

TRANSACTIONS WITH PERSONS OTHER THAN CLIENTS

Rule 4.1: Truthfulness in Statements to Others

1. Current Kentucky Rule with Official Comments:

SCR 3.130(4.1) Truthfulness in statements to others

In the course of representing a client a lawyer shall not knowingly make a false statement of material fact or law to a third person.

Supreme Court Commentary

Misrepresentation

[1] A lawyer is required to be truthful when dealing with others on a client's behalf, but generally has no affirmative duty to inform an opposing party of relevant facts. A misrepresentation can occur if the lawyer incorporates or affirms a statement of another person that the lawyer knows is false. Misrepresentations can also occur by failure to act.

Statements of Fact

[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 in this category, and so is the existence of an undisclosed principal except where nondisclosure of the principal would constitute fraud.

2. Proposed Kentucky Rule with Official Comments:

TRANSACTIONS WITH PERSONS OTHER THAN CLIENTS

SCR 3.130(4.1) Truthfulness in statements to others

In the course of representing a client a lawyer:

(a) shall not knowingly make a false statement of material fact or law to a third person; and

(b) if a false statement of material fact or law has been made, shall take reasonable remedial measures to avoid assisting a fraudulent or criminal act by a client including, if necessary, disclosure of a material fact, unless prohibited by Rule 1.6.

Supreme Court Commentary Comment

Misrepresentation

[1] A lawyer is required to be truthful when dealing with others on a client's behalf, but generally has no affirmative duty to inform an opposing party of relevant facts. A misrepresentation can occur if the lawyer incorporates or affirms a statement of another person that the lawyer knows is false. Misrepresentations can also occur by failure to act partially true but misleading statements or omissions that are the equivalent of affirmative false statements. For dishonest conduct that does not amount to a false statement or for misrepresentations by a lawyer other than in the course of representing a client, see Rule 8.4.

Statements of Fact

[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. Lawyers should be mindful of their obligations under applicable law to avoid criminal and tortious misrepresentation.

Crime or Fraud by Client

[3] Under Rule 1.2(d), a lawyer is prohibited from counseling or assisting a client in conduct that the lawyer knows is criminal or fraudulent. Paragraph (b) states a specific application of the principle set forth in Rule 1.2(d) and addresses the situation where a client's crime or fraud takes the form of a lie or misrepresentation. Ordinarily a lawyer can avoid assisting in a client's crime or fraud by withdrawing from the representation. Nonetheless, sometimes a lawyer is required to take more overt measures

such as giving notice of the fact of withdrawal, disaffirming an opinion, document, affirmation or the like, to prevent the lawyer's services' being used to further the client's crime or fraud. In extreme cases, substantive law may require a lawyer to disclose information relating to the representation to avoid being deemed to have assisted in the client's crime or fraud. If the lawyer can avoid assisting a client's crime or fraud only by disclosing this information, then under paragraph (b) the lawyer is required to do so, unless the disclosure is prohibited by Rule 1.6. [See also, Rules 1.6(b), 1.13 (c) and 8.4(c).]

3. Discussion and Explanation of Recommendation:

a. Comparison of proposed Kentucky Rule with its counterpart ABA Model Rule.

(1) Paragraph (a) of the proposed Rule is substantively the same as MR 4.1 and the current KRPC 4.1.

(2) Paragraph (b) is substantially different from paragraph (b) of MR 4.1.

b. Detailed discussion of reasons for variances from the ABA Model Rule (if any).

(1) The Commission did not change ABA Model Rule 4.1(b), but added to the official Comments language and guidance (1) clarifying that mandatory disclosure is a "specific application" of Rule 1.2(d) which prohibits a lawyer from assisting a client in conduct the lawyer knows to be fraudulent or criminal; and (2) specifying what representations can be considered false or fraudulent (e.g., "partially true but misleading statements").

(2) Paragraph (b) of the proposed Kentucky Rule 4.1 follows closely the letter and intent of MR 4.1(b) and its accompanying Comment. MR 4.1(b) directs that a lawyer shall not knowingly "fail to disclose a material fact when disclosure is necessary to avoid assisting a criminal or fraudulent act by a client, unless disclosure is prohibited by Rule 1.6." The language has been altered by the Committee to direct the lawyer to "take remedial measures ... including, if necessary, disclosure of material facts" That language was preferred by the Committee because it emphasizes that disclosure of material facts (e.g., disavowing a false document) is an option of last resort to be employed only if that is the only means to avoid assisting in the commission of a crime or perpetrating a fraud. Similarly, the fourth sentence of Comment [3] of the proposed

Kentucky Rule adds language [“Nonetheless ...to prevent the lawyer’s services’ being used to further the client’s crime or fraud.”] that emphasizes that the mandate of this Rule serves as a bar to the fraudulent or criminal misuse of the lawyer’s services.

(3) It should be noted that MR 4.1(b) and the proposed Kentucky Rule “do not require disclosure of confidential information, even to avoid assisting a client’s crime or fraud. See ABA Formal Ethics Op. 93-375(1993) (lawyer representing client in bank examination may not reveal client’s lie to examiner and is not required to make “noisy withdrawal” from representation).” *Annotated Model Rules of Professional Conduct*, at 415 (5th Ed., 2003).

Dissent and Committee Response

Committee Members, Janet P. Jakubowicz, John T. Ballantine, Sheldon G. Gilman, Donald H. Combs, Olu A. Stevens, Peter L. Ostermiller, and William E. Johnson, respectfully dissent from the Committee’s Rule 4.1 recommendation. Their dissenting opinion is inserted here for consideration by the reviewing authorities. The results of the Committee’s consideration of this dissent follow the opinion.

We disagree with the Committee’s proposed Rule 4.1(b) for two reasons.

First, we believe that proposed Rule 4.1(b) places an unreasonable burden on a lawyer to take “remedial measures” including, if necessary, the disclosure of attorney-client privileged information if a lawyer learns after the fact that his or her client committed a fraudulent or criminal act. By way of example, if a corporate client misrepresents a material term of a sale to the purchaser and the deal closes, the proposed Rule would appear to require the lawyer representing the corporate seller during the transaction to reveal the misrepresentation to the non-client purchaser as soon as he or she becomes aware of the “fraud” – which could be one month, one year or even ten years after the fact. Similarly, a lawyer who prepared a legal opinion in support of a bond issue and who later discovers he was provided false data which was material to the issuance and marketing of the bonds would be required to “correct” that opinion. Not only is the lawyer put in the position of having to police the acts of his or her former clients and possibly reveal attorney-client privileged communications, the lawyer is likely to be sued by the former client for having done so in the first instance, and by the purchaser for not having learned of the “fraud”

sooner.

Moreover, contrary to the Committee's position, proposed Rule 4.1(b) does not require that the lawyer services have been used in committing the criminal or fraudulent acts by the client in order to trigger the Rule, nor does the proposed Rule apply only to situations where the client is "currently" committing or preparing to commit the bad acts. The proposed Rule makes clear that a lawyer will be responsible for correcting a client's past fraudulent or criminal conduct as well. Simply put, we do not believe that lawyers should be put in the position of being "whistleblowers" when they have no reason to know of a client's fraud or criminal act at the time of such act.

Second, proposed Rule 4.1(b) also requires that a lawyer take "reasonable remedial measures to avoid assisting a fraudulent or criminal act by a client including, if necessary, disclosure of a material fact, *unless prohibited by Rule 1.6.*" (emphasis supplied.) The application of Rule 4.1 with reference to Rule 1.6 is fraught with pitfalls for the well-intended lawyer who is faced with a situation where a client's conduct has adversely affected the financial interests or property of another. The phrase "unless prohibited by Rule 1.6," was intended to limit a lawyer's required duty to reveal confidential client information; however, the reference in Rule 4.1(b) to Rule 1.6's limitation was adopted before the ABA's major revision to Rule 1.6. The amended version of Rule 1.6 now permits a lawyer to reveal confidential client information when the client's actions were reasonably certain to result in or have resulted in substantial injury to the financial interests or property of another. Before this recent revision, Rule 1.6 prohibited disclosures unless necessary to prevent reasonably certain death or substantial bodily harm. The amended version of Rule 1.6, when applied to Rule 4.1, results in the unfortunate situation where the lawyer is required to reveal confidential client information in the circumstances described in Rule 4.1. Disclosures under Rule 1.6 are, as stated, permissive, and, therefore, when applied in conjunction with Rule 4.1 will result in the unintended mandatory disclosure of confidential client information. For the foregoing reasons, we believe the current Rule 4.1 should be retained.

Committee Consideration of the Dissent to its Recommendation: The dissent suggests that the mandate of Rule 4.1(b) is far broader than it is when read (as directed) in conjunction

with Rule 1.6. Rule 4.1(b) mandates disclosure of a false statement of material fact (1) if the statement is being used to commit a fraud; (2) if the lawyer, by remaining silent, is assisting in that commission; and (3) only if such a disclosure is permitted by Rule 1.6. Disclosure is permitted by Rule 1.6 *only* if the lawyer's services *are* being used to further a crime or fraud *and* the lawyer reasonably believes that a third party will suffer substantial injury absent the disclosure. The dissent in effect would allow a lawyer knowingly to permit her services to be used to commit a fraud despite the resulting serious damage to third parties. While the confidential relationship between lawyer and client is highly valued, that relationship becomes corrupt if a lawyer is permitted to participate in a client's fraudulent conduct. The proposed rule protects practitioners from unscrupulous clients who bank on confidentiality to highjack a reputable lawyer's services for their own nefarious ends. That likely is the reason most jurisdictions in the United States have adopted or are recommending adoption of proposed Rule 4.1(b). The reputation of the legal profession has suffered mightily in recent times from just such silent complicity by lawyers in their clients' wrongdoing. No client should expect a lawyer to stand by silently while her services are being so employed.

Committee proposal adopted without change. Order 2009-05, eff 7-15-09.