2004

Enron, Titanic, and the Perfect Storm

Nancy B. Rapoport
University of Nevada, Las Vegas -- William S. Boyd School of Law

Enron, Titanic, *and* The Perfect Storm*

*Nancy B. Rapoport***

> [Former Enron CEO Jeffrey] Skilling offered a hypothesis for what brought Enron down, calling it a "perfect storm" of events.
>
> He speculated that questions raised about the quality of Enron's accounting and about self-dealing caused a loss of confidence in the financial community. That led to Enron's debt being downgraded.
>
> That downgrade, he said he was told by an Enron executive after he left, meant Enron couldn't access several billion dollars of back-up credit lines. A liquidity crunch followed, he said, even though Enron was solvent and highly profitable.
>
> —Laura Goldberg, *Houston Chronicle*[1]

* Originally published at 71 FORDHAM L. REV. 1373 (2003). Reprinted with permission.

** Dean and Professor of Law at the University of Houston Law Center. All views expressed in this essay are mine alone, and not those of the University of Houston or its faculty, staff, or administration. I want to thank Emily Chan-Nguyen, Kelli Cline, Luddie Collins, Bala Dharan, Patrick Flanagan, Jimmy Halvatzis, Susan Hartman, Michele Hedges, Morris & Shirley Rapoport, Harriet Richman, Jeff Van Niel, and Michelle Wu. I also want to thank the students in my 2002 Seminar on *Special Issues in Ethics:* Sara Alonso Oliver, Justin Berg, Alison Chien, Doug Du Bois, Trevor Fish, Patrick Flanagan (who gets thanked twice, because he was also one of the cite-checkers for this article), Kim Havel, Cathy Helenhouse, Colin Moore, Sandy Oballe, Kevin Powers, Barry Rienstra, Ron Smeberg, and Tiffany Toups.

[1] Laura Goldberg, *Did No Wrong, Skilling Says: Defends His Role in Enron Fall,* HOUS. CHRON., Jan. 17, 2002, *available at* http:// www.chron.com/cs/CDA/story.hts/special/enron/dec01/1183520; *see also Good Morning America* (ABC television broadcast, Feb. 7, 2002) ("All eyes will be on former CEO Jeff Skilling. Skilling blames Enron's collapse on an unfortunate collision of events—the perfect storm. Congressional investigators point out he was at Enron's helm at the time."). Of course, now everyone—and I mean everyone—has latched onto this "perfect storm" metaphor. *See, e.g.,* Federal Document Clearing House, Worldcom CEO John Sidgmore Testifies Before the U.S. Senate Committee on Commerce, Science and Transportation, July 30, 2002, *available at* 2002 WL 1753183, at *3 (statement of John Sidgmore, CEO, WorldCom) ("Several factors . . . converged to create, I'll use Mr. Legere's words, a kind

> Of course, we now know the extraordinary combination of circumstances that existed at that time which you would not meet again in 100 years; that they should all have existed just on that particular night shows, of course, that everything was against us.
>
> —Second Officer Charles Lightoller, *RMS Titanic*[2]

> I had some misgivings about calling [my book] *The Perfect Storm,* but in the end I decided that the intent was sufficiently clear. I use perfect in the meteorological sense: a storm that could not possibly have been worse.
>
> —Sebastian Junger[3]

Much has been written about the Enron fiasco, from scholarly articles[4] to popular books,[5] and I'm sure that much more will be written about the deals that brought the

---

of perfect storm—and I guarantee you we did not rehearse this—that ripped through the telecommunications industry."); Federal Document Clearing House, *Harming Patient Access to Care: The Impact of Excessive Litigation,* July 17, 2002, *available at* 2002 WL 1584492, at *3 (statement of Richard Anderson, CEO, The Doctor's Company) ("The combination of these factors created . . . the perfect storm . . . for medical liability insurers."); Federal Document Clearing House, *House Committee on Education and the Workforce Holds a Hearing on Enron's Benefits Plan and its Compliance With Laws on Employer-Sponsored Pension Plans,* Feb. 7, 2002, *available at* 2002 WL 203240, at *12 (statement of Teresa Ghilarducci, Associate Professor of Economics, University of Notre Dame) ("The 1990s was the perfect storm for pensions to increase."); Federal Document Clearing House, *U.S. Senate Judiciary Committee Holds Hearing on Accountability Issues: Lessons Learned From Enron's Fall,* Feb. 6, 2002, *available at* 2002 WL 188865, at *11–12 (statement of Christine Gregoire, Attorney General, Washington State) ("In Washington [State,] we feel like Enron has been the gathering of the perfect storm. First, they gouged our consumers and rate payers with highly questionable power prices last year. And now, sadly, they have defrauded our investors and others across the nation.").

One of the coolest things that can happen to a law professor happened to me after I first published this article in the *Fordham Law Review.* I sent a copy to Sebastian Junger, author of THE PERFECT STORM. He read it and said that I was correct in my understanding of the "perfect storm" concept. Thank you, Mr. Junger!

[2] WALTER LORD, THE NIGHT LIVES ON 47 (1987) [hereinafter THE NIGHT LIVES ON].

[3] SEBASTIAN JUNGER, THE PERFECT STORM: A TRUE STORY OF MEN AGAINST THE SEA xiv (1997).

[4] *See, e.g.*, Michelle Chan-Fishel, *After Enron: How Accounting and SEC Reform Can Promote Corporate Accountability While Restoring Public Confidence,* 32 ENVTL. L. REP. 10965 (2002); Timothy P. Duane, *Regulation's Rationale: Learning from the California Energy Crisis,* 19 YALE J. ON REG. 471 (2002); Marisa Rogoway, *Recent Developments, Proposed Reforms to the Regulation of 401(k) Plans in the Wake of the Enron Disaster,* 6 J. SMALL & EMERGING BUS. L. 423 (2002); Marissa P. Viccaro, *Can Regulation Fair Disclosure Survive the Aftermath of Enron?,* 40 DUQ. L. REV. 695 (2002).

[5] *See, e.g.*, DIRK J. BARREVELD, THE ENRON COLLAPSE: CREATIVE ACCOUNTING, WRONG ECONOMICS OR CRIMINAL ACTS? A LOOK INTO THE ROOT CAUSES OF THE LARGEST BANKRUPTCY IN U.S. HISTORY (2002); ROBERT BRYCE, PIPE DREAMS: GREED, EGO, AND THE DEATH OF ENRON (2002); LOREN FOX, ENRON: THE RISE AND FALL (2002); PETER C. FUSARO & ROSS M. MILLER, WHAT WENT WRONG AT ENRON: EVERYONE'S GUIDE TO THE LARGEST BANKRUPTCY IN U.S. HISTORY (2002).

company down, the arrogance of some of the main players, and the ethical and moral issues that seemed to come to light only after the story broke in the media.[6] Enron's collapse, along with the failures of such other mega-businesses as WorldCom and Global Crossing,[7] triggered new legislation[8] and introduced such heretofore arcane acronyms as "SPEs" into the general lexicon.[9] The metaphor most used to describe Enron's quick descent into chapter 11 has been the "perfect storm."

That "perfect storm" metaphor irks me no end. I maintain, and this essay is designed to illustrate, that what brought Enron down—at least as far as we know—wasn't a once-in-a-lifetime alignment of elements beyond its control. Rather, Enron's

[6] One of the reasons that I'm sure more will be written is that I'm working on such a project: ENRON: CORPORATE FIASCOS & THEIR IMPLICATIONS (with Bala G. Dharan).

[7] Take a look at the largest bankruptcies, in terms of approximate stated liabilities, in the past twelve months [2001–02]: WorldCom (7/02 bankruptcy filing) ($43 billion, including $2 billion more in liabilities discovered after the bankruptcy filing); Enron (12/01) ($32 billion); NTL, Inc. (5/02) ($23.4 billion); Adelphia (6/02) ($18.6 billion); Global Crossing (1/02) ($12.4 billion); KMart (1/02) ($10.2 billion). *See* American Bankruptcy Institute, *A Look Inside the Mega-Case*, 10th Annual Southwest Bankruptcy Conference, Sept. 12–15, 2002; Bill Atkinson, *Kmart Files Chapter 11 Bankruptcy; No. 3 Discounter Cites Weak Economy, Tough Competition; 'Couldn't Pay the Bills'; Swift Move Surprises; $2 Billion Loan to Aid Firm's Reorganization*, BALT. SUN, Jan. 23, 2002, at 1A ("The Troy, Mich.-based firm listed $17 billion in assets and $11.3 billion in liabilities. . . . [A]lthough Kmart's bankruptcy is large, it pales in comparison to the largest bankruptcy in history, filed last month by Enron Corp . . . [which] listed $49 billion in assets and $31.2 billion in debts."); Julie Creswell, *Going For Broke; Crash! There Goes Another Company into Bankruptcy. How Did We Get Here? (Long Story.) Are We on the Mend? (Don't Bet on It.)*, FORTUNE, Feb. 18, 2002, *available at* 2002 WL 2190302; Lorrie Grant, *Discounter Hopes for Fast Reorganization*, USA TODAY, Jan. 23, 2002, at B02 ("Kmart listed $16.28 billion in assets and $10.34 billion in debts."); Andrew Leckey, *Bankruptcies Leave Investors in the Lurch*, CHI. TRIB., Aug. 27, 2002, *available at* 2002 WL 2689322; Alexandra R. Moses, Chern Yeh Kwok, & Thomas Lee et al., *Retailer Kmart Files for Bankruptcy; Officials Plan to Close Some Stores, Reorganize*, ST. LOUIS POST-DISPATCH, Jan. 23, 2002, at A1 ("[Kmart] has $10.25 billion in debt."); Chris Reidy, *Kmart Tumbles Discount Retail Chain in Record Chap. 11 Filing*, BOSTON GLOBE, Jan. 23, 2002, at C1 ("In its bankruptcy filing, Kmart and its US subsidiaries listed $17 billion in total assets at book value and total liabilities of $11.3 billion as of the quarter ended Oct. 31."); Gary Young, *Major Bankruptcies Filed in New York City*, 228 N.Y. L.J. 5 (Aug. 1, 2002).

[8] *See, e.g.*, Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745, Corporate and Criminal Fraud Accountability Act of 2002, Pub. L. No. 107-204, 116 Stat. 800 (codified at 18 U.S.C. § 1348, 1514A, 1519–20) [hereinafter Sarbanes-Oxley]; *Framework for Enhancing the Quality of Financial Information Through Improvement of Oversight of the Auditing Process*, 67 Fed. Reg. 44964-01 (proposed July 5, 2002) (to be codified at 17 C.F.R. pt. 210, 229).

[9] If you don't believe me, just do a search in WESTLAW or LEXIS on "SPEs" and see how many documents you get, especially documents dated after October 2001, when the Enron disaster began to break. A search of major newspaper articles (Westlaw database NPMJ) for the terms "special purpose entity" or "special purpose entities" during the year 1999 yielded zero results. The first article in this database appeared in October 2001 and a search of 2002 now yields over 328 results (as of the second week in October 2002, with more being added daily).

demise was a synergistic combination of human errors and hubris: a *"Titanic"*[10] miscalculation, rather than a "perfect storm."[11]

I. WHY *TITANIC* IS A BETTER METAPHOR FOR ENRON'S EVENTUAL DOWNFALL THAN IS *THE PERFECT STORM*

The story of the *Titanic* is well-known. The ship was, at the time of its maiden (and only) transatlantic voyage, the largest in the world, carrying a microcosm of society.[12] The glitterati of the United States and Europe were on board, as were hundreds of immigrants trying to make their way to a new land. The ship was built with watertight compartments that extended from the keel up several decks (some to D Deck and some to E deck); she also had a double bottom for extra protection.[13] She was designed to float with any two consecutive compartments flooded and even with three of the first five compartments (out of sixteen) flooded,[14] thanks to electronic doors that could be closed by a single command.[15] And she was touted as "unsinkable," at least in some press reports.[16]

But sink she did, based upon a series of miscalculations, no single one of which might have proved fatal, but all of which, taken together, doomed the ship. In a chapter of his follow-up book to *A Night to Remember*, called *The Night Lives On*,[17] Walter Lord enumerates the many individual mistakes made that night:

---

[10] And, no, it wasn't the Leonardo DiCaprio movie (TITANIC (20th Century Fox 1997)) that first piqued my interest in the ship's history. I've been fascinated by it for probably thirty or so years. Among other things, I'm a member of the Titanic Historical Society, and I probably own virtually every book and movie about the ship. If you're wondering if I'm a bit obsessed with the ship and its tale, you're right. But everyone needs a hobby.

[11] I've used the *Titanic* comparison once before. *See, e.g.*, Mike Tolson, *The Fall of Enron/'Convenient whipping boy'/Enron Scandal Offers Fodder for Wide Range of Groups Seeking a Symbol for Their Cause*, HOUS. CHRON., Mar. 3, 2002, at 26, *available at* 2002 WL 3245488. Others have also made the comparison between Enron and the *Titanic*. *See* Edward J. Cleary, *Lessons For Lawyers From The Enron Debacle*, BENCH & B. MINN., Apr. 2002, at 16 (footnotes omitted) (quoting George F. Will, *Indignation Over Enron is Just the Beginning*, WASH. POST, Jan. 16, 2002) ("Given that Enron employee pensions were decimated with, as one commentator noted, the employees "locked in steerage like the lower orders on the *Titanic*, and given that many state pension funds were among the casualties, both state and national public officials will be forced to act."); Martha Neil, *Partners at Risk*, 88 A.B.A. J. 44 (Aug. 2002) ("The collapse of Enron might give partners at law firms reason to ponder another epic disaster: the sinking of the *Titanic*.").

[12] WALTER LORD, A NIGHT TO REMEMBER 1 (1997) [hereinafter A NIGHT TO REMEMBER].

[13] *Id.* at 174–75. She did not, however, have a double hull. *Id.*

[14] *Id.* at 26.

[15] *Id.* at 8.

[16] *Id.* at 175.

[17] THE NIGHT LIVES ON, *supra* note 2.

- the calm sea, which meant that the lookouts couldn't see any waves breaking against the bergs;[18]
- the numerous, apparently ignored ice warnings from ships already crossing the Atlantic Ocean that were using the same route as the *Titanic;*[19]
- the lack of any systematic procedure to deliver ice and weather warnings from the Marconi telegraph room to the bridge;[20]
- the fact that the lookouts' binoculars had been lost earlier in the trip;[21]
- the failure of the *Titanic's* officers to urge Captain Smith (or each other) to take a more cautious approach to travel, based on the calm sea and rapidly dropping temperature;[22]
- not enough lifeboats for the number of souls aboard;[23]
- Captain Smith's failure to hold lifeboat drills[24] or to do more than a perfunctory test of the ship's braking speed and maneuverability;[25]
- First Wireless Operator Phillips's famous response to an ice warning from the *Californian* (the ship that, according to some accounts, was closest to the *Titanic* when it sunk), "Shut up, shut up . . . I am working Cape Race";[26]
- the fact that lookout Frederic Fleet spotted the berg too late to stop the ship or otherwise to avoid the berg;[27]
- First Officer Murdoch's decision to port around the berg rather than ramming it head-on, a counterintuitive action that might have saved the ship;[28] and
- the *Californian's* decision not to come to the aid of a vessel in enough obvious distress to fire white distress rockets (apparently visible to the *Californian's* crew) at several intervals.[29]

The list of miscalculations goes on and on.[30] But Walter Lord tells it best:

> Given the competitive pressures of the North Atlantic run, the chances taken, the lack of experience with ships of such immense size, the haphaz-

[18] *Id.* at 47.

[19] *Id.* at 48–53.

[20] *Id.* at 53.

[21] *Id.* at 60.

[22] *Id.* at 53–54.

[23] *Id.* at 72–80.

[24] A NIGHT TO REMEMBER, *supra* note 12, at 42.

[25] THE NIGHT LIVES ON, *supra* note 2, at 56.

[26] *Id.* at 58.

[27] *Id.* at 59–60.

[28] *Id.* at 59.

[29] *Id.* at 134–59.

[30] And so have I, at some social gatherings, as my very indulgent husband can attest.

> ard procedures of the wireless room, the casualness of the bridge, and the misassessment of what speed was safe, it's remarkable that the *Titanic* steamed for two hours and ten minutes through ice-infested waters without coming to grief any sooner.
>
> "Everything was against us?" The wonder is that she lasted as long as she did.[31]

The Perfect Storm, on the other hand, describes a combination of meteorological bad luck and human miscalculation, born less of arrogance than of desperation. Granted, Billy Tyne, captain of the *Andrea Gail,* made a fatal mistake by sailing into the storm,[32] but he did "what ninety percent of us would've done—he battened down the hatches and hung on."[33] Although the signs were clear that bad weather was coming, the sheer magnitude of the storm was far beyond the experience (or imagination) of any of the ship captains in the large area covered by the storm, and each of them had to make a quick decision:

> [The weather bulletin describing Hurricane Grace] reads like an inventory of things fishermen don't want to hear. . . . Every boat in the swordfish fleet receives this information. Albert Johnston, south of the Tail, decides to head northwest into the cold water of the Labrador Current. . . . The rest of the sword fleet stays far to the east, waiting to see what the storm does. They couldn't make it into port in time anyway. The *Contship Holland,* a hundred miles south of Billy, heads straight into the teeth of the thing. Two hundred miles east, . . . the Liberian-registered *Zarah,* also heads for New York. Ray Leonard on the sloop *Sartori* has decided not to head for port; he holds to a southerly course for Bermuda. The *Laurie Dawn 8* keeps plowing out to the fishing grounds and the *Eishin Maru 78,* 150 miles due south of Sable Island, makes for Halifax harbor to the northeast. Billy can either waste several days trying to get out of the way, or he can stay on-course for home. The fact that he has a hold full of fish, and not enough ice, must figure into his decision.[34]

Billy Tyne's decision proved wrong, and the *Andrea Gail* lost all six hands aboard.[35] *Titanic* lost over 1,500 souls, with only 705 saved.[36] Both events were tragic. But only

---

[31] THE NIGHT LIVES ON, *supra* note 2, at 61.

[32] Special thanks to Boyd Henderson for reminding me, at a luncheon, that some human error contributed to the fate of the *Andrea Gail.*

[33] JUNGER, *supra* note 3, at 124 (quoting Captain Tommie Barrie, of the ship *Allison*).

[34] *Id.*

[35] *Id.* at 186.

[36] A NIGHT TO REMEMBER, *supra* note 12, at 176.

the *Titanic* can trace the loss of life directly to human arrogance.[37] When I compare the two tragedies in light of Jeffrey Skilling's claim that the fall of Enron was based on factors outside of the company's control—an economic "perfect storm"—I find that Skilling's claim falls flat.

II. HOW A FAILURE OF CHARACTER CAN TURN "PERFECT STORMS" INTO *TITANIC* MISTAKES

I'm not going to rehash the mechanics of the various Enron deals here. Others have done a good job of describing the problems with the deals,[38] with the Board's lack of oversight of the deals,[39] and with the general culture of Enron that encouraged aggressive risk-taking and short-term profits.[40] We obviously don't know enough about the deals or the people yet to reach any final conclusions, so my comments are going to concentrate on one theme—character. If we are to believe that there is a single root cause of the Enron mess (an arguable point at best in such a complicated situation), failure of character gets my nomination.

[37] The Golden Age's love of, and faith in, science contributed to the tragedy as well, as some of the miscalculations that Captain Smith made were based on the scientific advances in ship design.

[38] *See, e.g.*, WILLIAM C. POWERS, JR., ET AL., REPORT OF INVESTIGATION BY THE SPECIAL INVESTIGATIVE COMMITTEE OF THE BOARD OF DIRECTORS OF ENRON CORP., 2002 WL 198018 (CORPSCAN 1980818 (ENRON)) [hereinafter Powers Report]. The Powers Report is also available at http://i.cnn.net/cnn/2002/LAW/02/02/enron.report/powers.report.pdf. There is also a lot of good Congressional testimony on the subject. *See, e.g.*, Federal Document Clearing House, *Strengthening Accounting Oversight: Hearing Before the Subcomm. on Commerce, Trade and Consumer Protection of the House Comm. on Energy and Commerce*, June 26, 2002, *available at* 2002 WL 1381127 (statement of Bala G. Dharan, J. Howard Creekmore Professor of Management, Rice University); Federal Document Clearing House, *U.S. Senate Governmental Affairs Committee Holds a Hearing on the Collapse of Houston-based Enron Corporation*, Jan. 24, 2002, *available at* 2002 WL 93421 (statement of John Langbein, Professor of Law, Yale Law School); Federal Document Clearing House, *Deregulating Capital Markets, Outline of the Testimony of Professor John C. Coffee, Jr., before the Subcommittee on Telecommunications and Finance of the House Commerce Committee*, Nov. 14, 2002, *available at* 2002 WL 1381127 (statement of John C. Coffee, Jr., Columbia University).

[39] *See* SENATE PERMANENT SUBCOMMITTEE ON INVESTIGATIONS OF THE COMMITTEE ON GOVERNMENTAL AFFAIRS, 107TH CONG., THE ROLE OF THE BOARD OF DIRECTORS IN ENRON'S COLLAPSE, July 8, 2002, *available at* http:// www.access.gpo.gov/congress/senate/senate12lp107.html [hereinafter Senate Print].

[40] *See, e.g.*, Tom Fowler, *The Pride and the Fall of Enron*, HOUS. CHRON., Oct. 20, 2002, at A25 [hereinafter *The Pride and the Fall*] ("[One manager, told that a deal would take a year, said,] 'I haven't got a year. If I can't do it in three months I won't do it because my bonus depends on it'" since "bonuses were based on the total value of the deal, not the cash it brought in."); Greg Hassell, *The Fall of Enron/The Culture/Pressure Cooker Finally Exploded*, HOUS. CHRON., Dec. 9, 2001, at 1.

Character and leadership are inextricably linked.[41] When the leaders are engaging in self-dealing and side deals,[42] and the supervisors of those leaders are also engaging in side deals,[43] and the gatekeepers are approving those side deals,[44] what should the rank and file be thinking? Given the magnitude of the potentially illegal profits made by CFO Andrew Fastow and CEO Jeffrey Skilling,[45] and the sense of entitlement that Enron encouraged,[46] it must have taken significant strength of character to resist getting on that gravy train. And yet, several people did resist. Who resisted, and why?

By now, those following the Enron case know that Sherron Watkins tried to alert CEO Kenneth Lay to serious concerns that she had about Enron's deals:

> Shortly after Enron announced Skilling's unexpected resignation on August 14, 2001, Watkins sent a one-page anonymous letter to Lay. The letter stated that "Enron has been very aggressive in its accounting—most notably the Raptor transactions." The letter raised serious questions concerning the accounting treatment and economic substance of the Raptor transactions (and transactions between Enron and Condor Trust, a subsidiary of Whitewing Associates), identifying several of the matters discussed in this Report. It concluded that "I am incredibly nervous that we will implode in

[41] Mary C. Daly, *Panel Discussion on Enron: What Went Wrong?*, 8 FORDHAM J. CORP. & FIN. L. 1, S28 (2002) ("What the literature teaches is that the ethical behavior is taught from the top down . . . . It is management's commitment to ethical standards that sets the tone.").

[42] The self-dealing by former Enron CFO Andrew Fastow was, apparently, approved by Enron's Board of Directors when the Board waived its ethics rules (more than once) to allow Fastow to head two partnerships that would be negotiating with Enron. *See, e.g.*, Letter from Max Hendrick, III, Vinson & Elkins, to James V. Derrick, Jr., Enron [Re: Preliminary Investigation of Allegations of an Anonymous Employee] (Oct. 15, 2001), *available at* 2001 WL 1764266 (CORPSCAN); *see also* Senate Print, *supra* note 39, at 23–24; Powers Report, *supra* note 38, at *68–71.

[43] The Enron Board apparently had several directors who also had consulting agreements with Enron, enabling a form of double-dipping. *See* Senate Print, *supra* note 39, at 51–55.

[44] *See* Powers Report, *supra* note 38, at *10 ("There was an absence of forceful and effective oversight by Senior Enron Management and in-house counsel, and objective and critical professional advice by outside counsel at Vinson & Elkins, or auditors at Andersen.").

[45] *Fastow Charged With Fraud, Conspiracy in Enron Case*, WASH. POST, Oct. 3, 2002, at A01; April Witt & Peter Behr, *Dream Job Turns Into a Nightmare; Skilling's Success Came at High Price*, WASH. POST, July 29, 2002, at A01; *see also* Senate Print, *supra* note 39, at 24, 34–36; Powers Report, *supra* note 38, at *3, 10.

[46] Enron employees who mastered the art of trading and deal-making could earn fantastic sums. Annual bonuses were as high as $1 million. Shortly after each bonus time, a new crop of silver Porsches—the most favored status symbol at Enron—would appear in the company garage. "I remember one trader going crazy because his bonus was only $500,000. He was cursing and screaming and throwing things at his desk," one former Enron employee recalls. "He thought because he was so brilliant, they should be paying him a lot more."

Hassell, *supra* note 40, at 1.

> a wave of accounting scandals." Lay told us that he viewed the letter as thoughtfully written and alarming.[47]

Watkins later told Lay that she had written the letter and met with him regarding her concerns.[48] Lay referred the matter to Enron's General Counsel, James Derrick, a former Vinson & Elkins partner.[49] Derrick in turn asked Vinson & Elkins, one of Enron's key outside law firms, to conduct a preliminary review of the situation—but not to review the underlying transactions that Watkins had discussed in her letter.[50] Within the confines of Derrick's request, Vinson & Elkins conducted an investigation (interviewing Watkins, among others).

V&E concluded that "none of the individuals interviewed could identify any transaction between Enron and LJM that was not reasonable from Enron's standpoint or that was contrary to Enron's best interests." On the accounting issues, V&E said that both Enron and Andersen acknowledge[d] "that the accounting treatment on the Condor/Whitewing and Raptor transactions is creative and aggressive, but no one has

---

[47] Powers Report, *supra* note 38, at 79. Note the new standards of behavior imposed on company attorneys by Sarbanes-Oxley:

> Not later than 180 days after the date of enactment of this Act, the Commission shall issue rules, in the public interest and for the protection of investors, setting forth minimum standards of professional conduct for attorneys appearing and practicing before the Commission in any way in the representation of issuers, 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.

Sarbanes-Oxley Act of 2002 § 307, 15 USC § 7245 (West Supp. 2002). After a whole slew of parties filed objections to the SEC's Proposed Rule regarding attorney conduct (with many of the objections focused on the "noisy withdrawal" provisions of the Proposed Rule, *see* http://www.sec.gov/rules/proposed/s74502.shtml), the SEC apparently abandoned the "noisy withdrawal" provision in its final rule, *see* http://www.sec.gov/news/press/2003-13.htm. As of this writing, I have only seen the press release regarding the final rule, not the actual text of the rule.

The days of taking an issue only partially up the chain of command are over, at least for publicly traded companies. But haven't lawyers always had the responsibility of taking matters all the way up the chain of command? *See* MODEL RULES OF PROF'L CONDUCT R. 1.13 (2002). I wonder whether Ms. Watkins, as an accountant, had a similar duty under her profession's ethics rules. If she did have such a duty, and she didn't go all the way to the Board of Directors (and beyond) with her concerns, was she really a whistleblower? (Mind you, what she did took some guts, even though she was not a whistleblower in the true sense.)

[48] Powers Report, *supra* note 38, at 79.

[49] *See* Ellen Joan Pollock, *Anderson: Called to Account: Enron Lawyers Face Congress Over Their Role*, WALL ST. J., Mar. 15, 2002, at C13 (noting that Derrick used to be a partner at Vinson & Elkins).

[50] Powers Report, *supra* note 38, at 79.

reason to believe that it is inappropriate from a technical standpoint." V&E concluded that the facts revealed in its preliminary investigation did not warrant a "further widespread investigation by independent counsel or auditors," although the firm did note that the "bad cosmetics" of the Raptor related-party transactions, coupled with the poor performance of the assets placed in the Raptor vehicles, created "a serious risk of adverse publicity and litigation."[51]

One observation: Vinson & Elkins's undertaking of the investigation had certain restrictions, including Enron's request not to review the bona fides of the underlying transactions.[52] We don't know what sort of give and take occurred between Enron and Vinson & Elkins about the usefulness of such a request.[53] At some point, thanks to the ability of Enron's chapter 11 management to waive the attorney-client privilege,[54] we

[51] *Id.* at *80.

[52] *Id.* at *79. "The result of the V&E review was largely predetermined by the scope and nature of the investigation and the process employed . . . . The scope and process of the investigation appear to have been structured with less skepticism than was needed to see through these particularly complex transactions." *Id.* at *81 (footnote omitted).

[53] Jordan Mintz, Enron Global Finance's General Counsel, has stated that Vinson & Elkins "fulfilled its professional duties" in terms of the advice it gave to Enron. Laura Goldberg, *Enron's Words as Relevant as Deeds/Reports May Have Told Partial Truths*, HOUS. CHRON., Feb. 11, 2002, at 1. Because of Vinson & Elkins's ties to Enron's General Counsel James Derrick, though, Mintz hired a separate firm, Fried, Frank, Harris, Shriver & Jacobson, to review the deals of which Watkins had complained. Rone Tempest, *Enron Counsel Warned About Partnerships Probe: Company's Legal Executive Asked Opinion of Law Firm in April. Congressional Investigators Say It Was to 'Halt This Practice,'* L.A. TIMES, Jan. 31, 2002, at C1. I'm not yet ready to get on the bandwagon that denounces all of Enron's lawyers.

[54] The principal case involving privilege in the bankruptcy context is, of course, Commodity Futures Trading Commission v. Weintraub, 471 U.S. 343, 358 (1985) ("[W]e hold that the trustee of a corporation in [a chapter 7] bankruptcy has the power to waive the corporation's attorney-client privilege with respect to pre-bankruptcy communications."). Weintraub answered the question of how much control a chapter 7 trustee had over the corporation's attorney-client privilege. *Id.* Subsequent cases have answered the question about how far the Weintraub holding could go in a chapter 11 context. *See, e.g.*, Am. Metrocomm Corp. v. Duane Morris & Heckscher LLP, 274 B.R. 641, 654–56 (Bankr. D. Dela. 2002) (stating that debtor-in-possession controls attorney-client privilege, and debtor-in-possession can request documents from attorneys even if attorneys raise work product privilege as a defense); *In re* Bame, 251 B.R. 367, 370, 374 (Bankr. D. Minn. 2000) (converting chapter 11 case to chapter 7 case; holding that chapter 7 trustee can access the post-petition, pre-conversion communications between the debtor-in-possession and its lawyers because the privilege is held by the estate, and not by the debtor-in-possession); Whyte v. Williams (In re Williams), 152 B.R. 123, 129 (Bankr. N.D. Tex. 1992) ("The liquidating trustee [under a confirmed chapter 11 plan] controls the power to waive or invoke the evidentiary privileges that arise in connection with the causes of action transferred to the liquidating trust under Article 25.5 of the confirmed plan."); *see also* S. Air Transp., Inc. v. SAT Group, Inc., 255 B.R. 706, 711 (Bankr. S.D. Ohio 2000) (citations omitted).

> The Court agrees that a corporate fiduciary is precluded from asserting privileges to protect his own interests that are adverse to those of the corporation. Corporate officers must "exercise the privilege in a manner consistent with their fiduciary capacity to act in the best interests of the corporation and not of themselves individually."

Id. The interesting part about the privilege issue in the Enron bankruptcy context is whether Steve Cooper (the restructuring expert currently running Enron) is going to waive the privilege in order to get

may learn more. But I have to admit, right off the bat, that I have a hard time believing that Vinson & Elkins, or any of Enron's other law firms, knowingly advised Enron to do anything that was clearly illegal. The real issue is how Enron handled the grey areas of the law, based on the advice of all of its lawyers (both its in-house and outside counsel).

Watkins wasn't the lone voice questioning Enron's deals; others, including Enron Global Finance's General Counsel Jordan Mintz, were concerned about the structure and disclosure of the various deals.[55] Apparently, Fastow and Skilling didn't brook disagreement willingly. Those who objected often found themselves the subject of pressure, downright abuse, and exile.[56]

I'd like to put forward one striking similarity between the *Titanic* and Enron: a failure of meaningful communication stemming from a belief that someone else had "taken care of it." Here's how a recent newspaper article described the problem:

> [S]ince most only saw their part of the business, they assumed the problems were isolated. . . . "You understood your piece of the business and maybe what the guy next to you did, but very few understood the big picture. . . .

---

information from the various law firms that represented Enron and then, if the information gives rise to a cause of action against any of Enron's lawyers, use that very information to pursue them in bankruptcy court. Mr. Cooper can also pursue Enron's officers and directors using that privileged information, as the privilege belongs to the client (Enron) and not to any of the client's employees. I've been following the work of the Severed Enron Employees Coalition in the pursuit of the prepetition bonuses paid to certain Enron executives on the theory that the bonuses were fraudulent conveyances. Severed Enron Employees Coalition v. N. Trust Co., No. 02-0267 (S.D. Tex. complaint, filed Jan. 24, 2002). Any privileged advice, on the order of "Should we pay this person a retention bonus? What will we get in terms of a benefit for the retention bonus?," could be helpful in this regard.

[55] *See, e.g.*, Senate Print, *supra* note 39, at 28 n.81 (quoting an internal memorandum from Mintz):

> [T]he Company needs to improve both the process it follows in executing such transactions and implement improved procedures regarding written substantiation supporting and memorializing the Enron/LJM transactions . . . . [F]irst is the need for the Company to implement a more active and systematic effort in pursuing non-LJM sales alternatives before approaching LJM . . . ; the second is to . . . impose a more rigorous testing of the fairness and benefits realized by Enron in transacting with LJM.

Id.; *see also* Dan Feldstein, *Skilling Says He Did No Wrong / Lawyer Told Not to Stick Neck Out*, HOUS. CHRON., Feb. 8, 2002, at 1 (describing how Fastow tried to bully Mintz into blessing irregularities in certain Enron deals).

[56] *See, e.g.*, *The Pride and the Fall*, *supra* note 40, at 27A (listing three people—Andersen partner Carl Bass, former Enron CFO (after Fastow) Jeff McMahon, and former Merrill Lynch analyst John Olson—who were demoted (Olson was fired) after criticizing the aggressive Enron deals and accounting methods); *see also* Editorial Desk, *Not Quite a Whistle-Blower*, N.Y. TIMES, Feb. 15, 2002, at A20; Andy Geller, *"I Believe Mr. Skilling and Mr. Fastow Duped Mr. Lay"—Enron VP Rips Duo Before Congress*, N.Y. POST, Feb. 15, 2002, at 9; Susan Schmidt, *CEO Was 'Misserved' At Enron, Hill Told; Former Executive Blames Other Top Managers*, WASH. POST, Feb. 15, 2002, at A01; Peter Spiegel, *The Architect of Enron's Downfall: Internal Probe Reveals Andy Fastow as a CFO who Bullied Staff and Even Wall Street Banks, Enriching Himself by More than Dollars 45m in the Process*, FIN. TIMES, May 21, 2002, at A20.

> That segmentation allowed us to get work done very quickly, but it isolated that institutional knowledge into the hands of very few people."[57]

Certainly, the Powers Report describes the failure of follow-through regarding several of the Enron deals—the failure to ascertain if the checks and balances, supposedly part of each deal's structure, were in place and working.[58] As John Coffee explains,

> Enron . . . furnish[es] ample evidence of a systematic governance failure. Although other spectacular securities frauds have been discovered from time to time over recent decades, they have not generally disturbed the overall market. In contrast, Enron has clearly roiled the market and created a new investor demand for transparency. Behind this disruption lies the market's discovery that it cannot rely upon the professional gatekeepers—auditors, analysts, and others—whom the market has long trusted to filter, verify and assess complicated financial information. Properly understood, Enron is a demonstration of gatekeeper failure, and the question it most sharply poses is how this failure should be rectified.[59]

Failures of gatekeeper professionals aren't new. The savings and loan crisis, which also represented a significant gatekeeper failure, occurred a mere twenty years ago;[60] the Salomon Brothers Treasury bonds trading scandal occurred just ten years ago.[61]

---

[57] *See, e.g., The Pride and the Fall, supra* note 40, at 27A. Remember that those "very few people" included members of the Board of Directors, which waived Enron's ethics rules more than once to allow self-dealing by some of Enron's executives. *See supra* note 42.

[58] *See* Powers Report, *supra* note 38, at *18–28.

[59] John C. Coffee, Jr., *Understanding Enron: It's About the Gatekeepers, Stupid,* 57 BUS. LAW. 1403 (2002) (footnote omitted), *reprinted in this book at* 125–143.

[60] Now that I wear bifocals, twenty years just doesn't seem that long ago.

[61] Daly, *supra* note 41, at S25–S28; Federal Document Clearing House, *U.S. Senate Committee on Commerce, Science and Transportation Holds a Hearing on Enron Bankruptcy,* Dec. 18, 2001, *available at* 2001 WL 1623334 (statement of John Coffee, Columbia University) ("Well, when a debacle like Enron occurs, the critical question for Congress and for regulators is to ask, as you've been beginning to ask, where were the gatekeepers; where were the watchdogs? . . . Here, all failed, and all failed fairly abysmally.").

> The fallout from [the savings and loan] scandal included a Justice Department action against the prestigious New York firm of Kaye, Scholer, Fierman, Hays & Handler. Kaye, Scholer and partner Peter Fishbein were said to have gone beyond mere aggressive lawyering, and more than one observer viewed their representation as akin to aiding and abetting, while others attributed any errors to simple inattentiveness. Ultimately, the case was settled, with the firm and its malpractice carrier paying $41 million in settlement, and the Keating lawyers paid for their alleged sins, notwithstanding their ability to spread the loss to other lawyers via malpractice insurance coverage.

Jeffrey W. Stempel, *Embracing Descent: The Bankruptcy of a Business Paradigm for Conceptualizing and Regulating the Legal Profession,* 27 FLA. ST. U. L. REV. 25, 111–12 (1999) (footnotes omitted). For a

It's certainly possible that many of the legal and accounting professionals (the in-house and the outside professionals) who advised Enron assumed that Enron's own businesspeople were doing the follow-through; moreover, many of those same professionals may well have thought that it was not the lawyers' or accountants' "place" to bill Enron for continued checks of the system. (I know nothing about the training of accountants, so I'm going to limit the rest of this discussion to the training of lawyers.) If the lawyers saw themselves as morally independent from Enron, rather than morally interdependent, then they might well have believed that it was Enron's job, not theirs, to ensure follow-through. A more complex explanation is that cognitive dissonance—well-documented in social science literature and applied to lawyers by, among others, David Luban—prevented the lawyers from seeing some of these deals more clearly. My hunch is that both concepts (a mistaken belief in moral independence, rather than interdependence, and the effects of cognitive dissonance) played a part in any failures by the gatekeepers.

A. "Moral Independence" Versus "Moral Interdependence" as an Explanation

For the longest time, lawyers have done everything they could to distinguish the client's ends from the means that the lawyers used to achieve those ends. This "moral independence" theory has been used to justify everything from lawyers who take on unpopular causes to lawyers who facilitate shady deals, even though the original theory was never intended to justify shady deals.[62]

---

wonderful discussion of the Kaye, Scholer firm and the savings and loan crisis, see David B. Wilkins, *Making Context Count: Regulating Lawyers After Kaye, Scholer*, 66 S. CAL. L. REV. 1147 (1993). As Clarence Darrow apparently said, "History repeats itself, and that's one of the things that's wrong with history." The Quotations Home Page, *available at* http://www.geocities.com/~spanoudi/topic-h3.html#history.

[62] According to a study by Erwin Smigel, lawyers'

> independence derived from two sources. First, "they . . . 'represent' the law and must therefore separate themselves from the client." Second, the commodity they sold was "[i]ndependent legal opinion." Smigel observed that "client[s] desire that a firm maintain its autonomy" so that they can obtain the best advice. Moreover, as the large firms grew older, they increased their number of clients and moved away from fundamentally relying on one or a few clients. This shift "strengthened . . . a firm's ability to retain its independence" because "no one client provid[es] enough income to materially or consciously influence the law office's legal opinion."

Russell G. Pearce, *Lawyers as America's Governing Class: The Formation and Dissolution of the Original Understanding of the American Lawyer's Role*, 8 U. CHI. L. SCH. ROUNDTABLE 381, 406 (2001) (footnotes omitted) [hereinafter Governing Class] (quoting ERWIN O. SMIGEL, THE WALL STREET LAWYER: PROFESSIONAL ORGANIZATION MAN? (1964)).

The fun part about the history of the bar's independence theory is its link with the robber barons of yesteryear. *See, e.g.*, Thomas L. Shaffer, *The Profession as a Moral Teacher*, 18 ST. MARY'S L.J. 195, 222–23 (1986) [hereinafter *Moral Teacher*]; Thomas L. Shaffer, *The Unique, Novel, and Unsound Adversary Ethic*, 41 VAND. L. REV. 697, 703–04 (1988). As Russell Pearce points out,

Several scholars have recognized, though, that the complexity of modern legal practice forces lawyers to take a more active role in shaping not just the clients' advice but the clients' deals and litigation as well.[63] Richard Painter's "moral interdependence" theory of the lawyer-client interaction is a more realistic view of the lawyer's modern role, especially when it comes to complex transactions or complex litigation.[64]

When you overlay the lawyer's moral interdependence on top of a cutthroat culture, you get Enron (and WorldCom, and Tyco, etc.). We still don't know a lot of the facts behind Enron's various deals, including what the various lawyers said, Enron's response to that advice, or how much the accountants' advice contradicted (or supported) the lawyers' advice. But we do know that the structure of Enron itself encouraged a constant pushing of the outside of the envelope.[65] Enron encouraged a "me, first" structure, not a cooperative one.

> "Enron sought to redefine the rules of the industry," said Robert Bruner, a professor at the University of Virginia who has made a case study of Enron's culture. "It was a culture of challenge and confrontation."
>
> . . . .
>
> [Former CEO Jeffrey] Skilling also is responsible, many insiders say, for creating a mercenary, cutthroat culture to stoke the fires beneath the enterprise. One of the hallmarks of the Skilling regime was a performance review process that employees called "rank and yank." The evaluations compared the performance of employees against one another, with the bottom 15 percent getting axed every year.

> In becoming hired guns, elite lawyers abandoned the traditional governing class ideology. They were no longer acting as a disinterested political leadership capable of discerning and pursuing the common good. Instead, they were advocates of private interests. They had violated professionalism's taboo on acting as a servant of big business and could no longer claim the special tie to the public good which distinguished them from those in business.

Pearce, *Governing Class*, *supra*, at 400–10.

[63] Richard W. Painter, *The Moral Interdependence of Corporate Lawyers and Their Clients*, 67 S. CAL. L. REV. 507, 511, 544–45 (1994); *see also id.* at 526 ("Joint decisionmaking by lawyer and client has become both efficient and prudent.") (footnote omitted).

[64] For example, the Powers Report points out that, with respect to preparing the various disclosure forms that Enron filed, "[w]hile accountants took the lead in preparing the financial statement footnote disclosures, lawyers played a more central role in preparing the proxy statements, including the disclosures of the related-party transactions." Powers Report, *supra* note 38, at 84. This interdependence is by no means limited to the lawyers who worked on Enron's deals. *See Governing Class*, *supra* note 62, at 408–09 (citing Robert A. Kagan and Robert Eli Rosen, *On the Social Significance of Large Law Firm Practice*, 37 STAN. L. REV. 399 (1985) and Robert L. Nelson, *Ideology, Practice, and Professional Autonomy: Social Values and Client Relationships in the Large Law Firm*, 37 STAN. L. REV. 503 (1985)). Both the Kagan & Rosen study and the Nelson study are well worth reading.

[65] I first saw this phrase in TOM WOLFE, THE RIGHT STUFF 12 (1979).

> The evaluations were done by asking employees to judge others' performance. They did so knowing their own promotions and survival hung in the balance.
>
> "Because of that, you never helped one another," said one former Enron employee. "Everyone was in it for themselves. People stabbed you in the back."
>
> Teamwork, once a source of strength, started to disappear.
>
> "It was every man for himself," a former Enron executive said.
>
> What sense of teamwork survived "rank and yank" was undermined by Enron's reward system, which seemed to place no value on group goals but lavishly rewarded individual accomplishment. An employee who could close big deals got big bonuses and promotions. Those who couldn't were shown the door.[66]

Let's take this moral interdependence theory one step further. Add to the theory (1) Enron's culture, and (2) the personality traits of a large number of lawyers (whether or not they ever had Enron as a client), and you have a disaster just waiting to happen. Susan Daicoff has summarized the literature on lawyers' personality traits quite nicely in a series of articles.[67] Lawyers tend to have certain personality characteristics that contribute to their need to "win." They "appear to be more competitive, aggressive, and achievement-oriented, and overwhelmingly Thinkers (instead of Feelers). . . . Lawyers are more often motivated by a need for achievement than are others, which includes a need to compete against an internal or external standard of intelligence."[68] No matter which way you slice it, these gatekeepers were too closely involved with their client[69] to be able to stand up and say, "You shouldn't do that." At some point, we need lawyers to say, "The law lets you do it, but don't. . . . It's a rotten thing to do."[70]

---

[66] Hassell, *supra* note 40. For a masterful compendium of the theories surrounding community norms in monitoring and shaping the roles of lawyers, see W. Bradley Wendel, *Nonlegal Regulation of the Legal Profession: Social Norms in Professional Communities*, 54 VAND. L. REV. 1955 (2001) [hereinafter *Social Norms*].

[67] *See, e.g.*, Susan Daicoff, *Lawyer, Know Thyself: A Review of Empirical Research on Attorney Attributes Bearing on Professionalism*, 46 AM. U. L. REV. 1337 (1997) [hereinafter *Know Thyself*]; Susan Daicoff, *(Oxymoron?) Ethical Decisionmaking by Attorneys: An Empirical Study*, 48 FLA. L. REV. 197, 217–18 (1996).

[68] *Know Thyself*, *supra* note 67, at 1408–09 (footnotes omitted). According to Daicoff, law students come into law school hard-wired with these traits. *Id.* at 1349–50. Imagine my relief at knowing that law school didn't "ruin" them.

[69] *See, e.g.*, *supra* notes 49–50 and accompanying text.

[70] Sol M. Linowitz, *Moment of Truth for the Legal Profession*, Address at the University of Wisconsin Law School (Oct. 24, 1997), *in* 1997 WIS. L. REV. 1211, 1214–15 ("I believe Elihu Root once again had it exactly right when he told a client: "The law let[s] you do it, but don't . . . . It's a rotten thing to do.").

B. Cognitive Dissonance as an Explanation

Even if the gatekeepers weren't so closely involved with the client, there's yet another reason for their failure to protest the deals that were on (or over) the edge: cognitive dissonance. My sociologist friends[71] tell me that moral development alone—which is an individual trait—can't explain how an individual will react to a particular situation.[72] The situation itself will interact with the traits of the individual, and both the person's individual traits and his situation will affect an outcome.[73]

Peer pressure is one such particular influence. There are some well-regarded studies showing that even relatively obvious physical conclusions, such as the distance from one point to another or the length of a line, can become subject to "groupthink," placing peer pressure on the unbelieving minority to conform to the wrong-headed thinking of the majority.[74] And if hard-wired concepts, such as size and location, are manipulable by the particulars of the situation, what about the fuzzier concept of behavior?

Stanley Milgram's studies on the willingness of experimental subjects to inflict pain (electrical shocks) on complete strangers can give us a glimpse into how powerful the effect of a particular situation can be. In Milgram's best-known study, the actual subject was asked to give a series of progressively more severe shocks to someone who was posing as a fellow experimental subject. Although the actual subject usually agonized about administering the shocks, he went ahead and administered them nonetheless.[75]

In analyzing Milgram's experiment, Lee Ross and Richard Nisbett concluded that the powerful structure of the situation—the authority figure setup; the calm tones of

---

[71] Special thanks go to Julia McQuillan, who guided me through the literature and theories in her field.

[72] *Cf.* Julia McQuillan & Julie Pfeiffer, *Why Anne Makes us Dizzy: Reading Anne of Green Gables from a Gender Perspective*, 16 MOSAIC 34/2, June 2001, at 19 ("In an attempt to explain variation within sex categories, sociologists have argued that external social structures (our actual experiences in the world) organize our behavior more than socialization (how we've been told to behave).").

[73] The thought that moral development alone can predict a person's behavior without regard to the particular situation is called the "fundamental attribution error." *See* DAVID J. LUBAN, THE ETHICS OF WRONGFUL OBEDIENCE, *in* ETHICS IN PRACTICE: LAWYERS' ROLES, RESPONSIBILITIES, AND REGULATION 94, 101 (Deborah L. Rhode ed., 2000) [hereinafter WRONGFUL OBEDIENCE]; *see also* Lee M. Johnson, et al., *General Versus Specific Victim Blaming*, 142 J. OF SOC. PSYCHOL. 249 (Apr. 2002) ("The fundamental attribution error occurs when individuals overemphasize personal attributes and discount environmental attributes in their judgments of others"); LEE ROSS, THE INTUITIVE PSYCHOLOGIST AND HIS SHORTCOMINGS: DISTORTIONS IN THE ATTRIBUTION PROCESS, IN 10 ADVANCES IN EXPERIMENTAL SOCIAL PSYCH. 173 (Leonard Berkowitz ed., 1977); *see generally* DAVID C. FUNDER, PERSONALITY JUDGMENT: A REALISTIC APPROACH TO PERSONAL PERCEPTION (1999).

[74] LEE ROSS & RICHARD E. NISBETT, THE PERSON AND THE SITUATIONS: PERSPECTIVES OF SOCIAL PSYCHOLOGY 30 (1991) ("Our most basic perceptions and judgments about the world are socially conditioned and dictated.") (citing Sherif's "autokinetic effect" studies and Asch's "comparison lines" studies).

[75] *Id.* at 56–57.

the experimenter standing next to the subject who was administrating the shocks; the experimenter's repetition of the phrases, "The experiment requires that you continue; you have no choice"—served to overcome the subjects' expressed desire to stop the experiment before reaching the "severe shock" stage.[76] Most of the subjects were stymied by uncertainty and couldn't overcome the social pressure of the situation. It's not that the subjects were sadists. But the structure of the situation prevented them from acting on their own reluctance to continue the shocks.

David Luban has also described the Milgram experiment and has pointed out that almost two-thirds of the subjects in Milgram's experiments actually did go all the way to 450 volts.[77] He posits that a "corruption of judgment" stemming from cognitive dissonance caused two-thirds of the subjects of Milgram's experiments to "kill" the learner:

> [T]he key to understanding Milgram compliance lies in features of the experimental situation. . . . The teacher moves up the scale of shocks by 15-volt increments, and reaches the 450-volt level only at the thirtieth shock. Among other things, this means that the subjects never confront the question "Should I administer a 330-volt shock to the learner?" The question is "Should I administer a 330-volt shock to the learner given that I've just administered a 315-volt shock?" It seems clear that the latter question is much harder to answer. . . .
>
> Cognitive dissonance theory teaches that when our actions conflict with our self-concept, our beliefs and attitudes change until the conflict is removed. . . . Cognitive dissonance theory suggests that when I have given the learner a series of electrical shocks, I simply won't view giving the next shock as a wrongful act, because I won't admit to myself that the previous shocks were wrong.[78]

Luban's most important point is that lawyers aren't immune to the effects of cognitive dissonance. He does a masterful job of linking the *Berkey Photo-Inc. v. Eastman Kodak Co.*[79] case and Stanley Milgram's experiments on obedience to explain how very well-intentioned lawyers can find themselves slipping into serious breaches of ethics. For those who aren't familiar with this case, Brad Wendel describes it nicely:

---

[76] One of Milgram's later variations on the study involved changing the setting from Yale to an inner-city, run-down, suspicious-looking lab in another town. He recorded approximately the same results, no matter the setting. *See id.* at 55.

[77] WRONGFUL OBEDIENCE, *supra* note 73, at 97 ("In reality, 63 percent of subjects complied all the way to 450 volts. Moreover, this is a robust result: it holds in groups of women as well as men, and experimenters obtained comparable results in Holland, Spain, Italy, Australia, South Africa, Germany, and Jordan. . . .") (footnote omitted).

[78] *Id.* at 102 (footnotes omitted).

[79] 74 F.R.D. 613 (S.D.N.Y. 1977).

> The lawyers representing Kodak had retained an economist as an expert witness, expecting that he would testify that Kodak's domination of the market was due to its superior technological innovations, not to anticompetitive behavior. The plaintiff's counsel requested any documents pertinent to the expert's testimony, Kodak's lawyer's resisted, and ultimately a magistrate ordered production of numerous documents including interim reports prepared by the economist. At the economist's deposition, one of Kodak's lawyers stated that he had destroyed the interim reports, which were somewhat unfavorable to Kodak's defense. The lawyer even filed an affidavit in a subsequent discovery dispute in the case, stating under oath that the documents had been destroyed. In fact, the lawyer had not destroyed the documents, but had hidden them in his office and withheld them from production. The affidavit was perjurous. The fallout was a calamity for the firm. Kodak fired it and hired one of its arch-rivals to defend the antitrust case. The firm paid its client over $600,000 to settle Kodak's claims related to its conduct of the litigation. It lost Kodak's business, which had accounted for approximately one-fourth of the firm's billings and had employed thirty lawyers full-time. The partner who had coordinated the firm's preparation of the economist's testimony was released from the firm and spent twenty-seven days in jail for contempt of court.[80]

In his discussion of the *Berkey-Kodak* case, Luban relates the following episode:

> Joseph Fortenberry, the associate working for [Mahlon Perkins, the partner representing Kodak], knew that Perkins was perjuring himself and whispered a warning to him; but when Perkins ignored the warning, Fortenberry did nothing further to correct his misstatements. "What happened" recalls another associate, "was that he saw Perkins lie and really couldn't believe it. And he just had no idea what to do. I mean, he . . . kept thinking there must be a reason. Besides, what do you do? The guy was his boss and a great guy!"[81]

Fortenberry's comments highlight how fledgling lawyers will take many social cues from those more experienced lawyers whom they respect.[82] Of course, the pressure

[80] W. Bradley Wendel, *Morality, Motivation, and the Professionalism Movement*, 52 S.C. L. REV. 557, 606–07 (2001) (footnotes omitted); *see also* Walter Kiechell III, *The Strange Case of Kodak's Lawyers*, FORTUNE, May 8, 1978, at 188. If I were a superstitious sort, I'd worry about the fact that one of the two "smoking guns" in the case was Exhibit 666. *Id.* I am *not* making this up.

[81] WRONGFUL OBEDIENCE, *supra* note 73, at 95 (footnotes omitted).

[82] Cognitive dissonance isn't limited to outside counsel. In a study of inside counsel, Hugh and Sally Gunz found that the lawyers' advice was not always independent from the direction that the company itself intended to go:

that the senior lawyers have to keep their clients, maintain their billings, and compete with other elite lawyers at other firms (who are all too happy to steal clients away), is relentless pressure indeed. But if the more senior lawyers can't withstand the pressure, then who will teach the fledgling lawyers to resist?

III. WHERE DO WE GO FROM HERE?

If we want lawyers to spend more time understanding themselves and their relationship to their clients, then we're going to have to lead from the top, with judges, partners, bar associations, and other senior lawyers all singing the same tune. It won't be sufficient for law professors to warn students against the temptations and pressures of law practice. As a matter of fact, it's depressing how little influence law professors have on their students' understanding of legal ethics.

Larry Hellman's study on cognitive dissonance in a legal ethics class is proof of the need to have top lawyers do the preaching, not law professors.[83] Hellman asked the students in his ethics course to keep diaries of possible ethics violations that they observed while working for lawyers during the semester, and those students recounted bad lawyering in an astonishing variety of forms—neglect, incompetence, conflicts of interest, and the like.[84] If we want to train newly minted lawyers to be ethical, it's just not enough for law professors to talk the talk. We must join forces with the lawyers and judges in the "real world," those who can walk the walk.

Lawyers need to behave as true counselors to their clients, rather than as hired guns who are just following orders. Society needs us to take on the role of the social con-

---

> From a practitioner standpoint, the model highlights issues surrounding the nature of the advice that organizations can expect to obtain from their in-house counsel when placed in positions of ethical conflict. In our original study of OPC [organizational professional conflict], we suggested that an important implication of our findings was that in-house counsel might not necessarily always provide disinterested professional advice. In their different ways, the Technician and Organization Person might produce superficially helpful advice, which could, under certain circumstances, be dangerously misleading. The Technician, for example, may deliver clever but myopic solutions, and the Observer could well misjudge a situation and remain silent inappropriately. But the Advisor, by avoiding the "cop" aspect of the Lawyer role (in the sense that there is no implication that he or she intends to report the situation to the next level higher within the organization, or to a regulator outside the organization), stays closer to the Lawyer's advice. So the model, as revised, suggests an even greater variety of potential responses than in its initial L[awyer], T[echnician], and O[bserver] form, underlining yet more firmly the need to avoid making simplistic assumptions about the nature of the advice in-house counsel provide their employer[s].

Hugh P. Gunz & Sally P. Gunz, *The Lawyer's Response to Organizational Professional Conflict: An Empirical Study of the Ethical Decision Making of In-House Counsel*, 39 AM. BUS. L.J. 241, 279–80 (2002) (footnotes omitted).

[83] Lawrence K. Hellman, *The Effects of Law Office Work on the Formation of Law Students' Professional Values: Observation, Explanation, Optimization*, 4 GEO. J. LEGAL ETHICS 537 (1991).

[84] *Id.* at 601–05.

science (or, if that sounds too darn highfallutin', the role of the grease that helps society run). As David Luban has pointed out,

> If lawyers have special responsibilities to legal justice, that is not because they are divinely elected, or better and holier that [sic] the rest of us. It is because of how their role fits into an entire division of social labor. Lawyers represent private parties before public institutions, or advise private parties about the requirements of public norms, or reduce private transactions to a publicly-prescribed form, or ratify that transactions are in compliance with public norms. To say that they have special duties of fidelity to those norms is no more ecstatic and supernatural than saying that food-preparers have heightened duties to ensure their hands are clean. It is their social role, not the brush of angels' wings on their foreheads, that requires [food service workers] to wash their hands every time they go to the bathroom.[85]

We used to be better at setting good examples, or so I've heard. In the "golden days" that Tom Shaffer recounts, some of the lawyers that he observed set wonderful examples for their newly minted lawyer colleagues. In my favorite article of his, *The Profession as a Moral Teacher*, he tells story after story of lawyers who did the right thing.[86] The constant choice of ethical over unethical behavior helped mold the lawyer that Shaffer eventually became:

> [Those two partners in my former law firm] were philosophically and temperamentally different and . . . practiced law in different ways. That they were so much alike in these moral matters said something about their personal character, of course, but, in view of their personal differences, it also said something about the way the firm practiced law—about the way the firm functioned as the profession (for me) and, as the profession, functioned (for me) as a moral teacher. It was not, that is, an apprenticeship, in which I was learning my craft, and the morals of my craft, from a master—or at least it didn't seem, then, that it was. It was the profession (the law firm) that was the moral teacher. . . . It was even more like the moral formation a person gets from family, town, and church. Which is to say that, here, code depended on character.[87]

[85] David Luban, *Asking the Right Questions*, 72 TEMP. L. REV. 839, 849–50 (1999).

[86] *Moral Teacher*, *supra* note 62, at 214–17.

[87] *Id.* at 216–17.

From his experience as a young lawyer, Shaffer took the moral lesson that a lawyer should also be a gentleman.[88] Tom Shaffer's view of the "gentlemanly" lawyer, of course, has its critics,[89] including Shaffer himself.[90] And yet, we do understand the concept that he's trying to express:[91] that of a lawyer who understands her role in society as more than just a mere scrivener or functionary, and who tries always to take the moral high ground.[92]

---

[88] Thomas L. Shaffer, *On Being a Professional Elder*, 62 NOTRE DAME L. REV. 624, 630–31 (1987) [hereinafter *Professional Elder*] ("When character is in place, fortified by 'a few rules' that have to do with professional craft, the professional person becomes dependable. Professional character is the connection between virtue and craft. The convention has been to describe that connection with the word gentleman.") (footnotes omitted). If you haven't read Tom Shaffer's work on this topic, you should. For a quick shortcut—not to be confused with reading Shaffer's work—Leslie Gerber has created a good primer. *See* Leslie E. Gerber, *Can Lawyers Be Saved? The Theological Legal Ethics of Thomas Shaffer*, 10 J.L. & RELIGION 347 (1994).

[89] *See, e.g.*, Ann Bartow, *Still Not Behaving Like Gentlemen*, 49 U. KAN. L. REV. 809, 810–11 (2001); Susan Daicoff, *Asking Leopards to Change Their Spots: Should Lawyers Change? A Critique Of Solutions to Problems with Professionalism by Reference to Empirically-Derived Attorney Personality Attributes*, 11 GEO. J. LEGAL ETHICS 547, 582–83 (1998); William J. Wernz, *Does Professionalism Literature Idealize the Past and Over-Rate Civility? Is Zeal a Vice or a Cardinal Virtue?*, 13 PROF. LAW. 1 (2001) (disputing the claim that "back then"—whenever "then" was—lawyers were more professional and more civil).

[90] Thomas L. Shaffer, *The Gentleman in Professional Ethics*, 10 QUEEN'S L.J. 1, 11 (1984).

> The 19th century gentleman in North America gave us slavery, Manifest Destiny, the theft of half of Mexico, the subjugation of women, the exploitation of immigrant children, Pinkerton detectives, yellow-dog contracts, and the implacable genocide of American Indians. You could make a case . . . that the gentleman's ethic is not worth taking seriously. If the gentleman has left the professions, the best thing for us would be to bar the door lest he get back in.

Id.; *see also* Thomas L. Shaffer, *Inaugural Howard Lichtenstein Lecture in Legal Ethics: Lawyer Professionalism as a Moral Argument*, 26 GONZ. L. REV. 393, 400 (1991); *Professional Elder*, *supra* note 88, at 633–34.

[91] Edward McGlynn Gaffney, Jr., *In Praise of a Gentle Soul, Remarks at the Annual Banquet of the Journal of Law and Religion* (Oct. 14, 1993), *in* 10 J.L. & RELIGION 279, 284 (1993/1994).

> The acid test of [Tom Shaffer's] reliance on the ethics of gentlemen is whether it, too, is not flawed at its core. Is it not by definition limited to males, and does it have any space for minorities? Only one like Shaffer, who by decades of living like a gentleman himself and reflecting carefully on that ethic, could have come to the conclusion that the ethic of the gentleman-lawyer has greater possibilities for the subversion of patriarchy than the ABA's model of professionalism.

Id. (footnotes omitted).

[92] Bill Hodes points out that "[t]he acid test of ethical lawyering is rarely what to do in the face of crisis—a client shows you the buried bodies or drops a bloody knife on your desk or commits perjury or destroys or hides material property asked for in discovery." W. William Hodes, *Accepting and Rejecting Clients—The Moral Autonomy of the Second-to-the-Last Lawyer in Town*, 48 U. KAN. L. REV. 977, 978 (2000) (citing the classic cases of People v. Belge, 372 N.Y.S. 2d 798 (N.Y. Crim. Ct. 1975) (buried bodies), State v. Olwell, 394 P.2d 681 (Wash. 1964) (bloody knife), Nix v. Whiteside, 475 U.S. 157 (1986) (perjury), and Berkey Photo, Inc. v. Eastman Kodak Co., 74 F.R.D. 613 (S.D.N.Y. 1977) (work product)). For a wonderful discussion of how social norms affect lawyering, see *Social Norms*, *supra* note 66.

What happens when we don't set the right example? We can call doing the right thing "behaving like gentlemen," or we can use some other, less "loaded" phrase. If we don't exert some leadership and emphasize the role of character in the practice of law, some very smart lawyers will continue to do stupid things, and some clients will continue to do stupid (or venal) things. Some of these people will even trot out the hoary (and discredited) old saw that they were "just following orders."[93]

So how do we encourage lawyers to withstand peer pressure and client pressure, especially in those grey areas in which the lawyer gives advice akin to "it's an aggressive interpretation of the law" and the client chooses to use that aggressive interpretation, even at the risk of later litigation? Remember, we're not talking about lawyers who deliberately counsel clients to flout the law. Rather, we're talking about lawyers who say that a particular interpretation could go either in favor of the client or against it.

Personally, I like Russ Pearce's idea that we create a new Model Rule 1.0. His Model Rule 1.0 would provide that "lawyers are morally accountable for their conduct as lawyers."[94] That rule hits the question of moral interdependence head on, and it provides a powerful reminder that "just following orders" is the weakest of excuses.[95]

We can blame part of Enron's downfall on the economy. We can blame part of it on corporate misbehavior, on board malfeasance, and on pure greed. We can blame part of it on a structure that allowed gatekeepers and reputational intermediaries—the board, the accountants, and the lawyers—to rely on the other two categories to understand the overall picture of what Enron was doing. We can even blame the Enron employees who chose to place too much Enron stock in their own 401(k) plans, thereby betting twice with the same money.[96] But one thing we can't blame is fate. Enron's collapse

---

[93] *See, e.g.*, Tom Fowler, *Ex-Andersen auditor defended / Aide: Boss was told to shred files*, HOUS. CHRON., Mar. 7, 2002, at 1 ("An assistant to the Arthur Andersen lead partner who handled the Enron account said she believes her boss was just following orders when he told workers to destroy Enron-related documents last fall."); Marcy Gordon, *SEC, Informal Wall Street System Failed to Detect Enron Failure, Report Finds*, ASSOCIATED PRESS NEWSWIRES, Oct. 7, 2002, Westlaw, Allnewsplus Library (Fastow's lawyer contends that his client was just following orders).

[94] Russell G. Pearce, *Model Rule 1.0: Lawyers are Morally Accountable*, 70 FORDHAM L. REV. 1805, 1807–08 (2002). Pearce points out that Model Rule 1.0 would not take sides in current disputes regarding the lawyer's role. What it would do is move the debates regarding the lawyer's moral duties, like that between Freedman, who favors zealous representation, and Luban, Rhode, and Simon, who favor some significant limits on that representation, to the center of the bar's legal ethics conversations. While the bar currently pays some slight attention to these issues, Model Rule 1.0 would move them to a more prominent place in the bar's official deliberations and continuing legal education courses, as well as in the efforts of the conscientious lawyer to explore her own moral accountability.

[95] I'm not sure how one might enforce a Model Rule 1.0, but at least Pearce is heading in the right direction.

[96] *See, e.g.*, Mark Davis, *The Fallout of a Fallen Enron; Too Much Company Stock in 401(k); Plans Poses Risk*, KAN. CITY STAR, Jan. 20, 2002, at A1; Kaja Whitehouse, *401(k) Woes? Might Be Your Own Fault*, DOW JONES NEWS SERV., Jan. 18, 2002, Westlaw, Allnewsplus Library. Of course, the freeze on selling stock as the value of the stock spiraled downward also had something to do with the losses in the employees' 401(k) plans. *See, e.g.*, Davis, *supra*; Editorial, *Enron and Frontier Justice Fear of Angry Workers Sends Energy Trading Firm to New York to File for Bankruptcy*, PORTLAND OREGONIAN, Dec. 4, 2001, at D06.

wasn't due to a "perfect storm" of mere coincidence—the collapse was caused by humans and their hubris. We need to ensure that hubris doesn't blind us to the first rule of leadership: It's all about character.