

GETTING (TOO) COMFORTABLE: IN-HOUSE LAWYERS, ENTERPRISE RISK, AND THE FINANCIAL CRISIS

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In-house lawyers are now a principal focus of attention in the study of the legal profession. So it is appropriate in the aftermath of the global financial crisis to inquire about lawyers' perception of, and complicity in, such wrongdoing as may have occurred. This Essay describes the perceptual biases that may distort judgment notwithstanding proximity, including failures of expertise and excessive deference, difficulties in seeing change, and motivated inference. It ends by setting forth a research agenda for the study of how in-house lawyers "get comfortable"—or not—with client demands.

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INTRODUCTION

When lawyers speak, they sometimes use “get comfortable” to describe the thought process by which they conclude that what the client wants to do is permissible—that is, does not generate unacceptable legal risk. The phrase is both fascinating and evocative as a matter of social cognition. The reference to “comfort” aptly captures the point that most decisions we make are driven by intuition and feelings as much (or more) than explicit deductive or inductive reasoning. Metaphorically, our gut and our brain make choices together. The reference to process signaled by the word “get” further suggests that there is a motivational goal being pursued, a preference in favor of the client’s stated intentions to which the lawyer’s mind is trying to work its way.

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There is obvious danger here. Psychologically, a large cluster of behavioral traits works to enable people to see what they want to see, and feel as “right” that which they are motivated to prefer, objective evidence notwithstanding.¹ These traits involve both social-cultural processes and cognitive ones, and can be intensified in cohesive groups and organizations.² As a result, the process of “getting comfortable” may too readily become a process of collective rationalization. If so, one value that lawyers are supposed to bring to the client interaction—objectivity (or as I have termed it elsewhere, “cognitive independence”)—is predictably diminished.

In theory, at least, the externalization of the provision of legal advice in the business enterprise setting, relying heavily on lawyers from outside law firms, is supposed to counteract this tendency.³ Outside lawyers presumably have many different clients and hence less need to engage in a strategy of acquiescence. That might suggest that the striking rise of the in-house counsel in size and power (i.e., the internalization of legal authority and resources) over the last few decades might be troubling in terms of the objectivity of legal advice,⁴

1. The psychological literature on professional judgment is extensive, and my Essay will not attempt to be anything more than illustrative in its citations. For a recent survey of the pitfalls of biased professional judgment in business settings, with useful references to the psychological literature, see MAX H. BAZERMAN & ANN E. TENBRUNSEL, *BLIND SPOTS: WHY WE FAIL TO DO WHAT'S RIGHT AND WHAT TO DO ABOUT IT* (2011). For lawyers, a good resource is PAUL BREST & LINDA HAMILTON KRIEGER, *PROBLEM SOLVING, DECISION MAKING, AND PROFESSIONAL JUDGMENT: A GUIDE FOR LAWYERS AND POLICYMAKERS* (2010).

2. See Donald C. Langevoort, *The Epistemology of Corporate-Securities Lawyering: Beliefs, Biases and Organizational Behavior*, 63 *BROOK. L. REV.* 629 (1997); Milton C. Regan, Jr., *Moral Intuitions and Organizational Culture*, 51 *ST. LOUIS U. L.J.* 941 (2007).

3. See generally Richard W. Painter, *The Moral Interdependence of Corporate Lawyers and their Clients*, 67 *S. CAL. L. REV.* 507 (1994).

4. This has been well documented by many in the legal profession and professional responsibility literature. *E.g.*, Mary C. Daly, *The Cultural, Ethical and Legal Challenges in Lawyering for a Global Organization: The Role of the General Counsel*, 46 *EMORY L.J.* 1057 (1997); Robert Eli Rosen, “*We’re All Consultants Now*”: *How Change in Client Organizational Strategies Influences Change in the Organization of Corporate Legal Services*, 44 *ARIZ. L. REV.* 637 (2002); David B. Wilkins, *Team of Rivals? Toward a New Model of the Corporate Attorney/Client Relationship*, in 62 *CURRENT LEGAL PROBLEMS* 2009, at 478 (Colm O’Cinneide ed., 2010). On the functionality of this shift, see Omari Scott Simmons & James D. Dinnage, *Innkeepers: A Unifying Theory of the In-House Counsel Role*, 41 *SETON HALL L. REV.* 77 (2011), and Steven L. Schwarcz, *To Make or to Buy: In-House Lawyering and Value Creation*, 33 *J. CORP. L.* 497 (2008).

and indeed there is a sizable body of legal scholarship in professional responsibility raising precisely this concern.⁵

I would rather not make too much of the distinction between in-house and outside counsel, however. Competitive shifts in the marketplace for legal services have made outside counsel acutely sensitive to client preferences,⁶ so that threats to cognitive independence readily cross the inside-outside divide. Indeed, within the hypercompetitive world of high-end business work done by outside lawyers, I sense that many outside lawyers are seeking to channel the values, language, habits, and mindset of in-house counsel elites in order to become synchronous with their preferences.⁷ The norms and language associated with in-house lawyering thus seem to be diffusing into private practice, a reversal of direction from a couple of decades ago.

If that is the case, it simply underscores that studying the in-house world today is central to the study of professional responsibility more generally. How in-house lawyers “get comfortable,” or not, with strategic business decisions and practices in their companies is the particular question that concerns me here, and it is a timely one.⁸ The recent financial crisis poses some more of the “Where were the lawyers?” questions first asked after the post-Watergate corporate bribery scandals, then again in the savings and loan debacle,⁹ and yet again in the aftermath of Enron, Worldcom, and the financial accounting debacles earlier in the last decade.¹⁰ Inside the financial services firms that dominated the processes by which subprime debt was originated, securitized, derivatized, and sold off, in-house legal and compliance departments were large and visible, run by well-known (and often very distinguished) general counsel.

5. See, e.g., Sung Hui Kim, *Gatekeepers Inside Out*, 21 GEO. J. LEGAL ETHICS 411 (2008). From the sociology literature, see Sally Gunz & Hugh Gunz, *Ethical Decision Making and the Employed Lawyer*, 81 J. BUS. ETHICS 927 (2008).

6. Ronald Gilson's classic work explores this competitive pressure. Ronald J. Gilson, *The Devolution of the Legal Profession: A Demand Side Perspective*, 49 MD. L. REV. 869 (1990). For a more recent work, see Marc Galanter & William Henderson, *The Elastic Tournament: A Second Transformation of the Big Law Firm*, 60 STAN. L. REV. 1867 (2008).

7. For some evidence of this, see Rosen, *supra* note 4, at 671.

8. See Christine E. Parker et al., *The Two Faces of Lawyers: Professional Ethics and Business Compliance with Regulation*, 22 GEO. J. LEGAL ETHICS 201, 202–07 (2009).

9. For my contribution, emphasizing the psychological issues, see Donald C. Langevoort, *Where Were the Lawyers?: A Behavioral Inquiry into Lawyers' Responsibility for Clients' Fraud*, 46 VAND. L. REV. 75 (1993).

10. See, e.g., Milton C. Regan, Jr., *Teaching Enron*, 74 FORDHAM L. REV. 1139 (2005).

We must tread carefully here, to be sure. For all the inquiries, scholarly and political, into the causes of the financial meltdown, there is still no consensus on the extent of the legal wrongdoing associated with the subprime-driven bubble.¹¹ As I recently noted in another paper, there are three distinct sets of explanations for the behavior of the financial intermediaries in the events leading up to the crisis.¹² The first is that sophisticated financial actors on both the sell and buy sides were aware of the risk embedded in the various portfolios and derivatives but chose to transact anyway because of short-term incentives to do so, a manifestation of agency costs and moral hazard.¹³ The second is a variant: sophisticated actors were aware, but the buy side was not, so that the sales process involved deliberate opportunism, and maybe fraud.¹⁴ The third is very different: that there was a systematic under-appreciation of the risk on both the sell and buy sides. Each of these types of explanations generates a different evaluation as to possible wrongdoing, especially intentional wrongdoing.¹⁵ Parsing through these explanations is very hard, particularly in hindsight, wherein innocent explanations seem so implausible and the desire to find someone to blame so strong.

My Essay here is not the place to attempt any such parsing. At this point, I am still agnostic about the extent to which lawyers (or even their clients) were at fault in any of the events leading to the crisis, at least on the corporate/securities matters with which I am most familiar.¹⁶ What I want to do, however, is explain why psychologists would argue that the third explanation—lack of contemporaneous appreciation and awareness on the part of lawyers and others working on the inside—is more plausible than one might think.¹⁷ To the extent that the lawyers were indeed privy enough to the inner workings of their organizations and yet blinded to objective reality, this would be a

11. For a good exploration of the many issues, focusing mainly on outside lawyers capacity for intervention, see Steven L. Schwarcz, *The Role of Lawyers in the Global Financial Crisis*, 24 AUST. J. CORP. L. 214 (2010).

12. Donald C. Langevoort, *Chasing the Greased Pig Down Wall Street: A Gatekeeper's Guide to the Psychology, Culture and Ethics of Financial Risk Taking*, 96 CORNELL L. REV. 1209 (2011).

13. *Id.* at 1210.

14. *Id.* at 1210–11.

15. *Id.* at 1211.

16. There has been substantial reporting about the role of in-house lawyers in certain aspects of legal compliance at such firms as Bank of America, Countrywide, and Lehman Brothers. Obviously, each of these instances is highly fact-intensive in terms of who, what, when, and how the relevant legal advice was sought.

17. See Geoffrey P. Miller & Gerald Rosenfeld, *Intellectual Hazard: How Conceptual Biases in Complex Organizations Contributed to the Crisis of 2008*, 33 HARV. J.L. & PUB. POL'Y 807 (2010).

manifestation of our “getting too comfortable” concern: cognitive co-dependency rather than professional independence. Of course we cannot assume that the in-house lawyers were privy to what was happening internally and its significance in terms of enterprise or compliance risk. Some level of complexity is beyond the capacity of even the smartest, most motivated lawyer to grasp, and even with respect to more comprehensible facts, some in-house legal staffs are marginalized or walled-off from sensitive portions of the business and so lack fair opportunity to sense danger. But I will assume that in some cases, some of the time, in-house lawyers have a chance to understand looming business risks.¹⁸ This Essay is about those situations.

I have written much about cognitive bias inside business organizations, and so much of what follows is derived from this prior work. But I have not yet tried to connect this specifically to in-house lawyers, and so that will be my main effort here. I also want to try to be constructive, rather than simply lament the risk of co-dependency. So, I will include some lessons from psychology on ways to promote greater mindfulness in business settings, though without suggesting that there are any easy cures. All of this is in the spirit of extending the research agenda for work on in-house lawyering. Conceivably, the very best in-house lawyers recognize these risks, and in the field there are initiatives—internal organization and procedures, selection of personnel, training, etc.—that are sensitive to them. If so, discovering variations in how in-house legal staffs organize themselves and conduct their activities in order to find greater objectivity in the internal perception of enterprise and compliance risks would be very helpful.¹⁹ This Essay offers a rough sketch for such a study.

I. LAW, ETHICS, AND COMPLIANCE—COMMONALITIES AND DISTINCTIONS

Before judging the work of the in-house counsel, an important organizational point deserves consideration. Business organizations have a great deal of freedom to choose their internal structures, and there is substantial variation as to the location of responsibilities

18. On the difficulties of assigning blame to lawyers in a setting of informational diffusion that encourages “plausible deniability,” see William H. Simon, *Wrongs of Ignorance and Ambiguity: Lawyer Responsibility for Collective Misconduct*, 22 YALE J. ON REG. 1, 5–6 (2005).

19. See, e.g., Robert Eli Rosen, *Problem-Setting and Serving the Organizational Client: Legal Diagnosis and Professional Independence*, 56 U. MIAMI L. REV. 179 (2001).

relating to law, ethics, compliance, and risk management.²⁰ Some of the lawyering literature assumes that law and compliance go hand in hand, so that compliance issues are naturally under the direction of the General Counsel or Chief Legal Officer (CLO). In turn, this same literature often claims that the lawyering-compliance role situates the CLO and staff as a guardian of corporate integrity, the “conscience of the corporation” or some variant thereof, so that the legal role takes on ethical responsibilities as well.²¹ This is undeniable with respect to small- and medium-size firms, but it is interesting to note that for larger organizations there is a robust debate among compliance professionals as to whether the CLO should be walled off from too much influence over the corporate compliance and ethics function. Many firms now have chief ethics and compliance officers (CECO) with separate staffs, who may utilize in-house counsel for advice (and perhaps have specialized lawyers of their own), but who report directly to the CEO and may well have “dotted line” reporting responsibilities to the board of directors or a committee of the board—not through the CLO. The argument is sometimes made that the CECO should *not* be a lawyer (or at least not be the CLO) and that we should treat the role as entirely distinct from the function of the in-house lawyer.²² Before we assess the psychology of how lawyers might act as the conscience of the corporation, we should consider this debate more carefully.

To an outside observer, there is a strong scent of professional competition here. The fast-developing compliance industry seeks both status and autonomy in the corporate world,²³ which requires a separation from control by the legal profession; conversely, precisely because there is no clear conceptual distinction between legal advice and compliance oversight, CLOs will naturally resist the threat to both authority and resources.

My sense, however, is that there is more to the debate than just professional in-fighting, and goes to the capacity of in-house lawyers to bolster the corporate conscience. To be sure, lawyers vary in this

20. See Tanina Rostain, *General Counsel in the Age of Compliance: Preliminary Findings and New Research Questions*, 21 GEO. J. LEGAL ETHICS 465, 470–84 (2008). On the broadening of the field of “enterprise risk management,” see Michelle M. Harner, *Barriers to Effective Risk Management*, 40 SETON HALL L. REV. 1323 (2010).

21. See Ben W. Heineman, Jr., *Caught in the Middle*, CORP. COUNS. (Apr. 1, 2007), <http://www.law.com/jsp/cc/PubArticleCC.jsp?id=900005476298>.

22. There are, of course, other reasons than this to separate, including giving the in-house lawyers the ability to investigate compliance-related issues without the conflict that comes from also bearing responsibility for the compliance function.

23. See, e.g., Tanina Rostain, *The Emergence of “Law Consultants”*, 75 FORDHAM L. REV. 1397 (2006). But see Christine Parker, *The Ethics of Advising on Regulatory Compliance: Autonomy or Interdependence*, 28 J. BUS. ETHICS 339 (2000).

capacity, and no doubt some will be exemplary ethicists. But there is a strong strand in the organizational behavior literature (admittedly, a field dominated by non-lawyer academics) that something in the training, socialization, and professional identity of the lawyer interferes with the ability to generate an ethical corporate culture.²⁴ Some explain this by reference to lawyers' obsession with lawfulness, which crowds out non-legal influences on decision-making. As one commentator has put it:

Ironically, the prevalent practice of having legal counsel advise the board on "compliance and ethics" may tend to present an excessively legalistic approach to the topic, which can obscure other relevant considerations such as, for example, the cultural influences that impact employee behaviors or the nuances that distinguish between a "paper program" . . . and one that actually drives desired behavior in a meaningful way.²⁵

When the law is indeterminate, as it so often is (something lawyers are trained early-on to spot), the ability to "get comfortable" grows simply by finding enough argumentative space. The lawyer's work is then done. Lawyers' power comes from the ability to control legal interpretation, and so many tend to obsess on that alone.

A separate argument has to do with personality. In many organizations, senior lawyers seem to be chosen because they exemplify the characteristics and traits associated with zealous and aggressive promotion of the company's best interests, as those interests are construed by its board and CEO. Words like intensity, drive, and loyalty come to mind, maybe even a mean streak deployed against anyone who gets in the way of the corporate mission.²⁶ If those are

24. See Linda Klebe Treviño et al., *Managing Ethics and Legal Compliance: What Works and What Hurts*, 41 CAL. MGT. REV. 131, 146 (1999) ("[Lawyers'] education and background best prepare them to develop a legal compliance approach, not a values approach.").

25. John P. Hansen, Corporate Counsel Perspective: The Crisis of Ethics and the Need for a Compliance-Savvy Board, Remarks at the Rand Center for Corporate Ethics and Governance Conference (May 12, 2000), in CONFERENCE PROCEEDINGS: DIRECTORS AS GUARDIANS OF COMPLIANCE AND ETHICS WITHIN THE CORPORATE CITADEL: WHAT THE POLICY COMMUNITY SHOULD KNOW 41, 44, available at http://www.rand.org/content/dam/rand/pubs/conf_proceedings/2010/RAND_CF277.pdf.

26. On the variations in lawyer personality types and their relation to leadership in an organization or team, see DEBORAH L. RHODE & AMANDA K. PACKEL, LEADERSHIP: LAW, POLICY, AND MANAGEMENT 41-56 (2011); see also 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 (1998); Susan Daicoff,

traits associated with the CLO or general counsel, one can see why someone else should probably be given charge of ethics.

Of course, an organization that wants an attack dog for a general counsel is probably not going to generate a strong ethical culture in any event—the generalized tone at the top is likely to prize those same traits, so that ethics and compliance becomes just so much window dressing.²⁷ Here the debate over the proper structuring of ethics and compliance responsibilities blends into the bigger picture of corporate governance: the compliance profession insists on the need for independent directors to play a role in protecting the autonomy and resources of the CEO from threats by other managers, including the general counsel. While the role of independent directors generally can be contested in terms of predictably generating shareholder value, there is some support for the notion that truly independent directors have a stronger legal compliance orientation than those with close ties to the senior executives. When well chosen,²⁸ they are more closely attuned to other elites (in government, the media, etc.) who expect the company to satisfy standards of social legitimacy. This really is a political struggle for the heart, mind, and soul of the company, as are so many of the contemporary debates about corporate governance.²⁹

My point in raising this is not to try to resolve the question of whether “legal” and “ethics/compliance” should be separated in an organization. Plainly, the right outcome depends on the particular firm’s history, incentives, and culture—particularly what its ethical/compliance history has been and what the perceived role of in-house counsel was in those events. In any event, one unfortunate risk of separation bears note: to the extent that compliance and ethics are formally removed from the in-house legal function, the implicit message to the lawyers may be that ethics is not their turf, which simply reinforces the tendency to obsess on legality.

Lawyer, Know Thyself: A Review of Empirical Research on Attorney Attributes Bearing on Professionalism, 46 AM. U. L. REV. 1337 (1997).

27. See Kimberly D. Krawiec, *Cosmetic Compliance and the Failure of Negotiated Governance*, 81 WASH. U. L.Q. 487 (2003).

28. On the association between legally-trained directors and more conservative financial reporting, see Jayanthi Krishnan et al., *Legal Expertise on Corporate Audit Committees and Financial Reporting Quality*, 86 ACCT. REV. 2099 (2011). There is, of course, no reason to assume that outside directors will be chosen for any quality relating to either shareholder value or social legitimacy; the case for agency cost explanations for director selection in many corporations is still strong. For a warning against over-reliance on independent directors, see Usha Rodrigues, *The Fetishization of Independence*, 33 J. CORP. L. 447 (2008).

29. See, e.g., William W. Bratton & Michael L. Wachter, *The Case against Shareholder Empowerment*, 158 U. PA. L. REV. 653 (2010).

Rather, the more subtle point to consider here takes us to a crucial issue in the study of in-house counsel. *Who* gains power in-house, *how*, and *why*? This really is a matter of career patterns, which may be quite different in large business organizations as compared to the more usual place where this question is posed, law firms. As in-house staffs become larger and more complex, and the rewards for ascending to the top considerable, we should ask about the kinds of persons who likely succeed in the promotion “tournament” (i.e., the kinds of selection biases that favor some kinds of lawyers and disfavor others in the race to the top).

We can illustrate this by the following example, which takes us to the events leading to the financial crisis. Assume you have a large financial services firm heavily involved in financial innovation (i.e., the development and marketing of new products like complex securitizations and derivatives for the institutional and high-end retail marketplace). The pace of innovation is fast, so that novel legal/compliance questions are generated regularly, and competition among rivals (and among units within firms) is intense. Assume further that the legal issues are clearly identifiable but have no determinate answers—it’s often a matter of judgment and hence tolerance for some legal risk.

Three lawyers—*A*, *B*, and *C*—have the ability to say yes or no to a particular innovative strategy. *A* is a risk preferrer adept at “getting comfortable” with the chosen strategy, *B* is a risk hater more inclined to say no, and *C* is indecisive, a habitual worrier. Over a large number of iterations, who does best?³⁰ If we assume that legal outcomes are generated evenly (that is, the legal system will offer an answer that either rewards or punishes, with no bias in either direction) the process will favor the lucky risk-taker, the person who says yes and happens to hit a good streak of positive feedback. That may well be *A*.

Of course, the luck could turn bad, and *A* will suffer. But if we are thinking in terms of a sizable number of decisions made by a sizable number of persons, even a random distribution of good and bad legal luck will generate a “tail” of fortunate risk-takers in the bell curve of outcomes. To the extent that these lawyers are judged by the profitability of their clients’ strategies, they will look very good and be

30. For a similar model of executive promotion, see Anand M. Goel & Anjan V. Thakor, *Overconfidence, CEO Selection, and Corporate Governance*, 63 J. FIN. 2737 (2008). The “types” described here are not dissimilar to the “cops,” “counsel,” and “entrepreneurs” typology proposed by Nelson and Nielsen. Robert L. Nelson & Laura Beth Nielsen, *Cops, Counsel and Entrepreneurs: Constructing the Role of Inside Counsel in Large Corporations*, 34 LAW & SOC’Y REV. 457, 462–68 (2000). My additional point is that these roles may not simply be adopted, but reflect the personalities of the persons involved—with significant consequences.

sought after for future responsibilities—in other words, good in-house promotion material. At the same time, however, *B* or *C* might also look good as well if their hesitancy can be associated with identifiable situations where the conservatism led the client to avoid a loss, so we should not overstate lucky *A*'s competitive advantage.

It is thus an interesting question whether lucky risk-takers are prized more than prudent risk-avoiders who turn out to be right under conditions that evenly generate positive and negative legal feedback. I suspect so, but don't want to pursue that point because the assumption of an even mix of positive and negative feedback seems artificial. A variety of forces in our society lead to a general under-enforcement of the law, especially in business settings. Litigation is costly and difficult; public enforcement is under-funded. And lobbying by business organizations can "capture" the law or law-enforcers in such a way as to reduce the risk of negative feedback, perhaps considerably. If we introduce an under-enforcement bias in outcomes, *A*'s competitive advantage in the promotion tournament grows. Positive feedback to risk-taking is now more likely than negative, so that the risk-taker is rewarded more often.

In financial services, at least, there is a predictable cyclicity to under- and over-enforcement that allows us to generate even more interesting predictions.³¹ During runs of good economic performance (e.g., a strong stock market) the bias toward under-enforcement can become extreme. The commitment to public enforcement drops because of the positive returns being generated for a wide variety of stakeholders, and those returns also tend to hide a multitude of potential legal sins. The political lobbying power of the industry grows as well.

During good times, then, the *A*'s of this world thrive, and tend to crowd out the *B*'s and *C*'s. *A*'s get the promotions, and hence the power and status. And because their risk tolerance has been proven "right" by positive feedback, they tend to become evangelists for an entrepreneurial style of professional behavior on compliance matters that emphasizes flexibility: the willingness to "get comfortable" as an in-house virtue. Voices of conservatism are thereby silenced. The longer the run of good times, the more entrenched this overconfidence becomes. To state the almost self-evident, we went through an unusually lengthy period of time in financial services of nearly no serious legal or economic pushback to aggressive financial innovation.

31. See, e.g., Amatai Aviram, *Counter-Cyclical Enforcement of Corporate Law*, 25 YALE J. ON REG. 1, 11-14 (2008).

It is hard to imagine that entrepreneurial risk-preferrers did not gain immense power and prestige as in-house lawyers as a result.³²

My hypothesis about in-house counsel is that an above-average tolerance for legal risk and a “flexible” cognitive style in evaluating such risk are survival traits in settings where corporate strategy and its surrounding culture are strongly attuned to competitive success. In other words, those who rise to the top as CLO are more likely, on average, to display such traits. There is nothing necessarily about psychology here of course—an economist would observe that there is a positive expected return to such strategies, so that people will naturally choose to follow them. But I have long been convinced by those who argue that evolutionary fitness is strongest among those who come naturally to the perceptions and inferences that are commonly rewarded, and who do not have to exert scarce cognitive resources to formulating an unnatural strategy. If so, people whose psychological make-up inclines them toward risk and flexibility without the burdens of doubt will be the likely winners in the promotion tournament.³³

And that would not be particularly good news for either legal or business ethics, which brings us back for a moment to the “Where were the lawyers?” question. In settings like the ones just described, moral thinking tends at best toward the utilitarian, not deontological, and is fairly gut-driven. Certain kinds of people are so inclined. For instance, those who have higher levels of hormones that promote competitive drive and status-seeking³⁴ apparently exhibit more coldly utilitarian styles of ethical judgment (i.e., a willingness to harm others if they believe, accurately or not, that a greater good is being served).³⁵ When such people take charge of a legal compliance issue, it tends to be nothing more than a balancing of cognizable costs and benefits, though

32. For an elaboration of this story in the industry generally (as opposed to its lawyers), see Malcolm Gladwell, *Cocksure: Banks, Battles, and the Psychology of Overconfidence*, NEW YORKER, July 27, 2009, at 24.

33. See Goel & Thakor, *supra* note 30, at 2740; Langevoort, *supra* note 12, at 1219; cf. Eric Van Den Steen, *Rational Overoptimism (and Other Biases)*, 94 AM. ECON. REV. 1141 (2004) (discussing overoptimism as leading to a systematic bias). Similarly, firms that display such tendencies have an advantage vis-à-vis their competitors. See Donald C. Langevoort, *Organized Illusions: A Behavioral Theory of Why Corporations Misperceive Stock Market Investors (And Cause Other Social Harms)*, 146 U. PA. L. REV. 101 (1997).

34. See, e.g., Deepak Malhotra, *The Desire to Win: The Effects of Competitive Arousal on Motivation and Behavior*, 111 ORGANIZATIONAL BEHAV. & HUM. DECISION PROCESSES 139 (2010).

35. See Dana R. Carney & Malia F. Mason, *Decision Making and Testosterone: When the Ends Justify the Means*, 46 J. EXPERIMENTAL SOC. PSYCHOL. 668, 670 (2010).

perhaps rationalized to preserve self-image. Those are issues we will turn to in the next Parts of this Essay.

To summarize my argument thus far, the study of the role of in-house lawyers has to attend to the pathways by which lawyers gain power, status, and resources inside companies—a matter well studied among executives generally, less so with respect to in-house lawyers. I think there are traits associated with the likelihood of success along these pathways, which include cognitive flexibility in accommodating business imperatives and greater-than-average willingness to take calculated legal risks in light of the prevailing regulatory environment, which varies in the rewards and punishments it generates for legal risk-taking. Most importantly, if these inferences are right, then we ought to judge the ethical capacity of in-house lawyers by paying attention to who is most likely to succeed, and under what circumstances.

There are important limitations and conditions to my argument. First, I am assuming that both the company and lawyers inside it face robust competition. Where there is entrenchment instead, the pathways to success will differ, for better or worse. I have no doubt that there are companies where the legal and compliance roles take on a life of their own so that an institutional conservatism can take hold. After all, that may well be lawyers' inclination, all other things being equal.³⁶ But the evolution of our economy has introduced competitive pressure to a wider variety of companies, so that the trend is probably more in the direction of my hypothesis. Second, I am assuming an asymmetry in the rewards and punishments associated with legal risk-taking, which will vary both over time and within different economic environments. Where conservatism is consistently rewarded or aggressiveness punished often enough, my predictions as to who succeeds in-house will not hold.

Finally, I want to be careful not to suggest that this world of in-house survival differs categorically from the ecology faced by outside lawyers. In fact, I would argue the opposite: that the pathways to success in large law firms today similarly reward a great deal of cognitive flexibility and a taste for legal risk-taking, to a far greater extent than a decade or two ago. So I am by no means arguing that the ethical challenges and constraints that are faced in-house are by themselves a reason to reallocate the balance of professional power as between inside and outside lawyers.

36. See Donald C. Langevoort & Robert K. Rasmussen, *Skewing the Results: The Role of Lawyers in Transmitting Legal Rules*, 5 S. CAL. INTERDISC. L.J. 375 (1997).

II. WHAT LAWYERS PERCEIVE

Any argument that lawyers should have done more to intervene in the risky financial innovation of the last decade, based either on legal or ethical concerns, depends on the assumption that the lawyers saw enough as to what was going on to appreciate the problems. Legally, that could run the gamut of mental states from actual knowledge of illegality, reckless disregard, conscious indifference, or negligence—but still, something making the failure to intervene blameworthy. So far as law is concerned, many of the issues relate to disclosure: while risky behavior may not be unlawful per se, there are many kinds of disclosure obligations that require some warnings about that risk to other affected stakeholders (e.g., corporate disclosure under the securities laws).

In this Part I want to consider various reasons that lawyers might have missed seeing the problems until it was too late, if at all. Some are familiar (I have been writing about this subject for some time now), others less so. Inevitably, many readers are skeptical of accounts of cognitive blindness as they relate to possible wrongdoing, especially when there are pecuniary motives for complicity—greed stories of the sort that dominate public discussion of the financial crisis. Without doubting that there are many examples of deliberate wrongdoing that took place, we should be careful because we are judging in hindsight, where things always look clearer than they were at the time. An illustration from cognitive psychology underscores this vividly.³⁷ In a famous set of experiments involving some combination of basketballs, umbrellas, and a gorilla, subjects are told to focus intently on a challenging cognitive task while watching a video, such as counting the number of times the basketball is passed among people in the video who are wearing white shirts.³⁸ Once concentrating so heavily on this discrete task, most subjects will not even notice other fairly dramatic things going on in the video—like the presence of someone in a gorilla suit or a lady opening an umbrella—that anyone not engaged in the task would think was impossible to miss.³⁹ In many ways, our task here is to try to explain why so many in-house lawyers never saw any gorillas.⁴⁰

37. See Daniel J. Simons & Christopher F. Chabris, *Gorillas in Our Midst: Sustained Inattention Blindness for Dynamic Events*, 28 PERCEPTION 1059 (1999); see also BAZERMAN & TENBRUNSEL, *supra* note 1.

38. Simons & Chabris, *supra* note 37, at 1066.

39. *Id.* at 1066, 1069–70.

40. For a more general discussion of these kinds of challenges, see David De Cremer et al., *Regulating Ethical Failures: Insights from Psychology*, 95 J. BUS. ETHICS 1 (2010).

Of course, there may not have been any gorillas at all from the vantage point of lawyers engaged narrowly in discrete legal tasks touching on financial risk. Again, I'm focusing on the subset of cases where lawyers were indeed close enough to the problems. Here, as Steven Schwarcz has argued, there are legal tasks that plainly call for deep involvement, and lawyers who are well-trained enough to at least be expected to call into question the realism of "worst case scenarios" and other assumptions embedded in the firm's business model.⁴¹ There are times and places where in-house lawyers could see gorillas in the distance if they look carefully enough and ask the right questions.

A. Failures of Expertise and Excessive Deference

The legal rules with which in-house counsel struggle are varied, of course. Some are quite familiar and intuitive to the well-trained lawyer and readily routinized. But in many situations—especially in financial services—the lines separating law, accounting, business, and finance blur in ways that pose vexing challenges to the lawyer. The most obvious illustration here relates to financial risk management, both in terms of prudential regulation (rules restricting risk-taking) and disclosure regulation (disclosure of whatever level of risk was assumed). Assessing and describing the level of risk embedded in the firm's portfolio of assets and liabilities is immensely challenging, involving the aggregation of a vast store of information and the application of skills in quantitative analysis well beyond the capacity of any non-expert—and as we learned painfully enough, maybe even beyond the capacity of the experts as well.⁴²

For both the psychology and sociology of in-house lawyering, this is a central challenge. How do lawyers *learn* inside an organization, when application of their legal skills depends on highly subjective factual inference on which they have no deep knowledge of their own? The obvious intuition is that they seek out those who are more expert and/or better situated and try to gain insight through them. This takes us to two familiar problems in organizational behavior.

The first is that oftentimes the information necessary for accurate legal analysis is diffused throughout the organization, so that no one has a sufficient knowledge base. This really is a management information system or internal controls problem, and it can be caused by any number of factors—political factionalization inside the company that

41. See Schwarcz, *supra* note 11, at 4.

42. See Miller & Rosenfeld, *supra* note 14, at 809–10; see also Erik F. Gerding, *Code, Crash, and Open Source: The Outsourcing of Financial Regulation to Risk Models and the Global Financial Crisis*, 84 WASH. L. REV. 127, 129–135 (2009).

discourages information sharing, or maybe just that the information is too complex to gather and process at reasonable cost.⁴³ The Sarbanes-Oxley Act and various other interventions relating to internal controls try to address these problems by imposing greater responsibilities for diligent information gathering by managers and boards of directors, but the recent crisis amply shows how much room remains for improvement. This is largely an issue above the typical general counsel's pay grade, though in-house lawyers probably should be more sensitive to the problem. Exacerbating this problem is the circularity of what psychologists describe as social proof: the tendency to rely heavily on the apparent perceptions of others when one lacks confidence in one's own perceptions. It is commonplace, I suspect, for in-house lawyers to assume greater knowledge of situations on the part of other business units and assume that if they are not worried, then the lawyers need not be either. But others in the organization may be doing the same thing: relying on other's lack of concern to justify their own. Problems thereby fall through the cracks. Apparently, for example, there was heavy reliance in many financial firms on so-called "value at risk" models for risk management, which involved highly sophisticated mathematical modeling generated by the so-called "quants."⁴⁴ These models generated impressive risk assessments, used in both compliance and disclosure. But their confidence was illusory—though heavily influential—because the quants saw their task as data-driven and so built their models around the best available data. But the data were not of long-enough duration to justify such confidence from a standpoint of regulatory obligations, a point that probably would have been largely inaccessible to any non-expert, including those in the legal and compliance departments.

The second problem arises when information is available to other business units, but they interpret it in a biased fashion. Here again, the risk is that if the lawyer simply derives his or her inferences from managers closer to the situation or more expert on the subject, those biases will taint the legal analysis. This is a subject on which I have written extensively, because it goes to the heart of why firms either ignore risk or disclose it poorly (two obvious legal problems, especially in securities law): there are natural and common perceptual biases in organizations that favor optimistic construal over anxiety.⁴⁵ To some

43. See Timothy F. Malloy, *Regulation, Compliance and the Firm*, 76 TEMP. L. REV. 451 (2003).

44. See Kenneth Bamberger, *Technologies of Compliance: Risk and Regulation in a Digital Age*, 88 TEX. L. REV. 669, 704–10 (2010); see also sources cited *supra* note 42 and accompanying text.

45. See Langevoort, *supra* note 12; Langevoort, *supra* note 33; Langevoort & Rasmussen, *supra* note 36; see also Catherine M. Schrand & Sarah L. C. Zechman,

extent, this is captured by the familiar term “groupthink,” the strong tendency to ignore concerns or risks that are inconsistent with a group’s preferred interpretation of the situation it faces. Optimistic construals are high-grade corporate “grease.” They facilitate motivation, cooperation, and trust, and thus—on average—facilitate internal behaviors that make the firm more competitive vis-à-vis its rivals. In other words, it is a survival trait. Firms that lose this capacity get mired in internal dissension and doubt, which deflates motivation, cooperation, and trust.

In-house lawyers cannot afford to internalize this kind of bias when they make compliance or disclosure judgments that depend on a high degree of perceptual accuracy. However, that is easier said than done, especially when the inferences are highly complicated and outside the lawyer’s expertise. My sense is that there are two pathologies here about which good lawyers need to worry. In deciding whose perceptions we can trust, people use quick and dirty heuristics (people we like, for example, are more influential than people we don’t like). Here, we rely on our gut more than our ability to reason.

In highly competitive organizations, I suspect that there is a strong inclination for everyone—including lawyers—to trust the leaders who best display the markers associated with loyalty and care. In other words, we are suspicious of those who seem too self-promoting or inclined to make others do the hard work. Conversely, we admire those who display intensity, passion, and commitment. The key point, on which I have elaborated at length elsewhere, is that this is a risky inference, and the cause of many judgmental mistakes. Intensity, passion, and commitment are associated with *unrealistic* situational construals, especially as they relate to risk. They suggest the presence of overconfidence, which is a positive trait in the corporate promotion tournament—and in greasing the corporate culture—but, once again, can be very dangerous when factored too readily into a compliance assessment. What lawyers and other gatekeepers need to learn, I argue, is how to see these appealingly benign traits as potential risk markers rather than as reasons to defer. That is neither easy (especially when those managers are also powerful), nor intuitive.

The other pathology was referred to earlier. In the face of ambiguity about the law as applied to factual complexity or a changing environment, the natural cognitive tendency is to employ a trial-and-error strategy: small steps that test the legal landscape, pulling back if there is negative feedback, but taking increasing steps forward if there is not. The problem, once again, is that negative legal feedback can be

highly cyclical, absent for sustained periods of time when victims are few (i.e., during economic bubbles) and regulators are captured or lulled into complacency. Without the wake-up associated with stark legal challenges, there is little for the lawyer to push back with, so that reliance on the heuristics of intensity, passion, and commitment is far less likely to be checked.

B. Perceiving Change

The famous gorilla/umbrella experiments mentioned earlier point to another kind of cognitive bias that, I suspect, can adversely affect the judgment of in-house lawyers. People are fairly adept at perceiving change when the cues are salient enough, but poor when change is slow and gradual. This is especially true when we are busy, cognitively engaged (if not overloaded) in tasks that employ scripts and schemas to make sense of situations that are largely continuous. The familiar reference here—perhaps untrue as a natural matter—is that frogs will jump out of hot water in which they are placed, but boil to death when put in warm water where the temperature is then gradually raised. Cognitive psychology is filled with references to various status quo biases, ways in which the mind anchors on an initial reference point and then refuses to adjust appropriately thereafter.⁴⁶

Some of this is purely perceptual, but it connects to phenomena like cognitive dissonance as well. Cognitive dissonance is the well-recognized tendency of the mind to interpret new information so as to maintain consistency with past choices, preserving the sense that those choices were justifiable rather than mistaken. In other words, once we voluntarily make a judgment about something—thereby committing ourselves to that view—we are motivated to see that as right and the mind will work to make it so, even if it involves ignoring or dismissing some inconvenient facts that might be troubling to someone without the prior commitment.

The world of lawyering, in-house especially, is marked by a high degree of both continuity and busyness. Lawyers have particular spheres and subjects of responsibility, and work to get done. When the initial encounter with a matter is benign—no red flags or serious warning signs—it becomes very easy to anchor on that perception, so that subsequent learning is biased toward confirming that “no worry” stance. The connection here to the story behind the financial crisis is worth emphasizing. Increased reliance on securitization and derivatives

46. *E.g.*, Francesca Gino & Max H. Bazerman, *When Misconduct Goes Unnoticed: The Acceptability of Gradual Erosion in Others' Unethical Behavior*, 45 J. EXPERIMENTAL SOC. PSYCHOL. 708, 717–18 (2009).

occurred very gradually from its starting point (roughly) in the 1990s. Both product innovation and the step up in effort to find product—more and more subprime loans, and eventually the acceptance of synthetic portfolios that obviated the need for real loans, thereby expanding the degree of leverage exponentially—occurred without particular breakpoints that required de novo legal analysis. (It didn't help that Congress and the regulators during this period tended to endorse prevailing practices through acquiescence or explicit deregulatory approval, as with the gradual demise of Glass-Steagall and the “leave it to the market” approach to over-the-counter derivatives).

What this meant was that any lawyer caught up in the intensely busy work of securitization would probably start, especially early on, with a schema that there was no particularly significant enterprise or legal risk associated with the innovations. Early on, the products were indeed fairly moderate in their approach to risk. Once that schema takes root, then very small innovations in deal structure and how assets are identified are measured against the assumption of permissibility, even as these innovations gradually aggregate into significant changes over time. *Put simply, these lawyers would never come upon a discrete point in time where what might have been appropriate before is palpably no longer appropriate.* To blow the whistle now on any common practice or pattern of innovation would raise troubling questions about the prior months or years when the lawyer acquiesced in what was happening. The mind fights such inference.

And here, the two kinds of psychological phenomena we have considered join together. As new lawyers come into the work to accommodate its increasing deal flow, they are likely to take their cues from the lawyers and business people already there, who are visibly untroubled, committed, and intense. Those cues invite conforming perceptions, a form of legal groupthink. Without the ammunition of critical feedback from regulators or courts, the commitment to the course of action hardens, and the ability to think afresh about the legal or enterprise risks diminishes.

C. Lawyers' Motivated Inference

The third psychological tendency that can lead in-house lawyers astray as sources of objective advice and counsel is motivated inference: we tend to see what we want to see.⁴⁷ A robust set of

47. See, e.g., David M. Bersoff, *Why Good People Sometimes Do Bad Things: Motivated Reasoning and Unethical Behavior*, 25 PERSONALITY & SOC. PSYCHOL. BULL. 28 (1999); Shaul Shalvi et al., *Justified Ethicality: Observing Desired*

experiments going back decades supports the intuition that a person who wants to come to a particular inference will, subconsciously, look for a way to do so. This research has been applied in depth to the study of accountants and auditors, finding that it does not take a conventional conflict of interest for accounting professionals—who supposedly prize objectivity just as lawyers do—to tend toward a genuine belief in the answer that favors their client, so long as the governing rules are subjective enough. So, too, with lawyers, at least in the litigation and negotiation contexts.

In recent work, Max Bazerman and various colleagues have described an interesting three-phase structure to this psychology.⁴⁸ Prior to a difficult ethical (or presumably legal) decision, most people genuinely intend to do the right thing. They hold themselves out to others, and seem themselves internally, as responsible actors—think, for instance, of lawyers active in bar associations and other public interest settings. But “fading” occurs in the second phase, when the hard choice is imminent. Here, choices are reframed in terms of the pressures immediately at hand, at best utilitarian and often corner-cutting. Finally, there is the restoration phase: the person re-imagines the decision in a way that rationalizes it with some (fairly plastic) conception of acceptable behavior, thereby allowing the person to return to the first position, the self-image of a good citizen.⁴⁹

The psychological motivator here is self-interest, which raises an important contextual question as applied to in-house lawyers. One can readily imagine some companies where the in-house lawyers are motivated *toward* conservatism (i.e., risk avoidance). Indeed, this is probably the natural inclination, because lawyers will be blamed for giving the go-ahead to a course of action later sanctioned, without necessarily gaining comparable credit for either giving a green light to the course of action that goes unchallenged or preventing a course of action that would be punished if undertaken.⁵⁰ But one of the noticeable developments in the practice of lawyering over the last decade or two has been corporate client sensitivity to lawyers’ natural conservatism bias and hence the deliberate effort to counteract it. The response is both political and cultural: the promotion of lawyers who exhibit a disdain of “nay-saying” and a willingness to work with business units to craft aggressive strategies at an acceptable level of legal risk (to the

Counterfactuals Modifies Ethical Perceptions and Behavior, 115 ORGANIZATIONAL BEHAV. & HUM. DECISION PROCESSES 181 (2011).

48. See BAZERMAN & TENBRUNSEL, *supra* note 1; Ann E. Tenbrunsel et al., *The Ethical Mirage: A Temporal Explanation as to Why We Are Not as Ethical as We Think We Are*, 30 RES. ORGANIZATIONAL BEHAV. 153 (2010).

49. BAZERMAN & TENBRUNSEL, *supra* note 1, at 66–76.

50. See source cited *supra* note 36 and accompanying text.

firm, not to the particular lawyer). In other words, lawyers who are adept at getting comfortable. No doubt this occurs initially at the level of the CLO, who will occupy that role only to the extent that the CEO finds him or her compatible in attitude toward risk and embrace of the challenges of doing business. Companies that do not manage this task well, and leave their lawyers too much freedom to lean against strategic aggressiveness will, on average, find themselves at a competitive disadvantage in intense product markets.

Precisely how this countering is done is an interesting behavioral question. “Tone at the top” from the CLO and his or her senior team plays a role, as does incentive compensation that couples attorney pay with the success of the company, as through options or employee ownership arrangements.⁵¹ But the most powerful effect is probably cultural, when the lawyers develop a sense of identity that is tied as much or more to their status as key employees as to their status as professional attorneys. This is a visceral process, generating the kind of loyalty that results from bonding experiences early on and, over time, being caught up in the competitive arousal and sense of corporate mission. It means bringing lawyers into the corporate team.

When this effort succeeds, the psychological consequences are significant. The in-group corporate identity provokes greater aggressiveness vis-à-vis whoever is considered the firm’s “opponents” (in-group/out-group rivalry).⁵² The most obvious rivals are the firm’s immediate competitors (e.g., J.P. Morgan versus Goldman Sachs), and lawyers will be drawn in by the visceral desire to help their firm win that competition. In financial services, one of the noticeable developments underlying the process of aggressive financial innovation was the banks’ disdain for any sense that they owed special fiduciary-like obligations to their institutional customers—a way of distancing themselves so as to rationalize hyper-competitive behavior toward the customers, too.⁵³ Lawyers baptized in that ideology would fail to see the repercussions of taking that stance a step too far—essentially, the legal posture in which so many financial firms have found themselves.

My sense, however, is that the most pernicious consequence of embracing the internal belief system has to do with the lawyers’ stance

51. John S. Dzienkowski & Robert J. Peroni, *The Decline in Lawyer Independence: Lawyer Equity Investments in Clients*, 81 TEX. L. REV. 405 (2002).

52. As ordinary observation suggests, the presence of a competitive threat makes it more likely that people will respond with “tit for tat” dishonesty, rationalizing it along familiar utilitarian lines. Pavel Atanasov & Jason Dana, *Leveling the Playing Field: Dishonesty in the Face of Threat*, 32 J. ECON. PSYCHOL. 809, 815–16 (2011); see Gavin J. Kilduff et al., *The Psychology of Rivalry: A Relationally Dependent Analysis of Competition*, 53 ACAD. MGT. J. 943 (2010).

53. See Langevoort, *supra* note 12, at 1216.

toward the law itself. Where the law itself is ambiguous, lawyers' intuition as to how far to let a client go in terms of aggressiveness is heavily influenced by a subjective evaluation of how legitimate the law's claim is. Where a loyalty to the corporate mission comes to color the lawyers' thinking, it becomes easy to start thinking of regulators and the courts as rivals—anachronistic, inexpert policy-makers who mindlessly burden entrepreneurial innovation. Once this kind of cynicism and disdain takes root, there is little to restrain the lawyers' encouragement of legal risk-taking except for their sense of the probability of detection and magnitude of possible sanction—which, as we have seen, can diminish for extended periods of time. I would venture a strong guess that in legal departments at some of the big financial services firms earlier in the last decade, the inside view as to the legitimacy and competence of financial regulation had eroded considerably, thereby enabling more aggressive motivated inference as to the law's minimal demands.

III. PUTTING THE STORY IN MOTION

To summarize, let me respond to the “Where were the lawyers?” question as it relates to the recent financial crisis, by offering the following stylized story based on all of the foregoing discussion:

The financial services firms that made up the emergent “shadow banking system” were in intense competition with each other to innovate and respond with asset-backed products and derivatives.⁵⁴ Early on, regulators showed a willingness to acquiesce in this innovation—whether voluntarily or under political pressure—in a way that signaled to the lawyers in these firms that the legal risks associated with these products were manageable. The lawyers quickly got comfortable with the general framework and approach. Even at this point, however, the product complexity was such that the lawyers had at best a simplistic knowledge—the better understanding lay elsewhere in the firm, and even there may have been fairly speculative. In any event, during this early phase the feedback was positive, and the lawyers reasonably developed a positive schema through which to view the legal risk analysis.

Over the next decade, the shadow banking system grew through rapid product innovation, but without any dramatic shifts or bumps that would prompt any rethinking of the initial schemas. The pace of work grew just as fast, giving anyone closely involved little time to think through the blur of a full pipeline of deals. And as this is happening,

54. See Charles K. Whitehead, *Reforming Financial Regulation*, 90 B.U. L. REV. 1, 16–36 (2010).

the competition among firms intensifies (as does profitability), producing an arousal that sharpens the desire to win and facilitates rationalization. As such, the developments that gradually lead to the destruction of the system—the reach for lower-quality subprime assets, the enhanced leveraging through incredibly complicated synthetic derivatives—are not well perceived as threats. All this is reinforced by social proof: as participants on both the buy side and sell side continue business as usual, with stable credit ratings as reference points, no one senses any cause for alarm. To the lawyers, I suspect, it took quite a while to shift out of the positive script. In other words, lawyers simply didn't notice that gorillas had come into the picture.

This is an immense generalization, of course. No doubt in various places there were alarms—at Lehman Brothers, for example, an entire business unit apparently concluded that the firm was heading toward disaster well before the collapse and made futile efforts to steer it away.⁵⁵ But I doubt lawyers—with their relative lack of financial expertise and lack of access to diffuse risk-related data—were particularly well positioned to appreciate the gradual changes taking place until it was too late. Nor was the law ever clear enough to allow them to push back effectively against the preferred interpretation of the business people even if they had become alarmed.

This temporal point is important. The message of the psychology we have been considering is not that people remain blind to disconfirming information once a schema is set. Rather, it is that we are slow to notice and change, especially in the face of cognitive complexity. The tragic dimension to this is that by the time reality starts to set in, our complicity is set as well—we *should* have known it sooner, and face blame in hindsight for not having done so—so that the impulse to cover up is strong. Moreover, setting things right is not easy. Imagine, for instance, a CLO who realizes too late that mistakes were made that may well (but not necessarily) involve legal wrongdoing, the consequences from which are continuing. There are two courses of action. One is to confess the truth, which by itself may send the company spiraling into insolvency and/or make it and its management the target of prosecution. The other is to cover up, hoping that the damage to the institution—including thousands of employees and their families, as well as current shareholders and other stakeholders—can be avoided by some fancy maneuvering or just blind luck. While the former may be the lawful course of action, I suspect that most people—especially those with intense loyalty toward the

55. See LAWRENCE G. McDONALD & PATRICK ROBINSON, A COLOSSAL FAILURE OF COMMON SENSE: THE INSIDE STORY OF THE COLLAPSE OF LEHMAN BROTHERS 124–30 (2009).

institution—would take the latter route and, in their gut, not feel all that guilty about it.

CONCLUSION—A RESEARCH AGENDA

To date, we lack the “smoking gun” evidence of extensive lawyer complicity with client fraud in the aftermath of the financial crisis comparable to what we had after the savings and loan scandal or Enron. Still, I suspect that some lawyers were close enough to those events that they could have functioned as gatekeepers if willing and able.⁵⁶ My account here—which I do not necessarily intend as either legally or morally exculpating—is simply to explain how one can be very close to a situation and not perceive what others, later on in hindsight, see as patently obvious.

The payoff from an exercise like this is to think more clearly about the challenges associated with being an in-house lawyer. The subject of in-house lawyering has attracted its share of high-quality legal scholarship in the last decade or two, but there is so much more worth examining. A series of projects deserve a place on the research agenda.

The first is to ask whether in-house lawyers consider the problem of biased inference—on the part of the company’s senior management, mainly, but also the lawyers’ own biases—something to worry about. To be sure, many aspects of the in-house lawyer’s work aren’t filtered through executive perceptions: whether a bribe was paid that violates the Foreign Corrupt Practices Act, for example, isn’t a matter of subjective judgment on which corporate managers have superior knowledge. But business risk perception is embedded in many legal problems, particularly under the securities and financial services laws. I have made the case for lawyers needing to overcome cognitive biases to do their work well, but it would not surprise me if many CLOs turn away from this risk rather than confront it.⁵⁷ To the extent that a biased (overly optimistic) view of the company’s state of affairs is deeply engrained and embraced throughout the organization, pushing back against it is politically risky, threatening the working relationship between the CEO and the CLO. This is especially so in times when evangelists for risky behavior have risen to power and may be particularly threatened by dissenting voices. It may be safer from a career perspective to drink the corporate Kool Aid along with everyone else, even if the legal work suffers as a result. How CLOs negotiate this territory—how much do they really want to know about enterprise and compliance risks, and how do they survey inner workings of the

56. See Schwarcz, *supra* note 11.

57. See Simon, *supra* note 18.

business in a politically savvy way—would have to be elicited with considerable sensitivity.

Second, to the extent that the in-house lawyers do take this risk seriously, how do they respond? It is possible, for example, that CLOs in firms with strong corporate governance structures and unfiltered access to independent directors can enlist their support to help de-bias the firms' official perceptions. Or there may be back door channels to independent auditors on financial reporting matters. Within the in-house legal department, it would be interesting to find out if there is attention to techniques suggested by organizational psychologists for addressing the risks of bias and groupthink.

The final two research questions reach more broadly. The third: what is the career progression by which someone becomes a CLO (or part of the senior legal team), and are there particular traits associated with making it to the top? Though discouraging to contemplate, it is quite possible that an adaptive survival instinct is the ability to get comfortable with risky courses of action—not to be so much of a worrier, even if worry is what the situation deserves. This is consistent with work on how executives are promoted, and it is not clear that lawyers are much different in terms of biases that foster success in the probationary crucibles of the promotion tournament. As we come to see CLOs as the ultimate elite of the legal profession, knowing more about how and why they got there becomes crucial.

Fourth, I find intriguing the simmering debate over whether lawyers (or at least the in-house legal department) should be disqualified from primary responsibility for ethics and compliance inside the company. Is this simply self-serving inference by the emerging ethics and compliance industry, as a way of promoting their own professional autonomy? Or is there something to the claim that lawyers predictably frustrate focus on ethics beyond minimal legal compliance? If there is something to it, then the research questions become more specific: is there something in the language, training, socialization, personality and/or professional identity of lawyers that has this effect? All this surely deserves a closer look by legal academics.

Finally, there is the relationship between inside and outside counsel. I suggested at the outset that once upon a time, inside lawyers seemed to regard outside counsel as the true elites and mimicked their language, habits, and norms with considerable envy. Today, for most outside corporate lawyers, the opposite has come to be so: CLOs have become the elites, and (putting aside certain specialty practices) outside lawyers envy the economic clout their clients have and are learning to speak, act, and think like them in order to appear completely and utterly responsive to their needs. Whether this is in fact so is worth

examining, and if it is, we might have to reorient our thinking about the professional lives of corporate lawyers.

The common thread in all these inquiries is what has come to dominate my thinking as the most compelling set of questions we face in business law: the role of hyper-competition in economic behavior.⁵⁸ The familiar forces of technology and globalization have made it increasingly likely that any form of slack, any lingering inefficiency, will be discovered and arbitrated away. This is palpably so for both lawyers and their corporate clients, in-house or otherwise. As a result, we have to ask hard questions about what traits—attitudinal, emotional, perceptual—have the most robust competitive fitness in terms of who succeeds as a corporate lawyer in this Darwinian professional world. We know the answer that we would like to be so: those with the integrity and detachment not only to give accurate calculations as to legal risk and the ways of managing it, but also to be a “conscience of the corporation.” But as academics we have to be careful to avoid our own motivated reasoning. If the traits that generate competitive success in seeking the outsized rewards in income, status, and power conferred on top in-house lawyers are different, maybe less inspiring ones—those associated with intense synchronicity with client preferences and an appetite for legal risk (i.e., being adept at getting comfortable—we had better learn precisely what they are and how they play out institutionally in the corporate world).

58. See Scott Rick & George Loewenstein, *Hypermotivation*, 45 J. MARKETING RES. 645, 645 (2008). For a similar point, see Donald C. Langevoort, *The Organizational Psychology of Hyper-Competition: Corporate Irresponsibility and the Lessons of Enron*, 70 GEO. WASH. L. REV. 968, 973–75 (2002); Langevoort, *supra* note 12, at 1228–31.

