

LEGAL ADVICE ABOUT CONTEMPLATED ACTS: THE DECISION TO OBTAIN ADVICE, ITS SOCIAL DESIRABILITY, AND PROTECTION OF CONFIDENTIALITY

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I. INTRODUCTION

WHEN will a party decide to obtain legal advice about a contemplated act, and when will he decide to commit it? In this paper, I will examine a model that describes how parties rationally make both types of decisions and how their decisions are influenced by the presence or absence of rules protecting the confidentiality of their communications with legal advisors¹ about contemplated acts.² The acts of concern will be those that may result in sanctions, that is, in criminal or civil penalties or in the payment of damage judgments. Included, therefore, are not only acts in the traditional area of crime but also, for example, behavior that may violate tax or securities law, or environmental or safety regulations, and conduct that may give rise to private actions in tort or for breach of contract.³

In addition to studying parties' decisions about whether to obtain legal advice and whether to commit contemplated acts, I will ask when provi-

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¹ While in the model legal advisors can be interpreted to be any persons who supply legal advice, the reader will no doubt wish to think of legal advisors as attorneys or, perhaps, as accountants.

² I will not discuss communications with legal advisors about acts *already* committed. This will be the subject of a successor paper.

³ Not of interest are plans, such as the drafting of a will, that do not ordinarily expose parties to sanctions.

sion of legal advice will result in socially desirable changes in behavior, that is, either in parties not committing undesirable acts that they would have committed in the absence of legal advice or in their committing desirable acts that they would not have committed in the absence of advice. Protection of confidentiality will lead to socially desirable changes in behavior when it both encourages parties to obtain legal advice (something that, as will be shown, is not always the case) and when the legal advice they obtain will promote desirable changes in behavior.

Three types of legal advice will be distinguished in the model: advice concerning the legality or "sanctionability" of acts,⁴ advice concerning the probability or magnitude of sanctions, and advice instructing parties how to lower the probability or magnitude of sanctions. The main part of the paper will analyze the model informally (the Appendix will analyze the model formally), and the concluding portion will comment briefly on the interpretation of the analysis and the relevant law.⁵

⁴ I use the term "sanctionability" rather than "legality" or "illegality" because I want to refer to the broadest category of acts that may result in sanctions (for instance, acts that do not violate any statutes and are not illegal but for which parties might be liable in tort).

⁵ The principal contribution of this paper is that it identifies how the effects and the social desirability of legal advice and protection of confidentiality depend on the type of advice about contemplated acts that is sought; but the fact that the analysis employs a model of rational choice will also, I hope, prove clarifying. I am not aware of other work studying explicitly the decision to obtain legal advice about contemplated acts or the social desirability of the advice. However, much has been written on the protection of the confidentiality of legal advice about contemplated acts (or, in the parlance of legal ethics, "future acts"). See Jeremy Bentham, 5 *The Rationale of Judicial Evidence* 308-12 (1827), and John H. Wigmore, 8 *Evidence in Trials at Common Law*, rev. John T. McNaughton, 572-80 (1961). See also, for example, Note, *The Future Crime or Tort Exception to Communications Privileges*, 77 *Harv. L. Rev.* 730 (1964); Geoffrey Hazard, *An Historical Perspective on the Attorney-Client Privilege*, 66 *Calif. L. Rev.* 1062 (1978); John McCormick, McCormick on *Evidence*, rev. Edward Cleary et al., 229 (3d ed. 1984); Note, *Developments in the Law—Privileged Communications*, 98 *Harv. L. Rev.* 1501-14 (1985); Charles Wright & Kenneth Graham, *Federal Rules of Evidence, Rejected Rules* 502 to 503, in 24 *Federal Practice and Procedure* 493-528 (1986); Charles W. Wolfram, *Modern Legal Ethics* 279-82, 692-706 (1986); Frank Easterbrook, *Insider Trading, Secret Agents, Evidentiary Privileges, and the Production of Information*, 11 *Sup. Ct. Rev.* 309 (1981); and B. Peter Pashigian, *Regulation, Preventive Law, and the Duties of Attorneys, in The Changing Role of the Corporate Attorney* 28-41 (William J. Carney ed. 1982).

Bentham is well known for his criticism of protection of confidentiality. In essence, his criticism amounts to the claims that (a) protection of confidentiality will benefit those who intend to break the law and thus will dilute deterrence, while (b) the protection will not benefit law abiders, so that absence of the protection will not hurt them. The general form of response to Bentham has been (a) that the law is not always clear, so that not all acts can be seen as clearly violative of the law or as clearly conforming to it, and (b) that protection of confidentiality encourages parties to obtain legal advice, which is a good thing. I will comment on Bentham's argument and this response in notes 22, 29, 31, and 33 *infra*.

II. ANALYSIS OF THE MODEL

In the model, it will be assumed that parties choose between alternative courses of action on the basis of the probability-discounted or "expected" values of the actions; that is, parties will be assumed to be "risk neutral."⁶ Their decisions whether to obtain legal advice and whether to commit acts will be described and evaluated for each of the three types of advice just noted.

A. Parties Are Uncertain Whether Acts Are Sanctionable

Here it will be supposed that parties are initially uncertain whether a contemplated act is sanctionable, but they do know the probability and magnitude of the sanction that will apply if the act is sanctionable.⁷ Thus, legal advice will concern only the sanctionability of acts. Two cases will be examined.

1. Case in Which Legal Advice about Sanctionability Is Definitive

It will be assumed in this case that legal advice about the sanctionability of acts is definitive—the advice will either be that an act is surely sanctionable or that it is surely not (and the advice will be correct and realized to be so).

Behavior in the Absence of Legal Advice. In the absence of definitive legal advice about the sanctionability of an act, a party's decision whether to commit the act will depend on how likely to be sanctionable he believes it is, together with the probability and magnitude of sanctions if it is sanctionable and the gain he would obtain from it. Consider the following two examples.

1. The owner of a small plant is deciding whether to release a chemical waste product into a nearby river. He does not know whether the waste product would be considered toxic under an environmental safety ordinance and therefore does not know whether discharging the waste product into the river would constitute a violation of the ordinance. The owner

⁶ Readers who are unfamiliar with the concepts of expected value and risk neutrality will be unlikely to have difficulty understanding the present analysis if they are careful to follow the numerical examples; however, they may wish to consult Howard Raiffa, *Decision Analysis* (1968), for an introduction to decision theory. It will be clear to readers who are familiar with decision theory that the qualitative nature of the results to be obtained does not depend on the assumption of risk neutrality.

⁷ In reality, of course, parties will often be uncertain about a combination of factors. I assume uncertainty over only one factor at a time in the present analysis in order to isolate each factor's importance.

would save \$3,000 by discharging the waste product into the river (rather than transporting it to a dump), but the penalty for violating the ordinance would be \$5,000. If, in the owner's opinion, the probability of a violation is, say, 40 percent, and he discharges the waste product into the river, his expected net gain will be $\$3,000 - (.40 \times \$5,000) = \$3,000 - \$2,000 = \$1,000$.⁸ He will therefore proceed; in general, he will proceed as long as his subjective probability of a violation is less than 60 percent.⁹

In this example, it was assumed that, if a party committed a sanctionable act, a sanction would be applied with certainty (a discharge that violated the ordinance would definitely be noticed). In the next example, which concerns the permissibility of a tax deduction, it is assumed that an impermissible act will be sanctioned only with a probability, that of a tax audit.

2. A person considers claiming a deduction from his taxable income that would allow him a \$20,000 saving in taxes. He estimates that the probability that the deduction is permissible is 50 percent. He also believes that, given the nature of the deduction, the chance that his tax return will be audited is 75 percent and that, if his return is audited and the deduction is found impermissible, he will lose his deduction and have to pay a penalty of \$10,000.¹⁰ Thus, if he claims the deduction and it is in fact impermissible, his expected penalty will be $.75 \times \$10,000 = \$7,500$, and his expected gain will be $.25 \times \$20,000 = \$5,000$. Hence, if he claims the deduction, his expected net gain will be $(.50 \times \$20,000) + .50 \times (\$5,000 - \$7,500) = \$8,750$. Therefore, he will decide to claim the deduction (and would do so as long as he thinks the likelihood of its permissibility exceeds 11.11 percent).¹¹

⁸ Note that the expected net gain may be interpreted as the average net gain if the owner made many similar decisions.

⁹ At a probability of a violation of 60 percent, his net expected gain would be zero: $\$3,000 - (.60 \times \$5,000) = 0$.

¹⁰ The nature of the deduction and prior experience with the taxpayer can strongly influence the probability of an audit. Thus, even though only a small proportion of all returns are now audited by the IRS, it is not necessarily unrealistic to assume that the probability is 75 percent in a particular case. With regard to the penalty, the reader should note that under the new tax law (1986), the no-fault penalty for understatement of taxes is 25 percent of the amount of the tax savings resulting from the understatement (I.R.C. § 6661); the penalty for negligence is 5 percent plus 50 percent of interest owed (I.R.C. § 6653(a)); the civil penalty for fraud (which may be established merely by a preponderance of the evidence) is 75 percent plus 50 percent of interest owed (I.R.C. § 6653(b)); interest is compounded on taxes not paid (I.R.C. § 6622); and neither penalties nor interest is tax deductible (I.R.C. §§ 162(f) and 163(h)). Taking these factors into account, a penalty of \$10,000 on a \$20,000 savings that is due to tax understatement may not be unrealistic in certain cases. In any event, the present example is not intended to portray a typical situation facing a taxpayer; its chief purpose is to illustrate the character of a taxpayer's decision making.

¹¹ For $.1111 \times \$20,000 - .8889 \times \$2,500 = 0$.

Further reference to these two examples will be made below.

Behavior if Legal Advice Is Obtained. To ascertain whether it will be worth his while to obtain legal advice about the sanctionability of an act, a party must ask himself what use he would make of the advice that he might be given. If he learns that an act he contemplates is in fact not subject to sanctions, he will commit the act (presuming he will obtain a positive gain from doing so). If he learns that an act is sanctionable, he will not commit it if the expected sanction exceeds his expected gain, but he will go ahead and commit it if the expected sanction is less than his expected gain. In example 1, the plant owner clearly will not discharge the waste product into the river if he learns that this would violate the environmental ordinance, since his gain of \$3,000 would be exceeded by the \$5,000 penalty. In example 2, the person will not claim a tax deduction if he learns that it is not permissible, since his expected gain would be \$5,000—recall he would escape audit 25 percent of the time—and his expected penalty would be \$7,500. However, if the probability of audit were lower, for instance, 10 percent, the person would decide to claim the deduction even if he knew it was impermissible, since his expected gain would be \$18,000 and since his expected penalty would be only \$1,000.

The Decision Whether to Obtain Legal Advice. A party will obtain legal advice if its expected value exceeds its cost. The expected value of advice is determined by the probability that advice will lead a party to alter his behavior, multiplied by the benefit he will obtain from his altered behavior.¹² Consider a party who, in the absence of advice, will decide not to commit a contemplated act. For him, the expected value of advice will equal the probability that he will learn that the act is not sanctionable, multiplied by the gain he will enjoy from then committing the act. On the other hand, consider a party who will commit an act in the absence of advice but will not if he learns that the act is sanctionable. For him, the expected value of advice will equal the probability that he will be told that the act is sanctionable, multiplied by the expected sanction he would have borne, less the expected gain that he would have enjoyed had he committed the act. The owner of the plant in example 1—who believes that the probability of a violation of the ordinance is 40 percent and will thus discharge the waste product into the river in the absence of advice—will calculate advice to have an expected value of \$800. With a probability of 40 percent, the owner believes he will learn that a discharge into the river

¹² While it should seem plausible that this is the expected value of advice, the point can be demonstrated directly by computing the net expected gain if a party obtains advice (taking into account how he will wish to act given advice) and then by subtracting the net expected gain if a party does not obtain advice. For an introductory discussion of the expected value of information, see Raiffa, *supra* note 6, at 27–32.

would constitute a violation and will then take the waste product elsewhere, avoiding a penalty of \$5,000 but forgoing savings of \$3,000. Thus, advice will benefit him by $\$5,000 - \$3,000 = \$2,000$ with a probability of 40 percent, and $.40 \times \$2,000 = \800 . (With a probability of 60 percent, the owner believes he will learn that a discharge would not constitute a violation; but this fact does not enter into the calculation since, in that case, his behavior will not be altered.)¹³ In consequence, the owner will obtain advice if its cost is less than \$800. Similar calculations show that the expected value of advice about the tax deduction in example 2 is \$1,250. With a probability of 50 percent, the person will learn that the deduction is impermissible and will not claim it, thereby avoiding expected penalties of $.75 \times \$10,000 = \$7,500$ but forgoing expected gains of $.25 \times \$20,000 = \$5,000$. Advice will therefore result in expected savings of \$2,500 with a probability of 50 percent, and $.50 \times \$2,500 = \$1,250$.

It should be noted that advice will be of no value to a party, and therefore will not be obtained, if advice would never lead him to alter his behavior. This will be the case only if, in the absence of advice, a party will commit an act and if, on learning that the act is sanctionable, he will still commit the act because the expected sanction will still be less than the expected gain. That will be true in example 2 if the probability of an audit is only 10 percent, for, as mentioned above, the person will then claim the deduction even if he knows it is impermissible.¹⁴

*Social Desirability of Legal Advice.*¹⁵ Before asking whether legal advice leads to socially desirable changes in behavior, we must say which acts are considered socially desirable and which are considered undesirable. Let us suppose that it is socially undesirable for an act to be committed if the party's gain from it would be less than the harm done, but it is

¹³ However, suppose that the owner would not discharge the waste product in the absence of advice because he initially thinks the probability of a violation is higher, say 80 percent. In this situation, the expected value of advice would derive from the possibility that he would learn that a discharge would not constitute a violation; the expected value of advice would equal $.20 \times \$3,000 = \600 , which is the probability that he will learn that a discharge will not constitute a violation multiplied by the gain from then discharging the waste product into the river.

¹⁴ Actually, a qualification going outside the model is worth mentioning. It may be that a person who would claim a deduction (or commit some other act), whether or not he is told that it is definitely impermissible, will still place a positive value on knowledge of its impermissibility. One reason is that this knowledge may be useful in deciding whether he should later take steps to conceal his act (such as not claiming a similar deduction the following year); if he learns his act is impermissible, he may well want to take such steps.

¹⁵ When I speak of the social desirability of legal advice (and later of protection of confidentiality), I will limit consideration to whether it induces parties to make socially desirable decisions; I will not ask whether any change for the better in parties' decisions is justified by the cost of legal advice.

desirable for the act to be committed otherwise.¹⁶ Let us also suppose that acts are sanctionable if and only if they are harmful and that, if an act is sanctionable, the expected sanction for committing it is less than or equal to the harm.¹⁷

Now consider the question whether definitive legal advice about the sanctionability of an act results in socially desirable changes in behavior. Observe, first, that the advice cannot lead a party to commit a sanctionable act that he would not otherwise have committed; if a party would not commit an act in the absence of advice and if the act is sanctionable, he will learn this when he obtains advice, and that will only reinforce his decision not to commit the act.¹⁸ Hence, advice can lead to only two types of change in behavior: to a party's committing an act that is not sanctionable and that he would not otherwise have committed (because he erroneously thought it likely to be sanctionable) or to a party's not committing a sanctionable act that he would otherwise have committed (because he erroneously thought it unlikely to be sanctionable). Both these types of change in behavior are socially desirable. Given the assumptions of the last paragraph, it is socially desirable for an act that is not sanctionable to be committed, and it is socially undesirable for an act that is sanctionable to be committed if the expected sanction exceeds the gain.

Effect of Protection of Confidentiality. It has been implicitly assumed so far that obtaining legal advice will not raise the likelihood or magnitude of sanctions if a party commits a sanctionable act. It was taken for granted in example 2, for instance, that the probability of audit and the size of the possible penalty will not rise if a person obtains advice about the permissibility of a tax deduction. Such an assumption will be interpreted as reflecting legal protection of confidentiality of communications with legal ad-

¹⁶ The reader should not be detained by this particular assumption or by the thought that there may be some acts that are socially undesirable, whatever the gain to the parties who commit them. The main importance of the assumption is that it allows the category of desirable acts to be described very simply.

¹⁷ This assumption seems the one of greatest relevance to me because both casual empiricism and theoretical considerations (having to do with the costliness of imposing sanctions) suggest that expected sanctions are more often less than or equal to the level necessary to achieve optimal deterrence rather than greater than necessary. However, the interested reader will have no difficulty in tracing out the consequences of the assumption that the expected sanction exceeds the harm. For the most part, the qualitative nature of the conclusions under that assumption is the same as that for the case in which the expected sanction is less than the harm.

¹⁸ Of course, advice about facts other than the sanctionability of an act might lead a party to commit a sanctionable act that he would not have committed in the absence of advice. As will be discussed below, advice that the expected sanction for an act is lower than a party initially thought may well lead him to commit it.

visors.¹⁹ In the absence of protection, it will be supposed that the probability or magnitude of sanctions will rise if a party obtains legal advice.²⁰

It will now be shown that protection of confidentiality will have *no* effect on a party's decision to obtain definitive legal advice about the sanctionability of an act. Remember from above that a party will decide to obtain such legal advice only if he would *not* commit an act that he learns is sanctionable. Therefore, it will be irrelevant to a party who decides to obtain advice that the probability or magnitude of sanctions might be raised as a consequence; this would only strengthen his decision not to commit an act that he learns is sanctionable. Hence, the expected value of legal advice will not be changed if confidentiality is unprotected, and a party will therefore decide to obtain advice exactly when he would have if confidentiality had been protected.

To illustrate, in example 2 we reasoned that, if the probability of a tax audit is 75 percent and the penalty for an impermissible deduction is \$10,000, the person will not claim a deduction if he learns that the deduction is impermissible. Accordingly, if he decides to obtain advice, it will not matter to him that the size of the penalty for an impermissible deduction or the probability of audit might be raised.²¹ The expected value of advice will thus still be \$1,250, and he will still obtain legal advice if and only if its cost is less than this amount.

Because protection of confidentiality will have no effect on a party's decision to obtain definitive advice about the sanctionability of an act or on his behavior if he obtains advice, protection of confidentiality will have no effect on whether he commits a contemplated act.

Social Desirability of Protection of Confidentiality. This issue is moot in the present case since protection of confidentiality has no effect on behavior.²²

¹⁹ Legal advisors' motives, and the ability to enforce legal rules regarding confidentiality and disclosure, will be discussed briefly in the concluding section.

²⁰ If a legal advisor discloses a client's intentions, the likelihood that the client will be caught and sanctioned will generally increase, and the magnitude of the sanction may rise as well, since it may depend on the client's state of mind.

²¹ The fact that being audited may be time consuming and unpleasant is ignored.

²² In the present case, why is Bentham's argument (see note 5 *supra*) against protection of confidentiality wrong? The answer is that the disadvantage of protection that he mentioned—that lawbreakers would be helped—is irrelevant because those who would break the law do not obtain legal advice. At the same time, what I called the general response to Bentham is also irrelevant since protection of confidentiality does not encourage parties to obtain legal advice.

2. Case in Which Legal Advice about Sanctionability Is Not Definitive

It will now be assumed that legal advice is in the form of an opinion expressed by a probability that an act is or is not sanctionable. In this case, the conclusions about the effects and the desirability of legal advice concerning the sanctionability of acts and of protection of confidentiality will differ from the case just examined.

Behavior in the Absence and in the Presence of Legal Advice. The Decision to Obtain Advice. How a party will behave in the absence of advice here is, of course, identical to how he behaved in the absence of advice before. Here, however, if a party obtains advice, he will employ the legal advisor's probability of the sanctionability of an act in deciding whether to commit the act. That is, a party will compare the expected gain from the act to the advisor's probability that the act is sanctionable, multiplied by the expected sanction for a sanctionable act. For instance, if the plant owner in example 1 is told by his legal advisor that the likelihood of a violation of the ordinance is 80 percent, he will not discharge the waste product into the river, since he will compare the gain of \$3,000 to 80 percent of \$5,000, or \$4,000. The expected value of advice will be found, as before, by multiplying the probability that a party would be led to change his decision whether to commit an act by the expected benefit that he would obtain as a consequence,²³ and a party will obtain advice if its expected value exceeds its cost.

Social Desirability of Legal Advice. In considering this matter, it will be assumed that the legal advisor's probabilistic opinion constitutes the best information available to the party ex ante about the sanctionability of an act or, equivalently, about whether the act would be socially harmful.²⁴ Further, it will be assumed that it will be socially desirable ex ante for a party to commit an act if and only if the gain he would obtain exceeds the expected harmfulness of the act, computed by multiplying the legal ad-

²³ For example, suppose that the owner in example 1 initially believes that the probability of a violation is 50 percent, that with probability 50 percent, a legal advisor will tell him that the probability of a violation is 20 percent, and, with a probability of 50 percent, the advisor will tell him the probability of a violation is 80 percent. (Note that the person's initial probability equals the probability-weighted average of the probabilities he might learn: $.50 \times .50 + .20 \times .50 \times .80$. This must be true by the definition of conditional probabilities.) Then, in the absence of advice, we know that the owner will discharge the waste product, and we know that, if the advice is that the probability of a violation is 80 percent, he will not discharge the waste product. Hence, the expected value of advice is $.50 \times (.80 \times \$5,000 - \$3,000) = .50 \times \$1,000 = \500 .

²⁴ Recall from above that the assumption is that an act will be sanctionable if and only if it is harmful.

visor's probability that the act is sanctionable by the harm the act would do. Suppose, in example 1, that, if discharging the waste product is a violation, the magnitude of the harm (in terms, say, of the death of fish) would be \$5,000, so that this figure multiplied by the advisor's probability of a violation equals the expected harm that would result from the discharge.²⁵ Then, since the gain from the discharge would be \$3,000, the assumption is that it will be socially desirable ex ante that the waste product be discharged if the legal advice is that the likelihood of a violation is less than 60 percent (recall that 60 percent of \$5,000 is \$3,000).

Note from this illustration that, when parties act desirably in the ex ante sense, it may well be that they commit acts that turn out to be sanctionable.²⁶ That this should be the case ought not disturb the reader. If, according to the best information available at the time a decision is made, an act is thought to be harmful and sanctionable only with a probability, it makes sense that the act should be committed when the benefits from doing so are sufficiently high. A contrary conclusion would lead to the reductio ad absurdum that, when there is any chance that an act is sanctionable, it should not be committed, however large the gains would be.

With this in mind, it is easy to answer the question whether legal advice about the probability that acts are sanctionable will lead to socially desirable behavior. The advice will lead to such behavior if the expected sanctions for sanctionable acts equal the expected harm the acts would do. For then parties will, desirably, be led to compare their expected gains from contemplated acts to the expected harmfulness of the acts. Thus, in example 1, since the sanction for a violation of the ordinance was assumed to equal \$5,000, legal advice will lead to socially desirable decisions.

If, however, expected sanctions for sanctionable acts are less than the harm they would do, then legal advice might not lead to socially desirable behavior. In the absence of advice, a party might decide against commit-

²⁵ In fact, reflection about this computation of expected harm reveals an artificiality in the assumption that an act is harmful if and only if it turns out to be sanctionable. Where there is uncertainty about whether discharging a waste product into a river will violate an ordinance intended to protect the health of the river, the uncertainty presumably often arises because the waste product in question *verges* on the toxic. Hence, (a) even if the waste product does not turn out to be considered toxic under the ordinance, discharging it may well cause some detrimental change in the river. On the other hand, (b) if the waste product does turn out to be considered toxic under the ordinance, discharging it will probably usually cause less harm to the river than would the discharge of an unambiguously toxic waste product. Since these factors work in opposite directions and may be offsetting, taking them into account would not materially affect the analysis here, and, for expositional reasons, I ignore them.

²⁶ Also, it may be that, when parties act desirably in the ex ante sense, they do not commit acts that would turn out not to be sanctionable.

ting an ex ante undesirable act if his estimate of the likelihood of its sanctionability is high enough. Yet, with advice that the act is less likely to be sanctionable, the party may decide to commit the undesirable act, since he will face an expected sanction that is less than the expected harm. This might be true in example 1 if the penalty for a violation was \$4,000 (rather than the harm of \$5,000), if the owner's initial belief of a violation was 80 percent, and if the legal advisor's probability was 70 percent.²⁷ A similar case might arise in example 2 if the audit probability or penalty was inadequate and if the person would not take a deduction in the absence of advice but might do so with advice.²⁸

The preceding paragraph is not meant to imply that legal advice will necessarily be undesirable in the ex ante sense when expected sanctions understate the harmfulness of acts. Advice might well still be desirable if, although expected sanctions are low, parties will be induced to behave appropriately with advice and will not otherwise.

Effect of Protection of Confidentiality. Protection of confidentiality in the present case will tend to encourage parties to obtain legal advice. The reason is that parties will know that, after obtaining advice, they may decide to commit an act that could turn out to be sanctionable. This in turn means that anything—in particular, protection of confidentiality—that reduces or prevents the increase of the probability or size of sanctions for committing sanctionable acts will be desired by parties who obtain legal advice. Protection of confidentiality will therefore raise the expected value of advice to them and may be what leads them to obtain advice. For instance, the person in example 2 contemplating the tax de-

²⁷ To complete this example, suppose that the owner believes he will be told with a probability of 50 percent that the probability of a violation is 90 percent and, with a probability of 50 percent, that the probability of a violation is 70 percent. Then, since in the absence of advice his probability of a violation is 80 percent (for $.50 \times .90 + .50 \times .70 = .80$), he will not discharge the waste product, for the expected penalty will be $.80 \times \$4,000 = \$3,200$, which will exceed his gain of \$3,000. However, he will decide to discharge the waste product if he obtains advice and is told that the probability of a violation is only 70 percent, since, in that case, the expected penalty will be only $.70 \times \$4,000 = \$2,800$, which is less than \$3,000. But discharging the waste product will be socially undesirable even if the probability of a violation is 70 percent, since the expected harm will be $.70 \times \$5,000 = \$3,500$, which exceeds \$3,000.

²⁸ Note the contrast with the situation in which advice was definitive; in that situation, recall, advice was desirable independent of the magnitude of expected sanctions. There, a party who would not commit an act in the absence of advice would be led by advice to commit it only if he were advised that the act was definitely not sanctionable. Here, as just explained, however, a party could be led to commit an act merely because the advice is that the act is more unlikely to be sanctionable than he had thought—which leaves open the possibility that it is sanctionable. For this latter reason, it is important here, but was not before, that the party with advice face an appropriately high expected sanction if the act is sanctionable. That is why here, but not before, it matters whether the expected sanction is fully equal to the harm.

duction might say to himself, "I will claim the deduction if my legal advisor informs me that the likelihood of its impermissibility is low. But since the deduction may still turn out to be impermissible, I am glad that my advisor will not go to the tax authorities and suggest they audit my tax return. Indeed, if my advisor might do that, I might not consult him."

As this should make clear, the expected value to a person of protection of confidentiality inheres entirely in the possibility that he will decide, on the basis of advice, to commit an act that turns out to be sanctionable. Hence, the extent to which protection of confidentiality encourages parties to obtain legal advice will depend on how likely they believe they are to decide to commit sanctionable acts after obtaining advice.

Social Desirability of Protection of Confidentiality. Since protection of confidentiality encourages parties to obtain legal advice, protection of confidentiality will result in socially desirable changes in behavior if expected sanctions equal the harm that results from sanctionable acts.

However, where expected sanctions are less than the harm done by acts, legal advice and thus protection of confidentiality may or may not lead to socially desirable behavior. Specifically, one must consider the effect of protection of confidentiality on two groups of parties. The first group consists of those who would obtain legal advice even without protection of confidentiality. Protection of confidentiality can have only a socially undesirable effect on the behavior of this group; for, since confidentiality will prevent the expected sanction from rising to a more appropriate level, confidentiality can lead only to parties committing undesirable acts that they would not have committed in the absence of confidentiality. The second group is those who will obtain legal advice only if there is protection of confidentiality. Protection of confidentiality for this group may or may not have a socially undesirable effect since, as stated, the provision of legal advice may or may not have that effect.²⁹

B. Parties Are Uncertain about the Magnitude or Probability of Sanctions

In this section, it will be assumed that parties know which acts are sanctionable and that they will therefore commit acts that are not sanctionable.

²⁹ In the present case, Bentham's argument against protection of confidentiality is not really applicable since it does not address the situation where, after obtaining legal advice, parties do not know whether their acts will be sanctionable. This, recall, was part (a) of the general response to Bentham. However, part (b) of the response—that protection of confidentiality is good because it encourages parties to obtain legal advice—is not necessarily a correct response. It is not necessarily correct because, as we have seen, the provision of legal advice is not always good. The response is also incomplete because it overlooks the effect protection of confidentiality has on those who would have obtained advice even in the absence of protection.

tionable. The parties' only uncertainty will be over the magnitude or probability of sanctions applying where acts are sanctionable, and attention will thus be restricted to sanctionable acts. Suppose, for instance, that in example 1, the plant owner knows that discharging the waste product will violate the ordinance but is unsure of the penalty for a violation; or suppose that the person in example 2 realizes that the tax deduction is impermissible but is not clear about the audit probability or the size of the possible penalty. Because such uncertainty is in many respects similar to uncertainty about whether acts are sanctionable, it can be briefly treated.

Behavior in the Absence and in the Presence of Legal Advice. The Decision to Obtain Advice. In the absence of legal advice about the probability or magnitude of sanctions, a party will decide whether to commit a contemplated sanctionable act by comparing his estimate of the expected sanction to the expected gain from the act. If the person in example 2 is unsure of the audit probability, he will estimate the likelihood of different possible audit probabilities, calculate the expected gain and the expected penalty, and make his decision whether to claim the deduction accordingly.³⁰ The expected value of advice is determined in the manner specified earlier. A party will multiply the probability that advice will lead him to alter his behavior by the expected benefit he will obtain from his altered behavior. He will obtain advice if its cost is less than its expected value.

Social Desirability of Legal Advice. The conclusions here parallel those in Section II.A.2., in which advice was sought regarding the likelihood that acts were sanctionable. That is, the provision of legal advice about the probability and magnitude of sanctions will lead to socially desirable changes in behavior if the probability and magnitude of sanctions are set so that expected sanctions equal the harm that results from acts. In that event, informed parties will be induced to behave in a socially desirable way, whereas, if parties do not obtain legal advice and incorrectly estimate expected sanctions and thus the expected harmfulness of acts, they may decide to commit undesirable acts or they may decide not to commit desirable acts.

On the other hand, the provision of legal advice may or may not promote socially desirable behavior when the probability and magnitude of sanctions is less than the harm caused by acts. The possibility that the

³⁰ Suppose, for instance, that the person believes that the audit probability is either 30 percent or 90 percent, and he thinks that the two possibilities are equally likely. Then, if he claims the deduction, the expected penalty will be $(.50 \times .30 + .50 \times .90) \times \$10,000 = .60 \times \$10,000 = \$6,000$, and the expected gain will be $.40 \times \$20,000 = \$8,000$, so he will claim the deduction.

provision of legal advice will be undesirable arises because it may lead parties to commit undesirable acts that they would not otherwise have committed because they overestimated expected sanctions.

Effect of Protection of Confidentiality. Protection of confidentiality will raise the willingness of parties to obtain legal advice for essentially the same reason it did in Section II.A.2. Parties will reason that they may, on the basis of advice, decide to commit sanctionable acts. Hence, they will be better off and will value advice more if the probability or magnitude of sanctions is not increased as a consequence of their obtaining advice.

Social Desirability of Protection of Confidentiality. As in Section II.A.2., protection of confidentiality will lead to socially desirable changes in behavior when expected sanctions equal the harmfulness of acts, but it may or may not encourage desirable behavior when expected sanctions are lower.³¹

C. Parties Wish to Lower the Probability or Magnitude of Sanctions

It will be assumed here that parties know which acts are sanctionable and what the usual probability and magnitude of sanctions are but that they can lower the probability or magnitude of sanctions if they obtain certain advice. For instance, suppose in example 2 that the person can obtain advice from his legal advisor, enabling him to reduce the probability of a tax audit.³²

Behavior in the Absence and in the Presence of Legal Advice. The Decision to Obtain Advice. A party will, as before, decide whether to commit a contemplated sanctionable act on the basis of the expected gain and the expected sanction. The difference that the type of advice now under consideration will make is that it will lower the expected sanction and thus make it more likely that the party will commit the act. Advice will be valuable to the party whenever, given advice, he will commit the

³¹ In the case just considered, Bentham's argument overlooks the possible advantage of protection of confidentiality for the simple reason that his argument does not take into account two things: that committing a sanctionable act may sometimes be desirable and that a party who is encouraged to obtain legal advice may decide not to commit an undesirable sanctionable act because he learns the expected sanction is higher than he had thought. The general response to Bentham overlooks the factors that were mentioned in note 29 *supra*.

³² He might be told that, by changing the place on the tax return where he claims the deduction (for instance, in the place for miscellaneous deductions rather than in the place for deductions for business expenses), the audit probability will be significantly lowered or that, if he appends a statement to his return, the probability will be similarly reduced.

Advice may also enable a person to lower the sanction for a given act, for example, by allowing him to better conceal evidence that would have helped to establish intent.

act. The party will obtain advice when its cost is less than its expected value.

Social Desirability of Legal Advice. The provision of legal advice that lowers the probability or magnitude of sanctions is socially undesirable because it can lead only to an increased number of socially undesirable acts.

Effect and Social Desirability of Protection of Confidentiality. The effect of protection of confidentiality is plainly to encourage individuals to obtain the type of legal advice under consideration. Since, as just observed, provision of this advice is socially undesirable, protection of confidentiality is socially undesirable.³³

III. CONCLUDING DISCUSSION

This section will summarize the conclusions from the model, note a significant omission from the analysis, review the law governing the confidentiality of attorney-client communications about planned acts, and comment on the sense, or lack thereof, that this law makes.

A. Summary of Conclusions from the Model: Prediction of Behavior

With regard to prediction of parties' behavior, several points were developed in the model. First, a party will choose to engage in a contemplated act if the benefit would outweigh the expected sanction that might be associated with the act. Second, a party will decide to obtain legal advice about an act on the basis of a comparison of the cost of advice with its value, namely, any advantages flowing from an advice-induced change in his decision about whether to commit the act, discounted by the likelihood of his receiving advice that leads to such a change. Parties' decisions about whether to obtain legal advice and whether to commit acts were illustrated in several numerical examples, indicating, it is hoped, the potential for making realistic predictions.³⁴

Third, the value to a party of protection of confidentiality inheres in the possibility that, *after* he obtains advice, he will decide to commit an act for which he might be sanctioned. It is only in this circumstance that his legal advisor's not communicating with enforcement authorities will do

³³ In the present case, Bentham's argument is correct. The general response to him is incorrect because, although protection of confidentiality encourages parties to obtain legal advice, the provision of advice is socially undesirable.

³⁴ Given data on the cost of legal services and on the character of information individuals possess in the absence of advice (obtained, perhaps, through survey sampling), it should be possible to estimate the demand for legal advice.

him good. Hence, protection of confidentiality will be most valuable to parties and will most encourage them to obtain legal advice when legal advice is unclear or when the level of sanctions is inadequate, for, if either is so, then, after obtaining advice, parties will often decide to engage in acts that may turn out to be sanctioned. On the other hand, protection of confidentiality will be least valuable when the opposite is true. The extreme case is where legal advice about whether acts are sanctionable is definitive. In this case, parties who choose to obtain advice will not commit acts that they learn are sanctionable, and protection of confidentiality will therefore have no effect on the decision to obtain legal advice.

B. *Summary of Conclusions from the Model: Social Desirability of Legal Advice and Protection of Confidentiality*

The answer to the question of when provision of advice and, equally, of when protection of confidentiality will result in socially desirable changes in parties' behavior, depends on the type of advice parties seek. First, when advice is sought regarding whether acts are sanctionable and the advice is definitive, then advice can lead only to desirable changes in behavior. Legal advice is sometimes exactly of this character; where the law is settled, this will often be so.

Second, when the law is not clear or when advice concerns the magnitude or probability of sanctions, whether advice will lead to desirable changes in behavior will depend on the level of expected sanctions. If the level of expected sanctions equals the expected harmfulness of acts, advice will be socially desirable: parties with advice will be led to take into correct account the harmfulness, if any, of their acts because they will know the expected sanctions associated with their acts. Hence, one would usually expect provision of legal advice about tort, contract, and much regulatory law to be socially desirable, for, in principle, damages and often penalties for violations are supposed to equal the harm done, and violations will frequently be noticed and sanctioned or settlements paid.

On the other hand, if the level of expected sanctions is less than the expected harmfulness of acts, advice may or may not lead to desirable changes in behavior. Advice will not lead to desirable behavior if, without advice, parties would overestimate the level of expected sanctions, and that would lead them to act more appropriately than they would with advice; advice will lead to desirable behavior, however, if parties initially underestimate the level of expected sanctions. When will the level of expected sanctions be too low to induce informed parties to behave desirably? One supposes that this could sometimes be true in the area of tort,

contract, or regulatory enforcement,³⁵ and that it will very often be true in the area of crime. Thus, in these areas, answering the question of whether advice about contemplated acts will lead to undesirable or desirable changes in behavior will require us to know how parties' initial beliefs concerning the level of expected sanctions diverge from their actual level.

Third, when advice helps to lower (rather than only to inform about) the probability or magnitude of sanctions, advice can lead only to the commission of undesirable acts and is therefore undesirable.

C. *Behavior of Legal Advisors*

The behavior of legal advisors was not analyzed in the model, and two important questions about it arise. Namely, what are the incentives to legal advisors to keep confidential or to disclose information about their clients? And how effectively can legal advisors' behavior in these respects be controlled?

As a general matter, one suspects that legal advisors will not wish to disclose information that their clients want held confidential, since the advisors will wish to please their clients. Therefore, it seems that legal advisors would usually have to be legally required to reveal information for that to be accomplished, and enforcement would have to rely on the discovery of communications that establish that advisors knew their clients' plans. Demonstrating this might be difficult, since what would be at issue is a kind of behavior (frequently, mere verbal communications) and about which there would often be no evidence that the involved parties would ordinarily want to conceal. Consequently, the ability to enforce requirements that legal advisors disclose information is circumscribed.³⁶

There may, however, be occasions in which it will be in a legal advisor's self-interest to disclose information. For example, by reporting that a client is about to perpetrate a securities fraud, it is conceivable (although admittedly unlikely) that a legal advisor would better his reputation in the community of potential victims and would profit sufficiently from greater future business from them to justify disclosure. In addition, a legal advisor's public reputation might be enhanced by revealing certain

³⁵ Consider difficulties in establishing causation (allowing a tortfeasor or violator to go free), the judgment proof problem (weakening deterrence in any setting), and patently incorrect sanctions for regulatory infractions (a small fine for failure to repair a crack in a dam).

³⁶ I do not want to overstate this point, however. There will occasionally be evidence of communications, such as recordings of conversations or documents. In addition, there may be an opportunity to enforce rules mandating disclosure through use of undercover agents. The agents would pose as clients and make statements that advisors would be required to disclose. Finally, the threat of barring a legal advisor from engaging in his profession is a very severe one and might therefore aid enforcement even if the likelihood of an advisor being sanctioned is small.

information, and, of course, his notions of morally proper behavior might lead him to do the same.

Where, for reasons such as these, a legal advisor wishes to disclose information, it may be that a rule against disclosure applies. Enforcement of such a rule appears straightforward if an advisor reveals his own identity when making a disclosure, for the advisor could then be sanctioned, and his disclosure could also be ignored by courts and even by police or other authorities (although it would not be by victims). If, however, a legal advisor would make an anonymous disclosure, it might be difficult to sanction him. Still, in some cases, an inference that he was the source of information could be made. Also, an anonymous disclosure might not be believed; even if believed, anonymity might deny the legal advisor the benefit (an enhanced reputation) that he seeks from disclosure. Thus, the situation is complex, but the ability to enforce a rule against disclosure appears to be substantially greater than the ability to enforce a rule requiring disclosure.

A remark about the collective incentive of legal advisors—that is, of their professional associations—should be added. Other things being equal, one would expect a professional association of legal advisors to favor policies that increase the demand for advisors' services. Thus, one would expect a professional association to favor rules preserving confidentiality.³⁷ This bias may be important because professional associations may strongly influence the rules regarding confidentiality and, as just argued, because there are real possibilities for enforcing rules against disclosure.

D. *The Law Regarding Attorney-Client Communications about Planned Acts*

In the United States, the law is roughly this.³⁸ (i) Attorneys are generally *not obligated to disclose* planned acts of clients communicated to

³⁷ While association committees responsible for drafting rules may be composed of the most civic-minded individuals, what the committees propose can be voted down by an association's membership (see note 39 *infra*), and, in any event, the committees may, anticipating the response from the membership, propose only what they think will be acceptable to the membership.

³⁸ The law is not easy to summarize because some states have adopted the American Bar Association (ABA) Model Code of Professional Responsibility [hereinafter cited as Code] and others (a minority), the ABA's 1983 revision of the Code, the Model Rules of Professional Conduct [hereinafter cited as Rules]. Moreover, states have often modified the Rules or the Code. In addition, the meaning and interpretation of the rules within a given state may be uncertain. A further complication is that the rules applying with respect to disclosure of information by an attorney outside court (for example, to police or to a potential victim) may differ from the rules concerning an attorney's disclosures in court. For example, an attorney might be forbidden from revealing information outside of court, but he may have the obligation to do so in court.

them in confidence.³⁹ (ii) Attorneys in all states have the *discretion to disclose* clients' planned acts if the acts are crimes threatening serious bodily injury; in most states, attorneys have the discretion to disclose any type of crime or fraud.⁴⁰ (iii) Attorneys generally *cannot disclose* information about other planned acts, such as an intention to commit a breach of contract or much behavior that could give rise to a tort. Furthermore, in some states, attorneys cannot disclose information about any planned act unless it is a crime threatening serious bodily injury.⁴¹ (iv) However, an attorney's obligation not to disclose a planned act might not apply if he gains his information inadvertently (for example, if he overhears his client talking to another person), if a third party who would not be expected to maintain confidentiality is present when the client speaks to the attorney, if the attorney has been drawn into assisting an illegal act, or if the client waives the privilege of confidentiality. In such cases, attorneys may have the discretion to disclose planned acts.⁴²

E. *The Law in Light of the Analysis*

What do the conclusions from the model suggest about the social desirability of the law described above? The conclusion that protection of confidentiality is undesirable when a client's purpose is to obtain advice enabling him to evade the law by lowering expected sanctions implies that it may be advantageous for attorneys to have a duty to disclose certain planned acts. Thus, a duty to disclose might be desirable when an individual obtains advice from his attorney helping him to conceal capital gains from the tax authorities or when a client corporation obtains advice about the timing of inspections at its factory that will allow it to avoid being caught for violations.⁴³ That the law does not impose an obligation on

³⁹ There is, however, an exception concerning proceedings at court. An attorney may be obligated to disclose to the court a client's plan to deceive the court; see Rule 3.3(a)(2) of the Rules; and DR 7-102(A)(3) of the Code, *supra* note 38. Also, some states have introduced their own provisions requiring attorneys to make certain disclosures, as noted in Andrew Kaufman, Problems in Professional Responsibility 190 (2d ed. 1984). It should also be mentioned that, according to a rejected version of the Rules, attorneys were required to disclose clients' plans to commit acts that would result in death or serious bodily harm. See the discussion in Kaufman, *supra* 189-91.

⁴⁰ See Rule 1.6(b) of the Rules; and DR 4-101(C) of the Code, *supra* note 38.

⁴¹ See Rule 1.6(a) of the Rules; and DR 4-101(B) of the Code, *supra* note 38.

⁴² This is based in part directly, and in part inferentially, on Rules 1.2(d) and 1.6 of the Rules; and DR 4-101(A-C) of the Code, *supra* note 38. See also §§ 89, 91, and 93 of McCormick; and §§ 6.3-4 of Wolfram, *supra* note 5.

⁴³ An attorney is not supposed knowingly to aid a client in evading the law in such ways as these. But attorneys may not discover how their clients will thereby be aided until after they have supplied information or performed a service.

attorneys to disclose clients' plans in such situations, or that it may forbid disclosure, raises questions.⁴⁴

Another conclusion was that it is unclear whether protection of confidentiality is undesirable or desirable when advice, while not enabling clients to evade the law, provides information about expected sanctions and the sanctions are not high enough to ensure that parties will act desirably. The model does not suggest, therefore, whether attorneys ought to disclose or keep secret clients' plans to commit crimes or other acts for which expected sanctions might be thought inadequate. To make a recommendation, data are needed on the effects of confidentiality versus disclosure on the incidence of these acts, yet essentially no data exist.⁴⁵ Moreover, intuition about the effects does not furnish me, at least, with real guidance. I can easily adduce reasons why more bad acts would be prevented if attorneys were obligated to disclose clients' plans,⁴⁶ and I can also adduce quite plausible reasons why more bad acts would be prevented were attorneys forbidden from disclosing clients' plans.⁴⁷

⁴⁴ It is true that enforcement of a requirement to disclose would require courts to differentiate between situations such as these and situations in which attorneys were merely supplying information about the probability or magnitude of sanctions. While this would often be a difficult task, it would not always be so. Suppose, to elaborate on the example mentioned above, that a court determined that an attorney learned that the information he supplied about the timing of inspections (that they occurred only during the day) would allow a corporation to adopt a definite strategy to avoid detection (dumping toxic wastes at night) and that the corporation would probably do this. Then the attorney could be found liable for failure to disclose. If the court knew only that the attorney had given the general odds of inspection but not that the corporation could or would adopt a particular strategy to lower the odds, then the attorney would not be found liable for failure to disclose.

⁴⁵ The only study of which I am aware is described in Functional Overlap between the Lawyer and Other Professionals: Its Implications for the Privileged Communications Doctrine, Note, 71 Yale L.J. 1261-73 (1962). The study reported on a survey of the opinions of laymen, attorneys, judges (and accountants, psychiatrists, and other professionals) as to the effects of rules of confidentiality. This, it need hardly be said, is not the sort of information normally relied on in social scientific empirical research. Such research is usually based on observation of actual changes in behavior, not somebody's predictions of changes in behavior.

⁴⁶ The argument might run along the following lines. Most individuals who disclose plans to commit bad acts are either crazy or stupid. In either case, attorneys are unlikely to convince the individuals not to commit murder. Therefore, disclosure to police or to the potential victims of the individuals' plans may prevent bad acts. Further, since attorneys are themselves unlikely to be able to convince individuals not to commit bad acts, the fact that a policy mandating disclosure may discourage some individuals from revealing their plans to attorneys cannot be counted as the loss of a valuable opportunity. Finally, if most individuals who disclose plans to commit bad acts are crazy or stupid, perhaps they will be unaware of an obligation attorneys might have regarding disclosure.

⁴⁷ The argument, of course, is this. Most individuals will not disclose plans to commit bad acts if they think that attorneys will, or are even allowed to, disclose this information. If individuals do disclose plans to commit bad acts, however, they can often be convinced not to carry them out. Indeed, the type of person who would ever admit his plans to an attorney

I should add that I see no obvious justification for distinguishing the treatment of attorneys' information about clients' plans to commit many "lesser" bad acts from attorneys' knowledge of plans to commit such serious crimes as murder. To be sure, murder is more important to prevent than robbery, fraud, and the like. But how does this bear on the question of whether a policy of disclosure or of confidentiality will result in prevention of more bad acts? It is not apparent. With regard to bad acts, the main advantage of disclosure, we know, is that individuals who see and are not dissuaded from acting by attorneys in the absence of disclosure may be led to change their minds or may be prevented from acting by disclosure. The main advantage of confidentiality is that more individuals will discuss their plans with attorneys and then may decide against acting. I do not see why the comparison of these advantages should be influenced in a general way by the gravity of the bad act.

Nevertheless, the law and many commentators seem to agree that disclosure is more appropriate for serious crimes than for lesser ones. The explanation probably lies in a disposition to think first of the direct effect of disclosure—that, in the case at hand, disclosure may prevent an identified harm from being done (a known individual from murdering another individual)—and, in an accompanying reluctance to count properly the unseen, indirect effects of disclosure on incentives to reveal information to attorneys.

An additional conclusion from the model is that protection of confidentiality is desirable when expected sanctions are sufficient to induce informed parties to behave desirably. From the perspective of this conclusion, it makes some sense that attorneys must not disclose information about planned breaches of contract and also about certain tortious behavior and behavior that would or might with some probability violate certain regulations, for, as noted earlier, the expected sanctions for such acts should often approximate the harm in which they result. At the same time, and as was also suggested before, there will be some such acts for which expected sanctions are too low (the small fine for leaving unpaired a crack in a dam). That attorneys may well be obligated to maintain confidentiality about clients' plans of this type (instead, say, of having discretion to report them) gives one pause.

A final point about the law that was not addressed directly in the model should be added. There is an obvious reason why attorneys should not be

might be the type of individual who wants, consciously or subconsciously, to be dissuaded, for why else would he discuss his plans? Hence, making it impermissible for attorneys to disclose plans to commit bad acts could significantly increase the number of people who both disclose such plans and who are convinced by their attorneys not to commit bad acts.

obligated to keep confidential information that they obtain inadvertently, in the presence of third parties not expected to maintain confidentiality, or from clients who waive the privilege of confidentiality. The possibility that attorneys will disclose such information should have little or no effect on parties' incentives to seek legal advice. A person will probably not expect to be overheard any more by his attorney than by others, so this factor will not weigh much in his calculation of whether to obtain legal advice. Likewise, a person's decision as to whether to obtain legal advice will be unlikely to be affected by the chance of his attorney's disclosure if he is willing to allow the presence of third parties who would not necessarily be expected to maintain confidentiality. And plainly, if a person is willing to allow disclosure, then he will hardly be discouraged from seeking advice if there is disclosure.

APPENDIX

FORMAL ANALYSIS OF THE MODEL

The assumptions are essentially those discussed informally in Section II. Risk-neutral parties contemplate engaging in acts that will yield them a gain, that may do harm, and that may be sanctionable.⁴⁸ Parties may obtain legal advice before deciding whether to commit acts. Specifically, let

- g = gain to a party from committing an act; $g > 0$;
- h = harm due to committing an act; $h \geq 0$;
- s = magnitude of the sanction applying if a sanctionable act is sanctioned; $s \geq 0$;
- p = probability of imposition of a sanction for a sanctionable act; and
- c = cost of legal advice; $c \geq 0$.

A party's initial knowledge and the nature of the legal advice he may obtain will be described below.

Assumptions about the social desirability of acts and the relation between sanctions and the social desirability of acts are as follows. An act will be considered socially desirable if it results in a gain exceeding the harm. Acts that cause no harm will not be sanctionable. Thus, it will be socially desirable for parties to

⁴⁸ Gains, harm, and sanctions are assumed to be monetary or to have monetary equivalents; it will be obvious that the qualitative nature of the results do not depend on this assumption. Also, gains will be assumed to be obtained with certainty if an act is committed, rather than only if a sanction is not imposed. This assumption, however, amounts merely to one of convenient formulation. A situation in which a gain of g is enjoyed only if a sanction s is not imposed is equivalent to a situation in which g is enjoyed with certainty, and the sanction is $s + g$. (Conversely, a situation in which g is enjoyed with certainty, and the sanction is s , is equivalent to a situation in which g is enjoyed only if a sanction is not imposed, and the sanction is $s - g$.) Thus, the second example of the text, in which it was assumed that a party would benefit from claiming a tax deduction only if he was not sanctioned, is described by the model studied here.

commit such acts. Acts that cause actual harm will be sanctionable, and the expected sanction for such acts, ps , will be less than or equal to the harm h . It follows that if $ps = h$, it will be socially desirable for sanctionable acts to be committed if and only if $g > ps$. If $ps < h$, it may be socially undesirable for an act to be committed even if $g > ps$; for only if $g > h$ will it be socially desirable for an act to be committed. The analysis will appear in three parts, as in Section II.

A. Parties Are Uncertain Whether Acts Are Sanctionable

It will be assumed here that parties do not know whether contemplated acts are sanctionable in the absence of legal advice and that parties know the probability p and sanction s applying if an act is sanctionable.

1. Case in Which Legal Advice Is Definitive

Here it will be supposed that legal advisors will tell parties for sure whether acts are sanctionable. Let q = party's subjective probability that an act is sanctionable. If a party does not obtain advice, he will commit an act if⁴⁹

$$g > qps, \quad (A1)$$

in which case his expected net gain will be $g - qps$; otherwise he will not commit an act, and his gain will be 0.

If a party obtains advice and is told that an act is not sanctionable, he will commit it and obtain g . If he is told that an act is sanctionable, he will not commit it if

$$g \leq ps. \quad (A2)$$

Hence, if (A2) holds and a party obtains advice, his expected net gain will be

$$(1 - q)g; \quad (A3)$$

and if (A2) does not hold and he obtains advice, his expected net gain will be

$$g - qps. \quad (A4)$$

Given the foregoing, the expected value of advice—the expected net gain if advice is obtained less the expected net gain if it is not—can be calculated. If (A2) does not hold, then clearly (A1) must hold; therefore, the expected value of advice will be $(g - qps) - (g - qps) = 0$. (As discussed in Section II.A.1., the explanation is that, if (A2) does not hold, the party will commit the act whether or not he learns it is sanctionable; advice will thus be valueless since it will not lead to a change in behavior.) If (A2) and (A1) hold, the expected value of advice will be

$$(1 - q)g - (g - qps) = q(ps - g), \quad (A5)$$

that is, the expected savings in sanctions avoided net of gains if the party learns that the act is sanctionable and does not commit it. If (A2) holds and (A1) does not hold, the expected value of advice will be

$$(1 - q)g, \quad (A6)$$

⁴⁹ It will be assumed for concreteness that, if $g = qps$, a party will not commit an act, and similar assumptions will be made below without comment.

the expected gain if the party learns the act is not sanctionable and thus does commit it.

Hence, a party will not obtain advice if (A2) does not hold; otherwise, he will obtain advice if its value, as given by (A5) or (A6), exceeds c .

The provision of advice can lead only to socially desirable changes in behavior. From what has been said, it is evident that advice can lead to only two types of changes in behavior. On the one hand, a party may decide to commit an act that is not sanctionable that he would not have committed in the absence of advice. That would be socially desirable given the assumption that acts that are not sanctionable cause no harm. On the other hand, a party may decide not to commit an act that is sanctionable that he would have committed in the absence of advice. That would be socially desirable, since, if a party decides on the basis of advice not to commit a sanctionable act, then $g \leq ps \leq h$.

To this point, it has been assumed that the probability or magnitude of sanctions will not rise as a consequence of obtaining advice, in other words, that confidentiality of communications with legal advisors is protected. Assume now that there is no protection of confidentiality, so that, if a party obtains legal advice, the probability or magnitude of sanctions will rise. Let p' , s' = probability and magnitude of sanctions, respectively, if there is no protection of confidentiality and a party obtains legal advice; $p's' > ps$. Lack of protection of confidentiality will not affect parties' behavior under any circumstances. To see why, let us show that in each possible situation there will be no change in behavior.

Suppose first that (A2) does not hold. In that situation, the value of advice was 0 before, so that a party would not obtain advice, and he would commit the act. In the absence of confidentiality, if (A2) does not hold, there are two possibilities: either $g > p's'$, or $g \leq p's'$. If $g > p's'$, then, since a party will commit his act even if he learns that it is sanctionable, the expected value of advice will be $(g - qp's') - (g - qps) = q(ps - p's') < 0$; advice would have negative expected value and would not be obtained. (The apparent peculiarity that advice has negative expected value is due to the fact that, if the act is sanctionable, the expected sanction rises owing to advice.) If $g \leq p's'$, then, since a party will not commit his act if he learns it is sanctionable, the expected value of advice will be (A5), which will be negative. Thus, in this case as well, a party will not obtain advice and will commit his act.

Now assume that (A2) and (A1) hold. Recall that before, a party would obtain advice if (A5) exceeded c and would commit the act only if he learned it was not sanctionable. If (A5) did not exceed c , he would commit the act. In the absence of protection of confidentiality, since (A2) holds, $g < p's'$. Hence, if a party obtains advice and learns his act is sanctionable, he will not commit it. Therefore, if he obtains advice, he will behave as before, and, if he does not obtain advice, he will obviously behave as before. As a consequence, (A5) will, as before, be the expected value of advice. Hence, a party will obtain advice if and only if (A5) exceeds c and will behave the same as before.

Finally, assume that (A2) holds and that (A1) does not hold. Then, as before, a party would obtain advice if (A6) exceeded c and would commit the act only if he learned it was not sanctionable. If he did not obtain advice, he would not commit the act. In the absence of protection of confidentiality, for reasons analogous to those given in the preceding paragraph, if a party obtains advice, he will commit the act only if he learns it is not sanctionable. Therefore, as before, a party will obtain advice if and only if (A6) exceeds c , and will behave identically.

PROPOSITION 1. In the case where legal advice concerns whether an act is sanctionable, and the advice will be definitive, (a) a party's decision whether to obtain advice is as described in the paragraph containing expressions (A5) and (A6), (b) protection of confidentiality will have no effect on parties' behavior, and (c) the provision of legal advice can lead only to socially desirable changes in behavior.

2. Case in Which Legal Advice Is Not Definitive

Now assume that legal advice is in the form of a probability that an act is sanctionable. Let

t = probability that an act is sanctionable as reported by a legal advisor to a party who obtains advice; and
 $f(t)$ = party's probability density over advice t .

Thus, note, we have the identity

$$q = \int_0^1 tf(t)dt.$$

As in the preceding case, if a party does not obtain advice, he will commit an act if $g > qps$, and his net expected gain will be $g - qps$.

If a party obtains advice and confidentiality is protected, he will commit an act if $g > tps$; hence, his net expected gain will be

$$\int_0^{g/ps} (g - tps)f(t)dt; \quad (A7)$$

exp. (A7) less $g - qps$ (if $g > qps$) or 0 (if not) is then the expected value of advice.

With regard to the social desirability of legal advice, suppose, as is natural, that t is the best information available to the party and that it is socially desirable for an act to be committed if and only if $g > th$. Then if $ps = h$, legal advice will be desirable because with advice parties will act desirably but might not otherwise. On the other hand, if $ps < h$, legal advice may or may not be socially desirable. Advice may be desirable, since it may sometimes lead parties not to commit undesirable acts that they would otherwise commit, and advice may be undesirable, since it may also lead parties to commit undesirable acts that they would not otherwise have committed.⁵⁰

⁵⁰ To see that advice can be undesirable when $ps < h$, consider a simple discrete example: $g = 10$; $t = .6$ with probability 50 percent; and $t = 1$ with a probability of 50 percent; $p = .5$; $s = 30$; and $h = 20$. Here it is socially undesirable for the act to be committed, as it is undesirable for it to be committed if $t = .6$ (since $10 = g < th = .6 \times 20 = 12$) or if $t = 1$ (since $10 < 20$). The act will not be committed in the absence of advice, since the expected sanction will be $.8 \times .5 \times 30 = 12 > 10$. Yet, if advice is obtained, then if $t = .6$, the act will be committed, since $.6 \times .5 \times 30 = 9 < 10$. Hence, advice is socially undesirable.

To see that advice can be desirable when $ps < h$, consider a modification of the previous example; the modification will be such that, in the absence of advice, a party will commit the act, yet given advice, he will not commit the act in the case where he learns $t = 1$. Assume that the probability that $t = .6$ is 90 percent. Then, in the absence of advice, the party will

If a party obtains advice and there is no protection of confidentiality, he will commit an act only if $g > tp's'$ —less often than if confidentiality is protected—and his net expected gain will be

$$\int_0^{g/p's'} (g - tp's')f(t)dt. \quad (A8)$$

This is smaller than exp. (A7) since $p's' > ps$. Thus, the expected value of advice will be lower, and parties will obtain advice less often when there is no protection of confidentiality.

Since protection of confidentiality results in parties obtaining legal advice more often, protection of confidentiality will be socially desirable if $ps = h$, and protection of confidentiality may or may not be desirable if $ps < h$.⁵¹

PROPOSITION 2. In the case in which legal advice concerns whether an act is sanctionable and the advice will be in the form of a probability, (a) a party's decision whether to obtain advice is as described in the paragraph containing exp. (A7), (b) protection of confidentiality will lead parties to obtain legal advice more often than they otherwise would, and (c) provision of legal advice and protection of confidentiality will lead to socially desirable changes in behavior if expected sanctions are adequate ($ps = h$), but they may or may not lead to desirable changes if expected sanctions are inadequate ($ps < h$).

B. Parties Are Uncertain about the Magnitude or Probability of Sanctions

In this part, it will be assumed that parties are uncertain about the magnitude or probability of sanctions but do know which acts are sanctionable. Thus, parties will seek legal advice only about sanctionable acts, and attention will be confined to these acts. If a party obtains legal advice about a sanctionable act, it will be supposed that he will learn the true probability and magnitude of sanctions. Let $h(p,s)$ = party's probability density over p and s .

If a party does not obtain legal advice about an act, he will commit the act if $g > E(ps)$ (where E is the expectation operator), and $g - E(ps)$ will be his expected net gain; otherwise, his gain will be 0.

If a party obtains legal advice about an act, he will commit the act if $g > ps$, and his expected net gain will be

commit the act, since the expected sanction will be $(.9 \times .6 + .1 \times 1) \times .5 \times 30 = .64 \times .5 \times 30 = 9.6 < 10$. However, given advice, the party will decide not to commit the act if he learns that $t = 1$ since $1 \times .5 \times 30 = 15 > 10$.

⁵¹ To see that protection of confidentiality might be undesirable when $ps < h$, observe that, in note 50 *supra*, it was assumed that there was confidentiality—since p was assumed to be .5 regardless of whether advice was obtained. In the example of the first paragraph of the note, we saw that, if advice was obtained, that was socially undesirable. It is also clear from that example that advice has positive value to the party. Thus, if the cost of advice is low enough, the party will obtain advice. But, in the absence of protection of confidentiality, the party might not obtain advice (for example, suppose that p would rise to 100 percent if the party obtained advice). Hence, protection of confidentiality might be undesirable. To see that protection of confidentiality might be desirable, a similar scenario can be described with the example of the second paragraph of note 50 *supra*.

$$\int_0^{g/p} (g - ps)h(p,s)dpds. \quad (A9)$$

The expected value of advice equals (A9) less $g - E(ps)$ or 0, as the case may be, and the party will obtain advice if its expected value exceeds c .

The provision of legal advice will be socially desirable if $ps = h$, for, in that situation, parties with advice will commit acts if and only if $g > h$. However, if $ps < h$, the provision of legal advice may or may not be socially desirable.⁵²

If there is no protection of confidentiality, the probability density of $p's'$ will clearly be to the right of the density of ps . Hence, if parties obtain legal advice, parties will commit acts less often, and the expected value of legal advice will decline. Therefore, parties will obtain legal advice less often.

Because protection of confidentiality will induce parties to obtain legal advice more often, and because the advice will necessarily be desirable only if $ps = h$, protection of confidentiality will necessarily be desirable only if $ps = h$; if $ps < h$, confidentiality may or may not be desirable.⁵³

PROPOSITION 3. In the case where legal advice concerns the probability or magnitude of sanctions, (a) a party's decision whether to obtain advice is as described in the paragraph containing (A9), (b) protection of confidentiality will lead parties to obtain advice more often than they otherwise would, and (c) provision of legal advice and protection of confidentiality will lead to socially desirable changes in behavior if expected sanctions are adequate ($ps = h$) but may or may not lead to desirable changes if expected sanctions are inadequate ($ps < h$).

C. Parties Wish to Lower the Probability or Magnitude of Sanctions

It will be assumed here that parties can obtain legal advice that will reduce the probability or magnitude of sanctions from their usual levels. It will also be assumed that parties know which acts are sanctionable so that, again, attention will be restricted to sanctionable acts. Let $\bar{p}, \bar{s}$ = the probability and magnitude of sanctions given advice on how to lower them; $\bar{p}\bar{s} < ps$.

If a party does not obtain legal advice about a sanctionable act, he will commit the act if $g > ps$, and, if he does obtain advice, he will commit the act if $g > \bar{p}\bar{s}$ and thus more often. If $g > \bar{p}\bar{s}$, the expected value of advice will be $ps - \bar{p}\bar{s}$ in the case

⁵² To see that advice could be undesirable, assume as in the first paragraph of note 50 *supra*, except that $s = 32$ with probability 50 percent and that $s = 16$ with probability 50 percent. Then the party will not commit the act in the absence of advice, since the expected sanction will be $.5 \times (.5 \times 32) + .5 \times (.5 \times 16) = 12 > 10$. However, if he obtains advice, the party will commit the act if $s = 16$. Hence, advice will be undesirable.

An example in which advice is desirable is the following. Assume as in the paragraph above, except that the likelihood of $s = 32$ is 10 percent and the likelihood of $s = 16$ is 90 percent. Then, in the absence of advice, the party will commit the act, since the expected sanction will be $.1 \times (.5 \times 32) + .9 \times (.5 \times 16) = 8.8 < 10$. On the other hand, if he obtains advice, the party will not commit the act if $s = 32$.

⁵³ In the examples of note 52 *supra*, it was assumed that there was protection of confidentiality. If there is not, the party may be discouraged from seeking advice and will therefore act in the way a person without advice will act. Hence, examples can be constructed in which protection is desirable and in which it is not.

where $g > ps$ (the act would have been committed in the absence of advice), and $g - \bar{p}\bar{s}$ in the case where $g \leq ps$; advice will be obtained if its expected value exceeds c . If $g \leq \bar{p}\bar{s}$, advice will have no value.

The provision of legal advice of the type under consideration can only be socially undesirable, since it may lead a party to commit a sanctionable act when he would not otherwise have done so, that is, when $g < ps \leq h$, and thus when commission of the act is socially undesirable.

The protection of confidentiality is socially undesirable. In its absence, if legal advice is obtained, the expected sanction will be $p's' > \bar{p}\bar{s}$. Therefore, in the absence of protection of confidentiality, legal advice will be obtained less often, which, as explained in the last paragraph, is socially preferable.

PROPOSITION 4. In the case where legal advice will enable a party to lower the probability or magnitude of sanctions, (a) a party's decision whether to obtain advice is as described in the second paragraph of this part, (b) protection of confidentiality will lead parties to obtain advice more often than they otherwise would, and (c) provision of advice and protection of confidentiality are socially undesirable.