withheld information on the basis of privilege or protection as trial preparation material to make the claim so that the requesting party can...
4. Scope and Form of Production

a. Introduction

Rule 26(a)(1)(B) is amended to substitute “electronically stored information” for “data compilations” as a category of the required initial disclosures. New subsection 26(b)(2)(B) is added to excuse a party from providing discovery of electronically-stored information that is “not reasonably accessible because of undue burden or cost,” but the burden remains on the responding party to make the required showing. If the showing is made, “the court may nonetheless order discovery from such sources if the requesting party shows good cause, considering the limitations of Rule 26(b)(2)(C). The court may specify conditions for discovery.”\(^{72}\)

Interestingly, as noted below the Advisory Committee notes for 26(b)(2) go well beyond the language of the rule amendments and sketch an entire vision of e-discovery.

b. Subdivision (b)(2)

The amendment to Rule 26(b)(2) is designed to address issues raised by difficulties in locating, retrieving, and providing discovery of some electronically stored information. Electronic storage systems often make it easier to locate and retrieve information. These advantages are properly taken into account in determining the reasonable scope of discovery in a particular case. But some sources of electronically stored information can be accessed only with substantial burden and cost. In a particular case, these burdens and costs may make the information on such sources not reasonably accessible.

It is not possible to define in a rule the different types of technological features that may affect the burdens and costs of accessing electronically stored information. Information systems are designed to provide ready access to information used in regular ongoing activities. They also may be designed so as to provide ready access to information that is not regularly used. But a system may retain information on sources that are accessible only by incurring substantial burdens or costs. Subparagraph (b)(2)(B) is added to regulate discovery from such sources.

Under this rule, a responding party should produce electronically stored information that is relevant, not privileged, and reasonably accessible, subject to the Rule 26(b)(2)(C) limitations that apply to all discovery. The responding party must also identify, by category or type, the sources containing potentially responsive information that it is neither searching nor producing. The identification should, to the extent possible, provide enough detail to enable the requesting party to evaluate the burdens and costs of providing the discovery and the likelihood of finding responsive information on the identified sources.

A party’s identification of sources of electronically stored information as not reasonably accessible does not relieve the party of its common-law or statutory duties to preserve evidence. Whether a responding party is required to preserve unsearched sources of potentially responsive information that it believes are not reasonably accessible depends on the circumstances of each case. It is often useful for the parties to discuss this issue early in discovery.

The volume of—and the ability to search—much electronically stored information means that in many cases the responding party will be able to produce information from reasonably accessible sources that will fully satisfy the parties’ discovery needs. In many circumstances the requesting party should obtain and evaluate the information contained on sources that are not reasonably accessible. If the requesting party continues to seek discovery of information from sources identified as not reasonably accessible, the parties should discuss the burdens and costs of accessing and retrieving the information, the needs that may establish good cause.


for requiring all or part of the requested discovery even if the information sought is not reasonably accessible, and conditions on obtaining and producing the information that may be appropriate.

If the parties cannot agree whether, or on what terms, sources identified as not reasonably accessible should be searched and discoverable information produced, the issue may be raised either by a motion to compel discovery or by a motion for a protective order. The parties must confer before bringing either motion. If the parties do not resolve the issue and the court must decide, the responding party must show that the identified sources of information are not reasonably accessible because of undue burden or cost. The requesting party may need discovery to test this assertion. Such discovery might take the form of requiring the responding party to conduct a sampling of information contained on the sources identified as not reasonably accessible, allowing some form of inspection of such sources; or taking depositions of witnesses knowledgeable about the responding party's information systems.

Once it is shown that a source of electronically stored information is not reasonably accessible, the requesting party may still obtain discovery by showing good cause, considering the limitations of Rule 26(b)(2)(C) that balance the costs and potential benefits of discovery. The decision whether to require a responding party to search for and produce information that is not reasonably accessible depends not only on the burdens and costs of doing so, but also on whether those burdens and costs can be justified in the circumstances of the case. Appropriate considerations may include: (1) the specificity of the discovery request; (2) the quantity of information available from other and more easily accessed sources; (3) the failure to produce relevant information that seems likely to have existed but is no longer available on more easily accessed sources; (4) the likelihood of finding relevant, responsive information that cannot be obtained from other, more easily accessed sources; (5) predictions as to the importance and usefulness of the further information; (6) the importance of the issues at stake in the litigation; and (7) the parties' resources.

The responding party has the burden as to one aspect of the inquiry—whether the identified sources are not reasonably accessible in light of the burdens and costs required to search for, retrieve, and produce whatever responsive information may be found. The requesting party has the burden of showing that its need for the discovery outweighs the burdens and costs of locating, retrieving, and producing the information. In some cases, the court will be able to determine whether the identified sources are not reasonably accessible and whether the requesting party has shown good cause for some or all of the discovery, consistent with the limitations of Rule 26(b)(2)(C), through a single proceeding or presentation. The good-cause determination, however, may be complicated because the court and parties may know little about what information the sources identified as not reasonably accessible might contain, whether it is relevant, or how valuable it may be to the litigation. In such cases, the parties may need some focused discovery, which may include sampling of the sources, to learn more about what burdens and costs are involved in accessing the information, what the information consists of, and how valuable it is for the litigation in light of information that can be obtained by exhausting other opportunities for discovery.

The good-cause inquiry and consideration of the Rule 26(b)(2)(C) limitations are coupled with the authority to set conditions for discovery. The conditions may take the form of limits on the amount, type, or sources of information required to be accessed and produced. The conditions may also include payment by the requesting party of part or all of the reasonable costs of obtaining information from sources that are not reasonably accessible. A requesting party's willingness to share or bear the access costs may be weighed by the court in determining whether there is good cause. But the producing party's burdens in reviewing the information for relevance and privilege may weigh against permitting the requested discovery.

The limitations of Rule 26(b)(2)(C) continue to apply to all discovery of electronically-stored information, including that stored on reasonably accessible electronic sources.73

According to one commentator:

[7] The cost allocation question has been considered in Zubulake v. UBS Warburg, LCC.74 In that case, U.S. District Judge Shira Scheindlin held that courts must consider factors such as the likelihood of discovering critical information and the cost of the document production compared to the amount in controversy and the resources available to each party. The amendment attempts to codify Zubulake by establishing a two-tier standard in which lawyers first obtain and examine information that can be provided from easily accessed sources such as computer hard drives, personal digital assistants (PDA), removable media such as USB devices, etc. and then determine whether it is necessary to search the difficult-to-access sources such as back up tapes.75

Rule 33 concerning interrogatories is amended to specify that electronically-stored information may qualify as appropriate business records from which an answer to an interrogatory may be derived or ascertained.76

Rule 34(a) concerning the scope of production requests is amended to reference electronically-stored information. Rule 34(a)(1) is expansive and includes any type of information that is stored electronically. For example, discovery of electronic communications, such as e-mail, is often sought. The rule covers—either as documents or as electronically-stored information—information

74. 383 F. Supp. 2d 535 (S.D.N.Y. 2005). See also infra this text and notes 83-87.
“stored in any medium,” to encompass future developments in computer technology. Rule 34(a)(1) is intended to be broad enough to cover all current types of computer-based information, and flexible enough to encompass future changes and developments.  

Rule 34(b) is amended to supply a procedure for specifying and objecting to the form in which electronic information is to be produced. Under new subsections 34(b)(ii) and 34(b)(iii), the default form for producing electronically-stored information is that “in which it is ordinarily maintained [or] reasonably usable,” and “a party need not produce the same electronically stored information in more than one form.” However, the amendment to Rule 34(b) permits the requesting party to designate the form or forms in which it wants electronically-stored information produced. The form of production is more important to the exchange of electronically-stored information than of hard-copy materials, although a party might specify hard copy as the requested form.  

5. Preservation

New Rules 16(b) and 26(f) both direct the parties to discuss preservation of electronic information.

New Rule 37(f) is added. It states, in full:

(f) Electronically Stored Information. Absent exceptional circumstances, a court may not impose sanctions under these rules on a party for failing to provide electronically stored information lost as a result of the routine, good-faith operation of an electronic information system.  

The Advisory Committee Note explains that the premise for this amendment is that ordinary computer use necessarily involves routine alteration and deletion of information for reasons unrelated to litigation.  

It is important to note that this “safe harbor” provision only applies to information lost due to the “routine operation of an electronic information system” – the ways in which such systems are generally designed, programmed, and implemented to meet the party’s technical and business needs.

Similarly, Rule 37(f) applies to information lost due to the routine operation of an information system only if the operation was in “good faith.” Good faith in the routine operation of an information system may involve a party’s intervention to modify or suspend certain features of that routine operation to prevent the loss of information, if that information is subject to a preservation obligation.

When a party is under a duty to preserve information because of pending or reasonably anticipated litigation, intervention in the routine operation of an information system is one aspect of what is often called a “litigation hold.” Among the factors that bear on a party’s good faith in the routine operation of an information system are the steps the party took to comply with a court order in the case or a party agreement requiring preservation of specific electronically-stored information.

Rule 45 relating to subpoenas is also amended to make clear that it applies to electronically-stored information. “A subpoena may specify the form in which electronically stored information is to be produced.”

6. Zubulake v. UBS Warburg L.L.C.

Spoliation of evidence, document retention, and e-discovery came to a dramatic intersection in an employment discrimination case from the Southern District of New York. The case produced six published opinions relating to attorney and client obligations and electronically-stored information.

On April 6, 2005, the New York jury awarded Laura Zubulake $9.1 million in compensatory damages and $20.2 million in punitive damages for discrimination against her on the basis of sex. Zubulake’s lawyer argued that UBS destroyed emails and UBS witnesses lied on the witness stand. Before the jurors began deliberating, Judge Shira Scheindlin instructed them to assume that the emails UBS deliberately discarded after Zubulake filed her EEOC complaint would have hurt the bank’s case.

This negative inference instruction stemmed from UBS’s failure to preserve electronically-stored information. The district court found in Zubulake V that UBS and its counsel failed to meet these obligations and issued sanctions including that the jury empanelled to hear the case would be given an adverse inference instruction with respect to e-mails deleted and, in particular, with respect to e-mails that were irretrievably lost when UBS’s backup tapes were recycled.

C. Emerging Issues Under the Model Rules

1. Rule 4.2 and the Pro se Lawyer

Can a lawyer acting pro se speak directly with employees and managers of an entity that the lawyer knows is regularly

82. See Proposed Fed. R. Civ. P. 37(f), advisory committee notes.
87. See Zubulake V supra note 85.
represented by counsel? Apparently, the answer depends upon which jurisdiction the lawyer is in. In a pair of decisions by state regulators issued just one day apart, Alaska allows contact while Washington would subject the lawyer to discipline. The issue involves Model Rule 4.2.

Model Rule 4.2 prohibits a lawyer who is representing a client from communicating about the subject matter of the representation with a party or person the lawyer knows to be represented by another lawyer in the matter, unless authorized by law or the other lawyer. Does this rule apply when a lawyer represents herself such as when a lawyer-consumer has a complaint about a product or service or a lawyer-homeowner has a concern about the city government's refusal to issue a building permit?

The Alaska Bar Association Ethics Committee considered this question and concluded that a lawyer acting pro se is subject to Rule 4.2, which regulates attorney's communications with parties known to be represented by counsel. But the rule does not prevent a lawyer from contacting the entity's employees or managers directly until the lawyer is notified that the corporation is represented by counsel in the particular matter.

Just one day earlier, on January 26, 2006, a splintered Washington Supreme Court announced that lawyers acting pro se must comply with the disciplinary rule against communicating with represented persons. In this case, Haley was a shareholder, board member, and primary legal counsel for a closely-held software company. Haley sued its former CEO. After the trial, Haley represented himself and communicated directly with the former CEO to propose a settlement. CEO's counsel warned Haley that he was violating Rule 4.2 and to leave his client alone. Despite the warning, Haley left voice-mail messages for the CEO, again proposing a settlement.

The court concluded that Rule 4.2 prohibited a lawyer acting pro se from contacting a party who is represented by counsel. According to the court, other jurisdictions such as Idaho, Illinois, Nevada, Texas, West Virginia, and Wyoming "have considered the rule's applicability to lawyers acting pro se have generally concluded that the policies underlying the rule are better served by extending the restriction to lawyers acting pro se." Nonetheless, the court found the rule impermissibly vague and determined that its decision to apply the Rule 4.2 to pro se lawyers would only have a prospective application.

2. Unauthorized Practice of Law (UPL)

The Ohio Supreme Court proved that it intends to get serious about UPL, by imposing a $1 million dollar civil penalty and permanent injunction against a so-called "trust mill." The Cleveland Bar Association filed a UPL complaint against "The Estate Plan" (TEP), its owner, and Sharp Estate Services, which operated as "advisors" in marketing TEP products in Ohio. The Sharp advisors made the sales pitch to elderly customers at their homes. Once the advisor had a signed purchase contract and obtained two checks (one for the advisor and one for a review attorney), the advisor would send the information to a review attorney who would enter the information into a software program without having any contact with the customer. Sharp's fees ranged from $1,995 to $2,195 for modest estates. According to a partial list, at least 468 living trust and estate plans were sold in Ohio.

The court held that the use of review attorneys did not insulate the practice from UPL charges. "Because the advisor, not the attorney, sells the trust or estate plan and makes the decisions necessary to create the trust or estate document, the use of attorneys does not cure the UPL violation."

Emphasizing the gravity of UPL violations, the court permanently enjoined TEP and Sharp from marketing living trusts in Ohio. The court then assessed a penalty of $1,027,260, effectively forcing TEP and Sharp to disgorge the amounts they received from Ohioans from the sale of the living trust packages.

3. Multijurisdictional Practice (MJP)

Out of all the U.S. jurisdictions, about half provide for some type of temporary practice by lawyers licensed elsewhere beyond pro hac vice. Most of these jurisdictions have adopted some version of Model Rule 5.5 including California, Florida, Georgia, and Pennsylvania. Others like Virginia and Michigan permit temporary practice without yet having adopted a version of the Model Rule. However, not all jurisdictions are so welcoming. The Connecticut State Bar mixed the idea of allowing lawyers licensed in other jurisdictions to engage in temporary practice in Connecticut. The Montana Supreme Court apparently takes the same position only with less spine. After deferring adoption of Rule 5.5 and 8.5 until the comment period ran on other MJP-related proposals, the Montana Supreme Court rejected the reforms without even mentioning the two Model Rules. According to Montana State Bar counsel Betsy Brandborg: "It's pretty clear we have a solid fence around the state."
Interestingly, even if a jurisdiction adopts Rule 5.5 it can still be protectionist. Consider New Mexico. Since 2003 it has been legal for lawyers licensed elsewhere to enter into New Mexico and perform limited legal services. Approved on August 13, 2003 by the New Mexico Supreme Court, New Mexico basically follows Rule 5.5. However, few may be aware of the rule change. Following adoption of its version of Rule 5.5, the change was not published in the state's bar bulletin at the time. As of April 2005, it was not available online either.

In 2006, it is possible to access New Mexico Rule of Professional Conduct 16-505; however, it is available only through a private site.

### D. Duty of Good Faith and Fair Dealing in Negotiations

Debate continues as to the appropriate duty a lawyer owes to his opponent in the course of negotiation. Traditionally, Model Rule 4.1, “Truthfulness in Statements to Others,” would control. Rule 4.1 requires that “[i]n the course of representing a client a lawyer shall not knowingly...make a false statement of material fact or law to a third person.” While the rule itself seems straightforward, the comments that follow significantly alter the burden for a lawyer in the context of negotiation:

[2] This Rule refers to statements of fact. Whether a particular statement should be regarded as one of fact can depend on the circumstances.

Under generally accepted conventions in negotiation, certain types of statements ordinarily are not taken as statements of material fact. Estimates of price or value placed on the subject of a transaction and a party’s intentions as to an acceptable settlement of a claim are ordinarily in this category, and so is the existence of an undisclosed principal except where nondisclosure of the principal would constitute fraud.

Consequently, in the context of a negotiation, “puffery” is permissible.

Recently, the Litigation Section of the ABA began its first formal attempt to recognize a distinction between the ethical duties of a lawyer in the courtroom versus settlement negotiations. In August 2002, theABA Litigation Section issued Ethical Guidelines for Settlement Negotiations (Guidelines). The Guidelines include a duty of fair-dealing. A lawyer’s conduct in negotiating a settlement should be characterized by honor and fair-dealing. Similarly, an “attorney may not employ the settlement process in bad faith.” As to false statements of material fact, the Guidelines include section 4.1.1, False Statements of Material Fact, that states: "In the course of negotiating or concluding a settlement, a lawyer must not knowingly make a false statement of material fact (or law) to a third person.” The comments, however, continue to embrace the Model Rules definition of materiality:

The prohibition against making false statements of material fact or law is intended to cover only representations of fact, and not statements of opinion or those that merely reflect the speaker’s state of mind. Whether a statement should be considered one of fact, as opposed to opinion, depends on the circumstances. Model Rule 4.1, comment 2. “Under generally accepted conventions in negotiation, certain types of statements ordinarily are not taken as statements of material fact. Estimates of price or value placed on the subject of a transaction and a party’s intentions as to an acceptable settlement of a claim are ordinarily in this category...." The refusal of the Guidelines to alter the materiality definition is a source of criticism.

The effect of the Guidelines on lawyer ethics remains to be seen. At least one additional limitation is the fact that the Guidelines have not been approved by the full ABA. Consequently, the Guidelines carry the following disclaimer:

The Ethical Guidelines for Settlement Negotiations have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and, accordingly, should not be construed as representing the policy of the American Bar Association. However, the American Bar Association

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103. See id.
104. See http://www.americanbar.org/legalnews/BriefBrief.html#7.2 (Rule 16-505).
109. Id. § 2.3.
110. Commentary to section 2.3 notes the novelty of this approach:

While there is no Model Rule that expressly and specifically controls a lawyer’s conduct in the context of settlement negotiations, lawyers should aspire to be honest and fair in their conduct and in their counseling of their clients with respect to settlement. Model Rule 2.1 recognizes the importance of considering moral factors that may influence the endeavors of the parties to the proceedings before the court. Model Rules, Rule 3.2, notes that for ethical reasons a lawyer’s conduct should be characterized by honor and fair-dealing. Similarly, an “attorney may not employ the settlement process in bad faith.” As to false statements of material fact, the Guidelines include section 4.1.1, False Statements of Material Fact, that states: “In the course of negotiating or concluding a settlement, a lawyer must not knowingly make a false statement of material fact (or law) to a third person.” The comments, however, continue to embrace the Model Rules definition of materiality:

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E. Attorney Misconduct and the Duty to Report

In our largely self-regulating profession, members of the bar are required to report misconduct of other lawyers if it raises questions as to the lawyer's honesty, trustworthiness, or fitness as a lawyer. In ABA Formal Ethics Opinion 04-433 issued on August 25, 2004, the Standing Committee on Ethics and Professional Responsibility explored the obligation of a lawyer to report professional misconduct by a lawyer not engaged in the practice of law. Formal Opinion 04-433 concludes with a sweeping duty:

We interpret Rule 8.3 as requiring a lawyer to report professional misconduct at anytime by a licensed but non-practicing lawyer. Even misconduct arising from purely personal activity must be reported if it reflects adversely on the lawyer's fitness to practice law. A lawyer violates the Model Rules and is subject to professional discipline when she fails to report such professional misconduct, in circumstances in which Rule 8.3 requires such reports.

The formal opinion identifies examples of situations where such an obligation might arise. For example, a lawyer practicing in a corporation may learn of misconduct by a fellow employee who is licensed but employed by the corporation in a nonlegal capacity. Or a lawyer in private practice may discover misconduct by an employee of the firm (such as an in-house accountant) who the lawyer knows is admitted to law practice. Finally, the example that is closest to my heart: a lawyer observing the misconduct may himself not be engaged in active practice—such as faculty of a law school—and learns of misconduct by another law professor who is licensed to practice but also exclusively engaged in teaching. Of course, not all misconduct must be reported. Two thresholds must be reached to trigger the reporting requirement. First, the lawyer must "know" of the violation. Second, the misconduct must raise a "substantial question" as to the lawyer's honesty, trustworthiness or fitness as a lawyer.

The Committee even recognized the "awkwardness and potential discomfort" of reporting a colleague's misconduct—a situation compounded if the lawyer to be reported is the superior of the reporting lawyer. The Committee concludes:

Whether employed in a law firm, a corporate law department, on a law school faculty, or elsewhere, the lawyer may be facing the same dilemma: jeopardize her career by making the report, or jeopardize it by remaining silent in violation of the rules of ethics.

The reporting obligation is not, however, absolute. If reporting the misconduct would reveal confidential information in violation of Rule 1.6(a), the duty to report is subordinate to the duty of confidentiality. If a lawyer determines that the information necessary to report the misconduct is protected by Rule 1.6, the lawyer should seek informed consent from the client to disclose. However, any discussion to disclose must include the potential adverse impact that the disclosure may have on the client. Given this, the Committee notes that as "a practical matter, there may be little benefit for the client in consenting to report the misconduct to the disciplinary authorities."

IV. Alternative Dispute Resolution

A. New Mediation Rules

1. Uniform Mediation Act

In the mediation context, two developments are significant. First, consider the Uniform Mediation Act (UMA). The UMA was adopted by the National Conference of Commissioners on Uniform State Laws in August 2001. The UMA contains significant new provisions regarding the confidentiality of mediation communications and the privilege against disclosure. On May 13, 2003, Nebraska became the first state to adopt the UMA. Illinois followed. On November 22, 2004 New Jersey followed suit. Then Ohio enacted the UMA in December 2004. On April 5, 2005, the Washington legislature passed the UMA. Other jurisdictions having subsequently adopted the UMA are Iowa, Utah, and the District of Columbia. In Vermont, the UMA passed the House in March and Senate in early April 2006. It was signed by Governor Jim Douglas and took effect July 1, 2006. Other jurisdictions considering bills to enact the UMA at this writing include: Connecticut, Massachusetts, Minnesota, and New York.

2. New Model Standards of Conduct for Mediators

In 1994, the original Model Standards of Conduct for Mediators (Model Standards) were issued. The Model Standards were the collaborative effort of the American Arbitration Association (AAA), the ABA, and the Society of Professionals

118. See id.
119. Id.
120. Id.
121. Id.
122. See Uniform Mediation Act §5 (confidentiality and privilege), § 6 (waiver and preclusion of privilege), § 7 (exceptions to privilege), § 8 (mediator disclosure).
adopted by the two organizations and became effective March 1, 2004.\textsuperscript{123}

The 2004 Code of Ethics purports to address the problem of nonneutral party-appointed arbitrators that has been a lightning rod for criticism of the former ethical code. Under the old Code of Ethics, “persons who have the power to decide should observe fundamental standards of ethical conduct.”\textsuperscript{126} To ensure broad public confidence, an arbitrator has a responsibility, not only to the parties but also to the process itself, to observe high standards of conduct preserving the integrity and fairness of the process.\textsuperscript{127} Canon V. also precludes predispension by an arbitrator.\textsuperscript{128} However, these obligations were diluted if one is a nonneutral party-appointed arbitrator. A nonneutral “may be predisposed toward the party who appointed them but in all other respects are obligated to act in good faith with integrity and fairness.”\textsuperscript{129} While the nonneutral still must act in good faith and with integrity and fairness, the specific prohibitions of the Code of Ethics—delaying tactics, harassment of witnesses, making knowingly untrue or misleading statements—punctuate the difference in standards applicable to neutral and nonneutral arbitrators.\textsuperscript{130}

This fundamentally different treatment is reflected in the different disclosure and ex parte communication requirements. Before accepting appointment, arbitrators should disclose: (1) direct or indirect financial or personal interest in the outcome of the arbitration; and (2) any existing or past financial, business, professional, family, or social relationships which are likely to affect impartiality or may reasonably create the appearance of bias. This includes disclosure of such relationships with any party, lawyer, or witness. The obligation extends to relationships involving members of their families or current employers, partners, or business associates.\textsuperscript{131} If requested to withdraw by less than all parties, the neutral arbitrator should do so, unless the parties’ agreement establishes procedures for challenges, or the arbitrator determines that the challenge is not substantial.\textsuperscript{132} In contrast, nonneutral arbitrators essentially have a one-time general disclosure requirement. Their disclosure “should be sufficient to describe the general nature and scope of any interest or relationship, but need not include as detailed information as is expected from persons appointed as neutral arbitrators.”\textsuperscript{133} Significantly, there are no formal obligations to withdraw if requested.\textsuperscript{134}

The “hallmark” of the party-appointed arbitrator is the ability to communicate with the nominating party about any part of the case. Party-appointed need only inform the other participants that they intend to engage in ex parte communication; content is not disclosed.\textsuperscript{135} This ability is considered by many as one of the key benefits of arbitration.\textsuperscript{136}

Scholars have criticized the dual ethical standards of the Code of Ethics. They argue that because a party-appointed is less constrained by the ethical rules, the arbitrator is free to act less impartially, yielding a decision tainted by partiality. Given that the arbitrator’s role is pivotal to the entire process and that commercial arbitration forms a significant part of our justice system, the highest standards of ethical conduct should be imposed on all arbitrators.\textsuperscript{137}


\textsuperscript{123} The final version of the Model Standards of Conduct for Mediators is available at http://www.dhs.gov/xlibrary/publications/standardsofconductformediators.pdf.

\textsuperscript{124} A copy of the 2004 Code of Ethics is available from the AAA website at www.aaa.com.

\textsuperscript{125} See Canon II(A).

\textsuperscript{126} See Canon III(B).

\textsuperscript{127} See Canon VI(A).

\textsuperscript{128} See Canon VII(B)(b).

\textsuperscript{129} See Canon VII(A)(f).

\textsuperscript{130} See Canon VII(A).
The 2004 Code of Ethics establishes a presumption of neutrality for all arbitrators, including party-appointed arbitrators. However, the parties by agreement can provide for the use of nonneutral party-appointed arbitrators. The 2004 Code of Ethics requires all party-appointed arbitrators, whether neutral or not, to make pre-appointment disclosures of any facts which might affect their neutrality, independence, or impartiality. The 2004 Code of Ethics also requires all party-appointed arbitrators to ascertain and disclose as soon as practicable whether the parties intended for them to serve as neutral or not. The Code of Ethics expects all arbitrators to preserve the integrity and fairness of the process.\textsuperscript{138}

If the parties choose to use nonneutral party-appointed arbitrators, special ethical considerations apply in Canon X. of the 2004 Code of Ethics. In essence, Canon X. reinstates the provisions of the old Code: Canon X. arbitrators may be predisposed toward the party who appointed them but in all other respects are obligated to act in good faith and with integrity and fairness. For example, Canon X. arbitrators should not engage in delaying tactics or harassment of any party or witness and should not knowingly make untrue or misleading statements to the other arbitrators.\textsuperscript{139}

This is precisely the language of the old Code. Additionally, Canon X. arbitrators are not obliged to withdraw if requested to do so only by the party who did not appoint them.\textsuperscript{140} The 2004 Code of Ethics also allows extensive ex parte communication between the nonneutral party-appointed arbitrator and the party.\textsuperscript{141} It remains to be seen if the use of Canon X. arbitrators will erode the attempt at uniformity intended by the 2004 Code of Ethics.

On March 4, 2005, the Alabama Supreme Court Commission on Dispute resolution officially adopted the 2004 Code of Ethics. Effective immediately on that date, arbitrators on the state’s roster of arbitrators must sign an agreement to abide by the new Alabama Code of Ethics.\textsuperscript{142}

However, at its quarterly meeting in July 2003, the Council of the ADR Section of the State Bar of Texas decided to adopt the 1977 Code of Ethics for Arbitrators following the report of a section task force that studied the AAA-ABA Code of Ethics, JAMS’ Ethics Guidelines for Arbitrators, the Code of Professional Responsibility for Arbitrators of Labor-Management Disputes, and the Ethics Standards for Neutral Arbitrators in Contractual Arbitration adopted in California.\textsuperscript{143}

C. Model Rule for the Lawyer as a Third Party Neutral

An additional source of ethical guidance in ADR is worth noting. In November 2002, the CPR-Georgetown Commission on Ethics and Standards in ADR (sponsored by Georgetown University Law Center and CPR Institute for Dispute Resolution) released its proposed Model Rule for the Lawyer as a Third Party Neutral. The purpose of the proposed rule is to offer a framework for consideration by the appropriate bodies of the ABA and any state agency or legislature charged with drafting lawyer ethics rules. The proposed Model Rule addresses the ethical responsibilities of lawyers serving as third-party neutrals, in a variety of different ADR fora.

D. Duty to Advise

1. Introduction

Academics and proponents of alternative dispute resolution have long argued that lawyers have a duty to advise clients about ADR options.\textsuperscript{144} Client choice of means of dispute resolution is likely to have a significant impact on the client’s time, money, relationship, privacy, and ultimately satisfaction.\textsuperscript{145}

Because of the central importance of client choice, many scholars believe that there should be an express mandatory duty to advise clients of ADR options.\textsuperscript{146} Such a requirement, however, is largely absent from the ethical codes.

2. The Model Rules

The Model Rules as revised in 2002 slightly strengthen the duty to advise clients about ADR options. Three areas should be noted. First, Rule 1.2 concerning the allocation of authority between client and lawyer requires a lawyer to “abide by a client’s decisions concerning objectives of representation and, as required by Rule 1.4, shall consult with the client as to the means by which they are to be pursued.”\textsuperscript{147} Rule 1.4 (Communication) specifically outlines that lawyer’s duty to: promptly inform of decisions or circumstances involving informed consent; consult about means; inform about the status of the matter; comply with requests for information; and consult about limitations on the lawyer’s conduct.\textsuperscript{148} However, there is no specific reference to ADR. The lawyer’s duty to “reasonably consult with the client about the means by which the client’s objectives are to be accomplished” is the most likely source of an attorney duty to inform the client concerning ADR options. Finally, the comments to Rule 2.1

140. 2004 Code of Ethics X(B)(2).
141. See 2004 Code of Ethics X(C).
147. Model Rules of Prof’l Cond. R. 1.2(a).
ing and settling disputes." Colorado incorporates the notification provision in the text of its Rule 2.1: "In a matter involving or expected to involve litigation, a lawyer should advise the client of alternative forms of dispute resolution which might reasonably be pursued to attempt to resolve the legal dispute or to reach the legal objective sought." Hawaii has a similar provision.

Michigan demonstrates the client control model. In a recent ethics opinion, the State Bar of Michigan was asked whether lawyers have an ethical obligation to inform their clients of alternatives to litigation. Based upon Rules 1.2, 1.4, and 2.1, the committee concluded that a "lawyer has an obligation to recommend alternatives to litigation when an alternative is a reasonable course of action to further the client’s interests, or if the lawyer has any reason to think that the client would find the alternative desirable." The obligation was firmly rooted in client control:

There is generally an ethical duty to inform the client of any options or alternatives which are reasonable in pursuing the client’s lawful interests. MRPC 1.4. While not all options which are theoretically available need be discussed, any doubt about whether a possible option is reasonably likely to promote the clients interests, as well as any doubt about whether the client would desire the use of any particular option, should be resolved in favor of providing the information to the client and allowing the client to render a decision. This decision should be rendered with the assistance of the lawyer’s best advice and judgment.

E. Collaborative Law

The ADR newcomer currently getting the most attention is collaborative law. The collaborative law approach uses attorneys in a nonadversarial capacity to negotiate with the parties to achieve settlement. This paradigm shift from adversarial to collaborative is typically embodied in a participation agreement or contractual commitment between counsel and parties. The terms typically include a commitment to good faith negotiation, including full, open, and honest disclosure of all relevant information without request. Collaborative law’s unique twist is that legal counsel participates solely for settlement purposes, thereby increasing the stakes for participants in reaching agreement and diluting the litigation threat. This is embodied as a disqualification or termination provision providing that if any party decides to litigate, or there is abuse of the collaborative process, representation terminates requiring the parties to get new counsel.

The collaborative law movement began in 1988 in the family law area. Since then, over 3,000 lawyers have been trained in collaborative law techniques. The practice flourishes in certain states, including Minnesota, Ohio, and Texas, as well as in Canada. Currently there are eighty-seven identifiable collaborative law practice groups. The results of two recent empirical studies illustrate the effectiveness (and limitations) of collaborative law.

Texas was the first state to officially recognize the use of collaborative law in the family law area where it is now provided for by statute. This has served

149. Model Rules of Prof’l Conduct R. 3.1 cmt. 5.
150. See Cockran, supra note 145, at 918-99 (describing weaknesses).
151. See Cockran, supra note 145, at 905-06.
153. The Ten, Lawyer’s Creed—A Manifest for Professionalism § II A(1)(52002).
157. Id.
as a model for other states exploring the collaborative law model. Whether collaborative law will take hold outside of the family law area remains to be seen.

One possible limitation to the overall expansion and use of collaborative law is legal ethics. A flurry of recent academic commentary explores whether collaborative law practices and procedures are consistent with current ethical codes.


New HUD Predatory Lending and...

(Continued on page 5113)

- all properties acquired by sellers by inheritance;
- all sales by GSEs;
- all sales by state and federally-chartered financial institutions;
- all sales by nonprofit organizations approved to purchase HUD REO single-family properties at a discount with resale restrictions;
- all sales by local and state governments and their instrumentalities; and
- only upon announcement by HUD through issuance of a notice, sales of properties located in areas designated by the President as a federal disaster area (the notice will specify how long this exemption will be in effect).

These exceptions recognize that there are many instances where a short-term resale at a higher price may be appropriate. Not addressed (except for federal disaster areas) are cases where local market conditions change or the seller renounces a distressed property. Also not excluded from the bar are properties that are purchased in a run-down condition and then refurbished for resale at a higher price (an important function in inner-city and older residential areas). Instead, the exceptions focus on who the seller is, rather than the circumstances of the transactions.

The final rule became effective on July 7, 2006.

Montgomery County Injunction Extended

On Thursday, July 6, 2006, the judge hearing the law suit brought by the American Financial Services Association (AFSA) against the Montgomery County, Maryland, predatory lending ordinance indefinitely extended the preliminary injunction enjoining Montgomery County from enforcing the ordinance. The preliminary injunction will remain in effect until the court rules on AFSA’s motion for a permanent injunction. Your authors have received no information suggesting when the court will rule on the permanent injunction.

Exclusion of YSPs from California’s Anti-Predatory Lending Law

On Friday, February 17, 2006, the California Department of Corporations (Department) issued Release No. 55-FS, in which the Department concluded that yield-spread premiums (YSPs) should not be included in the points and fees calculation under California’s anti-predatory lending law. In reaching its conclusion, the Department cited Woski v. Fremont Invest. & Loan, despite the fact that Woski has not been ultimately resolved.

As a result of the Department’s release, your authors have concluded that YSPs may now be excluded from the points and fees calculation.