

# Is Your Legal Team On A Collision Course With GAAP?

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It seems as though the accounting rules that just a few short years ago seemed to be carved in stone and generally accepted by almost all businesses, are now more like accounting questions that are subject to ongoing challenge, discussion and debate. It also appears that rules governing the once sacrosanct relationships between corporate counsel and senior-level corporate executives are also now open to ongoing discussion.

These new rules, established under the Sarbanes-Oxley Act of 2002 and enforced by the Securities and Exchange Commission, require both in-house and outside lawyers who see evidence of any "material" wrong-doing in businesses to report it up the corporate ladder. This rule is causing quite a stir in the executive ranks, where all business-related discussions between corporate executives and corporate counsel were previously considered protected under the attorney-client privilege.

Senior-level executives, who were once comfortable discussing sensitive legal matters and tough business decisions with corporate counsel, aren't quite as conversational anymore. These now tight-lipped corporate executives feel that frank and open discussions with their corporate counsel may not be in their best interest, and at some point could be used against them in a court of law. The fear of being dragged into court, or worse, being dragged in front of their Board of Directors, has many of them taking a vow of silence.

The Securities and Exchange Commission meanwhile, contends that there's no need for concern over issues of attorney-client privilege between senior executives and corporate counsel, because the privilege never existed. The SEC's position is that corporate counsel works for the corporation and shareholders, not the senior-level managers.

Former SEC chairman Harvey L. Pitt left no doubt as to where corporate lawyers should pledge their allegiance. "Lawyers for public companies represent the company as a whole and its shareholder-owners, not the managers who hire and fire them." This tidbit of information comes as breaking news to many senior executives who for years have openly discussed sensitive legal matters acting under the belief that they were protected by the attorney-client privilege.

I'm sure that most corporate attorneys wouldn't argue against the idea of protecting shareholder interest. It's just that by placing attorneys in the role of corporate whistleblower, the SEC has created an adverse relationship between corporate counsel and the senior-level executives they're hired to represent and advise.

In addition to making waves in the corporate boardrooms, these new rules of attorney-client conduct also seem to directly challenge state's rights governing attorney-client conduct. Some argue that Sarbanes-Oxley and the SEC have overstepped their bounds in an overzealous attempt to regulate business conduct, and in the process have taken regulation of corporations and their corporate counsel away from the states and turned it over to the federal government.

That question is still open to debate, and will be for quite some time. But what is known, however, is that in the new Sarbanes-Oxley world, accounting rules and regulations are subject to change and should be considered an ongoing work in progress.

You can expect new and revised rules to keep showing up every month or so at the federal, state and local levels, and while the SEC appears willing to consider some minor changes to existing regulations, possibly scaling back rules affecting smaller companies, don't expect any sweeping changes.

And with the new rules being added and existing rules being revised, expect both legal spend and accounting costs to continue to soar for many years to come. Richard A. Hall is founder and President/CEO of LexTech, Inc., a legal information consulting company. Mr. Hall has a unique breadth of experience which has enabled him to meld technology and sophisticated statistical analysis to produce a technology driven analytical model of the practice of law.

As a busy civil trial attorney, he was responsible for the design and implementation of a LAN based litigation database and fully automated document production system for a mid-sized civil defense firm. He developed a task based billing model built on extensive statistical analysis of hundreds of litigated civil matters. In 1994, Mr. Hall invented linguistic modeling software which automatically reads, applies budget codes, budget codes and analyzes legal bill content. He also served as California Director and lecturer for a nationwide bar review. Mr. Hall continues to practice law and perform pro bono services for several Northern California judicial districts.