Part II: Corporate Citizenship in Practice: The Role of the Attorney in Promoting Good Corporate Citizenship

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CORPORATE CITIZENSHIP IN PRACTICE: THE ROLE OF THE ATTORNEY IN PROMOTING GOOD CORPORATE CITIZENSHIP

Karl A. Groskaufmanis
Elliot I. Portnoy
Professor Andrea Schneider

Professor Andrea Schneider: Our second panel this morning focuses on the role of the attorney in promoting good corporate citizenship, and we are lucky enough to have illustrious attorneys who spend most of their day allegedly promoting good corporate citizenship. So, they're going to talk to us about that. Our first attorney is Karl Groskaufmanis, who is a partner in the Washington D.C. office of Fried Frank Harris Schriver & Jacobson. His securities practice includes SEC enforcement actions, civil and criminal litigation, and corporate counseling. Mr. Groskaufmanis serves as Chairman of the Practicing Law Institute's Advanced Securities Workshop. He also acts as co-chair of the ABA Business Law Section Ad-Hoc Committee on public companies' disclosure practices. Mr. Groskaufmanis is an author and co-author of numerous articles and a frequent speaker on corporate and securities law issues. He has appeared as a guest lecturer at the Wharton School of Business, University of Michigan Business School, and at Cardozo, Cornell, Georgetown, Harvard and Stanford Law Schools, and now at Marquette Law School. Mr. Groskaufmanis is an honors graduate of Cornell University and received his J.D. from University of Pennsylvania and an L.L.B. from the University of Toronto. He was named one of the forty top lawyers under 40 by Washingtonian Magazine. Our other attorney joining us this morning is Elliott Portnoy, who is a partner with the Washington D.C. firm of Arent Fox Kintner Plokin & Kahn. He represents the video game industry in efforts to develop and implement codes of conduct and rating systems for games with violent themes. For the last six years he has lobbied the U.S. Congress, the Executive branch, and state and local governments to block passage of content-restrictive legislation and to shape the video games industry's response to allegations that its products cause violent behavior by children. Mr. Portnoy is also the founder and coordinator of Kids Enjoy Exercise Now, KEEN Foundation, an innovative non-profit organization that provides free recreation opportunities to children with severe and profound disabilities. He's been recognized in
Time and was named the 1999 Washingtonian of the Year by the Washingtonian Magazine for his community service efforts. Mr. Portnoy is a graduate of Harvard Law School and Oxford University and a former Rhodes scholar. Professor Timothy Fort who was to join us this morning as our third panelist is not joining us due to a case of strep. As his role was to question our attorneys here, I will be serving that role with some questions based on the remarks he had prepared for today.

**Karl Groskaufmanis:** My topic today examines the receipt of common stock of public companies as payment for legal services. It is an ethical issue being confronted by a broad cross-section of counsel to public companies.

The idea that lawyers promote good corporate citizenship is not simply an academic concept. It is a central principle in the regulation of U.S. capital markets. These capital markets are governed to a great extent by two statutes that were adopted right at the beginning of the New Deal—the Securities Act of 1933\(^2\) and the Securities Exchange Act of 1934.\(^2\)

The primary securities statutes reflect a choice between two approaches that could be taken. The first approach might be a system by which a national regulator would decide when companies are ready to sell securities to the marketplace. The second approach would allow for the market to decide the merits of a security after the company provides full and frank disclosure about their securities.

The second model ultimately prevailed. A company does not need to be profitable to sell securities in the marketplace. It only has to tell investors that it is not profitable (and that disclosure may even warn that the company may never be profitable). Given that approach, ever since the New Deal, lawyers have played an important role in how securities markets function. In essence, the disclosure is crafted by lawyers both on the government side in terms of developing the disclosure standard and then on the private securities bar side in terms of developing the disclosures.

My presentation today breaks into three parts. First, I would like to create an empirical picture of what practices are common in the marketplace regarding stock for services. Second, we should consider

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what legal standards might be implicated. Finally, we should consider the guidelines that counsel might consider when accepting stock for fees.

Common stock has become an important currency in the economy. It is used to compensate executives. Stock also has served as an important currency for mergers and acquisitions. There is a great deal of news about stock for stock transactions. It is inevitable that stock was going to be used also to pay lawyers. Historically, lawyers have not been particularly anxious to take stock due to potential conflicts of interest. Nonetheless, law firms that represent public companies are confronting the issue of stock payment for services.

Looking at some empirical data, it is clear that there has been a shift. The *ABA Journal* recently examined the SEC filings of about 500 companies that issued their stock through initial public offerings in 1999.23 The survey found that one-third of the lawyers representing the company that was the issuer owned some stock in the company when it went public.24 Looking at it another way, lawyers representing either the company or the underwriter owned stock in 175 of these approximately 500 companies. Taking that subset, forty percent of the law firms disclosing interests in company stock had positions whose value exceeded $1 million when the company went public.

This has significant implications for lawyers in their role as gatekeepers for the capital markets. Picture yourself as a lawyer for a public company, and as a result of working on the IPO, your law firm has 100,000 shares. The shares are currently valued at forty dollars, so your law firm has a $4 million stake in this company. You get a call from the Chairman of the board's Audit Committee. He indicates that former accounting employees have contacted him and alleged that they accelerated improperly the recognition of revenue from a number of key contracts. The former employees claim they engaged in improper accounting practices at the direction of the company's Chief Financial Officer. The former employees claim that the CFO directed these improper practices so that the company could recognize sufficient revenue to meet marketplace expectations regarding the company's earnings.

The Audit Committee Chairman says he wants to retain independent counsel to investigate these allegations and report back to the Audit Committee. There is a separate question for you as the outside securities counsel to the company: Should the company disclose

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24. *Id.*
the existence of this internal inquiry to the marketplace?

This is a question of judgment and, often, there is no single clear answer. There is no SEC rule that mandates disclosure of this investigation. Indeed, the allegations may be the meritless claims of disgruntled former employees. Disclosure may be premature and, in many ways, could do a disservice to the company. Since this is not a clear cut question of law, an attorney must exercise a judgment about whether to recommend disclosure. In this instance, the attorney's law firm would be impacted by the advice. Even a hint that the company manipulated the accounting rules to meet earnings expectations would have a dramatic impact on the company's stock price. Suppose that disclosure would cause the company's forty dollar per share stock price to plummet to twenty dollars a share by the end of the next trading day. That would cost the firm $2 million. What is already a difficult judgment is made more difficult by the potential conflict of interest in rendering advice in this situation.

A number of ethical standards are relevant to this discussion. ABA Model Rule 1.5 requires an attorney's fee to be reasonable, and reasonableness depends on a number of factors. Ascertaining reasonableness can be difficult when a firm is taking stock as compensation. For example, VA Linux stock increased six-hundred ninety-eight percent on the first day of trading in 1999.27 At the end of that day, a 100,000 share position was worth $24 million.28 The concept of reasonableness must be reassessed when the currency being used to pay for legal services—common stock—can appreciate (or decline) dramatically.

Model Rule 1.7 deals with conflicts of interest and requires that a lawyer "refrain from representing a client when representation of that client may be limited by that client's own interests except if the lawyer reasonably believes that the representation will not be adversely affected, and if, after consultation, the client consents to representation under these circumstances." Lastly, Model Rule 1.8 requires that the lawyer not enter into a business transaction with a client, nor acquire an ownership interest adverse to the client, unless the transactions and

26. MODEL RULES OF PROF'L CONDUCT RULE 1.5.
28. Id.
29. MODEL RULES OF PROF'L CONDUCT RULE 1.7.
terms on which the lawyer acquires the interest are fair and reasonable for the client and are "fully disclosed and transmitted in writing in a matter which can be reasonably understood by the client." The client also must be given a reasonable opportunity to seek the advice of counsel independent to the transaction and needs to consent in writing.

There is little in terms of reported decisions that deal with the conflicts associated with the receipt of public company stock for fees by lawyers. For example, one decision that touches some of these issues is a 1994 Iowa Supreme Court opinion involving a lawyer named Humphreys. The lawyer failed to advise the client of a potential conflict of interest when he received stock in a privately held company. He failed to advise the client that he may have had a potentially adverse business interest that would affect his professional judgment. Humphreys also had four felony tax evasion convictions, and then he commingled client assets with his defense being that his mother was the bookkeeper and she was responsible. This case provides little direct guidance to counsel receiving stock compensation from publicly traded companies.

In assessing how counsel might address the potential conflicts, it is important to start with the principle that a lawyer is a fiduciary. If an engagement is ever challenged, the burden of proving its fairness and that it was reasonable will rest with the lawyer. It is also important to remember that the ABA's standing committee on professional responsibility issued an informal opinion in July 2000 which relates to acquiring ownership of a client in connection with performing legal services. From all of these sources, you can derive four principles that a lawyer should consider when accepting stock for fees.

First, the terms of the engagement should be explained in writing. The engagement letter affords the lawyer an opportunity to describe what services are being provided and what compensation is being paid. Even if such an engagement letter is not required by the lawyer's home jurisdiction, one should be prepared for engagements in which equity is received. The writing documents the reasonableness of the fee in the context in which the lawyer was retained (and provides that lawyer with

30. MODEL RULES OF PROFESSIONAL CONDUCT RULE 1.8.
32. Id. at 398-99.
33. Id. at 399.
34. Id. at 397-98.
35. ABA Formal Ethics Opinion No. 00-418 (July 2000).
a basis for defending the engagement if counsel has the good fortune to be retained by a stock market darling).

Second, looking at Rule 1.8 and its subsequent reinforcement in the July 2000 ABA opinion, a lawyer should advise the client that he may want to seek independent counsel to determine if the fee arrangements are reasonable. Practitioners need to take into account who the client is, and whether the consent they are seeking is truly informed. For example, representation of a company seeking to initiate an initial public offering may involve financially sophisticated individuals or a group of young managers with a novel concept. Attorneys should adjust their disclosure to the client with whom they are dealing.

Third, the lawyer should secure a written waiver from the client that acknowledges the terms of the stock component and the fact that the compensation could have an impact on the lawyer's ability to provide future services to the client. Coupled with that, the firm should receive acknowledgement from the client that, at some point the lawyer will be free to sell the company's stock. There may come a point in time where it may not be in the client's interest for the lawyer to sell its stock. The lawyer should address this point at the outset and secure the client agreement that the lawyer retains the ability to dispose of the securities paid for legal services.

Finally, the law firm must develop safeguards so that any transactions involving client stock do not involve the illegal use of material information received from the client. If the lawyer continues to serve as the company's lawyer, one approach may be to subject the law firm's transactions in the stock to the same restrictions that are imposed on the company's top insiders. If the company has a policy, as many companies do, that insiders can only trade in the period after quarterly results are announced, their lawyers may not want to be structuring their trading any differently. In a law firm setting, there may be an opportunity to delegate such trading decisions to colleagues who are not involved, on a day-to-day basis, in the representation of the client.

No one formula is an apt fit for every situation. The bottom line is that lawyers have the ability to structure the relationship with the client at the outset. When a law firm is taking stock for its fees, the retention agreement becomes critically important. Even if such letters are not required in the jurisdiction, it is critical that a good record be created reflecting the nature of the engagement.

Elliott I. Portnoy: Good morning. I am going to shift gears to a slightly different and perhaps more provocative topic depending on your perspective. Paducah, Kentucky; Conners, Georgia; Pearl, Mississippi;
Jonesboro, Arkansas. Littleton, Colorado... Kids killing kids. What do all of these horrible tragedies have in common? In the wake of each of them federal, state, and local legislators rushed to do what? Make it harder for kids to gain access to guns? Makes sense. But no. Hire more police officers, security guards to patrol our nation's public schools? No. Require metal detectors in public schools to keep guns out of the buildings? No. Hire more school psychologists, mental health professionals and school nurses to help identify and intervene with troubled students? No. What Congress, over a dozen states, and hundreds, of local communities did do or have looked at doing in the wake of school violence is this: attempt to ban or otherwise restrict access by kids to video games with violent themes. That, in essence, is the landscape in which a team of lawyers that I direct at my law firm have worked almost non-stop for six years on behalf of the coin-operated side of the video game industry.

This morning what I'd like to do is talk a little bit about the role that lawyers play in helping an industry that has been demonized in the media and vilified by elected officials of all stripes and from all parties as the industry attempts to articulate and then pursue a sense of corporate responsibility. This may be one of the first times this audience has heard "corporate responsibility" and "video game industry" within the same sentence. Indeed, as demonstrated by the events of just this week alone, this issue could not possibly be more timely or less abstract.

Karl had indicated that in a law school setting, a hypothetical was often desired and I wish that this was hypothetical. In fact, this could not possibly be less hypothetical in terms of the way it's playing out on a daily basis. On Monday of this week, the Federal Trade Commission released a report that was a year in the making that examined the business, marketing, and advertising practices of the entire entertainment industry other than television: the video game, movie, and recording industries. The report found that most sectors of the entertainment industry deliberately, aggressively, and pervasively advertise and market games that are rated for adult audiences directly to children. Wednesday, Senator John McCain, failed presidential candidate and chairman of the U.S. Senate Commerce Committee, convened a hearing at which, not only all the members of the Senate Commerce Committee appeared and spoke, but about a dozen other members of Congress came together with the chairman of the FTC, and Senator Joseph Lieberman, who's rather busy these days, Lynn Cheney, the wife of Republican vice-presidential nominee Dick Cheney, and
mental health organizations and industry groups to examine the marketing of violence to children—high profile, highly publicized—that was Wednesday. Today, about two hours ago, my colleagues at Arent Fox are standing before a federal judge in Indianapolis, just a bit south of here, seeking a preliminary injunction to enjoin the implementation of an ordinance that was passed in Indianapolis in July that bans and restricts access by children to coin-operated video games in Indianapolis and in Marion County, Indiana. There's not enough time to talk about the events of just this week, and certainly not to go into all of the aspects of this issue. What I propose to do is outline the contours of the debate and try to discuss the role that lawyers have historically played, and are currently playing, in helping an industry that's been singled out for blame for horrendous acts of violence and for desensitizing and corrupting America's youth despite the absence of any causal link between playing violent video games and any act of violence, and in the wake of steadily declining rates of youth violence. To try to frame the role that lawyers play is what I'd like to do.

I guess a little history is helpful. In fact, the industry was first challenged to articulate the way it would relate to its customers and the public on issues of video game content in 1993. Not in the wake of school violence; not in the wake of any shootings, but in the wake a press conference convened by Senator Joseph Lieberman, Democrat from Connecticut, Democratic vice-presidential nominee, and Senator Herb Kohl from right here in your great state, as the two of them began to focus their political and legislative efforts on attempting to do two things with my clients. One was to encourage them to reduce the levels of violence in the material that they were producing and making available for play by children and, second, to develop codes, standards, practices and policies that would help parents make informed decisions about the games their kids might encounter. I was involved in those initial discussions in 1993, and was given the responsibility by two national trade associations to help define and implement their vision of corporate responsibility. Interestingly, rather than requesting our help to develop a framework that would shield them from government regulation, or alternately asking us to develop a framework that relied principally on the First Amendment to defend their actions, they asked us as lawyers—to work with them and explore the boundaries and contours of a social contract that they wished to have with their public, and that they felt obligated to uphold as parents and as responsible members of the business communities in which they did business, to be able to respond to cultural, moral, and social norms and perceptions.
We brought the industry together for focus groups, for summit meetings, and we were able to get the industry to buy in unanimously to a very different set of marching orders than that which had been in place in the past for their lawyers. That was to prepare the policies, the standards, and the practices that would allow the industry essentially to do three things. First, to reduce the levels of violence that in fact were in the video games that were being made available to the public. Second, to develop a tool that would allow parents to help their children make responsible game-playing decisions by disclosing the content in each and every game. Third, to implement a code of conduct which would very clearly articulate the way in which the video game industry was going to relate to its customers.

As a starting point, lawyers created and implemented a rating system for all coin-operated video games. At its core the system was designed very simply, modeled on a traffic light to provide parents and children with a user-friendly, very simple way to quickly ascertain the content of potentially objectionable material in games. Yet, they and we were concerned that simply creating the rating system was not enough without creating both internal and external awareness of how that system worked, and the industry again turned to us as counsel to help them in attempting to respond to the needs and values of the community while at the same time having a framework that would allow them to respond to and oppose unreasonable and unconstitutional government censorship. So, we started out and we created a landmark code of conduct relating to the way in which the video games were developed, the way in which they were advertised and marketed, and the way in which they were made available for play by children.

The bottom line, in 1993, 1994, and 1995 is that the industry responded, and in an entirely self-regulatory way, reacted to the concerns that had been articulated by Congress and by members of the community. Importantly, all these things happened well before any of the shootings that I rattled off at the beginning of my presentation. I think the industry learned that the exercise of corporate responsibility is far easier and certainly more widely accepted by the public when responding in an entirely pro-active way than in a defensive and reactive way—a lesson that I suspect the folks at Bridgestone/Firestone have learned only too well these past few weeks.

These efforts that I've outlined yielded great success. Levels of violence in the video games declined. Industry compliance with the self-regulatory system was at an all-time high, and the industry developed educational materials and programs to help parents and children learn
how to use the rating system to guide responsible game-playing decisions. In response, Congress for the most part backed-off, and there was virtually no legislative activity at the state or local level. Indeed, until last year there was no serious effort made to enact legislation, and Congress and the President and child advocacy organizations praised publicly the industry for being good corporate citizens and for doing the right thing. Then came Littleton, and Congress and the President and a dozen states and many dozen local communities needed a visible target. They chose to demonize the video game industry for the acts of violence that occurred in Littleton, and have launched efforts alternately to zone, tax, license or otherwise ban violent video games out of existence.

Just in case you didn't know it, it's an election year. I believe there are fifty-four days to go before the election. I tick them off each morning when I wake up—glad that there's one less to go. The cry to regulate video games and the subsequent burden that's imposed on lawyers representing the industry has reached a fevered pitch. Both presidential contenders talk about this almost every day in their stump speeches. Their vice-presidential nominees talk about it every day, and in some cases, it is a central part of their stump speeches. The wives of the presidential contenders and the vice-presidential nominees talk about it. The President mentioned it in his final State of the Union address, the President's wife in her Senate campaign includes it in every single one of her speeches, and it's included in speeches of too many state and local candidates to count. Certainly in the wake of these developments the role of lawyers in counseling the industry has grown much more challenging. Having adopted and implemented rating systems and codes of conduct, having helped to engineer a reduction in the level of violence of all of their games.

At the same time the nation has seen a precipitous decline in youth violence—not just violence overall, but youth violence; not just youth violence, but shootings by kids of other kids—it becomes increasingly difficult for us to advocate that the industry must do more to respond to the needs and values of the community. We add to this landscape a new enemy. In what I regard as a particularly ironic and perverse twist, our principal opponent in many of our legislative and political battles is the gun industry and the NRA. They, like the video game industry, are attempting to deflect attention from themselves and as Congress, state legislators, and local elected bodies meet to address the issue of youth violence and look in the range of options at potential gun control legislation, the finger is pointed in such a way that the response is, "It's not the guns, it's the games." And in the wake of these political, legal,
and regulatory challenges, our role in counseling the industry to take proactive, responsible stances has shifted to one where we now recognize until the video game industry stops making games that have violence, despite the absence of any link between those games and any act of violence, they'll be perceived to have breached the social contract that they felt they had reached with the public in years past.

Having done what it regards as that which was required by responsible members of the business community, the industry is now turning to us as lawyers to articulate the very arguments that it asked us to not make in 1993, 1994, and 1995 when the issue first came up. Arguments such as, "We're only responding to the needs of the marketplace that demands, some would say has an insatiable thirst, for games with violent themes," to remind policymakers that video games are entitled to the protection of the First Amendment. "Try to ban us, and we'll see you in court," as we're doing today in Indianapolis. To respond that "the ultimate responsibility for monitoring children's exposure to violent entertainment, and entertainment generally, rests with parents and parents alone." Finally, the industry could simply say, as it increasingly is being forced to say, as the tobacco industry before it, that "our games are not harmful; leave us alone." The absence of any definitive, direct, conclusive, scientifically proven causal link between the playing of a violent video game and any act of violence means that our games aren't harmful and therefore can't be regulated. That leaves us necessarily in what you could characterize as a defensive position. Like today in Indianapolis, in response to laws and statutes and regulations that ban or otherwise restrict access by children to the products of this industry, we have to argue that legislation or regulation is unnecessary, that it's ineffective, that it violates and contravenes the First Amendment to the Constitution, that it is inconsistent with well-established Supreme Court and other judicial precedent.

While the industry recognizes very well, as all responsible and successful businesspersons do, that it won't thrive if it can't adapt to meet the needs of the community it serves and is prepared to renegotiate the terms of a social contract, it has now concluded that the critics who have both emotion on their side—and indeed in their arguments they suggest they have God on their side as well—that they will accept nothing less than surrender from the industry. As a parent, I certainly hope and pray that there will be no further acts of violence in our nation's schools and community centers. As a lawyer, I know that's not the case, and I'm equally confident that when the next round of copycat violence occurs in the wake of the next shooting, that the media,
politicians, and the public will seek a quick, easy fix to the complex causes of youth violence. There will be an instinctive reaction to point the finger of blame, and I can assure you that the finger of blame will be pointed squarely at the entertainment industry. As an industry that has tried to behave over a long period of time as responsible corporate citizens looks at the advocacy options, it realizes that there's very little it can do.

Those are some brief comments. As a lawyer representing an industry that is demonized but constitutionally protected, and helping it grapple with a sense of corporate responsibilities, we find that it's a work in progress. I anticipate my cell phone will ring sometime in the next two or three hours, and I'll know more about the ground rules of this debate because they will change depending upon where the federal judge comes out this afternoon in a landmark case which will be the first to explore the extent to which video games are indeed entitled to the protection of the First Amendment. I look forward to your frank comments on this issue, and would enjoy hearing any insights that you have on the way that lawyers have an opportunity to shape the outcome of what has proven to be a fairly interesting and provocative public policy debate.

Professor Schneider: I'm going to start with Karl since he will be leaving us a little early today, and then I have a couple questions for both of you. Karl, as you know and you've seen Professor Fort's writing, he wrote a lot about how compliance programs don't work. Employees don't remember what they signed, they haven't read it, and furthermore, that a lot of these compliance programs are pretty negative—don't do this, don't do that, be sure to disclose that—and they're not all that inspiring. So, employees are not likely to follow this, and he writes that we need a corporate credo in order to get compliance with these programs. What do you think?

Karl Groskaufmanis: It's easy to say because he's not here, but he's got it wrong. He's got it really wrong, and it's kind of academic B.S. Look, to be fair it's something that's hard to measure because in effect one of the most important things you do as counsel, particularly as in-house counsel, is you take concepts that are not intuitive. Price-fixing and antitrust issues—that is not intuitive. People don't inherently understand that. A lot of what I do is defend people in SEC insider trading investigations. The concept that you work on a transaction or quarterly results fifteen hours a day and you come home at the end of the day and your spouse says "what did you do all day," it's like talking to my kids about school. "What did you at school today?" "Nothing."
That's not an intuitive response. That's just not the way real people react to things. One of the things counsel does it takes all these non-intuitive reactions and communicates them in a workplace setting, and a lot of times when we get called in and the bodies are all being chalked off on the pavement it's because that hasn't really been communicated well. Where it does work—and it really does work in a lot of settings but is hard to measure because that management has never been through a U.S. attorney's investigation and had to fund a conference like this—is where management has not been through an SEC investigation. But, it is inherently one of the most valuable things that in-house counsel does. It's mundane stuff. It doesn't get you on the front page of the American Lawyer, but it is what allows your management to focus on their day-to-day business rather than their Bridgestone Tires. So, the reality is that these programs do exist. People do develop an understanding because when you typically go through an investigation people generally understand what the revenue recognition rules are. People understand what insider trading law is, and all that is not intuitive. What counsel are trying to do is inherently important. It's just that you can't measure it as well because you're measuring a negative when something bad hasn't happened. All those things are important, but they're important in the way in which you implement the prohibitions that you have. When you have a stand that says we don't accept bribes when your number one salesman is out bribing all of his most important vendors, you need a management team that sucks it up and says we're going to fire this person. If you think that's an easy thing to do, you're wrong. It's not that morality doesn't matter; it really does matter. It's just that implementing it on a day-to-day basis is hard. But to say that compliance programs are unimportant is fundamentally wrong, and it understates one of the most valuable roles that in-house counsel play and get no credit for. If you mess up and you're managing tons of litigation, the way it typically works is as general counsel you probably get paid more because you're in effect doing more. If you've done all of the mundane things—you have the good advocate that says here are the ten things you'll never do and get immediately fired if you do them—you don't really get recognized for that, but you're really serving an important function for the company, and beyond that, I think you're serving an important social function. So I think the thesis is flawed.

Professor Schneider: How do you think you can create this culture of compliance. I mean, what can a lawyer do?

Karl Groskaufmanis: Well, one of the things a lawyer does is take a
system of rules and regulations that are not written in plain English and you say, "Now I'm going to explain to our regional managers—now I'm going to explain it to our senior management." I'm going to figure out where our greatest legal risks are. If you're in the coin-operated video game business, it's not hard to figure out where our greatest pressure points are, but as an in-house counsel you say, "The kinds of things we're going to have to be careful of is to screen our new products as they come up. We've agreed to all these standards. We're going to actually check and make sure that we're doing the things we commit to."

When we go public for the first time we have a bunch of brilliant scientists or software designers who haven't seen daylight for about three years, we're going to talk them through. Now you're at a public company. Here are the things you can't do anymore. And again, this is the mundane stuff that people don't get credit for, but it can be done and it's not rocket science, but you can't understate how important it is because a lot of my practice is when people haven't done it and now people are paying the consequences.

**Professor Schneider:** A last question, I think. A lot of this conference has already focused in terms of how corporate ethics and creating citizenship is a little different than just what's legally required. How would you differentiate that? Is corporate citizenship actually going above and beyond doing what is legally required?

**Karl Groskaufmanis:** Well, in many instances it is because there's a line in a lot of different areas of law. If you back-date a document consistently and recognize revenue you have likely violated the law and could get sued. A lot of companies set standards that are more than what the law requires. In other words, there's no law that requires that CEOs and CFOs of public companies do all their trading in about a two-to-three week period after they announce quarterly results, but most public companies do it that way for a variety of reasons including maintaining public appearances and knowing that these trades are transparent. So, companies are consistently trying to do more than the minimum that the law requires just because the process of extricating yourself from either civil litigation or governmental investigation is—the costs of that are so great in terms of lost time and effort not to mention all of our reasonable legal fees, that most companies set the bar significantly lower. It's not that people aren't under tremendous pressure because one of the great engines of our economy is the quarterly reporting system, and it's not just quarterly reporting. The marketplace demand information all the time, and you do have to perform. If you don't perform, you're out, and it's not to say that there
isn't a tension there, but it is both morally and economically in a company's interest to not enmesh themselves in the system and in effect not need our services for these things and for more productive things like raising capital.

**Professor Schneider:** Elliott, this morning as you started off you were telling us Monday was a big day already in terms of finding out that the marketing of some of these entertainment programs was not following the codes of compliance that companies had set forth for themselves. You spent a lot of time telling us how good the video game industry has been in setting forth this code of conduct. Exactly what happens when they don't follow it?

**Elliott Portnoy:** Well, in the context of my clients we have a particular dilemma because in fact the 104-page Federal Trade Commission report which was so damning and critical of the entire entertainment industry, and its 240-page appendices, actually contains not a word of criticism for the coin-operated side of the industry and indeed includes praise. The one thing that my clients do not do, in part because of resources, in part because of history, is directly advertise and market to children. The focus of FTC report was how the movie industry will advertise an R-rated movie in a forum that has approaching a majority teen audience. So, for instance a magazine like *Sports Illustrated for Kids* or on Nickelodean or as a trailer before a G-rated movie. The challenge frankly for my clients is how do we attempt to get the media which has shown no ability to differentiate between elements of the industry to realize that, when it comes to compliance, there's one element of the industry that may not be as pure as driven snow, but is in compliance. In fact, the real challenge is the overlay of the Constitution in that you have members of Congress screaming and yelling about how awful it is at the same time all of these products, the medium, is protected by the Constitution. So, you end up having this debate where both sides pass in the night with no recognition that Congress can't really do anything to stop the practice and no real dialogue on what should be done to attempt to beef up voluntary codes of conduct, to increase the self-regulatory efforts, to enhance the public education process about these products. So, as horrible as Monday was, my clients were quite pleased in that they, as we knew they would, received no criticism for their practices in a somewhat perverse and ironic way.

**Professor Schneider:** This is more of a question of personal ethics here. For you, and I included some things in your biography so that everyone would also have some perspective, a lot of what you do out of
the office is work directly to help kids, and yet the majority of us probably sitting here before we heard you speak would look at what you do in the office as hurting kids. How does an attorney go about reconciling what appears to be very clear outside values with what their doing inside the office?

Elliot Portnoy: It actually has proven to be not terribly difficult to reconcile for a variety of reasons. First, I would suggest that the moment that there was any definitive and conclusive proof that the products of this industry caused harm directly and were linked to violence, not only would I stop doing the work, but more importantly, the industry would stop producing the games. So, I have a firm belief that in fact the products of this industry, notwithstanding all of the hype, rhetoric and hysteria, do not cause kids to kill kids. Second, I have a strong and abiding belief in the Constitution, and no matter how disgusting, offensive, repulsive I may find these games, no matter how offensive and unworthy you may find these games to be, despite the fact that I won't let my son play those games, they are protected. What differentiates our society and our country from others is the overlay of the First Amendment. So, I don't feel like I go from the office needing to take a cold shower before I start helping kids. I wouldn't suggest that video games are necessarily on the list of most positive influences in every child's life, but indeed there are studies that do point to some positive benefits. There are also studies that point to some less positive and more detrimental benefits. But, as someone who took an oath to zealously advocate on behalf of my clients, I have found that it has been challenging and actually on some days even a little bit of fun.

Professor Schneider: How would you compare your role because you represent a lot of other clients in terms of promoting good corporate citizenship. Is this industry particularly different in terms of what you've done with other industries?

Elliot Portnoy: I think it is because, like Karl, in other contexts the compliance work and the counseling work we do relates to compliance with the law. In this industry they're in full compliance with every law and every regulation, so we need to go far beyond the notion of compliance with the law because the compliance issue is entirely irrelevant in the context of this very emotional debate. So, this industry is unique to the extent that when you counsel it to be good corporate citizens you're only talking about going beyond what the law requires, whereas in most contexts it is much more nuanced and you are talking about compliance with a basic set of understood principles, rules, regulations, and laws.
**Audience:** I'm curious why you would not allow your child to play the games once he's old enough.

**Elliot Portnoy:** My son is two-and-a-half so we have a period of time before he can play. My sense is that when he is old enough, which is to say when he is in a position of being able to make decisions for himself to distinguish between fantasy and reality, I will have absolutely no problems with having him play the games. As a parent, that's a decision for me to make, and I'm the one who should be exercising the control and making the decisions about the games he plays and giving him guidance about what games he can play rather than allowing the local government, the state government, or Congress to dictate that which I can allow him to play. So, I should expand on that; it's not that he will never be permitted, it's once he reaches the joysticks he'll probably be four or five, and my view is that certain types of entertainment are clearly and obviously inappropriate for young children. Certainly clearly and obviously inappropriate for young children unless their parents are present and participating in an interactive way in that entertainment at the same time.

**Audience:** I don't understand the application of the First Amendment to movies and television. My little understanding is that it is not as strong or as clear cut as it is in the freedom of speech or press principles.

**Elliot Portnoy:** Actually, in many ways it is. In fact, the only way in which a content-based law can survive constitutional scrutiny is if the material is shown to be either obscene or harmful to minors. So in fact, movies, books, the Internet have been deemed by the Supreme Court and all the federal courts to have the full protection of the First Amendment. Only in those instances where a product is deemed to be obscene or harmful to minors there can be regulation and in fact there's not a single court that's ever held that non-obscene, violent content can be regulated, and that's what is at stake today in Indianapolis—whether the definition of obscenity, the variable obscenity test articulated in the *Miller* case can be expanded for the first time beyond sex, beyond sexual content, beyond material that deals in sex, to pure violence. This will be a landmark case, not only in exploring the contours of First Amendment protections of video games, but more importantly, whether you can carve out an exception to the First Amendment for violent content.

**Audience: Dr. Valerie Hans, University of Delaware:** I wanted to ask you about your statement that there is no clear and conclusive proof about the linkages between involvement in violent video games or other kinds of violent media and violence on children. Looking collectively at
exposure to media violence, there are certainly some studies where responsible scholars unconnected to one side or the other would say we have some concerns here. There's a worry among certain children—children that have a propensity to violence—this is the kind of thing that could in fact exacerbate their violence levels. I'm sure you're familiar with the research and you know the kinds of studies I am talking about. So, I think this does raise an interesting question. Obviously the video industry does not want to not be in the position that tobacco companies are now in saying, we sponsored the research and the research didn't show any clear and conclusive proof. Does the industry or lawyers have the responsibility to sponsor this kind of research? If so, how can you avoid some of the consequences of corporate sponsorship of research that might tend to show potential harm? I think this raises fascinating questions both for the industry and also for academic scholars who are doing the research in the first place.

Elliot Portnoy: Well, on the core issue, you're right. There are thousands of studies on media violence many of which, indeed the overwhelming majority of which, point to some measure of concern, many of which point to a direct link between prolonged exposure to media violence and aggressive behavior. I think we're generally very careful from an industry perspective to differentiate between aggressive behavior or aggressive play that may perhaps be the result of prolonged exposure to media violence and violent behavior. To date, there is yet to be any study that conclusively, scientifically shows the link between playing a violent video game and an act of violence. The industry has had extensive discussions about whether it should sponsor the landmark study that in fact will either conclusively or inconclusively demonstrate the link between violent behavior and violent media exposure, and has concluded that there is so much interest and so many studies underway that it simply does not warrant the industry doing anything more than having its scholars and reviewers analyze the literature and wait for something more definitive to arrive. We simply don't believe you can prove a negative. We're not going to be able to have a study that definitively and conclusively shows there's no causal link between an act of violence and playing violent video games. So, in response we wait for government and for social science researchers to produce more literature that we then review and respond to. It may not be a very appropriate response, but the consensus is that it's not a battle we can win by sponsoring another study. We can certainly review the literature and attack the methodology if appropriate, and in many cases we have no particular concerns with the methodology or the results. They just
don't show that there is a link, and indeed, the most cited study is a recent one by Anderson and Dill, and that's the study that most cities, communities, states and even Congress point to as the landmark study. Its own authors suggest that trying to conclude that there's a link between prolonged exposure to video games and acts of violence is risky at best, so that's where we come out on that issue.

**Dr. Valerie Hans:** If I could just follow up. If you take the tobacco situation as a comparison, it's hard to imagine the epidemiological study that would provide conclusive proof. So as a scientific matter it may be much more difficult than the health issues that have arisen.

**Elliot Portnoy:** And from a constitutional perspective it requires a very different analysis than perhaps the tobacco industry faced.

**E. Michael McCann, District Attorney for Milwaukee County:** As a representative of the American Bar Association, I served in the National Cable Television Violence Study. It was a three-year study and involved major medical associations, pediatric, psychological associations and I was stunned at the volume of studies that showed there was linkage between violent ingestion, intellectual ingestion by children of violent materials and their influence on their aggressive behavior. I've also been a trial lawyer, and the type of testing you're talking about as the definitive causal connections that this very material is not going to permit. I agree you'll probably be protected by the First Amendment. I have no doubt about that, but I think what you're doing is definitely injurious to our society. I think the evidence is overwhelming of that, and I hope, and I say this as a prosecutor, that the civil trial lawyers who will probably have a better chance of getting you, bankrupt you because I think it would be distinct service to this society. A few of the streets of this city are the witness to nightly gunfire. I'm not blaming all that on television violence, but there is some causal connection. The very children who are plopped in front of the television set are not in homes where parents aggressively assert and pass on traditional values, they're in homes that are frequently dysfunctional. That's part of the problem, of course, but I think it's disingenuous to say it hasn't been proven beyond doubt that there isn't a connection. It is injurious to our society. I don't know what's going to happen in this decision. I know that sexual obscenity is virtually the only category that isn't protected, and I suspect this court opinion is going to say no to including violence in that category. You're right—I think it's constitutionally protected, I think it is definitely injurious to our society, and I hope the civil trial lawyers bankrupt you out of business.

**Elliot Portnoy:** Well, they're trying. How do we deal with the
paradox that at the same time there is a pervasiveness of violence available in a variety of media formats and youth violence—I would hazard a guess (I don't know what Milwaukee statistics are) but every other part of the country as measured by the C.D.C, the Department of Justice, and the F.B.I. reports a precipitous decline in youth violence: How can it be that it is the entertainment media that's responsible for the perceived increase in youth violence when in fact there's less youth violence than there's ever been? There's less shootings than there have been in decades. The paradox that we face is that we put in place a regulatory system, we've given parents the tools that they need to help their kids make responsible game-playing decisions, we've reduced levels of violence in games, and there's less violence on our streets and yet, the finger of blame gets pointed first at the entertainment media. I don't hear any of the same rhetoric about access by children to guns. It's remarkable to me that the first instinct—and I don't know the district attorney so I'm not directing this at him—but the first instinct of most law enforcement officials, of most elected officials, of most politicians, is to look first at the entertainment industry as the leading cause if not the sole cause of violence. At the same time, there's less of it out there. It puts lawyers representing the industry frankly, where having done what we believe was right in the self-regulatory realm, in a quandary. How do we advise our clients how to respond to the kind of vitriol that's regularly launched against the industry in the absence of the definitive proof that would be needed to enact regulations? It calls for some interesting moral, ethical, and legal dilemmas on a daily basis.

GOVERNMENT REGULATION OR MORAL RENEWAL? HOW TO IMPROVE CORPORATE CITIZENSHIP

Dr. William J. Bennett

Dr. William J. Bennett: Ladies and gentlemen, good afternoon. I do have a Jesuit background; I went to Jesuit high school. People who hear me speak in public will often ask, "Just how long did they have you?" They had me pretty long, but more importantly they had me early.

It's a pleasure to be at a university. I do not receive many invitations to them, even though the university is supposed to be committed to the free marketplace of ideas. Let me illustrate with this story—it's not a complaint, just something I find interesting. In 1980, before I entered the Reagan administration, I was thirty-eight years old, and I had